no reasonable shareholder could consider the proposed amendment to be beneficial to the company. (For further discussion on this point see Williams (2007) 'Bona Fide in the Interest of Certainty', CLJ 500.)

Fourthly, where the rights of different classes of shareholders are contained in the articles, then, as noted above, s 33 would appear to permit these rights to be changed by way of a special resolution of the members of the company. However, this is another area in which the law aims to protect minorities within a company from the potential oppression of majority rule. As such, the general principle is that rights attaching to a class of shares should not be altered by the holders of another class of shares without gaining the consent of the class in question for the alteration to take place. This is covered by s 630 of the Companies Act 2006 which states that rights attached to a class of a company's shares may only be varied (a) in accordance with provision in the company's articles for the variation of those rights; or (b) where no such provision exists then by way of a special resolution passed at a separate general meeting of the holders of that class sanctioning the variation, or by consent in writing (s 630(2),(4)).

It should also be noted that according to s 633, the holders of not less than 15 per cent of the issued shares of the class, who did not vote for the variation, may apply to the court within 21 days of the consent of the class being given, whether in writing or by resolution, to have the variation cancelled. Once such an application has been made, usually by one or more dissentients on behalf of the others, the variation will not take effect unless and until it is confirmed by the court.

See p. 144

As will be examined further in Chapter 7, an issue which is frequently explored is whether the issue of further shares, which do not remove the current rights of a particular class but simply enjoy the same rights as the existing ones (effectively expanding the class and, as such, diluting the voting power of the original holders of that class of shares), may amount to a variation of class rights; ***White* v *Bristol Aeroplane Co Ltd*** [1953] Ch 65. This is also an area in which s 633 may prove useful to those shareholders who suddenly find their position diluted within a particular class and outvoted on a s 630 resolution.

Northern Counties Securities Ltd* v *Jackson & Steeple Ltd
[1974] 1 WLR 1133

The defendant company has agreed to use its best endeavours to allot a certain number of shares to the plaintiffs resulting from a Stock Exchange quotation for its shares. However, it was necessary for the company to gain consent via its General Meeting. After a period of inactivity the plaintiffs successfully gained an order from the court against the company. Nevertheless, the court emphasised that fact that even though a General Meeting must be called, together with a circular inviting members to support the resolution, the members could not be compelled to vote in favour of the resolution and would not be in contempt of court if they opposed it. Per Walton LJ:

> Mr Price argued that, in effect, there are two separate sets of persons in whom authority to activate the company itself resides. Quoting the well known passages from Viscount Haldane L.C. in ***Lennard's Carrying Co Ltd* v *Asiatic Petroleum Co Ltd*** [1915] AC 705, he submitted that the company as such was only a juristic figment of the imagination, lacking both a body to be kicked and a soul to be damned. From this it followed that there must be some one or more human persons who did, as a matter of fact, act on behalf of the company, and whose acts therefore must, for all practical purposes, be the acts of the company itself. The first of such bodies was clearly the body of directors, to whom under most forms of articles – see article 80 of Table A, or article 86 of the defendant company's articles which is in similar form – the management of the business of the company is expressly delegated. Therefore, their acts are the defendant company's acts; and if they do not, in the

present instance, cause the defendant company to comply with the undertakings given by it to the court, they are themselves liable for contempt of court. And this, he says, is well recognised: see RSC, Ord. 45, r 5 (1), whereunder disobedience by a corporation to an injunction may result directly in the issue of a writ of sequestration against any director thereof. It is of course clear that for this purpose there is no distinction between an undertaking and an injunction: see note 45/5/3 in *The Supreme Court Practice* (1973).

This is, indeed, all well established law, with which Mr Instone did not quarrel, and which indeed his first proposition asserted. But, continues Mr Price, this is only half of the story. There are some matters in relation to which the directors are not competent to act on behalf of the company. The relevant authority being 'the company in general meeting', that is to say, a meeting of the members. Thus in respect of all matters within the competence – at any rate those within the exclusive competence – of a meeting of the members, the acts of the members are the acts of the company, in precisely the same way as the acts of the directors are the acts of the company. Ergo, for any shareholder to vote against a resolution to issue the shares here in question to the plaintiffs would be a contempt of court, as it would be a step taken by him knowingly which would prevent the defendant company from fulfilling its undertaking to the court. Mr Price admitted that he could find no authority which directly assisted his argument, but equally confidently asserted that there was no authority which precluded it.

Mr Instone indicted Mr Price's argument as being based upon 'a nominalistic fallacy'. His precise proposition was formulated as follows: 'While directors have special responsibilities as executive agents of the defendant company to ensure that the company does not commit a contempt of court, a shareholder, when the position has been put before the shareholders generally, who chooses to vote against such approval will not himself be in contempt of court' . . .

In my judgment, these submissions of Mr Instone are correct. I think that, in a nutshell, the distinction is this: when a director votes as a director for or against any particular resolution in a director's meeting, he is voting as a person under a fiduciary duty to the company for the proposition that the company should take a certain course of action. When a shareholder is voting for or against a particular resolution he is voting as a person owing no fiduciary duty to the company and who is exercising his own right of property, to vote as he thinks fit. The fact that the result of the voting at the meeting (or at a subsequent poll) will bind the company cannot affect the position that, in voting, he is voting simply in exercise of his own property rights.

Perhaps another (and simpler) way of putting the matter is that a director is an argent, who casts his vote to decide in what manner his principal shall act through the collective agency of the board of directors; a shareholder who casts his vote in general meeting is not casting it as an agent of the company in any shape or form. His act therefore, in voting as he pleases, cannot in any way be regarded as an act of the company . . .

I now come to paragraph 4 of the notice of motion, which seeks an order restraining the individual respondents and each of them from voting against the resolution. Mr Price says that, as the executive agents of the defendant company, they are bound to recommend to its shareholders that they vote in favour of the resolution to issue the shares, and hence, at the least, they cannot themselves vote against it, for they would thereby be assisting the defendant company to do that which it is their duty to secure does not happen. If, as executive officers of the defendant company, they are bound to procure a certain result if at all possible, how can they, as individuals, seek to frustrate that result?

I regret, however, that I am unable to accede to Mr Price's arguments in this respect . . . I think that a director who has fulfilled his duty as a director of a company, by causing it to comply with an undertaking binding upon it is nevertheless free, as an individual shareholder, to enjoy the same unfettered and unrestricted right of voting at general meetings of the members of the company as he would have if he were not also a director.

It is also worth bearing in mind the fact that a shareholder may have agreed to vote subject to certain restrictions and/or guidelines contained in a separate contract. If this is the case then the agreement is binding on the member and may be enforced by way of an injunction.

Puddephatt* v *Leith [1916] 1 Ch 200

The case involved the transaction of a loan of 2,500 *l* the payment of which, with interest at the rate of 5½ per cent per annum, was secured to the defendant by an agreement under seal dated 14 February 1913, whereby the plaintiff transferred to the defendant by way of mortgage 2,500 fully-paid shares of 1 *l* each in a company called the London and Cosmopolitan Mining Company, Limited. That mortgage was preceded by a collateral agreement which took the form of a letter addressed by the defendant to the plaintiff in which the defendant said that the plaintiff's voting rights in virtue of the shares held in mortgage by him during the period of the loan would be untouched though the shares would be in his name and his voice might give the vote; that he would give no such vote without consulting the plaintiff; and that he would vote in all cases where a vote was necessary in respect of those shares as the plaintiff wished him to do. A general meeting of the company was approaching, and the defendant threatened to vote as he thought fit in respect of the shares and to disregard, as he had done once before, the plaintiff's expressed wishes on this subject. As such, the plaintiff commenced this action in the Chancery Division claiming an injunction to restrain the defendant from voting upon a poll at any meeting of the company in respect of the 2,500 shares otherwise than in accordance with her directions. Per Sargent J:

> In my opinion, therefore, the right of the plaintiff is clear, and the only remaining question is whether she is entitled to a mandatory injunction to enforce her right. It is not disputed that she is entitled to a prohibitive injunction, and in my opinion she is also entitled to a mandatory injunction. Prima facie this court is bound . . . to give effect to a clear right by way of a mandatory injunction. There are no doubt certain exceptions from this rule, as in the case of a contract of service, because in such cases, it is impossible for the court to make its order effective, but . . . in the present case, in as much as there is one definitive thing to be done, about the mode of doing which there can be no possible doubt, I am of the opinion that I ought to grant not only the prohibitive but also the mandatory injunction claimed by the plaintiff, and I make an order accordingly.

Held – The Court ordered the defendant to comply with the undertaking.

Breaches of contract arising out of alteration of the articles

A company cannot by altering its articles escape liability for breach of a contract into which it has entered. The difficulty has arisen with regard to the remedies of the other party to the contract. In ***Punt*** v ***Symons & Co Ltd*** [1903] 2 Ch 506 it was said that the other party to the contract could sue the company for damages for breach, but could not obtain an injunction to prevent the alteration taking effect. Then followed a series of cases which revealed considerable judicial indecision on this point. For example, in ***Baily*** v ***British Equitable Assurance Co Ltd*** [1904] 1 Ch 374 the Court of Appeal seems to have been prepared to grant an injunction to restrain an alteration of the articles in breach of contract although in fact it was only asked to give a declaratory judgment as to the state of the law. However, in ***Southern Foundries*** v ***Shirlaw***, 1940 (below), Lord Porter in an obiter dictum gave support to the view that the other party to the contract can sue the company for damages only, and cannot obtain an injunction to prevent the alteration from taking effect. It may be said, therefore, that a company is quite free to alter its articles, though if in doing so it breaks a contract which it has made, it must face an action in damages by the party aggrieved. There may also be an action against those who voted for the alteration.

Southern Foundries (1926) Ltd* v *Shirlaw [1940] AC 701

The appellant company was incorporated in 1926 as a private company, and was engaged in the business of iron founders. The respondent, Shirlaw, became a director of the company in 1929 under a provision in the articles. In 1933 he became managing director under a separate contract, the appointment to be for 10 years, and containing restraints under which Shirlaw agreed that he would not, for a period of three years after leaving the employment of the appellants, engage in foundry work within 100 miles of Croydon. In 1935 there was a merger between the appellant company and ten other concerns, and the group was called Federated Industries. The members of the group agreed that they should make certain alterations in their articles regarding directors; the articles of each member were altered, and in their new form gave Federated Industries power to remove any director of the company, and also stipulated that a managing director should cease to hold office if he ceased to be a director. In 1937 Shirlaw was removed from office as a director, under the provision in the articles, by an instrument in writing, signed by two directors and the secretary of Federated Industries. This meant that Shirlaw could no longer be managing director of Southern Foundries, and since his contract had still some time to run, he brought this action for wrongful dismissal. The trial judge found for Shirlaw and awarded him £12,000 damages, and the Court of Appeal affirmed that decision. The company now appealed to the House of Lords.

Held – by a majority – that Shirlaw's contract as managing director contained an implied term that the article making him a director would not be altered. Since it had been altered, there was a breach of contract and the company was liable for it. Lord Wright took the view that since there was no privity of contract between Shirlaw and Federated Industries, it was difficult to see how they could dismiss him. Lord Romer, dissenting, did not think a term against alteration of the articles could be implied and thought that Shirlaw took the risk of alteration. Lord Porter lent support in this case to ***Punt* v *Symons***, 1903, and said that a company could not be prevented by injunction from altering its articles but that the only remedy for an alteration which has caused a breach of contract was damages.

Comment

(i) From statements made in this case it appears that any member who votes for the alteration will also be liable to the claimant for inducing the company to break its contract if the inevitable consequence of the alteration is that the contract will be broken.

(ii) In ***Shirlaw*** the articles said that a managing director was to be subject to the same provisions for removal as any other director 'subject to the provisions of any contract between him and the company'. There was an implied term in the contract of service which overrode the power of removal without compensation in the articles.

(iii) In ***Nelson* v *James Nelson & Sons Ltd*** [1914] 2 KB 770 a service contract appointing the claimant to act as managing director 'so long as he shall remain a director of the company' was also held to override an article giving a power of removal without compensation. Damages were awarded to the claimant because his contract was terminated by his removal from office as a director. That was a breach by the company of his contract as managing director which he could then no longer perform.

The position is different where a person contracts with a company and the contract incorporates a provision of the articles by implication. In such a case the other party is deemed to know that the company may alter its articles, and therefore takes the risk of the contract failing because of such an alteration, even to the extent of failing in an action for damages (***Shuttleworth* v *Cox Bros & Co (Maidenhead) Ltd***, 1927, see above). However, there are certain limitations upon the above rule:

(a) Rights which have already accrued under the contract cannot be disturbed by the alteration.

Swabey* v *Port Darwin Gold Mining Co (1889) 1 Meg 385

Swabey had served the company as a director under a provision in the company's articles which provided for his salary. The articles were altered so as to reduce that salary and it was *held* – by the Court of Appeal – that, although the alteration was effective to reduce the salary for the future, Swabey could not be deprived of his salary at the original figure for the period he had served prior to the alteration of the articles. Lord Esher MR stated:

> The articles do not themselves form a contract, but from them you get the terms upon which the directors are serving. It would be absurd to hold that one of the parties to a contract could alter it as to service already performed under it. The company has power to alter the articles, but the directors would be entitled to their salary at the rate originally stated in the articles up to the time the articles were altered.

(b) It is felt that the obligations of the other party cannot be made more onerous by an alteration of the articles. Thus, if the articles appoint a director to serve for a period of years on a part-time basis, he cannot be required to give his full time to the company by the company altering its articles so as to require him to do so.

(c) As we have already seen, where the company has shares of more than one class, it cannot vary the rights of a class of shares merely by altering them in the memorandum or articles. Section 630 applies and requires the consent of three-quarters of the class and there are dissentient rights.

Alteration of the articles by the court

As discussed above, the articles are a contract between the company and each member and in this connection the court has power to rectify contracts. For example, if parties have agreed for a lease of land for 25 years that is written down in the lease by mistake as 21 years then if one of the parties is not prepared to co-operate in changing this provision of the lease the court can be asked to rectify the lease by an order inserting 25 years as the term of the lease provided the evidence shows to the satisfaction of the court that this was the intention of the parties. The court has ruled however that it does not have power to rectify the statutory contract set out in the articles.

Scott* v *Frank F Scott (London) Ltd [1940] Ch 794

The defendant company was a private company with three members, Frank, Stuart and Reginald Scott, the business of the company being that of butchers. On the death of Frank Scott, his widow, Marie Scott, became entitled under his will to certain preference shares and ordinary shares in the company, as executrix. When she sought to be registered in respect of the shares, Stuart and Reginald Scott claimed that under a provision in the articles the shares must on the death of a member be offered to the other members at par, but the article was not so well drafted as to make this clear beyond doubt. This action was brought to interpret the article, and also to ask the court to rectify the article to carry a right to pre-emption if the article was not so drafted as to achieve this.

Held – by the Court of Appeal – that the article did give the right of pre-emption claimed by Stuart and Reginald Scott. However, if it had not done so, the court could not have rectified it; the alteration could only be carried out by special resolution.

However, the High Court departed from this general ruling when faced with an absurd result of bad drafting.

Folkes Group plc* v *Alexander [2002] 2 BCLC 254

The Folkes family held a substantial proportion of the voting shares in the listed plc. The other shareholders had no voting rights unless the Folkes family holdings fell below 40 per cent. An article to ensure that this could never happen was drafted and agreed and became part of the articles. Later it was noticed that certain holdings of the Folkes family were excluded from the voting category so that their voting holdings fell to 23.9 per cent, thus triggering the voting rights of the other members. The former non-voting shares would not use their newly acquired voting power to change the articles to what was originally intended. The court did however do so by ordering the insertion of five words into the altered article to give it the effect intended. The judge's justification was that to leave the article as it was would flout business common sense and legal decisions might on occasion have to yield to business common sense following comments in the House of Lords in ***Investors Compensation Scheme Ltd* v *West Bromwich Building Society*** [1998] 1 BCLC 493.

Essay questions

1 Describe the procedure for alteration of articles and detail the considerations made in determining the validity of the alteration. (*The Institute of Company Accountants*)

2 H plc wishes to change its articles of association to add a clause which states 'any director of the company may be removed from office if all other directors give notice in writing of their desire that the named directors be so removed'.

You are required to explain the procedure for alteration and discuss the difficulties the company might encounter in adding this new clause.

(*The Chartered Institute of Management Accountants*)

3 Free Range Chickens R Us wishes to change its articles of association to add a clause which would state that 'any director of the company may be removed from office if all other directors give notice in writing of their desire that the named directors be so removed'.

You are required to explain the procedure for alteration and discuss the difficulties which the company might encounter in adding this new clause. (*Authors' question*)

4 Perfect Puddings Ltd was incorporated to purchase the chocolate manufacturing business previously carried on by Louise. The contract of sale between the company and Louise provided, inter alia, that as long as Louise held 20 per cent of the shares of Perfect Puddings, she was entitled to be managing director of the company. The Articles of Association which otherwise follow Table A reproduce this provision and also contain the following:

> *David shall be entitled to be the company's deputy managing director for life. On any resolution to remove him from office, the shares held by him shall carry three votes per share.*

Louise, David, George, John and Claire each hold 20 per cent of the issued share capital of Perfect Puddings and George as well as Louise and David are the directors. Louise and David wish to develop a new product, but George, John and Claire are opposed to this. At a forthcoming meeting, George, John and Claire are planning to propose a resolution to remove Louise and David from their directorships.

Advise Louise and David. (*University of Hertfordshire*)

Suggested further reading

Drury, 'The Relative Nature of a Shareholder's Right to Enforce the Company Contract', (1986) CLJ 219

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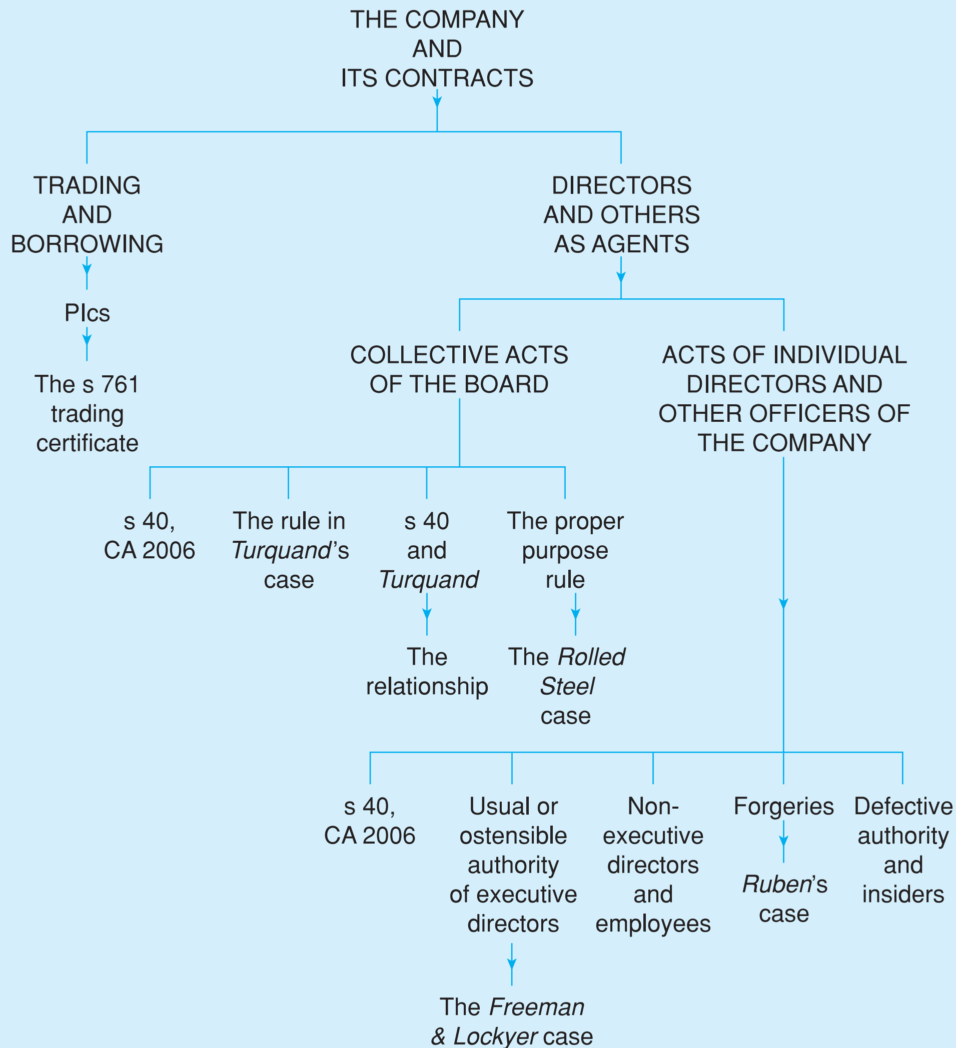
6 The company and its contracts



A company necessarily contracts through agents such as its directors and other officers, and senior employees. This chapter is, in the main, concerned with the problems which can arise when these agents enter into transactions which they are not authorised to make or use their powers for an improper purpose, or exercise them by irregular procedures. First, however, this is an appropriate place to deal with transactions entered into by public companies before receipt of a s 761 certificate from the Registrar.

Public companies and the s 761 certificate

Under s 761 a public company, registered as such on its initial incorporation, cannot commence business or exercise any borrowing powers unless the Registrar has issued what is known as a s 761 trading certificate. A private company does not require such a certificate.

The trading certificate will be issued when the Registrar is satisfied that the nominal value of the company's allotted share capital is at least £50,000 (s 763) and not less than one-quarter of the nominal value of each issued share in the company plus the whole of any premium on such shares has been received by the company, whether in cash or otherwise. A share allotted in pursuance of an employees' share scheme may not be taken into account in determining the nominal value of the company's allotted share capital unless it is paid up at least as to one-quarter of the nominal value of the share and the whole of any premium on the share.

In order to obtain a s 761 certificate, the company must file with the Registrar a statement of compliance and application specifying the following items as detailed in s 762:

(a) that the nominal value of the company's allotted share capital is not less than the authorised minimum;
(b) the amount, or estimated amount, of the preliminary expenses of the company and the persons by whom any of those expenses have been paid or are payable; and
(c) any amount or benefit paid or given or intended to be paid or given to any promoter of the company and the consideration for the payment or benefit.

The object of the ss 761–762 provisions is to ensure that a plc has some significant starting capital. The disclosure of preliminary expenses and promoter payments is required because if these are large and paid from the initial capital, then the provision for a significant initial capital is defeated.

When a trading certificate is issued it is conclusive evidence that the company is entitled to commence business and exercise borrowing powers (s 761(4)). Failure to comply with s 761 may, according to s 767, result in a fine on the company and any officer in default.

If a public company has not obtained a s 761 certificate within a year of registration, the Secretary of State for Trade and Industry may present a petition to the court to wind it up.

If a company does commence business or borrow without a s 761 certificate, transactions with traders and lenders are nevertheless enforceable against the company. However, if the company cannot meet its obligations in terms of payment of a debt or repayment of a loan incurred during the period of unlawful trading, within 21 days of being called upon to do so, the directors of the company are jointly and severally liable to indemnify the trader or lender in respect of his loss resulting from the company's failure to meet its obligations. Therefore, s 767(3) leaves the company liable and the directors become personally liable if

the company does not pay, as where it goes into insolvent liquidation without discharging its liability on a transaction.

Directors and others as agents

See p. 78

If the board acting together (that is collectively), or one director or other officer of the company acting on his own, has actual authority to make a particular contract on behalf of the company, and that contract is within the company's powers (or if not the transaction is protected by s 39 – see Chapter 3), then the contract, when made, will be binding on the company. However, where the directors act together, or as individuals, beyond their authority the position for them and other officers is as set out below.

Collective acts of the board

(a) The Companies Act 2006

See p. 334

Section 40(1) provides that in favour of a person dealing with the company in good faith, the power of the board of directors to bind the company or authorise others to do so shall be deemed free of any limitation under the company's constitution (see further Chapter 17), and a person shall not be regarded as acting in bad faith just because he knows that an act is beyond the powers of the directors (s 40(2)(b)). In addition, under s 40(2)(b) there is no duty to enquire as to the directors' authority and there is no constructive notice of any provision of the company's constitution limiting authority. Therefore, provided the above requirements are met, a transaction entered into by the board beyond its powers will bind the company. This applies not only where the directors are acting beyond their powers but also where they are within their powers but have failed to observe proper internal procedures.

TCB v Gray [1987] 3 WLR 1144

A company issued a debenture to secure a loan. The transaction was within the company's powers and within the authority of the board. The debenture was issued under the company's seal. On this the articles of the company said 'every instrument to which the seal shall be affixed shall be signed by a director'. In this case it was signed by a solicitor to whom one of the directors had given a power of attorney to act as his agent. The question of the validity of the debenture arose and the court held that it was valid under s 35A which protected not only against lack of authority but also against the use of incorrect procedures.

In addition, it will be noted that the section deals with a situation where the directors authorise other persons to make contracts on behalf of the company. This is to overcome the common law rule that a company can only act through organs of the company. At common law the board of directors is an organ of the company but only if acting collectively. Section 40(1) overcomes this by making it clear that an act done by a person authorised by the board is in effect an act of the board and therefore an act by an organ of the company. For example, if the board authorises the company's purchasing officer to buy materials from outsiders for use in the company's manufacturing process, each purchase within the officer's authority will

be a transaction decided upon by the directors and therefore a transaction decided upon by a common law organ of the company. There is no longer an assumption as in previous legislation that all commercial decisions are made at boardroom level. If, therefore, the board collectively makes a decision and enters into a transaction which is beyond its powers, s 40 will make the transaction enforceable, and the same is true if an individual authorised by the board exceeds the powers of the directors by a contract which he as an authorised individual has made.

Good faith. Under s 40(2)(b) a person is to be regarded as acting in good faith unless the contrary is proved. Thus the burden of proof will be on the company if it wishes to avoid a transaction on the 'bad faith' ground.

Member injunctions. A member of a company is not prevented by s 40 from asking the court for an injunction to stop the directors from acting beyond their powers, but this cannot be done if the transaction has been entered into (see s 40(4)).

Director liability. The directors are liable to compensate the company as they always have been if they cause the company loss by acting outside their powers (s 40(5)).

Section 40: use by shareholders. The section has been viewed as essentially an outsider's protection as where a creditor relies on the section to validate a contract entered into by the directors without authority. However, in the following case it was held to be available to shareholders in regard to a disputed issue of bonus shares.

EIC Services Ltd v *Phipps* [2003] 3 All ER 804

A shareholder in the company challenged a bonus issue of shares that it had made by capitalising the sum standing to the credit of its share premium account because, if his claim had succeeded, he would have owned a substantially greater proportion of the company. The challenge was based upon the company's articles which provided that the bonus shares should be applied in proportion to the amounts paid up on the shares and following an ordinary resolution of the members. The contention was that a very substantial number of the bonus shares were issued to shareholders whose shares were not paid up and that no resolution of members was passed but only a resolution of the board. The High Court ruled, however, that the bonus issue was enforceable. The relevant shareholders were entitled to rely on the CA 1985, s 35A (now s 40 of the Companies Act 2006) which provides that, in favour of a person dealing with the company in good faith, the power of the board of directors to bind the company or authorise others to do so shall be deemed free of any limitation under the company's constitution, e.g. its articles. Regarding the fact that certain of the recipients of the bonus shares were directors, the judge referred to the further provisions of what is now s 40 which state that a person shall not be regarded as acting in bad faith because he knows that the act is beyond the powers of the directors. The judge felt that they did not know that the issue of the bonus shares was beyond their powers, though as directors they should have done. In any case, the judge felt that they had acted in good faith. The issue of all the bonus shares was therefore valid.

Comment

The issue was also challenged on the ground that the directors made it under a misapprehension of their powers. The contract for the shares, therefore, was void at common law for operative mistake. The court rejected this on the grounds that the mistake was not sufficiently fundamental to avoid the contract.

Section 40: use by directors. Section 40 states that it applies 'in favour of a person dealing with the company in good faith'. The matter of whether a director could claim to be included in the word 'person' arose in the following case.

Smith* v *Henniker-Major & Co (a Firm) [2002] All ER (D) 310 (Jul)

A director of a company who was in dispute with the other directors wished to bring a claim by the company against the defendant solicitors. The company was not pursuing the claim. The director, believing that he had power under the company's articles, acted alone and, without a quorate board meeting, made an agreement as agent of the company under which the company's claim against the solicitors was assigned to him personally. The assignment was later ratified by deed, presumably to prevent a ruling that the assignment was ineffective as lacking consideration. On the issue of the authority of the director to make the assignment for the company, the solicitors contended that since the company's board did not hold a quorate meeting the assignment was invalid and ineffective, so the claimant's case against them should not proceed. On the question whether a director of the company could claim to be included in the word 'person' in what is now s 40, the majority of the Court of Appeal said no. The words were wide enough to cover a director but not in this case. The claimant, Mr Smith, was the chairman of the company and it was his duty to see that the company's constitution was adhered to. The articles did not permit him to turn himself into a one-man board and he could not rely on his own error as to the company's constitution to validate a transaction with himself. His appeal against a decision striking out his claim against the defendants was dismissed.

Comment

It may be that a director not so senior as Mr Smith but, say, a more junior director – perhaps only recently appointed – might have succeeded. The decision does not rule this out.

(b) The rule in *Turquand*'s case: the indoor management rule

This rule is best explained by looking straightaway at the facts of the case (below).

Royal British Bank* v *Turquand (1856) 6 E & B 327

The claimant bank lent £2,000 to a joint stock company called Cameron's Coalbrook Steam Coal & Swansea and London Railway Company, which was at the time of the action in course of winding-up. Turquand was the general manager of the company and was brought into the action to represent it. The company had issued a bond under its common seal, signed by two directors, agreeing to repay the loan. The registered deed of settlement of the company (which corresponded to the articles of a modern company) provided that the directors might borrow on bond such sums as they should be authorised by a general resolution of the members of the company to borrow. In the case of this loan it appeared that no such resolution had been passed.

Held – by the Court of Exchequer – that the bond was nevertheless binding on the company, because the lenders were entitled to assume that a resolution authorising the borrowing had been passed. There was no need to go indoors the management to make active enquiries.

Comment

This case succeeded because the ordinary resolution involved did not have to be filed with the Registrar of Companies. Therefore, there was no constructive notice of it. During the period when there was constructive notice of a company's memorandum and articles and the contents of its

file at the Registry, it was decided that ***Turquand*** could not apply where the resolution required was a special or extraordinary resolution because these have to be filed and an outsider would have constructive notice that they had not been. The relevant decision is ***Irvine*** v ***Union Bank of Australia*** (1877) 2 App Cas 366.

Since the enactment of the Companies Act 2006, s 40 and the abolition of constructive notice, the importance of the rule in ***Turquand***'s case should now be diminished.

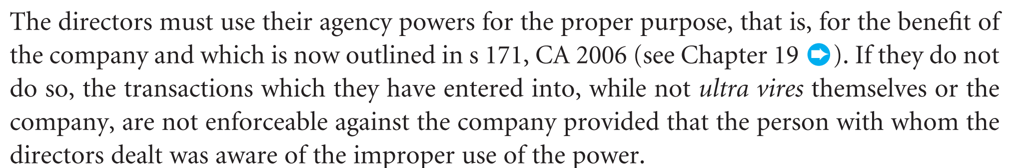
(c) The relationship between s 40 and the rule in *Turquand*'s case

Section 40 gives the same protection as ***Turquand*** in regard to unauthorised collective acts of the board and also where correct internal procedures were not followed as in ***TCB*** v ***Gray***, 1987 (above).

While one could argue that ***Turquand***'s case would appear to be wider than s 35A under the Companies Act 1985, because it applied to make a transaction by the company enforceable against it in ***Mahoney*** v ***East Holyford Mining Co*** (1875) LR 7 HL 869, where the directors who made the transaction had never been appointed at all, and again in ***Davis*** v ***R Bolton & Co*** [1894] 3 Ch 678 the rule was applied where the directors made a transfer of shares without a quorum at the meeting. The transfer was nevertheless held to be valid. This position has now been affected by the new wording of s 40 (Companies Act 2006), which refers to any 'limitation under the *company's constitution*' on the power of the board to bind the company.

Although s 40 has not been fully interpreted by the courts, it seems logical to suppose that it would not apply in the circumstances of either ***Mahoney*** or ***Davis*** because the court will presumably expect that when an English statute says 'the power of the directors to bind the company' it means directors who are properly appointed and have a quorum at the relevant meeting. Until s 40 has been more fully interpreted, it is perhaps safer to assume that ***Turquand***'s case still has a role to play.

(d) The proper purpose rule

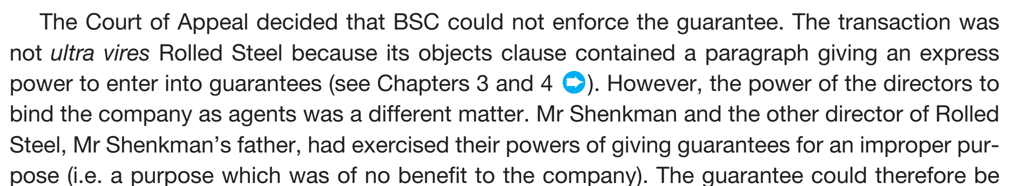


See p. 379

The directors must use their agency powers for the proper purpose, that is, for the benefit of the company and which is now outlined in s 171, CA 2006 (see Chapter 19). If they do not do so, the transactions which they have entered into, while not *ultra vires* themselves or the company, are not enforceable against the company provided that the person with whom the directors dealt was aware of the improper use of the power.

Rolled Steel Products (Holdings) Ltd **v** ***British Steel Corporation***
[1985] 2 WLR 908

A Mr Shenkman was a 51 per cent shareholder and director in Rolled Steel and held all the issued share capital in another company called Scottish Steel of which he was also a director. Scottish Steel owed a lot of money to BSC and Mr Shenkman had given his personal guarantee of that debt. Later BSC wanted more security and Mr S caused Rolled Steel to enter into a guarantee of the Scottish Steel debt. There was no benefit to Rolled Steel in this and BSC knew there was not.



See p. 79

The Court of Appeal decided that BSC could not enforce the guarantee. The transaction was not *ultra vires* Rolled Steel because its objects clause contained a paragraph giving an express power to enter into guarantees (see Chapters 3 and 4). However, the power of the directors to bind the company as agents was a different matter. Mr Shenkman and the other director of Rolled Steel, Mr Shenkman's father, had exercised their powers of giving guarantees for an improper purpose (i.e. a purpose which was of no benefit to the company). The guarantee could therefore be

avoided by the liquidator of Rolled Steel provided that those to whom it was given were aware of the improper purpose. Since BSC knew that there was no benefit to Rolled Steel in the guarantee, it could not enforce the guarantee and prove in the liquidation.

Comment

(i) If BSC had not been on notice of the circumstances in which Rolled Steel had been made to enter into the guarantee, it could have claimed in the liquidation.

(ii) It should be noted that if the members of Rolled Steel had passed an ordinary resolution ratifying the making of the guarantee, then it would have been enforceable against the company. Where the directors act for an improper purpose, this can be put right by an ordinary resolution of the members even if, as here, the 'wrongdoer' can himself obtain an ordinary resolution. This would not apply if the 'wrongdoer' acted fraudulently, which was not the case here.

Acts of individual directors and other officers of the company

We must now consider the extent to which a company will be bound by a transaction entered into by an individual director or other officer, e.g. the company secretary, who has no actual authority to enter into it. There are the following possibilities:

(a) The Companies Act 2006

As we have seen, s 40 states that in favour of a person dealing with a company in good faith the power of the directors to authorise other persons to bind the company shall be regarded as free from any limitation under the company's constitution. Therefore, an individual director, company secretary, employee or other agent, authorised by the directors to bind the company, will do so even if he exceeds the powers given to the board itself or other agents of the company by the articles. Once again, knowledge of the lack of power in the individual making the transaction on behalf of the company is not bad faith and does not prevent the transaction from binding the company.

(b) The rules of agency: the doctrine of holding out

Where a director or other officer of a company has no actual authority, or authorisation under s 40, an outsider may be able to regard a transaction entered into by such an individual as binding on the company if the person with whom he negotiated was held out by the company as having authority to enter into it, in regard to all commercial activities relating to the running of the business.

Since it is usual to delegate wide powers to a managing director and other executive directors, and Table A (replaced by the new Model Articles in newly incorporated companies) allows the board to delegate widely to such persons, an outsider will normally be protected and the transaction will bind the company if he has dealt with a managing director or other executive director (e.g. a sales director) or other officer (e.g. the company secretary) and this applies even if the person concerned has not actually been appointed to the post.

Freeman & Lockyer* v *Buckhurst Park Properties Ltd [1964] 1 All ER 630

A Mr Kapoor carried on a business as a property developer, and entered into a contract to buy an estate called Buckhurst Park at Sunninghill. He did not have enough money to pay for it, and obtained financial assistance from a Mr Hoon. They formed a limited company with a share capital

of £70,000, subscribed equally by Kapoor and Hoon, to buy the estate with a view to selling it for development. Kapoor and Hoon, together with two other persons, comprised the board of directors. The quorum of the board was four, and Hoon was at all material times abroad. There was a power under the articles to appoint a managing director but this was never done. Kapoor, to the knowledge of the board, acted as if he were managing director in relation to finding a purchaser for the estate; and again, without express authority of the board but with its knowledge, he employed on behalf of the company a firm of architects and surveyors, the claimants in this case, for the submission of an application for planning permission which involved preparing plans and defining the estate boundaries. The claimants now claimed from the company the fees for the work done, and the company's defence was that Kapoor had no authority to act for the company. The Court of Appeal found that the company was liable, and Diplock LJ said that four conditions must be fulfilled before a third party was entitled to enforce against a company a contract entered into on its behalf by an agent without actual authority to make it:

(a) A representation must be made to the third party that the agent had authority. This condition was satisfied here because the board knew that Kapoor was making the contract as managing director but did not stop him.
(b) The representation must be made by the persons who have actual authority to manage the company. This condition was satisfied because the articles conferred full powers of management on the board.
(c) The third party must have been induced to make the contract because of the representation. This condition was satisfied because the claimants relied on Kapoor's authority and thought they were dealing with the company.
(d) Under the memorandum and articles the company is not deprived of the capacity either to make a contract of the kind made or to delegate authority to an agent to make the contract. This condition was satisfied because the articles allowed the board to delegate any of its functions of management to a managing director or a single director.

The court also decided that although the claimants had not looked at the articles, this did not matter: for the rule does not depend upon estoppel arising out of a document, but on estoppel by representation.

Hely-Hutchinson* v *Brayhead [1968] 1 QB 549

Under the articles of the company the directors were empowered to decide who should draw bills of exchange on behalf of the company. A Mr Clarke, who was the Manchester branch manager of Schenkers, drew bills of exchange on the company's behalf in favour of Kreditbank. He had no authority to do so. The court later held that the bills were not binding on the company because it was, on the evidence, unusual for a branch manager.

Richards, the chairman of the defendant company, Brayhead, acted as its de facto managing director. He was the chief executive who made the final decision on any matters concerning finance. He often committed the company to contracts without the knowledge of the board and reported the matter afterwards. The board knew of and acquiesced in that. In July 1964 the plaintiff, the chairman and managing director of a public company, Perdio, gave a personal guarantee to bankers for a loan of £50,000 to Perdio. Towards the end of 1964 Perdio was sustaining losses and needed financial assistance. Brayhead was prepared to help, with the intention eventually to obtain control of Perdio. In January 1965 Brayhead bought 750,000 Perdio ordinary shares from the plaintiff for over £100,000 and proposed to inject £150,000 into Perdio. About the same time the plaintiff became a director of Brayhead, but did not attend any board meetings until 19 May 1965. After that meeting, in an office outside, in a discussion between Richards and the plaintiff, the

plaintiff agreed to put more money into Perdio if Brayhead would secure his position. To that end Richards, on behalf of Brayhead, as chairman signed two letters on Brayhead's paper dated 19 May 1965, and addressed to the plaintiff. In one Brayhead purported to indemnify the plaintiff against loss on his personal guarantee of £50,000 and in the other Brayhead purported to guarantee to repay money lent by the plaintiff personally to Perdio. In reliance on those letters the plaintiff advanced £45,000 to Perdio.

Article 99 of Brayhead's articles of association provided that 'A director may contract with and be interested in any contract . . . with the company . . . and shall not be liable to account for any profit made by him by reason of any such contract . . . provided that the nature of the interest of the director in such contract . . . be declared at a meeting of the directors as required by . . . section 199 of the Companies Act, 1948', but no disclosure of the two contracts was in fact made to the board.

Despite the plaintiff's and other advances by Brayhead, Perdio's financial position remained hopeless and it went into liquidation. The plaintiff was called on to honour his guarantee. He paid the bankers £50,000 and claimed that sum and the £45,000 lent to Perdio, from Brayhead. Brayhead denied liability contending that Richards had no authority to sign the letters, alternatively, that since the plaintiff had not disclosed his interest in the contracts as required by article 99 of Brayhead's articles of association and section 199 of the Companies Act 1948, the contracts were unenforceable.

Roskill J held that although Richards had no actual authority to enter into contracts, he had ostensible or apparent authority to do so; that the plaintiff's breach of article 99 of Brayhead's articles of association and section 199 of the Act of 1948, only rendered the contracts voidable, not void or unenforceable; and that the plaintiff was entitled to recover.

On appeal, Denning MR stated:

> I need not consider at length the law on the authority of an agent, actual, apparent, or ostensible. That has been done in the judgments of this court in ***Freeman & Lockyer*** v ***Buckhurst Park Properties (Mangal) Ltd***. It is there shown that actual authority may be express or implied. It is *express* when it is given by express words, such as when a board of directors pass a resolution which authorises two of their number to sign cheques. It 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 appoint one of their number to be managing director. They thereby impliedly authorise him to do all such things as fall within the usual scope of that office. Actual authority, express or implied, is binding as between the company and the agent, and also as between the company and others, whether they are within the company or outside it.
>
> Ostensible or apparent authority is the authority of an agent as it *appears* to others. It 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 scope of that office. Other people who see him acting as managing director are entitled to assume that he has the usual authority of a managing director. But sometimes ostensible authority exceeds actual authority. For instance, when the board appoint the managing director, they may expressly limit his authority by saying he is not to order goods worth more than £500 without the sanction of the board. In that case his actual authority is subject to the £500 limitation, but his *ostensible* authority includes all the usual authority of a managing director. The company is bound by his ostensible authority in his dealings with those who do not know of the limitation. He may himself do the 'holding-out'. Thus, if he orders goods worth £1,000 and signs himself 'Managing Director for and on behalf of the company', the company is bound to the other party who does not know of the £500 limitation, see ***British Thomson-Houston Co Ltd*** v ***Federated European Bank Ltd***, which was quoted for this purpose by Pearson LJ in ***Freeman & Lockyer***. Even if the other party happens himself to be a director of the company, nevertheless the company may be bound by the ostensible authority. Suppose the managing director orders £1,000 worth of goods from a new director who has just joined the company and does not know of the £500 limitation, not having studied the minute

> book, the company may yet be bound. Lord Simonds in ***Morris* v *Kanssen***, envisaged that sort of case, which was considered by Roskill J in the present case.
>
> Apply these principles here. It is plain that Mr Richards had no express authority to enter into these two contracts an behalf of the company: nor had he any such authority implied from the nature of his office. He had been duly appointed chairman of the company but that office in itself did not carry with it authority to enter into these contracts without the sanction of the board. But I think he had authority implied from the conduct of the parties and the circumstances of the case. The judge did not rest his decision on implied authority, but I think his findings necessarily carry that consequence. The judge finds that Mr Richards acted as de facto managing director of Brayhead. He was the chief executive who made the final decision on any matter concerning finance. He often committed Brayhead to contracts without the knowledge of the board and reported the matter afterwards. The judge said 'I have no doubt that Mr Richards was, by virtue of his position as de facto managing director of Brayhead or, as perhaps one might more compendiously put it, as Brayhead's chief executive, the man who had, in Diplock LJ's words, "actual authority to manage", and he was acting as such when he signed those two documents.' And later he said: 'The board of Brayhead knew of and acquiesced in Mr Richards acting as de facto managing director of Brayhead.' The judge held that Mr Richards had ostensible or apparent authority to make the contract, but I think his findings carry with it the necessary inference that he had also actual authority, such authority being implied from the circumstance that the board by their conduct over many months had acquiesced in his acting as their chief executive and committing Brayhead Ltd to contracts without the necessity of sanction from the board.

Held – appeal dismissed but on the grounds that Richards had actual authority to bind his company.

Panorama Developments (Guildford) Ltd* v *Fidelis Furnishing Fabrics Ltd
[1971] 3 All ER 16

The claimant company trading as Belgravia Executive Car Rental sued the defendant company for £570 in respect of car hiring. Belgravia had a fleet of Rolls Royce, Jaguar and other cars. Fidelis was a company of good reputation which employed a new man, X, as its secretary. He got in touch with Belgravia and booked cars which he wanted to drive for the company to meet important customers when they arrived at Heathrow Airport. On the first occasion, X wrote a cheque on his own account and it was met. In January 1970 he gave a list of dates for which he required cars on hire to Belgravia. It confirmed that the cars would be available and sent a written confirmation to Fidelis and not to X. Belgravia allowed the cars to go out on credit, asking for references. X gave references of the company which proved to be satisfactory. The printed forms of hiring and insurance agreements showed that X, the company secretary, was the hirer. These forms were signed by X or the sales manager of Fidelis. X used the cars which were never paid for. Belgravia sent the statement of account to Fidelis but it did not pay. Later the managing director of Fidelis found many unpaid bills in the company's name and disputed X's authority to act on behalf of the company.

Held – by the Court of Appeal – that the defendant company was liable for the hire because, among other things, X as company secretary had ostensible authority to enter into the contracts for the hire of the cars on behalf of the defendant.

Comment

(i) The observations of Lord Denning on the position of a company secretary are of interest. He said:

> 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.

(ii) It should be noted that the judges in this case referred to the power of the company secretary to bind the company in this limited way as being based on ostensible authority. The reader should, however, be aware that it is sometimes referred to as 'usual' authority', i.e. being what, for example, a managing director or company secretary can 'usually do'.

Non-executive directors and employees

Where the outsider deals with a non-executive director or employee not occupying a designated office within the company-law structure, neither of whom have been authorised under s 40, the position of the outsider is much less secure and there is little authority in case law which deals with the ostensible or usual authority of middle and lower management: such as there is would suggest that their unauthorised acts are unlikely to bind the company.

Of course, where the company allows an employee to hold himself out as an executive director, he may assume the actual ostensible or usual authority of such a director in regard to an outsider who is not aware of the true position, as the following case illustrates.

Electronics Ltd* v *Akhter Computers Ltd [2001] 1 BCLC 433

Mr David Bennett was employed by Skynet, a division of Akhter, as 'director PSU sales'. In fact, he was not a director of any company in the Akhter Group. He worked from a small sales office in Basingstoke with two other people, his assistant Andy Wall and a secretary. Mr Bennett's primary duty was to promote sales and he was paid large commissions when he was successful. He was given a very high degree of autonomy. He even had the habit, known to and permitted by his employers, of writing on Skynet notepaper and describing himself as a 'director'. This Skynet notepaper, in breach of s 351 of the Companies Act 1985, omitted to contain the registered name, company number, and address of Akhter, leaving the reader no indication as to whom David Bennett might answer. Mr Bennett made a contract on behalf of Skynet to arrange for the supply of power-supply units to Pitney-Bowes and share the commission with SMC, which had passed the procurement contract on to Akhter through Mr Bennett. Later Akhter contended that it was not required to pay SMC a share of the commission because Mr Bennett had no authority to make the commission-splitting deal.

Held – by the Court of Appeal – that since the agreement was reasonably associated with his job, Mr Bennett had actual authority to enter into the deal. In any event, he had ostensible authority to enter into commission agreements generally because that was ordinarily incidental to his duties. Furthermore, SMC was not on notice of any lack of authority.

Comment

There was no argument in the case that this contract was beyond the powers of the company or the board, so that it was presumably not necessary to use s 35A of the Companies Act 1985 to validate Mr Bennett's actions. The court was merely applying the common rules of agency. The provisions of Mr Bennett's employment contract were also of crucial importance. The relevant provision was in the following terms: 'Job title: Director PSU sales. You must perform such duties as may be reasonably associated with your job title.' Perhaps Akhter should have been more restrictive.

Kreditbank Cassel* v *Schenkers Ltd [1927] 1 KB 826

Under the articles of the company the directors were empowered to decide who should draw bills of exchange on behalf of the company. A Mr Clarke, who was the Manchester branch manager of Schenkers, drew bills of exchange on the company's behalf in favour of Kreditbank. He had no authority to do so. The court later held that the bills were not binding on the company because it was, on the evidence, unusual for a branch manager to have such authority.

Where the company document which the outsider relies upon is a forgery

The rules of law laid down in ***Turquand*** and the other general rules of agency described above together with the statutory contribution of s 40 will not validate a forgery. A forgery is a crime and in no sense a genuine transaction.

Ruben* v *Great Fingall Consolidated [1906] AC 439

Rowe was the secretary of the company and he asked the appellants, who were stockbrokers, to get him a loan of £20,000. The appellants procured the money and advanced it in good faith on the security of the share certificate of the company issued by Rowe, the latter stating that the appellants were registered in the register of members, which was not the case. The certificate was in accordance with the company's articles, bore the company's seal, and was signed by two directors and the secretary, Rowe; but Rowe had forged the signatures of the two directors. When the fraud was discovered, the appellants tried to get registration, and when this failed, they sued the company in estoppel.

Held – by the House of Lords – a company secretary had no authority to do more than deliver the share certificates, and in the absence of evidence that the company had held Rowe out as having authority to actually issue certificates, the company was not estopped by a forged certificate. Neither was the company responsible for the fraud of its secretary, because it was not within the scope of his employment to issue certificates. This was a matter for the directors. The Lord Chancellor, Lord Loreburn, said:

> The forged certificate is a pure nullity. It is quite true that persons dealing with limited liability companies are not bound to inquire into their indoor management, and will not be affected by irregularities of which they had no notice. But this doctrine, which is well established, applies only to irregularities that might otherwise affect a genuine transaction. It cannot apply to a forgery.

Defective authority and insiders

The rule in ***Turquand***'s case, and the ostensible or usual authority rules of agency which have been considered above, are in general designed to protect persons who deal with the company from outside against defects in the internal management of the company's affairs. Members of a company can take advantage of the rule and in ***Bargate* v *Shortridge*** (1855) 5 HL Cas 297 it was held that a member could rely upon a written consent purporting to be given by the board, as required by the articles, allowing him to transfer his shares, even though it was given by the managing director alone. The company could not set aside the transfer and restore the member's name to the register.

Directors and persons who act as such in regard to the transaction in question are regarded as insiders and cannot rely on the rule. Thus, an allotment of shares made to a director at a meeting at which he was present by a board, some or all of whom were not properly appointed, would be invalid. As Lord Simonds said in ***Morris* v *Kanssen*** [1946] 1 All ER 586 (the case in point) in regard to directors: 'To admit in their favour a presumption that that is rightly done which they themselves have wrongly done is to encourage ignorance and careless dereliction from duty.'

However, if a director does not act as such in connection with a transaction, he may be able to rely on the rule. Thus in ***Hely-Hutchinson* v *Brayhead*** [1968] l QB 549 it was held that a director who lent money to his company's subsidiary, and also guaranteed loans to it by other persons, could enforce an agreement to indemnify him given in the company's name by a fellow director who had assumed the functions of managing director on an irregular basis but with the acquiescence of the board. The company was represented in the transaction only by the fellow director, and the director who made the loan was not therefore prevented from relying on the rule. Lord Denning MR observed:

> The judge held that Mr Richards had ostensible or apparent authority to make the contract, but I think that his findings carry with them the necessary inference that he had also actual authority, such authority being implied from the circumstance that the board, by their conduct over many months, had acquiesced in his acting as their chief executive and committing Brayhead to contracts without the necessity of sanction from the board.

Essay questions

1 (a) State the legal rules applying to a transaction within the powers of the company, but entered into by directors in excess of their authority.

AND

(b) Bob is chairman of Light Ltd. He functions as the company's chief executive and makes most decisions regarding its business. He reports his various decisions to the board in order to inform them of what has happened. The articles of Light Ltd provide that:

> The directors may from time to time appoint one or more of their body to be managing director. The directors may entrust to and confer upon a managing director any of the powers exercisable by them, subject to such restrictions as they think fit.

Bob has on a number of occasions given Light Ltd's guarantee of loans from finance companies to Light Ltd's customers. Each of these transactions was later reported to the board. In June 1999 in a boardroom dispute, the directors resolve that in future such guarantees may only be given after approval by the full board. On 1 August Bob as a matter of urgency acts on his own initiative to give Light Ltd's guarantee to Slow Ltd, a new and potentially valuable customer. The lender is Sharp Ltd, a finance house with whom Light Ltd has had previous dealings. Sharp Ltd has a copy of Light Ltd's articles. The board refuses to adopt Bob's action and Light Ltd disclaims liability on the guarantee.

Advise Sharp Ltd on the enforceability of the guarantee.

(*University of Central Lancashire*)

2 In what circumstances will an agent bind a company to a contract made with a third party? What effect does the company's constitution have on the power of agents to bind companies to such contracts? (*The Institute of Chartered Secretaries and Administrators*)

3 B is the managing director of T Ltd. He has decided that the company should have a new factory built. He arranges for P Ltd to carry out the building work on the usual standard term contract for the building industry which requires that T Ltd makes progress payments on a three-monthly basis.

The articles of association of T Ltd provide that the directors of the company may negotiate any contract on the company's behalf up to a value of £100,000 but contracts in excess of this sum must be approved by the company passing an ordinary resolution in general meeting.

The value of this building contract is £500,000. B did not obtain the approval of the general meeting. The first progress payment has now fallen due and the other directors of T Ltd have resolved not to pay it on the grounds that the contract was not properly authorised by the shareholders.

You are required to explain whether T Ltd is bound to pay this progress payment and more generally whether T Ltd is bound to the contract with P Ltd.

(*The Chartered Institute of Management Accountants*)

4 (a) What is the rule in ***Royal British Bank* v *Turquand*** (1856), and what defences against its application are available to a company?

(b) Beetlecrush Ltd was a company involved in pest control. In 1999 Pellet was appointed as managing director of the company by a board resolution, which gave him exclusive power to manage the company, subject only to a requirement to get the approval of the board for all contracts in excess of £50,000.

On behalf of the company, Pellet began negotiating for the purchase of insecticides from Toxin, who had supplied the company with similar products for a number of years. Before these negotiations were concluded, Toxin accepted an invitation to become a member of the board of Beetlecrush Ltd, and thenceforth duly attended its board meetings. Some months after this, Pellet, without getting the approval of the board, signed a contract with Toxin for the supply of £80,000 worth of insecticides.

Preliminary trials with these insecticides have revealed that they are not as effective as the company had been hoping. The board, with the exception of Pellet and Toxin, is now seeking some way in which the company can claim that it is not bound by its obligations under the contract.

Advise the board. (*The Association of Chartered Certified Accountants*)

5 Contrast the rules governing contracts purporting to be made on behalf of a company before it has been incorporated under the Companies Act with those governing contracts made by or on behalf of an incorporated company before it is entitled to do business.

(*The Institute of Company Accountants*)

6 The company secretary of Beech Ltd has in the past been permitted to order office equipment and stationery for the company but no single transaction has exceeded £500. Recently, without the knowledge of the directors, he ordered a computer installation costing £200,000. The board does not wish to proceed with the purchase but the supplier is claiming that the company is bound by the contract.

Advise the directors. (*The Institute of Chartered Accountants in England and Wales*)