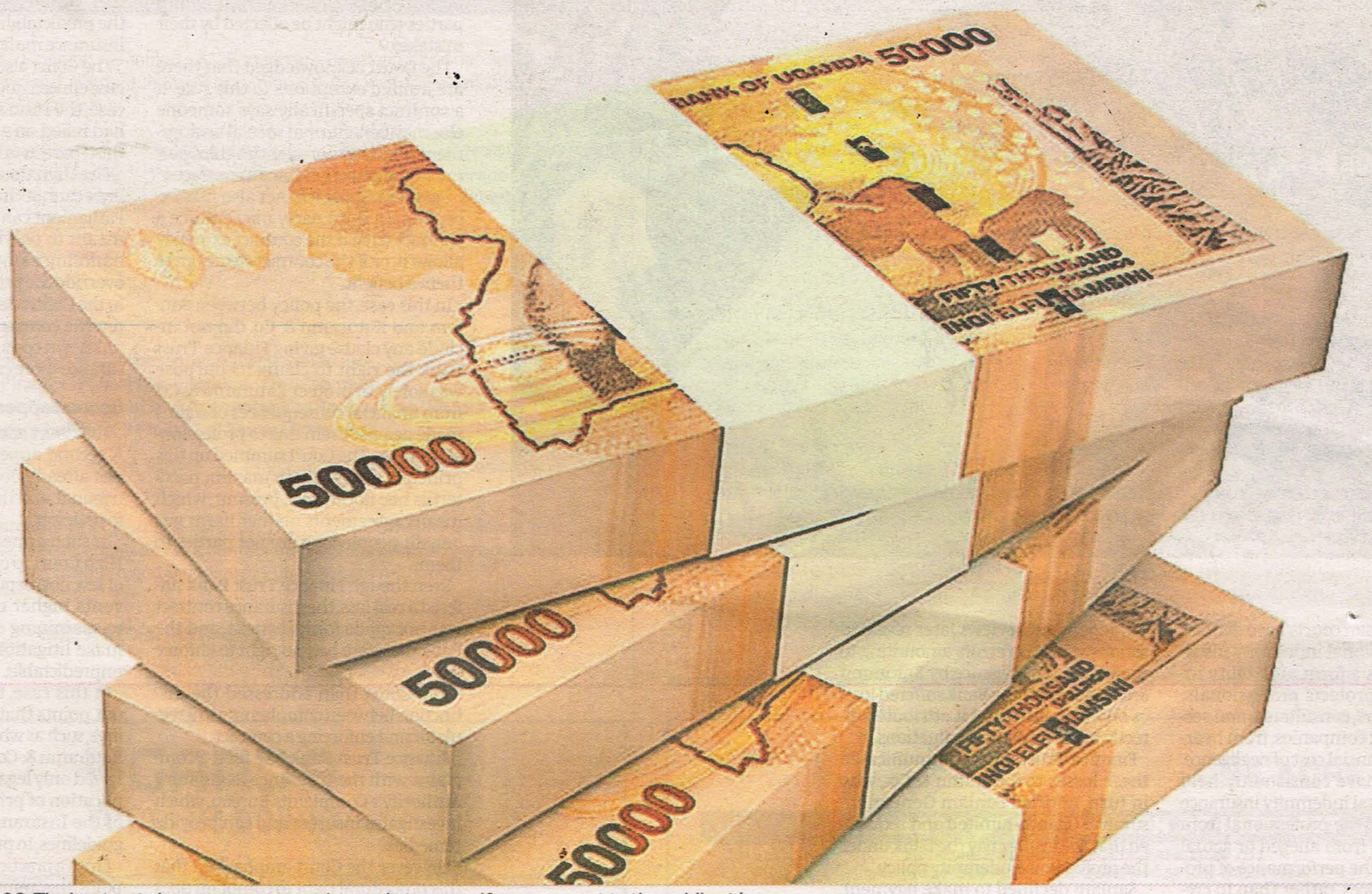

A bundle of Shs50,000. The law treats insurance as a promise made to a specific person, not to the public at large. PHOTO/FILE

Claiming directly after negligence

If anyone who suffered loss could demand payment, insurers would face unpredictable costs, premiums would rise, and the system would become unstable.

INSURANCE

DEOGRATIUS WAMALA

Imagine your neighbour takes out insurance for his house. One day, because he was careless, a fire started in his home and spread to yours, destroying part of your property.

You suffer a loss and want to be compensated.

When you learn that your neighbour is insured, your first instinct is to go straight to his insurer and ask to be paid. From an ordinary point of view, this seems sensible. Insurance exists to deal with loss, and the loss has already happened.

But insurance does not work like a general compensation fund. In simple economic terms, insurance is priced and taxed as a private contract.

The insurer calculated the premium based on the risk of protecting your neighbour, not the risk of paying every person who might be affected by his actions. If anyone who suffered loss could directly demand payment, insurers would face unpredictable costs, premiums would rise sharply, and the system would become unstable.

For this reason, the law treats insurance as a promise made to a specific person, not to the public at large.

Your right to compensation exists, but it is against the neighbour who caused the fire. The insurance steps in only to reimburse him after liability is established, not to pay you directly.

This everyday situation mirrors a recurring problem in professional services and finance. When a professional makes a mistake that causes financial loss, and an insurance policy exists in the background, the injured party often assumes that the presence of insurance creates a direct right to payment.

The law, however, tests a different question: not whether a loss occurred, but who is legally entitled to enforce the insurance contract.

Recently, the High Court of Uganda delivered a significant decision in Sanlam General Insurance Uganda Limited v Finance Trust Bank Limited, Civil Appeal No. 0046 of 2024, addressing critical issues surrounding professional indemnity insurance, third-party rights, and the doctrine of privity of contract.

The ruling guides insurers, financial institutions, and legal practitioners on the enforceability of insurance contracts and the limits of regulatory intervention in contractual relationships, particularly in respect of professional indemnity policies.

This article examines Court's reasoning and the key legal principles considered, particularly the doctrine of privity of contract in professional indemnity insurance, locus standi to enforce insurance claims, and the legal force of regulatory guidelines.

A traffic police officer looks at an accident scene. The Court reaffirmed that the doctrine of privity of contract remains central to insurance law. PHOTO/FILE

Ugandan courts have defined professional indemnity insurance as a form of liability insurance that protects professionals; such as advisers, consultants, and service-providing companies, from bearing the full financial cost of negligence.

The courts have consistently held that professional indemnity insurance exists to shield the professional from claims arising from alleged or actual negligence in the performance of professional services, rather than to create a direct payment right in favour of third parties who suffer loss.

The case

Finance Trust Bank Limited engaged Katuramu & Company Consulting Surveyors Limited to inspect and value properties offered as security before the Bank granted credit facilities to its customers.

As part of this arrangement, and as a condition for providing professional services, Katuramu & Co. held a professional indemnity insurance policy issued by Sanlam General Insurance Uganda Limited.

The policy was intended to protect the surveyors against the financial consequences of claims arising from negligence, errors, or omissions committed in the course of their professional work.

Relying on valuation reports prepared by Katuramu & Co., Finance Trust Bank advanced loans to its customers.

The valuations formed a key part of the Bank's lending decisions, as they influenced both the amount of credit extended and the assessment of risk.

At this stage, the insurance policy remained in the background, operating as a risk-management tool for the professional rather than as a guarantee to the Bank.

Problems arose when several borrowers defaulted on their loans. When the Bank moved to foreclose on the secured properties, it discovered that the values stated in the valuation reports were significantly overstated.

Independent reviews later revealed serious valuation errors amounting to professional negligence by Katuramu & Co. As a result, the Bank suffered losses on foreclosure that it attributed directly to the inaccurate valuations.

Finance Trust Bank communicated these losses to Katuramu & Co., who in turn, notified Sanlam General Insurance Uganda Limited and requested that the insurer pay the Bank under the professional indemnity policy.

Sanlam declined to make payment, taking the position that the policy did not create a direct obligation to compensate the Bank.

Rather than pursuing recovery solely through Katuramu & Co., Finance Trust Bank complained with the Insurance Regulatory Authority's Complaints Bureau.

The Complaints Bureau ruled in the Bank's favour and awarded Shs1.9 billion, directing Sanlam to pay the amount within 30 days. Sanlam appealed this decision to the Insurance Appeals Tribunal, which upheld the ruling of the Complaints Bureau.

Dissatisfied with the outcome, Sanlam lodged a further appeal to the High Court. On appeal, the High Court overturned the decisions of both the Insurance Complaints Bureau and the Insurance Appeals Tribunal.

The Court held that Finance Trust Bank, as a third party, could not enforce the professional indemnity insurance contract entered into between Katuramu & Co. and Sanlam General Insurance Uganda Limited.

The High Court's reasoning

At the centre of the High Court's decision was a simple but important question: who has the right to enforce an insurance contract? The Court relied on the doctrine of privity of contract. In plain terms, privity means that only the people who sign a contract can enforce it or take legal action under it. If you did not agree to the contract, you usually cannot go to court and demand that it be fulfilled.

Insurance policies exist to protect the person who purchases them, not third parties who might be affected by their mistakes.

The Court acknowledged that there are limited exceptions to this rule. If a contract specifically says someone else may benefit, or in special arrangements like trusts or agency, a third party can sometimes enforce a contract.

Uganda's Contracts Act also lists exceptions: a third party may enforce a contract term if the contract expressly allows it, or if the contract clearly gives them a benefit.

In this case, the policy between Sanlam and Katuramu & Co. did not include any clause giving Finance Trust Bank the right to claim. Its purpose was solely to protect Katuramu & Co. from financial consequences of claims made against them due to professional mistakes. The Court summed up this principle using a Latin maxim: pacta tertiis nec nocent nec prosunt, which means agreements neither harm nor benefit people who are not parties to them.

Even though Finance Trust Bank suffered a real loss, the insurance contract was not made for its benefit, and the Bank therefore had no right to enforce it.

The Court then addressed the distinction between complaining to a regulator and enforcing a contract.

Finance Trust Bank had filed a complaint with the Insurance Regulatory Authority's Complaints Bureau, which investigates insurers and can provide remedies.

However, the Court emphasised that this procedural right to complain does not create a new right to claim payment directly under the insurance contract. It is like being able to complain to a building inspector that a contractor did shoddy work; you can raise a complaint, but that does not give you a direct right to the contractor's insurance.

From an economics perspective, this makes sense. Insurance is a risk-sharing tool, and insurers calculate premiums based on known risks and known parties.

If anyone who suffered a loss could step in and claim payment, insurers would face unpredictable liabilities.

This would force them to raise premiums for everyone, potentially pricing insurance out of reach for the professionals who rely on it. Keeping enforcement limited to the insured protects the predictability and efficiency of the insurance market.

The Court also considered the role of guidelines issued by regulators. In this case, the Insurance Appeals Tribunal had relied on guidelines that allowed third parties to lodge complaints.

The High Court clarified that guidelines cannot change the law itself; only Parliament can do that. Guidelines are meant to provide clarity or steps for handling complaints—they cannot override the principle of privity set out in the Contracts Act. If guidelines could rewrite contracts, insurers would face unknown costs, which would make insurance more expensive and unstable.

Second appeals

The Court addressed second appeals. A second appeal occurs when a case has already been decided by a lower tribunal, and the higher court is asked to review it.

In such appeals, the law allows the High Court to consider only questions of law, not disputes over facts. This prevents higher courts from endlessly re-examining evidence, which would make litigation long, expensive, and unpredictable.

In this case, the High Court struck out points that relied on factual findings, such as whether the valuations by Katuramu & Co. were accurate, and allowed only legal questions; like the application of privity, the interpretation of the Insurance Act, and the role of guidelines, to proceed.

From a practical and economic standpoint, this approach promotes efficiency, reduces costs, and ensures certainty for insurers, professionals, and clients alike.

The High Court emphasised that insurance follows the contract, not the loss. Even if a third party suffers real harm, they cannot automatically turn to the insurer unless the policy or law explicitly allows it. This principle maintains certainty, fairness, and stability in insurance markets, protects professionals and insurers from unpredictable claims, and ensures that risk is properly priced and shared.

Implications

As noted in a litigation analysis by Alex Ahimbisibwe Kabayo, a partner, and two legal assistants from the SM & Co. Advocates litigation team, Brian Osenda Kalagala and Ian Ssezibwa, the High Court's judgment guides both insurers and professionals on the proper procedure while also clarifying the limits of third-party intervention.

The Court made clear that even if a third party suffers a loss as a result of a professional's negligence, the rights to enforce the insurance policy remain with the professional themselves.

In the trio's words: "The High Court's judgment provides clarity on the proper procedure for pursuing claims arising from professional indemnity insurance policies. Where a third party suffers loss as a result of the negligence of an insured professional, it is the insured professional that must lodge a claim for indemnity and any complaint against the insurer before the Insurance Regulatory Authority.

Contract

'Insurance follows the contract, not the loss. Even if a third party suffers real harm, they cannot automatically turn to the insurer unless the policy or law explicitly allows it.'