

September 14, 2021

## ALP COMPLIANCE MEMO

Banks with Securities comprised in *Mailo* and Freehold Land owned by Non-Citizen Companies

### *A. Background*

On July 22, 2021, the Court of Appeal rendered judgment in the case of *Biyinzika Enterprises Ltd & Others v Biyinzika Farmers Ltd & Another*, Civil Appeal No. 18/2012 and held that where the Articles of Association of a company do not restrict transfer of shares to non-Ugandan citizens, it is deemed a Foreign Company and cannot hold *mailo* land irrespective of the fact that Ugandan citizens have majority controlling interest. The Court further held that where such non-citizens own *mailo* land, that ownership is an illegality and a nullity. This decision was premised on Article 237(2)(c) of the *Constitution of Uganda*, 1995 and section 40(7) of the *Land Act*, Cap 227 which provide for the definition of a non-citizen for purposes of ownership of land (Section 40(7)) and the land tenure that non-citizens can own (Article 237(2)). This land tenure is explicitly stated to be leasehold.

This Compliance Memo therefore seeks to propose the way forward for banks that have obtained a security interest on *mailo* or freehold land owned by companies deemed as Non-Citizen Companies.

### *B. Land Ownership in Uganda*

Article 237 of the *Constitution* provides that land in Uganda belongs to the citizens of Uganda and shall vest in them in accordance with the land tenure systems provided in the constitution. This is also provided for under section 2 of the *Land Act*.

Article 237(2)(c) of the *Constitution* provides that non-citizens may acquire leases in land in accordance with the laws prescribed by Parliament, and the laws so prescribed shall define a non-citizen for purposes of this paragraph. Section 40(4) of the *Land Act* provides that “subject to other provisions of this section, a non-citizen shall not acquire or hold *mailo* or freehold land”. In the case of a company, the company should satisfy the requirements of a citizen company under the *Land Act*, specifically under section 40(7).

Non-citizens can only acquire leases on land for a maximum period of 99 years until renewed under section 40(3) of the *Land Act*.

### *C. Meaning of a Non-Citizen Company*

Section 40(7) of the *Land Act* defines a Non-Citizen as:

- (a) A person who is not a citizen of Uganda as defined by the Constitution and the Uganda Citizenship Act;
- (b) In the case of a corporate body, a corporate body in which the controlling interest lies with noncitizens;
- (c) In the case of bodies where shares are not applicable, where the body’s decision making lies with noncitizens;
- (d) A company in which the shares are held in trust for noncitizens;
- (e) A company incorporated in Uganda whose articles of association do not contain a provision restricting transfer or issue of shares to noncitizens.

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Therefore, any company that falls within the ambit of (b) and (e) of section 40(7) is deemed to be a non-citizen company and thus cannot own *mailo* or freehold land. However, it is pertinent to note that in *Biyinzika Enterprises Ltd case*, Court held that the 1st respondent was a non-citizen company from the very beginning because its articles did not contain a provision restricting the transfer of shares to non-citizens and, under Article 237(1) of the *Constitution* and section 40(4) of the *Land Act*, it was immaterial the controlling interest was with Ugandans.

#### ***D. Consequences of illegal land ownership to security interests***

Where a non-citizen company purchased and registered a tenure other than lease-hold, in the *Biyinzika Enterprises Ltd case*, the Court held that such transaction was illegal hence null and void. Therefore, it followed that the 1st Respondent in the case could not recover the land which had been fraudulently sold because their purchase of such land was void *ab initio*. It also follows that all other transactions whose strength/security is the illegal title, for instance, mortgages are void.

In *Formula Feeds & 3 Others v KCB Bank Uganda Limited*, CA No 76/2016, the appellants entered a credit facility with the Respondent Bank secured with *mailo* titles registered in names on non-citizens who were Kenyan nationals. Upholding the judgment of the trial court, the Court of Appeal stated that:

*"We agree with the finding of the trial Judge. The only challenge remains the mortgage which was illegal because the underlying Mailo land Titles are held in the names of non-Ugandans which is prohibited by the law. Such a non-Ugandan can only hold a lease under the said titles. So a lease not MAILO TITLE should have been issued to the first Appellant since it paid valuable consideration for land. This would avoid an absurdity in this transaction. This is clearly an error /illegality made at the time of registration. There can therefore be no enforcement under the mortgage as it stands ..."*

The court added a recommendation of rectification of the certificates of title to cater for the Respondents' interest in the said property.

However KCB Bank Uganda Limited filed HCEMA No. 390/2016 for execution of the decree in High Court (Commercial Division) in HCSS No. 289/2014 whereupon the said application was only allowed in part on condition that the 1st Respondent (KCB) disposes off only part of the suit land to realize the equivalent of UGX. 2,159,000,000/= and the Court further ordered that no execution should be made beyond the stated sum.

When the appeal of this decision failed in CA No 76/2016, KCB Bank relied on the High Court decision and, through a bailiff in an execution process, sold the said properties to the 3rd Respondent (Southgate Properties (U) Limited) purportedly to fulfil a decree against the Applicants.

In a subsequent application—*Formula Feeds Limited & Another v KCB Bank Uganda Limited & 2 Others*, Civil Misc. Appln No 208/2020—the Applicants prayed for orders that 1st and 2nd Respondents' purported sale of the 1st Applicant's lands to the 3rd Respondent was illegal and that the same ought to be set aside. The Court held that:

*"It cannot therefore be argued that the Applicants lost the appeal and therefore execution by attaching the questioned suit land was lawful. Both parties to this case did not consider this important issue of illegality yet they all concede that the mortgages and debenture are unenforceable.*

*"The finding of the Court of Appeal shows that the Applicants in this case are indebted but the debt cannot be realized by attachment and sale of the illegally obtained securities which are the subject of this application ... Both the High Court and the Appellate Court, found that the executed mortgages were null and void ab initio having accrued from an unlawful/illegal registration right from the certificates of title and could not therefore be the basis of a successful execution in the current state."*

*It is therefore surprising that despite court's outright decline to order any enforcement accruing from the void certificates of title, Defendant's counsel went ahead to initiate execution proceedings vide EMA No.390 of 2016 wherein they sought to attach and sale the properties vested in the void certificates of title.*

The Court therefore held the registrar of court erred in law and in fact when he issued execution of attachment and sale of the securities whose registration was illegal and mortgages over them declared null.

Further, the Court gave orders that the execution of the decree was illegal and set it aside and made orders for rectification. The Court derived guidance from the judgment of the Court of Appeal which recommended the remedy of rectification of the certificates of title, and held that:

*The 3rd Respondent is directed to deliver up all the certificates of title from the impugned sale to this Court for safe custody and submission to the Registrar of Titles to cancel the illegal registration of the 3rd Respondent's entry on the certificate of titles and Register Book and return the same to the Applicants for rectification as their current registration as Mailo Owners is illegal under the law.*

### **E. Way Forward**

#### *(i) Revision of the bank's security interests*

Several companies have been non-compliant with the requirement to have a clause in their articles restricting transfer of shares to Non-Ugandans and in turn most of these companies own mailo and freehold titles illegally.

It is therefore upon the bank to conduct searches on the companies that they have entered credit facilities with to ensure that their titles are legally owned by confirming that the companies are indeed citizen companies within the meaning of section 40(7) of the *Land Act*.

#### *(ii) Applying for rectification.*

Where the bank discovers that the titles are registered illegally on the basis of the companies being non-citizen companies, the bank's remedy having obtained an equitable interest on illegally owned tenure, is to apply for rectification before the Commissioner Land Registration, to invoke the registrar's power to call for the surrender of the company's illegal interest and obtain a leasehold interest.

In *Formula Feeds & 3 Others v KCB Bank Uganda Limited*, CACA No 0076/2016, the Court of Appeal, while maintaining the illegality and unenforceability of the mortgage because the Appellants owned a mailo interest and yet they were non-citizens, observed that though the mortgage could not be enforced because of the illegality, the remedy available to the Appellants was to invoke the special powers of the Commissioner Land Registration under section 91 of the *Land Act* and apply for the rectification of their title on grounds that it was issued in error and the rectification would be by way of obtaining a leasehold.

This recommendation was later effected in *Formula Feeds Limited & Another v KCB Bank Uganda Limited & 2 Others* (above), in which Court directed delivery of “*the certificates of title from the impugned sale*” to the Registrar of Titles to “*cancel the illegal registration ... [and] entry on the certificate of titles and Register Book and return the same to the Applicants for rectification*” given their illegal registration as *mailo* owners.

In terms of who can apply for rectification, this is governed by the *Registration of Titles Act*, Cap 230. Section 156 of the Act provides:

*“A proprietor may apply to have his or her certificate of title amended in any case in which the boundaries, area or position of the land described in it differ from the boundaries, area or position of the land actually and bona fide occupied by him or her and purporting to be so occupied under the title in respect of which the certificate of title was issued, or in any case in which the description in the certificate of title is erroneous or imperfect on the face of it.”*

Section 1(l) of the Act defines proprietor as:

*“proprietor” means the owner whether in possession, remainder, reversion or otherwise of land or of a lease or mortgage whose name appears or is entered as the proprietor of that land or lease or mortgage in the Register Book; “proprietor” also includes the donee of a power to appoint or dispose of that land or lease or mortgage.*

Therefore, having an equitable interest on land by virtue of the mortgage entered on the certificate of title, a Bank is a proprietor within the meaning of the Act and can apply for the rectification of the titles.

The mortgagor, as the (original) owner of the land, can also apply for rectification.

Therefore, in order for banks to obtain legal interest in the land, they should apply to the Commissioner Land Registration for the rectification of illegally registered *mailo* or freehold titles under section 91 of the *Land Act* to bring them in line with the constitution and land law as discussed in this memo.

### ***F. Conclusion***

In light of the foregoing, it is the ALP advisory that:

Any bank having a security interest on illegal *mailo* or freehold land tenures should apply for rectification under section 91 of the *Land Act* in order to rectify their illegal registration into leasehold and have their mortgage effected onto that new leasehold title. The illegality or otherwise of the bank's interest can only be ascertained after the bank has carried out a thorough securities review.

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