



**UGANDA COURT OF APPEAL REVISITS APPLICATION OF THE “INDOOR MANAGEMENT RULE” IN RESPECT TO VALIDITY OF MORTGAGES AND EXECUTION OF MORTGAGE DEEDS**

**COURT OF APPEAL CIVIL APPEAL NO. 219 OF 2013 – NECTA (U) LTD AND JOHN NDYABAGYE VS CRANE BANK LIMITED.**

The Court of Appeal has revisited and emphasized various aspects in regard to validity of mortgages, execution and attestation of mortgage deeds. Court emphasized obligations of both the mortgagor and mortgagee in that respect thus widening the scope of the mortgagee’s inquiry into the borrower’s constitutional documents to ascertain whether the relevant authorizations have been duly obtained.

Moses J. Adriko SC of M/s MMAKS Advocates represented the Respondent (“the Bank”) in this matter.

**Background**

The Bank advanced various credit facilities to the Appellants which were secured by the 1<sup>st</sup> Appellant’s property. The Appellants defaulted and pursuant to the mortgage, the security was sold to a third party who was the 2<sup>nd</sup> Defendant in the main suit. The Appellants filed a suit challenging the validity of the mortgage and the resultant sale. The High Court dismissed the suit with costs and held that the mortgage deed was valid and so was the sale of the security. The High Court additionally held that the Plaintiffs (Appellants) had failed to prove settlement of the credit facilities and that there was an outstanding debt due to the Bank.

The Appellants appealed to the Court of Appeal mainly on validity of the mortgage and the sale of the security.

**Court of Appeal judgment.**

The Court of Appeal found that as at the date of execution of the resolution used to pledge the company property as security, the 1<sup>st</sup> Appellant had 4 directors who were all supposed to sign notwithstanding that two of those directors were stated to be minors at the time the resolution to obtain facilities was signed. In that regard, Court held that the resolution to pledge the company property as security was invalid and it was the Bank’s duty to inquire beyond the resolution presented to it as whether the two directors who signed were the only ones authorized by the company’s articles of association.

In relation the validity of the mortgage and the sale, Court held that the further charges on the property and the further overdrafts were unauthorized and illegal.

The Court found that having not affixed the company seal on the said charges, a stamp would not substitute the company seal and the scribbled signatures without indicating the names of the signatories contravened the requirements of the Registration of the Titles Act.

Having declared the mortgage invalid, Court held that the sale arising out the mortgage was equally declared invalid.

The Court invoked the principle of unjust enrichment to uphold the decretal sum of Ug. Shs. 218,144,745/= awarded by the trial court which was to be paid to the Bank by the Appellants. Court further noted that although the mortgage had been impugned, the.

Appellants were duty bound to make good their contractual obligations under the mortgage deeds

Surprisingly, Court without highlighting aggravating circumstances awarded the 1<sup>st</sup> Appellant aggravated damages for sale of its property.

#### Relevance of the Decision.

Below is a summary of the judgment of the Court of Appeal in regard to various hitherto settled aspects in a mortgagor mortgagee relationship.

- The Mortgagee is obligated to inquire into whether company documents presented to it have been duly authorized and executed in accordance with the constitutional documents of the borrower. This disregards the common law “indoor management rule” to the effect that a party contracting with a company is entitled to assume that the corporate acts provided in the company’s constitutional documents have been duly performed and such a party is not bound to inquire beyond that.
- The Court placed an added obligation on Financial Institutions to conduct greater due diligence on a surety where it is sought to

register a third-party mortgage, more so where the surety are husband and wife to dispel any claim of undue influence by a spouse for the express purpose of obtaining consent for registration of a charge.

- Any further charges on existing security are treated as fresh borrowing and must be specifically authorized under a fresh company resolution clearly sanctioning the additional borrowing as opposed to the resolution authorizing the initial borrowing.
- Company documents that are supposed to be executed as deeds must be legally executed under the company’s common seal. A company stamp neither authenticates nor validates company documents and its usage is merely to give a semblance of officialdom to documents that would not legally require an official company seal.

Although we appreciate the Court’s clarion call on financial institutions to heed to legal requirements in mortgage transactions, we take the view that the Court over stretched the mortgagee’s obligations in many respects regarding execution of mortgage documents and thus the Respondent is appealing the decision.



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