# The powers and authority of directors to act on behalf of a company under South African law

by

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## SUMMARY

As a company is a juristic person it can only act through human agency. A question that arises because of this fact is under what circumstances a company can be held to a contract by a third party where its representative was unauthorised to enter into such contract. There should be a careful weighing and balancing of the interests of the shareholders and the company on the one hand and the contracting third party on the other. It is further important to have legal certainty on the validity and enforceability of contracts concluded by and with companies as the absence of certainty can hamper business dealings with companies which would have an impact on the economy.

The common-law principles of agency form the foundation upon which representation within the context of company law takes place. The law of agency has been adapted in the context of company law to satisfy the unique needs that have originated in this regard. One such adaptation is the creation of the *Turquand* rule by the English courts which rule was taken over by the South African courts. One of the primary reasons for creating the *Turquand* rule was due to the harsh effect that the common-law doctrine of constructive notice had on third parties dealing with a company.

In this study an examination of the current legal position regarding representation of a company in South Africa was undertaken. The history and development of the common-law principles of agency and doctrines that are unique to representation in a company law context are analysed and the relevant sections of the Companies Act 71 of 2008 are discussed. The integration of the common-law principles with the relevant provisions of the Companies Act 71 of 2008 is considered and recommendations are made in respect thereof.

In support of the analysis, a comparative study was undertaken of the history and development of this subject matter in England. It was concluded that South African company law, with all its shortcomings and uncertainties is still to be preferred above the position in England.

## OPSOMMING

Aangesien ‘n maatskappy ‘n regspersoon is, kan dit slegs deur middel van natuurlike persone as agente optree. ‘n Vraag wat as gevolg van hierdie feit ontstaan is onder watter omstandighede ‘n maatskappy deur ‘n derde party gebonde gehou kan word aan ‘n kontrak waar die maatskappy se verteenwoordiger nie gemagtig was om die kontrak aan te gaan nie. Daar behoort ‘n versigtige afweging te wees tussen die belange van die maatskappy en sy aandeelhouers aan die een kant en ‘n derde party wat met die maatskappy kontrakteer aan die ander kant. Dit is verder belangrik om regsekerheid te hê oor die geldigheid en afdwingbaarheid van kontrakte wat met maatskappye aangegaan word aangesien die afwesigheid daarvan besigheidsverkeer met maatskappye kan kortwiek wat ‘n impak op die ekonomie tot gevolg sal hê.

Die gemeenregtelike beginsels van verteenwoordiging vorm die basis waarop verteenwoordiging binne die konteks van maatskappyereg plaasvind. Verteenwoordigingsreg is aangepas binne die konteks van maatskappye om voorsiening te maak vir die unieke behoeftes wat in hierdie verband ontstaan het. Een sodanige aanpassing is die skepping van die *Turquand* reël deur die Engelse howe, welke reël deur die Suid-Afrikaanse howe oorgeneem is. Een van die hoofredes vir die skepping van die *Turquand* reël is die onregverdige uitwerking wat die gemeenregtelike leerstuk van toegerekende kennis op derde partye gehad het wat met ‘n maatskappy onderhandel.

‘n Studie van die huidige regsposisie rakende verteenwoordiging van ‘n maatskappy in Suid-Afrika is hierin gedoen. Die geskiedenis en ontwikkeling van die gemeenregtelike beginsels van verteenwoordiging en leerstukke eie aan verteenwoordiging in die konteks van maatskappyereg is geanaliseer. Die betrokke artikels van die Maatskappywet 71 van 2008 wordbespreek. Die integrasie van hierdie gemeenregtelike beginsels met die betrokke bepalings van die Maatskappywet 71 van 2008 is oorweeg en aanbevelings in verband daarmee gemaak.

Ter ondersteuning van die analise is ‘n vergelykende studie van die gekiedenis en ontwikkeling van hierdie onderwerp in Engeland onderneem. Daar is tot die slotsom gekom dat die Suid-Afrikaanse maatskappyereg, met al sy tekortkominge en onsekerhede nogsteeds bo die posisie in Engeland te verkies is.

**Keywords**

Agency
Representation
Authority
Doctrine of constructive notice
*Turquand* rule
Estoppel
Section 20(7) of the Companies Act, 2008
Section 66(1) of the Companies Act, 2008
“RF” company

**Sleutelwoorde**

Agentskap
Verteenwoordiging
Magtiging
Leerstuk van toegerekende kennis
*Turquand* reël
Estoppel
Artikel 20(7) van die Maatskappyewet 71 van 2008
Artikel 66(1) van die Maatskappywet 71 van 2008
“RF” maatskappy

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# CHAPTER 1 INTRODUCTION

## 1.1 Foundation of representation of a company

The purpose of this study is to evaluate the legal position in South Africa in terms of the common law and the Companies Act 71 of 2008 (hereinafter referred to as the Companies Act of 2008) regarding representation of companies to identify and analyse possible problem areas and shortcomings and to propose solutions to rectify identified weaknesses. The integration of the common law with the Companies Act of 2008 is also analysed in an endeavour to clarify the uncertainty regarding such integration.

When a company acts, the result may be liability by the company on grounds of delict, crime or contract. This dissertation only deals with external relationships of a company that were contractually created. The internal consequences of a contractual act are also not examined.

In order for a contract to be valid and binding on a company –

a) contracting parties must have the necessary capacity to contract (or must be deemed or presumed to have that capacity); and
b) agents effecting the transaction on behalf of parties must have the necessary authority (real or apparent) to do so (or are deemed or presumed to have that authority).[1]

These two aspects should be clearly distinguished from one another.

In both these instances, it is sometimes said that an act is *ultra vires*. An act *ultra vires* the capacity of the company and an act *ultra vires* the directors are, however, two distinct concepts. When reference is made to the capacity of a company, it means the ability of the company itself to enter into the particular transaction.[2] If the company does not have the power to perform the specific act, such act will be

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1 Sealy and Worthington *Sealy's Cases and Materials* 78.
2 Birds *et al Boyle & Birds' Company Law* 150.

*ultra vires*. When the term *ultra vires* the directors is used, it relates to acts which fall outside the authority of the directors.[3]

This dissertation does not deal with the first aspect. Only the authority of the agents who contract on behalf of the company is considered. The English and South African common law still applies in respect of this topic, although in both cases legislation has impacted on the common law.

The general principles of the law of agency form the foundation upon which representation within the context of company law takes place.[4] These principles can be found in the common law[5] and they are still in force today.[6] The law of representation in the context of company law has evolved to cater for its unique needs.[7] One such development is the creation of the *Turquand* rule by the English courts.[8] This rule was taken over by the South African courts.[9] One of the primary reasons for creating the *Turquand* rule[10] was to mitigate the harsh effect that the common-law doctrine of constructive notice had on third parties dealing with a company.[11]

### 1.2 The *Turquand* rule

Although the *Turquand* rule was created by the courts, the exact content of this rule of fairness and the sphere of its application were not clearly circumscribed. Through the passage of time the rule was developed by the courts in a casuistic

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3 Leveson *Company Directors* 95; Naudé 1971 *SALJ* 505 at 505.

4 Cilliers *et al Cilliers and Benade Corporate Law* 179.

5 *Transvaal Cold Storage Co Ltd v Palmer* 1904 TS 4 at 19. See *Inter-Continental Finance and Leasing Corporation (Pty) Ltd v Stands 56 & 57 Industria Ltd* 1979 3 SA 740 (W) 748E-F where these common-law principles were applied.

6 Delport *Nuwe Ondernemingsreg* 101.

7 Cilliers *et al Cilliers and Benade Corporate Law* 179.

8 *Smith v The Hull Glass Company* 138 ER 729; *The Royal British Bank v Turquand* (1856) 6 E&B 327 Exch Ch; *Ernest v Nicholls* 10 ER 1351 (HL).

9 *Paddon and Brock Ltd v Nathan* 1906 TS 158; *Acutt v Seta Prospecting and Developing Co Ltd* 1907 TS 799; *Welgedacht Exploration Co Ltd v Transvaal and Delagoa Bay Investment Co Ltd* 1909 TH 90; *SA Securities Ltd v Nicholas* 1911 TPD 450; *Legg & Co v Premier Tobacco Co* 1926 AD 132; *The Mine Workers' Union v Prinsloo* 1948 3 SA 831 (A).

10 Another reason for the creation of the *Turquand* rule is that a company as an independent juristic person can only act through its representatives – Oosthuizen *Turquand-reël* 123.

11 Oosthuizen *Turquand-reël* 4.

manner.[12] This resulted in conflicting decisions by the courts. The English, and sometimes, the South African courts did not, for example, regard the *Turquand* rule as an independent rule, but as an appearance form of estoppel and therefore insisted on compliance with the requirements of estoppel to succeed with a plea based on the *Turquand* rule.[13] As estoppel requires more elements to be proved than the *Turquand* rule,[14] this resulted in disturbing the balance between the interests of the company and its shareholders on the one hand, and the interests of the contracting third party on the other.[15] The possible consequence was that third parties might hesitate to contract with companies, as there was too great a risk of prejudice towards them.[16]

In South Africa the courts generally saw the *Turquand* rule as an independent rule[17] and did not make the protection of the third party dependent upon compliance with the requirements for estoppel.[18] It is, however, important to establish the boundaries within which the *Turquand* rule operates so as not to benefit the third contracting party at the expense of the company[19] and to create certainty regarding its field of operation. There is still uncertainty as to what these boundaries are.[20] Furthermore, the danger exists that the South African courts may in future fall back on decisions made by the English courts where even greater confusion regarding the sphere of application of the rule exists.[21] See, for example, *Makate v Vodacom (Pty) Ltd,*[22] referring to *One Stop Financial Services*

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12 Oosthuizen *Turquand-reël* 126 and 417.

13 *Houghton & Co v Nothard, Lowe & Wills Ltd* [1927] 1 KB 246 (CA) followed by *Kreditbank Cassel GMBH v Schenkers Ltd* [1927] 1 KB 826 (CA); *British Thomson-Houston Company Limited v Federated European Bank Limited* [1932] 2 KB 176 (CA); *Clay Hill Brick & Tile Co Ltd v Rawlings* [1938] 4 All ER 100; *Rama Corporation Ltd v Proved Tin & General Investments Ltd* [1952] 1 All ER 554 (KB); *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA); *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA); *Insurance Trust and Investments (Pty) Ltd v Mudaliar* 1943 NPD 45; *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 264; *Johaadien v Stanley Porter (Paarl) (Pty) Ltd* 1970 1 SA 394 (A) 401.

14 Rabie *Verteenwoordiging* 165.

15 Oosthuizen *Turquand-reël* 126 and 418.

16 Cassim *et al Business Structures* 144.

17 Jooste 2013 *SALJ* 464 at 465; Rabie *Verteenwoordiging* 164.

18 *The Mine Workers' Union v Prinsloo* 1948 3 SA 831 (A) at 831; Cassim *et al Contemporary Company Law* 184.

19 Oosthuizen *Turquand-reël* 124.

20 Rabie *Verteenwoordiging* 255.

21 Jooste 2013 *SALJ* 464 at 465, states that there is a school of thought that does conflate the *Turquand* rule and estoppel and refers to McLennan 1979 *SALJ* 329.

22 2016 4 SA 121 (CC) [110].

*(Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)*, where it is stated that

> [i]t has been said that the *Turquand* rule of company law is merely an application of estoppel.[23]

There is also a need for more clarity on the principle of estoppel, as applied in a company law setting. Estoppel (or ostensible authority) has been confused with implied authority[24] and more recently ostensible authority has been said to be actual authority and something other than estoppel with fewer requirements to prove.[25] This is a deviation from a long line of authorities since the early twentieth century.[26]

### 1.3 The Companies Act of 2008

With the enactment of the Companies Act of 2008 an opportunity arose for the legislature to expel any uncertainties pertaining to estoppel and the *Turquand* rule as well as their sphere of application, by codifying these rules. The legislature also had the opportunity to abrogate the doctrine of constructive notice which several writers had been advocating.[27]

The new Companies Act of 2008 indeed has more extensive provisions regarding representation and also deals with the doctrine of constructive notice.

Section 19(4) of the Companies Act of 2008 effectively abolishes the doctrine of constructive notice.[28] This abrogation should be welcomed. However, the doctrine of constructive notice still applies in relation to, *inter alia*, the so-called

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23 [2015] 4 All SA 88 (WCC) [25].

24 *Zelpy 1780 (Proprietary) Limited v Mudaly* 2015 JDR 0187 (KZP) [49]; *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 266E.

25 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC).

26 As per the minority decision in *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [109]. Also see Delport and Vorster *Henochshberg 2008* 98.

27 Du Plessis 1997 *SA Merc LJ* 281 at 284; Grobler *Toegerekende kennis* 41-46; McLennan 1986 *SALJ* 558 at 560; Oosthuizen 1979 *TSAR* 1 at 14. The doctrine was abolished in England by section 35 of the Companies Act 1985 and in Australia by section 165 of the Corporations Law of 1989 which was perpetuated by section 130 of the Corporations Act of 2001.

28 Jooste 2013 *SALJ* 464 at 468.

"RF" companies.[29] The reason why the doctrine of constructive notice has been maintained in cases of "RF" companies is unclear.[30] An "RF" company's Memorandum of Incorporation contains one or more restrictive conditions applicable to the company and any requirement for the amendment of any such condition in addition to the normal requirements for amendment which are set out in section 16 of the Act. As "restrictive conditions" are not defined in the Act, it is uncertain what these words mean. These restrictive conditions may only pertain to conditions restricting the capacity of the company to act (capacity of the company), or it may refer to conditions placing a restriction on the authority of the directors to act (representation) or to both. This uncertainty calls for clarity.

As the doctrine of constructive notice has been abolished[31] (except for the very limited instances where the doctrine still applies)[32] the questions arise as to whether there is still any room for the application of the *Turquand* rule as one of the special rules pertaining to company representation, seeing that the doctrine of constructive notice was the main reason for creating the *Turquand* rule.[33]

### 1.4 The *ultra vires* doctrine

As stated above, the capacity of the company, relating to the company itself and the authority of the directors, relating to the directors as agents of the company should be clearly distinguished from one another. The need for emphasising the differentiation between the two concepts is because the distinction has become blurred in the way that the Companies Act of 2008 has been drafted. Both these concepts are dealt with in the same section, namely section 20, where some of the subsections only pertain to the capacity of a company,[34] other subsections to the

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29 An "RF" company's Memorandum of Incorporation contains one or more restrictive conditions applicable to the company and any requirement for the amendment of such restrictive condition(s) in addition to the requirements set out in section 16 of the Companies Act of 2008. The doctrine of constructive notice applies to these restrictive conditions, provided the company's name includes the element "RF" and the company's notice of incorporation or a subsequent notice of amendment draws attention to such restrictive conditions. See s 19(5) of the Companies Act of 2008.

30 Cassim *et al Business Structures* 143.

31 S 19(4) of the Companies Act of 2008.

32 S 19(5) of the Companies Act of 2008. See the previous paragraph.

33 Cassim *et al Business Structures* 144.

34 Ss (1) and (4).

authority of directors as well as the capacity of the company[35] and others only to the authority of the directors.[36] It is not always clear whether some of the subsections of section 20 pertain to only the capacity of a company or the authority of the directors to act on behalf of a company or both. Due to the modern trend of drafting legislation in plain and understandable language, it might have been better to more clearly distinguish between these concepts by using different sections for each.

### 1.5 Statutory provisions regarding non-compliance with formal and procedural requirements

Section 20(7) of the Companies Act of 2008 introduces a rule that appears to be similar to the common-law *Turquand* rule. Instead of clarifying the uncertainty that prevails as mentioned above, it only added to it.

Some of the differences and conflicts between the *Turquand* rule and section 20(7) will be discussed. These differences and conflicts create a problem in integrating the *Turquand* rule with section 20(7). There is a presumption in the interpretation of statutes that the legislature intended to alter the existing law no more than is necessary.[37] To the extent that the common law is not amended by statute, it still applies. As the boundaries within which section 20(7) should apply have not been set out in this subsection, it would mean that it is left up to the courts to set those boundaries when dealing with section 20(7). As already mentioned, the application by the courts of the *Turquand* rule and the establishment of boundaries within which the rule may find application differ from court case to court case and have been conflated with estoppel. Furthermore, due to the conflicts between section 20(7) and the common-law *Turquand* rule, it might prove to be very difficult and artificial to supplement the statutory rule with the common law.

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35 Ss (2), (3), (5) and (6).

36 Ss (7) and (8).

37 This is subject thereto that such interpretation does not conflict with the Constitution of the Republic of South Africa 108 of 1996 and that statutory rights and remedies more advantageous to those who stand to benefit from them will take precedence over common-law rights and remedies. See Du Plessis *Re-Interpretation of Statutes* 181.

In terms of section 20(8) of the Companies Act of 2008, section 20(7) must be construed concurrently with and not in substitution for any relevant common-law principle. The common-law principle that comes to mind is the *Turquand* rule. This section can thus be interpreted that the other contracting party has a choice between relying on the statutory rule formulated in section 20(7) or on the common-law *Turquand* rule, thereby choosing the more favourable option. Conversely, this section can also be interpreted that section 20(7) must be used, but to the extent that it does not alter the common-law principles of the *Turquand* rule as created and developed by the courts.

If section 20(8) is interpreted to allow a contracting party to use either section 20(7) or the common-law *Turquand* rule, a problem arises as they conflict in certain respects.[38] The Companies Act of 2008 does not indicate which one should take precedence in the event of a conflict, as it does in respect of other possible conflicts that may arise.[39] Clarification regarding the relevant provisions of the Companies Act of 2008, as well as its integration with the common-law principles of representation in a company law context is therefore necessary.

Another common-law principle that comes to mind when reading section 20(8) of the Companies Act of 2008, is estoppel. The question whether section 20(8) also refers to estoppel needs to be answered. A clear distinction should be made between the *Turquand* rule and estoppel, as these two doctrines differ from one another and the former is not an appearance form of the latter. The question whether a third contracting party, if he has chosen to raise the statutory *Turquand* rule will be debarred from utilising any further possible remedies such as estoppel in the alternative, will also be analysed. It is, however, not the intention to do an in-depth study of estoppel. Estoppel has a very wide field of application. This study will be limited to the role of estoppel in the context of company law representation.

38 Jooste 2013 *SALJ* 464 at 469.

39 See for example sections 5(5) and 5(6) of the Companies Act of 2008.

## 1.6 Directors to manage business and affairs of the company

Another section that has been introduced in the 2008 Companies Act dealing with representation is section 66. Section 66(1) provides that the business and affairs of a company must be managed by or under the direction of the board of directors. Under the Companies Act 61 of 1973 a provision similar to section 66(1) was usually incorporated in the articles of association of a company.[40] However, the question arises as to what the position would be if the board acts according to a resolution that was taken at a meeting where the procedural requirements were not met, for example the necessary quorum was not present. Since it is not always practical for the whole board of directors to, in each and every transaction, represent the company, the board will usually delegate its authority to one director.[41] Section 66 indeed makes provision for such delegation as it provides that the business and affairs must be managed by or *under the direction* of the board.[42] In this event the question regarding the authority of the director that acts, brings one back to the application of the principles of representation in a company law context. These principles are therefore still very relevant and important and representation cannot be solved by only referring to section 66. Section 66 provides further that the Memorandum of Incorporation might provide contrary provisions regarding the authority of the board of directors. In such an instance the common-law principles regarding representation must again be reverted to. This section therefore does not expel the uncertainties pertaining to representation as entrenched in the common-law context and does not give a solution to the uncertainties and problems as discussed above.

## 1.7 Methodology

In Chapter 2 a study of the historical development of representation in England is undertaken. The reason why England is important for this study is due to the shared history that it has with South Africa in respect of company law.[43] Although Roman Dutch law forms the basis of the common-law position regarding

40 Gibson *et al Mercantile Law* 337.
41 Davies and Worthington *Gower and Davies' Company Law* 177.
42 My emphasis.
43 Rabie *Verteenwoordiging* 162.

representation (agency) in South Africa,[44] these principles were further developed by the application of English law.[45] An examination of the initial principles and the reason for the formulation of those principles that were taken over can assist in the examination of the position in South Africa. England and South Africa have, however, through legislation moved into two different directions from the common point. It would therefore be worth considering whether South Africa can benefit or learn from the new approach followed in England.

The common-law principles of agency in England and South Africa are therefore discussed in Chapter 2 and not again in Chapter 3 on South African law to avoid duplication. As the main aim of this dissertation is not to analyse the principles of agency in depth,[46] only the main features of the common-law principles of agency ("rules of attribution"[47]), which includes ostensible authority, with regard to contracts are discussed.[48] The further common-law principles and doctrines that have developed in company law that are discussed, are the doctrine of constructive notice and the *Turquand* rule.

Another reason for focusing on England is that the current Companies Act of England contains a statutory *Turquand* rule[49] discussed in Chapter 2. This lays the foundation for comparing this rule with the statutory rule that has been introduced in South Africa in section 20(7) of the Companies Act of 2008. This

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44 Kahn, Lewis and Visser *Contract and Mercantile Law* 844.

45 Rabie *Verteenwoordiging* 12 and 162.
Principles taken over from English law are for example -
a) the *Turquand* rule - *Paddon and Brock Ltd v Nathan* 1906 TS 158; *Acutt v Seta Prospecting and Developing Co Ltd* 1907 TS 799; *Welgedacht Exploration Co Ltd v Transvaal and Delagoa Bay Investment Co Ltd* 1909 TH 90; *SA Securities Ltd v Nicholas* 1911 TPD 450; *Legg & Co v Premier Tobacco Co* 1926 AD 132; *The Mine Workers' Union v Prinsloo* 1948 3 SA 831 (A); Oosthuizen *Turquand-reël* 5.
b) The doctrine of disclosure - Cilliers *et al Cilliers and Benade Corporate Law* 188.
c) The doctrine of constructive notice – Oosthuizen *Turquand-reël* 15.
d) The *ultra vires* doctrine – Rabie *Verteenwoordiging* 109-112.
e) Former company legislation of South Africa (Cape Joint Stock Companies Liability Act 23 of 1861, Transvaal Companies Act 31 of 1909) - Oosthuizen *Turquand-reël* 37.

46 Whether a company will be bound by the acts of its agent in respect of a third party in the first instance depends on the rules of agency – Griffin *Company Law* 119.

47 Davies and Worthington *Gower and Davies' Company Law* 181.

48 Sealy and Worthington *Sealy's Cases and Materials* 124; Birds *et al Boyle & Birds' Company Law* 179-188; Girvin, Frisby and Hudson *Charlesworth's Company Law* 119-123; Millet *et al Gore-Browne on Companies* 8-19 to 8-21.

49 S 40 of the Companies Act 2006.

comparison is dealt with in Chapter 4. A comparison with the Companies Act 2006[50] of England can prove useful in making recommendations.

In Chapter 3 the history of the common-law principles pertaining to representation is not discussed again. Merely a brief look is taken at its development in South African law. Thereafter relevant sections of the Companies Act of 2008 are discussed in light of the relevant common-law doctrines. The doctrines of representation as applied in South Africa are then considered in light of the development and/or abolition of similar doctrines in England.

In conclusion, the weaknesses and omissions of the application of the common law by South African courts and of the Companies Act of 2008 regarding representation are summarised in Chapter 4 and recommendations are made regarding possible improvements and amendments to the Companies Act of 2008 that will bring certainty to this important aspect of corporate law.

To the best of my knowledge the law stated in the dissertation was correct as at 30 November 2018.

[50] Companies Act 2006 (c 46), hereinafter referred to as the Companies Act 2006.

# CHAPTER 2 ENGLISH LAW

## 2.1 Introduction

Due to the exceptional nature of the company as juristic person the common-law principles of agency law as applied to companies have undergone a process of adaption and amendment.[51] In particular, the doctrine of constructive notice and the *Turquand* rule have been developed to cater for specific needs of outsiders transacting with companies.[52]

The common-law principles in England are therefore discussed first, by looking at the principles of agency, namely actual authority that can be either express or implied, the concept of usual authority and ostensible authority[53] as applied to companies, as well as common-law doctrines that have been developed specifically in the field of company law. These doctrines are the doctrine of constructive notice and the *Turquand* rule.[54] Thereafter the relevant sections of the Companies Act 2006 [55] are analysed in determining how the common law has been amended and the interaction between the Companies Act 2006 and the common law.

## 2.2 Common law

A company is an independent juristic person distinct from its shareholders and directors.[56] It is the carrier of its own rights and obligations.[57] As the company is

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51 Cilliers *et al Cilliers and Benade Corporate Law* at 179; Oosthuizen 1979 *TSAR* 1 at 1.

52 Naudé 1971 *SALJ* 505 at 505.

53 Also referred to as "apparent authority".

54 Although the law of agency in South Africa is based on our Roman-Dutch common law, the basic principles applicable to companies in particular are very similar to that of England as will become apparent in this Chapter and Chapter 3 dealing with South African law. This is primarily due to the fact that South Africa adopted the English common-law principles applicable to companies: Kahn, Lewis and Visser *Contract and Mercantile Law* 844; Rabie *Verteenwoordiging* 12 and 162.

55 Companies Act 2006 (c 46), hereinafter referred to as the Companies Act 2006.

56 Griffin *Company Law* 6*;* Pennington *Pennington's Company Law* 36. Also see s 16 of the Companies Act 2006.

57 Birds *et al Boyle & Birds' Company Law* 57; Girvin, Frisby and Hudson *Charlesworth's Company Law* 4.

only a reality in the juridical sense, it cannot act on its own but must necessarily act through agents.[58]

The authority of persons who act on behalf of a company is therefore determined by the common-law principles of agency and a special common-law principle of company law namely the *Turquand* rule.[59] Although this aspect has been largely covered in England by the Companies Act 2006, agency principles remain important in determining whether a company can be bound by the actions of its agent.[60]

In England, the principles of the law of agency determine whether a principal (irrespective of whether that principal is a company or not) will be bound by the acts of an agent who purported to act on behalf of the principal.[61]

In order to bind the company, it is necessary that the transaction with the company should have been authorised by the board or entered into by an agent with delegated authority from the board.[62]

The basis for liability of the company is therefore still determined by the common-law principles of agency. A representative who acts within the boundaries of his authority will bind the principal and not himself.[63]

As the common-law principles of agency, as developed in England, have strongly influenced South African law,[64] reference to South African sources will therefore also be made in the discussion of these common-law principles.

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58 Girvin, Frisby and Hudson *Charlesworth's Company Law* 113.

59 These principles are derived mainly from case law although statutory reforms have affected them – Birds *et al Boyle & Birds' Company Law* 150.

60 Birds *et al Boyle & Birds' Company Law* 150.

61 Davies and Worthington *Gower and Davies' Company Law* 180.

62 Griffin *Company Law* 119-120.

63 Kunst *et al Henochsberg 1973* 127; Oosthuizen 1979 *TSAR* 1 at 6.

64 Rabie *Verteenwoordiging* 12. It should be noted, however, that in *Trust Bank van Afrika Bpk v Eksteen* 1964 3 SA 402 (A) the court cautioned that doctrines of English law may not without more be taken over by South African courts but should only be used for legal comparison purposes.

### *2.2.1 Actual authority*

In both England and South Africa actual authority is seen as a legal relationship, based on an agreement between the principal (company) and the agent. The scope of the actual authority granted is to be determined by applying the ordinary principles of construction of contracts.[65] The contracting third party is not part of this agreement and may even be totally ignorant thereof.[66] Actual authority, unless the language explicitly points to the contrary, is confined to acts done for the benefit of the principal.[67] Actual authority may be expressly[68] or impliedly granted by the principal to the agent[69] and can include usual authority.

In England, the board of directors has express actual authority to exercise those powers of the company which are vested in it by the company's memorandum and articles.[70] The board must act collectively.[71] The board of directors will, however, not usually act as a body on behalf of the company in the day to day transactions entered into by the company.[72] In such an instance the board should delegate authority to an agent. The board will only be authorised to delegate authority to such an agent if the board is duly empowered to do so by the articles of the company.[73]

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65 This includes any implications from the express words used, trade usages and the course of business between the principal and agent.

66 *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 1 QB 480 (CA) 502-503 per Diplock LJ.

67 Blackman *et al Commentary* ch 4 30; Montrose 1934 *LQR* 224 at 228.

68 Express authority could have been granted in words (orally) or in writing. Examples where express authority is given are in a power of attorney, board resolution and letters of authority – Reynolds *Bowstead and Reynolds Agency* 106 para 3-003.

69 Munday *Agency* 43. Also see Reynolds *Bowstead and Reynolds Agency* 105 para 3-003; Birds *et al Boyle & Birds' Company Law* 179; Davies and Worthington *Gower and Davies' Company Law* 181.

70 Birds *et al Boyle & Birds' Company Law* 179; Griffin *Company Law* 120.

71 Pennington *Pennington's Company Law* 145

72 Millett *et al Gore-Browne on Companies* 8-19.

73 Pennington *Pennington's Company Law* 145. Other than in England, the power of the board under South African law is not delegated authority, but original. See para 3.3.1.1 in Ch 3.

The delegation by the board to an agent can take place either expressly[74] or impliedly. When delegation has taken place, the scope of authority of the agent must be determined.[75]

Express authority is authority that has been granted through explicit words or actions.[76] It could have been granted either in writing or orally.[77] Usually this type of authority does not present any problems.[78]

Authority is implied when it is inferred from the conduct of the parties and the circumstances of the case, such as when the board of directors appoints one of their number to be a managing director or where it can be regarded as customary authority.[79] They thereby impliedly authorise him to do all such things as would fall within the usual scope of that office.[80] Authority will also be implied if the agent performs acts that are reasonably incidental to the proper performance of these duties[81] (to the extent that such reasonable incidental acts are not expressly excluded by the principal).[82] An agent therefore has implied authority in respect of

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74 This authority can be delegated by means of, for example, the memorandum of incorporation or by a resolution of the shareholders or directors – *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) 14.

75 Davies and Worthington *Gower and Davies' Company Law* 180.

76 Delport and Vorster *Henochsberg 2008* 95.

77 Kerr *Agency* 64; Benade *et al Entrepreneurial Law* 146.

78 Rabie *Verteenwoordiging* 15.

79 *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA) 583; Birds *et al Boyle & Birds' Company Law* 179; Munday *Agency* 50. Munday *Agency* at 56 states that a party to a contract can only be bound by usages that apply in the market within which the agent operates if those usages are certain, notorious and reasonable; Reynolds *Bowstead and Reynolds Agency* 106, para 3-003 and at 135 para 3-039. The authority of the agent under these circumstances is expanded by the acquiescence of his principal when the agent exercises further powers.

80 *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA) 583 per Lord Denning MR.

81 This would be the case where the agent has implied authority to do whatever is necessarily or normally incidental to the act for which he has received express authority – see Reynolds *Bowstead and Reynolds Agency* 106 para 3-003.

82 Davies and Worthington *Gower and Davies' Company Law* 181 as per Lord Denning in *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA); Girvin, Frisby and Hudson *Charlesworth's Company Law* 120. In *SMC Electronics Ltd v Akhter Computers Ltd* [2001] 1 BCLC 433 (CA) a company was therefore held liable for the acts of its director on grounds of implied authority even where that director's employment contract was potentially ambiguous.

> … matters that are necessary to enable him to perform the ordinary duties incidental to his position as agent or which form part of the ordinary course of business transacted by that agent.[83]

Implied authority may also arise as a reasonable inference from the course of conduct (dealing) of the principal (company), where the company, through the person or persons empowered to confer a mandate, acquiesces in the activities of the agent.[84]

Implied authority constitutes actual authority and it is not ostensible authority.[85] In many instances it is not possible to ascertain whether the English courts in the nineteenth century based their decision on implied actual authority or ostensible authority and in some of those cases where it is clear that the court's finding is based on ostensible authority, the courts have termed it as implied authority.[86]

Actual authority (whether express or implied) is binding between the company and the agent and also between the company and others, whether they are within or outside the company.[87]

In England the usual authority of an agent or representative can be described as the authority to execute those legal acts that are normally attributable to the position of representatives or officers of that class.[88] Usual authority can therefore take on several different forms: [89]

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83 In *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) 14. Also see Blackman *et al Commentary* ch 4 29.

84 *De Villiers and Another NNO v BOE Bank Ltd* 2004 3 SA 1 (SCA); *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) 14-15; *Rosebank Television & Appliance Co (Pty) Ltd v Orbit Sales Corporation (Pty) Ltd* 1969 1 SA 300 (T) 303; *Coetzer v Mosenthals* [1963] 3 All SA 484 (A); *Dickson v Acrow Engineers (Pty) Ltd* [1954] 1 All SA 308 (W) 311; Davies and Worthington *Gower and Davies' Company Law* 181. In other words, authority may be implied from the conduct of the parties and the circumstances of the case, as per *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA). Also see *Fusion Interactive Communication Solutions Ltd v Venture Investment Placement Ltd* [2006] BCC 187 (Ch).

85 *Coetzer v Mosenthals Ltd* [1963] 3 All SA 484 (A) at 486-487; Kerr *Agency* 67.

86 Reynolds *Bowstead and Reynolds Agency* 107 para 3-005 and 337 para 8-016. Also see Millett *et al Gore-Browne on Companies* 8-22 and Du Plessis *Grondslae* 192-199.

87 *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA) 583 per Lord Denning MR. Also see Reynolds *Bowstead and Reynolds Agency* 106 para 3-004.

88 Oosthuizen *Turquand-reël* 45. See *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 502-505 and *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA) 583, 593. This is also the position under South African law.

89 Birds *et al Boyle & Birds' Company Law* 180.

First the usual authority could have been expressly granted to the representative. That is called express authority.

Secondly, usual authority can also have been granted impliedly. Over and above the authority that has been expressly granted to an agent, an agent also has the authority that is necessary to comply with his obligations towards his principal as well as authority normally, in terms of trade usage, granted to an agent. If this implied authority has not expressly been limited by the principal (company), this implied authority, which is nothing more than usual authority, equals actual authority.[90] In this instance it can be termed "implied usual authority".[91]

In respect of the abovementioned two instances there is no defect in the authority of the representative.[92]

According to *Bowstead and Reynolds* the English courts do not regard usual authority as an independent type of authority.[93] Usual authority is, therefore, not a separate ground on which a company can be held liable. It is merely an aid to determine whether the company can be held bound on grounds of either implied authority, ostensible authority or the *Turquand* rule.[94]

### *2.2.2 Doctrine of constructive notice and Turquand rule*

In applying the law of agency in a company law context, there are two additional aspects that have an impact on whether, in common law, a company can be held bound to a contract. These are first, that a contracting third party, through the

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90 Birds *et al Boyle & Birds' Company Law* 180; Reynolds *Bowstead and Reynolds Agency* 108 para 3-006; Girvin, Frisby and Hudson *Charlesworth's Company Law* 120 and Griffin *Company Law* 120; Rabie *Verteenwoordiging* 16.

91 Cassim *et al Contemporary Company Law* 191; Griffin *Company Law* at 120 speaks about usual (real) authority.

92 Where the usual authority of the agent has been restricted or limited by private instruction or where such authority has been made dependent on the compliance with certain conditions which have not been complied with, a third party who is unaware that limitations or restrictions have been placed on the usual authority of the agent may still hold the company bound on grounds of ostensible authority or the *Turquand* rule. See paras 2.2.2 and 2.2.3 below.

93 Reynolds *Bowstead and Reynolds Agency* 110 para 3-006.

94 Usual authority is also not regarded as an independent type of authority in the law of agency in South Africa. See Rabie *Verteenwoordiging* 16.

doctrine of constructive notice, is deemed to know the content of a company's public documents; and secondly, that since a company cannot itself act, it must do so through agents whose authority may have been made dependent on compliance with some or other internal requirement.[95]

The doctrine of constructive notice was developed in the nineteenth century by the English courts[96] entailing that any person dealing with a company registered under the companies' legislation was deemed to have notice of its "public documents" (which would include the company's then memorandum and now articles of association)[97] which are required to be filed at the Companies House.[98] The doctrine of constructive notice originated from the fact that the courts treated companies in the same way as partnerships in matters of representation.[99]

In terms of this doctrine any person negotiating with a company is deemed to have knowledge of the arrangement of powers as it is set out in the public documents[100] of the company.[101] The basis for this doctrine lies in the publicity that is given to such public documents.[102] A third party contracting with the company is therefore deemed to be aware of any limitation imposed on the authority of company

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95 Although the common-law position pertaining to the first aspect has been affected by the Companies Act 2006, such impact can only be appreciated if the common-law position is considered. The same applies to the situation in South Africa: see Chapter 3 para 3.2.2 below.

96 See for example the celebrated case of *Ernest v Nicholls* 10 ER 1351 (HL) and *Mahony v The East Holyford Mining Co Ltd* (1874-75) LR 7 (HL) 869.

97 *The Royal British Bank v Turquand* (1856) 6 E&B 327; Davies and Worthington *Gower and Davies' Company Law* 169; Morse *et al Palmer's Company Law* 3044; Millett *et al Gore-Browne on Companies* 8-13; Griffin *Company Law* 110; Benade *et al Entrepreneurial Law* 147; Oosthuizen 1979 *TSAR* 1 at 4; Delport 2011 *THRHR* 132 at 133; McLennan 2009 *Obiter* 144 at 145.

98 Davies and Worthington *Gower and Davies' Company Law* 169; Millett *et al Gore-Browne on Companies* 8-13; Griffin *Company Law* 110; Reynolds *Bowstead and Reynolds Agency* 348 para 8-034; Pennington *Pennington's Company Law* 129. Also see *The Royal British Bank v Turquand* (1856) 6 E&B 327 Exch Ch; *Ernest v Nicholls* 10 ER 1351 (HL).

99 See Oosthuizen *Turquand-reël* 92(3). Before the Companies Act of 1844 (England) the position of joint stock companies was governed by the ordinary law of partnership – Montrose 1934 *LQR* 224 at 236.

100 Although it is unsure what would constitute all the public documents of a company, it would include the constitution of the company, in other words the memorandum and articles of association. These documents have been accepted as public documents in *Ernest v Nicholls* 6 HLC 401 and *Mahony v The East Holyford Mining Co Ltd* (1874-75) LR 7 HL 869. Public documents would be those documents registered at the Companies Registry - Birds *et al Boyle & Birds' Company law* 178.

101 Oosthuizen *Turquand-reël* 1; Oosthuizen 1977 *TSAR* 210; Oosthuizen 1977 *TSAR* 1 at 6.

102 Oosthuizen *Turquand-reël* 2; Oosthuizen 1977 *TSAR* 210; Oosthuizen 1977 *TSAR* 1 at 6.

officials.[103] It is irrelevant whether the third party has actual knowledge or whether it could reasonably have been expected of him to have notice thereof. Logically, this would mean that where the authority of the board has, for example, been made dependent on the compliance of certain internal requirements, the third party, in light of his knowledge thereof (actual or constructive), is placed on his guard and must investigate further to determine whether there was compliance with the prerequisites for authority.[104]

Whether the necessary procedures have been followed will not be gleaned from the public documents.[105] Indirectly this duty to investigate is therefore extended to those aspects to which no publicity is given. As no publicity is given to the internal administration of the company it would be unfair and unrealistic to expect from an outsider to ascertain whether certain requirements have been complied with or whether a particular agent has indeed been given the required authority.[106] Examples of internal management are where the authority of the board has been made dependant on sanction by the general meeting, whether the officers of the company have been duly appointed, whether meetings have been properly summoned and conducted, whether the necessary quorum requirements have been adhered to and whether resolutions have been passed by the requisite majorities.[107] The third party can at most obtain knowledge of the potential authority of a representative.[108]

The *Turquand* rule was introduced and developed by the English courts[109] to temper the unfair operation of the doctrine of constructive notice[110] because the

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103 Any limitation of the capacity of the company will necessarily also be a limitation on the authority of the directors.

104 Oosthuizen 1977 *TSAR* 1 at 6.

105 Millett *et al Gore-Browne on Companies* 8-13

106 Oosthuizen *Turquand-reël* 2; Oosthuizen 1977 *TSAR* 210; Oosthuizen 1977 *TSAR* 1 at 6.

107 Sealy and Worthington *Sealy's Cases and Materials* 116.

108 Oosthuizen 1977 *TSAR* 1 at 6.

109 *The Royal British Bank v Turquand* (1856) 6 E&B 327 Exch Ch; *Mahony v The East Holyford Mining Co Ltd* (1874-75) LR 7 (HL) 869; *Kreditbank Cassel GMBH v Schenkers Ltd* [1927] 1 KB 826 (CA); *British Thomson-Houston Company Limited v Federated European Bank Limited* [1932] 2 KB 176 (CA).

110 Birds *et al Boyle & Birds' Company Law* 178; Oosthuizen 1977 *TSAR* 210.

third contracting party does not have access to the internal administration of the company.[111]

In *The Royal British Bank v Turquand*[112] from whence the rule derives its name, it was formulated as follows:

> We may now take for granted that the dealings with these companies are not like dealings with other partnerships, and that the parties dealing with them are bound to read the statute and the deed of settlement. But they are not bound to do more. And the party here, on reading the deed of settlement, would find, not a prohibition from borrowing, but a permission to do so on certain conditions.[113] Finding that the authority might be made complete by a resolution, he would have the right to infer the fact of a resolution authorizing that which on the face of the document appeared to be legitimately done.[114]

The third party's knowledge (actual or constructive) of the company's constitution will only reveal, for example that the authority in question might have been conferred upon the agent.[115] Provided the agent would otherwise be held to have authority to enter into the transaction in question, the third party's claim is not to be defeated solely on grounds of the non-compliance with some or other internal formality.[116] In terms of the *Turquand* rule a third party (outsider) negotiating with a company in good faith is therefore entitled to assume that the internal management[117] and procedures required by the articles of that company have properly taken place.[118]

The third party is not released from his duty to investigate matters which receive publicity, but his duty is limited to those aspects.[119] The third party is therefore

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111 Oosthuizen *Turquand-reël* 4. The *Turquand* rule was also imported from England into South Africa. See Ch 3 para 3.2.2.

112 (1856) 5 E & B 248 and on appeal 119 ER 886; (1856) 6 E & B 327. This rule was laid down by the court of the Queen's Bench and confirmed by the Exchequer Chamber.

113 In other words, the agent is authorised to act, but his authority is subject to compliance with some or other internal requirement.

114 (1856) 6 E & B 327 per Jervis CJ at 332. The *Turquand* rule was approved and applied in *Mahony v East Holyford Mining Co Ltd* (1874-75) LR 7 (HL) 869.

115 In other words, the constitution of the company provides merely for the potential authority of the agents, for example that a managing director may be appointed and certain authority may be delegated to him, or that certain powers may be granted to a director or particular official of the company – Cilliers *et al Cilliers and Benade Corporate Law* 191.

116 Morse *et al Palmer's Company Law* 3053.

117 Also known as indoor management.

118 Sealy and Worthington *Sealy's Cases and Materials in Company Law* 117; Oosthuizen 1977 *TSAR* 210 at 210. Cilliers *et al Celliers and Benade Corporate Law* 191.

119 Oosthuizen 1977 *TSAR* 210; Oosthuizen 1977 *TSAR* 1 at 6.

protected against the internal irregularities in respect of which no publicity is given.[120] If that third party acts *bona fide*, he is entitled to assume that the internal management of the company has been conducted properly and that all internal requirements have been met. He does not need to make further investigations in that regard.[121] He therefore does not need to satisfy himself for example that the directors' meeting has been convened on proper notice, or whether a quorum was present or whether the directors have properly been appointed.[122] In instances where the internal management has not properly taken place, the *Turquand* rule can therefore assist the third party to hold the company bound if the transaction was not contrary to the constitution of the company.[123] In this way the *Turquand* rule tempers the unrealistic and unfair operation of the doctrine of constructive notice and third parties are protected in the process.

The *Turquand* rule therefore did not abolish the doctrine of constructive notice but only limited the extent of the investigation that is required from a third party to those aspects to which publicity is given.[124]

Without the *Turquand* rule, the transacting of business with companies would be very cumbersome, laborious and risky to third parties and even impossible, as a third party would not have access to the internal management of a company to ensure that the transaction that he is about to conclude with that company was duly authorised.[125] The rule was therefore created to make negotiations with companies simpler and thereby improve the position of the third contracting party.[126] Although one reason for this rule is business convenience, a much more

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120 Oosthuizen 1977 *TSAR* 210.

121 Oosthuizen 1977 *TSAR* 1 at 6.

122 Leveson *Company Directors* 97.

123 Oosthuizen 1977 *TSAR* 1 at 6; Oosthuizen *Turquand-reël* 2.

124 *SA Securities v Nicholas* 1911 TPD 450.

125 *Legg & Co v Premier Tobacco Co* 1926 AD 132 at 143-144 and quoted with approval in *Wolpert v Uitzigt Properties (Pty) Ltd and Others* 1961 2 SA 257 (W) at 264. Also see *Morris v Kanssen* [1946] 1 All ER 586 at 592; [1946] AC 459 at 475 per Lord Simonds:

> The wheels of business will not go smoothly round unless it may be assumed that that is in order which appears to be in order.

126 In *The Mineworkers' Union v Prinsloo* 1948 3 SA 831 at 845 it was stated that the *Turquand* rule is based

> … on the principle of convenience, for business could not be carried on if a person dealing with the apparent agents of a company was compelled to call for evidence that all internal regulations had been duly observed.

Also see *Morris v Kanssen* [1946] AC 459 at 475; [1946] 1 All ER 586 at 592 (HL); Blackman *et al Commentary* ch 4 34; Cassim *et al Contemporary Company Law* 181.

important reason is the fact that a person dealing with a company does not have a right to insist on proof that the provisions of the memorandum and articles of the company have been complied with. He can therefore not be penalised by the attribution of constructive notice for a failure to comply with these provisions which he is unable to verify.[127] *Palmer's* regards the *Turquand* rule as

> … eminently practical, for business could not be carried on if a person dealing with the apparent agents of a company was compelled to call for evidence that all internal regulations had been duly observed.[128]

The *Turquand* rule amends the normal principles of agency.[129] This rule operates in favour of the contracting third party (outsider) against the company. If this rule is applied without setting down certain boundaries within which it can find application, the scale would tip too heavily in favour of the third contracting party to the detriment of the company, which is compelled to contract through representatives.[130] Although the exact boundaries within which the rule finds application are still uncertain,[131] the operation of the rule has been limited in the following respects:[132]

i) It does not find application in dealings between natural persons.[133]

ii) Where the third contracting party knew (or was deemed to know, due to the operation of the doctrine of constructive notice) that the internal requirements set down in the articles of the company have not been complied with.[134]

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127 Pennington *Pennington's Company Law* at 130 Also see *County of Gloucester Bank v Rudry Merthyr Steam and House Coal Colliery Co* [1895] 1 Ch 629 at 636 per Lindley LJ.

128 Morse *et al Palmer's Company Law* at 3053. The doctrine of constructive notice in English law has been abolished insofar as the third contracting party can bring the relevant transaction within the scope of s 40 of the Companies Act 2006. S 40 is discussed in para 2.3 below. If not, then the doctrine of constructive notice still operates and if an agent acts on behalf of a company in contravention with a provision in the articles of the company that deprives him of authority, it will still be deemed that the third party had knowledge of such limitation on the authority of such agent even if such third party did not have knowledge thereof as he did not actually read the articles of the company. In such an instance the application of the *Turquand* rule still plays a relevant and much needed role in assisting the third contracting party to hold the company to the contract.

129 Oosthuizen *Turquand-reël* 124.

130 Oosthuizen 1979 *TSAR* 1 at 10.

131 Rabie *Verteenwoordiging* 255; Du Plessis *Grondslae* 207-210.

132 Cilliers *et al Cilliers and Benade Corporate Law* 192; Van Dorsten *Company Directors* 160.

133 *The Mine Workers' Union v Prinsloo* 1948 3 SA 831 (A); *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 264F.

134 See for example the following English judgments and authors: *Criterion Properties Plc v Stratford UK Properties LLC* [2004] 1 WLR 1846 (HL) 1856; *Rolled Steel Products*

iii) Where there are reasonable grounds for suspecting that the representative of the company did not have the necessary authority to act on behalf of the company.[135] There are reasonable grounds for suspicion if a transaction is so unusual as to put the third contracting party on inquiry.[136]

iv) The act which the organ or officer performs on behalf of the company must be one that is normally consistent with that position (in other words, the organ or officer had to act within his usual authority[137]).[138] The act of the representative must therefore be of such a nature that it does not make the third party suspicious.

v) In cases of fraud.[139]

The English courts have confused the *Turquand* rule with estoppel, seeing it as just another form of estoppel.[140] This confusion led to the apparent extension of the application of the *Turquand* rule to situations for which it was not originally

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*(Holdings) Ltd v British Steel Corporation* [1986] Ch 246 (CA) 284 and 304; Birds *et al Boyle & Birds' Company Law* 178; Morse *et al Palmer's Company Law* 3053.
This is also the case in South African law. See for example: *Levy v Zalrut Investments (Pty) Ltd* 1986 4 SA 479 (W) 487B-C*; Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 266; *Burstein v Yale* 1958 1 SA 768 (W) 772; *The Mineworkers' Union v Prinsloo* 1948 3 SA 831 (A) 845 and 849. Also see Cilliers *et al Cilliers and Benade Corporate Law* 192; Blackman *et al Commentary* ch 4 34-1.

135 *Big Dutchman (South Africa) (Pty) Ltd v Barclays National Bank Ltd* 1979 3 SA 267 (W) 284-285.

136 English decisions in this regard are: *Wrexham Association Football Club v Crucialmove Ltd* [2007] BCC 139; *Rolled Steel Products (Holdings) Ltd v British Steel Corporation* [1986] Ch 246 (CA) 284. Also see Davies and Worthington *Gower and Davies' Company Law* 170-171; Morse *et al Palmer's Company Law* 3058; Birds *et al Boyle & Birds' Company Law* 178; Millett *et al Gore-Browne on Companies* 8-13; Pennington *Pennington's Company Law* 130.
Judgments in South Africa include *Big Dutchman (South Africa) (Pty) Ltd v Barclays National Bank Ltd* 1979 3 SA 267 (W) 280; *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 266. Also see Cilliers *et al Cilliers and Benade Corporate Law* 192.

137 For acts within usual authority in English law, see *British Thomson-Houston Company Limited v Federated European Bank, Limited* [1932] 2 KB 176 (CA) 181; *Freeman and Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA). In South Africa see *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W).

138 For an English judgment see *Rama Corporation Ltd v Proved Tin and General Investments Ltd* [1952] 1 All ER 554 (KB).
Examples of South African decisions include *Holgate v Minister of Justice* 1995 3 SA 921 (E) 932; *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 265-267; *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) 14-15. This requirement would have excluded the application of the *Turquand* rule in situations such as *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W).

139 See *Ruben v Great Fingall Consolidated* [1906] AC 439, HL, particularly per Lord Loreburn LC at 443; Griffin *Company Law* 123; Girvin, Frisby and Hudson *Charlesworth's Company Law* 124-125 in respect of English law and Cilliers *et al Cilliers and Benade Corporate Law* 192 for South African law.

140 *Kreditbank Cassel GMBH v Schenkers Ltd* [1927] 1 KB 826 (CA); *Houghton & Co v Nothard, Lowe & Wills Ltd* [1927] 1 KB 246 (CA).

intended. The courts applied another legal rule, usually estoppel, and the success of a third party was made dependant on compliance with the requirements laid down for estoppel. The courts, however, then labelled the doctrine as being that of the *Turquand* rule instead of estoppel.[141] This has led to a lot of confusion and the requirements to be successful with an estoppel have been supplanted by the application of the *Turquand* rule.[142] The *Turquand* rule should, however, be seen as an independent rule. There is also support for this approach in England.[143]

### *2.2.3 Ostensible authority*[144]

Ostensible authority is described in *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [145] as a

> … legal relationship between the principal and the contractor created by a representation, made by the principal to the contractor, intended to be and in fact acted upon by the contractor, that the agent has authority to enter on behalf of the principal into a contract of a kind within the scope of the 'apparent' authority, so as to render the principal liable to perform any obligations imposed upon him by such contract. To the relationship so created the agent is a stranger. He need not be (although he generally is) aware of the existence of the representation but he must not purport to make the agreement as principal himself. The representation, when acted upon by the contractor by entering into a contract with the agent, operates as an estoppel, preventing the principal from asserting that he is not bound by the contract. It is irrelevant whether the agent had actual authority to enter into the contract.[146]

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141 A typical example hereof is *Houghton & Co v Nothard, Lowe & Wills Ltd* [1927] 1 KB 246, CA

142 McLennan 2009 *Obiter* 144 at 150; Du Plessis *Grondslae* 166.This conflation of the *Turquand* rule and ostensible authority (estoppel) also affected South African writers and courts. See Ch 3 para 3.3.2.5 below.

143 Millett *et al Gore-Browne on Companies* 8-14; Pennington *Pennington's Company Law* 130.

144 Also called apparent authority. The term "ostensible authority" is actually a misnomer, as it does not constitute authority at all. It is sometimes referred to as "estoppel", "estoppel by representation" or "agency by estoppel". See for example *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 498 and 503; *Ebeed (trading as Egyptian International Foreign Trading Co) v Soplex Wholesale Supplies Ltd and P S Refson and Co Ltd (The Raffaella)* [1985] BCLC 404 (CA) 411; *Ernest v Nicholls* 10 ER 1351 (HL) 412; *Rama Corporation Ltd v Proved Tin & General Investments Ltd* [1952] 1 All ER 554 (KB) 556; *Kreditbank Cassel GMBH v Schenkers Ltd* [1927] 1 KB 826 (CA) 835.

145 [1964] 2 QB 480 (CA) per Diplock LJ.

146 *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 503, per Diplock LJ.

The burden of proof lies with the person alleging ostensible authority,[147] in other words, on the third party contracting with the company.

For a more modern formulation, ostensible authority is described in *ING Re (UK) Ltd v R & V Versicherung AG* [148] as follows:

> The doctrine of apparent or ostensible authority is based on estoppel by representation. Where a principal (P) represents or causes it to be represented to a third party (T) that an agent (A) has authority to act on P's behalf, and T deals with A as P's agent on the faith of that representation, P is bound by A's acts to the same extent as if A had the authority which he was represented as having.[149]

It is possible for a company to be bound by a contract with a third party if, although the agent acting on behalf of the company did not have actual authority, the agent had ostensible authority to bind the company.[150] Actual and ostensible authority may overlap, coincide and co-exist,[151] but either one of the two may exist without the other and their respective scopes may be different.[152] Ostensible authority can for example be present in the instance where the agent has no actual authority.[153]

In this regard the relationship between ostensible (apparent) authority and actual authority has been stated to be as follows:

> [A]pparent authority … often coincides with actual authority. Thus, when the board appoint one of their number to be managing director, they invest him not only with implied authority, but also with ostensible authority to do all such things as fall within the usual authority of a managing director.[154]

147 Reynolds *Bowstead and Reynolds Agency* 337 para 8-016.
148 [2006] EWHC 1544 (Comm), per Toulson J.
149 *ING Re (UK) Ltd v R&V Versicherung AG* [2006] EWHC 1544 (Comm) [99].
150 Girvin, Frisby and Hudson *Charlesworth's Company Law* 120. According to *Charlesworth's Company Law* (at 121) actual and ostensible authority are not mutually exclusive and may in certain instances co-exist.
151 *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA) 583 per Lord Denning MR; Munday *Agency* 61.
152 *Freeman & Lockyer v Buckhurst Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 502 per Lord Diplock LJ.
153 Birds *et al Boyle & Birds' Company Law* 180; Munday *Agency* 52 and 61; Reynolds *Bowstead and Reynolds Agency* 107 para 3-005.
154 *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 459 (CA) 583.

If that is the case, usual as well as ostensible authority will apply and they are therefore not mutually exclusive.[155]

According to Munday[156] it is no easy task to establish the legal foundation of ostensible authority especially since the decisions of the courts are difficult to reconcile, as the court itself has admitted. In this regard the following is stated in *Rama Corporation Ltd v Proved Tin & General Investments Ltd*:[157]

> Ostensible or apparent authority … is merely a form of estoppel and has been termed agency by estoppel, and a party cannot call in aid an estoppel unless three ingredients are present: (i) a representation, (ii) a reliance on a representation, and (iii) an alteration of his position resulting from such reliance.[158]

The contracting third party will not be able to rely on the ostensible authority of the agent and thereby seek to bind the company if the third party knew that the agent did not have actual authority to bind the company.[159] The third party will also not be able to enforce a contract against a company if he was put on inquiry as to whether the agent was acting within his authority because of, for example, suspicious circumstances. In other words, the third party ought to have known that the agent did not have actual authority to act.[160]

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155 *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 459 (CA) 593 per Lord Pearson Birds *et al Boyle & Birds' Company Law* 180-181; Munday *Agency* 52; Morse *et al Palmer's Company Law* 3054; Reynolds *Bowstead and Reynolds Agency* 107 para 3-005.

156 Munday *Agency* 62. See for example *Thanakharn Kasikorn Thai Chamkat (Mahachon) v Akai Holdings Ltd (in liquidation)* [2010] HKCFA 64 at [42] per Lord Neuberger of Abbotsbury NPJ.

157 [1952] 1 All ER 554 (KB).

158 [1952] 1 All ER 554 (KB) at 556 per Slade, J.

159 *Criterion Properties plc v Stratford UK Properties LLC* [2004] 1 WLR 1846 (HL); Davies and Worthington *Gower and Davies' Company Law* 185; Millett *et al Gore-Browne on Companies* 8-22; Sealy and Worthington *Sealy's Cases and Materials* 107; Griffin *Company Law* 121; Pennington *Pennington's Company Law* 149; Munday *Agency* 73; Reynolds *Bowstead and Reynolds Agency* 361 para 8-050; Morse *et al Palmer's Company Law* 3053.

160 *AL Underwood, Limited v Bank of Liverpool and Martins* [1924] 1 KB 775; *Rolled Steel Products (Holdings) v British Steel Corporation* [1986] Ch 246 (CA); The duty to enquire as to the authority of the agent is only present under circumstances where the agent performs an act that an agent of his type would not normally transact. Also see Reynolds *Bowstead and Reynolds Agency* 362 para 8-051. This is also the current position. See for example *Hopkins v TL Dallas Group Ltd* [2004] EWHC 1379 (Ch); *Criterion Properties plc v Stratford UK Properties LLC* [2004] 1 WLR 1846 (HL) 1856; Millett *et al Gore-Browne on Companies* 8-22; Davies and Worthington *Gower and Davies' Company Law* 185 Pennington *Pennington's Company Law* 150; Morse *et al Palmer's Company Law* 3053; Munday *Agency* 86.

The classic case in which the requirements to succeed with reliance on ostensible authority were laid down is *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd*.[161] These requirements are that –

(i) there must have been a representation that the agent had the authority to enter on behalf of the company into a contract of the kind sought to be enforced;

(ii) the representation must have been made by a person or persons who themselves had actual authority to manage the business of the company either generally or in respect of those matters to which the contract relates;

(iii) the third party must have relied upon the representation;

(iv) the company should not under its memorandum or articles of association have been deprived of the capacity to enter into a contract of the kind sought to be enforced.

2.2.3.1 Representation of authority

Without a representation there cannot be ostensible authority, as the basis for ostensible authority is a representation.[162] The representation can be made in different ways.

A representation can be made by words or conduct, including acts, omissions or silence.[163] The representation may for example be contained in the company's public documents[164] or in the power of attorney granted to the agent[165] or in the official correspondence of the company that a particular person possesses the necessary authority.[166] Representation by the company can therefore also entail a

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161 [1964] 2 QB 480 (CA) 506 per Diplock LJ.

162 Reynolds *Bowstead and Reynolds Agency* 337 para 8-017.

163 Griffin *Company Law* 121; *Universal Stores Ltd v OK Bazaars* 1973 4 SA 747 (A) 761; *Insurance Trust and Investments (Pty) Ltd v Mudaliar* 1943 NPD 45 at 54.

164 Girvin, Frisby and Hudson *Charlesworth's Company Law* 121; Also see *Lovett v Carson Country Homes Ltd* [2011] BCC 789 (Ch). If the third party relies on a representation in the company's constitution, such reliance must be as a direct result of the third party's actual knowledge thereof – Griffin *Company Law* 121; Pennington *Pennington's Company Law* 151. The doctrine of constructive notice, which has only a negative application, cannot be applied in such an instance. See Davies and Worthington *Gower and Davies' Company law* 186.

165 *Mercantile Bank of India Ltd v Chartered Bank of India, Australia and China* [1937] 1 All ER 231.

166 *Rama Corporation Ltd v Proved & and General Investments Ltd* [1952] 1 All ER 554 (KB).

representation by the members or the board of directors,[167] or duly authorised executive[168] being a positive statement that the agent is authorised, or it may arise out of the conduct of the members or directors whereby they acquiesce in the acts of the agent, with full knowledge thereof.[169]

Where a company appoints a representative in a particular position it creates the appearance that that representative possesses all the powers which are normally associated with that office. In such event the authority of the officer could have been restricted by a confidential agreement between the company and the officer. Where that officer then exceeds his authority the third party can rely on ostensible authority to hold the company bound to the acts of its agent.[170] What the precise extent of the officer's authority will be is, however, a question of fact that must be determined by taking into account the usage in trade, the nature of the business and the position that the representative holds in the company.[171]

The representation may also be implied by previous dealings between the parties.[172] In other words, the holding out should be determined by looking at the factual circumstances of each case.[173]

2.2.3.2 Representation made by person with actual authority to manage the business

The representation must have been made by the company and not by the agent. A particular difficulty arises with this requirement in the case of a company as a company can only act through human agency. The question that arises is which representatives' representation will be regarded as that of the company.

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167 Girvin, Frisby and Hudson *Charlesworth's Company Law* 121.

168 Griffin *Company Law* 121.

169 *Hely-Hutchinson v Brayhead Ltd* 1 QB 549 (CA) 592 per Pearson LJ; *Freeman & Lockyer v Buckhurst Properties (Mangal) Ltd* [1964] 2 QB 480 (CA); Birds *et al Boyle & Birds' Company Law* 184; Morse *et al Palmer's Company Law* 3056; Reynolds *Bowstead and Reynolds Agency* 337 para 8-017.

170 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [165] per Wallis AJ.

171 *Kreditbank Cassel GMBH v Schenkers Ltd* [1927] 1 KB 826 (CA). For the position in South Africa in this regard, see Ch 3 para 3.2.3.1.

172 Munday *Agency* 68; Reynolds *Bowstead and Reynolds Agency* 337 para 8-017.

173 Birds *et al Boyle & Birds' Company Law* 184. See the remarks of Pearson LJ in *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 498 as qualified by his later remarks in *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA) 593.

This question was analysed in *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [174] where it was required that the representation as to the authority of the agent had to be made by some person or persons who have "actual" authority to manage the business of the company either generally or in respect of those matters to which the contract relates.[175] The agent himself can therefore not represent that he has more authority than what he in actual fact has[176] and generally neither can an agent who does not have authority represent that someone else has authority, who does not really have authority.[177]

In *Ebeed (trading as Egyptian International Foreign Trading Co) v Soplex Wholesale Supplies Ltd and P S Refson and Co Ltd (The Raffaella)*[178] Browne-Wilkinson LJ remarked *obiter* that a third party should be able to rely, as part of the holding out by a company, on a representation by an agent with ostensible authority about the authority of another agent of the company to enter into a transaction, where such representation was incorrect.[179]

This was confirmed in *ING Re (UK) Ltd v R&V Versicherung AG*,[180] but the court added that the critical requirement is that the authority of the second agent, who enters into the transaction on behalf of the company must be able to be traced back to the company by a representation or chain of representations upon which the third party acted and whose authenticity the company is estopped from denying by its representation through words or conduct.[181]

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174 [1964] 2 QB 480 (CA) per Diplock LJ.

175 645B and at 645F. Also see *Hely-Hutchinson v Brayhead Ltd* 1 QB 549 (CA) 593; Birds *et al Boyle & Birds' Company Law* 185.

176 *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 506 per Diplock LJ; Davies and Worthington *Gower and Davies' Company Law* 182; Munday *Agency* at 75; *Zelpy 1780 (Proprietary) Limited v Mudaly* 2015 JDR 0187 (KZP) [42]; *Glofinco v ABSA Bank Ltd t/a United Bank* 2002 6 SA 470 (SCA) [13]; *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) 15H. This has also been confirmed in South African case law. See *Northern Metropolitan Local Council v Company Unique Finance (Pty) Ltd* 2012 5 SA 323 (SCA) [28]; *NBS Bank Ltd v Cape Produce (Pty) Ltd* 2002 1 SA 396 (SCA) [25]; *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [66].

177 Birds *et al Boyle & Birds' Company Law* 186.

178 [1985] BCLC 404 (CA).

179 [1985] BCLC 404 (CA) 414. This was followed by the court in *First Energy (UK) Ltd v Hungarian International Bank Ltd* [1993] BCC 533 (CA).The principles in the *First Energy* case were also applied in *Kelly v Fraser* [2012] UKPC 25.

180 [2006] EWHC 1544 (Comm).

181 *ING Re (UK) Ltd v R&V Versicherung AG* [2006] EWHC 1544 (Comm) [100].

This line of reasoning is to be welcomed. If a company can be held bound by acts of an agent who has ostensible authority to conclude a contract on its behalf, the company should also be capable of being held bound by a representation made by an agent who has ostensible authority to bind the company.

This approach which is more favourable to the third party has, however, according to Munday,[182] still to be fully developed.

2.2.3.3 Reliance on the representation by the third party

Whether this requirement has been satisfied should be determined by looking at the factual circumstances of each case.[183]

The third party can only successfully rely on ostensible authority if he can prove that he relied on the representation whereby he has been moved to conclude the contract.[184] In other words, there must be a causal link between the representation and the acts of the third party.[185] The causal connection is not present where the third party has knowledge of the true state of affairs.[186]

It seems that it would not be very difficult for the contracting third party to prove that he relied on the representation. In this regard the following has been said in *Thanakharn Kasikorn Thai Chamkat (Mahachon) v Akai Holdings Ltd (in liquidation)* by Lord Neuberger of Abbotsbur, NPJ:

> [O]nce a third party has established that the alleged agent had apparent authority, … and that the third party has entered into a contract with the alleged agent on

182 Munday *Agency* 84.

183 Birds *et al Boyle & Birds' Company Law* 184.

184 *Midland Bank v Reckitt* [1933] AC 1 (HL) 17; *Rama Corporation Ltd v Proved Tin & General Investments Ltd* [1952] 1 All ER 554 (KB) 556; *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 506.

185 Munday *Agency* 85.

186 In *Armagas Ltd v Mundogas SA, The Ocean Frost* [1986] 2 All ER 385 (HL) the contracting third party could not prove that the principal represented that the agent had authority to enter into a three-year charter-party. It was known that the agent did not have authority to do so and the third party could only show that it entered into the transaction through misguided reliance on what the agent himself had represented.

> behalf of the principal, then, in the absence of any evidence or indication to the contrary, it would be an unusual case where reliance was not presumed.[187]

Although not applied to the facts of the case, the court held that a third party could rely on the agent's appearance of authority unless its "belief in that connection was dishonest or irrational (which includes turning a blind eye and being reckless)".[188]

2.2.3.4 Knowledge of the constitution

In *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd*[189] the court held that the memorandum and articles of association are always relevant (whether they are in fact known to the third party or not) in determining whether this requirement has been fulfilled.[190] If the common law is applied, a third party may not, due to the doctrine of constructive notice, be able to hold a company bound on grounds of ostensible authority where the agent of the company concluded the transaction in breach of the provisions in the articles which limit his authority.[191] This would be the case even if the contracting third party did not actually have knowledge of the contents of the articles.[192]

2.2.3.5 Alteration of position by third party

An additional requirement laid down in *Rama Corporation Ltd v Proved Tin & General Investments Ltd*[193] is that there has to be an alteration of position on the

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187 [2010] HKCFA 64 at [75].This statement was delivered by the Hong Kong Final Court of Appeal.

188 [2010] HKCFA 64 at [62]. The test in the *Thanakharn* case was adopted in *Newcastle International Airport Ltd v Eversheds LLP* [2012] EWHC 2648 (Ch). In South African law the reliance must be reasonable. This is discussed in Ch 3 para 3.2.3.4.

189 [1964] 2 QB 480 (CA).

190 *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 506.

191 Davies and Worthington *Gower and Davies' Company Law* 185-186.

192 One part of this requirement, *ie* that the memorandum or articles of association of the company should not deprive the company of the capacity to enter into the particular contract, is no longer relevant as the *ultra vires* doctrine has effectively been abolished in its external operation in England by the Companies Act – s 39(1) of the Companies Act of 2006. This, however, falls outside the scope of this dissertation.
The other part of this requirement, *ie* that the delegation of authority by the company may not be restricted by its articles, has been affected by s 40 of the Companies Act of 2006 and is discussed in para 2.3 below. See Ch 3 para 3.2.3.6 below for a discussion of this requirement in South Africa law.

193 [1952] 1 All ER 554 (KB) 556.

part of the third party. Sometimes actual loss is expressly stated as a requirement for ostensible authority.[194]

In most agency cases the courts only require an alteration of position, without evidence of prejudice suffered.[195] The alteration of position need only consist of the third party entering into the contract with the principal.[196]

Munday[197] questions whether an alteration of position actually constitutes a separate requirement at all in light of these court cases. *Bowstead and Reynolds*[198] are also of the opinion that this requirement merges with the requirement that the third party should have relied on the representation.

2.2.3.6 Culpability

Initially the view of the courts was that the representation must have been made intentionally by the company in order to succeed on grounds of ostensible authority (estoppel),[199] or that at least negligence was required.[200] It is now accepted that even non-intentional conduct would be sufficient and that *culpa* on the side of the estoppel-denier is not the decisive factor: it is the effect that the representation has on the person relying on estoppel.[201]

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194 *Whitechurch Ltd v Cavanagh* [1902] AC117 (HL). In this case at 135 the following was stated in this regard:

> My Lords, the case of the respondent is one of estoppel, and it is an essential element in such cases …. that the person to whom the representation was made has suffered loss by acting upon it; or, to put it another way, has altered his position to his detriment by acting on the representation.

195 See Munday *Agency* 89 and Reynolds *Bowstead and Reynolds Agency* 342-343 para 8-026 and the cases cited there.

196 Also see *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) per Diplock LJ at 503:

> The representation, when acted upon by the contractor by entering into a contract with the agent, operates as an estoppel, preventing the principal from asserting that he is not bound by the contract.

197 Munday *Agency* 89.

198 Reynolds *Bowstead and Reynolds Agency* 343 at para 8-026. See Ch 3 para 3.2.3.4 below for a discussion of this requirement in South African law.

199 *Pickard v Sears* (1837) 6 AD & E 469.

200 *Freeman and another v Cooke* [1843-60] All ER Rep 185; Oosthuizen *Turquand-reël* 90.

201 *Freeman and another v Cooke* [1843-60] All ER Rep 185.

According to *Gore-Browne*[202] it might be argued that in the *Freeman* case[203] it was required that the company should subjectively have intended that the third party should act on the representation but the author believes that the test should be objective, in other words, how a reasonable person would view the representation. In this regard, the following passage from *ING Re (UK) Ltd v R&V Versicherung AG* [204] is referred to:

> If, however, the circumstances are such that the person dealing with the supposed agent knew or ought reasonably to have appreciated that the representation relied upon was not intended to be made to him or for his benefit, then there is no good reason in principle why that person should be entitled to rely on the representation to create a contract.[205]

*Bowstead and Reynolds*[206] also regard the statement in the *Freeman* case[207] requiring that the principal should have intended that his representation should be acted upon as too narrow and points out that the wording does not appear elsewhere in the judgment.

## 2.3 Companies Act 2006

English company law underwent a fundamental change with the promulgation of the Companies Act 2006.[208] As will become clear in the discussion below, the Companies Act 2006 and sections 40[209] and 41 in particular, also had an effect on the common-law doctrines regarding the representation of a company.

Griffin[210] suggests a two-step process to be followed in order to ascertain whether the agent of the company had the necessary authority to act on behalf of the company and therefore to bind the company to a contract.

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202 Millett *et al Gore-Browne on Companies* 8-23.
203 *Freeman & Lockyer v Buckhurst Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 503.
204 [2006] EWHC 1544 (Comm).
205 [2006] EWHC 1544 (Comm) [104].
206 Reynolds *Bowstead and Reynolds Agency* 339 para 8-020.
207 *Freeman & Lockyer v Buckhurst Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 503.
208 Benade *et al Entrepreneurial Law* 66.
209 The previous Companies Act 1985 (c 6), hereinafter referred to as the Companies Act 1985 had a similar provision set out in section 35A thereof.
210 Griffin *Company Law* 120.

a) The first step is to determine, by applying the common-law principles relating to agency, whether the board of directors or an agent acting with delegated authority of the board, had the necessary authority.[211]

b) The second step is to ascertain whether there are limitations on the authority of company agents in the company's constitution, resolutions by the company or its shareholders or in shareholders' agreements.

After the first step has been conducted, as suggested by Griffin,[212] the second step should be followed, which entails determining whether there are limitations on the authority of company agents in the company's constitution, resolutions by the company or its shareholders or in shareholders' agreements. The doctrine of constructive notice, the *Turquand* rule and ostensible authority may be relevant in this determination.[213] If the situation can be brought under the provisions of section 40, then section 40 of the Companies Act 2006 shall apply. If section 40 is not applicable, one must revert back to the common law which entails the doctrine of constructive notice, the *Turquand* rule and ostensible authority.[214]

The reason why section 40 is only used as a second step is due to the negative operation of section 40.[215] This means that the limitations in the company's constitutive documents (or resolutions or agreements, as the case may be) placed on the powers of the directors to bind the company, are removed.[216] Section 40 does not make provision for determining whether the directors have the power to

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211 Griffin *Company Law* 120. The situation is the same in South African law where the liability of the company against a third contracting party must also be partly tested against the normal principles of agency: see Naudé 1971 *SALJ* 505 at 507-508; Fourie 1992 *TSAR* 1 at 2.

212 For a discussion on the application of the common-law principles in this first step, see para 2.2.1-2.2.3 above.

213 If a third party, for example, relies on the ostensible authority of the representative and he has proved all the other requirements for ostensible authority, save for the requirement that the delegation of authority by the company should not have been restricted by the company's memorandum or articles, this last requirement can be negated by the provisions of section 40 of the Companies Act of 2006. See para 2.2.3.4 above.

214 If the contracting third party is not able to rely on section 40, the last recourse would be to determine whether the transaction cannot be brought within the ambit of the *Turquand* rule to temper the operation of the doctrine of constructive notice and hold the company bound on those grounds – Davies and Worthington *Gower and Davies' Company Law* 186.

215 Morse *et al Palmer's Company Law* 3045.

216 Morse *et al Palmer's Company Law* 3045.

bind the company or authorise others to bind the company in the instance where there are no limitations in the company's constitution.[217]

In terms of section 40 of the Companies Act 2006 the power of the directors to bind the company, or authorise others to do so,[218] is deemed to be[219] free of any limitation under the company's constitution, in a resolution of the company or of any class of shareholders, or in any agreement between the shareholders or any class of them. This deemed provision is in favour of a person dealing with a company in good faith and does not operate in favour of the company who wants to enforce a contract where the authority of its representative is lacking because a restriction in the articles was exceeded.[220]

The goal of section 40 is to negate the doctrine of constructive notice thereby making it easier for third parties to contract with a company, as section 40 deems the power of directors to bind the company to be free of any limitation under the company's constitution.[221] However, the operation of section 40 is limited by a number of factors as explained below.

### *2.3.1 Documents in which the limitations must be contained*

The power of directors to bind the company is only deemed to be free of any limitation entrenched in the *constitution* of the company. If the limitation on the directors' power is the result of another document or arrangement, then section 40 will not find application.[222]

Although there is no definition of what constitutes a company's constitution, the articles of association of a company will definitely form part of the constitution of

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217 See *Wrexham Association Football Club Ltd (in admin) v Crucialmove Ltd* [2007] BCC 139 at 152.

218 The board of directors or individual directors are not usually involved in the day to day running of the company including the conclusion of day to day contracts, which are left to the officers of the company, especially in larger companies.

219 This deeming provision overrides any wording to the contrary in the constitution – Millett *et al Gore-Browne on Companies* 8-15.

220 Millett *et al Gore-Browne on Companies* 8-15.

221 Davies and Worthington *Gower and Davies' Company Law* 178 to 179.

222 Davies and Worthington *Gower and Davies' Company Law* 179.

the company.[223] The reference to any limitations on the director's powers under the company's constitution include resolutions of the company or of a class of shareholders as well as agreements between members of the company or any class of them.[224]

Examples of areas where limitations can be found that are not in the constitution of the company are the bylaws, authorising resolutions by the board, coupled with restrictions or other internal rules of the board of directors.[225]

### *2.3.2 Types of limitations*

Objects clauses now form part of the articles of a company and may restrict the authority of the directors to act on behalf of the company in the same manner as other clauses in the articles, for example restrictions on borrowing.[226]

The restriction could therefore be a limitation in the objects of a company (in respect of those companies incorporated under older legislation which did not delete their objects clauses or those companies which elected to have objects clauses) or limitations imposed by other provisions of the articles.[227] Limitations further include limitations imposed by a resolution of the company or a meeting of any class of shareholders or from any agreement between the members of the company or any class of shareholders.

This would therefore include a restriction in the articles where the directors have to obtain an ordinary resolution at a general meeting of shareholders before they are

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223 Morse *et al Palmer's Company Law* 3045.

224 Section 40(3); Davies and Worthington *Gower and Davies' Company Law* 176; Morse *et al Palmer's Company Law* 3052; Girvin, Frisby and Hudson *Charlesworth's Company Law* 117.

225 Davies and Worthington *Gower and Davies' Company Law* 179; Morse *et al Palmer's Company Law* 3052.

226 Millett *et al Gore-Browne on Companies* 8-11. In terms of section 28 of the Companies Act 2006 the clauses in the memorandum of a company incorporated before the coming into operation of the Companies Act 2006 should be regarded as provisions of the articles. As the objects clauses previously set out in the memorandum are now found in the articles, these clauses do not have an impact on the capacity of the company anymore, but they still restrict the authority of the directors.

227 Birds *et al Boyle & Birds' Company Law* 167. Also see Davies and Worthington *Gower and Davies' Company Law* at 168; Millett *et al Gore-Browne on Companies* 8-15.

allowed to borrow money on behalf of the company.[228] It would also include *ad hoc* special resolutions or shareholder agreements limiting authority that was otherwise delegated to directors. It will also apply to direct restrictions in the articles placed on, for example, the authority of a managing director as they are indirect limitations on the board to grant a wider authority.[229]

*Gore-Browne*[230] is of the opinion that section 40 would not apply to procedural irregularities such as where a board has not been appointed or where a board is appointed at a meeting where the required quorum was lacking or where improper notice of the meeting was given.[231] The view that section 40 would also cover procedural irregularities is, according to *Gore-Browne*,[232] strained and the *Turquand* rule should rather be used to settle such matters.

Although the third contracting party is not deemed to know of any limitations in the constitution of the company where section 40 applies, he must nevertheless ensure that the person who acts on behalf of the company was authorised by the board as a first step.[233] This is impliedly confirmed by section 40(b)(2)(i) where it is provided that the third party is not bound to enquire *as to any limitation on the powers of the directors to bind the company or authorise others to do so.*[234] When a director therefore enters into a transaction on behalf of the company without any authority from the board of directors, the third party will not be able to rely on the authority of such director.[235]

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228 *Smith v Henniker-Major & Co* [2002] BCC 544 (Ch) 549. These are the facts of *The Royal British Bank v Turquand* (1856) 6 E&B 327 Exch Ch.

229 Millett *et al Gore-Browne on Companies* 8-15.

230 Millett *et al Gore-Browne on Companies* 8-15.

231 His opinion is in line with *Smith v Henniker-Major & Co* [2002] BCC 544 (Ch) 550.

232 Millett *et al Gore-Browne on Companies* 8-15. See, however, *TCB Ltd v Gray* [1986] 1 All ER 587 (Ch) 596; *Smith v Henniker-Major & Co* [2003] Ch 182 (CA) [35]-[41] per Walker LJ (minority decision) and *Ford v Polymer Vision Ltd* [2009] EWHC 945 (Ch) [74] and [78] for the view that procedural irregularities would also be covered by section 40.

233 Griffin *Company Law* 126. Although this was stated in respect of section 35A of the Companies Act 1985 as amended by the Companies Act 1989, the principles still apply in respect of section 40. Also see *Smith v Henniker-Major & Co* [2003] Ch 182 (CA).

234 Griffin *Company Law* 126. Although Griffin still refers to section 35B of the Companies Act 1985, its wording is almost the same as that of section 40(2)(b)(i).

235 *Smith v Henniker-Major & Co* [2002] BCC 544 (Ch) 550 per Rimer J. The appeal against the decision of Rimer J was dismissed. Griffin *Company Law* 126.

The reference to "directors" in section 40, instead of "board of directors" as referred to in Section 35A of the Companies Act 1985,[236] caused new uncertainties in its interpretation.

According to *Palmer's*[237] it is possible to interpret section 40 as not being available in respect of an act by a single director. *Charlesworth's*[238] state that "directors" should be interpreted as the board acting as such. *Boyle & Birds'*[239] are of the opinion that it is possible to interpret "directors" as that each individual director or several directors acting together can bind the company under section 40. There are cases decided under section 40 where the acts of a single director were regarded as being capable of falling under section 40.[240]

It should be noted that only acts by a person who holds the office of a director or a person authorised by a director will fall under the protection of section 40, which would exclude any non-director's act or authorisation.[241]

### *2.3.3 The power of directors to authorise others to bind the company*

It is very rare that the whole board of directors or the whole body of shareholders would act on behalf of the company in transactions concluded by the company.[242] This would be impractical and inconvenient.[243] It is therefore commendable that section 40 not only covers the instance where the "directors" act directly with a contracting third party but also where lesser officers are authorised by the directors to act on behalf of the company.[244] Where a company is represented by a single director, or manager or other person, the question arises as to how section 40 applies to such a situation.

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236 Under the Companies Act 1985 the phrase "board of directors" also caused uncertainties about its interpretation. See Birds *et al Boyle & Birds' Company Law* 167-170; Griffin *Company Law* 128; Morse *et al Palmer's Company Law* 3046.

237 Morse *et al Palmer's Company law* 3046.

238 Girvin, Frisby and Hudson *Charlesworth's Company Law* 117.

239 Birds *et al Boyle & Birds' Company Law* 170.

240 *Ford v Polymer Vision Ltd* [2009] EWHC 945 (Ch) and *Sargespace Ltd v Eustace* [2013] EWHC 2944 (QB).

241 Birds *et al Boyle & Birds' Company Law* 170.

242 Millett *et al Gore-Browne on Companies* 8-19.

243 Davies and Worthington *Gower and Davies' Company Law* 177.

244 Birds *et al Boyle & Birds' Company Law* 168; Millett *et al Gore-Browne on Companies* 8-16.

The powers of the directors to authorise others to act are also deemed to be free of any limitation in the constitution of the company. Where the board (or even a single director) authorises a lesser officer (for example a manager or senior employee) to act on its behalf in contravention of a limitation in the company's constitution to delegate such authority, such lesser officer would not be authorised to act on behalf of the company. In such an instance the third party would not be able to rely on ostensible authority of the lesser officer, as the directors would not have any authority under the constitution of the company to make a representation that such lesser officer does have the necessary authority to act. Section 40 would under these circumstances come to the rescue of the *bona fide* third contracting party as section 40 deems the directors to have that authority.[245]

Section 40 only removes limitations in the articles on the power of directors to authorise others to bind the company. If the board of directors therefore has total power to authorise others to act on behalf of the company and grants authority to an agent to act on behalf of the company, but restricts the power granted to the agent, section 40 does not apply.[246] Such limitation will in the first place not fall under a limitation that would be covered by section 40 and secondly it will also not be a limitation on the board's competence to authorise the agent, but a restriction on the authority of the agent himself. In such an instance, section 40 will not come to the rescue of a *bona fide* third party and the common-law principles of agency law must then be applied.

It should further be noted that section 40 only allows the third party to deem that the directors have the power to delegate authority free from any limitation of such power to delegate as might be contained in the constitution of the company. It does not deem that delegation has in actual fact taken place.[247] Whether delegation has taken place or whether the company may be estopped from denying that the delegation has taken place, should be answered by applying the principles of agency, (actual or implied authority) or should be answered by

245 Birds *et al Boyle & Birds' Company Law* 168.
246 Davies and Worthington *Gower and Davies' Company Law* 180.
247 Griffin *Company Law* 126.

applying the principles of ostensible authority and will be determined by the particular circumstances of each case.[248]

### *2.3.4 Dealing with a company*

A third party can only utilise the protection of section 40 if he *dealt with the company* in good faith. As there was doubt under section 9(1) of the European Communities Act 1972 and later section 35 of the Companies Act 1985 whether a third party that deals with a company would include a third party dealing in respect of a gratuitous transaction with the company,[249] section 40(2)(a) of the Companies Act 2006 specifically provides that a person "deals with" a company if he is a party to any transaction[250] or other act[251] to which the company is a party. The third party would therefore be entitled to the protection of section 40 of the Companies Act 2006, not only where he has concluded an agreement with the company but also in respect of gratuitous acts by the company in his favour for example gifts, the distribution of assets, the grant of a debenture or an option.[252]

### *2.3.5 Good Faith*

Only third parties that acted in good faith may benefit from the protection afforded by section 40. Section 40(2)(b) of the Companies Act 2006 sets out what is meant by good faith and grants wide protection to third contracting parties.

Section 40(2)(b)(i) provides that a person dealing with a company is not bound to enquire about any limitation on the powers of the directors to bind the company or authorise others to do so. This section limits the application of the doctrine of constructive notice. If a contracting third party did not make such inquiries the

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248 Birds *et al Boyle & Birds' Company Law* 168. Also see Morse *et al Palmer's Company Law* 3052 and Griffin *Company Law* 126.

249 *International Sales and Agencies Ltd v Marcus* [1982] 3 All ER 551 at 559-560; Griffin *Company Law* 114; Morse *et al Palmer's Company Law* 3046; Birds *et al Boyle & Birds' Company Law* 170-171; *Re Halt Garage (1964) Ltd* [1982] 3 All ER 1016 (Ch) 1039-1040.

250 For example if the third party is a party to the contract – Davies and Worthington *Gower and Davies' Company Law* 173.

251 For example the payment of money – Davies and Worthington *Gower and Davies' Company Law* 173.

252 Birds *et al Boyle & Birds' Company Law* 170-171; Girvin, Frisby and Hudson *Charlesworth's Company Law* 115; Millett *et al Gore-Browne on Companies* 8-16.

company cannot successfully argue that the third party has not acted in good faith.[253] There is therefore no duty on the contracting third party to enquire as to the restrictions in the articles.[254]

The third contracting party is further presumed to have acted in good faith, unless the contrary in proved.[255] This procedural provision places the burden of proving that the third contracting party did not act in good faith upon the company that wants the protection afforded by section 40 not to apply in favour of the third contracting party.[256]

Section 40(2)(b)(iii) further provides that a person dealing with the company

> is not to be regarded as acting in bad faith by reason only of his knowing that an act is beyond the powers of the directors under the company's constitution.

Although the Act does not stipulate what will constitute bad faith, knowledge alone will not constitute bad faith, but most probably an understanding and/or correct interpretation of the limitation in the constitution of the company by the third party may constitute the required bad faith.[257] According to *Gower* actual knowledge can, however, be a factor when determining bad faith.[258]

If the contracting third party was placed on notice due to suspicious circumstances, it would be difficult, according to *Gore-Browne*, to rely on the fact that the third party had been placed on notice as section 40(2)(b)(iii) states that even actual knowledge of the transgression does not in itself constitute *mala fides*.[259]

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253 Morse *et al Palmer's Company Law* 3047; Birds *et al Boyle & Birds' Company Law* 174.

254 Davies and Worthington *Gower and Davies' Company Law* 172.

255 S 40(2)(b)(ii).

256 Birds *et al Boyle & Birds' Company Law* 173; Davies and Worthington *Gower and Davies' Company Law* 172; Morse *et al Palmer's Company Law* 3047.

257 Morse *et al Palmer's Company Law* 3047; Millett *et al Gore-Browne on Companies* 8-16; Girvin, Frisby and Hudson *Charlesworth's Company Law* 116. According to the latter, it is unclear whether the understanding is to be subjectively or objectively tested. This section would also cover the instance where, although the third contracting party knows of the restriction, he misinterprets it – Millett *et al Gore-Browne on Companies* 8-16.

258 Davies and Worthington *Gower and Davies' Company Law* 172.

259 Millett *et al Gore-Browne on Companies* 8-16.

*Boyle & Birds'*[260] have an opposite view on this point and are of the opinion that the particular circumstances of a transaction placing the contracting third party on inquiry, and the third party makes no such inquiry, would defeat the presumption of good faith.

There is great uncertainty as to what good faith (or bad faith) entails and section 40,[261] instead of clarifying the uncertainty, only added thereto.

### *2.3.6 Exceptions*

In terms of section 40(6) there are two instances where the effect of section 40 is limited. These exceptions are regulated by sections 41 and 42[262] respectively.

Section 41 applies when a director of the company (or a director of the company's holding company or a person connected[263] with any such director) is a party to a transaction with the company where the directors of such company have transgressed any limitation set out in the constitution of the company and the validity of the transaction thus depends upon section 40.[264] In such a case the transaction is voidable at the instance of the company.

The contract will thus be binding unless set aside by the company, without the necessity of having to approach the court.[265] The transaction remains valid until it

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260 Birds *et al Boyle & Birds' Company Law* 174. As support for this view they refer to *Wrexham Association Football Club Ltd (in admin) v Crucialmove Ltd* [2007] BCC 139 [47] where the third contracting party had knowledge of the fact that the directors who acted on behalf of the company had a conflict of interest. Also see Pennington *Pennington's Company Law* 150 (Pennington does, however, hold this view in respect of section 35A of the Companies Act 1985).

261 Birds *et al Boyle & Birds' Company Law* 174; Griffin *Company Law* 125.

262 S 42 relates to companies that are charities and provides that *inter alia* s 40 does not apply to acts of a company that is a charity, subject to certain limitations. This will not be discussed further as it does not form part of the scope of this dissertation.

263 S 41(7) provides that reference to a person connected with a director has the same meaning as set out in s 252.

264 Morse *et al Palmer's Company Law* 3048.

265 Davies and Worthington *Gower and Davies' Company Law* 175. In multi-party transactions, where one of the third parties to the contract also includes a person who is not a director of the company or of its holding company, or a person connected with any such director, the contract remains valid for him and the court may, on the application of the company or any such party, make an order affirming, severing or setting aside the transaction on such terms as appear to the court to be just (s 41(6) of the Companies Act 2006).

is voided by the company (unless it is void for some other reason).[266] If the transaction, however, falls outside section 40 it will be governed by common law and it will not be binding unless it is ratified by the company.[267]

In *Smith v Henniker-Major & Co*[268] the court had to deal with the interaction between the predecessors[269] of sections 40 and 41 of the Companies Act 2006. In terms of the minority judgment[270] the now section 40 can also be used by a third contracting party who is an insider, such as a director, although the validity of the transaction could still be trumped and therefore voided through the now section 41. In other words, the word "person" in section 40 would always include corporate insiders. Where a corporate insider (the same as any other independent person) falls within the ambit of application of section 40, the protection that he obtains is laid down in section 41 with the result that the transaction is voidable as opposed to void.[271]

The majority of the court[272] disagreed with this reasoning and were of the opinion that as the agreement was concluded by an inquorate board meeting, one Smith had no authority to act on behalf of the company. Carnwath LJ was of the opinion that as Smith was not only a director of the company but also its chairman,[273] he was under a duty to ensure that the constitution of the company was properly applied and that he could not rely on now section 40

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266 Girvin, Frisby and Hudson *Charlesworth's Company Law* 118.

267 Davies and Worthington *Gower and Davies' Company Law* 175 and Morse *et al Palmer's Company Law* 3048.

268 [2003] Ch. 182 (CA). This judgment was based on ss 35A and 322A of the Companies Act 1985 (the present ss 40 and 41 of the Companies Act 2006).

269 Ss 35A and 322A of the Companies Act 1985 are substantially the same as ss 40 and 41 of the Companies Act 2006.

270 Per Walker LJ.

271 *Smith v Henniker-Major & Co* [2003] Ch 182, CA [50] per Walker LJ:

> … Section 322A, by contrast, is said to have effect 'notwithstanding' section 35A, so (as it were) allowing section 35A to play its card, but then trumping it to the extent that a director or associate is involved (a three-cornered transaction between a company, a director and an outsider illustrates this).

See also Davies and Worthington *Gower and Davies' Company Law* 175.

272 Carnwarth and Schiemann LJJ.

273 This is a rare recognition of the importance of the chairman of the board. See Davies and Worthington *Gower and Davies' Company Law* 175 and Morse *et al Palmer's Company Law* 3048.

> to turn his own decision, which had no validity of any kind under the company's constitution, into a decision of 'the board'.[274]

The position must then be determined by common law instead of the now section 41 of the Companies Act 2006. Carnwath LJ held that as chairman, the director was responsible for the error in the transaction with him.

Schiemann LJ accepted that technically a director could also fall under a "person" referred to in the now section 40, but in the present case,

> there is no difficultly in excluding from such persons the very directors who overstepped the limitations in the company's constitution. [275]

Commentators are divided in their opinions on the judgment in *Smith v Henniker-Major & Co*.[276] Some[277] summarise the position that has arisen through this judgment as being that directors who deal with a company would be entitled to rely on section 40 except where they have transgressed their authority.[278] They criticise this position as unnecessarily confusing and regrettable that the 2006 Companies Act did not clear up this confusion.[279]

In other words, if a director is the "person" referred to in section 40, the transaction will fall under section 40. As the "person" is a director, section 41 will apply, namely the contract will be voidable at the option of the company. In the instance where the director has overstepped his authority, the transaction will not fall under section 40 and as a result section 41 cannot apply. In such an instance the validity of the transaction will be determined by the application of the common law, unless it is ratified by the company.

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274 [2002] 2 BCLC 655 at [125].

275 [2002] 2 BCLC 655 at [128]. Also see Griffin *Company Law* 128.

276 [2003] Ch. 182 (CA).

277 Birds *et al Boyle & Birds' Company Law* 172. Also see Morse *et al Palmer's Company Law* 3048.

278 In *EIC Services Ltd v Phipps* [2003] EWHC 1507; [2003] 3 All ER 804 Neuberger J held the view in the *Smith v Henniker-Major* case to mean that where the director was responsible for the mistake (whether it was innocent or not) that resulted in the breach of the articles of the company, he could not rely on s 35A (now s 40). If he was not so responsible, s 40 would find application, subject to s 41.

279 Birds *et al Boyle & Birds' Company Law* 173.

Others, however, agree with the reasoning in the minority decision set out above that, due to the fact that the legislature has expressly dealt with corporate insiders in the now section 41 of the Companies Act 2006, the courts do not have to enforce a limitation on the interpretation of "person" in the wording of section 40. According to this view, corporate insiders who deal with the company in good faith should also be entitled to the protection afforded by section 40, subject to the provisions of section 41.[280]

There is also uncertainty regarding the position of a shareholder as a third party. In *EIC Services Ltd v Phipps*[281] the directors of the company allotted bonus shares to shareholders. The constitution of the company required an ordinary resolution of shareholders to be passed for such an act. This resolution was not passed. The Court of Appeal did not regard the issue of bonus shares to the shareholders as dealing by the shareholders with the company.[282] As section 35A of the Companies Act 1985 (the predecessor of section 40 of the Companies Act 2006) was only available to a third party who *dealt*[283] with the company, this meant that the shareholders could not rely on this section to hold the company bound.

Even if the issue of the shares could be seen as a "dealing" by the shareholders with the company, it would appear that the court was still of the opinion that section 35A of the Companies Act 1985 would not apply.[284] The court referred to Art 9(2) of the First Council Directive on Company Law,[285] which was the source for drafting section 35A of the Companies Act 1985 and in which a distinction is made between third parties and members. The court believed that "third party" referred to persons other than the company and its members. As Art 9(2) of the Directive is not available to shareholders (members), the same had to be said of section 35A of the Companies Act 1985.[286]

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280 Davies and Worthington *Gower and Davies' Company Law* 175.
281 [2005] 1 WLR 1377 (CA).
282 [2005] 1 WLR 1377 (CA) 1387.
283 My emphasis.
284 Morse *et al Palmer's Company Law* 3050.
285 68/151/EEC.
286 [2005] 1 WLR 1377 at 1387. Also see Griffin *Company Law* 128.

Section 40 can therefore not be utilised if the third party is a shareholder and the transaction is entered into between the company and the shareholder as shareholder.

According to *Gower*,[287] as the legislature expressly made provision in section 41 for directors, it is unlikely that it would not have dealt with shareholders if it had wished to qualify the protection afforded to shareholders by section 40. The word "person" in section 40 should, therefore not be strictly interpreted to exclude shareholders.

*Boyle & Birds'*[288] make a distinction between the instance where the shareholder transacts with a company in his capacity as a shareholder (which they refer to as "inside" transactions, for example the issue of bonus shares) and where the contracting third party happens to be a shareholder (which they refer to as "outside" transactions). They contend that a shareholder in an outside transaction will be entitled to rely on the provisions of section 40. Where the shareholder, however, transacts with the company in his capacity as shareholder, he would not be able to rely on section 40.[289]

### *2.3.7 Effect of section 40 on the Turquand rule*

The common-law *Turquand* rule has not been repealed by this legislation and operates alongside the statutory protection of section 40.[290] The importance of the *Turquand* rule has, however, decreased due to the protection now afforded by section 40 of the Companies Act 2006.[291] It is possible that section 40 and the *Turquand* rule overlap as in the following example based on the facts in *The Royal British Bank v Turquand*:[292]

> [I]f the articles cap the directors' borrowing power by requiring them to seek the approval of the shareholders in general meeting by ordinary resolution for borrowings over a certain amount, the lender can either assume that the ordinary

287 Davies and Worthington *Gower and Davies' Company Law* 175 at fn 40.
288 Birds *et al Boyle & Birds' Company Law* 172.
289 Birds *et al Boyle & Birds' Company Law* 172.
290 Pennington *Pennington's Company Law* 130.
291 Birds *et al Boyle & Birds' Company Law* 178.
292 *The Royal British Bank v Turquand* (1856) 6 E&B 327 Exch Ch.

> resolution has been obtained, because, under the *Turquand* rule, this matter is a matter of internal management, or can disregard the need for the resolution because this is a limitation on the directors' power which is overridden by s 40.[293]

At common law a third party cannot rely on the *Turquand* rule in cases where he knew that the agent's authority was defective or where he was put on inquiry.[294] The nature of a transaction can even put a third party on inquiry.[295] Where there is an overlap between section 40 and the *Turquand* rule, the contracting third party might benefit more from section 40 because even actual knowledge of the irregularity does not constitute bad faith and such third party would still be able to rely on section 40.[296]

Section 40 only removes restrictions in the constitution of the company on the powers of the directors to bind the company in a transaction with a third party. It does not confer the power on directors to deal with a third party on behalf of the company.[297] To firstly ascertain whether an agent (board of directors or an individual) had the necessary authority to act on behalf of the company, the common-law principles of agency (including ostensible authority) and the *Turquand* rule must be applied. Only if it is ascertained that the agent did have authority, can any limitation in the constitution of the company restricting the power of that agent, be ignored through the operation of section 40. If no authority can be established in the first place, but for a limitation in the constitution of the company, section 40 can never come to the rescue of the third party.

The converse is also true. If section 40 does not apply, the question whether the company will be bound to the contract must be answered by referring to the common-law principles of agency and the *Turquand* rule.[298]

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293 Birds *et al Boyle & Birds' Company Law* 178.

294 *B Liggett (Liverpool) Ltd v Barclays Bank Ltd* [1928] 1 KB 48; *Morris v Kanssen* [1946] 1 All ER 586 (HL); *Rolled Steel Products (Holdings) Ltd v British Steel Corporation* [1986] Ch 246 (CA).

295 *AL Underwood Limited v Bank of Liverpool and Martins* [1924] 1 KB 775; *Northside Developments Pty Ltd v Registrar-General* [1990] HCA 32.

296 Birds *et al Boyle & Birds' Company Law* 178.

297 Morse *et al Palmer's Company Law* 3053.

298 Morse *et al Palmer's Company Law* 3053. In other words, actual and ostensible authority.

As section 40 only applies in the instance where the contracting third party dealt with the board of directors or an agent authorised by the board of directors (in other words the delegation of authority by the board to an agent), it will not find application where the agent was not authorised by the board to act on behalf of the company.[299] In such an instance the common-law principles of the *Turquand* rule or ostensible authority should be applied to determine whether the company may be held bound.

Although the *Turquand* rule was originally developed to mitigate the severe effects of the doctrine of constructive notice, the function of the *Turquand* rule was wider than that alone. It might be that questions regarding compliance with internal management arise even though no requirements were expressly laid down in the constitution of the company. In *Mahony v The East Holyford Mining Co Ltd* [300] the liability of the company did not depend on the bank having knowledge or notice of any particular provision in the constitution of the company. As section 40 only removes limitations in the constitution of the company and in shareholders' resolutions, the *Turquand* rule will therefore still be of assistance where, for example, the board has delegated authority to an individual director but placed certain restrictions on such delegated authority (which restrictions are not contained in the articles of the company or in a shareholders' resolution).

When applying the *Turquand* rule where the third contracting party is a director of the company with which he transacts, the courts have made a distinction between

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299 Pennington *Pennington's Company Law* 148-149.

300 (1874-75) LR 7 (HL) 869. In this case a mining company was founded by Wall and certain of his friends and relatives. The memorandum and articles were registered and subscriptions for shares were obtained from the applicants. These moneys were paid into the bank which had been described in the prospectus as the company's bank. Cheques issued by the company and signed by two of the three named directors, were honoured by the National Bank, Dublin. The bank had done so after it had received a letter signed by a person who described himself as the secretary of the company, enclosing a copy of the resolution by the board of directors of the company in which three directors were named and the bank was instructed to pay cheques that were signed by any two of them and countersigned by the secretary and to which their signatures were appended. When the funds of the company were almost depleted, the company was ordered to be wound up. However, neither a secretary nor any directors were duly appointed by the company, but Wall and his friends and relatives had assumed these roles and had appropriated the subscription moneys. The subscribers of the memorandum were aware of this conduct but did not do anything to stop it. The bank was successful in resisting an action by the liquidator for the repayment of the money. As there was nothing contrary in the articles of the company, the bank was entitled to assume that the directors were properly appointed.

the instance where the director as third party is also the agent who represents the company in the contract concluded with him, on the one hand and instances where another person acts as agent of the company in concluding the contract with the director as third party.[301] In the former case, the director may not rely on the *Turquand* rule, whereas in the latter case he may.

Section 41 of the Companies Act does not make this distinction and treats directors under all circumstances in the same way. Where a contract that a director of a company has concluded with his company transgresses limitations in the articles of the company, such contract is voidable irrespective of the involvement of the director on behalf of the company. A director cannot rely on the *Turquand* rule in respect of a transaction which is voidable in terms of section 41.[302]

## 2.4 Conclusion

England and South Africa have a shared history with regard to the common-law principles of representation in a company law context, as principles of common law in England particular to companies have been taken over by South African courts, such as the doctrine of constructive notice and the *Turquand* rule.[303] With the enactment of statutes by both England and South Africa the paths of these two countries have diverged and each has followed its own direction. This is just as well for South Africa, because the current position in England is anything but satisfactory.

England has made a half-hearted effort to deal with the doctrine of constructive notice. Instead of following through and abolishing this doctrine, it enacted section 40 of the Companies Act 2006. This section provides that the power of directors to bind the company, or authorise others to do so, is deemed to be free of any limitation under the company's constitution, in a resolution of the company or of

301 In this regard, see *Hely Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA).

302 Birds *et al Boyle & Birds' Company Law* 179. He would also not be able to rely on the *Turquand* rule where he has knowledge that a meeting of the board was improperly constituted and unable to act. In this regard, see *Smith v Henniker-Major* [2002] BCC 544 (Ch) and on appeal [2003] Ch 182 (CA).

303 See para 2.2 above.

any class of shareholders, or in any agreement between the shareholders or any class of them. This deemed provision is in favour of a person dealing with a company in good faith.[304] The default position in England remains that the doctrine of constructive notice applies to documents of a company which receives publicity. Section 40 is not at all clear and does not solve the difficulties of representation of a company.

Section 40 does not address the problem where the board or another agent acts on behalf of the company without the necessary authority. Whether a company may be bound to a contract entered into on its behalf should therefore still be determined by first ascertaining whether the board of directors or an agent acting with delegated authority of the board had the necessary authority to enter into the contract on behalf of that company[305] by applying the common-law rules of representation, being actual authority, implied or express, the *Turquand* rule or ostensible authority.

The principal will be bound by the acts of the agent if the agent acted within his actual authority or ostensible authority. The board of directors has express actual authority to exercise those powers of the company as are vested in it by its memorandum and articles.[306] Usually the board would delegate authority to an agent to act on its behalf. The board would only be authorised to delegate authority to such an agent if it has the power to do so under its articles.[307] Such delegation can take place either expressly or impliedly.

If an agent acts without authority or exceeds his authority, the company may still be held bound by a third contracting party on grounds of ostensible authority.[308] A company will be prohibited from denying liability if the third contracting party can prove all the requirements for the successful reliance on ostensible authority. Proving all these requirements is, however, very cumbersome.

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304 See para 2.3 above.
305 Griffin *Company Law* 120.
306 Birds *et al Boyle & Birds' Company Law* 179; Griffin *Company Law* 120.
307 Pennington *Pennington's Company Law* 145.
308 Also known as estoppel by representation.

Unfortunately, the courts have in some instances confused implied authority, which constitutes actual authority, with ostensible authority which does not, and have, for example, reached a conclusion that there is implied authority, terming it as such, even where it is clear that the reasoning of the court is in fact based on ostensible authority.[309]

In the field of representation in company law a further rule was created and developed by the English courts, namely the *Turquand* rule.[310] This rule was created to temper the unfair operation of the doctrine of constructive notice.[311] This rule provides that a third party negotiating with a company in good faith is entitled to assume that the internal management and procedures required by the articles of that company have properly taken place.[312]

In certain instances, both ostensible authority and the *Turquand* rule can be used as grounds for the liability of the company towards a third party.[313] In these circumstances the third party would have a choice between relying on ostensible authority or the *Turquand* rule as basis for holding the company liable. As there are more difficult requirements to prove when relying on ostensible authority, it would be easier for the third party to rely on the *Turquand* rule if the transaction can be brought within its application.[314]

The English courts have, however, in some cases confused ostensible authority and the *Turquand* rule and regarded the *Turquand* rule as only an appearance form of ostensible authority.[315] As a result, the requirements to succeed with ostensible authority have been imported into the application of the *Turquand* rule. This is a very unsatisfactory state of affairs, as the third party is deprived of the benefit of the *Turquand* rule in its pure form, which, as already stated, is easier to comply with.

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309 See para 2.2.1 above.
310 See para 2.2.2 above.
311 Birds *et al Boyle & Birds'Company Law* 178; Oosthuizen 1977 *TSAR* 210 at 210.
312 Oosthuizen 1977 *TSAR* 210 at 210.
313 Du Plessis *Grondslae* 206.
314 Oosthuizen 1979 *TSAR* 1 at 9-10; Du Plessis *Grondslae* 206.
315 *Kreditbank Cassel GMBH v Schenkers Ltd* [1927] 1 KB 826 (CA); *Houghton & Co v Nothard, Lowe & Wills Ltd* [1927] 1 KB 246 (CA).

The position regarding the application of the common-law principles of agency, which remain necessary to determine authority, are therefore mired in uncertainty and not clearly and consistently applied.

Later statutory provisions were enacted that impacted on the doctrine of constructive notice (although not abolishing this doctrine) and the foundation for liability of a company for the unauthorised acts of its agents.[316] As alluded to above this was, however, not a very commendable attempt.

After it has been determined that an agent of the company would have had authority, but for a particular limitation in the constitution of the company, the contracting party can then make use of section 40 of the Companies Act 2006 to hold the company bound to the contract.

Section 40 can also be used by a third contracting party who relies on ostensible authority to negate one of the requirements[317] that he has to prove for successful reliance on ostensible authority, as section 40 allows such third party to hold the company liable irrespective of any restrictions on the agent's authority that might be present in the articles of the company.[318]

The application of section 40 has its own challenges. There exists uncertainty as to the type of limitations which would be covered by this section and how the word "directors" should be interpreted [319] as well as what the requirement of "good faith" entails.[320] The scope of application of section 40 is further limited and might not always come to the rescue of a third contracting party acting in good faith.[321]

316 Ss 35A and 322A of the Companies Act 1985 followed by ss 40 and 41 of the Companies Act 2006.

317 The requirement that the company should not under its memorandum or articles of association have been deprived of the power to delegate authority to enter into a contract of that kind to the agent (s 40).

318 See para 2.3 above.

319 See para 2.3.2 above.

320 See para 2.3.5 above.

321 See para 2.3.1 - 2.3.6.

The exception to section 40, set out in section 41, is capable of different interpretations resulting in different outcomes in a particular set of facts.[322] This creates uncertainty which should have been avoided.

The common-law *Turquand* rule has not been repealed by the Companies Act 2006 and operates alongside the statutory protection of section 40.[323] As an alternative to relying on section 40, the third contracting party can therefore still make use of the common-law *Turquand* rule to bind the company. Under certain circumstances the contracting third party would be successful when relying on section 40, but not when relying on the *Turquand* rule and *vice versa*.[324]

Although the problems experienced by the application of the common-law principles pertaining to company representation have been alleviated by the introduction of section 40 of the Companies Act 2006, the limited operation of sections 40 and 41 and the uncertainties pertaining to its interpretation still leave this area of company law in an unsatisfactory state.

It would have made sense for South Africa to follow England with its statutory enactment, bearing in mind the shared common law of both these countries, but it is clear that the current position in England cannot be supported as a workable solution to company representation. The only thing that South Africa can learn from England is what not to do. However, although South Africa took a totally different direction with the enacting of its Companies Act of 2008, its position also needs serious reconsideration and attention.[325]

322 See para 2.3.6.
323 Pennington *Pennington's Company Law* 130.
324 See para 2.3.7.
325 See Ch 3 para 3.3 below.

# CHAPTER 3 SOUTH AFRICAN LAW

## 3.1 Introduction

When a body or agent acts on behalf of the company such body or person must be properly authorised to act by somebody or something.[326] In terms of section 66(1) of the Companies Act 71 of 2008 (hereafter referred to as the Companies Act of 2008 or the 2008 Act) the business and affairs of the company must be managed by or under the direction of the directors. The board, therefore, has all the powers to act on behalf of the company. Usually the board is only a body that determines the policy and procedures in the company and the day to day management is left to a managing director, other managers, and employees. When a company contracts with third parties it would therefore usually do so through the agency of the managing director, a single director or committee of directors, a manager, employees etcetera.

The normal common-law rules of agency provide the foundation for representation in company law in South Africa.[327] However, the common-law principles of agency could not in all instances provide a satisfactory solution to the problems that arose in the case of companies, due to the fact that the principal (the company) is a juristic person that cannot act on its own.[328] As a result, a specific branch of the law of agency developed that was used in instances where a company was the principal. For example, the doctrine of constructive notice and the *Turquand* rule were developed to cater for specific needs in the area of the law pertaining to the representation of a company.[329] In terms of the South African common law, the authority to represent a company as principal can be based on actual authority, the *Turquand* rule or estoppel. The general principles of common law in respect of agency are still applicable to representatives that act on behalf of

326 Gibson *et al Mercantile Law* 337; Delport 2011 *THRHR* 132 at 133.
327 Cilliers *et al Cilliers and Benade Corporate Law* 179; Benade *Ultra Vires* 137; Naudé 1974 *SALJ* 315 at 316-17; Naudé 1971 *SALJ* 505 at 507-508.
328 Cilliers *et al Cilliers and Benade Corporate Law* 179.
329 Naudé 1971 *SALJ* 505 at 505.

the company. The common-law principles are, however, subject to the provisions of the Companies Act of 2008.[330]

## 3.2 Common law

### *3.2.1 Actual authority*[331]

In order to bind the company, the agent should have actual authority. Actual authority can either be express or implied. The question whether the representative had actual authority to bind the principal (company) is a question of fact.[332] If a third party relies on the actual authority of the representative of the company, he will have to prove such actual authority.[333]

It is not difficult to ascertain whether express authority has been conferred on a particular agent. Express authority can be delegated by means of, for example, the Memorandum of Incorporation or by a resolution of the shareholders or directors or by a person with the authority to delegate such authority.[334]

With implied authority the position is rather more difficult. In *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief*[335] the following description of implied authority is quoted by the court:

> The rule applicable is set out in *The Law of agency in South Africa* by De Villiers and Macintosch, 2nd ed p 56: 'Where an agent is employed to act in the course of his trade, business or profession as agent, he has implied authority to bind his principal in regard to matters which are necessary to enable him to perform the

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330 Delport *Nuwe Ondernemingsreg* 101. One of the common-law principles pertaining to companies that have been amended by the 2008 Act is the application of the doctrine of constructive notice. This doctrine has to a large extent been abolished by the Act in s 19(4). See para 3.3.2 below.

331 See the discussion of "actual authority" in Ch 2 para 2.2.1 above, which is also the position under South African law.

332 Benade *et al Entrepreneurial Law* at 146.

333 *South African Broadcasting Corporation v Coop* 2006 2 SA 217 (SCA) 233; *Zelpy 1780 (Proprietary) Limited v Mudaly* 2015 JDR 0187 (KZP) [37].

334 *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) at 14.

335 1978 2 SA 11 (T) at 14.

> ordinary duties incidental to his position as agent, or which form part of the ordinary course of business transacted by that agent.

Implied authority may also be

> … inferred from the acquiescence of the directors in a course of dealing inside the company itself.[336]

It should be noted that implied authority constitutes actual authority and it is not estoppel (or ostensible authority as more commonly termed by the English courts).[337] In *Insurance Trust and Investments (Pty) Ltd v Mudaliar*[338] the court stressed the importance of clearly distinguishing between implied authority and estoppel as it considered the law in England at that time to be in a state of confusion, especially as applied to companies.[339] The court further stated that part of the confusion was seated in the fact that judges (in England) tended to use the same facts to conclude that there was implied authority as to conclude an estoppel.[340] Unfortunately this confusion also appears in the judgments of South African courts.[341]

I agree with Blackman *et al*[342] and Oosthuizen[343] that the view that implied authority may exist even where the agent exceeds his actual authority cannot, with respect, be correct, as implied authority is actual authority and where an official therefore exceeds his actual authority, he cannot have actual authority and

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336 *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) at 14-15. Also see *Rosebank Television & Appliance Co (Pty) Ltd v Orbit Sales Corporation (Pty) Ltd* 1969 1 SA 300 (T) at 303.

337 *Coetzer v Mosenthals Ltd* [1963] 3 All SA 484 (A) at 486-487; Kerr *Agency* 67.

338 1943 NPD 45 at 54 and 63 respectively.

339 Also see Montrose 1934 *LQR* 224 at 226:

> The term 'apparent authority' (or its synonym 'ostensible authority') has been used in what may be called an objective sense. This is due, perhaps to its confusion with 'implied authority,' or to the convenience of a distinction between 'apparent' and 'actual' authority applicable generally and not in a specific instance.

340 *Insurance Trust and Investments (Pty) Ltd v Mudaliar* 1943 NPD 45 at 62.

341 See for example *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 266E:

> [I]mplied authority can be inferred, when the official acting on behalf of the company purports to exercise an authority which that type of official usually has even though the official is exceeding his actual authority ... .

Unfortunately this view has been quoted with approval in *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) 14. It has also been followed in *Zelpy 1780 (Proprietary) Limited v Mudaly* 2015 JDR 0187 (KZP) [47].

342 Blackman *et al Commentary* ch 4 fn 197.

343 Oosthuizen 1978 *TSAR* 172 at 173.

therefore also not implied authority.[344] The third party may, however, be successful in relying on estoppel, provided that he is able to prove all its elements. The usual authority of an agent or representative can be described as the authority to execute those legal acts that are normally attributable to the position of representatives or officers of that class.[345]

Kerr[346] warns that, since the content of usual authority is determined by custom and usages of trade, it is not a stagnant concept and what the courts considered as being usual in the past might not be usual in present circumstances.

As is the case in England, usual authority cannot be regarded as an independent type of authority in the law of agency in South Africa. Usual authority only serves to ascertain whether actual or ostensible authority was present.[347] It also assists in determining whether the *Turquand* rule finds application.[348]

If the representative does not have the necessary authority or if he exceeds his authority, the principal (company) will usually not be bound. In such an instance the principal will only be liable at common law in one of the following three instances:[349]

a) If, after the conclusion of the contract, the principal supplements the lack of authority by ratifying or confirming it. The agent is thereby *ex post facto* clothed with the necessary authority and the position is as if he initially had the necessary authority; or
b) Through the operation of the *Turquand* Rule; or
c) If the principal has represented that the representative has the necessary authority and that the extent thereof is wider than what it really was. In this instance the principal's liability is founded on estoppel;[350]

344 Blackman *et al Commentary* ch 4 fn 197; Oosthuizen 1978 *TSAR* 172 at 173.
345 Oosthuizen *Turquand-reël* 45.
346 Kerr *Agency* 71.
347 Rabie *Verteenwoordiging* 16. For a discussion of usual authority, see Ch 2 para 2.2.1 above.
348 See para 3.2.2 below.
349 Rabie *Verteenwoordiging* 13.
350 Oosthuizen 1979 *TSAR* 1 at 6.

### *3.2.2 Doctrine of constructive notice and the Turquand rule*

The doctrine of constructive notice, as developed by the English courts, was taken over by South African law.[351] Historically the *Turquand* rule was introduced and developed by the English courts due to the operation of the doctrine of constructive notice applicable to companies.[352] The *Turquand* rule has also been taken over from England by South African law.[353]

The *Turquand* rule provides that a third party (outsider) negotiating with a company in good faith is entitled to assume that the internal management[354] and procedures required by the articles of that company have properly taken place.[355]

The *Turquand* rule amends the normal principles of agency.[356] This rule operates in favour of the contracting third party (outsider) against the company. The courts have applied this rule within certain boundaries, although the application of these boundaries is still uncertain.[357] The circumstances where the *Turquand* rule does not find application, listed in *Wolpert v Uitzigt Properties (Pty) Ltd*,[358] were later confirmed as still reflecting the current legal position.[359] Some of the aspects of the application of the *Turquand* rule are discussed below.

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351 *The Mine Workers' Union v Prinsloo* 1948 3 SA 831 (A) 845; *Potchefstroom se Stadsraad v Kotze* [1960] 3 All SA 402 (A); *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W). The doctrine of constructive notice has, however, effectively been abolished under South African law, save for, *inter alia*, so-called "ring-fenced" companies. See para 3.3.2 below. See paras 2.2.2 and 2.3 of Ch 2 above for the position regarding this doctrine in English law.

352 See para 2.2.2 in Ch 2 above for a discussion on the origin and content of the rule.

353 *Paddon and Brock Ltd v Nathan* 1906 TS 158; *Legg & Co v Premier Tobacco Co* 1926 AD 132; *The Mine Workers' Union v Prinsloo* 1948 3 SA 831 (A); *Farren v Sun Service SA Photo Trip Management (Pty) Ltd* 2004 2 SA 146 (C) to name but a few. In *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 261 the *Turquand* rule was also accepted as follows:

> South African law has adopted the 'rule in *Royal British Bank v Turquand,*' viz. that a person dealing with a corporation is bound by the terms of the statutes or constitution governing its contractual power, but that the necessary acts of internal management of the corporation are presumed to have been performed.

354 Also known as the indoor management.

355 Sealy and Worthington *Sealy's Cases and Materials* 117; Oosthuizen 1977 *TSAR* 210 at 210.

356 Oosthuizen *Turquand-reël* 124.

357 Oosthuizen 1979 *TSAR* 1 at 10. See Ch 2 para 2.2.2 above for the boundaries within which the South African courts have also applied the *Turquand* rule.

358 1961 2 SA 257 (W) 266.

359 *Quintessence Opportunities Ltd v BLRT Investments Ltd; BLRT Investments Ltd v Grand Parade Investments Ltd* [2008] 1 All SA 67 (C) 74.

3.2.2.1 Persons (bodies) representing the company[360]

The board is the organ of the company which is normally vested with full authority on matters that fall within the powers of the company.[361] It is usual that the board possesses these powers and insofar as the application of the *Turquand* rule is concerned, no further investigation is undertaken into the *bona fides* of the third party if he contracts with the board.[362] Usually these cases do not present any problems and the *Turquand* rule will find application.[363] In larger companies, however, a third party would usually not deal with the board but with one of its delegates and it is here where most of the problems occur.

Usually the board of directors delegates wide authority and powers to the managing director. It has become usual that a third party contracting with the company in good faith may assume that the managing director possesses all of the authority which, in terms of the articles, may be delegated to him[364] and which is not of such an extraordinary nature so as to put the third party on inquiry.[365]

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360 See Ch 2 para 2.2.2 bounday (iv).

361 Van Dorsten *Company Directors* at 153. The third party could therefore under the 1973 Companies Act assume that the board could exercise all powers which could be delegated to it in terms of the articles – Cilliers *et al Company Law* at 124; Oosthuizen 1978 *TSAR* 172 at 173-174. For the position of the board under the Companies Act of 2008, see para 3.3.1 below.

362 In *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 265 it is stated:

> The board is ordinarily the organ of a company vested with plenary authority on matters *intra vires* the company. There is therefore no difficulty in applying the *Turquand* rule in cases where the board has contracted.

This judgment was delivered in terms of the 1973 Companies Act. Section 34 of the 1973 Companies Act provided that a company shall have plenary powers, including the common-law powers as stipulated in Schedule 2 to the Act, to enable it to achieve its main and ancillary objects. Usually the articles of a company provided that the directors may exercise all the powers of the company which are not restricted to the company in general meeting.

363 *The Royal British Bank v Turquand* (1856) 6 E & B 327; 119 ER 886; *The Mineworkers' Union v Prinsloo* 1948 3 SA 831 (A) (where it was not the board that acted but an institution within a union akin to a board of directors); *Mahony v East Holyford Mining Co Ltd* (1874-75) LR 7 (HL) 869.

364 *Acutt v Seta Prospecting & Development Co Ltd* 1907 TS 799 at 816; *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) at 14-15; Van Dorsten *Company Directors* 154; Blackman *et al Commentary* ch 4 38; Oosthuizen 1978 *TSAR* 172 at 174. This was the case under the Companies Act of 1973, where the board could only delegate authority if authorised thereto in the company's articles. As the authority of the board under the Companies Act of 2008 is original, the board does not need to be authorised by the articles in order to delegate its authority. See para 3.3.1.2 below in this regard.

365 In terms of, for example, *Paddon and Brock Ltd. v Nathan* 1906 TS 158.

The courts have, however, held that the *Turquand* rule would not find application where an ordinary director acts on behalf of a company. An ordinary director does not have the authority, solely on the basis of his directorship, to bind the company as a director,[366] as he is not, in that capacity, an agent of the company.[367] Here the importance of distinguishing between the powers contained in the articles and the means used to exercise these powers become more obvious. In terms of the doctrine of constructive notice a third party would be presumed to know that, for example, any one of the directors may be authorised to act in a particular transaction by means of a resolution of the board. The third party would, however, not know whether the authority has indeed been granted by the board to the particular director that he is dealing with, in other words, whether the particular director has been selected as the means through which the company exercises the power. The outsider will therefore have to prove that the ordinary director had either actual authority, or that an appearance of authority has been created by the company whereby the company can be estopped from denying authority.[368]

It is possible that in a small private company one of the only two directors has usual authority to manage the company.[369] In big companies it may even be a risk to assume that individual directors may perform administrative acts. In this regard Claassen J in *Wolpert v Uitzigt Properties (Pty) Ltd* declared:

> … the position of an ordinary director may vary from company to company. In some companies, particularly in large public companies, he usually only attends board meetings, and only takes part in the decisions of the board, but he takes no part in the internal running of the affairs of the company. In other companies again, and that is often true of private companies, the ordinary director besides attending board meetings, also takes an active part in the day to day running of the affairs of the company. If that is the case, he may also have some managerial functions …[370]

It would therefore be wise for a third party to not rely on any usual authority of an individual director, but to ascertain whether such director has actual authority to

366 *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 266-267; *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168 at 216-217; *Rosebank Television & Appliance Co (Pty) Ltd v Orbit Sales Corporation (Pty) Ltd* 1969 1 SA 300 (T).

367 *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168 at 216.

368 Leveson *Company Directors* 99.

369 *Rosebank Television & Appliance Co (Pty) Ltd v Orbit Sales Corporation (Pty) Ltd* 1969 1 SA 300 (T). If there is only one director he would of course have authority to contract on behalf of the company – *Milne v Fabric House (Pty) Ltd* 1957 3 SA 63 (W).

370 1961 2 SA 257 (W) at 267.

enter into the contract on behalf of the company.[371] As the usual authority of a director is limited in extent and has an uncertain content, a third party would only be entitled to rely on the *Turquand* rule in highly exceptional instances.[372]

It could be that the required authority was delegated to the director, but that the actual exercise of that authority has been made subject to compliance with some or other internal formalities. In such an instance, the *Turquand* rule may be relied on.[373]

In respect of company secretaries, it would seem that their position in the company has changed and the English courts have also supported the view that a company secretary would be authorised to conclude contracts that relate to administrative issues on behalf of the company.[374] The question whether our courts would follow the English courts was, however, left open in *Tucker's Land and Development Corporation (Pty) Ltd v Perpellief*.[375]

*Henochsberg*[376] states that the mere fact that a person holds the office of a secretary can never imply that the board of directors delegated some of their powers to such secretary for any purpose and that such secretary has been

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371 See ch 2 para 2.2.2 above where one of the boundaries within which the *Turquand* rule finds application is that the representative had to act within his usual authority.

372 *Welgedacht Exploration Co Ltd v Transvaal and Delagoa Bay Investment Co Ltd* 1909 TH 90; *Strathsomars Estate Co Ltd v Nel* 1953 2 SA 254 (E); *Marshall Industrials Ltd v Khan* 1959 4 SA 684 (N).

373 *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) at 14-15; *Hosken Employee Benefits (Pty) Ltd v Slabe* 1992 4 SA 183 (W) at 190; Blackman *et al Commentary* ch 4 38.

374 *Panorama Developments (Guildford) Ltd v Fidelis Furnishing Fabrics Ltd* [1971] 3 All ER 16 (CA). In this case, at Denning MR stated at 19:

> He is an officer of the company with extensive duties and responsibilities. This appears not only in the modern Companies Acts, but also by the role which he plays in the day-to-day business of companies. He is no longer a mere clerk. He regularly makes representations on behalf of the company and enters into contracts on its behalf which come within the day-to-day running of the company's business. So much so that he may be regarded as held out as having authority to do such things on behalf of the company. He is certainly entitled to sign contracts connected with the administrative side of the company's affairs, such as employing staff, and ordering cars, and so forth. All such matters now come within the ostensible authority of a company's secretary.

Also see Pennington *Pennington's Company Law* 146-147.

375 1978 2 SA 11 (T) at 17. In *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) at 17 reference is made to *Strathsomars Estate Co Ltd v Nel* 1953 2 SA 254 (E) wherein Reynolds J applied the *dictum* of Bowen LJ in *Newlands v National Employers Accident Association Ltd* 53 LT 224 where the authority of a secretary of a company was considered and where the duties were said to be "clerical and ministerial and beyond that it is a question of fact in each case what his duties are."

376 Delport and Vorster *Henochsberg 2008* 99.

authorised to act in any type of contract merely because he is the secretary. According to *Henochsberg* a secretary is merely an employee of the company and the circumstances of each case will dictate whether such secretary had authority (either express or implied actual authority or ostensible authority). Although stated in respect of actual or ostensible authority, this principle can also be used to ascertain what the usual authority of the secretary is in the application of the *Turquand* rule.

If rules are laid down as to whether the *Turquand* rule may find application in every situation by looking at the type of person who represented the company, the law will be developed in a casuistic manner. It would be better to apply the boundaries referred to above to determine whether the third party would be able to hold the company bound to the contract. To exclude the application of the *Turquand* rule where ordinary directors or persons of lower rank have represented the company, relates directly to the fact that only *bona fide* third parties are entitled to the protection of the *Turquand* rule and that the rule does not find application where the third party has been placed on inquiry. Individual directors and persons with lower rank usually do not have the authority to contract on behalf of the company.[377]

3.2.2.2 Persons entitled to rely on the *Turquand* rule

As regards the person who may rely on the *Turquand* rule, the general view is that only outsiders will be entitled to use the common-law *Turquand* rule and that persons connected to the company (insiders) are not protected by this rule.[378]

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377 This falls under the boundary that the representative had to act within his usual authority. See Ch 2, para 2.2.2 above. The courts, for example regard a chairman as in the same position as an ordinary director and a third party dealing with such a director without actual authority from the board or the managing director, does so at his own peril – *Wolpert v Uitzigt Properties (Pty) Ltd and others* 1961 2 SA 257 (W) 266. The chairman of the board of directors is however one of the most important sources of legally binding decisions taken at board meetings. If he therefore presents a resolution from the minute book of a meeting of directors to a third party in terms of which he is authorised to contract on behalf of the company, the third party may rely on such resolution and can hold the company bound to the contract – *Goode, Durrant and Murray Ltd v Hewitt and Cornell* 1961 4 SA 286 (N) 289.

378 In *Mahony v The East Holyford Mining Company* (1874-75) LR 7 (HL) 869 at 894 the *Turquand* rule was intentionally connected with dealings with a company and "persons external to the company". In *County of Gloucester Bank v Rudry Merthyr Steam & House Coal Colliery Co* [1895] 1 Ch 629 (CA) 633 reference is made to the "outside person" who

Since the English decisions in *Howard v Patent Ivory Manufaturing Co*[379] and *Morris v Kanssen*[380] the common-law position in respect of the *Turquand* rule was generally accepted as not being available to directors as they have a duty to ensure that the management of the company takes place in the prescribed manner.

This position was changed by the judgment in *Hely-Hutchinson v Brayhead Ltd*[381] which distinguished the *Howard* and *Kanssen* cases from the case at hand by indicating that in the former two cases the director was not only the contracting third party but also the director of the company representing the company and was therefore considered to be an insider. In the *Hely-Hutchinson* case the court was of the opinion that where a director only acted in his capacity as a contracting third party and the company was represented by somebody else, he should not be regarded as an insider and should still be entitled to benefit from the *Turquand* rule.[382]

The approach in *Hely-Hutchinson v Brayhead Ltd*[383] is, however, criticised by several writers.[384] Other writers,[385] however, accept the exposition of the court as

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may rely on the *Turquand* rule; *Morris v Kanssen* [1946] 1 All ER 586 (HL) 592. Also see Blackman *et al Commentary* ch 4 40; McLennan 1979 *SALJ* 329 at 352.

379 (1888) LR 38 Ch D 156.

380 [1946] 1 All ER 586 (HL).

381 [1968] 1 QB 549 (CA) per Roskill J.

382 At 567. It should be noted that in this case, following *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [964] 2 QB 480 (CA), the *Turquand* rule was confused with estoppel and the two doctrines were intermingled.

383 [1968] 1 QB 549 (CA).

384 According to Oosthuizen *Turquand-reël* 176, such a view would be in conflict with the *Turquand* rule, because if the director knew from his position as director that there were internal irregularities he would not be *bona fide* anymore. The *Turquand* rule should not operate in favour of persons who form part of the management body of the company as these persons have access to the internal management of the company. Such a person has the means to ascertain the position regarding the internal management irrespective in which capacity he is acting (as director or as third contracting party). The view of Oosthuizen is supported by McLennan, with qualification, however. McLennan 1979 *SALJ* 329 at 354 states that:

> Whilst I would agree that this [the approach of Oosthuizen] is the better approach, one should not lose sight of the fact that some irregularities may be so well hidden that they would be extremely difficult to uncover. For instance, the authority to enter into a particular transaction may have been conferred by a resolution passed many years ago; it may be difficult, if not actually impossible, for a recently appointed director to discover, for example, that the notice convening the meeting had been defective or that a proper quorum had not been present. Such difficulties would be aggravated where minutes and other documents had been falsified by a previous management. In such circumstances a director ought not to be prejudiced: it is submitted, therefore, that the rule ought to be that a director is obligated to take all reasonable steps to ensure that internal regulations have been complied with; should he take such steps

the correct position. According to Du Plessis,[386] being an insider should not be made one of the exceptions to the *Turquand* rule when its application is excluded. The question whether the *Turquand* rule may be applied in such an instance should be whether there existed circumstances whereunder it could have been expected from the third party to investigate further whether the internal requirement has been complied with and whether he did indeed investigate further or not. In other words, the usual exception to the *Turquand* rule, being placed on inquiry due to suspicious circumstances, should be applied. I endorse this approach by Du Plessis. If the third contracting party is a director then that will form part of the circumstances in determining whether he has been put on inquiry. It can therefore be agreed with *Henochsberg*[387] that in principle a director would also be able to rely on the *Turquand* rule, but that it would be very difficult for such director not to be regarded as having been put on inquiry as a consequence of which the rule would not be available to him anymore.

3.2.2.3 Exercising powers for an improper purpose

In *Rolled Steel Products (Holdings) Ltd v British Steel Corporation*[388] the court held[389] that it is implied in a company's Memorandum of Incorporation that the

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and still fail to find the irregularity or if, in any event, he would not reasonably have suspected the existence of the irregularity, he should not be liable for the consequences.

385 Millett *et al Gore-Browne on Companies* 8-14; Baiketlile *Corporate Capacity* 16 fn 50; Girvin, Frisby and Hudson *Charlesworths' Company Law* 124. Compare, however, Griffin *Company Law* 123; Morse *et al Palmer's Company Law* 3058; Pennington *Pennington's Company Law* 144. Birds *et al Boyle & Birds' Company Law* 178 adds that if it is the duty of the director to have knowledge of the real position, he would not be entitled to rely on the *Turquand* rule.

386 Du Plessis *Grondslae* 70.

387 Delport and Vorster *Henochsberg 2008* 106(3). See para 3.3.4.1 below for the position of insiders and outsiders in the application of section 20(7) of the Companies Act 2008.

388 [1986] Ch 246 CA 292 to 293.

389 Slade LJ followed *In Re David Payne & Co Ltd* [1904] 2 Ch 608 (CA). In the *David Payne* case the court held that the loan by the company (which was represented by a director) was not invalid due to the fact that the director intended to use the money for a purpose not authoritsed by the constitution of the company, as the third party did not have any knowledge of such intention of the director. The court held (at 613, per Buckley J and at 617 per Romer LJ) that a person who lends money to a company, where the constitution provides for a general power to borrow, limited only that it should be done for the purposes of the company's business, is not bound to inquire to what purpose the borrowing company is about to apply the borrowed money. In *In re Jon Beauforte (London) Ltd* [1953] Ch 131 the court held that a transaction where coke (fuel) was purchased by the company was void as the coke was purchased for a purpose other than for the business of the company and the contracting third party knew this. In *In Re Introductions Ltd, Introductions Ltd v National Provincial Bank Ltd* [1970] Ch 199 the court held that where money borrowed by

directors can only exercise their powers on behalf of the company if it is for purposes of the company's business.[390] If the third contracting party therefore knew that the board exceeded the authority conferred on them by the company by entering into a transaction for purposes other than the company's corporate purpose (in other words for an improper purpose) he or she cannot rely on the *Turquand* rule and hold the company liable. On the other hand, if the third party did not have any knowledge that the directors exercised their authority for an improper purpose, they would be able to rely on the *Turquand* rule and assume that the directors were acting properly and regularly in the internal management of its affairs by exercising their powers for the purpose of the company's business.[391] The court further stated that if the third party is able to prove all the elements of estoppel, he can also hold the company liable on estoppel under these circumstances.[392]

Blackman[393] does not agree with the reasoning of the court in the *Rolled Steel Product*s case.[394] Although he agrees that the company should be held bound, he

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the company are to be used for a purpose not authorised by the objects of the company, the company would be bound to the contract. In this case the bank did not have knowledge of the unauthorised purposes for which the monies were to be used and the contract was therefore held to be valid and binding.

From the above cases the following rule transpired, namely that the knowledge of the contracting third party of the purpose for which the director enters into the transaction determines whether a transaction is *ultra vires* or not. I agree with Blackman 1990 *SA Merc LJ* 1 at 2 that such a rule causes confusion and is uncertain. It seems as though an *ultra vires* act (beyond the capacity of the company) is confused with the authority of the directors to act.

390 The court held that a transaction is not *ultra vires* the company just because the directors were acting for a purpose not authorised by the objects clause of the company. To ascertain whether a transaction is *ultra vires*, an objective test is used, in other words it should be determined whether the transaction is capable of being performed as

> reasonably incidental to the attainment or pursuit of any of its express objects, unless such act is expressly prohibited by the memorandum (at 287).

It would be a matter of interpretation to ascertain whether a particular act falls within the capacity of the company or not. It might, however, happen that, although the transaction is *intra vires* the company, the directors acted for an improper purpose in other words not for the purpose of the business of the company. Although the directors in such an instance are in breach of their fiduciary duty towards the company, they also act beyond their authority. As a part of internal management, a contracting third party can therefore assume that the directors of the (for example, borrowing) company were acting properly and regularly in the internal management of its affairs and were acting (for example, borrowing) for purposes of the company's business.

391 Even if there is an express requirement in the constitution of the company that the power is only exercisable for purposes of the company's business, the third party is not put on inquiry – per Browne-Wilkinson LJ at 306.

392 At 292.

393 Blackman 1990 SA Merc LJ 1 at 12

is of the view that the basis for liability can be neither estoppel[395] nor the *Turquand* rule.[396] If the directors exercise their powers for an unauthorised purpose, so he reasons, they are in breach of their fiduciary duty but they do not act beyond their powers: they just abuse their powers.[397] According to him, such a transaction would be binding on the company, except if the third party knew of the fact that the directors acted for an improper purpose, in which event the transaction would be voidable at the option of the company.[398]

Blackman[399] explores the basis of the generally accepted principle in agency law that the liability of a principal (including a company) is not affected by the unknown motives of his agent (including directors of a company). He refers to two theories in this regard:

The first theory is that where an agent (director) acts for an improper purpose (in other words not for the purposes of the business of his or her principal or for his or her own personal interest), the transaction concluded by the agent would be beyond the authority of such agent (or director) and would therefore be void. The third party may under these circumstances rely on estoppel or the *Turquand* rule to hold the principal (company) bound to the transaction.

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394 [1986] Ch 246 CA at 292-293.

395 Blackman 1990 *SA Merc LJ* 1 at 12-13:

> If the third party is to rely on ostensible authority in this situation, he will have to establish not that the company represented that its directors had authority to do 'anything which its memorandum of assocation expressly or impliedly empowered the company to do', but that it represented that its directors had authority to act for purposes not authorised by its memorandum.

396 Blackman 1990 SA Merc LJ 1 at 14:

> In *Contemporary Refrigeration (Pty) Ltd* Miller J said, correctly, that 'the rule in *Turquand's* case may not strictly be applicable'. In truth, it is not applicable at all. The rule in *Turquand's* case merely provides that a person dealing with a company may assume that the internal formalities of the company's constitution have been complied with. To state the obvious, failure on the part of directors to act for the purposes authorised by their company's memorandum is not a failure on the company's part to comply with the internal formalities prescribed by its constitution.

Also see Blackman *et al Commentary* ch 4 51.

397 Blackman 1990 *SA Merc LJ* 1 at 10. Blackman distinguishes the situation where the directors do not act with authority, which would mean that the directors act in excess of their authority as opposed to the situation where the directors abuse their powers in which event they do not act in excess of their authority.

398 See Blackman 1990 *SA Merc LJ* 1 at 15 and the cases cited there. Also see Blackman *et al Commentary* ch 4 51.

399 Blackman 1990 *SA Merc LJ* 1 at 11.

The second theory, which Blackman supports, entails that although a transaction entered into for an improper purpose is in excess of the authority of the agent (director of a company), it is not beyond the powers of such agent (director). The transaction would therefore be binding on the principal (company). Where the contracting third party has, however, notice of the fact that the transaction was concluded for an improper purpose, such contract would be voidable at the instance of the principal (company).[400]

Support for the first theory can be found in court cases[401] like *Paddon and Brock Ltd v Nathan*,[402] *Harcourt v Eastman,*[403] *Contemporary Refrigeration (Pty) Ltd (In Liquidation) v Leites and Sonpoll Investments (Pty) Ltd,*[404] *Jones v John Barr & Co (Pty) Ltd*[405] and *AL Underwood Limited v Bank of Liverpool and Martins.*[406]

The reasons why Blackman[407] supports the second theory, save for the fact that the great weigth of authority supports it,[408] are that it provides an acceptable justification for *bona fide* third parties to be unaffected by improper purposes of directors, that it leads to a more fair result to the effect that *male fide* third parties cannot rely on invalidity of transactions unless avoided by the company and that it places the duty of directors to act for the purpose of the company's business within the fiduciary duties of directors. Blackman *et al*[409] are of the opinion that an objective test should be used to determine whether the directors acted within the scope of their authority. The subjective motive of the directors (for example the purposes for which they intend to use the money that they are borrowing on behalf of the company) does not detract from the fact that it is within their powers to borrow money on behalf of the company.

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400 Blackman 1990 *SA Merc LJ* 1 at 11.

401 In the majority of these cases the courts were of the view that the basis upon which the company could be bound under these circumstances would be on estoppel. One or two of the cases also referred to the *Turquand* rule.

402 1906 TS 158 at 164.

403 1953 2 SA 424 (N) at 429.

404 1967 2 SA 388 (D) at 391-393.

405 1967 3 SA 292 (W) at 302-303.

406 [1924] 1 KB 775 at 785-787 per Bankes LJ, at 791-792 per Scrutton LJ, and at 796 per Atkin LJ.

407 Blackman 1990 *SA Merc LJ* 1 at 16.

408 For a list of cases that supports this view, see Blackman 1990 *SA Merc LJ* 1 at 15 fn 80.

409 Blackman *et al Commentary* ch 4 51.

3.2.2.4 Forgeries[410]

Since the judgment of the Court of Appeal in 1906 in *Ruben v Great Fingall Consolidated*[411] it is accepted that the *Turquand* rule does not find application in cases of forgery.[412] If someone therefore forged the signature of the director or secretary on company documents, the company cannot be held bound by a third party relying on the *Turquand rule*.[413]

No definition has been given for "forgery". The circumstances of the case where Lord Loreburn stated that the *Turquand* rule could not be applied were where the signatures of the directors were counterfeited by the secretary. The English courts have, however, extended the application of the term "forgery" to more than just where a person would be guilty of the crime forgery, and used it in a wider sense than just the forgery of another person's signature by accepting the instance where the signature of the representative is authentic (genuine) but was affixed without authority and for a fraudulent purpose (genuine but fraudulent cases) as well as where the signature of the representative is genuine and innocently affixed but without actual authority (genuine and innocent cases).[414]

I question whether forgery can be so widely interpreted. It would mean that most unauthorised acts where documents are involved, would amount to a forgery and take away the protection of the third party. Some English writers are of the view that it would be a misuse of the word "forgery" to regard it as a forgery where the representative attached his own signature to a document although he did not have

410 See Ch 2 para 2.2.2, boundary (v) above.

411 [1906] AC 439 (HL).

412 Accepted with approval in *Kreditbank Cassel GMBH v Schenkers Ltd* [1927] 1 KB 826 (CA) 831 and confirmed in *Uxbridge Permanent Benefit Building Society v Pickard* [1939] 2 All ER 344 at 350. Also see Blackman *et al Commentary* ch 4 41; Rabie *Verteenwoordiging* 173; Thompson (1959) *UTLJ* 248 at 274.

413 It is possible that the company may be bound on grounds of estoppel. In the present case, however, the company did not hold out the secretary as having authority to do anything more than the mere delivering of a share certificate, which was properly executed. Also see Birds *et al Boyle & Birds' Company Law* 187-188 and Millett *et al Gore-Browne on Companies* at 8-26.

414 *Kreditbank Cassel GMBH v Schenkers Ltd* [1927] 1 KB 826 (CA); *South London Greyhound Racecourses Ltd v Wake* [1931] 1 Ch 496. Also see Blackman *Commentary* ch 4 41.

authority to do so and thereby characterise this (his own) signature as a forgery.[415] They are further of the opinion that forgeries should not be treated as a special rule but that the normal principles of agency should be applied (ie lack of either actual or ostensible authority).[416] According to the general principles of agency, fraudulent acts (including forgeries)[417] may bind the principal if the agent acts within his ostensible authority.[418]

To regard it as a forgery in all cases where a representative, without the necessary authority, places his signature on a document and to exclude the applicability of the *Turquand* rule in such a case would, according Oosthuizen[419] be a ludicrous and an unnecessary interference on the worthiness of the outsider to be protected. It is in these cases where the third party needs the protection most. The matter should therefore be dealt with in a more acceptable manner within the existing boundaries of the *Turquand* rule, without adding forgery as a further exception.[420]

Other South African writers[421] are of the opinion that the *Turquand* rule should only be excluded in the instance where someone else's signature is forged and not when a person without authority attaches his own signature to a document in accordance with the decision in the Ruben's case.[422] This is also the position in

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415 Pennnington *Pennington's Company Law* 139; Birds *et at Boyle & Birds' Company Law* 188 Millett *et al Gore-Browne on Companies* 8-26.

416 Birds *et al Boyle & Birds' Company Law* 188; Millett *et al Gore-Browne on Companies* 8-26; Pennington *Penningston's Company Law* 139-140. According to Thompson 1959 *UTJL* 248 at 273 and further, a company may be held bound by estoppel in cases of forgeries, but the *Turquand* rule cannot apply in such cases.

417 Forgeries are not treated differently from other fraudulent acts – *Uxbridge Building Society v Pickard* [1939] 2 All ER 344 (CA).

418 Millett *et al Gore-Browne on Companies* 8-26. Also see *Northside Developments Pty Ltd v Registrar-General* [1990] HCA 32 [17] per Mason CJ:

> It may be, as Gower's Principles of Modern Company Law, 4th ed. (1979), suggests (at pp204-205), that forgery is not a true exception to the rule in *Turquand's* Case and that the cases are capable of explanation on the footing either that the forged document was not put forward as genuine by an officer acting within the scope of his actual or apparent authority or that the third party was put upon inquiry … . For purposes of the present case it is not necessary to resolve this question because it is possible to decide the case on the basis that forgery is not an exception to the rule. However, it will become apparent from what follows later in these reasons that, if there is a forgery exception, it has a limited area of operation.

419 Oosthuizen *Turquand-Reël* 285.

420 Oosthuizen *Turquand-Reël* 285.

421 Blackman *et al Commentary* ch 4 at 42.

422 *Ruben v Great Fingall Consolidated* [1906] AC 439 (HL).

Australia where the proposition in the *Kredit Bank* and *South London* cases were considered, but rejected.[423]

It appears that this aspect has not yet been considered by South Africa courts and if it should, the South African courts would most probably follow the English courts, which would lead to similar confusion.[424]

I submit that the view of Oosthuizen should be followed. In other words, forgeries should not exclude the operation of the *Turquand* rule. The established boundaries within which the *Turquand* rule operates would sufficiently provide a balance between the third party on the one hand and the company and its shareholders on the other. Should the courts not approve of such a view, it is hoped that the court would then at least follow the view of Blackman[425] and limit the exclusion of the *Turquand* rule only to those instances where there was a counterfeit signature by the agent.

3.2.2.5 *Turquand* v estoppel

The English courts have confused the *Turquand rule* and estoppel, regarding the former as merely a form of estoppel. This intermingling of the *Turquand* rule and estoppel also affected South African writers[426] and courts.[427] The *Turquand* rule

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423 Blackman *et al Commentary* ch 4 at 42.

424 Oosthuizen *Turquand-Reël* 282; Rabie *Verteenwoordiging* 174 mentions *Oranje Benefit Society v Central Merchant Bank Ltd* 1976 4 SA 659 (A) as a South African case where it appears at first glance to involve a forgery. The secretary, who was the principal executive officer, and the chairman of the executive committee of the Oranje Benefit Society wrote a letter to the bank and signed the letter with their own signatures, quoting the resolution of the society to stand surety for the debt of one Grundling, when in fact such resolution had been rescinded by a subsequent resolution of the executive committee of the society. In the same letter they also confirmed that they had the power, as chairman and secretary of the society to sign documents on behalf of the society. They subsequently also signed a document in terms of which the society stood surety for the indebtedness of Grundling to the bank. In this instance, however, the Bank sued the society for damages in delict because it was misled and induced by the misrepresentation of the secretary and chairman and the *Turquand* rule was not mentioned. The facts can in any event not be seen as representing a "forgery" in the narrow sense as discussed above.

425 Blackman *et al Commentary* ch 4 42.

426 Du Plessis *Grondslae* 203 fn 115; According to Fourie the position in South Africa regarding estoppel and the *Turquand* rule is not clear. See Fourie 1992 *TSAR* 1 at 3 and his references to the court cases.

427 See for example the comment of Claassen J in *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 264.

should, however, be seen as an independent rule. Support for this is found in England[428] and South Africa.[429] Although the appeal court in South Africa confirmed that the *Turquand* rule is an independent rule,[430] the risk exists that South African courts would apply the rule as an appearance form of estoppel. In a recent constitutional court decision the minority, for example, referred with approval to *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor),*[431] where it is stated that "[i]t has been said that the *Turquand* rule of company law is merely an application of estoppel."[432] This risk is not far-fetched at all in light of the recent majority decision of the highest court of South Africa where the court confused principles of representation where there had not even been confusion about it before.[433] To avoid this risk and to create certainty regarding the boundaries within which the *Turquand* rule finds application, Rabie suggested, before the promulgation of the Companies Act of 2008, that the repeal of the common-law doctrines of estoppel and the *Turquand* rule and its replacement with statutory counterparts in South Africa can resolve this problem.[434] Although section 20(7) of the Companies Act 2008 introduced, what appears to be a statutory *Turquand* rule, it differs from the common-law rule. The rule was not repealed and this only adds to the confusion regarding its interpretation and its integration with the common-law *Turquand* rule.[435] Furthermore, the Companies Act of 2008 does not deal with estoppel, with the result that the common law also still applies in this regard.

It is imperative that these two rules should be distinguished from one another, although they complement each other. There are far more requirements to prove

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428 Millett *et al Gore-Browne on Companies* 8-14; Pennington *Pennington's Company Law* 130.

429 *Farren v Sun Service SA Photo Trip Management (Pty) Ltd* 2004 2 SA 146 (C) 157; *The Mine Workers' Union v Prinsloo* 1948 3 SA 831 (A); Cilliers *et al Cilliers and Benade Corporate Law* 192; Blackman *et al Commentary* ch 4 at 47; Oosthuizen 1979 *TSAR* 1; Du Plessis 1997 *SA Merc LJ* 281 at 295-306; Rabie *Verteenwoordiging* 164.

430 *The Mine Workers' Union v Prinsloo* 1948 3 SA 831 (A).

431 [2015] 4 All SA 88 (WCC) [25].

432 See, for example, *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [110], referring to *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)* [2015] 4 All SA 88 (WCC) [25], where it is stated that

> [i]t has been said that the *Turquand* rule of company law is merely an application of estoppel.

433 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC). See para 3.2.3.7 below for a discussion of the confusion regarding ostensible authority and estoppel.

434 Rabie *Verteenwoordiging* 167.

435 See para 3.3.4 below.

for a successful plea of estoppel than when relying on the *Turquand* rule. There may, however, be instances where both the *Turquand* rule and the doctrine of estoppel may find application. In such instance the two principles should not be seen as being in conflict with one another, but rather as two doctrines complementing/supplementing each other.[436] The third party would in other words have a choice between relying on the *Turquand* rule or proving the requirements of estoppel in holding a company bound to a contract. It would be easier for the third party to comply with the fewer requirements of the*Turquand* rule in such a case. Should the third party not be able to comply with the requirements and boundaries of the *Turquand* rule, he would still be able to rely on estoppel if he is able to comply with all its requirements.

3.2.2.6 Extension of the *Turquand* rule to other bodies

The application of the *Turquand* rule has been extended to bodies, other than companies, for example municipalities and unions.[437]

*3.2.3 Estoppel*

As the field of estoppel is very wide, the focus in this study is limited to the circumstances where a company representative (agent) has exceeded his authority. Although the estoppel doctrine is not limited to company law, only its effect on company law will be discussed.

The earliest decisions in South Africa in this regard were based on the Roman law, although the courts acknowledged that the application of English law on estoppel would have had the same result.[438] In later decisions, the appeal court of South Africa applied the principles of English law regarding estoppel in South Africa.[439] In *Trust Bank van Afrika Bpk v Eksteen* the court found that the doctrine of estoppel in South Africa and in England is not the same and that the English

436 Du Plessis *Grondslae* 175-176.
437 For an indepth discussion of the extension of the *Turquand* rule, see Oosthuizen *Turquand-reël* 318-341.
438 Rabie *Verteenwoordiging* 200.
439 Rabie *Verteenwoordiging* 202.

"estoppel by representation" could not merely be taken over from England, although it may be used as an aid.[440] Its development in South Africa has taken place against the background of our own legal system.[441] Although English case law must therefore be treated with great caution, use may be made of English judgments.

Estoppel is a fairness principle that operates when it would be unreasonable if the principal (estoppel denier) would be permitted to rely on the true situation which does not correspond with the representation that he has made, if the third party (estoppel raiser) relied on such representation to his detriment.[442] It is said that a person has ostensible authority (also known as agency by estoppel or estoppel by representation or the holding out of authority) where that person does not have actual authority to bind the company but the company is prevented (estopped) from denying the authority.[443] Being a fairness principle, its aim is to prevent unreasonable unfairness.[444]

In certain instances, ostensible authority may overlap with implied authority and may be applicable to the same set of facts,[445] but these concepts must be clearly distinguished from one another.[446] In the case of implied authority, the agent has actual authority to act on behalf of the company whilst in the case of ostensible authority, no actual authority exists, but the company holds the representative out

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440 1964 3 SA 402 (A). For a full discussion on the origin of estoppel, see Rabie *Verteenwoordiging* 199-206.

441 *Connock's (SA) Motor Co Ltd v Sentraal Westelike Ko-operatiewe Maatskappy Bpk* 1964 2 SA 47 (T) 49.

442 Sonnekus *Estoppelleerstuk* 3.

443 *Big Dutchman (South Africa) (Pty) Ltd v Barclays National Bank Ltd* 1979 3 SA 267 (W) 284; *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 503.

444 Sonnekus *Estoppelleerstuk* 3.

445 *NBS Bank Ltd v Cape Produce Co (Pty) Ltd* 2002 1 SA 396 (SCA) at 411; *Glofinco v ABSA Bank Ltd t/a United Bank* 2002 6 SA 470 (SCA) 481 and the minority judgment at 492); *Randcoal Services Ltd v Randgold and Exploration Co Ltd* 1998 4 SA 825 (SCA) 841; *Coetzer v Mosenthals Ltd* [1963] 3 All SA 484 (A) 486-487; 1963 4 SA 22 (AD) at 23-24; *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) 14-15; *Inter-Continental Finance and Leasing Corporation (Pty) Ltd v Stands 56 and 57 Industria Ltd* 1979 3 SA 740 (W) 747-749; *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 502-506; [1964] 1 All ER 630 at 644-646.

446 *Coetzer v Mosenthals Ltd* [1963] 3 All SA 484 (A) 486-487; *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) 14-15; *Inter-Continental Finance and Leasing Corporation (Pty) Ltd v Stands 56 and 57 Industria Ltd* 1979 3 SA 740 (W) 747-749.

as having actual authority.[447] Unfortunately Van Zÿl J in *Zelpy 1780 (Proprietary) Limited v Mudaly* [448] makes the same error as that made in *Wolpert v Uitzigt Properties (Pty) Ltd*[449] on this point by stating:

> [t]he implied authority of an agent ..., may be inferred in circumstances where he purports to exercise authority of the type which such a director usually has, even though he was exceeding his actual authority.

It is also important to make a distinction between estoppel and the *Turquand* rule and regard them as two separate rules.[450] Although these two doctrines are independent and distinct from one another, the courts and writers sometimes confused the two and regarded the *Turquand* rule as just an appearance form of estoppel.[451] This resulted in the transplantation of the requirements of estoppel onto the *Turquand* rule.

Two further concepts which are often distinguished but should not be, are ostensible authority and estoppel. According to Oosthuizen[452] the stance was taken that ostensible authority was not based on estoppel but on independent contractual principles. Although this has led to heated differences of opinion, Oosthuizen contends that today it is generally accepted that ostensible authority and estoppel are one and the same. Although Kerr[453] still makes a distinction between ostensible authority and estoppel by representation, he has to admit that there is not yet

> … conclusive South African authority on the question whether or not agreement between the third person and the person who apparently has authority gives rise to a contract under which the apparent principal can both sue and be sued.[454]

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447 *Coetzer v Mosenthals Ltd* [1963] 3 All SA 484 (A) 486-487; Kerr *Agency* 67.

448 2015 JDR 0187 (KZP) [49].

449 1961 2 SA 257 (W) 266E.

450 Benade *et al Entrepreneurial Law* 151. See par 3.2.2.5 above.

451 See the references in Oosthuizen 1979 *TSAR* 1 at 8-9. Also see *Northside Developments Pty Ltd v Registrar General* [1990] HCA 32 [22]; McLennan 1979 *SALJ* 329 and 2009 *Obiter* 144 at 147; Thompson 1959 *UTLJ* 248 at 255 where this view is supported. Even in a recent constitutional court decision, namely *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [110], the court refers, albeit *obiter*, to *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)* [2015] 4 All SA 88 (WCC) [25], where the following is stated: "It has been said that the Turquand Rule of company law is merely an application of estoppel."

452 Oosthuizen *Turquand-reël* 70.

453 Kerr *Agency* 25-29.

454 Kerr *Agency* 26.

This distinction has featured prominently in the recent constitutional court case of *Makate v Vodacom (Pty) Ltd.*[455]

This case is discussed below[456] where I agree with the minority judgment in this case in that ostensible authority is just an appearance form of estoppel. The discussion that follows therefore emanates from the view that ostensible authority and estoppel are the same concept.

The leading case in England regarding estoppel is *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd.*[457]

The requirements that the third contracting party must prove to be successful when relying on estoppel have been laid down by the South African Supreme Court of Appeal in *NBS Bank Ltd v Cape Produce Co (Pty) Ltd,*[458] with approval of the *Freeman* case. These requirements are:[459]

a) The company must have represented (by words or conduct), that the agent had the necessary authority to represent the company;
b) The representation must have been made by the company and not by the agent;
c) The representation must have been in a form that the company should reasonably have expected that an outsider would act on the strength of it;
d) The third party should have been induced to deal with the agent because of the representation (in other words, reliance on the representation by the third party);
e) the reliance of the third party should have been reasonable; and
f) the third party should have been prejudiced by the representation.

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455 2016 4 SA 121 (CC).

456 Para 3.2.3.7 below.

457 [1964] 2 QB 480 (CA) 499. The aspects that have to be proved before a party can rely on estoppel by representation as set out by Diplock LJ are listed and discussed in Ch 2 para 2.2.3. These requirements are similar to those set out in the South African judgment in *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 266-267. Also see *Big Dutchman (South Africa) (Pty) Ltd v Barclays Bank Ltd* 1979 3 SA 267 (W) 282.

458 2002 1 SA 396 (SCA) [26].

459 These essentials were also stated by Navsa JA in *South African Broadcasting Corporation v Coop* 2006 2 SA 217 (SCA) 233-234. Also see *Northern Metropolitan Local Council v Company Unique Finance (Pty) Ltd* 2012 5 SA 323 (SCA) 334.

When comparing the requirements laid down in the *Freeman* case[460] with those listed in the *NBS* case,[461] it seems as though the *NBS* case[462] requires three further elements to be proved, namely the requirements set out under the *NBS* case[463] above in (c), (e) and (f). The *Freeman* case[464] has a further requirement that is not listed in the *NBS* case, being the fourth requirement regarding the role of the memorandum and articles of association of the company. The requirements under English law have been discussed in Chapter 2 above.[465] Only the differences between the requirements laid down by the two courts will be discussed here.

3.2.3.1 Representation of authority[466]

In South African law it was held that although the position that the representative holds in the company should be taken into consideration, it is not sufficient to establish an estoppel.[467] All the other surrounding circumstances ("trappings") must also be considered.[468]

3.2.3.2 Representation made by person with actual authority to manage the business[469]

In a recent South African judgment,[470] Wallis AJ, in his minority decision, confirmed that the representations by the agent alone, in whatever form, can never be sufficient to establish an estoppel. However, he extended this statement by stating that:

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460 *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 506 per Diplock LJ.
461 *NBS Bank Ltd v Cape Produce Co (Pty) Ltd* 2002 1 SA 396 (SCA).
462 *NBS Bank Ltd v Cape Produce Co (Pty) Ltd* 2002 1 SA 396 (SCA).
463 *NBS Bank Ltd v Cape Produce Co (Pty) Ltd* 2002 1 SA 396 (SCA).
464 *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA).
465 Ch 2 para 2.2.3 above.
466 See Ch 2 para 2.2.3.1 above.
467 In *NBS Bank Ltd v Cape Produce Co (Pty) Ltd* 2002 1 SA 396 (SCA) [32]; *South African Broadcasting Corporation v Coop* 2006 2 SA 217 (SCA) 236; *Northern Metropolitan Local Council v Company Unique Finance (Pty) Ltd* 2012 5 SA 323 (SCA) 339 and 340; Delport and Vorster *Henochsberg 2008* 98.
468 *South African Broadcasting Corporation v Coop* 2006 2 SA 217 (SCA) 236-237.
469 See Ch 2 para 2.2.3.2 above.
470 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC).

> … the conduct and statements relied upon may be those of the agent, provided the conduct or statements are themselves within the actual or ostensible authority of the agent.[471]

In other words, an agent of a company (principal) who does not have actual authority to make representations that another person (second agent) has authority, may have *ostensible authority* (through, for example, the conduct of the company placing that person in a particular position where a person in that position would usually have authority to make such representations) to make such a representation, in which event the company will be bound by the acts of the second agent, even though that second agent did not have actual authority to do the act on behalf of the company.[472]

The approach followed by Wallis AJ is in line with the development of ostensible authority in England in cases such as *Ebeed (trading as Egyptian International Foreign Trading Co) v Soplex Wholesale Supplies Ltd and P S Refson and Co Ltd (The Raffaella)*[473] and *ING Re (UK) Ltd v R&V Versicherung AG* referred to above.[474]

This line of thought is to be welcomed. If an agent has ostensible authority to act on behalf of a company and binds the company through that act, there is no reason why such an agent cannot have ostensible authority to make a representation through words or conduct that another person (second agent) has authority to bind the company and thereby clothing the second agent with ostensible authority.[475]

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471 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [165] per Wallis AJ.

472 Wallis AJ was of the view that the Director Product Development (second agent) had ostensible authority to conclude the contract with the third party on behalf of Vodacom through a representation of the Group CEO of the holding company of Vodacom and Executive Chairman of the operating company, who was also clothed with ostensible authority to make such a representation.

473 [1985] BCLC 404 (CA)

474 [2006] EWHC 1544 (Comm). Also see *AfrAsia Special Opportunities Fund (Pty) Ltd v Royal Anthem Investments 130 (Pty) Ltd* [2016] 4 All SA 16 (WCC) [42].

475 Oosthuizen 1978 *TSAR* 172 at 175 also shares this view. His reasoning is that as a managing director may on grounds of ostensible authority bind a company, he should on the same principle be in a position to create the appearance that some other person is authorised to bind the company in respect of a particular contract.

3.2.3.3 Culpability[476]

This was not listed as a requirement of estoppel in the *Freeman* case. In *Connock's (SA) Motor Co Ltd v Sentraal Westelike Ko-operatiewe Maatskappy Bpk*[477] the court stated that although estoppel has "migrated" to South Africa from England and guidance should be sought from English decisions, once the principles of estoppel had been permanently absorbed here, they tended to develop along lines that are specific to South Africa against the background of our own law.[478] In *Strachan v Blackbeard and Son*[479] one element to be complied with before estoppel can be founded has been stated to be that the representation had to be "of such nature that it could reasonably have been expected to mislead".[480] Although this was stated *obiter dictum,* the court accepted it in *Monzali v Smith.*[481]

The "reasonable expectation by the principal that the representation will mislead" was thereafter also adopted in *Connock's (SA) Motor Co Ltd v Sentraal Westelike Ko-operatiewe Maatskappy Bpk*[482] and several prior cases.[483] When the court assessed whether the representor should reasonably have expected that his conduct would mislead the representee, it was stated that the court should take into account the representor's knowledge or ignorance of any facts that gave his conduct a particular significance attached to it by the representee.[484] If the representor were ignorant of certain facts it might mean that he could not reasonably have expected that his conduct would mislead the representee.[485]

476 See Ch 2 para 2.2.3.6 above.
477 1964 2 SA 47 (T) at 49 per Trollip J.
478 Since the first formulation of estoppel, the doctrine has undergone constant development even in England, according to Trollip J – *Connock's (SA) Motor Co Ltd v Sentraal Westelike Ko-operatiewe Maatskappy Bpk* 1964 2 SA 47 (T) 49.
479 1910 AD 282.
480 *Strachan v Blackbeard and Son* 1910 AD 282 at 289.
481 *Monzali v Smith* 1929 AD 382 at 386, per Stratford JA.
482 1964 2 SA 47 (T) at 49.
483 These cases are listed in *Connock's (SA) Motor Co Ltd v Sentraal Westelike Ko-operatiewe Maatskappy Bpk* 1964 2 SA 47 (T) 51.
484 *Connock's (SA) Motor Co Ltd v Sentraal Westelike Ko-operatiewe Maatskappy Bpk* 1964 2 SA 47 (T) 51.
485 *Connock's (SA) Motor Co Ltd v Sentraal Westelike Ko-operatiewe Maatskappy Bpk* 1964 2 SA 47 (T) 51.

In *Johaadien v Stanley Porter (Paarl) (Pty) Ltd*[486] the majority of the Court of Appeal found that negligence by the representor needs to be proved by the representee.[487] Only one appeal court judge mentioned in his minority judgment that the appeal court did not, in the *Stachan* and *Monzali* cases, require negligence as an indispensable requirement for estoppel, but that the court in the two cases referred only to the expectation in the sense of an element of estoppel in the case of omission.[488]

In *NBS Bank Ltd v Cape Produce (Pty) Ltd*[489] the court applied the *dictum* in *Hely-Hutchinson v Brayhead Ltd* [490] as follows:

> Although an intention to mislead is not a requirement of estoppel, where such an intention is lacking and a course of conduct is relied on as constituting the representation,[491] the conduct must be of such a kind as could reasonably have been expected by the person responsible for it, to mislead. Regard is had to the position in which he is placed and the knowledge he possesses.[492]

Sonnekus[493] is of the opinion that the reasonable expectation of the representor requirement, as discussed above, does not constitute a requirement of negligence in relation to estoppel in a setting of representation. According to him the well-known test for negligence, as used in the law of delict, is two-fold: Firstly it is asked whether the reasonable person in the position of the perpetrator of the delict could foresee prejudice to others due to his unlawful conduct; and secondly, if he, as a reasonable person would have taken steps to prevent the foreseeable prejudice.[494] Sonnekus[495] refers to the above quotation from the *NBS* case and states that the quoted test is not a two-fold test as required for negligence, as the second part of the test is absent. He is of the opinion that the above quotation does not require that negligence by the principal should be proved in all cases of

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486 1970 1 SA 394 (A) per Steyn JA and supported by three of the other appeal court judges..

487 According to Steyn (presiding), the reasonable expectation requirement as laid down in *Strachan v Blackbeard and Son* 1910 AD 282 and *Monzali v Smith* 1929 AD 382 cannot really be distinguished from negligence.

488 *Johaadien v Stanley Porter (Paarl) (Pty) Ltd* 1970 1 SA 394 (A) 412-413 per Rumpff JA.

489 2002 1 SA 396 (SCA) per Schutz JA.

490 [1968] 1 QB 549 (CA) 583A-G.

491 As opposed to a representation by words.

492 At [25].

493 Sonnekus *Estoppelleerstuk* 301.

494 Sonnekus *Estoppelleerstuk* 265.

495 Sonnekus *Estoppelleerstuk* 301.

estoppel by representation. According to Sonnekus[496] proof of the increased risk of prejudice for third parties due to the use by a principal of a representative whose boundaries of authority to represent the principal are not clearly shown to outsiders, would be sufficient. The third party will, however, so Sonnekus[497] contends, only be able to hold the principal liable if the representative acted within his usual authority, that is, within the authority that a person in the position of the representative would normally have with the principal.

Certain writers[498] require guilt as one of the essential elements of estoppel. Other writers[499] do not require guilt as an essential requirement in all instances of estoppel. It seems as though the guilt requirement in an agency setting has not been finally settled in our law.

I agree with Sonnekus that the cases, although not expressly requiring guilt when estoppel is pleaded, do require that the representation that the agent had the required authority to bind his principal (the company), should have been in a form that the principal (company) should reasonably have expected that an outsider would act on the strength of such representation.[500]

3.2.3.4 Reasonable reliance by the third party

One of the factors that is taken into consideration when determining whether the reliance of the third party was reasonable is to look at the position that the

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496 Sonnekus *Estoppelleerstuk* 301 and 302.

497 Sonnekus *Estoppelleerstuk* 301 and 303.

498 See Sonnekus *Estoppelleerstuk* 271-273 where he sets out the viewpionts of different academic writers; Lewis 1986 *SALJ* 69 at 73; Cilliers *et al Cilliers and Benade Corporate Law* 193.

499 See the opinions of writers set out in Sonnekus *Estoppelleerstuk* 273-276. Also see McLennan 1979 *SALJ* 329 at 367:

> Although it is apparently settled law that a defendant seeking to set up an estoppel to defeat an owner's vindicatory action must prove negligence or fault of some kind on the owner's part, … it has never been definitely established whether the fault requirement applies to this branch of law.

McLennan at 367 suggests that it should not be required from the third party to prove negligence:

> Setting up an estoppel against a company which is governed by organs whose membership often changes is inherently more difficult than proving an estoppel against a natural person; to add the fault requirement to the third party's difficulties would weigh the balance too heavily in favour of the company.

500 Also see Delport and Vorster *Henochsberg 2008* 98.

representative holds in the company. If the representative does not act within the powers that would usually be conferred on an official in the same capacity as him, then a third party will not be reasonable in his reliance on the fact that such a representative did have the necessary authority to perform that particular act.[501]

In the instance where there were suspicious or extraordinary circumstances that placed the third party on inquiry[502] (for example, where the representative used money due to the company for his own personal benefit),[503] the third party cannot make use of estoppel against the company, as it cannot be said that the third party reasonably relied on a misrepresentation by the company. It should be noted that a third party can also not estop a company by relying on a lack of authority in instances where that third party was aware of such lack of authority.[504] The third party should therefore be *bona fide*.

3.2.3.5 Prejudice suffered by third party

The third party raising the estoppel must not only prove that the principal (company) had made a representation, but also that the third party had been moved to act on the representation so as to alter his own previous position to his detriment.[505] A mere change in position is not determinant if the third party cannot prove prejudice.[506]

501 *Zelpy 1780 (Proprietary) Limited v Mudaly* 2015 JDR 0187 (KZP) [50].
502 Blackman *et al Commentary* ch 4 46.
503 *Contemporary Refrigeration (Pty) Ltd (In Liquidation) v Leites and Sonpoll Investments (Pty) Ltd* 1967 2 SA 388 (D) 393.
504 Blackman *et al Commentary* ch 4 46. Also see *Criterion Properties Plc v Stratford UK Properties LLC* [2004] 1 WLR 1846 (HL) [31].
505 Sonnekus *Estoppelleerstuk* 210.
506 Sonnekus *Estoppelleerstuk* 210.

3.2.3.6 Fourth requirement in *Freeman*-case[507] (that under its memorandum or articles of association the company was not deprived of the capacity either to enter into a contract of the kind sought to be enforced or to delegate authority to the agent to enter into a contract of that kind[508])

In the instance where the Memorandum of Incorporation limits or restricts the authority of the board as provided for in section 66(1), or the authority of any director, officer or other agent, due to the non-applicability of the doctrine of constructive notice, the third party will still succeed in raising estoppel as a defence. Obviously in the instance where the doctrine of constructive notice still operates in respect of such restrictive condition, (as the limitation can be regarded as a restrictive condition to which attention has been drawn in the Notice of Incorporation or further Notice of Amendment of an "RF" Company[509]) the third party would be deemed to know of those restrictions. The third party would not be able to rely on estoppel. Due to the existence of the restrictive condition, for example that a certain director may not act on behalf of the company, there could not have been a representation regarding the agent's authority as such agent could never have any authority.[510]

In the event that the third party had actual knowledge of the restriction on the powers of the board to authorise a particular person or restrictions on the powers that may be delegated to a particular person, estoppel can also not come to the aid of the third party.[511]

3.2.3.7 Ostensible (apparent) authority and estoppel

In a recent case, *Makate v Vodacom (Pty) Ltd*[512] the majority judgment of the Constitutional Court made a distinction between ostensible (apparent) authority and estoppel and indicated that ostensible authority is now a type of actual

507 *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA).
508 See Ch 2 para 2.2.3.4.
509 Section 19(5)(a). See para 3.3.2 below.
510 Cilliers *et al Cilliers and Benade Corporate Law* 191; Du Plessis *Grondslae* 205; Oosthuizen 1979 *TSAR* 1 at 5.
511 Cassim *et al Contemporary Company Law* 190.
512 2016 4 SA 121 (CC).

authority, not based on estoppel.[513] In this case Makate, an employee of Vodacom, invented the "Please call me" idea.

Makate and Geissler, the Director of Product Development (and a member of the board of directors of Vodacom) negotiated and orally agreed that Vodacom would use the idea of Makate in developing a new product. The new product would then be put on trial to ascertain its commercial viability. Should the product prove to be a success, Makate would be compensated by sharing in the revenue generated by the product resulting from his idea. No agreement was, however, reached on the amount or percentage of remuneration and the negotiations in this regard were postponed to a later stage, after the product had been tested for commercial viability. They did, however, agree that if they fail to agree on compensation, the Chief Executive Officer of Vodacom, Knott-Craig, would determine the remuneration.

After developing and launching the product "Please call me", the product proved to be an instant success which generated billions of rand for Vodacom. This product was launched before Vodacom received formal approval for it from its board of directors. This business decision and its implementation without board approval were, however, customary practice at Vodacom.

Although the product was a success, Vodacom did not negotiate any remuneration with Makate for the use of his idea. Instead, Knott-Craig (the CEO) and Geissler falsely credited the origin of the idea to Knott-Craig.

Makate instituted action against Vodacom in the South Gauteng High Court to enforce his rights regarding the use of his idea by Vodacom.[514] After ruling that Makate did, on a balance of probabilities, prove that he entered into an agreement with Geissler on the terms that he testified to, the court had to determine whether Makate had proved on a balance of probabilities that Vodacom was bound by the agreement.

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513 Delport and Vorster *Henochsberg 2008* 98.

514 *Makate v Vodacom (Pty) Limited* [2015] JOL 34657 (GJ).

The High Court rejected Makate's claim for compensation because he had failed to plead estoppel in replication. According to the court, instead of pleading estoppel in his particulars of claim, Makate should have pleaded estoppel in his replication.

The court also found that Makate would in any event not have been successful upon a plea of ostensible authority, as he could not prove the requirements for estoppel as laid down in[515] *Northern Metropolitan Local Council v Company Unique Finance (Pty) Ltd*[516] and *NBS Bank Ltd v Cape Produce Co (Pty) Ltd.*[517] The High Court dismissed the claim of the plaintiff (Makate). The High Court and the Supreme Court of Appeal refused to grant leave to appeal and Makate appealed to the Constitutional Court.

The one issue of relevance for this dissertation that the Constitutional Court had to decide was whether Makate had proved all the requirements for estoppel and whether he pleaded estoppel correctly.[518]

The majority[519] of the court held that although estoppel is a shield and not a sword and could therefore only be pleaded in replication, the High Court confused estoppel with ostensible authority and that the correct concept to be used in the matter was the latter. According to the court, estoppel and ostensible authority are two different things, although it conceded that in the past it has been treated by the courts as the same thing.[520] It distinguished the two by stating that ostensible authority is authority but estoppel is no authority at all.[521] The court held the view that, as it was stated in *Hely-Hutchinson v Brayhead Ltd*,[522] ostensible authority

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515 Note that in both of these Supreme Court of Appeal cases, the courts, when listing the requirements, indicated that they were the requirements for "ostensible authority". In other words, these courts did not make use of the concept "estoppel".

516 2012 5 SA 323 (SCA) [28].

517 2002 1 SA 396 (SCA) [26].

518 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [1].

519 Per Jafta J.

520 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [44].

521 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [45] – [47].

522 [1968] 1 QB 549 (CA) 583A-G per Lord Denning. Note that in this case Lord Denning at 583 accepted the law as was laid down in *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) and did not find it necessary to consider it at length. It is interesting to note that the court found liability on implied authority in this case and not on ostensible authority.

(apparent authority) is authority as it appears to others, which means that only the creation of an appearance by the principal needs to be proved, whereas many more elements have to be proved if estoppel is to be relied upon.[523]

The majority judgment criticised the minority decision and insisted that:

> … there is not a single case referred to in our law that holds that apparent [ostensible] authority is estoppel, except *NBS Bank* and subsequent decisions that followed it.[524]

The court concluded that Vodacom could be held bound to the agreement on grounds of ostensible authority (as opposed to estoppel). According to *Henochsberg*[525] the facts of the case would appear to indicate implied authority rather than ostensible authority.

I cannot, with respect, agree with the view of the majority that ostensible authority is authority and that estoppel is not. Neither ostensible authority nor estoppel constitutes authority.

The minority decision of the Constitutional Court,[526] also found in favour of Makate. They, however, disagreed that ostensible authority and estoppel are two different concepts.

In terms of the minority judgment, it is settled law that ostensible authority is a form of estoppel, commonly referred to as agency by estoppel.[527] Wallis AJ accepted that estoppel has a wide range of application in other fields and listed a few that occurred to him.[528] He then concluded that on both principle and authority he was

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523 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [49].

524 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [70].

525 Delport and Vorster *Henochsberg 2008* 106(2).

526 Per Wallis AJ with Cameron J, Madlanga J, Van der Westhuizen J concurring.

527 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [109].

528 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [110]. Examples that he listed are motor dealer cases, share dealing transactions and vindicatory actions. Unfortunately he directly thereafter stated, referring to *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)* [2015] 4 All SA 88 (WCC) [25], that

> [i]t has been said that the Turquand Rule of company law is merely an application of estoppel.

The *Turquand* rule is an independent rule and this statement cannot be accepted. See in this regard the discussion of Oosthuizen 1979 *TSAR* 1 at 7-9.

convinced that ostensible authority is merely one more instance of estoppel.[529] He stated that ostensible authority is no authority at all, express or implied and that takes it into the realm of estoppel.[530] In reacting to the majority judgment, Wallis AJ stated that they based their understanding of English law on a single sentence in a judgment of Lord Denning in the Court of Appeal,[531] which is inconsistent with the authoritative judgments of English courts.[532] The approach of the majority is also inconsistent with the judgments of our courts since the early twentieth century, as well as the views of our textbook writers.[533] Further, the majority only tried to make a distinction because of the erroneous approach of the trial court to the proper pleading of ostensible authority.[534]

On grounds of the unbroken line of authorities in English and South African law, Wallis AJ asserts that ostensible authority was squarely placed within the framework of estoppel by the appeal court decision of *NBS Bank Ltd v Cape Produce (Pty) Ltd*[535] as follows:

> As Denning MR points out,[536] ostensible authority flows from the appearances of authority created by the principal. Actual authority may be important, as it is in this case, in sketching the framework of the image presented, but the overall impression received by the viewer from the principal may be much more detailed. Our law has borrowed an expression, estoppel, to describe a situation where a representor may be held accountable when he has created an impression in another's mind, even though he may not have intended to do so and even though the impression is in fact wrong. Where a principal is held liable because of the ostensible authority of an agent, agency by estoppel is said to arise.[537]

Wallis AJ thereafter came to the conclusion that:

> … in English law ostensible authority is an estoppel by representation and that the earlier decisions of our courts that say that ostensible or apparent authority is a

529 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [110].
530 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [110]. Also see Reynolds *Bowstead and Reynolds Agency* 106 para 3-005.
531 *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA).
532 Wallis AJ referred to *inter alia Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) and *Armagas Ltd v Mundogas SA, The Ocean Frost* [1986] 2 All ER 385 (HL).
533 See *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [140]-[153] and the authorities listed there.
534 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [109].
535 2002 1 SA 396 (SCA), per Schutz JA.
536 Schutz JA referred here to the judgment of Denning MR in *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA) 583A-G.
537 *NBS Bank Ltd v Cape Produce (Pty) Ltd and Others* 2002 1 SA 396 (SCA) [25].

> form of estoppel are correct. That is also the view of the academic commentators both here and overseas.[538]

From the line of decisions, both in England and later in South Africa, I, with respect, agree with the minority decision of the Constitutional Court per Wallis AJ, that ostensible authority and estoppel are the same thing.

According to the majority the only requirement for holding a company bound on grounds of ostensible authority is that the principal (company) created an appearance that the agent has authority to act on its behalf. If this were so it would result in an unfair balance of rights and interests between the company and the third party. It might, for example, happen that the third party is not even aware of the representation, so it would be impossible for him to rely on such representation when he enters into the contract. It would be unfair if the company is to be held bound under these circumstances. If the third party is not aware of the representation he can therefore not rely on the representation. The requirement that the third party should have relied on the representation is therefore essential and was listed as a requirement in both the *Freeman* case and subsequent cases such as the *NBS* case.[539]

Wallis AJ further also stated in this regard that a representation alone was not sufficient. The contracting third party should have reasonably acted upon the representation to his prejudice. If the latter requirement was not met as well, it would again have the unfair result that a contracting third party could hold a company liable on grounds of ostensible authority in cases where he had actual knowledge that the authority of the agent who acts on behalf of the company had been restricted, although it appeared that he had authority.[540]

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538 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [154].

539 See for example *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) 504, 506 and 508. On page 508 the following is stipulated:

> Since … the representation on which he in fact relied as inducing him to enter into the contract comprised the articles of association of the company as well as the conduct of the board, it would be necessary for him to establish first, that he knew the contents of the articles … and secondly, that the conduct of the board in the light of that knowledge would be understood by a reasonable man as a representation that the agent had authority to enter into the contract to be enforced, ... .

Also see *Insurance Trust and Investments (Pty) Ltd v Mudaliar* 1943 NPD 45 at 55 and 57:

> It is for the plaintiff to plead and prove the estoppel he relies on. If he relies on the contents of the articles as constituting a representation, he must prove that he knew the contents.

540 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [139].

The viewpoint of the minority in the *Makate* case, as per Wallis AJ regarding the fact that ostensible authority is a form of estoppel is to be preferred and is supported over the decision of the majority.[541]

In light of the uncertainty created in the recent constitutional court judgement in *Makate v Vodacom (Pty) Ltd*[542] regarding the concept of ostensible (apparent) authority and estoppel and the confusion that these are different concepts with different requirements, it is recommended that estoppel and the application and requirements thereof in a company environment should be codified in the form of legislation.[543]

## 3.3 Companies Act of 2008

### *3.3.1 Directors to manage the business and affairs of the company - section 66(1)*

The two primary organs in a company are the board of directors and the shareholders in general meeting.[544] The Companies Act 61 of 1973 (hereafter called the Companies Act of 1973) did not prescribe the manner in which power had to be divided between these two organs and the company could decide on this by making provision for the division of power in its constitution.

According to Cassim *et al*[545] the Companies Act of 2008 follows the approach of the United States of America by allocating the powers of the directors in the Act itself. In this regard, section 66(1) of the Companies Act of 2008 provides that the business and affairs of a company must be managed by or under the direction of the board of directors.[546]

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541 Also find support for the viewpoint of Wallis AJ in Delport and Vorster *Henochsberg 2008* 98 and Cassim and Cassim 2017 *SALJ* 639 at 647. Further, see the critical discussions of this case by Sharrock 2016 *PELJ* 1-21 and Sonnekus 2016 *TSAR* 538-563.

542 2016 4 SA 121 (CC).

543 Rabie pleaded for the repeal and replacement of the doctrine of estoppel by a statutory equivalent. The reason he gives is that the South African courts have dealt with the application of estoppel in a haphazard way and that the estoppel doctrine is in conflict with several academic viewpoints in South Africa (Rabie *Verteenwoordiging* 217-218).

544 Katz 2010 *Acta Juridica* 248 at 258.

545 Cassim *et al Contemporary Company Law* 123.

546 The powers of the board are, however, subject to the company's Memorandum of Incorporation and the Companies Act of 2008. See s 66(1).

A distinction should be drawn, when this section is read, between the acts of the board of directors on the one hand and acts of individuals who act under the authority that was conferred on them by the board of directors.

3.3.1.1 Acts of the board of directors

The differences of opinion under the Companies Act of 1973 on whether the power of management conferred on the board of directors was original or delegated[547] have been removed by the Companies Act of 2008 in that the power conferred on the board by the Act can without a doubt be described as original.[548] The ultimate power in the company now lies with the board of directors.[549] According to *Henochsberg*[550] it will not be necessary for a third party to prove actual authority if the board of directors acts in terms of section 66.

The Companies Act of 2008 has provided balances and measures to ensure that the directors do not misuse these wide powers that have been granted to the board.[551] The 2008 Act still requires shareholder approval where the board exercises its powers in respect of certain fundamental transactions.[552] It is, however, not the purpose of this dissertation to investigate these checks and balances. It should be noted that it is the board who must act, which means that it should act as a unit.[553] In other words, the board must still exercise its powers collectively as a board.[554]

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547 In this regard, see Du Plessis *Grondslae* 47 and the authorities cited there.

548 Delport and Vorster *Henochsberg 2008* 250(3); *Pretorius v PB Meat (Pty) Limited* [2016] JOL 35367 (WCC) [25]; Coetzee *Business and Affairs* 42. In other words, the power of the directors is not derived from an agreement through the machinery of the articles as under the Companies Act of 1973. In England, however, the board derives its powers from the articles of the company – see Ch 2 para 2.2.1.

549 Delport and Vorster *Henochsberg 2008* 250(3); *Pretorius v PB Meat (Pty) Limited* [2016] JOL 35367 (WCC) [25]; *Navigator Property Investments (Pty) Ltd v Silver Lakes Crossing Shopping Centre (Pty) Ltd* [2014] JOL 32101 (WCC) [31].

550 Delport and Vorster *Henochsberg 2008* 95-96.

551 See for example s 76 of the Companies Act of 2008.

552 Katz 2010 *Acta Juridica* 248 at 259. In this regard see for example s 112 of the Act pertaining to the alienation of all or the greater part of the assets or undertaking by the company.

553 Delport and Vorster *Henochsberg 2008* 250(2).

554 *Navigator Property Investments (Pty) Ltd v Silver Lakes Crossing Shopping Centre (Pty) Ltd* [2014] JOL 32101 (WCC) [31].

The powers of the directors are defined by what is meant by "business and affairs". As these two words are not defined in the 2008 Act, their interpretation can be sought in, among other things, judgments and older legislation.

When comparing section 66 with, for example, article 59 of Table A[555] of the Companies Act of 1973, it is clear that the board of directors has wider powers under section 66 than under the Companies Act of 1973 if the company adopted Table A of that Act. Not only are the directors empowered to manage the business of the company but also its affairs. Although the *dictum* in *Ex Parte Russlyn Construction (Pty) Ltd*[556] pertains to Article 59 of Table A of the 1973 Companies Act, I agree with *Henochsberg*[557] that the interpretation of the word "affairs" in that case should also be applied to the use of the word "affairs" as set out in section 66 of the 2008 Act. In this case the question that the court had to consider was whether the directors had the power to liquidate the company of which they were directors, without the approval of the shareholders in general meeting. The court regarded "affairs" as being a concept wider than "business" and that the power to manage the business of a company most probably includes the power to stop the trading activities of the company.[558] However, it would not include the power to liquidate the company.[559] *Henochsberg*[560] supports the view taken in the *Russlyn* case that "affairs" has a broader meaning than "business".

The board of directors further has the authority to exercise all of the powers of the company and to perform all of the functions of the company. This wording was not part of article 59 of Table A under the 1973 Act. [561]

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555 Article 59 of Table A under the Companies Act of 1973 provides *inter alia* that:

> The business of the company shall be managed by the directors who may … exercise all such powers of the company as are not by the Act, or by these articles, required to be exercised by the company in general meeting, … .

556 1987 1 SA 33 (D).

557 Delport and Vorster *Henochsberg 2008* 250(2).

558 *Ex Parte Russlyn Construction (Pty) Ltd* 1987 1 SA 33 (D) 36-37, approved and followed in *Ex Parte New Seasons Auto Holdings (Pty) Ltd* 2008 4 SA 341 (W).

559 At 36H-J to 37A-B.

560 Delport and Vorster *Henochsberg 2008* 250(2).

561 Coetzee *Business and Affairs* 47.

3.3.1.2 Agent acts under direction of the board

From the above it is clear that the board of directors has, save for having the power to manage, direct and supervise the business and affairs of the company, the right to delegate one or more of these powers to a board committee, managing director, director or other agent. Although the standard Memorandum of Incorporation in the regulations to the Companies Act of 2008 does not expressly authorise the board to appoint a managing director,[562] and does not provide that the board may from time to time entrust to or confer upon a managing director or manager, for the time being, such of the powers and authorities vested in them as they may think fit, as the standard articles under the Companies Act of 1973 did,[563] I agree with *Henochsberg*[564] that even if the board was not authorised to delegate its authority in section 66(1), it would still be entitled to do so, as its authority is original and not delegated and therefore the rule *delegatus delegare non potest* does not apply.[565] The board will therefore be entitled to, for example, appoint a managing director.

The board may appoint any number of committees of directors and may delegate any of its authority, subject to the Memorandum of Incorporation, to such board committees.[566]

The common-law principles of agency will therefore continue to be applicable where the board has delegated its authority.[567]

A company will be bound to a contract entered into on its behalf by its managing director, where such managing director had actual (either express or implied) authority conferred upon him by the board of directors to conclude that contract.[568]

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562 See for example CoR15.1E (although it refers to the appointment of officers) and CoR15.1B.

563 See for example Article 62 of Table A. If the articles did not make provision for a managing director to be appointed by the board, a person could not be appointed as a managing director – *Moresby White v Rangeland Ltd* 1952 4 SA 285 (SR) 287.

564 Delport and Vorster *Henochsberg 2008* 250(5).

565 Also see Cassim *et al Contemporary Company Law* 417.

566 S 72(1) of the Companies Act 71 of 2008.

567 Cassim *et al Contemporary Company Law* 187.

568 Delport and Vorster *Henochsberg 2008* 251; Cassim *et al Contemporary Company Law* 188.

If the managing director did not have actual authority the company will nevertheless be bound where the company ratifies such contract.[569]

The managing director would have implied authority if he acted within the scope of his office as managing director. In other words all those powers that usually relate to or are incidental to the position of a managing director of a company that carries on the kind of business that the company carries on would fall within the implied authority of the managing director.[570] The implied authority of the managing director may, however, have been restricted by the board of directors in which event it cannot be said that the managing director had implied actual authority to act on behalf of the company.[571] In such event, the company may still be held bound to the contract if the third party can successfully rely on the *Turquand rule*[572] or section 20(7) of the Companies Act of 2008 or if he is able to prove all the essential requirements for estoppel.[573]

It is submitted that the board has the power to appoint any other official and confer some of its powers on such official in the same way as it can appoint a managing director. It is submitted that the usual authority of an agent is still a helpful tool in establishing whether a particular officer had implied authority to act on behalf of the company.[574] As usual authority was used by the courts in the past and as the common law in this regard has not been expressly excluded by the Act, the common law still applies to the extent that it has not been altered by legislation.[575] If the usual authority of the officer has not been restricted by the board, his usual authority will be his implied authority.[576] In these instances, the application of the

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569 Delport and Vorster *Henochsberg 2008* 251.

570 Delport and Vorster *Henochsberg 2008* 251. See Ch 2 par 2.2.1 above.

571 Cassim *et al Contemporary Company Law* 416-417.

572 Obviously the third party would only be successful in relying on the *Turquand* rule if the particular set of facts fall under the application of the rule and the relief is not excluded under the exceptions applicable to the rule.

573 *Legg & Co v Premier Tobacco Co* 1926 AD 132 at 139-144; *Wolpert v Uitzicht Properties (Pty) Ltd* 1961 (3) SA 257 (W) 266-267; *Contemporary Refrigeration (Pty) Ltd (In Liquidation) v Leites and Sonpoll Investments (Pty) Ltd* 1967 2 SA 388 (D) 392; *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) 14.

574 See Ch 2 para 2.2.1 and para 3.2.1 above.

575 This is subject thereto that such interpretation does not conflict with the Constitution of the Republic of South Africa, 1996 and that statutory rights and remedies more advantageous to those who stand to benefit from them will take precedence over common-law rights and remedies. See Du Plessis *Re-Interpretation of Statutes* 177-181.

576 See Ch 2 para 2.2.1 above in this regard.

*Turquand rule* would be limited,[577] but the third party would still be able to hold the company bound if the requirements for estoppel can be proved.

Section 20 of the Companies Act of 2008 also deals with persons acting on behalf of a company. The organisation of the subsections in section 20 is rather chaotic. Whereas section 20(1), 20(2) and 20(5) pertains to contraventions of limitations, restrictions and qualifications *in the Memorandum of Incorporation* of a company, section 20(4) pertains to restrictions *in the Act*. Further, it takes a great effort on the part of the reader to ascertain whether a particular subsection relates to the capacity of the company (an act of the company) or only to a representation by the directors (act by directors) or to both capacity and representation.

I submit that only subsections (2), (3), (5), (6), (7) and (8) pertain to the authority of directors. Some of these subsections also relate to the capacity of the company. Subsections (2) and (3), pertaining to ratification and subsection (6) dealing with the internal consequences (as opposed to external consenquences) do not form part of the focus of this dissertation and are therefore not discussed. Subsection (5) is also not discussed.[578] Only subsections (7) and (8) [579] are discussed insofar as they relate to the authority of directors.

3.3.1.3 Powers of the board restricted by its Memorandum of Incorporation or by the 2008 Act

Section 66(1) of the Companies Act of 2008 further provides that the board has the authority to exercise all of the powers and perform any of the functions of the company, except to the extent that the Act itself or the Memorandum of Incorporation of the company provides to the contrary.

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577 *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) 15.

578 S 20(5) provides that certain interested parties may apply to the High Court for an interdict restraining *inter alia* the directors from doing anything inconsistent with a limitation, restriction or qualification in the Memorandum of Incorporation. Any such proceedings will, however, not prejudice the right of a third party to damages, if such third party obtained those rights in good faith and did not have actual knowledge of such limitation etc.

579 Ss (7) and (8) are discussed under paragraph 3.3.4 below.

In the event that the company's *Memorandum of Incorporation* places a total restriction on one of the powers of the board, for example, that the board may not borrow money in excess of R50 million and the board exceeds such restriction, the third party cannot simply hold the company to the loan agreement, by averring that he is not deemed to know of this restriction due to the abolition of the doctrine of constructive notice.[580] The fact that the third party is not deemed to know of this restriction, does not constitute a legal ground on which the company can be held liable. If, however, the third party is able to prove all the essential requirements for estoppel, he may be successful in holding the company to the contract on these grounds. The doctrine of constructive notice previously deprived a third party of the right to rely on estoppel.[581]

If an authority or power of the board is made dependent on compliance with some or other internal formality or formal or procedural requirement, for example, the board may only borrow money in excess of R10 million, subject to prior shareholder approval, again, the third party cannot use the fact that he is not deemed to know about this requirement as the legal basis to hold the company to the contract where the board entered into a loan agreement in excess of R10 million without prior shareholder approval. In this instance the third party may be able to hold the company to the contract if he is able to bring the transaction within the scope of application of either the *Turquand* rule or section 20(7) of the Companies Act of 2008.[582]

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580 See para 3.3.2 below for a discussion on the abolition of the doctrine of constructive notice.

581 See para 2.2.3.4 of Ch 2 above and para 3.2.3.6 of this chapter above. One or more shareholders, directors or prescribed officers of the company may apply to the High Court for an order to restrain the directors from doing anything inconsistent with such a restriction but this would not prejudice the right to damages of a *bona fide* third party – s 20(5). It is difficult to see how a third party could have acquired rights if the company has not yet entered into the contract because it is being restrained from entering into the contract. It might be that this section refers to the situation where the contract has already been concluded by the company, in other words the third party has acquired rights in terms of the contract, but the company is then restrained from complying with its obligations in terms of the contract. The chances that a third party would have suffered damages before any contract had been concluded are very slim (Van der Linde 2015 *TSAR* 833 at 838). As the third party is only entitled to damages, the benefit (for the shareholder, director, prescribed officer) lies in the fact that the third party cannot claim specific performance under the contract but will only be entitled to damages.

582 Section 20(7) is discussed in para 3.3.4 below.

Where the third party has actual knowledge of the total restriction or where he is deemed to have knowledge thereof due to the operation of the doctrine of constructive notice in the case where he deals with an "RF" company,[583] the third party would not be successful in relying on estoppel. In such an instance the *Turquand* rule also finds no application.[584] The restriction is absolute and not an authority that is granted but made dependent on compliance with some or other internal formality that can be made good by the *Turquand* rule. Section 20(7) of the Companies Act would also not be available to the third party.[585]

Where the third party has actual knowledge or deemed knowledge[586] of a limitation on the powers of the board, but which limitation may be overridden by compliance with an internal procedure, for example a requirement that a shareholders' resolution should be obtained before the board can do a particular act, then the third party may still be able to hold the company liable on grounds of the *Turquand* rule[587] or section 20(7),[588] if he complies with the parameters within which these who rules operate.

A third party will not be able to hold the company bound to a contract on grounds of the *Turquand* rule if the board of directors exceeded its authority, as restricted by the *Companies Act itself*.[589] If the restriction or limitation in the Act is of a substantive nature and cannot be said to be of a formal or procedural nature, the third party would also not be able to rely on section 20(7).[590]

I submit that the third party would also not be able to hold the company liable on grounds of estoppel under these circumstances.

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583 See para 3.3.2 below for a discussion on "RF" companies.

584 Van Dorsten *Company Directors* 157.

585 Similar to the *Turquand* rule, s 20(7) only operates to make good failure to comply with formal or procedural requirements laid down by the Memorandum of Incorporation, rules or the Act. For a discussion on s 20(7), see para 3.3.4 below.

586 In terms of the doctrine of constructive notice, in the case where the third party deals with an "RF" company.

587 See para 2.2.2 of Ch 2 above and para 3.2.2 of this chapter above.

588 See para 3.3.4 below.

589 See para 3.3.4.5 below.

590 See para 3.3.4.5 below.

3.3.1.4 Prescribed minimum number of directors

Section 66(2) prescribes a minimum number of directors to be in office in respect of different types of companies. Section 66(3) further provides that the Memorandum of Incorporation may specify a higher minimum number of directors. Any failure by a company at any time to have the prescribed minimum number of directors does not, however, limit or negate the authority of the board or invalidate anything done by the board of the company.[591]

### *3.3.2 Abolition of the doctrine of constructive notice and "RF" companies*

Section 19(4) of the Companies Act of 2008 provides that a person must not be regarded as having received notice or knowledge of the contents of a company document just because it has been filed or is accessible for inspection at the company's office. This provision is, however, subject to the provisions of section 19(5).

Section 19(4) of the Companies Act of 2008 expressly abolishes the doctrine of constructive notice.[592] A company can no longer deny liability on grounds of a contract entered into with a third party by reason of the fact that the entering into of the contract is in excess of a limitation on the authority of the representative, which the third party is presumed to know about.

In today's world, contracts are concluded electronically and on a global scale which would place a very onerous task on a third contracting party dealing with a company, requiring the third party to inspect documents filed at that company's office or at the companies office where such documents are to be filed in terms of the particular Act applicable to that company, as that third party might not even be in the same country as the company. Adherence to such inspection would be very time consuming and a delay in the conclusion of a contract might even lead to the forfeiture of that contract for the third party. Furthermore, in practice, inspections are not often carried out: "In the ordinary course of commercial dealings they

591 S 66(11).
592 Delport and Vorster *Henochsberg 2008* 92.

[inspections] simply are not feasible".[593] The abolition of the doctrine of constructive notice is commendable as it provides third contracting parties with greater security in dealing with companies.

The fact that a person must not be regarded as having notice or knowledge of the contents of a company's public documents will, however, not apply where the third party had actual knowledge of the content of the company's Memorandum of Incorporation.[594] It would also not be the case where the limitation can be regarded as a restrictive condition to which attention has been drawn in the Notice of Incorporation or further Notice of Amendment of an "RF" company.[595]

Section 15(2) of the Companies Act of 2008 provides *inter alia* that the Memorandum of Incorporation of any company may contain any restrictive conditions applicable to the company, and any requirement for the amendment of any such condition in addition to the requirements set out in section 16. Section 19(5) of the Companies Act makes the doctrine of constructive notice applicable to these restrictive conditions by providing that a person must be regarded as having notice and knowledge of any provision of a company's Memorandum of Incorporation contemplated in section 15(2)(b) or (c) if the company's name includes the element "RF" as contemplated in section 11(3)(b),[596] and the company's Notice of Incorporation or a subsequent Notice of Amendment draws attention to the relevant provision, as contemplated in section 13(3).[597]

No definition is provided in the Act for "restrictive conditions" as contemplated in section 15(2)(b) and there exists uncertainty about the kind of conditions which would a constitute restrictive condition.

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593 McLennan 1985 *SALJ* 322 at 324.

594 Delport and Vorster *Henochsberg 2008* 92.

595 S19(5)(a).

596 This section stipulates that if the company's Memorandum of Incorporation includes any provision contemplated in s 15(2)(b) or (c) restricting or prohibiting the amendment of any particular provision of the Memorandum, the name must be immediately followed by the expression "RF".

597 S 13(3) provides that if a company's Memorandum of Incorporation includes any provision contemplated in s 15(2)(b) or (c), the Notice of Incorporation filed by the company must include a prominent statement drawing attention to each such provision, and its location in the Memorandum of Incorporation.

First, uncertainty exists, for example, whether it only pertains to the capacity of the company or to the authority of the directors (and other agents) to act on behalf of the company or to both.[598] It is submitted that it pertains to both.[599]

Secondly, it is uncertain whether it is only required that the condition itself should be restrictive, or whether it should also be coupled with a requirement regarding its amendment which is more stringent than the requirements for a usual amendment of the Memorandum of Incorporation.[600] Some writers[601] do not find the former proposition problematic while other writers[602] view the distinguishing feature of a section 15(2)(b) restrictive condition that it is coupled with a requirement for its amendment that is more onerous than the usual amendment requirements. The latter view is to be preferred.[603]

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598 In this regard, see Katz 2010 *Acta Juridica* 248 at 250-253; Descroizilles March 2010 *De Rebus* 39 at 44; Stein and Everingham *Companies Act* 72; McLennan 2009 *Obiter* 144 at 150-151; Van der Linde 2015 *TSAR* 833 at 837; Locke 2016 *SALJ* 160 at 182, 185-188.

599 It would not make much sense for the legislature to enact s 15(2)(b) and (c) and make the doctrine of constructive notice applicable to it, if it has so little effect if it is assumed that these restrictive conditions only pertain to limitations on the capacity of the company. Where a company transgresses a limitation, restriction or qualification of its purposes, powers or activities as contemplated in s 19(1)(b)(ii), s 20(1) counters the consequences thereof in relation to a third party by providing that such an act will not be void due to the transgression (although internal consequences will still flow from such transgression). If restrictive conditions pertain to the capacity of the company, s 20(1) makes the provision for restrictive conditions pertaining to the capacity, to which the doctrine of constructive notice applies, pointless. *Bona fides* is not a requirement for the application of s 20(1). In the event that the third contracting party knew that the capacity has been exceeded or where he had constructive knowledge thereof (due to the operation of s 19(5)), the act would still be valid.

600 S 16 generally requires a special resolution by the shareholders to amend the Memorandum of Incorporation.

601 Delport and Vorster *Henochsberg 2008* 72:

> Paragraph (2)(b) of this section therefore enables a company to include in its Memorandum of Incorporation any restrictive conditions. It may also include requirements for the alteration of any such conditions in addition to those prescribed by s 16.

Cassim *et al Contemporary Company Law* 131. Also see the non-binding opinion dated 12 December 2011 and issued in terms of s 188(2)(b) of the Companies Act of 2008 titled *Interpretation of section 11(3)(b) read with section 65(12) and 15(2)(a)(iii) of the Companies Act, 2008 in relation to the use of "(RF)" in the name of a company.*

602 Van der Linde 2015 *TSAR* 833 at 837; Locke 2016 *SALJ* 160 at 167.

603 When reading s 15(2)(b) it would seem that what is meant is not only that the conditions should be restrictive *but also* that the condition should contain additional amendment requirements. This is supported by the wording of s 11(3)(b) which refers to the instance where the company's Memorandum includes any provision contemplated in s 15(2)(b) or (c) *restricting* or prohibiting the amendment of any provision of the Memorandum. It would seem that the emphasis here pertains to restrictions on the amendment of provisions and not to the restrictive conditions itself.It would have been easy for the legislature to follow the wording of s 53(a) of the Companies Act of 1973 if it intended for the restrictive condition to stand on its own, as it is very clearly stipulated in that section. The legislature, however, did not do so.

It is important to know what "restrictive conditions" entail as a company must draw attention to these conditions in its Notice of Incorporation or subsequent Notice of Amendment and it must add the suffix "RF" to the name of the company.[604] If these two requirements have been complied with, the doctrine of constructive notice shall operate in respect of these conditions as provided for by section 19(5) of the Companies Act of 2008.

The abolition of the doctrine of constructive notice has been advocated by many writers.[605] This doctrine has been abolished in other jurisdictions.[606] Furthermore, the original reason for the creation of this doctrine, that directors were regarded as having the same powers as partners in a partnership, has fallen away.[607] The doctrine may also be regarded as unconstitutional.[608] If this is taken into account, together with the the fact that it will not always be practical or economical to inspect the public documents of an "RF" company and the uncertainties regarding what types of conditions would qualify as restrictive conditions pertaining to "RF" companies (which may open the door for companies to abuse its use), it is recommended that the doctrine of constructive notice should be abolished *in toto*.

### *3.3.3 Common-law Turquand rule and Companies Act of 2008*

With the abolition of the doctrine of constructive notice,[609] except in the cases of an "RF" company and personal liability company, the question arises whether there is still a need for the *Turquand* rule.

It is obvious that the *Turquand* rule will still operate in respect of "RF" companies,[610] as the doctrine of constructive notice has been retained in that

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604 Delport and Vorster *Henochsberg 2008* 73.

605 Du Plessis 1997 *SA Merc LJ* 281 at 284; Grobler *Toegerekende kennis* 41-46; McLennan 1986 *SALJ* 558 at 560; Oosthuizen 1979 *TSAR* 1 at 14; Rabie *Verteenwoordiging* 108.

606 See in this regard the discussion of s 40 of the Companies Act of 2006 of England in para 2.3 of Ch 2 above. The doctrine has also been abolished in Australia by section 165 of the Corporations Law of 1989 which was perpetuated in section 130 of the Corporations Act of 2001 The doctrine was never adopted in the USA (Rabie *Verteenwoordiging* 105).

607 Oosthuizen 1979 *TSAR* 1 at 5.

608 See the discussion in Rabie *Verteenwoordiging* 99-105.

609 S 19(4) of the 2008 Companies Act.

610 Katz 2010 *Acta Juridica* 248 at 252 to 253; Delport 2011 *THRHR* 132 at 138.

respect.[611] It has been concluded above[612] that the restrictive conditions as contained in section 15(2)(b) include not only restrictions on the capacity of the company but also on the authority of directors and other representatives. The *Turquand* rule only applies in situations where the authority of the directors is defective and not where the company acts *ultra vires* its capacity.

The *Turquand* rule would also still operate in the instance where the third party did have actual knowledge of the content of the Memorandum of Incorporation (or the rules of the company) where restrictions are placed on the authority of the board of directors and other representatives of the company, and which relate to internal requirements upon which the authority of the representative is dependent.[613]

Where the Companies Act of 2008 itself imposes approval by the shareholders in addition to a resolution by the board of directors in, for example, sections 41, 44, 45 and 112, the only consideration is not whether the internal requirements relating to the board of directors' resolution have been complied with, but also the intention of the legislature in requiring approval by the shareholders.[614] Initially there was uncertainty as to whether the *Turquand* rule may be relied upon under these circumstances.[615] The Supreme Court of Appeal removed this uncertainty in 2011 when ruling that the *Turquand* rule does not apply.[616]

If a contracting third party does not have any knowledge of the public documents of the company and no knowledge of the public documents is attributed to the third

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611 Katz 2010 *Acta Juridica* 248 at 253.

612 Par 3.3.2 above.

613 Delport 2011 *THRHR* 132 at 138.

614 The purpose of shareholder authorisation is to protect the shareholders who have given general control of the company to its directors. The application of the *Turquand* rule would deprive the shareholders of such protection in which event the section of the Act requiring shareholder approval would serve no purpose. See *Stand 242 Hendrik Potgieter Road Ruimsig (Pty) Ltd v Göbel* [2011] 3 All SA 549 (SCA).

615 *Levy v Zalrut Investments (Pty) Ltd* 1986 4 SA 479 (W) 485; *Farren v Sun Service SA Photo Trip Management (Pty) Ltd* 2004 2 SA 146 (C) 156.

616 *Stand 242 Hendrik Potgieter Road Ruimsig (Pty) Ltd v Göbel* [2011] 3 All SA 549 (SCA). The court, at 555, also found that estoppel could not operate to allow a contravention of a statute.

party (because of the doctrine of constructive notice) it would appear as though the need for the *Turquand* rule vanishes. This is, however, not the case.[617]

First, from a thorough analysis of the *Turquand* rule it is apparent that the rule is not necessarily tied to the doctrine of constructive notice. The rule is not only available where the third party is prejudiced due to the attribution of knowledge regarding the internal limitations on authority stipulated in the Memorandum of Incorporation. It also serves to clear other irregularities that do not relate to the doctrine of constructive notice, for example, a defective appointment of directors, defective notice of meetings or the absence of the required quorum.[618] Under these circumstances, the third party's position is usually[619] not prejudiced by the doctrine of constructive notice. The third party indeed knows that directors must be duly appointed and that meetings should be preceded by due notice and, above all, that no publicity is given to these irregularities. The third party's need for protection does therefore not emanate from the operation of the doctrine of constructive notice. He is, however, not deprived of the protection of the *Turquand* rule.

If it is accepted that the *Turquand* rule can also exist in respect of irregularities of this nature apart from the doctrine of constructive notice, the same should apply in situations where internal limitations on authority have been laid down. It is true that the third party would be able to rely on estoppel, but that should not exclude the availability of the *Turquand* rule, especially as the *Turquand* rule may be more advantageous to the third party, as he needs prove fewer requirements in such a case.[620]

Secondly, the averment that, in the absence of the doctrine of constructive notice, the third party can rely on implied or ostensible authority oversimplifies the matter. There can be no question of implied authority where the company restricted the authority of the representative by means of an internal arrangement. If the third

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617 Oosthuizen 1977 *TSAR* 210 at 215-216 gives three reasons for the need for the *Turquand rule* in the absence of the doctrine of constructive notice, as set out above.

618 Oosthuizen 1977 *TSAR* 210 at 215.

619 Except perhaps in exceptional instances where the articles stipulate extraordinary requirements.

620 *Farren v Sun Service SA Photo Trip Management (Pty) Ltd* 2004 (2) SA 146 (C) 157.

party knows of the internal requirement that has been laid down, it would be almost impossible to prove estoppel on the side of the company. Not only will he have to prove that the company has made a representation that a particular person is clothed with the necessary authority, but also that a representation has been made that the required internal requirements have indeed been complied with. As the third party does not have access to the internal administration and management of the company, it is clear that it would be impossible for him to ascertain the true state of affairs. Under these circumstances[621] there is still a need for the protection of the *Turquand* rule.[622] If the third party is not permitted to rely on the *Turquand* rule, he will have no choice but to refrain from any negotiations.

Thirdly, the conclusion that the need for the *Turquand* rule will lapse in the absence of the doctrine of constructive notice, will have unacceptable consequences. Over and above the objections listed above, it would mean that the abolition of the doctrine of constructive notice will lead to the abolition of the *Turquand* rule from company law. To deprive a third party from the protection of the rule even where he has no access to the internal management of the company, is not acceptable.[623] The rule would indeed provide optimal protection under circumstances where the third party is not restricted by the doctrine of constructive notice.[624] The doctrine of constructive notice has an unnecessary restricting effect on the fair operation of the *Turquand* rule.[625] Third parties may only make use of the *Turquand* rule if the acts of the company representatives are in line with the public documents.[626] If that is not the case, the doctrine of constructive notice deprives the third party of the protection which he would otherwise have had.

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621 In other words where the third party knows that internal requirements have been set down.

622 Naudé 1972 *Codicillus* 62 at 63.

623 Oosthuizen *Turquand-reël* 331. Compare, however, *Potchefstroom se Stadsraad v Kotze* [1960] 3 All SA 402 (A).

624 Oosthuizen *Turquand-reël* 331.

625 Oosthuizen *Turquand-reël* 147.

626 *In re The Athenaeum Life Assurance Society; Ex Parte The Eagle Insurance Company* 70 ER 229 at 234. This will be the position even if the company clearly represented that the relevant company representative had the necessary authority. See Naudé 1971 *SALJ* 505 at 505-506.

According to Oosthuizen[627] the need for the *Turquand* rule is based on the fact that negotiations take place with a company where the members do not have individual authority to represent the company. The company therefore must participate through one or other management organ. The third party's need for protection stems from this and from the fact that third parties do not have access to the internal management of such entities.

Rabie[628] is also of the opinion that the *Turquand* rule can find application in the absence of the doctrine of constructive notice. In Australia, where the doctrine of constructive notice has also been abolished,[629] section 164 of the Corporations Law[630] made provision for a statutory *Turquand* rule.[631] This section has been taken over by section 129 of the Corporations Act of 2001.[632] A need for something akin to the *Turquand* rule has also been experienced in the USA where the doctrine of constructive notice has never found any application.[633]

Cassim *et al*[634] state that the *Turquand* rule, in its development, came to serve functions additional to the original function of mitigating the effect of the doctrine of constructive notice. If this were not the case, the *Turquand* rule would have been abandoned together with the doctrine of constructive notice.

From this, it is clear that although the doctrine of constructive notice has been abolished, there is still room for the application of the *Turquand* rule to enable a third party to hold a company to a contract. Otherwise it would impede business dealings with companies, as the risk to the third contracting party of being unable to hold a company bound under circumstances where he has no way of knowing of a defect relating to the internal management of the company, would be too great.

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627 Oosthuizen 1977 *TSAR* 210 at 217.

628 Rabie *Verteenwoordiging* 178 and 244.

629 Rabie *Verteenwoordiging* 187:

> Die leerstuk van toegerekende kennis is in die Australiese reg afgeskaf as gevolg van die negatiewe uitwerking wat hierdie leerstuk op die 'indoor management rule' gehad het.

630 1989.

631 Morrison 1996 *QUTLJ* 28 at 28.

632 Rabie *Verteenwoordiging* 185.

633 Rabie *Verteenwoordiging* 244.

634 Cassim *et al Contemporary Company Law* 181.

### *3.3.4 Statutory regulation of non-compliance with formal and procedural requirements*

The heading of section 20 (of which section 20(7) forms a subsection), refers to the "[v]alidity of company actions". As section 20(7) does not pertain to the validity of company actions but to the authority of representatives to act on behalf of the company, this subsection should not have been inserted under this heading. It appears that the legislature failed to distinguish between these two vitally different concepts throughout section 20 which leads to confusion in the interpretation of the subsections in section 20.[635]

At first glance, it seems as though section 20(7) of the 2008 Companies Act is the statutory counterpart of the common-law *Turquand rule*.[636] On a more careful reading, however, it transpires that what appears to be a codified common-law *Turquand* rule is not that at all, for two reasons: First section 20(8) provides that section 20(7) should be construed concurrently with and not in substitution for any relevant common-law principle relating to the presumed validity of the actions of a company in the exercise of its powers. Secondly, on close examination there are differences between section 20(7) and the common-law *Turquand* rule.[637]

Section 20(7) provides as follows:

> A person dealing with a company in good faith, other than a director, prescribed officer or shareholder of the company, is entitled to presume that the company, in making any decision in the exercise of its powers, has complied with all of the formal and procedural requirements in terms of this Act, its Memorandum of Incorporation and any rules of the company unless, in the circumstances, the person knew or reasonably ought to have known of any failure by the company to comply with any such requirement.

635 Also see Van der Linde 2015 *TSAR* 833 at 834.

636 Delport and Vorster *Henochsberg 2008* 106(3). Also see Cassim *et al Contemporary Company Law* 184; Van der Linde 2015 *TSAR* 833 at 841; Jooste 2013 *SALJ* 464 at 469; McLennan 2009 *Obiter* 144 at 152.

637 Locke 2016 *SALJ* 160 at 170.

Both these rules prohibit a company from relying on the non-compliance of certain requirements to evade liability and only *bona fide* third parties who have no knowledge of non-compliance are protected by these rules.[638]

3.3.4.1 Insiders v outsiders

Section 20(7) excludes directors, prescribed officers and shareholders from the benefit of this section.[639] There are differences of opinion in respect of the application of the common-law *Turquand* rule where the third party is an insider.[640]

These differences of opinion regarding the common-law *Turquand* rule, is not a problem in the application of section 20(7), as directors (and prescribed officers) are regarded as insiders, who cannot invoke the protection of section 20(7). In this sense the operation of section 20(7) is more restrictive than the common-law *Turquand* rule in its availability to these categories of persons.[641]

In terms of regulation 38 issued under the 2008 Companies Act, a prescribed officer, although not a director, exercises general executive control over and management of the whole, or a significant part of the business and activities of the company. From these prescribed functions can be determined that a prescribed officer should be treated in the same manner as a director.

The position of shareholders is, however, different under the common-law *Turquand* rule and section 20(7). The courts do not seem to have any difficulty granting the protection of the *Turquand* rule to shareholders.[642] Some writers also agree with this approach,[643] at least in respect of resolutions required to be taken at a board meeting.[644]

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638 Van der Linde 2015 *TSAR* 833 at 841.

639 Van der Linde 2015 *TSAR* 833 at 841; Jooste 2013 *SALJ* 464 at 471.

640 In this regard, see para 3.2.2.2 above.

641 Locke 2016 *SALJ* 160 at 171.

642 *George Bargate v Richard Shortridge* (1855) 5 HL Cas 297; *In re Fireproof Doors Ltd (Umney v The Company)* [1916] 2 Ch 142.

643 Delport and Vorster *Henochsberg 2008* 106(3); Oosthuizen *Turquand-reël* 179.

644 Jooste 2013 *SALJ* 464 at 471. The position is, for example different in the instance where the internal requirement that has to be complied with involves the granting of authority by the general meeting of shareholders. In such an instance, the shareholder should have

Baiketlile,[645] in comparing the company legislation of Botswana and South Africa, states that it could not have been the intention of the legislature to exclude insiders from the protection of the *Turquand* rule where they are clearly "outsiders". It would be unfair to exclude shareholders who do not have inside information regarding management decisions of the board of directors from the benefit of section 20(7). I agree that in this sense (especially in relation to board resolutions), section 20(7) cannot be supported.[646]

3.3.4.2 Presumption that requirements have been met

Section 20(7) states that the third contracting party is "entitled to *presume*"[647] that the formal and procedural requirements have been met. According to the common-law *Turquand* rule, the contracting third party is entitled to *assume* compliance with internal requirements. It is unfortunate that the word "presume" has been used in section 20(7) as a presumption can be rebutted.[648] This may imply that when the third party relies on section 20(7), the company can rebut the presumption that all the internal requirements have been complied with, leaving the third party with no remedy.[649] If the intention of the legislature was that this is a presumption that can be rebutted, section 20(7) would not serve any purpose and would be rendered nugatory. As there is a presumption when interpreting statutes that the legislature does not intend to make futile, pointless and ineffectual provisions,[650] I cannot agree with the interpretation of section 20(7) as providing for a rebutable presumption.

Further, the Companies Act of 2008 in the Afrikaans language does not speak about a presumption ("vermoede") but provides that the *bona fide* third party is "geregtig om te veronderstel…", which, when translated into English can mean

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knowledge that the required authority has not been granted and would not under these circumstances be in a position to rely on the *Turquand* rule.

645 Baiketlile *Corporate Capacity* 28-29.

646 Also see Jooste 2013 *SALJ* 464 at 471; Locke 2016 *SALJ* 160 at 171. For a contrary view in respect of shareholders, see Cassim *et al Contemporary Company Law* 185.

647 My emphasis.

648 Delport and Vorster *Henochsberg 2008* 106(3).

649 Jooste 2013 *SALJ* 464 at 473.

650 Du Plessis *Re-Interpretation of Statutes* 189-191.

"suppose; assume; conjecture; believe; imply; presume; hypothesise, (pre)suppose; take for granted; expect;".[651]

The *Turquand* rule has been described as only being an application of the rebuttable presumption *omnia praesumuntur rite esse acta*.[652] As this presumption is rebuttable and a characteristic of the *Turquand* rule is indeed that it would not assist the company to prove that the internal requirements were not complied with, this presumption cannot serve as explanation for the *Turquand* rule.[653] The courts have, when formulating the *Turquand* rule in the past used the word "presume" in stead of, for example, assume.[654] They have, however, not discussed it in the context of a presumption made by the third contracting party being capable of rebuttal by the company. It is therefore submitted that when the courts used the word "presume", they did not use it in the context of a presumption that may be rebutted, but merely meant that a third party could assume, suppose, believe and take for granted that the internal requirements had been observed.

A further presumption in the interpretation of statutes is that unless the contrary is clearly indicated, the intention of the legislature is not to amend the existing law more than is necessary.[655] As section 20(7) would be ineffective if it means a

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651 Du Plessis *et al* Pharos Dictionary.

652 This means that all things are presumed to have been done correctly and solemnly, unless it is proved to the contrary. See Oosthuizen 1979 *TSAR* 1 at 7 where he criticises this opinion and refers to sources where this opinion is supported. Also see Blackman *et al Commentary* ch 4 34; Wunsh 1992 *TSAR* 545 at 546 for authorities who support the view that the basis for the *Turquand* rule is the application of the presumption *omnia praesumuntur rite ac solemniter esse acta*.

653 Oosthuizen 1979 *TSAR* 1 at 7. Also see Blackman *et al Commentary* ch 4 34 who recommend not using the word "presumption" but to simply view the *Turquand* rule as that the third party acting in good faith may assume that all internal formalities have been met.

654 In *Potchefstroom se Stadsraad v Kotze* [1960] 3 All SA 402 (A) 414-415, where Malan AJA words the *Turquand rule*, he uses the word "presume". Also see, for example, *Legg & Co v Premier Tobacco Co* 1926 AD 132 at 144; *Biggerstaff v Rowatt's Wharf, Limited* [1896] 2 Ch 93 (CA) 106 and per Wessels J in *SA Securities Ltd v Nicholas* 1911 TPD 450 at 460.

In *The Mine Workers' Union v Prinsloo* 1948 (3) SA 831 (A) 847 where Greenberg JA discusses the *Turquand* rule he also uses the word "presume". Greenberg JA, however, also uses the words "presumed" and "assume" in the same breath at 849:

> It seems to me that the true position is that the necessary acts of internal management are presumed to have been performed and not that a particular person is entitled to assume that they have.

655 This is subject thereto that such interpretation does not conflict with the Constitution of the Republic of South Africa, 1996 and that statutory rights and remedies more advantageous to those who stand to benefit from them will take precedence over common-law rights and remedies. See Du Plessis *Re-Interpretation of Statutes* 177-181.

rebuttable presumption, and as the Afrikaans translation does not speak of a presumption but of a "veronderstelling", and as the court in discussing the common-law *Turquand* rule (with similarities to section 20(7)) used the word "presumption" but with a meaning akin to assumption (and not a legal presumption), it is submitted that "presume" in the context of section 20(7) does not refer to a rebuttable presumption but should be interpreted to mean "suppose", "assume", "believe" and "take for granted". Where section 20(7) is discussed in *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor* [656] Rogers J used the word "assume" and not "presume".[657]

3.3.4.3 Capacity of the company v authority of the directors

*Henochsberg*[658] suggests that it could be argued that section 20(7) pertains to the capacity of the company rather than the authority of the directors to act on behalf of the company. When reading the part of section 20(7) stating that a third party is entitled to presume that "… the *company*, in making any decision in the *exercise of its power*s …"[659] has complied with all the requirements, it seems, so *Henochberg*[660] contends, as though section 20(7) will only find application where the capacity of the company is concerned. When reference to "powers" is made in the Act, generally it relates to the capacity of the company, for example in section 20(1).[661] What makes this inference even stronger, according to *Henochsberg*, is that section 20(7) is organised under the same section as section 20(1), dealing with the capacity of the company.

As already alluded to above, the organisation of the subsections in section 20 causes confusion regarding whether the section relates to the capacity of the company, or the authority of the directors or to both. It cannot therefore be said that because section 20(7) falls under the heading "[v]alidity of company actions" that it pertains to the capacity of the company. If section 20(7) is intended to deal

656 [2015] 4 All SA 88 (WCC).
657 [2015] 4 All SA 88 (WCC) [55].
658 Delport and Vorster *Henochsberg 2008* 106(4).
659 My emphasis.
660 Delport and Vorster *Henochsberg 2008* 106(4).
661 Also see for example section 76.

with the capacity of the company, it would mean that the principles of section 20(1) would apply in terms whereof knowledge on the part of the third party is irrelevant to hold the company to the contract, while knowledge on the part of the third party is very relevant in the application of section 20(7).[662] When the principles of section 20(1) are applied, those principles would make section 20(7) ineffective and useless, as the company would be bound to the contract irrespective of whether the contracting third party had knowledge of non-compliance with requirements.[663] As it is presumed that the legislature does not intend making useless or purposeless provisions,[664] it could not have been the intention of the legislature that section 20(7) provides relief in the event of the capacity of the company being exceeded.

Van der Linde[665] comments on the possibility that section 20(7) pertains to irregularities relating to the capacity of the company as discussed by *Henochsberg* above. She states that this interpretation does not take into account the other important wording in this respect in the section. The third party is entitled to presume that "… the company, *in making any decision*[666] in the exercise of its powers …" means that the formal and procedural requirements relate to those that are required for a decision (resolution) of the company.[667] Van der Linde[668] further contends that for the decision to be in the exercise of the company's powers, such decision must be *intra vires*. I agree that this wording is capable of such an interpretation. This also holds true of the common-law *Turquand* rule.[669]

3.3.4.4 Meaning and scope of "formal and procedural" requirements

According to Van der Linde, [670] the most important feature of section 20(7), in distinguishing this section from the common-law *Turquand* rule, is the nature of the

662 Delport and Vorster *Henochsberg 2008* 106(4).
663 Delport and Vorster *Henochsberg 2008* 106(4).
664 Du Plessis *Re-Interpretation of Statutes* 189-191.
665 Van der Linde 2015 *TSAR* 833 at 842.
666 My emphasis.
667 Van der Linde 2015 *TSAR* 833 at 842. See, however, the critique in Delport and Vorster *Henochsberg 2008* 106(4).
668 Van der Linde 2015 *TSAR* 833 at 842.
669 Delport and Vorster *Henochsberg 2008* 106(1).
670 Van der Linde 2015 *TSAR* 833 at 841.

requirements that can be presumed to have been complied with. In a recent South African decision, *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)* [671] the court, however, expressed the view that "formal and procedural requirements" as contemplated in section 20(7) should be interpreted consistently with "… the conventional scope of *Turquand*".[672] The court expressed the view that where the prior approval of shareholders is a prerequisite for the authority of the board, such shareholders' approval would amount to a formal or procedural requirement.[673] The court further stated that the restrictions placed on the authority delegated to a managing director should also be regarded as formal or procedural requirements.[674] The judge, however, did not view the granting of authority to an ordinary director as falling within a formal or procedural requirement.[675]

The wording "… that the company, in *making any decision* [676] in the exercise of its power, has complied …" indicates, according to Delport,[677] that there should have been a decision that was actually taken and that it is presumed that that decision was properly taken. It is not presumed that a decision was taken. Van der Linde[678] believes that the choice of wording in section 20(7) ("decision" instead of "resolution" and "making" instead of "adopting") indicates that section 20(7) applies to "technically defective resolutions." She then concludes that where a resolution or decision itself is required for a particular act, the requirement for such a

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671 [2015] 4 All SA 88 (WCC) per Rogers J.

672 *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)* [2015] 4 All SA 88 (WCC) [55]. He therefore followed the approach in the interpretation of statutes that there is a presumption that the legislature does not intend to amend the existing law more than what it clearly indicates. See Du Plessis *Re-Interpretation of Statutes* 177-181.

673 *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)* [2015] 4 All SA 88 (WCC) [55].

674 *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)* [2015] 4 All SA 88 (WCC) [55]. In other words, where the managing director acts within the usual authority of a managing director, he would, the same as under the common-law *Turquand* rule, be able to rely on section 20(7).

675 *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)* [2015] 4 All SA 88 (WCC) [55]. In other words, he applied the common-law restriction to the *Turquand* rule, that it would only find application if the act of the representative can usually be associated with a person in his position in the company and that it is outside the usual authority of a single director to conclude a contract on behalf of a company, to s 20(7). In this regard, see Ch 2 para 2.2.1. Also see the discussion under para 3.3.4.6 below.

676 My emphasis.

677 Delport 2011 *THRHR* 132 at 137.

678 Van der Linde 2015 *TSAR* 833 at 842.

resolution or decision cannot be brought within the meaning of "formal and procedural requirements". Requirements for the adoption of these resolutions, would, however, be regarded as formal and procedural requirements in terms of section 20(7).[679]

I agree with both authors on this aspect. It means that the application of the common-law *Turquand* rule is wider than section 20(7) in this respect. Where the powers of the directors to perform a particular act are made subject to shareholders' approval in the constitution of the company, a third party is entitled to assume that the shareholders' approval was obtained.[680] This appears not to be the case under section 20(7). Only irregularities in the taking of the shareholders' resolution would be covered by section 20(7).

After determining requirements for decisions that may fall under the application of section 20(7), it should further be ascertained whether these requirements have a "formal and procedural" nature.[681] Van der Linde[682] believes a distinction should be drawn between substantive requirements and formal and procedural requirements.

According to Locke[683] "formal and procedural requirements" are not known under the common law. She opinions that "internal formalities" as contemplated in the common-law*Turquand* rule will fall under "formal and procedural requirements" as contemplated in section 20(7),[684] which means that the application of section 20(7) is wider in this regard. Examples of internal irregularities under the common-law *Turquand* rule are defective notice of board meetings[685] and shareholders'

679 Van der Linde 2015 *TSAR* 833 at 842. Requirements set out in the Companies Act would include notification and quorum requirements, requirements relating to the appointment of proxies, the manner of voting and the counting of votes, identification of shareholders, and the requirements for electronic participation in meetings. Many of these requirements may be amended and additional requirements added in the Memorandum of Incorporation. There may even be extra requirements set out in the rules of the company.

680 *The Royal British Bank v Turquand* (1856) 6 E&B 327 at 332; *The Mine Workers' Union v Prinsloo* 1948 3 SA 831 (A).

681 Van der Linde 2015 *TSAR* 833 at 842.

682 Van der Linde 2015 *TSAR* 833 at 842.

683 Locke 2016 *SALJ* 160 at 171.

684 Locke 2016 *SALJ* 160 at 171.

685 *Sugden v Beaconhurst Dairies (Pty) Ltd* 1963 2 SA 174 (E); *Burstein v Yale* 1958 1 SA 768 (W).

meetings,[686] that the required quorum was not present,[687] deficient appointment of officers, absence of a shareholders' resolution prescribed by the constitution of the company authorising the particular act.[688] In this last mentioned internal irregularity, there was, however, no decision that was taken, and it would not fall under section 20(7) in terms of the reasoning above.

3.3.4.5 Formal and procedural requirements in terms of the Companies Act of 2008

Section 20(7) provides for presumed compliance with internal requirements *set out inter alia in the Companies Act of 2008 itself.*[689] In this sense section 20(7) has a wider application than the common-law *Turquand* rule in that requirements laid down in various documents may be presumed to have been met.

Traditionally the common-law *Turquand* rule makes provision only for the assumption of compliance with internal requirements as found in the public documents (articles of association) of the company. The common-law *Turquand* rule does not find application in respect of statutory requirements that have been laid down, at least not regarding the statutory requirements in section 228 of the 1973 Companies Act.[690]

According to Jooste,[691] when looking at the reason for the decision of our courts with regard to the non-applicability of the *Turquand* rule in respect of statutory requirements laid down by section 228 of the 1973 Companies Act,[692] the reason being the protection of the shareholders, the question arises whether this reason

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686 *In re Hampshire Land Company* [1896] 2 Ch 743; *Pacific Coast Coal Mines Ltd v Arbuthnot* [1917] AC 607 (PC).

687 *In re Fireproof Doors Ltd (Umney v The Company)* [1916] 2 Ch 142; *Welgedacht Exploration Co Ltd v Transvaal and Delagoa Bay Investment Co Ltd* 1909 TH 90; *County of Gloucester Bank v Rudry Merthyr Steam & House Coal Colliery Co* [1895] 1 Ch 629 (CA).

688 *The Royal British Bank v Turquand* (1856) 6 E&B 327.

689 My emphasis.

690 A special resolution of the members of the company was required for the disposal of the whole or the greater part of the assets or undertaking of the company. In this regard, see *Farren v Sun Service SA Photo Trip Management (Pty) Ltd* 2004 2 SA 146 (C) and *Stand 242 Hendrik Potgieter Road Ruimsig v Göbel* [2011] 3 All SA 549 (SCA). Also see Jooste 2013 *SALJ* 464 at 470 and Van der Linde 2015 *TSAR* 833 at 841.

691 Jooste 2013 *SALJ* 464 at 470.

692 See *Stand 242 Hendrik Potgieter Road Ruimsig (Pty) Ltd v Göbel* [2011] 3 All SA 549 (SCA).

can be extended to other instances where the 2008 Companies Act requires a special resolution.[693] It seems that the requirement of a special resolution in many of these sections[694] is aimed at the protection of the shareholders, in which event the common-law *Turquand* rule may not find application. If it does find application, it would render the special resolution requirement useless. Seeing that section 20(7) condones lack of compliance with formal and procedural requirements contained in the Act itself, it seems at first glance as though section 20(7) renders the special resolution requirement useless. There is a presumption that the intention of the legislature is not to make ineffective and useless provisions.[695] It must therefore be presumed that the requirement of a special resolution in the Companies Act of 2008 under particular circumstances was not intended to be nullified by the application of section 20(7).

Furthermore, in some of these sections (for example sections 44 and 45) setting down a special resolution as requirement, a transaction in contravention of the section is visited with voidness if there is non-compliance with such requirement.[696] Section 20(7) may, however, be construed that the third party may use section 20(7) to hold the company to such a void act. There is therefore a conflict between the provisions of, for example, sections 44 and 45 and section 20(7) under these circumstances.[697]

Some authors[698] state that a distinction should be drawn between substantive provisions of the Companies Act of 2008 (which would not be covered by section

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693 Jooste 2013 *SALJ* 464 at 470 lists the following sections of the 2008 Companies Act:

> … the issue of shares (s 41); the issue of securities convertible into shares (s 41); the granting of options or other rights exercisable for securities (ss 41 and 42); financial assistance for the subscription for, or purchase of, securities (s 44); loans or other financial assistantce to the 'outsiders' referred to in s 45; 'repurchases' of shares from the 'outsiders' referred to in section 48(8); the disposal of all or the greater part of the assets or undertaking of a company (s 112); and the fundamental transactions referred to in s 115(1).

694 See the sections referred to in the previous footnote.

695 Du Plessis *Re-Interpretation of Statutes* 189-191.

696 To make these sections even more confusing, s 218(1) provides that an agreement or resolution that is void in terms of the Act is not void unless the court declares it void.

697 Jooste 2013 *SALJ* 464 at 470; Van der Linde 2015 *TSAR* 833 at 841.

698 Locke 2016 *SALJ* 160 at 171; Van der Linde 2015 *TSAR* 833 at 842.

20(7))[699] and formal and procedural requirements as contemplated in section 20(7).

According to this view, all acts which require a special resolution from the shareholders would be substantive and non-compliance with those would not entitle a third party to the protection of section 20(7).[700] This answers the concern raised by Jooste[701] above in respect of special resolutions and that the basis of the decision in *Stand 242 Hendrik Potgieter Road Ruimsig (Pty) Ltd v Göbel*,[702] namely the protection of the shareholders, should be extended to all instances where shareholders' approval by means of a special resolution is required by the Companies Act of 2008.[703]

I agree with the contention that the reference to "formal and procedural" requirements denotes that there must at least be an attempted resolution and that no resolution at all, will not be covered by section 20(7).[704] Where a decision is required[705] (irrespective of whether it is a decision of the board of directors or the shareholders), such requirement can never be regarded as a "formal or procedural" requirement as covered by section 20(7).[706] The requirements to which the resolutions are subject should also be tested to ascertain whether they are "formal and procedural" rather than substantive in nature.[707]

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699 Ratification by the company will also not be possible if the act whereby the authority of the directors is exceeded amounts to a contravention of the Companies Act of 2008 itself - s 20(3) of the Companies Act 71 of 2008.

700 Locke 2016 *SALJ* 160 at 171.

701 Jooste 2013 *SALJ* 464 at 470.

702 [2011] 3 All SA 549 (SCA).

703 Locke 2016 *SALJ* 160 at 171-172. S 65(11) lists the instances where a special resolution by the shareholders is required.

704 Van der Linde 2015 *TSAR* 833 at 842.

705 Either in the Act or the Memorandum of Incorporation or the rules. There are several requirements laid down by the Act regarding the taking of resolutions which includes notice of shareholders' meetings (s62), the quorum required at such meetings (s64), the appointment of proxies (s58), resolutions taken other than at a shareholders' meeting (s60), conducting of meetings (s63), board meetings (s73), directors acting other than at a meeting (s74) etc. Many of these requirements may be amended by the Memorandum of Incorporation and further requirements may also be laid down in the Memorandum of Incorporation.

706 Van der Linde 2015 *TSAR* 833 at 842.

707 Van der Linde 2015 *TSAR* 833 at 842.

I therefore agree with Van der Linde[708] that not only the wording "in making any decision" (as discussed above) but also the words "formal and procedural requirements" confirm that to pass a special resolution, even if it is required for the taking of another decision by, for example, the board, in itself cannot be regarded as a formal or procedural requirement. She further unequivocally states that;

> … [s]hareholder approval, whether by special or ordinary resolution or for that matter by unanimous assent cannot be relegated to the status of a formality or procedural step.[709]

Van der Linde[710] and Locke[711] (although their reasoning differs) agree that the taking of a special resolution cannot be seen as a formal or procedural requirement. I agree with them.

Locke,[712] however, goes further and asks what the position would be in the instance where a shareholder resolution was taken but there was non-compliance with the procedure of such meeting, for example the notice period, quorum requirement *etcetera*. From the wording of section 62(6) she avers that an inference can be drawn that where there was a material (rather than an immaterial) defect in the form or manner of giving notice or an intentional (as opposed to an unintentional) failure to give notice, this would affect the validity of the actions taken by the shareholders at that meeting. Although the other sections relating to requirements for the meetings of shareholders do not have a similar provision pertaining to the validity of resolutions upon non-compliance, Locke[713] states that these requirements are worded in a preremptory manner and could therefore also affect the validity of resolutions taken at such meetings. Whether non-compliance with these requirements would affect a contracting third party should, according to her, be considered by looking at the circumstances of each case and she suggests that the materiality of the defect and intentional failure as contemplated in section 62(6) should be taken into account when a court considers the validity of a resolution or to state it in her words, "… whether the

708 Van der Linde 2015 *TSAR* 833 at 842.
709 Van der Linde 2015 *TSAR* 833 at 842-843.
710 Van der Linde 2015 *TSAR* 833 at 842.
711 Locke 2016 *SALJ* 160 at 172.
712 Locke 2016 *SALJ* 160 at 172.
713 Locke 2016 *SALJ* 160 at 172.

meeting could be said to have voiced a valid opinion".[714] She voices the hope that the courts would also consider the extent of the defect and the potential prejudice to a contracting third party where the action of the company is invalid due to non-compliance with formal or procedural requirements. She goes on to state that under certain circumstances the third party would succeed in relying on section 20(7).[715] She further contends that in instances where the Act expressly renders non-compliance with, for example a special resolution, void,[716] non-compliance with an internal formality regarding such special resolution cannot be made good by section 20(7).[717]

Generally speaking, the position in respect of the requirement for an ordinary resolution laid down by the Act should be the same as for the requirement of a special resolution.[718] In other words, the absence of such a resolution cannot be made good by section 20(7). If requirements with a formal or procedural nature were, however, not complied with in the taking of the ordinary resolution, section 20(7) may come to the aid of the contracting third party.[719]

3.3.4.6 Person(s) representing the company: Formal or procedural requirements set out in the company's Memorandum of Incorporation or rules

As the court in *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)*[720] held that the restrictions in the application of the common-law *Turquand* rule in relation to the interpretation of "formal and procedural requirements" should be retained,[721] it viewed the restrictions placed on the authority of a managing director to act on behalf of a

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714 Locke 2016 *SALJ* 160 at 173. If understood correctly, this would mean that there is a valid resolution and section 20(7) would not be needed.

715 Locke 2016 *SALJ* 160 at 173.

716 See ss 44 and 45.

717 Locke 2016 *SALJ* 160 at 175-176.

718 I agree with Locke (2016 *SALJ* 160 at 173) that the purpose of an ordinary resolution is also the protection of shareholders.

719 Van der Linde 2015 *TSAR* 833 at 842-843:

> Shareholder approval, whether by special or ordinary resolution or for that matter by unanimous assent cannot be relegated to the status of a formality or procedural step.

See Locke 2016 *SALJ* 160 at 174-175 for an analysis of all the situations in the Companies Act where an ordinary resolution is required.

720 [2015] 4 All SA 88 (WCC).

721 [2015] 4 All SA 88 (WCC) [55].

company as falling under the concept of formal and procedural requirements, which would have the effect that the third party could rely on the protection afforded by section 20(7). The court, however, did not regard the granting of authority to an ordinary director to fall under "procedural or formal requirements".[722]

Unfortunately, the court, in its judgment, intermingled estoppel and the *Turquand* rule and saw the *Turquand* rule (and section 20(7)) as a sub-component of estoppel.[723] According to this view the contracting third party must firstly establish ostensible authority (if he cannot prove actual authority) to hold the company bound to the contract. Then, the third party, it was held:

> … cannot be non-suited because of non-compliance on the part of the company with some formal or procedural requirement which would have been necessary to make the ostensible agent's authority complete.[724]

I can, with respect, not agree with the above reasoning regarding the conflation of estoppel and section 20(7). I do, however, agree with the view of the court that the common-law principles should still be applied in the interpretation of legislation, unless the legislature specifically provided to the contrary.[725] It is therefore submitted that the application of section 20(7) should also be restricted to those instances where the act that a representative performs on behalf of a company is usually associated with the position that that representative holds in the company. In other words, if a representative acts outside his usual authority a contracting third party should not be able to hold the company to that contract in terms of section 20(7) in the same way that he would not be able to hold the company liable under the common-law *Turquand* rule. If the usual authority of an

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722 [2015] 4 All SA 88 (WCC) [55].

723 The *Turquand* rule is a rule independent of estoppel. See paras 3.2.2 and 3.2.3 above in this regard. It is submitted that section 20(7), as with the common-law *Turquand* rule, should not be seen as a component or appearance form of estoppel, but as functioning on its own.

724 *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)* [2015] 4 All SA 88 (WCC) [56].

725 Unless the contrary appears, it is presumed that the legislature does not want to change the existing law more than is necessary – This is subject thereto that such interpretation does not conflict with the Constitution of the Republic of South Africa, 1996 and that statutory rights and remedies more advantageous to those who stand to benefit from them will take precedence over common-law rights and remedies. See Du Plessis *Re-Interpretation of Statutes* 177-181.

officer is exceeded, that constitutes suspicious circumstances that should place a contracting third party on guard. Under these circumstances the third party cannot be said to be *bona fide*, which is a requirement of section 20(7).[726]

Where the restriction on the authority (for example prior approval of the shareholders [727] for particular acts) of the board or other representative is set out in the Memorandum of Incorporation of the company (rather than in the Companies Act of 2008 itself), it can be agreed with Locke[728] that both section 20(7) and the *Turquand* rule may come to the rescue of the third contracting party. It is, however, submitted that the protection of the common-law *Turquand* rule will stretch further than that of section 20(7). As already discussed above, for section 20(7) to apply, there must at least be an attempt at the taking of a resolution (in other words, for example, a shareholders' resolution, which was the prerequisite, must exist although it may be defective due to non-compliance of some or other procedural requirement), whereas the common-law *Turquand* rule can also make good the total absence of such shareholders' resolution.[729]

Only internal requirements set out in the Act, the company's Memorandum of Incorporation and the company's rules may be presumed to be regular under section 20(7). Section 20(7) does not provide for internal requirements that may be contained in an agreement between the shareholders and the company and the directors[730] or a resolution by shareholders restricting the authority of the directors.[731]

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726 This is also the view of Locke 2016 *SALJ* 160 at 177. She voices the hope at 178 that section 20(7) would be interpreted by the court bearing in mind the boundaries within which the *Turquand* rule finds application.

727 Irrespective of whether a special or ordinary resolution is required.

728 Locke 2016 *SALJ* 160 at 178:

> Since these requirements are contained only in the MOI and not in the Act, third parties cannot be deemed to be aware of them. But even if third parties become aware of these requirements, they will not be able to ascertain from the public documents alone whether these requirements have been met. This is the typical scenario where the common-law *Turquand* rule intervened to promote efficient business, and it must arguably be the intention that s 20(7) would apply, too.

729 See for example *The Royal British Bank v Turquand* (1856) 6 E&B 327.

730 Such an agreement does not fall under the definition of a shareholders' agreement as contemplated in section 15(7) of the Act.

731 Delport 2011 *THRHR* 132 at 137.

3.3.4.7 Good faith and knowledge of third contracting party

Reliance on the common-law *Turquand* rule is excluded if the third party knows of the irregularity or where the circumstances are suspicious and the third party has therefore been placed on his guard and in cases of fraud.[732] The *bona fides* of the third party is excluded under these circumstances [733] and the *Turquand* rule is only available to a *bona fide* third party.

Section 20(7) will not be available if the third party did not act in good faith and knew or reasonably ought to have known of any failure to comply with a procedural requirement.

Some authors[734] are of the view that "reasonably ought to have known" stretches much wider than the exclusion relating to knowledge under the common-law *Turquand* rule. According to this view the common-law *Turquand* rule will not be available to a third party who knew or *suspected* that an internal formality or procedure had not been observed, resulting in a subjective test. Against this, section 20(7) requires an objective test by denying a third party who *reasonably ought* to have known of non-compliance with a formality, its protection.[735] As the test is objective, as opposed to a subjective test used in applying the common-law *Turquand* rule, section 20(7) is narrower than the common-law rule in this regard.

Although I agree with these authors that an objective test is to be used in determining whether the third contracting party reasonably ought to have known of the non-compliance with an internal requirement as contemplated in section 20(7), I do not agree that the inquiry requirement is purely subjective under the common-law *Turquand* rule. Although the *bona fides* of a third party would be excluded if he subjectively suspected that there was an internal irregularity, suspicious circumstances that are objectively present would also deprive a third party from

732 Morse *et al Palmer's Company Law* 3053.
733 Oosthuizen *Turquand-reël* 256 and 264.
734 Jooste 2013 *SALJ* 464 at 472; Cassim *et al Contemporary Company Law* 185.
735 Cassim *et al Contemporary Company Law* 185-186. This view is also shared by Jooste 2013 *SALJ* 464 at 472; Delport 2011 *THRHR* 132 at 137 and Locke 2016 *SALJ* 160 at 180.

relying on the common-law *Turquand* rule.[736] Some of these authors[737] use the words "suspects" and "suspected". There is a difference between when a third party suspects an irregularity and where there are suspicious circumstances when it could have been expected from the third party to investigate further. It is submitted that the suspicious circumstances and therefore due inquiry exclusion was already a subjective but also an objective test. The question is not whether the third party found the particular circumstances suspicious subjectively, but whether there were reasonable grounds for suspecting that the representative of the company did not have the necessary authority to act on behalf of the company. The due inquiry exception has been linked with the requirement of a reasonable man, in other words, where the circumstances were such as to put a reasonable man on inquiry, which indicates an objective test.[738]

Locke[739] submits that when a third contracting party deals with an "RF" company whose constitution contains restrictive conditions, such third party should not be entitled to the protection afforded by section 20(7) if he did not investigate whether these restrictive conditions have been complied with. Such third party, so Locke[740] contends, cannot be said to have acted in good faith. As the doctrine of constructive notice applies to these restrictive conditions, so her argument goes, third parties dealing with such a company is deemed to have knowledge of these restrictive conditions which is bolstered by the suffix "RF" that is added to the name of such companies and which should put a third contracting party who deals with an "RF" company on inquiry.[741] According to Locke[742] this would mean that a third contracting party

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736 Oosthuizen *Turquand-reël* 272. The judgment in *AL Underwood Limited v Bank of Liverpool and Martins* [1924] 1 KB 775 indicates such an objective approach. Also see *Big Dutchman (South Africa) (Pty) Ltd v Barclays National Bank Ltd* 1979 3 SA 267 (W) 284.

737 Cassim *et al Contemporary Company Law* 185-186; Locke 2016 *SALJ* 160 at 180.

738 See for example Delport 2011 *THRHR* 132 at 135; McLennan 1979 *SALJ* 329 at 345; Rabie *Verteenwoordiging* 173; Kunst *et al Henochsberg 1973* 131; Millet *et al Gore-Browne on Companies* at 8-13; Pennington *Pennington's Company Law* 149-150; Griffin *Company Law* 123.

739 Locke 2016 *SALJ* 160 at 180.

740 Locke 2016 *SALJ* 160 at 180.

741 Locke 2016 *SALJ* 160 at 180.

742 Locke 2016 *SALJ* 160 at 180.

> … would reasonably be expected to gain actual knowledge of the content of the relevant clauses [restrictive conditions][743] in the MOI *as well as of compliance with those clauses* …

before they would be able to rely on the protection of section 20(7).

This argument can, with respect, only partly be supported. I agree that if the condition requires, for example, shareholders' approval, the third party should enquire whether such resolution was taken. That the resolution was taken, cannot be presumed.[744] If, however, compliance with formal or procedural requirements in the taking of the shareholders' resolution are lacking, the third party should still be able to make use of section 20(7).

If a third party is compelled to obtain actual knowledge of compliance with procedural and formal requirements pertaining to a restrictive condition of an "RF" company, section 20(7) can never be used when the third party contracts with an "RF" company. If the third party did not obtain actual knowledge of compliance with the restrictive condition (for example shareholder approval or debenture holders' approval), so Locke avers, he will not be able to rely on section 20(7), as there were suspicious circumstances (the "RF" added to the end of the name of the company). If the third party did obtain actual knowledge of compliance with the restrictive conditions (shareholder approval or consent of debenture holders) section 20(7) would be redundant, but Locke argues that the third party would then be entitled to rely on section 20(7). The reason why Locke[745] comes to this conclusion is because the suspicious circumstances would defeat the good faith of the third party.

As the common-law *Turquand* rule is also only available to *bona fide* third parties where there are no suspicious cicumstances that put the third party on inquiry, then the common-law *Turquand* rule should, by analogy to Locke's reasoning similarly not be able to come to the rescue of a contracting third party dealing with an "RF" company.

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743 See in this regard the definition of "knowing", "knowlingly" and "knows" in section 1 of the Companies Act of 2008.

744 See in this regard para 3.3.4.4 above.

745 Locke 2016 *SALJ* 160 at 180.

There is a presumption that unless the contrary is indicated the legislature does not intend to amend existing law more than is necessary.[746] Therefore the common law regarding the *Turquand* rule and the reasoning of its function and creation should still be relevant when interpreting section 20(7). The common-law *Turquand* rule was developed by the courts for the very reason that a third party is not compelled to investigate compliance with the internal management of a company, simply because it is not practically possible to do so.

If one follows Locke's reasoning, it would mean that under all circumstances, when a contracting third party deals with an "RF" company, it would constitute suspicious circumstances which would negate the good faith of such contracting third party. If that were the case, the legislature could easily have made express provision therefor. Furthermore, if that were the case, a third party could never safely contract with an "RF" company, as he would be expected to investigate whether the formal and procedural requirements, to which he has no access and to which he also does not have a right to access, have been met. To expect this from a third contracting party would make business dealings with "RF" companies impossible.[747] This would also inhibit the dealings by "RF" companies as no contracting third parties would want to risk doing business with them.

It is submitted that the default position is that the doctrine of constructive notice does not apply to the public documents of a company that is filed at the CIPC or is accessible for inspection at the office of a company.[748] The legislature is aware that the abolition of the doctrine of constructive notice has been advocated by many writers and that it has indeed been abolished in many jurisdictions including by the legislature itself in the Companies Act of 2008. In certain limited instances, however, the legislature decided to retain this doctrine, but to counter its severe effects and thereby bringing a better balance between the company and the third

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746 This is subject thereto that such interpretation does not conflict with the Constitution of the Republic of South Africa, 1996 and that statutory rights and remedies more advantageous to those who stand to benefit from them will take precedence over common-law rights and remedies. See Du Plessis *Re-Interpretation of Statutes* 177-181.

747 See for example *Legg & Co v Premier Tobacco Co* 1926 AD 132 per Solomon JA at 143-144:

> And, indeed, unless some such principle were accepted, no one would be safe in dealing with joint stock companies.

748 S 19(4) of the Companies Act of 2008.

contracting party. The legislature therefore provided that third parties should be alerted when this default position changes and consequently does not apply, in other words when the doctrine of constructive notice does apply to provisions in the Memorandum of Incorporation. This approach was also suggested by Benade.[749] It is therefore submitted that this is the function of the requirements that the name of the company should end with "RF" and that the notice of incorporation should draw attention to restrictive conditions contained in the Memorandum of Incorporation as contemplated in section 15(2)(b) or (c) contained in the Memorandum of Incorporation. [750] I agree that the requirement of good faith in section 20(7), would be excluded if there are suspicious circumstances that would objectively place the contracting third party on his guard or on inquiry regarding the compliance with formal or procedural requirements in the taking of, example, a shareholders' or debenture holders' resolution where such resolution is required in the restrictive condition. The "RF" suffixed to the name of a company, however, cannot constitute that suspicious circumstance.

Suspicious circumstances relate to something out of the ordinary that indicates that the formal or procedural requirement has not been complied with, for example, a representative of the company that acts outside the usual authority of a person in his position at the company or where he performs an extraordinary act. In other words, it refers to suspicious circumstances that the formal or procedural requirement has not been complied with. I cannot see how "RF" alone can make a person suspicious about the fact that a formal or procedural requirement has not been observed.

#### 3.3.4.8 Consequences of presumed compliance with formal and procedural requirements

Under the common-law *Turquand* rule, the company will be bound to a contract if the director did not have authority to represent the company in the conclusion of that particular contract due to non-compliance with an internal requirement. Section 20(7) does, however, not spell out the consequences of the presumed

749 Benade *Ultra Vires* 45.
750 Ss 11(3)(b), 13(3) and 19(5) of the Companies Act of 2008.

compliance with formalities and procedures in relation to the *bona fide* third party. A company's invalid decision or conduct does not suddenly become valid just because one person may presume that it is valid.[751]

3.3.4.9 Section 20(8)

Section 20(8) provides that section 20(7) should be construed concurrently with and not in substitution of any relevant common-law principle relating to the presumed validity of the actions of a company in the exercise of its powers.

Section 20(8) retains "relevant" common-law principles, which would aparrently include the common-law *Turquand* rule.[752] It would therefore seem that a third party would have a choice of alternatives, as it is stated that the common-law principles apply concurrently with (along with[753]) section 20(7).[754]

I agree with Jooste[755] that section 20(8) does not refer to the common-law principle of estoppel. Section 20(8) refers to a "common law principle relating to the presumed validity of the actions of a company in the exercise of its powers". The effect of raising an estoppel is that the company is prevented from raising the defence of invalidity of the contract. It does not operate to presume that the contract is indeed valid.[756]

According to Cassim *et al*,[757] the overlap between the common-law *Turquand* rule and section 20(7) could present difficulties in practice. In certain respects, section 20(7) can be applied more widely than the common-law *Turquand* rule and *vice versa* (see in this regard the comparison between the two above). Delport[758] is

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751 Delport 2011 *THRHR* 132 at 137.
752 Cassim *et al Contemporary Company Law* 185.
753 Jooste 2013 *SALJ* 464 at 469.
754 Delport 2011 *THRHR* 132 at 138. Also see Jooste 2013 *SALJ* 464 at 469 where he also states:

> It does not appear to be a case of the common law continuing to apply but subject to s 20(7), or vice versa – the wording does not appear to permit such a meaning.

755 Jooste 2013 *SALJ* 464 at 474.
756 Jooste 2013 *SALJ* 464 at 474.
757 Cassim *et al Contemporary Company Law* 185.
758 Delport 2011 *THRHR* 132 at 138.

also of the view that this overlap can lead to “legal arbitrage”. *Henochsberg*[759] is of the opinion that it would be an extremely challenging task to develop the common-law *Turquand* rule in line with section 20(7) and that the different circumstances under which either one of the two may be relied upon, are unclear.

## 3.4 Conclusion

### *3.4.1 Introduction*

In terms of section 66(1) of the Companies Act of 2008 the board of directors has original authority to bind the company,[760] except to the extent that its powers are limited by the Act itself or the Memorandum of Incorporation of the company.[761]

Where the board has acted (by acting itself or by delegating authority to an agent) in contravention of a total restriction on its powers set out in the Memorandum of Incorporation, the third party may still be able to hold the company bound if he can prove all the essential elements of estoppel. Because the doctrine of constructive notice has been abolished, save for a limited number of instances,[762] the third party cannot be deemed to have had knowledge of this restriction, which would have prevented him from relying on estoppel.[763] Where the power of the board has been made subject to compliance with some or other internal formality, the third party would still be able to hold the company to the contract if he can bring the transaction within the scope of application of either the *Turquand* rule or section 20(7) of the Companies Act of 2006.

The board also has the power to delegate one or more of its powers to a board committee, managing director, director or other agent.[764] Where such an agent acts on behalf of a company, the question whether the company may be bound

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759 Delport and Vorster *Henochsberg 2008* 106(5).
760 See para 3.3.1.1 above.
761 See para 3.3.1.3 above.
762 See par 3.3.2 above.
763 Only actual knowledge of the restriction can now disqualify the third party from relying on estoppel.
764 Section 66(1) of the Companies Act of 2008.

must still be answered by applying the common-law principles of agency.[765] If the agent has express or implied actual authority to act on behalf of the company, the company will be bound. Although express authority usually does not present any problem, it is not always easy to determine whether an agent was clothed with implied authority. The courts have in the past confused implied authority with estoppel, which impacts on the requirements necessary to be proved by the third party to hold the company bound.[766] A clear distinction should therefore always be made between implied authority, which constitutes actual authority, and estoppel, which is no authority at all.[767]

If the company cannot be held bound on grounds of actual authority (express or implied) of its agent, the third party may still be able to enforce the contract against the company on the grounds of the common-law *Turquand* rule, section 20(7) of the Companies Act, or estoppel. In relying on any of these grounds, the third party will, except if he dealt with an "RF" company, not be deemed to have knowledge of any restriction on the powers of the board, the powers of the board to delegate, or on the powers of the particular agent contained in the Memorandum of Incorporation on the powers of the board, the powers of the board to delegate or on the powers of the particular agent.

### *3.4.2 Problem areas*

The law of representation in company law in South Africa is in a totally unsatisfactory state, from the common law through to the Companies Act of 2008.

First, at common law, the courts confused implied authority with estoppel.[768] Not only the courts in England confused these two concepts, but also those in South

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765 See par 3.3.1.2 above.

766 See for example *Wolpert v Uitzigt Properties (Pty) Ltd and others* 1961 (2) SA 257 (W) 266E; *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 (2) SA 11 (T) 14; *Zelpy 1780 (Proprietary) Limited v Mudaly* 2015 JDR 0187 (KZP) [47]

767 See par 3.2.1 above.

768 See Ch 2 para 2.2.1 and this chapter para 3.2.1.

Africa.[769] Implied authority constitutes actual authority whereas estoppel is no authority at all. There cannot be authority present and absent at the same time.[770]

Secondly, an unsatisfactory state exists in respect of the persons who are entitled to rely on the *Turquand* rule.[771] There are conflicting decisions by the English courts about the nature of an insider who does not have the benefit of the *Turquand* rule.[772] The latest decision of the English court [773] has been criticised by South African writers.[774] The applicability of the *Turquand* rule should not be determined by labelling the third party as an insider or an outsider. Preferably, the usual boundary of determining whether there existed circumstances where the third party was placed on inquiry and therefore should have investigated further whether the internal requirement was met, and whether he did indeed investigate further, should be applied.

Thirdly, there is not yet certainty under what circumstances the application of the *Turquand* rule will be excluded in cases of forgery.[775] The English courts have extended the initial meaning of a forgery, being a counterfeit signature, to instances where the signature of the representative is authentic but was affixed without authority and for a fraudulent purpose or genuine and innocently affixed without actual authority.[776] This extension is unacceptable. It would mean that the *Turquand* rule would in most cases never find application. The suggestion from South African authors[777] that cases of forgery should be dealt with within the existing boundaries of the *Turquand* rule, without adding forgery as a further exception at all, is supported. It is hoped that the South African courts, when an opportunity arises to decide on this matter, will not follow the English courts.

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769 *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA 257 (W) 266E and confirmed with approval in *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 2 SA 11 (T) 14, also followed in *Zelpy 1780 (Proprietary) Limited v Mudaly* 2015 JDR 0187 (KZP) [47].

770 See para 3.2.3 above.

771 See para 3.2.2.2 above.

772 See *Howard v Patent Ivory Manufacturing Co* (1888) LR 38 Ch D 156 and *Morris v Kanssen* [1946] 1 All ER 586 (HL) against *Hely-Hutchinson v Brayhead Ltd* [1968] 1 Q B 549 (CA).

773 *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549 (CA).

774 Oosthuizen *Turquand-reël* 176; McLennan 1979 *SALJ* 329 at 354; Du Plessis *Grondslae* 70.

775 See para 3.2.2.4 above.

776 *Kreditbank Cassel GMBH v Schenkers Ltd* [1927] 1 KB 826 CA; *South London Greyhound Racecourses Ltd v Wake* [1931] 1 Ch 496.

777 Oosthuizen *Turquand-reël* 285.

Fourthly, although the *Turquand* rule and estoppel are two different principles, the English courts have confused the two and regarded the *Turquand* rule as merely an appearance form of estoppel.[778] Although the South African courts initially applied the two principles as separate doctrines, the concern that they would fall into the same trap as the English courts, has materialised.[779] The intermingling of the *Turquand* rule with estoppel should be rejected outright. It is much more onerous for a third party to rely on estoppel than on the *Turquand* rule, as more requirements need to be proved when relying on estoppel.[780]

Fifthly, in the application of estoppel, it is uncertain whether negligence is a necessary requirement to be proved by the third party. It appears that the requirement of fault as an essential element of estoppel has not been finally settled in our law. It is suggested in this regard that the third party should simply need to prove that the principal (company) should reasonably have expected that an outsider would act on its representation.[781]

Sixthly, as if the confusion between estoppel and the *Turquand* rule is not enough, the constitutional court recently managed to confuse estoppel with estoppel itself and made a distinction in estoppel where none is called for. In *Makate v Vodacom (Pty) Ltd* [782] the constitutional court distinguished estoppel and ostensible authority from one another by averring that ostensible authority is actual authority whereas estoppel is not. This judgment is against a long line of South African authorities and is objectionable in the strongest terms. [783] It simply added more fuel to the fire of confusion in the field of corporate representation.

All the errors in the application of the common law and the uncertainties that exist, presented a great opportunity for the legislature to dispel with these problems. However, the reaction of the legislature as embodied in the Companies Act of 2008 was, to say the least, very disappointing.

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778 See Ch 2 para 2.2.2 above.

779 *One Stop Financial Services (Pty) Ltd v Neffensaan Onwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)* [2015] 4 All SA 88 (WCC) [25]; Also see *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) [110].

780 See para 3.2.2.5 above.

781 See para 3.2.3.3 above.

782 2016 4 SA 121 (CC).

783 See para 3.2.3.7 above.

One thing that the legislature can be commended for, is the abolition of the doctrine of constructive notice.[784] The legislature has, however, countered this initiative by retaining the doctrine of constructive notice in respect of so-called ring-fenced companies and personal liability companies. This gives companies the opportunity to ensure that the company becomes an "RF" company whereby the doctrine of constructive notice is again resurrected shortly after its execution by the Companies Act of 2008. This time round the Companies Act of 2008 complicates the application of the doctrine of constructive notice by providing that it shall apply to restrictive conditions and any requirement for the amendment of any such condition in addition to the normal amendment requirements, if the name of the company includes the element "RF"and the Notice of Incorporation has drawn attention to these conditions. It is uncertain what kind of conditions would constitute "restrictive conditions" and whether it pertains to conditions only restricting the capacity of the company, the authority of the directors to act on behalf of the company or both. It is further uncertain whether a restrictive condition on its own would qualify as such or whether such condition must be coupled with a condition restricting its amendment. It is very unfortunate indeed that the commendable effort of abolishing the doctrine of constructive notice was spoilt by its retention under certain circumstances.[785]

The Companies Act of 2008 introduced a novel provision, namely section 20(7). The interpretation of section 20(7) is, however, littered with uncertainties. At first glace this section appears to be the statutory enactment of the common-law *Turquand* rule. However, on closer examination, section 20(7) differs from the *Turquand* rule, and its application is in certain instances wider and in other cases narrower than that of the *Turquand* rule. The application and scope of section 20(7) are full of uncertainties.

First, this section is arranged under section 20, with the heading "[v]alidity of company actions". It is uncertain whether section 20(7) finds application in respect of actions of the company relating to the capacity of the company, or to the

784 See para 3.3.2 above.
785 See para 3.3.2 above.

authority of the directors representing the company, or to both.[786] It is imperative that these two concepts are clearly distinguished from one another. However, the legislature found it appropriate to mix them throughout section 20, so that it is not clear whether a particular subsection relates to the one or the other or to both.

Secondly, the legislature has excluded shareholders from the protection of section 20(7). Whether a person may rely on section 20(7) should be determined by enquiring whether the person had access to the internal management of the company to establish whether the formal and procedural requirements of the company have been complied with. Shareholders do not have access to the internal management of the company, at least not as far as resolutions of directors are concerned. It is suggested that in respect of directors, prescribed officers and shareholders, it should first be determined whether they had access to the internal management of the company and secondly whether they had taken all reasonable steps to ensure that the internal requirements were observed. If they did not have access or if they did, but they had taken reasonable steps to ensure that the requirements had been met, they should not be deprived of the protection of section 20(7).[787]

Thirdly, the unfortunate use of the word “presume” in section 20(7) causes difficulties. A presumption can be rebutted and where the company proves that the formal and procedural requirements have not been complied with, a third party may not presume that they have to enable him to rely on section 20(7). This renders section 20(7) nugatory and it could just as well not have been enacted.[788] It would be better to replace “presume” with “assume”.

Fourthly, there is uncertainty as to what “formal and procedural” requirements entail. Many writers are of the view that it only relates to requirements in respect of a resolution or attempted resolution that was taken by the company and not where there was no resolution taken at all.[789] In other words, where, for example, a resolution of shareholders is required for the particular act over and above the

786 See para 3.3.4.3 above.
787 See paras 3.2.2.2 and 3.3.4.1 above.
788 See par 3.3.4.2 above.
789 See par 3.3.4.4 above.

resolution of the board, such shareholders' resolution cannot be seen as a formal and procedural requirement that may be made good by section 20(7). The application of section 20(7) in this regard is too narrow as this is an internal requirement of the company and a contracting third party would not be in a position to ascertain whether the shareholders' resolution was taken or not.

Fifthly, it is unclear how section 20(7) should be applied in respect of formal and procedural requirements laid down by the Companies Act itself, for example where the Act requires a a special resolution from the shareholders.[790] Clarity in this regard is called for.

Sixthly, some authors[791] interpret the good faith requirement of section 20(7) as excluding third parties dealing with "RF" companies where the doctrine of constructive notice finds application. The third party would, according to this view, be reasonably expected to gain actual knowledge of the content of the restrictive conditions in the Memorandum of Incorporation as well as of compliance with those clauses. This view cannot be supported and section 20(7) should be clarified so as to exclude this interpretation.[792]

Seventhly, section 20(7) does not spell out the consenquences of the presumed compliance with formalities and procedures in relation to *bona fide* third parties. A company's invalid decision or conduct will not suddenly become valid just because a third party may presume that it is valid.[793]

Lastly, there exists uncertainty regarding the manner of integration of the common-law *Turquand* rule with section 20(7).[794] It is uncertain how these two rules should be applied in relation to one another. Due to the uncertainties in the interpretation of section 20(7), common law will have to be applied by the court in its interpretation and application of this section. As the *Turquand* rule is seen as a rule on its own and as it is retained by the Companies Act, it might happen that the

790 See para 3.3.4.5 above.
791 Locke 2016 *SALJ* 160 at 180.
792 See para 3.3.4.7 above.
793 See para 3.3.4.8 above.
794 See section 20(8) of the Companies Act of 2008 and para 3.3.4.9 above.

principles of this rule are used by the courts in interpretaing section 20(7).[795] The risk exists that the uncertainties and incorrect application of the common-law *Turquand* rule will by implication then be imported into the interpretation of section 20(7). This may lead to a further watering down of the *Turquand* rule and conflation with section 20(7). It remains to be seen how the *Turquand* rule will continue to be used as an alternative to section 20(7). I agree with Delport[796] that the overlap between these two rules may lead to "legal arbitrage".

[795] This already occurred in *One stop Financial Services (Pty) Ltd v Neffensaan Onwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)* [2015] 4 All SA 88 (WCC).

[796] Delport 2011 *THRHR* 132 at 138.

# CHAPTER 4 CONCLUSION AND RECOMMENDATIONS

## 4.1 Introduction

As a company is a juristic person it can only act through human agency. A concern that arises because of this fact relates to the authority of the board of directors to represent the company externally and the protection of the company and its shareholders against possible transgressions of authority. The protection of a *bona fide* third party contracting with the company against the possibility that the representative of the company has exceeded his or her authority also becomes relevant and the question of the weighing and balancing of the interests of the shareholders and the company on the one hand and the contracting third party on the other needs to be considered. It is important to have certainty on the validity and enforceability of contracts concluded by and with companies as the absence of certainty can hamper transactions with companies and impact on the economy.

In this study an examination of the current legal position regarding representation of a company in South Africa was undertaken. The history and development of the common-law principles of agency and doctrines that are unique to representation in a company law context[797] were analysed. The integration of the common-law principles with the relevant provisions of the Companies Act of 2008 was considered. The study was limited to the external consequences in instances where the directors exceeded their authority in contracting with a third party and did not include the instances where a company exceeded its capacity to act. The study also did not focus on the internal consequences of transgression of authority by directors.

In support of the analysis, a comparative study was undertaken of the history and development of this subject matter in England. Although the company law of England is gradually moving away from South African company law, the origin of many of the common-law principles that have been taken over into South African

[797] Doctrine of constructive notice and the *Turquand* rule.

law is derived from England. The reason for the creation of these doctrines must therefore be sought in English law and an assessment must be done whether these original reasons still exist. It was considered whether it would be advisable to use the current situation in England as a model for South African company law or not. It was concluded that the law in England is even more unsatisfactory than the current position in South Africa.

The state of affairs regarding the application by the courts of the common law in South African law is all but acceptable and the introduction of the Companies Act of 2008 did not address this problem but rather added to the confusion and complicated the legal position even further. In this chapter an overview of the position in England and South Africa is given and the problem areas in the two systems are identified. Thereafter, a comparison between the two systems are undertaken, followed by suggested recommendations and solutions in that regard.

## 4.2 English law

In order to determine whether a company will be bound by the acts of its representatives in accordance with English law it should still be determined whether the board of directors or an agent acting with delegated authority of the board had the necessary authority, but for a limitation on the authority of such company agent set out in the company's constitution, resolutions by the company or its shareholders or in shareholders' agreements.[798]

To determine whether the representative had the necessary authority the common-law principles relating to agency must still be applied, which includes actual authority, ostensible authority and a specific common-law principle developed by the courts in a company law context, being the *Turquand* rule.[799]

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798 See Ch 2 para 2.3 above.

799 See Ch 2 para 2.2 above. It first needs to be determined whether the representative had actual (express or implied) authority to enter into the contract. If so, the company (principal) will be bound thereto. In both England and South Africa the usual authority of an agent or representative, being the authority to execute those legal acts that are normally attributable to the position of representatives or officers of that class, can assist to determine whether the representative had (implied) actual or ostensible authority.

The actual authority of the board of directors in England can be ascertained from the articles of the company which usually grant the authority to the board to manage the business of the company.[800] To this intent, it should be ensured that the articles do grant authority to the board. Alternatively, if no such authority has been granted in the articles (which would be very rare), it should still be determined whether the board had authority by applying the normal principles of agency, and in particular by looking at "usual authority" as a tool to assist in applying agency principles. Where an agent acts on behalf of the company, it should be determined whether the board was authorised to delegate authority to such an agent. That would only be the case if the board is duly empowered to do so by the articles of the company.[801] In the event of a single director or other agent acting on behalf of the company, his authority should therefore first be established in terms of the common-law principles of agency.

If a representative does not have the necessary authority or if he exceeds his authority, or if his authority is deficient, the principal (company) would normally not be bound. It would only be possible to hold the principal (company) bound on common-law principles if the principal ratified the act of the representative or through applying the principles of ostensible authority or the *Turquand* rule,[802] bearing in mind that under such circumstances the objectionable doctrine of constructive notice still applies.[803]

The application of these common-law principles presents a problem as the courts confuse the different principles with one another, using the one principle for explaining liability of the company but terming it as another principle.[804] The English courts have further confused the *Turquand* rule with estoppel, seeing the former as an appearance form of estoppel.[805] This has led to a lot of confusion

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800 See Ch 2, para 2.2.1 above.

801 See Ch 2, para 2.2.1 above.

802 The *Turquand* rule was created by the courts to temper the unfair operation of the doctrine of constructive notice. The *Turquand* rule, however, only finds application within certain boundaries and cannot come to the aid of the third party in all instances. See Ch 2, para 2.2.2 above.

803 See Ch 2, para 2.3.7 above for the effect of section 40 on the *Turquand* rule.

804 The courts, for example, have reached a conclusion that there is implied authority, terming it as such, but where it is clear that the argument of the court is rather based on ostensible authority. See Ch 2, para 2.2.1 above.

805 See Ch 2, para 2.2.2 above.

and the requirements to be successful with an estoppel have been supplanted to the application of the *Turquand* rule.[806]

As a creation by the courts, it was also left to the courts to develop the *Turquand* rule. Rather than to obtain clarity on the precise content of this fairness rule and the area within which it finds application, each case has been considered in a casuistic manner which led to irreconcilable judgements. The courts tried to reconcile these judgements for a uniform approach,[807] but it led to a darkness of subtle distinctions and qualifications to the *Turquand* rule. The result was uncertainty which brought the protection that the rule provided to third contracting parties in danger. Some reasons why this happened are firstly the failure of the courts to regard the *Turquand* rule as an independent rule with the result that it was confused with other legal rules, and especially estoppel. This confusion led thereto that the courts applied estoppel, and the success of a third party when relying on the *Turquand* rule, is made dependant on compliance with the requirements laid down for estoppel.[808] In applying the many rules and qualifications that have been laid down, the courts sometimes lose sight of the real underlying principle of the *Turquand* rule, namely reasonableness in favour of third parties who contract *bona fide* with a company. In English law, especially, the *Turquand* rule is seen as a mere appearance form of estoppel.

The problem in the incorrect application of the common-law principles of agency was not efficiently addressed in English law with the enactment of section 40 of the Companies Act 2006. First, this section does not address the problem where the board or another agent acted on behalf of the company without the necessary authority. Whether a company may be bound to a contract entered into on its behalf should therefore still be determined by applying the common-law principles of agency, which, as has been seen above, is in a state of uncertainty and confusion. Secondly, instead of abolishing the challengeable doctrine of constructive notice outright, it is still retained if the transaction cannot be brought within the scope of application of section 40. Thirdly, the confusion created by the

806 See Ch 2, para 2.2.2 above.

807 See for example *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480, CA.

808 See Ch 2, para 2.2.2 above.

courts between ostensible authority and the *Turquand* rule has not been resolved as the common-law *Turquand* rule has been retained alongside section 40.[809]

After it has been ascertained that an agent of the company would have had authority if it were not for a particular limitation in the constitution of the company, the contracting third party might be successful in relying on section 40 or the common-law *Turquand* rule.

According to section 40 of the Companies Act of 2006 the power of the directors to bind the company, or authorise others to do so, is deemed to be free of any limitation under the company's constitution, in a resolution of the company or of any class of shareholders, or in any agreement between the shareholders or any class of them. This deemed provision is in favour of a person dealing with a company in good faith.

Over and above the shortcomings of section 40 alluded to above, section 40 creates interpretational problems. The third party must still ensure that the person who acts on behalf of the company was authorised by the board to act, but for a limitation in the constitution.[810] If not, the third party would not be able to rely on section 40. There exists uncertainty as to what kind of limitations would be covered by section 40,[811] whether reference to directors would include a single director [812] and what good faith entails.[813]

The scope of application of section 40 is further limited and might not always come to the rescue of a third contracting party acting on good faith.[814]

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809 A third contracting party therefore has a choice between relying on the *Turquand* rule or section 40. Although circumstances where under both these two principles may be used may overlap, there are also circumstances where under the third party would not be able to bring the transaction within the application of section 40, but indeed under the application of the *Turquand* rule and *vice versa*. See Ch 2, para 2.3.7 above.

810 Ch 2, para 2.3 above.

811 Ch 2, para 2.3.2 above.

812 Ch 2, para 2.3.2 above.

813 Ch 2, para 2.3.5 above.

814 See Ch 2, paras 2.3.1-2.3.6 above.

Section 41 of the Companies Act of 2006 applies if a director (or connected person) is the third party dealing with his company and the directors have transgressed a limitation set out in the constitution of such company. It provides that where the validity of a transaction that has been entered into by a company depends on section 40 and the third party to that transaction is a director of the company or of its holding company or a person connected to such director, such transaction is voidable at the instance of the company.

There are different views regarding the interaction between sections 35A and 322A[815] (now sections 40 and 41 of the Companies Act of 2006) and how they should be applied.[816] This situation is criticised as being unnecessarily confusing and regrettable that the 2006 Companies Act did not clear up this confusion.

From the different views the outcome of a transaction by the company with one of its directors can differ depending on which view is followed. This creates yet another uncertainty in the application of section 40 and 41. There is also uncertainty regarding the position of a shareholder as a third party.[817]

## 4.3 South African law

### *4.3.1 Introduction*

The normal common-law principles of agency form the foundation for representation in South African company law.[818] The point of departure in determining whether a company can be held bound by the acts of its representative is therefore to ascertain whether the representative of the company had actual (express or implied) authority to bind the principal (company).[819]

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815 These are sections of the previous Companies Act of 1985.
816 See Ch 2, para 2.3.6 above.
817 See Ch 2, para 2.3.6 above.
818 See Ch 3, para 3.1 above.
819 See Ch 2, para 2.2.1 and Ch 3, para 3.2.1 above.

These principles could, however, not in all cases provide a fair solution to problems that arise in the case where the principal is a company that cannot act on its own. A specific branch of the law of agency therefore developed which was used in instances where a company was the principal.[820] Specific common-law principles akin to company law should be taken into account when determining whether a company may be held bound to the acts of its agent. Where actual authority of the representative is therefore lacking, the common-law doctrines that have developed due to the fact that a company is not a natural person should be considered to ascertain in what way they ought to affect the result. In particular the question should be asked whether the company can be held bound on grounds of the *Turquand* rule or estoppel. A common-law principle specific to company law that affects these two doctrines is the doctrine of constructive notice.

### *4.3.2 Doctrine of constructive notice*

The doctrine of constructive notice was developed by the courts to temper the unfair effect that the partnership analogy in company law originally had. According to the doctrine of constructive notice the limitations on authority in the public documents (which include *inter alia* the memorandum and articles of association) of a company are enforceable against third parties even if they did not have any knowledge of these restrictions. Due to the publicity given to these public documents notice of the content thereof is attributed to third parties. The third party can therefore not rely on the implied or ostensible authority that is in conflict with the public documents. This greater protection that the doctrine of constructive notice gave to the company and ultimately its shareholders, however, prejudiced the position of a third party who contracted with the company. A third party could only contract with safety with a company if he made sure what restrictions there were in the constitution of the company and to make sure that any requirements stated in the constitution have been complied with, including any internal requirements where the authority of a particular representative has been made dependant on compliance with some or other internal requirement. This is impossible for a third party as he does not have access to the minute book of the

820 See Ch 3, para 3.1 above.

company to determine whether the internal management of the company has been done properly. If he contracts with the company and it later transpires that the internal requirements were not complied with, the company will not be bound on grounds of the normal principles of agency.

The abolition of the doctrine of constructive notice in the Companies Act of 2008 is to be welcomed. Its abrogation was long overdue. However, there is some concern regarding the remnants of the doctrine where it still applies in respect of, *inter alia*, the so-called "RF" companies. Companies can decide to incorporate limitations on the authority of directors in its Memorandum of Incorporation, refer to these in the notice of incorporation (or subsequent notice of amendment, if the company has already been incorporated), add "RF" behind its name, and the unsatisfactory position as it existed under the Companies Act 61 of 1973 will then still apply.

The uncertainty created in section 15(2)(b)[821] of the Companies Act of 2008 by the vague wording "restrictive conditions", which is not defined in the Act, also leaves room for a wide interpretation thereof which may not only include limitations on the capacity of the company, but also on the authority of directors to act on behalf of a company. Although certain authors are of the view that a restrictive condition alone cannot qualify as a restrictive condition, but should be coupled with a requirement regarding the amendment thereof that is more stringent than the requirements for a usual amendment of the Memorandum of Incorporation, other authors regard a restrictive condition on its owns as qualifying as such.[822] This is also the view expressed in the non-binding opinion issued by the Companies and Intellectual Property Commission.[823]

What is even more disconcerting is the suggestion of certain authors[824] that the addition of "RF" to the name of the company and the drawing of attention to a

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821 Although the doctrine of constructive notice has been abolished by section 19(4) of the Companies Act of 2008, this doctrine has been retained in respect of *inter alia* provisions in a company's Memorandum of Incorporation contemplated in section 15(2)(b) or (c).

822 See Ch 3, para 3.3.2 above.

823 See Ch 3, para 3.3.2 above.

824 See Ch 3, para 3.3.4.7 above.

restrictive condition in the company's Memorandum of Incorporation[825] create suspicious circumstances in terms of which it would be expected from a third party to obtain actual knowledge of these restrictions as well as ensuring compliance therewith and consequently robbing a third party from the protection of the *Turquand* rule as well as section 20(7) of the Companies Act 2006. This reasoning places a third party in an untenable position. It imports the doctrine of constructive notice without tempering its severe effect on third parties by the *Turquand* rule or section 20(7), leaving the third party in an even more vulnerable position than was the case under the Companies Act of 1973.

Many writers have advocated for the abolition of the doctrine of constructive notice and the fact that this doctrine is still retained with regard to companies of which the Memorandum of Incorporation contains restrictive conditions (the co-called ring fenced companies), just brings new uncertainties to the front to an otherwise commendable innovation, namely the abolition of this doctrine in instances other than in respect of ring-fenced companies.[826] These uncertainties result therein that it would not be safe for a third party to deal with such a company at all. Legal certainty to promote economic business dealings are hampered by these provisions of the Act.

### *4.3.3 Turquand rule*

In an effort to establish a better balance between the shareholders and third parties, the English courts formulated the *Turquand* rule. The *Turquand* rule is a fairness rule primarily aimed to strengthen the position of *bona fide* third parties who contract with a company by eliminating some of the unfair consequences of the doctrine of constructive notice. It would be unfair to expect from an outsider third party to study the internal aspects of a company. According to this rule the examination by third parties are restricted to those aspects to which publicity is given. Provided he acts *bona fide*, a third party can assume that the internal management, to which he does not have any access, has properly taken place.

825 S 19(5) of the Companies Act of 2008.
826 See Ch 3, para 3.3.2 above.

The creation of the rule had the result of protecting a contracting third party and placed negotiations with companies on a firmer foundation.

Although the English courts have confused the *Turquand* rule with estoppel, the South African law is fortunately a bit clearer.[827] The appeal court, in *The Mine Workers' Union v Prinsloo*,[828] held that the *Turquand* rule is not a mere appearance form of estoppel and that the protection of the third contracting party should not be made dependent on the requirements laid down for estoppel.[829] In later judgments, the South African courts have, however, made the same mistake as the English courts and intermingled the *Turquand* rule with estoppel.[830] In such event the balance between the interests of the company and its shareholders on the one side and those of third parties dealing in good faith with the company on the other, is disturbed. Overemphasis on the interests of the company and its shareholders would discourage third parties to contract with companies and as such the company as business vehicle would also be prejudiced.

Due to this confusion and the existing uncertainty regarding the scope of its operation,[831] it is critical that the exact extent of the scope and application of the *Turquand* rule is clearly established to provide legal certainty and to ensure a fair balance of the rights between the contracting third party on the one hand the company and its shareholders on the other hand.

As the doctrine of constructive notice has been abolished (save for certain instances),[832] it might seem as though there is no further need for the *Turquand* rule. There is, however, still room for retaining the *Turquand* rule even if the doctrine of constructive notice has been abolished.[833]

A need for the *Turquand* rule might still be required in the instance where the third contracting party did indeed have knowledge of the Memorandum of Incorporation

827 See Ch 3, para 3.2.2.5 above.
828 1948 3 SA 831 (A).
829 *The Mine Workers' Union v Prinsloo* 1948 3 SA 831 (A) at 849.
830 See Ch 3, para 3.2.2.5 above.
831 See Ch 3, paras 3.2.2.2 and 3.2.2.4 above.
832 See Ch 3, para 3.3.2 above.
833 See Ch 3, para 3.3.3 above.

wherein the authority of the directors to act is dependent on the fulfilment of some or other procedural requirement.

Obviously the *Turquand* rule would also find application in the event that the doctrine of constructive notice applies as provided for in section 19(5) of the Companies Act of 2008. As the *Turquand* rule relates to the authority of a representative to bind a company, the *Turquand* rule would only find application in respect of a restrictive condition in an "RF" company's Memorandum of Incorporation, if such restriction relates to the authority of a representative and not where it relates to a restriction on the capacity of the company.

Another instance where the *Turquand* rule may still find application is where the irregularity does not relate to any limitations as set out in the Memorandum of Incorporation, for example defective notices of meetings, defective quorums and defective appointment of officials.[834] The *Turquand* rule will also still find application where the powers of the board have been restricted in the Memorandum of Incorporation as contemplated in section 66(1).[835]

To deprive a third contracting party of the *Turquand* rule would mean that the remedies of the contracting third party would be limited to implied and ostensible authority. Where the authority of an agent has been restricted by some internal arrangement, it would mean that the third party would not be able to rely on implied authority. In order to be successful with estoppel the third party would have to prove that the company has represented that a particular person had authority and has also represented that the required internal requirements have been complied with under circumstances where the third party had actual knowledge of the internal requirements that have been laid down. The third party does, however, not have access to the internal affairs of the company and would therefore not be able to establish the true state of affairs. The *Turquand* rule would have been the only avenue to follow for the third party in such an instance.[836]

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834 See Ch 3, para 3.3.3 above.
835 See Ch 3, para 3.3.1.3 above.
836 See Ch 3, para 3.3.3 above.

The boundaries wherein the *Turquand* rule finds application are not certain[837] and as the *Turquand* rule has in the past been merged with estoppel[838] it would have been a great opportunity for the legislature to expel any uncertainties in the field of its application by enacting a statutory *Turquand* rule, defining the boundaries within which it can find application. Instead of clarifying the content and application of the *Turquand* rule in legislation, the opposite has happened with the enactment of section 20(7) and 20(8) of the Companies Act of 2008. There are several conflicts between the *Turquand* rule and its statutory counterpart as set out in section 20(7) of the Companies Act of 2008. This creates a problem in light of the wording of section 20(8) of the Companies Act, which allows the common-law *Turquand* rule to also still operate. The intention of the legislature in respect of section 20(8) is unclear and the content thereof is open to several interpretations which lead to uncertainty.

### *4.3.4 Estoppel*

The requirements that the third contracting party must prove to be successful with reliance on estoppel have been laid down by the South African Supreme Court of Appeal in *NBS Bank Ltd v Cape Produce Co (Pty) Ltd and others,*[839] which approved *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd*.[840]

Additional requirements that were not required in the English judgment of the *Freeman* case[841] are that the representation must have been in a form that the company should reasonably have expected that an outsider would act on the strength of it, reliance on the representation by the third party and prejudice.[842] It seems as though fault as an essential requirement for estoppel in a company law context has not been finally settled in our law.[843]

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837 See Ch 2, para 2.2.2 above.
838 Ch 2, para 2.2.2 and Ch 3, para 3.2.2.5 above.
839 2002 1 SA 396 (SCA) [26]. For these requirements, see Ch 3, para 3.2.3 above.
840 [1964] 2 QB 480 (CA).
841 *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA).
842 See Ch 3, paras 3.2.3.3-3.2.3.5 above.
843 See Ch 3, para 3.2.3.3 above.

Estoppel has in the past been confused by the courts with implied authority.[844] Furthermore, the constitutional court has separated ostensible authority from estoppel and has determined them to be two different concepts, where substantially fewer requirements are necessary to be proved by a third party relying on ostensible authority than on estoppel and continuing to equate ostensible authority with actual authority.[845] This deviation by the court from a long line of authorities[846] could have been prevented by enacting a statutory estoppel to be used in a company law setting, which opportunity was not taken by the legislature.

### *4.3.5 Original authority of the board of directors*

Section 66(1) of the Companies Act of 2008 confers original power on the board of directors to manage the business and affairs of the company. These powers may, however, be restricted in the company's Memorandum of Incorporation or the Companies Act itself.

#### 4.3.5.1 Restriction on the powers of the board in the Memorandum of Incorporation

In the event that the company's *Memorandum of Incorporation* places a total restriction on one of the powers of the board, for example, the board may not borrow money in excess of R50 million rand, and the board exceeds such restriction, the third party cannot simply assert that since he is not deemed to know of the restriction due to the abolition of the doctrine of constructive notice he may hold the company bound to the loan agreement. The fact that the third party is not deemed to know of this restriction, does not constitute a legal ground on which the company can be held liable. If, however, the third party is able to prove all the essential requirements for estoppel, he may be successful in holding the

844 See Ch 3, para 3.2.1 above.
845 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC). See Ch 3, para 3.2.3.7 above.
846 See Ch 3, para 3.2.3.7 above.

company to the contract on grounds thereof. The doctrine of constructive notice previously deprived such third party of the right to rely on estoppel.[847]

If an authority or power of the board is made dependent on compliance with some or other internal formality or formal or procedural requirement, for example, the board may only borrow money in excess of R10 million subject to prior shareholder approval, again, the third party cannot use the fact that he is not deemed to know about this requirement as the legal basis to hold the company to the contract where the board entered into a loan agreement in excess of this amount without prior shareholder approval. In this instance the third party may be able to hold the company to the contract if he is able to bring the transaction within the scope of application of either the *Turquand* rule or section 20(7) of the Companies Act of 2008.

Where the third party has actual knowledge of the total restriction or where he is deemed to have knowledge thereof due to the operation of the doctrine of constructive notice in the case where he deals with a "RF" company, the third party would not be successful in relying on estoppel. He would, however, be able to hold the company bound if he can bring the transaction within the scope of either the *Turquand* rule or section 20(7) of the Companies Act of 2008, where the authority of the board was made dependent on compliance with certain internal formalities and procedures.

4.3.5.2 Restriction or limitation in the Act itself

A third party will not be able hold the company bound to a contract on grounds of the *Turquand* rule if the board of directors exceeded its authority, as restricted by the *Companies Act itself*.[848] If the restriction or limitation in the Act is of a substantive nature and cannot be said to be of a formal or procedural nature, the third party would also not be able to rely on section 20(7).[849]

847 See Ch 2, para 2.2.3.4 and Ch 3, para 3.2.3.6 above.
848 See Ch 3, para 3.3.4.5 above.
849 See Ch 3, para 3.3.4.5 above.

It is submitted that the third party would also not be able to hold the company liable on grounds of estoppel under these circumstances.

4.3.5.3 Restriction on powers of the agent in the Memorandum of Incorporation or underlying document, where an individual acts

The board of directors is also authorised to delegate its authority to one or more agents.[850] Where delegation of authority has taken place, the authority of the agent to act on behalf of the company should still be determined by applying the common-law principles of agency. If it cannot be proved that the agent had actual (express or implied) authority, the third party may still be successful in holding the company bound on grounds of the common-law principles of estoppel, the *Turquand* rule or section 20(7) of the Companies Act of 2008.

*4.3.6 Section 20(7) of the Companies Act of 2008*

The subsections of section 20, under the heading "Validity of company actions" leave the impression that the section pertains to the capacity of the company. It, however, deals with both the capacity of the company as well as the authority of the directors to act on behalf of the company. These two aspects are two very distinctive concepts and should be kept apart from one another.[851] In section 20 these two concepts however, are so intermingled that it is difficult to distinguish the one from the other.

Section 20(7) provides that a person dealing with a company in good faith is entitled to presume that the company, in making any decision in the exercise of its powers, has complied with all the formal and procedural requirements laid down in the Act itself, its Memorandum of Incorporation or rules of the company. Where such third party knew or reasonably ought to have known of non-compliance of such requirement, he would not be able to rely on section 20(7). Certain third parties, namely directors, prescribed officers and shareholders of the company are not entitled to rely on section 20(7). This is very harsh in respect of shareholders,

850 S 66(1) of the Companies Act of 2008.
851 See Ch 1, para 1.1 above.

at least in respect of decisions taken by the board of directors, as the shareholders would not have the means to ascertain whether the decisions of the board were regular.[852] The unfortunate use of the word "presume" in section 20(7) may lead to confusion as a presumption may be rebutted in which event the third party cannot rely on section 20(7).[853] There is further room for argument that section 20(7) relates to the capacity of the company and not the authority of the directors to represent the company.[854] There is also uncertainty as to what would fall under "formal and procedural requirements" as contemplated in section 20(7).[855] Even formal and procedural irregularities in the Act itself can be condoned by section 20(7).[856] This is in contravention of the common-law *Turquand* rule and also certain sections of the Companies Act of 2008 in terms of which non-compliance with, for example, the requirement of a special resolution results in voidness of a company's action. It would seem as though a distinction should be drawn between substantive requirements in the Act, where section 20(7) would not find application as opposed to formal and procedural requirements. There are also different views that can be held regarding the requirement that the third party should not have known or reasonably ought to have known of the defect in the compliance with the formality or procedure.[857] Section 20(7) further does not spell out the consequences of the presumed compliance with formalities and procedures in relation to the *bona fide* third party. A company's invalid decision or conduct will not suddenly become valid just because one person may presume that it is valid.[858]

### *4.3.7 Section 20(8) of the Companies Act of 2008*

According to section 20(8) of the Companies Act of 2008, section 20(7) must be construed concurrently with and not in substitution for any relevant common-law principle. The common-law principle that comes to mind is the *Turquand* rule. This section can be interpreted in that the other contracting party has a choice

852 See Ch 3, para 3.3.4.1 above.
853 See Ch 3, para 3.3.4.2 above.
854 See Ch 3, para 3.3.4.3 above.
855 See Ch 3, para 3.3.4.4 above.
856 See Ch 3, para 3.3.4.5 above.
857 See Ch 3, para 3.3.4.7 above.
858 See Ch 3, para 3.3.4.8 above.

between relying on the statutory rule formulated in section 20(7) or on the common-law *Turquand* rule thereby choosing the more favourable option. On the other hand, this section can be interpreted that section 20(7) must be used, but to the extent that it does not alter the common-law principles of the *Turquand* rule as created and developed by the courts.

In *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)*[859] the court expressed the view that "formal and procedural requirements" as contemplated in section 20(7) should be interpreted consistently with "… the conventional scope of *Turquand*."[860] The court also applied one of the restrictions applicable to the common-law *Turquand* rule, namely that it would only find application if the act of the representative can usually be associated with an act of a person in his position in the company, to section 20(7).[861] If the common-law principles of the *Turquand* rule may only be used to interpret and create boundaries in the application of section 20(7), and not as a rule on its own, the third party would be deprived from holding a company to a contract which he could have done if the common-law *Turquand* rule still applied as a rule on its own, since the application of the *Turquand* rule is in certain respects wider than section 20(7).[862]

If section 20(8) is interpreted to allow a contracting party to use either section 20(7) or the common-law *Turquand* rule, a problem arises as they conflict in certain respects.[863] The Companies Act does not indicate which one should take precedence in the event of a conflict as it does in respect of other possible conflicts that may arise.[864] *Henochsberg*[865] is of the opinion that it would be an extremely challenging task to develop the common-law *Turquand* rule in line with section 20(7) and that it is unclear under which circumstances which one of the two should be relied upon.[866] Clarification regarding the application of section

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859 [2015] 4 All SA 88 (WCC) per Rogers J.

860 *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd (The CRL Trust as intervening creditor)* [2015] 4 All SA 88 (WCC) [55].

861 See Ch 3, para 3.3.4.4 above.

862 See the comparison between the *Turquand* rule and section 20(7) in Ch 3, para 3.3.4.

863 See Ch 3, para 3.3.4 above.

864 See for example section 5(5) and 5(6) of the Companies Act of 2008.

865 Delport and Vorster *Henochsberg* 2008 106(5).

866 See Ch 3, para 3.3.4.9 above.

20(7) as well as its integration with the common-law principles of representation in a company law context is therefore necessary.

## 4.4 Comparison of English position with the current position under South African law

The approach of South Africa and England differs drastically. In South Africa the board of directors has original authority to manage the company, and to delegate their powers to a board committee, managing director, director or other agent.[867] Where the board has delegated its authority, the common-law principles of agency will continue to apply. A company will therefore be bound to a contract entered into on its behalf by its managing director or other agent, where such managing director (or other agent) had actual (either express or implied) authority conferred upon him by the board of directors to conclude that contract. If the managing director (or other agent) did not have actual authority, the company will nevertheless be bound where the company ratifies such contract.[868]

Where the agent did not have actual authority to conclude the relevant contract, the company may still be held bound to the contract if the third party is successful in relying on the *Turquand* rule[869] or section 20(7) of the Companies Act of 2008 or if he is able to prove all the essential aspects of estoppel.

Under English law the board of directors does not have original authority to act on behalf of the company, but its authority to bind a company must be granted in either the articles of association of the company or by delegation under a power contained in the articles.[870] The board will also only have the power to delegate their authority if authorised in the articles. To determine whether a contracting third party may hold a company to a contract concluded by the board of directors, the authority of the board should therefore firstly be ascertained from the articles of

867 See Ch 3, para 3.3.1 above.

868 See Ch 3, para 3.3.1.2 above.

869 Obviously the third party would only be successful in relying on the *Turquand* rule if the particular facts fall under the application of the rule and the relief is not excluded due to the exceptions applicable to the rule, namely where the third party was not *bona fide* or where the third party was placed on inquiry as discussed in Ch 2, para 2.2.2 above.

870 See Ch 2, para 2.2.1 above.

the company, failing which it should be determined whether the board had authority by applying the normal principles of agency.

Once such authority is established it should be determined whether there are any limitations placed on the board's authority to act or to authorise others to do so. If there are, section 40 of the Companies Act of 2006 may be applied to remedy this transgression.[871]

In contrast to the position in South Africa where the doctrine of constructive notice has been abolished,[872] the default position in England is that the doctrine of constructive notice still applies. If, however, the transaction can be brought within the provisions of section 40 of the Companies Act 2006 the operation of this doctrine is negated.

The approach in England is much more artificial than in South Africa where original power has been granted to the board to represent the company and where the doctrine of constructive notice has been abolished. It is submitted that South Africa took a step in the right direction by giving original powers to manage the business and affairs of a company to the directors and by abolishing the doctrine of constructive notice, except in limited instances. In that respect South Africa is ahead of the law of England where this doctrine has been retained, although the initial reason for its creation is no longer relevant.[873]

### 4.5 Recommendations and solutions

First, I recommend that the doctrine of constructive notice be abolished *in toto*, also with regard to companies where the Memorandum of Incorporation contains restrictive conditions. The initial reason for introducing this doctrine in England was due thereto that the Joint Stock Companies Act 1844 was largely influenced

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871 See Ch 2, para 2.3 above.

872 Except for certain limited instances.

873 The doctrine was originally created due thereto that the courts regarded a company the same as a partnership where any one is authorised to bind the partnership in respect of transactions that fall within the scope of the business of that partnership. See Ch 2, para 2.2.2 above.

by principles applicable to partnerships.[874] This reason is not relevant today and the need for such a doctrine at all (even in respect of "RF" companies) should be reconsidered. It is open for companies to abuse section 19(5) by adding "RF" to its name and by drawing attention to restrictive conditions in its notice of incorporation or subsequent notice of amendment and thereby resurrecting the doctrine of constructive notice.

Alternatively, if the doctrine of constructive notice is to be retained in respect of "RF" companies, I suggest that a definition should be included in the Act, clearly spelling out what would constitute a "restrictive condition" to clear up the uncertainties that currently exist in this regard as discussed.[875] Provision should also be made that where a company's name ends with "RF" and notice is drawn to the restrictive condition, the doctrine will not apply if the condition does not qualify as a restrictive conditions as contemplated by the definition thereof.

Due to the fact that the common-law *Turquand* rule has been confused with estoppel by the courts (in England and to some extent also in South Africa) it would provide legal certainty if the *Turquand* rule is abolished in respect of its application to companies.[876] The retention of the common-law *Turquand* rule alongside section 20(7) as provided for in section 20(8) of the Companies Act only adds to the confusion as it is uncertain how these two rules should be integrated. Section 20(7), showing similarities with the common-law *Turquand* rule, is however also unclear in its application and its scope of operation. I recommend that the existing section 20(7) should be revisited and its application be expanded in the areas where the scope of the *Turquand* rule is wider.[877] The uncertainty regarding the application of the *Turquand* rule in cases of forgery and what would constitute forgery should also be addressed.[878] It should be included that as part of the meaning of "reasonably ought to have known" that where organs, officers or agents of the company act outside the scope of those acts that are normally

874 Ch 2, para 2.2.2 above.

875 See Ch 3, para 3.3.2 above.

876 It should, however, not be abolished as far as bodies, other than companies, are concerned, as the enactment of a statutory provision will only apply to companies, whereby other bodies would be left remediless in this regard. See Ch 3, para 3.2.2.6 above.

877 The reason for this is that a third party would not be deprived of rights that he has under the common-law *Turquand* rule.

878 See Ch 3, para 3.2.2.1 above.

associated with their position or office in the company, the third party reasonably ought to have known that such organ did not have authority.

The uncertainties in section 20(7) should then also be dispelled with. First the legislature should define what is meant by "formal and procedural" requirements.[879] Secondly, the application thereof should not be excluded in the event where the third contracting party is a shareholder of the company.[880] Thirdly the word "presume" in section 20(7) should be replaced with "assume". Fourthly, it should be made clear that the section can only be used in the instance where the directors (or other agent) of the company exceed their authority and not where the capacity of the company is concerned. Fifthly clarity should be provided as to the good faith requirement in the current section 20(7).[881] Lastly, the consequences of presumed compliance by a *bona fide* third party of formalities and procedures should be spelt out in the section.[882]

It is therefore recommended that the *Turquand* rule be repealed in its totality as far as companies are concerned and that the statutory provision set out in section 20(7) of the Companies Act be amended to provide for clarity in its field of application and operation. It must be borne in mind that certain limitations must be built into this rule to provide for a fair balance between the interests of the company (and its shareholders) and *bona fide* third parties.

Abolishing the doctrine of constructive notice in all cases (even in respect of "RF" companies) and enacting a clearly demarcated statutory *Turquand* rule will have the result of the company carrying the risk in circumstances where this rule is applied and not the third party. I agree with Rabie[883] that this arrangement would be fair, as the company has the authority to appoint its own company representatives and should therefore carry the risk of those representatives who exceed their authority. There would be limitations on the operation of the statutory enactment which would limit its application for an equitable balance of rights. An

879 See the discussion in Ch 3, paras 3.3.4.4-3.3.4.6 above.
880 Except if the internal requirement pertains to authority to be granted at a general meeting of shareholders.
881 See the discussion in Ch 3, para 3.3.4.7 above.
882 See Ch 3, para 3.3.4.8 above.
883 Rabie *Verteenwoordiging* 196.

unauthorised act by a representative should only be dealt with in the internal relationship between such representative and the company.

I also agree with Rabie[884] that the doctrine of estoppel, as applied in a company law environment should be codified, to ensure that no intermingling takes place between this doctrine and the statutorily enacted *Turquand* rule.[885] I do not recommend that estoppel should be abolished in its entirety without a statutory replacement, as there might be instances where the statutory *Turquand* rule cannot come to the rescue of a *bona fide* third contracting party and the doctrine of estoppel will supply the only remedy for the company to be bound by an act. Although the statutory *Turquand* rule and estoppel may overlap these two principles should be given separate operation and the third party should be allowed to use any one of the two, or the one as an alternative to the other to hold the company bound to a contract.

A further reason why it is imperative for the enactment of a statutory estoppel is the danger of distinguishing estoppel from ostensible authority, regarding them as two distinct concepts as was incorrectly done by the constitutional court.[886]

Without professing to have the specialised skills of a legislature, I suggest that the Companies Act of 2008 be amended as follows:

First, there should be no retention of the doctrine of constructive notice and reference to “RF” companies and restrictive conditions should be removed where ever it appears in the Act.

Second, section 20(7) should be afforded its own section number and should not be arranged as a subsection under section 20 pertaining to the validity of company actions. Section 20(8) should be deleted. I suggest the following concept in this regard:

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884 Rabie *Verteenwoordiging* 257.

885 The Botswana Companies Act 32 of 2003, s27(1)(c) and (d), for example, already codifies ostensible authority. See Baiketlile *Corporate Capacity* 28-29.

886 *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC).

20A Compliance with internal, formal and procedural requirements may be assumed.

(1) For purposes of this section, the following words shall have the following meaning:

(a) "representative" means the board of directors, a director, a prescribed officer, and any other person with an office or position in the company[887] in respect of whom there was an actual appointment or election, or in respect of whom an act of appointment or election has been made, although there is one or other deficiency in the act of appointment or election: Provided that any such deficiency may be made good by this section;[888]

(b) "a person dealing with the company" does not include a person who has, by virtue of his or her position with or relationship to the company, access to the internal management and administration of the company, to such an extent that he or she would have been in a position to determine whether the relevant internal, formal and/or procedural requirements have been complied with and who did not take all reasonable steps to ensure that such requirements were observed.[889]

(c) "internal requirements" includes resolutions required in the documents contemplated in subsection (2)(b) to be adopted by the board of directors or the shareholders to authorise the particular transaction or act.[890]

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887 As the common-law *Turquand* rule is only available where it can be established that the representative acted within his usual authority in the company, the company would not be held bound where it has been represented by a normal representative who does not hold a position in the company.

888 There should be a nexus between the company and the representative of the company to prevent an imposter to purport to act on behalf of the company. If the representative was not appointed at all, the third party may still be able to hold the company bound if he can bring the transaction within the scope of application of the proposed section 20B below.

889 It is the third party's inability to ascertain whether the internal procedures have been complied with that makes him worthy of protection. The proposed section should not find application in favour of persons forming part of the management of the company who as such have access to the internal management matters of the company. If, for example, the internal requirement relates to approval of shareholders, a shareholder of the company who will in a position to have access to the meeting of shareholders, will be regarded as an insider who would not be entitled to the protection of the section.

890 This internal requirement can also be made good by the application of the *Turquand* rule. When the formal or procedural requirement is not prescribed by the Act itself, the proposed

(d) "formal and procedural requirements" includes formalities and procedures required for the taking of a proper resolution by the board of directors or the shareholders, but excludes the taking of a resolution itself.

(2) A person dealing with a representative of a company in good faith is entitled to make the following assumptions:[891]

(a) that a company representative who is usually clothed with authority to represent the company is duly authorised to act on behalf of the company; and

(b) that there was compliance with all the internal,[892] formal and procedural requirements-

(i) in the company's Memorandum of Incorporation and rules;

(ii) in resolutions, other internal rules and powers of attorney of the company's-

(aa) board of directors; or

(bb) shareholders or any class of shareholders

(iii) in agreements between the company's-

(aa) directors of the board;

(bb) the shareholders or any class of shareholders;

(cc) the board of directors and the shareholders or any class of shareholders; or

(dd) board of directors or shareholders or class of shareholders and the representative of the company; and

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section 20A also finds application where no resolution was taken. See subsection (2)(b) below.

891 The common-law *Turquand* rule could also find application if the potential authority of a representative was made subject to a condition, for example, the obtaining of a resolution. The wording here has therefore been widened (if compared to section 20(7)) to not require that there should at least have been a decision. Note that this will not apply in respect of resolutions required by Act itself. See subsection (2)(c) below in this regard.

892 This is added to cater for the instance where a directors' or shareholders' resolution is required. Such resolution in itself cannot be said to be a formal or procedural requirement, but the *Turquand* rule allowed a third party to assume that such resolution was taken even if it was not. See Ch 3, para 3.3.4.4 above.

(iv) in any other documents in which the authority of a representative of the company has been made dependent on compliance with internal, formal or procedural requirements,

on which such company representative's authority was made dependent; and

(c) that there was compliance with all the formal and procedural requirements in terms of this Act in respect of-

(i) any[893] resolution or other act[894] required by this Act;[895] or

(ii) any resolution or other act required by the documents referred to in subsection (2)(b).[896]

(3) A person dealing with a company shall be entitled to make the assumptions contemplated in subsection (2) even if the representative of the company acts fraudulently, or forges a document, in connection with the dealings.[897]

(4) The company shall not be entitled to assert in proceedings in relation to the dealings that any of the assumptions contemplated in subsection (2) are incorrect, but the company shall be bound by the transaction or other act concluded by its representative where such representative did not have authority due to non-compliance with an internal, formal or procedural requirement, on grounds of the said assumptions.[898]

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893 This would include special and ordinary resolutions by the shareholders.

894 An example would be where a person has been appointed or elected as director, and already acts as such, but has not formally in writing delivered his or her consent to the company as required by section 66(7)(b) of the Companies Act.

895 If a resolution is required by the Act itself, the third party cannot assume that the resolution has been duly adopted. If the resolution has, however been made, but is deficient due to non-compliance with a formal or procedural matter prescribed by the Act, this subsection allows the third party to rely on the proposed section 20A.

896 It might, for example, happen that the Memorandum of Incorporation requires a shareholders' resolution before the board may borrow money in access of R10 000 000. Although the shareholders' resolution has been taken, the notice of the meeting as required by the Act itself (s 62 of the Companies Act of 2008) was deficient. In such an instance the proposed section 20A(2)(c)(ii)) would come to the aid of the third party.

897 In the case of "forgery" the third party should still be able to rely on this section, within the boundaries as stipulated. See Ch 3, para 3.2.2.4 in this regard.

898 See para 3.3.4.8 above.

(5) A person dealing with a company shall not be entitled to make the assumptions contemplated-

(a) in subsection (2) if[899] he or she knew[900] or suspected[901] that the assumption was incorrect; and

(b) in subsection (2)(c)(i)[902] if non-compliance with the formal and/or procedural requirements in the taking of the resolution-

(i) is material or not accidental or inadvertent;[903] or

(ii) if the relevant section of the Act expressly visits non-compliance with an internal, formal or procedural requirement with voidness.[904]

(6) For purposes of this section,

(i) a person deals with a company if he or she is a party to any transaction or other act to which the company is a party.[905]

(ii) a person dealing with a company shall be deemed to have known that the assumption as contemplated in subsection (2) was incorrect if-

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899 As this section strengthens the position of the third party dealing with the company at the expense of the company, it is necessary to guard against the indiscriminate extension thereof. The application of the section should therefore be restricted to only find application in certain instances. Further restrictions have been placed on the application of the section in the definitions of "representative" and "person dealing with the company".

900 Included in the definition of "knowing", "knowingly" or "knows" in the Companies Act is where a person was in a position in which he reasonably ought to have –
i) had actual knowledge
ii) investigated the matter to an extent that would have provided the person with actual knowledge; or
iii) taken other measures which, if taken, would reasonably be expected to have provided the person with actual knowledge of the matter.

901 As the *Turquand* rule is a fairness rule, the third party should be *bona fide*. If the third party has subjectively been placed on his guard, then it would exclude his *bona fides*.

902 This subsection will only apply to instances where the requirement of, for example, a shareholders' resolution itself is also set out in the Act itself. Where the requirement of a prior approval by the shareholders is set out in, for example, the Memorandum of incorporation, the third party may assume that the procedures and formalities set out in the Act itself for the taking of the resolution was properly done, without the provisio that the deficiency may not be intentional or material.

903 See Ch 3, para 3.3.4.5 above.

904 See Ch 3, para 3.3.4.5 above.

905 This has been borrowed from s 40(2)(a) of the English Companies Act of 2006, which expelled the previous uncertainty as to what would constitute "dealing with" a company. See Ch 2, para 2.2.4.

(aa) the transaction or act is so unusual in respect of the normal business of the company so as to put a reasonable man in the position of the person dealing with the company on inquiry;

(bb) the act of the representative objectively falls outside the authority usually associated with the office that such representative holds in the company;[906] or

(cc) the company enters into a transaction or acts for purposes other than for purposes of its business.[907]

(iii) where the person dealing with a company is a company itself, it would, for purposes of subsection (3)(i) be regarded that the company had knowledge of the non-compliance if an officer or other official of such company had knowledge thereof and had a duty to communicate that knowledge to the company of which he is an officer or other official.

(7) The common-law *Turquand* rule, as applied to companies is hereby revoked.

20B Company estopped from denying authority of representative

(1) If a representation is made by words, acts or conduct or by silence, inaction or acquiesce to a representee that a representative has authority to act on behalf of a company or to enter into a particular transaction on behalf of a company, the company shall be estopped from denying the truth of such representation: Provided that the representee is able to prove that-[908]

(a) such representation was made or permitted to be made by a person or persons-

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906 This is a question of fact which should be answered with reference to the particular circumstances, including the nature of the business of the company, the trade usage and the position that the representative holds in the company. Also see Ch 2, para 2.2.2 and Ch 3, para 3.3.4.6 above.

907 See Ch 3, para 3.2.2.3 above.

908 The requirements as laid down in *NBS Bank Ltd v Cape Produce (Pty) Ltd* 2002 1 SA 396 [26] have been used here. See Ch 3, para 3.2.3 above.

(i) with actual authority to manage the business of the company either generally or in respect of a matter to which the transaction or act relates; or

(ii) whose authority to make such representation regarding the authority of a representative, the company is estopped from denying.

(b) the representation was in a form that the company should reasonably have expected to be acted upon by the representee;

(c) the representee was induced by the representation in relying thereon to deal with the representative;

(d) the reliance by the representee was reasonable; and

(e) as a consequence of such reliance, the representee has altered his or her position to his or her detriment.

(2) The representee shall not be entitled to rely on subsection (1) if, at the time of the act or transaction-

(a) the representee was actually aware[909] of the fact that the representative did not have the necessary authority to act on behalf of the company or to conclude the transaction on behalf of the company;[910] or

(b) the representee had, by virtue of his or her position with or relationship to the company, knowledge[911] of the fact that the representative did not have the necessary authority to act on behalf of the company or to conclude the transaction on behalf of the company.

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909 The word “knew” was purposely not used, as the definition of “knowing”, “knowingly” or “knows” in the Companies Act of 2006 is worded too widely. Only actual knowledge is meant here.

910 See Ch 3, para 3.2.3.4 above.

911 Knowledge, as defined on the Companies Act of 2008 here again as a wider meaning than just actual knowledge. This subsection disallows “insiders” to rely on estoppel where such insider had “knowledge”.

(3) In order to determine whether the reliance of the representee was reasonable as contemplated in subsection (1)(d), the following factors should be taken into account:

(a) whether the act of the representative objectively falls outside the authority usually associated with the office or purported office[912] that such representative holds in the company;[913]

(b) whether the transaction or act is so unusual or extraordinary in respect of the normal business of the company so as to put a reasonable man in the position of the representee on inquiry;[914]

(c) whether the company has entered into a transaction or acts for purposes other than for purposes of its business.[915]

(4) The common-law doctrine of estoppel and ostensible or apparent authority as applied to companies in an agency setting is hereby revoked.

## 4.6 Conclusion

The Companies Act of 2008 brought a new approach to South African law in so far as the authority of directors to act on behalf of a company is concerned. There are, however, still uncertainties regarding the intention of the legislature regarding the retention of the doctrine of constructive notice in respect of the so-called "RF" companies. The exact extent and application of section 20(7) of the Companies Act of 2008 is also unclear. Section 20(8) of the Companies Act further creates uncertainty as to how the common-law *Turquand* rule should be integrated with its statutory counterpart.

The whole section 20 of the Companies Act also intermingle the capacity of a company with the authority of the directors to act on behalf of the company which might give rise to confusion. These two concepts should rather be treated separately from one another.

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912 A representee should be entitled to rely on estoppel even if the representative of the company was never appointed by the company.

913 See Ch 3, para 3.2.3.4 above.

914 See Ch 3, para 3.2.3.4 above.

915 See Ch 3, para 3.2.2.3 above.

Amendments to the Companies Act of 2008 are necessary to provide clarity on the above uncertainties.

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## 6 OFFICIAL REPORTS AND PUBLICATIONS

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## 7 ABBREVIATIONS OF JOURNALS

| | |
|---|---|
| LQR | Law Quarterly Review |
| PELJ | Potchefstroom Electronic Law Journal |
| QUTLJ | Queensland University of Technology Law Journal |
| SALJ | South African Law Journal |
| SA Merc LJ | South African Mercantile law Journal |
| THRHR | Tydskrif vir Hedendaagse Romeins-Hollandse Reg (Journal of Contemporary Roman Dutch Law) |
| TSAR | Tydskrif vir die Suid-Afrikaanse Reg (Journal of South African Law) |
| UTLJ | The University of Toronto Law Journal |