

**IN THE SUPREME COURT OF ZAMBIA**

**APPEAL NO.13/ 2019**

**HOLDEN AT LUSAKA**

(Civil Jurisdiction)

**BETWEEN:**

**CAVMONT BANK LIMITED**

**AND**

**SPANCRETE ZAMBIA LIMITED**

**DAVIES CHOLA KATAYA**

**ANDISENI AILOSI PHIRI**



**APPELLANT**

**1<sup>ST</sup> RESPONDENT**

**2<sup>ND</sup> RESPONDENT**

**3<sup>RD</sup> RESPONDENT**

CORAM: Mambilima, CJ, Kajimanga and Kabuka, JJS.

On 11<sup>th</sup> August, 2020 and 15<sup>th</sup> December, 2020.

**FOR THE APPELLANT:**

Mr. S.C. Mwananshiku, Messrs. M & M Advocates.

**FOR THE RESPONDENTS:**

N/A

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## **JUDGMENT**

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KABUKA, JS, delivered the Judgment of the Court.

**Cases referred to:**

1. Edward Owen Engineering Limited v Barclays Bank International Limited [1978] 1 All ER 976.
2. Investors Compensation Scheme Limited v West Bromwich Building Society [1998] 1 All ER 98.
3. I.E. Constructions Limited v Lloyd Bank PLC and Rafiden Bank [1990] 2 Lloyds Reports 496.
4. Howe Richardson Scale Co v Polimex-Cekop [1978] 1 Lloyd's Rep. 161, 165 (CA).
5. Nwosu v Zenith Bank PLC (2015) 9 NWLR 314.
6. Friday Mwamba v Sylvester Nthenge & 2 Others (2013) ZR 257.
7. Edna Nyasalu v Attorney General (1983) ZR 105
8. Mohamed v The Attorney General 1982 Z.R. 49.

**Legislation and Other works referred to:**

1. The Law Reform (Miscellaneous Provisions) Act Cap. 74, s. 4.
2. Cranston: Principles of Banking Law, 2<sup>nd</sup> Edition, 2002, Oxford University Press page 426.
3. Uniform Rules for Demand Guarantees ('URDG'), ICC Publication No. 458 (1992).
4. Chitty on Contract General Principles Vol.1, 30<sup>th</sup> Edition, Sweet & Maxwell, 2008 paragraph 12-051 page 842.
5. Brian A. Garner: Black's Law Dictionary, 8<sup>th</sup> Edition, Thomson West, page 200.

**1.0 Introduction**

1.1 The appellant appeals against a Court of Appeal judgment dated 30<sup>th</sup> January, 2019 that upheld the respondents' claim that the appellant wrongly paid out monies to ZESCO Limited, on a demand letter that did not comply with the conditions of the Advance Payment Guarantee, pursuant to which the payment was made.

- 1.2 In terms of those conditions, such a demand could only be triggered if there was breach of specific obligations by the 1<sup>st</sup> respondent, on the underlying contract it had entered into with ZESCO Limited.
- 1.3 This appeal questions the duty of a bank, upon receipt of a written demand by a beneficiary of an advance payment guarantee, stating that the principal has failed to meet its obligations.

## **2.0 Background**

- 2.1 The background facts to the appeal are that, the 1<sup>st</sup> respondent, an engineering company had entered into a one-year contract with ZESCO Limited, for the supply of 1000 kilometers of 120mm<sup>2</sup> Aerial Bundled Cable ('AB cables'). In order for the 1<sup>st</sup> respondent to fulfill its obligations under the contract with ZESCO Limited, the respondents applied for an Advance Payment Guarantee Facility ('the Guarantee') from the appellant bank, in the sum of K7, 787, 436.00. The facility was secured by

mortgages over two properties put up by the respondents as collateral.

- 2.2 It was an express term of the Guarantee facility that the appellant irrevocably undertook to pay ZESCO Limited the sum of K7, 787, 436.00 upon receipt of its first demand in writing, declaring that the supplier was in breach of its obligation under the contract, because the supplier had used the advance payment for purposes other than towards delivery of the goods.
- 2.3 To ensure performance of the underlying contract, ZESCO Limited made an advance payment of K7, 787, 436.00 available to the 1<sup>st</sup> respondent, when the 1<sup>st</sup> respondent's account held with the appellant was credited with that amount. Thereafter, the 1<sup>st</sup> respondent instructed the appellant to transfer the equivalent of U\$168, 600.00 to Jinshui Cable in China, the company contracted to manufacture the AB cables. The 1<sup>st</sup> respondent also caused the remaining balance of K5, 800, 000.00 to be placed in a

fixed deposit account held with the appellant bank. This amount was further used by the 1<sup>st</sup> respondent as cash collateral for the Guarantee facility that had been provided by the appellant.

2.4 Jinshui Cable proceeded to manufacture the first batch of 250 kilometers of AB cables in readiness to supply ZESCO Limited. ZESCO Limited was meant to conduct a pre-shipment inspection of the cables on 15<sup>th</sup> February, 2015 but kept postponing the exercise for three months up to the 12<sup>th</sup> of May, 2015. This caused a delay in the shipment of the cables and as a result, ZESCO Limited incurred losses amounting to \$404,000.00 due to Jinshui Cable on account of a forfeited deposit and storage charges.

2.5 Seven days prior to the expiry of the Advance Payment Guarantee on 29<sup>th</sup> October, 2015 ZESCO Limited on 22<sup>nd</sup> October, 2015 wrote a demand letter to the appellant seeking a full refund of monies subject of the said Guarantee, on the basis that, the supplier was in breach of

its obligation, as it had failed to supply the 120mm<sup>2</sup> ABC cables and accessories on the underlying contract.

- 2.6 Upon receipt of the demand letter, the appellant promptly acted on it by calling up the sum of K5, 800, 000.00 that was sitting in the 1<sup>st</sup> respondent's fixed deposit account. The 1<sup>st</sup> respondent's current account was also overdrawn by K1,987, 436.00 to facilitate payment to ZESCO Limited, the guaranteed sum of K7, 787, 436.00.

### **3.0 Proceedings before the High Court**

- 3.1 In order to recover its monies, the appellant took out a mortgage action in the High Court by issuing, against the respondents, an originating summons claiming K2, 057, 705.43, plus interest due under the Advance Payment Guarantee. Alternatively, the appellant claimed an order that the respondents deliver to it, possession of the mortgaged properties, foreclosure and sale of the said properties.

- 3.2 The application was opposed by the respondents on grounds that the demand letter issued by ZESCO Limited did not specify that the 1<sup>st</sup> respondent had breached its obligations under the contract in that, 'it used the advance payment for purposes other than towards delivery of the goods', in accordance with the terms provided under the Guarantee. The respondents contended that the appellant had been negligent in paying out the guaranteed amount and on that basis, denied being indebted to the appellant.
- 3.3 After hearing the matter, the trial judge considered the evidence, various authorities on the law of guarantees and found that, the appellant had assumed financial payment obligations as security for the fulfillment of the 1<sup>st</sup> respondent's contractual obligations. That these obligations arose from an underlying contract entered into between ZESCO Limited and the 1<sup>st</sup> respondent. The trial judge also noted that, the rationale behind Advance Payment Guarantees is to ensure performance of the contract and

avoid prolonged litigation, so that the beneficiary is promptly availed its funds.

- 3.4 The learned trial judge relied on the English case of **Edward Owen Engineering Limited v Barclays Bank International Limited**<sup>1</sup> in which it was held that, a bank which gives a performance guarantee, must honour that guarantee according to its terms, and must not be concerned with the relations between the supplier and customer, nor with whether the supplier has performed his contracted obligation or not. That the bank must pay according to its guarantee on demand, if so stipulated, without proof or conditions except where there is clear fraud of which the bank has had notice.
- 3.5 Relying on the principle in the case of **Edward Owen Engineering Limited**<sup>1</sup> as stated at paragraph 3.4 above and other similarly decided cases, the learned trial judge found that the appellant was triggered to act upon its receipt of the demand letter from ZESCO Limited stating



that the 1<sup>st</sup> respondent was in breach of its obligations; and, was thus, bound by its undertaking to pay the guarantee.

3.6 The trial judge further found, the fact that the demand letter did not specify that the 1<sup>st</sup> respondent had used the advance payment for purposes other than towards delivery of the goods as contained in the Advance Payment guarantee did not render it invalid. According to the trial judge, this was so as the words “...*in breach of its obligations under the contract...*’ were all encompassing to include the failure to deliver the cables. Reference was made to the cases of **Investors Compensation Scheme Limited v West Bromwich Building Society**<sup>2</sup> and **IE Contractors Limited v Lloyd Bank Plc and Rafiden Bank**<sup>3</sup> which both speak to the need to consider the meaning of a document objectively, taking into account all the relevant background knowledge.

3.7 On the evidence before her, the learned trial judge found that the 1<sup>st</sup> respondent was indebted to the appellant in the

claimed sum of K2, 057, 705. 43 inclusive of interest. As there was no supporting evidence showing how the accrued interest was arrived at, the trial judge ordered that the appellant should avail the 1<sup>st</sup> respondent with a bank statement showing the interest charged on the principal amount, within 14 days of the delivery of her judgment. The judgment sum was to attract interest at short term deposit rate from the date of the originating summons to the date of its delivery and thereafter, interest would accrue at commercial lending rate until full payment.

#### **4.0 Proceedings before the Court of Appeal**

4.1 Aggrieved with the judgment of the High Court, the respondents launched an appeal to the Court of Appeal advancing five grounds, which in substance were as follows:

- 1. The learned trial judge erred in law and fact when she held that the guarantee issued by the respondent in favour of ZESCO Limited was payable on demand without proof or conditions.**
- 2. The learned trial judge erred in law and fact when she construed the true nature of the guarantee and held that the**

**demand from ZESCO Limited did comply with the terms of the guarantee.**

- 3. The learned trial judge erred in law in awarding the respondent interest incorporated in the pre-litigated claim of K2, 057, 705. 43 when the respondent failed to show how the said interest was arrived at.**
- 4. The learned trial judge erred in law by directing the respondent to adduce evidence relating to its claimed interest on the sum of K2, 057, 705. 43, post judgment.**
- 5. The court below erred in law by awarding interest to the respondent at the short-term deposit rate.**

4.2 The gist of the respondents' arguments before the Court of Appeal on grounds one and two, was that, there is a distinction between the terms of a guarantee and the terms of a contract underlying the guarantee. That the issue in contention in this case, was not the underlying contract or whether or not there was a breach of it. It was rather, whether there was an obligation by the appellant bank to pay, if the conditions precedent for settlement inherent in the guarantee, independent of the underlying contract, had not been met. It was argued that an obligation to pay on

the basis of a payment guarantee does not arise where the condition precedent has not been met.

- 4.3 The submission on the point was that, the interpretation given by the trial judge was wide and went beyond what the parties had contracted. That contrary to the wording of the Guarantee in question which was specific and subject to strict interpretation, the demand letter issued by ZESCO Limited went outside the scope of the provisions of the Guarantee, on default.
- 4.4 Regarding the trial court's finding on interest, subject of grounds three, four and five of the appeal, it was contended that matters of interest by their very nature are particularly contentious and therefore, require documentation to prove, in line with the legal principle that he who alleges must prove. The learned trial judge in this case, contrary to that position, ordered that the appellant produce evidence of the alleged interest *post facto* the trial and judgment, which was prejudicial to the respondents and unjust. Counsel for the

respondents further assailed the period and calculation of the rate of interest, arguing that the interest applicable is what was prevailing at the material time.

- 4.5 In response to those arguments and submissions, learned counsel for the appellant contended that the first ground of appeal was misconceived as the trial court did not hold that the Guarantee was payable without proof of conditions. According to counsel, what the trial judge held was that, the conditions in the Guarantee had been met by the demand letter from ZESCO Limited.
- 4.6 Counsel also contended that, there was no obligation on the appellant to carry out any investigations to ascertain whether the allegations made by ZESCO Limited that the 1<sup>st</sup> respondent was in breach of its obligations under the contract were true. The submission was that, the Guarantee did not stipulate that the words to be used in the demand letter should be a verbatim reproduction of what it stated.

- 4.7 On the third ground of appeal, the contention was that the respondents did not raise any specific objection before the trial court with regard to the interest claimed. The appellant argued that, the only complaint the respondents had in that regard, was that the appellant had claimed interest on the total amount paid out under the Guarantee without providing a statement of account. The submission was that, when the trial court considered this issue, it determined that the respondents had a duty to obtain their own bank statements for their account. That it was not proper for them at appeal stage, to raise the issue of interest when it was not raised before the trial court.
- 4.8 In relation to grounds four and five, the argument was that the learned trial judge did not direct the appellant to produce evidence, post judgment, as it was agreed and evident from the third-party mortgage that compound interest was payable. It was further argued that, interest is discretionary under **section 4 of the Law Reform (Miscellaneous Provisions) Act, Cap 74 of the Laws of**

**Zambia** and as such, a court is not precluded from making an order of interest to be paid at the rate it deems fit.

- 4.9 The Court of Appeal after considering the arguments deployed before it as recounted at paragraphs 4.2 – 4.8 dealt with the first two grounds together on the basis that they were interrelated. The remaining three grounds were also dealt with in like manner.
- 4.10 On grounds one and two, the finding of the Court of Appeal was that, the trial court did not hold that the Guarantee was payable on demand without proof or conditions. It's holding was that, the appellant was triggered by the demand letter received from ZESCO Limited, to honour the undertaking in accordance with the terms of the Guarantee.
- 4.11 The Court of Appeal held the view that in so finding, the trial court had misconstrued and misapplied the principle laid down in **Edward Owen Engineering Limited**<sup>1</sup> when it distinguished the said case from the one *in casu*. The Court of Appeal noted that, in the case referred to, the guarantee

was expressly said to be payable on demand without proof or conditions. In the present case however, the guarantee was payable upon the first demand in writing, declaring that the supplier was in breach of its obligations under the contract *'on the basis that the supplier, used the advance payment for purposes other than towards delivery of the goods'*.

4.12 The finding of the Court of Appeal was that, in the circumstances of the case *in casu*, it was indeed necessary for ZESCO Limited to inform the appellant that the default was due to the 1<sup>st</sup> respondent *'having used the Guarantee for purposes other than towards delivery of the cables.'* This was so, as payment was meant to be made only upon the trigger of that specified breach. That other breaches such as wanton refusal by the 1<sup>st</sup> respondent to give its approval of the manufactured product or mere delay in delivering the goods, were not covered by the Guarantee.



- 4.13 The Court of Appeal agreed with counsel for the respondents that the intention of the parties was to safeguard against the misuse of funds. The cases of **Investors Compensation Scheme Limited v West Bromwich Building Society**<sup>2</sup> and **I.E. Constructions Limited v Lloyd Bank PLC and Rafiden Bank**<sup>3</sup> were relied upon as held that, unlike the **Edward Owen Engineering Limited**<sup>1</sup> case where the guarantee was payable on demand without proof or conditions, in this case the guarantee was payable on demand, only if the condition occurred. The Court of Appeal concluded that, the demand letter of 22<sup>nd</sup> October, 2015 was not in compliance with the provisions of the Guarantee, and was therefore invalid.
- 4.14 Citing the case of **Howe Richardson Scale Co. v Polimex-Cekop**<sup>4</sup> the Court of Appeal underscored the point that, a bank has an obligation to perform that which is required of it in a particular contract, on the happening of a particular event. The Court was however, quick to clarify that, it was by no means implying that the appellant was duty bound

to investigate the matter in order to establish whether the supplier had misused the money.

4.15 On grounds three, four and five, relating to interest payable, the Court of Appeal determined that the issue of interest was properly raised by the 1<sup>st</sup> respondent in its affidavit in opposition. The fact that the respondents were at liberty to request for bank statements, notwithstanding, the Court of Appeal found that it was still incumbent upon the appellant to justify its claim for interest before the matter was determined. The conclusion reached was that, since the issue had been raised before the trial court, it was properly raised on appeal to the Court of Appeal.

4.16 In the event, the Court of Appeal was of the view that the trial court was under a duty to satisfy itself that the appellant had properly charged interest. Having failed to do so, the trial court had done an injustice to the respondents by granting unproven claims of interest in favour of the

appellant, post judgment, which was a misdirection that rendered all the orders made on interest erroneous.

4.17 Premised on its findings at paragraphs 4.10 – 4.16 above, the Court of Appeal set aside the judgment of the High Court and in its place, made an order that the appellant: (i) refunds the 1<sup>st</sup> respondent the sum of K5, 800, 000.00; (ii) yields vacant possession of the property known as Stand No: 1044/L/4 Makishi/Broads Roads, Rhodes Park which it possessed by way of writ of possession on 1<sup>st</sup> August, 2017 and had advertised for sale.

4.18 In the event that the mortgaged property had since been sold, that the respondents were entitled to its market value as at the time of execution of the writ of possession. The respondents were also awarded interest at average short-term deposit rate from the date of writ to date of judgment thereafter, interest was to accrue at the current commercial bank lending rate. The matter was further referred to the Deputy Registrar of the High Court for assessment of

damages. Costs of the matter in both the High Court and the Court of Appeal were awarded to the respondents.

## **5.0 Grounds of Appeal to this Court and Arguments**

5.1 Those are the findings that brought the appellant on appeal to this Court on four grounds, stated as follows:

- 1. The court below erred in law and fact when it held that the letter of demand dated 22<sup>nd</sup> October, 2015 was not in compliance with the provisions of the Advance Payment Guarantee issued by the appellant.**
- 2. The court erred in law and in fact when it held that the issue of interest payable was raised by the respondents in the High court, when the record shows that in the proceedings before the High Court there was no clear and specific objection raised by the respondents against the interest claimed by the appellant.**
- 3. The court below erred in law and fact when it directed the appellant to refund the sum of K5,800, 000.00, when there was no such claim made by the respondents in the High Court.**
- 4. The court below erred in law and fact when it awarded the respondents damages when there was no such claim made by the respondents in the High Court.**

5.2 Written heads of argument were filed in support of the grounds of appeal. The appellant's argument on ground one was that, the Court of Appeal fell into grave error when it

interpreted the letter of demand in isolation, without considering that the 1<sup>st</sup> respondent did not utilise the Guarantee facility exclusively for the supply of the 1000km of ABC cables to ZESCO Limited.

5.3 Learned counsel for the appellant argued that, the 1<sup>st</sup> respondent invested part of the money into a fixed deposit account it held with the appellant and further turned it into a cash collateral, which was not the intended purpose of the funds. The submission, in that regard, was that the respondents should have found their own cash collateral separate from the advance payment amount which was meant for performance of the contract.

5.4 Counsel further submitted that, the respondents had in fact sought to profit from the Guarantee as they had only used K1, 987, 436.00 of the K7, 787, 436.00 made available and placed the remaining K5, 800, 000.00 in a fixed deposit account. In so doing, according to counsel, the respondents were architects of breach of their own obligations to ZESCO

Limited which resulted in their subsequent failure to supply the cables as stated in the demand letter.

- 5.5 Counsel for the appellant further argued that, the Court of Appeal misdirected itself in applying the strict compliance principle. The appellant extensively quoted from **Ross Cranston: Principles of Banking Law, 2<sup>nd</sup> Edition, 2002, Oxford University Press page 426-7** in relation to demand guarantees requiring that banks must '*pay first and argue later;*' as the bank undertakes the primary obligation to pay, independent of the underlying contract; and, its obligation is to perform that which is required of it.
- 5.6 The appellant further cited the Nigerian case of **Nwosu v Zenith Bank PLC<sup>5</sup>** which is said to have held that a banker's guarantee shall effect payment on a written demand by a beneficiary, when the principal has failed to meet its obligations. The appellant also made reference to the **ICC's Uniform Rules for Demand Guarantees, (ICC Publication Number 458)** in emphasizing that, if the 1<sup>st</sup>

respondent had felt that the demand letter was non-compliant, it had recourse to sue ZESCO Limited, which it did, but had lost those cases both before the High Court and the Court of Appeal.

- 5.7 It was argued that words should be given their natural meaning and the intentions of the parties deduced from the surrounding circumstances. **Chitty on Contracts: General Principles Vol. 1 paragraph 12-105 page 842** was referred to for the submission that, the Court of Appeal ought to have considered the commercial purpose and factual background against which the Guarantee was made, as well as the ensuing demand letter, in relation to the 1<sup>st</sup> respondent's alleged breach. That the Court of Appeal had erred by giving the letter of demand such a strict and narrow interpretation and concluding that the letter was dishonest and invalid, when it missed the objective intention of the parties. The case of **Friday Mwamba v Sylvester Nthenge & 2 Others**<sup>6</sup> was cited in support of the submission.

- 5.8 The appellant also argued that the respondents committed a material breach of contract by failing to supply ZESCO Limited with the AB cables and accessories. Material breach as defined in **Black's Law Dictionary** was relied upon for the submission that, such breach amounts to total breach rather than a partial one and the 1<sup>st</sup> respondent not only failed to deliver the cables, but also misapplied the balance of K5, 800, 000.00 for a different purpose.
- 5.9 On ground two of the appeal, the argument was that the respondents had consented to the charging of interest and having it compounded. It was thus, within the appellant's rights to claim interest. The respondents should also have defined the issues and specified the aspects of interest to which they were objecting. They should have stated whether, their grievance was with the interest rates used, method of calculation, or the period in question.
- 5.10 On ground three, the appellant took issue with the order made by the Court of Appeal to refund the respondents the



sum of K5, 800, 000.00, when the monies were actually a balance on the Guarantee in favour of ZESCO Limited, and thus, remained the latter's monies until the contract was performed by the respondents. Counsel went on to argue that, in the event of failure to perform, ZESCO Limited was entitled to claim back the amount in contention, as it did not belong to the respondents who had used it as an investment to earn interest.

5.11 The appellant submitted that, sustaining the order for refund would result in unjust enrichment of the 1<sup>st</sup> respondent. The appellant maintained its position that the condition precedent was met by ZESCO Limited in its demand letter, as the 1<sup>st</sup> respondent had failed to supply the AB cables and accessories to ZESCO Limited by reason that K5, 800, 000.00 had been used for other purposes.

5.12 On ground four, the appellant challenged the award of damages made by the Court of Appeal in favour of the respondents on the basis that they were not expressly

pleaded. A plethora of cases were cited in arguing that, pleadings define the issues in a dispute and the parties cannot go beyond what is pleaded without leave of court to amend their pleadings. The submission was that the appellant was not given sufficient notice of the claim relating to damages in order to defend itself. In its judgment, the court also omitted to state the actual head of the damages awarded, or those to be assessed before the Deputy Registrar.

5.13 The appellant's submission in conclusion was that the respondents' allegation that the appellant was negligent in making the advance payment to ZESCO Limited was never proved, as the appellant was justified in adhering to the demand agreement and letter.

5.14 In their written response, the respondents on ground one of the appeal argued that, the appellant had convoluted the issues which were straight forward. Simply put, the issues are: whether the Advance Payment Guarantee required that

the letter of demand adopt the relevant wording as contained in the agreement. If so, whether the letter of demand complied with that format? If it did not so comply, whether the appellant had an obligation to settle ZESCO Limited's demand?

5.15 The respondents argued that the appellant adopted a wider meaning by contending that the advance payment guarantee was payable on demand, as there was no need to concern itself with whether the letter of demand complied with the format specified in the guarantee. The submission was that the Court of Appeal was correct in adopting the narrow approach that the demand letter ought to have adopted the format and wording provided at paragraph 1.4. of the Guarantee.

5.16 The respondents also underscored the point that parties are bound by their pleadings, whose function is to define the issues in contention and give the opposing party fair notice of the case it is going to meet. Further, that the issue of how

the K5, 800, 000.00 was used was not in contention at trial, was not raised before the Court of Appeal, and cannot now be raised on further appeal to this Court.

5.17 The respondents maintained that the appellant failed to exercise reasonable care and skill towards the 1<sup>st</sup> respondent as its client, by negligently acting on the letter of demand from ZESCO Limited, upon which it processed payment on the Guarantee.

5.18 The respondents objected to the arguments adopted by the appellant, including the '*pay first, argue later*' principle as mere after thoughts and subtle attempts at introducing new grounds of appeal which were not raised in the courts below. Their counter arguments were that the demand made by ZESCO Limited was not honest as the respondents had only utilised a portion of the funds meant for the purchase of the cables.

5.19 Regarding the appellant's contention on ground two of the appeal, that the issue of interest was never objected to by

the respondents, the case of **Edna Nyasalu v Attorney General**<sup>7</sup> was relied upon as authority for the submission that, the appellant had the obligation of discharging the burden of proof on its specific claim for interest.

5.20 On ground three, the respondents maintained that it is the appellant that is indebted to the 1<sup>st</sup> respondent in the sum negligently paid out on the Guarantee. On the appellant's argument that there was failure by the respondents to perform on the underlying contract, the submission was that, the appellant was not privy to the dealings between the 1<sup>st</sup> respondent and ZESCO Limited on their underlying contract. The respondents endorsed the finding by the Court of Appeal in that regard, that the principle underlying demand guarantees is that they are autonomous and not affected by disputes in the underlying contract between the beneficiary and the principal.

5.21 Lastly, on ground four of the appeal, the respondents' submission was simply that, the appellant did not expressly

traverse the contention in the 1<sup>st</sup> respondent's affidavit in reply, stating that the appellant was indebted to it for the sum negligently paid out.

## **6.0 Consideration of the Appeal by this Court and Decision**

6.1 We have read the record of appeal, written heads of argument filed by the parties, heard the oral submissions made by counsel for the appellant before us, taken note of the case law and other authorities we were referred to and for which we are indebted.

6.2 The record shows, it was not in dispute that the 1<sup>st</sup> respondent, acting through the 2<sup>nd</sup> respondent, approached the appellant bank for an Advance Payment Guarantee facility to enable it fulfill its contractual obligations to purchase and supply AB Cables to ZESCO Limited.

6.3 It was further not in dispute that it was a specific term of the Guarantee that the appellant would irrevocably undertake to pay ZESCO Limited any sum not exceeding K7, 787, 436.00 upon receipt of the first written demand that the '*supplier is*

*in breach of its obligations under the contract because the supplier used the advance payment for purposes other than toward delivery of the goods.'*

6.4 In our view, determination of this appeal hinges on whether the demand letter written by ZESCO Limited complied with the terms of the Advance Payment Guarantee as states that the supplier, who is the 1<sup>st</sup> respondent, had failed to supply 120mm<sup>2</sup> of AB cables and accessories and was thus in breach of its obligations on the underlying contract.

6.5 Needless to restate that an Advance Payment Guarantee is a guarantee that falls under what are known as demand guarantees. According to **Cranston: Principles of Banking Law**, a demand guarantee is defined as:

*'..the undertaking of a bank to pay a beneficiary, independent of the principal contract, possibly on written demand, possibly on presentation of a certificate by some independent third party, or possibly on submission of a court judgment or an arbitral award.'*

6.6 The **International Chamber of Commerce ('ICC')** in **Article 2 (a) of its Uniform Rules for Demand Guarantees (URDG)**

state that a demand guarantee is:

“...any guarantee, bond or other payment undertaking, however named or described, by a bank, insurance company or other body or person (hereinafter called the “Guarantor”) given in writing for the payment on a written demand for payment and such other document(s) (for example, a certificate by an architect or engineer, a judgment, or an arbitral award) as may be specified in the Guarantee, such undertaking being given;

- (i) at the request or on the instructions and under the liability of a party (hereinafter called “the Principal”); or
- (ii) at the request or on the instructions and under the liability of a bank, insurance company or any other body or person (hereinafter “the Instructing Party”) acting on the instructions of a Principal to another party (hereinafter the “Beneficiary”)

6.7 **Cranston** in his **Principles of Banking Law**, referred to at paragraph 6-4 above, goes further to explain that demand guarantees are by their very nature separate transactions from the contract or tender conditions on which they are premised. Alluding to the *‘pay first and argue later’* principle, he states that the duty of the guarantor under such guarantee is to pay the sum stated therein, on the presentation of a written demand for payment and other documents, if any, specified by the guarantee which appear on their face to be in accordance with the terms of the



guarantee. All other issues in dispute, if any, must be considered after the payment.

6.8 Against that backdrop of the law on demand guarantees, we note that the appellant's argument on ground one of the appeal is that the Court of Appeal ought to have widely interpreted the wording of the demand letter by considering the surrounding circumstances, including how the 1<sup>st</sup> respondent utilised the advance payment facility, in respect of its obligations to ZESCO Limited. The appellant contends that, not only should the natural meaning of the words have been taken into account, but also the intentions of the parties to the underlying contract, the factual background and the commercial purpose for which the Guarantee was made.

6.9 In countering that argument, the respondents identify the real issue as being, whether the Guarantee required that the demand letter adopt its exact wording and, if so, whether there was such compliance. The respondents

contend that, the Court of Appeal was correct in holding that the demand letter ought to have been framed in accordance with the wording and format in the Advance Payment Guarantee.

6.10 We are alive to the position, and it is not in dispute that, according to the terms and conditions of the Guarantee in issue, the appellant as guarantor, irrevocably undertook to pay the beneficiary ZESCO Limited, the sum of K7, 787, 436.00 upon receipt of a first demand in writing stating that the 1<sup>st</sup> respondent as supplier/principal, was in breach of its obligations under the contract. The condition was couched in the following terms:

4.1 **“At the request of the supplier, we Cavmont Bank Limited .....hereby irrevocably undertake to pay you any sum or sums not exceeding in total an amount of ZMW7,787,436 (Seven Million Seven Hundred and Eight Seven Thousand Four Hundred and Thirty-Six only) upon receipt by us of your first demand in writing declaring that the supplier is in breach of its obligation under the Contract** because the supplier used the advance payment for purposes other than towards delivery of the Goods,” (boldfacing for emphasis supplied).

6.11 Premised on the above terms, the demand letter from ZESCO Limited expressed the breach by the 1<sup>st</sup> respondent using the following words: *“that the supplier has to date failed to supply the 120mm<sup>2</sup> ABC cables and accessories to ZESCO Limited, thus being in breach of its obligation under this contract.”* It cannot be disputed that the demand letter declared that the supplier was in breach of its primary obligation on the underlying contract by reason of its failure to deliver the goods, even if it makes no mention of the 1<sup>st</sup> respondent using the Guarantee for purposes other than towards delivery of the said goods.

6.12 Since the appellant made the Guarantee subject to the URDG 458, we have taken time to peruse the said applicable rules. On the point are Articles 16 and 20, the relevant parts of which provide that:

16. **“A Guarantor is liable to the Beneficiary only in accordance with the terms specified in the Guarantee** and any amendment(s) thereto and in these Rules, and up to an amount not exceeding that stated in the Guarantee and any amendment(s) thereto.”

20. (a) **Any demand for payment under the Guarantee**

**shall be in writing and shall** (in addition to such other documents as may be specified in the Guarantee) **be supported by a written statement** (whether in the demand itself or in a separate document or documents accompanying the demand and referred to in it) **stating:**

(i) **that the Principal is in breach of this obligation(s) under the underlying contract(s)** or, in the case of a tender guarantee, the tender conditions; **and**

(ii) **the respect in which the Principal is in breach.**

(b) Any demand under the Counter-Guarantee shall be supported by a written statement that the Guarantor has received a demand for payment under the Guarantee in accordance with its terms and with this Article.

(c) Paragraph a) of this Article applies except to the extent that it is expressly excluded by the terms of the Guarantee. Paragraph b) of this Article applies except to the extent that it is expressly excluded by the terms of the Counter-Guarantee.

(d) Nothing in this Article affects the application of Articles 2b) and 2c), 9 and 11. (boldfacing for emphasis only).

6.13 Our understanding of the above Articles is that a demand for payment, whether made under a guarantee or counter guarantee, must be: *made in writing, in accordance with the terms of that guarantee, stating that the principal is in breach of its obligation under the underlying contract, and in what respect the principal is in breach.*

- 6.14 The respondents' firm position in that regard is that, the salient term under the guarantee *in casu*, is that the appellant would undertake to pay the sum of K7, 787, 436.00 upon receipt of the first demand in writing, declaring that the supplier was in breach of its obligation under the contract, *'because the supplier had used the advance payment for purposes other than towards delivery of the goods.'*
- 6.15 The respondents have pointed out that, the qualification as highlighted in the preceding paragraph changed the complexion of the term under which a breach could occur, by narrowing the circumstances specifically to the use of funds by the 1<sup>st</sup> respondent towards other ventures. The respondents argue that, the failure to deliver AB cables to ZESCO Limited was not included as a possible breach.
- 6.16 The appellant in response, has urged for a wider interpretation of the demand guarantee, pointing out that the real issue on the particular facts, was *whether the 1<sup>st</sup>*

*respondent had delivered on its main obligation.* The appellant referred to misapplication by the 1<sup>st</sup> respondent, of K5,800,000.00 out of the K7,787,436.00, towards creating an investment in form of a fixed deposit account that was also used as collateral for the same Guarantee.

6.17 It has been argued by the appellant, in *casu* and in our view properly so, that the event which the appellant bank had envisaged could occur under the guarantee was delivery of the AB cables but ZESCO Limited claimed, in writing, that there was a breach of that obligation by the 1<sup>st</sup> respondent's failure to deliver.

6.18 Granted that circumstance and relying on the '*pay first, argue later*' principle, we have no difficulty in determining that the appellant clearly had a responsibility to take into account that the rationale behind Advance Payment Guarantees is to ensure performance of the contract. In our view, the appellant in this appeal properly acted on the

demand letter stating that the 1<sup>st</sup> respondent had failed to meet that primary obligation.

6.19 We say so, as the bank's payment obligation on demand guarantees, is to perform according to its undertaking which is to pay without regard to the underlying contract. That position is also in accord with Articles 16 and 20 of the URDG 458 to which the Guarantee was made subject, as earlier reproduced at paragraph 6.12.

6.20 In the case in *casu*, the guarantee was payable upon '*the first demand in writing, declaring that the supplier was in breach of its obligations*' to perform, under the contract. In the event, we cannot fault the trial judge when she gave a wider interpretation to the terms of the Advance Payment Guarantee and found, the words '*...in breach of its obligations under the contract...*' were all encompassing to include the failure to deliver the cables.

6.21 In concluding our consideration of ground one of the appeal, we wish to comment on the respondents' argument

that the appellant has raised before this court, issues not raised in the High Court and before the Court of Appeal, such as how the K5, 800, 000.00 was utilised. Our quick response is that, appeals are generally a rehearing of the matter on the record and an appellate court is not precluded from resolving the issues in dispute on appeal, by referring to evidence that is on record. An appellate court is also at liberty to consider arguments canvassed around the grounds of appeal relating to that evidence in the light of the applicable law or authorities.

6.22 We note, in that respect, the evidence on record confirming that the 1<sup>st</sup> respondent (the appellant's customer) decided to keep a part of the funds of the advance payment guarantee amounting to K5, 800, 000.00 in a fixed deposit account held with the appellant, which was undoubtedly, an investment. In our view, that position does not assist the 1<sup>st</sup> respondent's claim that it did not apply the monies for purposes, other than for the purchase of AB cables and accessories.



- 6.23 We agree with the respondent's submission, that the appellant was not privy to the contract for purchase of the 250 kilometers of AB cables which was awaiting pre-shipment inspection. That the delay in inspection culminated into a delayed chain reaction of events in the delivery of the goods to ZESCO Limited and relates to the performance of obligations on the underlying contract which was not covered by the demand guarantee.
- 6.24 We, however, find that the Court of Appeal was obliged to give a wider interpretation to the terms of the Guarantee by taking into account the commercial purpose for the guarantee, which in this case was to ensure performance by the 1<sup>st</sup> respondent, of its primary obligation to deliver the AB cables and accessories.
- 6.25 From the evidence on record, it is clear that according to its terms, the guarantee was payable upon the first demand in writing, simply declaring that the supplier was in breach of its obligations on the underlying contract and no more.

That being the case, upon receipt of such demand letter from ZESCO Limited, the appellant bank as guarantor was obligated to effect payment on the Guarantee.

6.26 To achieve that objective which was the intention of the parties, words used apparently, qualifying payment in a way that restricted it to a single circumstance specifically, that *'the supplier used the advance payment for purposes other than towards delivery of goods,'* must be widely construed. This is in order to promote the intended commercial purpose. Such construction must take into account the intention of the parties which in this case, was to safeguard against the misuse of funds, for purposes of ensuring that they were directed to performance of the primary obligation, only and in terms of the words used in the Guarantee was referred to as *'towards delivery of the Goods.'*

6.27 In our view, the demand letter from the beneficiary ZESCO Limited, communicating that the 1<sup>st</sup> respondent as the supplier/principal had failed to perform its primary

obligation, satisfied the conditions for payment of the guarantee. Accordingly, we agree with the **Nwosu v Zenith Bank PLC**<sup>5</sup> as aptly describing the appellant's duty in such circumstances in its holding: that a banker's guarantee shall effect payment on a written demand by a beneficiary according to its terms, when the principal has failed to meet its obligations.

Ground one succeeds for those reasons.

6.28 Coming to ground two, the appellant on this ground seeks to assail the determination made by the Court of Appeal that the issue of interest payable was raised by the respondents before the trial court. The appellant argues that there was no clear and specific objection raised by the respondents against the interest claimed by the appellant in the High Court.

6.29 We are at pains, to appreciate this ground of appeal, as the record shows the trial court did make a finding of fact that the 1<sup>st</sup> respondent raised the issue of not knowing how the

interest charged by the appellant was calculated. The trial court went further to find that, although the appellant had provided an explanation as to how the amount claimed was arrived at, there was no supporting evidence to show how the accrued interest was calculated in the total sum claimed.

6.30 Accordingly, the trial court found that the appellant had a duty to furnish the 1<sup>st</sup> respondent with a bank statement showing the activities on the account, including accrued interest, while the 1<sup>st</sup> respondent had a corresponding duty to request for bank statements. It was this finding that led the trial court to order that the appellant should furnish the 1<sup>st</sup> respondent with a bank statement showing interest charged on the claimed amount of K2, 057, 705. 43 within 14 days, of the delivery of its judgment.

6.31 The Court of Appeal in considering that issue held that, the trial court had a duty to satisfy itself that the bank had charged interest properly. It further observed that the trial

court did an injustice by granting unestablished claims which the appellant was ordered to prove 14 days, post judgment. Granted that backdrop of the evidence on record, we have no basis for faulting the Court of Appeal when it set aside all the trial court's orders for payment of interest, which was not proved.

6.32 The law is well settled that he who alleges must prove. In the case of **Mohamed v The Attorney General**<sup>8</sup>, this Court did hold to the effect that, the unqualified proposition that a claimant should succeed automatically whenever a defence has failed is unacceptable as a claimant must prove his case and if he fails to do so, the mere failure of the opponent's defence does not entitle him to judgment. As the evidence on record reveals that the appellant did not give sufficient particulars of the interest constituted in its claim of K2,051,705.43, the Court of Appeal cannot be faulted for disallowing the interest component in the claim on the basis that it was not established with evidence. Ground two of the appeal fails for that reason.

6.33 On ground three, the appellant alleges that the Court of Appeal erred in law in ordering a refund to the respondents of K5, 800, 000.00 when no such claim was made by the respondents in the High Court. A perusal of the trial court's judgment in the record of appeal shows that the respondents did allude to the fact that the K5,800,000.00 held to its credit by the appellant bank was negligently paid out to ZESCO Limited. The relevant evidence also appears in the affidavit in opposition in which the 2<sup>nd</sup> respondent states that it is actually the appellant that is indebted to the 1<sup>st</sup> respondent for the sum *negligently* paid out on the Advance Payment Guarantee. That the amount (K5,800,000.00) was cash collateral not intended to be used by the 1<sup>st</sup> respondent.

6.34 In their submissions before the trial court, the respondents extensively argued on the negligence and breach of legal duty to take care by the appellant, when the appellant failed to ascertain whether there had been primary default by the

1<sup>st</sup> respondent, before proceeding to pay out the Advance Payment Guarantee to ZESCO Limited.

6.35 We note from those arguments that, the order made by the Court of Appeal for refund of the K5,800,000.00 was informed by its finding that the payment was premised on a demand letter that did not comply with the terms of the Guarantee and was therefore invalid. Having determined on ground one of the appeal, that the said letter was in fact valid, it follows that the sum of K5, 800,000.00 paid from the 1<sup>st</sup> respondent's fixed deposit account and K1, 987, 436.00 overdrawn from its current account in the total sum of K7, 787, 436.00 which was the amount covered by the Guarantee, was properly paid to ZESCO Limited. It is for those reasons that ground three must succeed.

6.36 Finally, on ground four, challenging an award of damages apparently made by the Court of Appeal to the 1<sup>st</sup> respondent when there was no such claim by the latter before the High Court. We have perused the judgment

appealed against and found the issue is only mentioned in the last paragraph of the judgment, where the Court of Appeal makes an order for assessment of damages without specifying the basis for awarding those damages. We find the order for assessment of damages in those circumstances, unsustainable and it is hereby set aside.

Ground four of the appeal equally succeeds.

6.38 The appellant having succeeded on three, out of the four grounds of appeal advanced, will have its costs of the appeal in this Court and in the Court of Appeal. Such costs are to be taxed in default of agreement.

Appeal succeeds.



.....  
I. C. MAMBILIMA  
**CHIEF JUSTICE**



.....  
C. KAJIMANGA  
**SUPREME COURT JUDGE**



.....  
J. K. KABUKA  
**SUPREME COURT JUDGE**