

A COMPARISON BETWEEN THE COMPANIES ACTS OF 1973
AND 2008 IN RESPECT OF PRE-INCORPORATION CONTRACTS

by

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DECLARATION

I, the undersigned, hereby declare that the work contained in this mini-dissertation is my own original work and that I have not previously, in its entirety or in part, submitted it at any other university in order to obtain an academic qualification.

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CHAPTER 1 - INTRODUCTION

Under common law it was recognised that an agreement could be entered into for the benefit of a person that was not in existence at the time that the agreement was concluded.¹ The focus of this mini-dissertation is a comparison between the common law position and the position as codified from time to time in the relevant prevailing legislation.

Chapter two will provide for an overview of the *Stipulatio alteri* a common law contract that could be created in favour of third party. The discussion in chapter will look at the requirements of such a contract and the liability of the person entering the contract for the third party as agent or trustee.

Chapters three and four focus on pre-incorporation contracts in terms Section 35 in the Companies Act 61 of 1973 and Section 21 in the Companies Act 71 of 2008. In these chapters a comparison is done between the requirements, liability of the person representing the company that is to be formed and short comings.

The comparison is narrowed in that it takes a more robust look at the liability facet of this agreement, and how the position has changed in respect of the person representing the company coming into existence, and how the role of trustee or agent differs.²

In this mini-dissertation, the noticeable changes in the law are pointed out from the confusing long winded single section 35 catered for in the Companies Act 61 of 1973(the “1973 Act”),³ to the more specific and detailed provision of the Companies Act 71 of 2008 (the “2008 Act”).⁴ Emphasis is placed on the fact that under the 2008 Act,⁵ the incorporator is deemed to be

¹ See discussion under 2.1.

² See discussion under 2.3, 3.2 and 4.2.

³ Section 35.

⁴ Section 21.

⁵ Section21(2).

liable should the agreement not be adopted or ratified by a company when it comes into existence. A further comparison is done in chapter five between the newly promulgated Act, the previous Companies Act and its counterpart in the United Kingdom.⁶

Portions of this mini-dissertation focus on the aspect of the capacity of the person representing the company that is to be incorporated and how this affects the representative's liability, as well as some of their additional rights and obligations.⁷

A discussion in chapter six is then led in respect of the evolution of pre-incorporation contracts and whether the legislature was paying attention to changes in the world's response to these contracts as well as shortcomings that were being experienced by our courts. Lastly, whether the adaptations made were suitable or whether they are trivial and without due consideration.⁸

From the outset, the submission made is that the legislature was not paying attention to the existing shortcomings felt by the courts and that although the newly adopted Companies Act does seem to adopt the world's majority view in respect of pre-incorporated contracts, there are certain shortfalls that have been so obviously missed that it makes the provisions, from a practical point of view, completely superfluous, and only really to the advantage of the well informed. Without much elaboration, these shortcomings include, *inter alia*, aspects pertaining to the manner of ratification to be employed; why trustees have been excluded and whether the legislature should have gone further to eradicate the common law position.⁹

⁶ See discussion under 3.4 and 5.1.

⁷ See discussion under 3.1.2 and 4.2.

⁸ See Chapter 6

⁹ See discussion under 4.3.

It should be noted that although the above submission is bold, and will require substantial re-enforcement in order to be held as correct, it should be noted that the purpose of the new Companies Act was to repeal the legislation that allowed for the creating of Close Corporations¹⁰ and in doing so, set out to allow for a process that would encourage entrepreneurship and enterprise efficiency¹¹, flexibility and simplicity in the formation and maintenance of companies¹², while, under this mini-dissertation, a savvy individual can use the provision, or not, to the benefit of himself or his client thus making the section redundant.

¹⁰ Close Corporations Act 69 of 1984

¹¹ Section 7(b)(i) of the Companies Act 71 of 2008.

¹² Section 7(b)(ii) of the Companies Act 71 of 2008.

CHAPTER 2 - POSITION UNDER COMMON LAW

2.1 *STIPULATIO ALTERI*

As a point of departure in discussing the above topic it is well worth noting the position under our common law and Roman Dutch law. The concept of a pre-incorporation contract, entered into on behalf of a company to be formed, in terms of common law was foreign and unknown. Despite this the common law can provide insight in the event that the statutory provision¹³ does not apply.

In terms of the common law, and more specifically Roman Dutch law, it was possible for a person to enter into an agreement in respect of and for the benefit of a third party. The position as to whether a *stipulatio alteri*, finds application in our law has been a debated topic in various matters.¹⁴

As stated by Innes CJ wherein a definition for *stipulatio alteri* was provided:

“It is merely a convenient expression to denote that the object of the agreement is to secure some advantage for a third person...the acceptance of the benefit (by the third party) would involve the undertaking of the consequent obligation.”¹⁵

The position pertaining to agreements made for the benefit of third parties was discussed by *Grotius* wherein contracts for the benefit of a third party were divided into two categories, the first being where a promise is made “to me” for the benefit of a third party and secondly a promise is “expressly” made in favour of a third party.¹⁶ In the former, according to *Grotius*, the one person can be held liable pending the decision of the third party and at the same time the promisor cannot revoke his undertaking but he can be released.¹⁷ In the latter *Grotius* makes two further distinctions, first for a person acting on behalf of a third party without authority and secondly for a person acting with

¹³ Section 35 of The Companies Act 71 2008.

¹⁴ *Mccullogh Appellant vs Fernwood Estate Ltd Respondent* 1920 AD 204.

¹⁵ *Mccullogh Appellant vs Fernwood Estate Ltd Respondent* 1920 AD 204 page 206.

¹⁶ *Mccullogh Appellant vs Fernwood Estate Ltd Respondent* 1920 AD 204.

¹⁷ *Mccullogh Appellant vs Fernwood Estate Ltd Respondent* 1920 AD 204.

authority. Both are valid. The difference seems to be where the person has no authority, he cannot grant remission and this must be given by the third party.

The position has been settled in that the sole test as to whether a *stipulatio alteri* is valid and whether the third person can enforce performance is whether the contract is still “open”.¹⁸ It is submitted that the reference to an agreement still being open relates to whether the agreement has been cancelled prior to acceptance by the third party.

McKerron¹⁹ point out that in terms of *Kynochs Limited v Transvaal Silver and Base Metals Limited*²⁰ that a contract is one that does not exist until the third party gives acceptance. McKerron²¹ states that such a contract would constitute an option that is kept open, and that an option constitutes a contract.

Once the third party exercises its rights to adopt the contract and the rights and liabilities that come with the contract, the trustee or agent fall out of the contract. McKerron²² points out that if the contract has corresponding obligations, then the third party will be bound to carry out these obligations upon giving acceptance. However, it is possible for a contract between two parties that is designed to enable a third person to come in as a party to the contract with one of the other two.²³ According to Jooste, where the promoter acts as *stipulans* or trustee, Jooste is of the view that the contract will have retrospective effect and take effect from date of acceptance²⁴ by the *stipulans*²⁵ or trustee.²⁶

The period in which the contract will remain open will depend on the agreement.²⁷ It is however submitted that the nature of the agreement may also provide a presumption in respect of the period in respect of when the contract will be open for adoption by the third party. An agreement by the

¹⁸ *Mccullogh Appellant vs Fernwood Estate Ltd Respondent* 1920 AD 204 page 208.

¹⁹ McKerron, RG “The Nature of Contracts for the Benefit of Third Persons” (1929) 46 S.A. SALJ L.J 387,395.

²⁰ 1922 W.L.D. 71.

²¹ McKerron, RG “The Nature of Contracts for the Benefit of Third Persons” (1929) 46 SALJ 387,395.

²² McKerron, RG “The Nature of Contracts for the Benefit of Third Persons” (1929) 46 SALJ 387,394.

²³ *Crookes NO & another v Watson & other* 1956 (1) SA 277 (A) at 291B-F.

²⁴ Jooste, R “When Do Pre-Incorporation Contracts Have Retrospective Effect” (1989) 106 SALJ,511.

²⁵ Jooste, R “When Do Pre-Incorporation Contracts Have Retrospective Effect” (1989) 106 SALJ,511.

²⁶ Jooste, R “When Do Pre-Incorporation Contracts Have Retrospective Effect” (1989) 106 SALJ,510.

²⁷ *Bagradi V Cavendish Transport Co (Pty) Ltd* (1957) 1 ALL SA 392 (D),397.

trustee for a license to be received by the third party would constitute such an agreement that would hold an assumption in respect of the time in which a contract would be open for adoption by third party.²⁸

2.2 REQUIREMENTS FOR THE *STIPULATIO ALTERI*

The position used to be that it was impossible for a person to act as trustee for a principal that did not exist at the time that the agreement was concluded.²⁹ It was impossible for a company to ratify or adopt a contract made for its benefit prior to its existence and as such a new agreement with identical terms would be needed.³⁰ This is not the current position.

An agreement for the benefit of a third party is almost totally governed by the contract itself. The contract made for the benefit of a third party is a tri-party agreement. Despite the third party needing a representative, the representative does not act in the capacity of an agent, but more of principal.³¹ This is due to the fact that the third party is unable to perform the function of a principal and therefore the representative must attend to this function, he must do so in his capacity as principle and not as trustee.³²

Despite being a trustee, if the contract provides for it, the trustee may also act in a personal capacity in conjunction to that of being trustee. This dual capacity must be provided for in terms of the contract.³³ If there is no provision in an agreement for the trustee to act in a dual capacity, then it is presumed that he was only vested with the power to act as trustee. It must be stated in the agreement that the trustee is entitled to receive the benefit of the agreement personally in order for the trustee to obtain the benefit of an agreement personally.³⁴

²⁸ *Bagradi V Cavendish Transport Co (Pty) Ltd* (1957) 1 ALL SA 392 (D)

²⁹ *Kelner vs Baxter* (L.R. 2 CP 174).

³⁰ *Natal Land and Colonization Company, Ltd. v Pauline Colliery and Developing Syndicate, Ltd.* (1904) 25 NLR 1.

³¹ *Ackerman N.O v Burland And Milunsky* (1944 WLD 172).

³² *Ackerman N.O v Burland And Milunsky* (1944 WLD 172).

³³ *Visser v Tonder* [1986] 3 All 423 (T), 424.

³⁴ *Visser v Tonder* [1986] 3 All 423 (T), 426.

It is clear that there is a lapse in time in respect of when the contract comes into existence and when the third party adopts the agreement. And as long as the agreement is open, the third party will be entitled to adopt the agreement. In respect of the question as to how much time must have elapsed before the contract would have expired or can be terminated, can be answered in that there must be a reasonable time that is allowed for the third party to come into existence and adopt the agreement.³⁵ In the event that a time period exists, expiry of the agreement will cause it to terminate. Where provided for in the agreement or where parties jointly consent, parties may agree to the extension of the time period for adoption.

Given that the trustee acts as principal, he will be entitled to sue in his or her own name on behalf of the third party. This may be done by the trustee if the implementation of legal proceedings is necessary to preserve the benefit under the agreement for the third party.

Despite having the ability to sue on behalf of the third party, the trustee does not necessarily incur the rights and obligations of the third party.³⁶ The trustee is as such not entitled to exercise rights or obligated to render the performance that is stipulated for the third party unless the contract so provides.³⁷

A third party cannot enforce the benefit of an agreement, even if made in its favour, if the third party is not provided for in the agreement. The mere fact that the third party is mentioned in the agreement does not make it a contract for their benefit.³⁸

Where the trustee enters into an agreement for a third party that requires the other party to tender performance in order to preserve the agreement and benefit for the third party, the trustee may sue in their capacity as principal for specific performance if necessary.³⁹

³⁵ *Semer v Retief And Berman* (1948) 1 ALL SA 106 (C), 118.

³⁶ *Nine Hundred Umgeni Road (Pty) Ltd* (1986) 1 ALL SA 289 (A), 290.

³⁷ *Nine Hundred Umgeni Road (Pty) Ltd* (1986) 1 ALL SA 289 (A), 291.

³⁸ *Barnett and Another v ABE SWERSKY & ASSOCIATES* [1986] 2 All SA 450 (C), 453.

³⁹ *Gardner v Richardt* (1974) 4 ALL SA 158 (C), 162.

In exercising the function of principal, and despite what has been said above, the trustee does not, as a general rule, acquire the right to request that specific performance takes place in terms of the agreement absent the third parties instructions. This is due to the consideration that this action may result in the benefit of the agreement being used up before the third party has an opportunity to adopt the agreement.⁴⁰ Thus there is no assumption that the trustee will be entitled to claim specific performance in the absence of an expressed provision and have the property that forms part of an agreement transferred into his name.⁴¹

Where the benefit of a pre-incorporated contract is specifically for the benefit of the third party, the trustee may not sue for specific performance.⁴² McKerron⁴³ submits that where the *promisee* contracts as principal, he is in reality securing for the third party an option and that the contract can be resolved into a promise that the promisor keeps open for the acceptance of the third party.⁴⁴

The trustee exercises his duties as if he or she was principal. Despite the wide powers that are vested in the trustee, upon the adoption of the agreement by the company, the trustee will, generally fall out of the contract altogether.⁴⁵

It is as a result of the fact that the trustee can sue in some instances and can't in others, as well as be a party to the agreement, but also fall out of the agreement from time to time that the contents of the agreement are of vital importance. McKerron⁴⁶ states that the relationship between the promisor and third party is easy to establish. The difficulty comes in determining the relationship between the promisor and *promisee*.

⁴⁰ *Gardner v Richardt* (1974) 4 ALL SA 158 (C), 163.

⁴¹ *Gardner v Richardt* (1974) 4 ALL SA 158 (C), 164.

⁴² McKerron, RG "The Nature of Contracts for the Benefit of Third Persons" (1929) 46 *SALJ* 387.

⁴³ McKerron, RG "The Nature of Contracts for the Benefit of Third Persons" (1929) 46 *SALJ* 387, 395.

⁴⁴ McKerron, RG "The Nature of Contracts for the Benefit of Third Persons" (1929) 46 *SALJ* 387, 394.

⁴⁵ *Bagradi V Cavendish Transport Co (Pty) Ltd* (1957) 1 ALL SA 392 (D), 397.

⁴⁶ McKerron, RG "The Nature of Contracts for the Benefit of Third Persons" (1929) 46 *SALJ* 387, 394.

2.3 LIABILITY OF PERSON ACTING AS AGENT OR TRUSTEE

In deciding the scope and extent of the powers of the person representing the third party it is important and worthwhile to note the capacity in which they act. In the event that the person acts as trustee, then they are the *dominus* in respect of the agreement and, depending on the terms of the agreement, may be entitled to request performance and may accept this performance personally.⁴⁷ According to Delport,⁴⁸ whether a person is personally bound at common law depends purely on the terms of the contract.

Despite the trustee accepting the responsible for the third party's counter performance, the trustee will not, as a rule, acquire the benefit of the agreement. But if the trustee conducts himself as if he was the third party, he may incur personal liability.⁴⁹ McKerron⁵⁰ points out that as a general rule the *promisee* may not claim from the promisor fulfilment of the contract. And although the *promisee* may not sue for performance, the *promisee* may sue to interdict the promisor from breaching the contract.⁵¹

The fact that a person acted as trustee will be no indicator that he or she is personally liable under a pre-incorporation contract in the event that the company is either not formed or failed to adopt the agreement upon coming into existence. In order to decide on the liability of the trustee, reference must be made to the agreement.⁵² In the event that there is no provision in respect of personal liability in the agreement, then there is nothing that the other party can do except resile from the contract. If not provided for in the agreement, the absence of a provision for personal liability may result in an agreement whereby the other party can do nothing but withdraw without even being able to claim damages.⁵³

⁴⁷ *Mccullogh Appellant vs Fernwood Estate Ltd Respondent* 1920 AD 209.

⁴⁸ Delport, P "Henocheberg on the Companies Act 71 of 2008" 5 ed (2011)– Notes – Common law.

⁴⁹ *Twenty Seven Bellevue CC V Hilcove* (1994) 2 ALL SA 293 (A).

⁵⁰ McKerron, RG "The Nature of Contracts for the Benefit of Third Persons" (1929) 46 *SALJ* 387, 391.

⁵¹ McKerron, RG "The Nature of Contracts for the Benefit of Third Persons" (1929) 46 *SALJ* 387, 391.

⁵² *Nine Hundred Umgeni Road (Pty) Ltd v Bali* (1986) 1 ALL SA 289 (A), 291.

⁵³ *Nine Hundred Umgeni Road (Pty) Ltd v Bali* (1986) 1 ALL SA 289 (A), 291.

The above is not an indication of the promisor having a right to revoke his promise. McKerron⁵⁴ points out that the promisor cannot revoke his promise to the *promisee* before the third party's acceptance. This however does not extend to agreement and McKerron⁵⁵ further states that the promisor and *promisee* may mutually agree to cancel the contract before the third party accepts.

The general rule is that when the company comes into existence and while the agreement is still open, the trustee will fall out of the contract altogether once adopted by the company. There may however be circumstances wherein the company comes into existence and adopts the contract, with liability still falling on the trustee. An example of such would be where the pre-incorporated contract pertains to the sale of immovable property, and the trustee becomes liable for transfer duties together with the company.⁵⁶

McKerron,⁵⁷ states that upon the third party's notification of acceptance, the *promisee* falls out of the contract all together. It is upon notification that the third party's rights come into existence.⁵⁸ Acceptance must be given within the time limits as prescribed in the contract or within a reasonable time.

According to Delpont,⁵⁹ at common law, where a juristic person is to accept the benefit conferred on it, unlike a natural person that can do this through intention and action, a juristic person can manifest this intent in its resolutions, directors and officials.

As such, it appears that it is not possible to formulate a test in advance in order to determine as to whether the trustee will be personally liable, and thus each case must be judged based on the terms of the agreement.⁶⁰

⁵⁴ McKerron, RG "The Nature of Contracts for the Benefit of Third Persons" (1929) 46 *SALJ* 387, 388.

⁵⁵ McKerron, RG "The Nature of Contracts for the Benefit of Third Persons" (1929) 46 *SALJ* 387, 389.

⁵⁶ *Commissioner for Inland Revenue v Collins* (1992) 2 ALL (A) 300.

⁵⁷ McKerron, RG "The Nature of Contracts for the Benefit of Third Persons" (1929) 46 *SALJ* 387, 391.

⁵⁸ McKerron, RG "The Nature of Contracts for the Benefit of Third Persons" (1929) 46 *SALJ* 387, 391.

⁵⁹ Delpont, P. 2017 "Henocheberg on the Companies Act 71 of 2008" – Notes – Common law.

⁶⁰ *Gardner V Richardt* (1974) 4 ALL SA 158 (C), 162.

CHAPTER 3 - POSITION UNDER THE COMPANIES ACT 61 of 1973

3. POSITION UNDER THE COMPANIES ACT 61 of 1973

As was the position under the Companies Act 46 of 1926 the legislature saw it fit to ensure that the 1973 Act should likewise retain a provision which allows for pre-incorporation contracts. Despite ensuring that such a provision was retained, little was done in improving the provision. Shortcomings that were noticeable pertained to aspects such as whether retrospectivity was possible and the liability of the agent or trustee.

3.1 REQUIREMENTS OF SECTION 35

Prior to a company's incorporation, the incorporators may require and desire to procure and secure various rights and obligations prior to the company's incorporation, such as leases, supplier contracts and other opportunities which may exist and would be to the company's benefit if it existed at the time.

The legislature recognised this and has taken various steps in attempting to address this. One such step was the incorporation of section 35 into the Companies Act of 61 of 1973. Cassim⁶¹ states that section 35 is "laudable" to the extent that it overcomes shortcomings in the common law. Despite this, Cassim⁶² states that there are shortcomings in section 35 in that it serves to protect the company and agent and does not provide sufficient regard for the position of the third party. As such, under section 35, the third party is left without remedy should incorporation of the company or ratification of the pre-incorporation contract not take place.⁶³

The requirements as laid down in section 35 make the process of entering a pre-incorporated contract strenuous, and for the most part were identical to the requirements laid down in terms of section 71

⁶¹ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 SALJ 364, 364.

⁶² Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 SALJ 364, 365.

⁶³ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 SALJ 364, 368 .

of the Companies Act 46 of 1926. According to Delpont,⁶⁴ if a contract capable rectification or adoption only in terms of section 35, and the requirements of section 35 have not been followed, then the contract is without effect as between anyone. The contract is void.

The Requirements as provided for in section 35 include that the contract must be:

- in writing;
- by a person professing to act as agent or trustee for a company yet incorporated;
- that the contract must be ratified or adopted by the company after being incorporated;
- the adoption of the contract must be an object of the company as provided for in the company's memorandum;
- two copies of the contract must be lodged with the registrar of companies;
- one of the contracts lodged with the registrar must be certified by a notary public.

It is submitted that the intention was to create a section that allowed for the transaction to be as transparent as possible. The problem was that section 35 never removed the common law position. Thus, under the 1973 Companies Act, it was still possible to enter into a *stipulatio alteri* with the third party being a company to be incorporated. In respect of a comparison between how the common law position differed from section 35, reference should be made to the requirements.

3.1.1 WRITTEN CONTRACT

Under section 35 it was mandatory for the contract to be written. Under common law, it was possible for the agreement to be an oral agreement.⁶⁵ Naturally where an agreement is oral, the exact terms of the agreement are difficult for the Court to confirm. However, this departure is substantial. Had a person entered into an oral agreement and relied on the common law position, the efforts made in the incorporation of section 35 would come to nil.

⁶⁴ Delpont, P. "Henocheberg On The Companies Act 61 of 1973" 5 ed (2011)- Notes – General Note, 62.

⁶⁵ *Semer v Retief And Berman* 1948 1 ALL SA 106 (C).

It is submitted that the departure as illustrated above, coupled together with the fact that the common law position is still valid, highlights a major flaw in the Act, and undermined its purpose.

On the other hand, the court has indicated that the legislator has not taken into consideration the circumstance where an oral contract is reduced to a written agreement.⁶⁶ An auction is by its nature an oral agreement, however, the courts⁶⁷ have stated that there is no reason that the contract cannot be reduced to writing for the purposes of compliance with the Act.

The courts have held that an auction is an oral contract which comes into existence at the time that the auctioneer knocked down.⁶⁸ If an agreement is later reduced to writing and signed by the relevant parties it can comply with the requirement that the agreement must be in writing⁶⁹ and an oral agreement that is later reduced to writing is sufficient for the formality that the contract must be in writing. The courts have held that this was because of the word 'made' in the connotation 'contract made in writing'.⁷⁰

It is possible for a pre-incorporated contract to exist in the form of an oral agreement, however, once reduced to writing, the contract is the determining document. Where a clear meaning exists, that meaning cannot by means of oral evidence be shown to have a contrary meaning.⁷¹ As a rule, the courts will confirm the sale where the purchase was done in *bona fide* manner and openly.⁷²

In reference to the company that will be entering the contract, the courts⁷³ have held that it is not necessary to make mention of the company's name in the pre-incorporated contract. This is because it often occurs that the agreement is entered prior to any consideration to the name of the company or its constitution.⁷⁴

⁶⁶ *Ex Parte Kramer: In Re Estate Selesnik* [1973] 4 All SA 199 (W), 203.

⁶⁷ *Ex Parte Kramer: In Re Estate Selesnik* [1973] 4 All SA 199 (W), 203.

⁶⁸ *Pledge Investments (Pty) Ltd v Kramer, No: Re Estate Selesnik* [1975] 4 All SA 1 (A), 5.

⁶⁹ *Pledge Investments (Pty) Ltd v Kramer, No: Re Estate Selesnik* [1975] 4 All SA 1 (A) – the prevailing section at the time of this case was Section 71 of the Companies Act 46 of 1926, but this section also required that the contract be reduced to writing.

⁷⁰ *Pledge Investments (Pty) Ltd v Kramer, No: Re Estate Selesnik* [1975] 4 All SA 1 (A), 6.

⁷¹ *Nordis Construction Co (Pty) Ltd v Theron, Burke An Disaac* [1972] 2 All SA 261 (D), 268.

⁷² *Ex Parte Kramer: In Re Estate Selesnik* [1973] 4 All SA 199 (W), 204.

⁷³ *Olifants Trust Co v Pattison* [1971] 1 All SA 32 (W).

⁷⁴ *Gaybelle Investments (Pty) Ltd v Hermer* 1951 (1) SA 486 (W), 488.

3.1.2 BY A PERSON PROFESSING TO BE AN AGENT OR TRUSTEE

It is submitted that in terms of section 35, the words trustee and agent are used almost as similes. Under common law the capacity that the person acted in made a difference as to what they were able to do in terms of the contract.

In terms of English common law,⁷⁵ this position was never possible as a trustee could never act on behalf of a non-existing principal. The position in South Africa is not the same. The courts have indicated that the previous Companies Act⁷⁶ altered the position under English common law.⁷⁷

Cassim,⁷⁸ indicates that section 35 did not apply to instances where the third party was unaware of the company's non-existence. Cassim⁷⁹, was of the view that this should be extended to include a third party that neither knows nor ought reasonably to have known of this fact.

Our courts have indicated that where a person acts as trustee they act as principal,⁸⁰ and that when the other contracting party commits breach, the trustee may be required to act in order to preserve the benefit of the contract. The trustee is entitled to react but must not sue in the capacity as trustee, but that of principal. This does not mean that a trustee automatically has the capacity to sue in the absence of breach. The courts have indicated that reference should be made to the contract⁸¹ and that as a course of law, the trustee does not incur the right to sue on the contract for specific performance as this may result in depriving the company of the benefit under the pre-incorporation contract⁸². Should a person have entered into a contract, in terms of section 35, which did not cater for a right entitling the incorporator or promoter to institute legal action, then in terms of section 35, read together with the above, the incorporator or promoter would not have the general authority to sue and would be limited to instances where the other contracting party has committed breach.

⁷⁵ *Kelner v Baxter* (L.R. 2 CP 174), 208.

⁷⁶ Section 71 of the Companies Act 46 of 1926.

⁷⁷ *Nordis Construction Co (Pty) Ltd v Theron, Burke An Disaac* [1972] 2 All SA 261 (D), 269.

⁷⁸ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 396.

⁷⁹ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 397 - 398.

⁸⁰ *Bagradi v Cavendish Transport Co (Pty) Ltd* [1957] 1 All SA 392 (D), 396.

⁸¹ *Gardner v Richardt* [1974] 4 All SA 158 (C), 161.

⁸² *Gardner v Richardt* [1974] 4 All SA 158 (C), 163.

The position of that of agent is less clear. According to common law,⁸³ distinction is created between a contract for a third party and of a specific person. In the former, the promisor can be held to the contract and the promisor cannot revoke his undertaking but may be released. In the latter, a further distinction is made between a person and their authority. If he has authority, the transaction is complete and there can be no withdrawal if there is no authority. Remission cannot be given pending the decision of the third party.

According to Delport,⁸⁴ section 35 does not determine the nature of the rights and obligations of the agent. As such, the nature of the rights and obligations is dependent on the terms of the particular contract. This nature of rights and obligations is extended to the liability of an agent and the terms of the contract must provide for liability.

In *Blower v Van Noorden*⁸⁵ the court discussed the position of an agent who acts on behalf of a company without the necessary authority. In this matter the court stated, without certainty, that where an agent acts on behalf of a principal without the necessary authority, the fact that the agent does not have authority is peculiar to the agent, however, the other party will know nothing of this. It justifies in implying, on part of the agent, that his principal will be bound. If not, the agent must place the other party in a position as good as if the principal were bound.

Ncube⁸⁶ is of the view that the only protection that section 35 offers to third parties is that it requires that the promoter must disclose or profess that he represents an unincorporated company. Such disclosure is in effect a warning to the third party. Given the limited extent of protection offered to third parties, Ncube⁸⁷ is of the view that third parties are already in a "precarious position" when entering into a pre-incorporation contract and as such deserve more protection and that this is the

⁸³ *Mccullough Appellant v Fernwood Estate Ltd Respondent* 1920 AD 204.

⁸⁴ Delport, P. "Henocheberg on the Companies Act 61 of 1973" 5 ed (2011)- Notes – General Note page 62.

⁸⁵ 1909 TS 890.

⁸⁶ Ncube, C. "Pre-Incorporation Contracts : Statutory Reform" (2009) Vol 126 Issue 2 *SALJ* 255, 258.

⁸⁷ Ncube, C. "Pre-Incorporation Contracts : Statutory Reform" (2009) Vol 126 Issue 2 *SALJ* 255, 259.

main criticism levelled against section 35.⁸⁸ Cassim is of the view that the requirement to “profess” to act as an agent or trustee is confusing.⁸⁹ The word should be substituted for “state” or declare”.⁹⁰

The representation can be made by the agent even if the agent signs sometime after the other party signed. The court have has that it is “wholly artificial to enquire into who signed first”.⁹¹

It may transpire that the company never comes into existence and the rights and obligations are not carried out and that the incorporators are required to attend to the contract on behalf of the company that has yet to come into existence. Under common law, where the incorporator acted as trustee, he can sue for cancellation, even if done in his personal capacity.⁹² In relation to the section 35 of the 1973 Act, reference is made to both agent and trustee. The question is, suppose that two pre-incorporation contracts are entered into. All formalities are met, with the only difference being that in one contract the representative refers to himself as a trustee, and in the other, as an agent.

In terms of *Bagradi v Cavendish Transport Co (PTY) Ltd*,⁹³ and the references made to previous decisions therein, the trustee would have the power to sue on the contract in the event that repudiation took place. As such, despite section 35 being wide in respect of the accepting that both agents and trustees can enter into pre-incorporated contracts, the actual agreement would be more decisive, once more leading a person to avoid following the statutory position and proceed with a contract in terms of common law.

3.1.3. THE CONTRACT MUST BE RATIFIED OR ADOPTED BY THE COMPANY

No time limit is provided for in terms of section 35 and only reference is made to the occurrence of an event, that being the company’s incorporation. Under common law⁹⁴ the only requirement was that the contract must still be open for acceptance. Cassim⁹⁵ points out that the position was that

⁸⁸ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 263.

⁸⁹ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 395

⁹⁰ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 395.

⁹¹ *Drieri v Du Preez* [1989] 2 All SA 254 (C), 258.

⁹² *Bagradi v Cavendish Transport Co (Pty) Ltd* [1957] 1 All SA 392 (D).

⁹³ [1957] 1 All SA 392 (D).

⁹⁴ *Mccullogh Appellant v Fernwood Estate Ltd Respondent* 1920 AD 204, 208.

⁹⁵ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 373.

ratification should take place within a reasonable time, however, a reasonable time would depend on the facts and circumstances of each case and would include the type of contract, obligations created, goods or service to be provided and other factors such as any backlogs at the Companies Offices.

Should the company not come into existence, the circumstance may arise that additional rights and entitlements were created in favour of the other contracting party. The courts have indicated that the reasonable man may come to a conclusion that if a company does not come into existence then no rectification can take place. As such, other rights created under the pre-incorporated contract would fall away.⁹⁶ It is submitted that it is the nature of the right that will determine as to whether it will survive in the event that the company does not come into existence and adopt the contract. (I.e. – A suretyship agreement would survive and create rights in favour of the other party if the company is not incorporated).⁹⁷

Should a company come into existence and fail to adopt a contract in terms of section 35, alternatively, should it fail to adhere to additional requirements set out in terms of section 35, the failure cannot be remedied through estoppel.⁹⁸

3.1.4 TWO OF THE CONTRACTS LODGED WITH THE REGISTRAR, ONE MUST BE CERTIFIED BY A NOTARY PUBLIC.

According to Delport,⁹⁹ the judgment of *Sentrale Kunsmis Korporasie (Edms) Bpk v NKP Kunsmisverspreider (edms) Bpk*¹⁰⁰ is correct in that the fourth requirement, being that two copies of the agreement must be lodged as well as a notarised copy, is not essential.

Further consideration that needs to be taken into account is the effect that this has on third parties.

According to Ncube¹⁰¹ the requirement of lodging copies of the pre-incorporated contract was

⁹⁶ *Malcom v Cooper And Others* [1974] 3 All SA 482 (C), 481.

⁹⁷ *Malcom v Cooper And Others* [1974] 3 All SA 482 (C).

⁹⁸ *Trust Bank of Africa Ltd v Appletime Engineering (Pty) Ltd and Others* [1981] 1 All SA 102 (D), 105.

⁹⁹ Delport, P "Henochoberg on the Companies Act 61 of 1973" 5 ed (2011) - Notes – General Note.

¹⁰⁰ 1970 (3) SA 367 (A).

¹⁰¹ Ncube, C. "Pre-Incorporation Contracts : Statutory Reform" (2009) Vol 126 Issue 2 *SALJ* 255, 261.

“inequitable to companies and their co-contracting parties alike” and that the requirement to lodge copies of the pre-incorporation contract prioritises the protection of potential creditors and investors.

Cassim¹⁰² argues that the requirement that “two copies of the pre-incorporation contracts need to be lodged at the Companies Office” is problematic in practice. Cassim submits that this provision is aimed at protecting investors and that the disclosure of details in pre-incorporation contracts to the public may be detrimental to third parties who wish to keep the contents of the pre-incorporation contract confidential. Cassim¹⁰³ is of the view that this requirement be wholly abolished.

3.1.5 RETROSPECTIVE EFFECT OF PRE-INCORPORATION CONTRACTS

Section 35 does not make provision for whether a pre-incorporation contract has retrospective effect. Jooste¹⁰⁴ points out that whether a pre-incorporation contract is retrospective may be of vital importance. The example that is given is that of a sale of business. If the pre-incorporation contract has retrospective effect, then the company would be entitled to profits from a date before the company’s incorporation.

According to Delport,¹⁰⁵ a term of a contract purporting to provide for its operation retrospectively prior to incorporation can take effect according to its “tenor”. According to the 1973 Act section 172 (5)(a) a contract entered into before a company is entitled to commence business shall be provisional only and shall become binding on the company on the date the company is entitled to commence business and not earlier.

Jooste¹⁰⁶ submits the view as presented in Delport¹⁰⁷ is “without substance” and states that the general rule in deciding whether the contract has retrospective effect can be decided on with

¹⁰² Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 393.

¹⁰³ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 394.

¹⁰⁴ Jooste, R “When Do Pre-Incorporation Contracts Have Retrospective Effect” (1989) 106 *SALJ*, 507.

¹⁰⁵ Delport, P “*Henochsberg on the Companies Act 61 of 1973*” 5 ed (2011)- Notes – General Note page 64.

¹⁰⁶ Jooste, R “When Do Pre-Incorporation Contracts Have Retrospective Effect” (1989) 106 *SALJ*, 507.

¹⁰⁷ Delport, P “*Henochsberg on the Companies Act*” 4 ed (1985)

reference to the contract. If the expressed or tacit terms of the contract provide for retrospective effect, then the contract undoubtedly has retrospective effect.¹⁰⁸

In his article devoted purely towards the application of retrospectivity, Jooste criticizes the views taken by Cilliers and Benade in respect of where the promoter acts as trustee or in his personal capacity.¹⁰⁹ Jooste indicates that where a promoter acts as trustee or in his personal capacity, he is in fact acting as principal. Further, Jooste indicates that the views of Cilliers and Benade are incorrect in that the contract would have retrospective effect. Jooste states that this conclusion goes against the basic principles of the law of contract.¹¹⁰ Jooste submits that the only rights that the promoter obtains “is the right of action to hold the *promittens* to his undertaking”.¹¹¹ Jooste¹¹² indicates that the confusions on this point as expressed by other authors is because of the decision *Peak Lode Gold Mining Company v Union Government*.¹¹³ Jooste states that the Court in *Peak Lode* did not go as far as to state that the principal acquires rights in terms of the contract, only that the principal has the right to prevent the promisor from cancelling the agreement.¹¹⁴ According to Jooste the confusion can be attributed towards the *Peak Lode* decision wherein the Court ruled that the contract does not operate retrospectively and Jooste submits that the court was incorrect and that had this point ever been taken on Appeal, the decision in *Peak Lode* would be overruled.¹¹⁵

According to Ncube¹¹⁶ if section 35 is complied with the contract should have retrospective effect unless the parties agree otherwise as this would make ratification consistent with ratification at common law.

¹⁰⁸ Jooste, R “When Do Pre-Incorporation Contracts Have Retrospective Effect” (1989) 106 *SALJ*, 507 - 508.

¹⁰⁹ Jooste, R “When Do Pre-Incorporation Contracts Have Retrospective Effect” (1989) 106 *SALJ*, 507.

¹¹⁰ Jooste, R “When Do Pre-Incorporation Contracts Have Retrospective Effect” (1989) 106 *SALJ*, 512.

¹¹¹ Jooste, R “When Do Pre-Incorporation Contracts Have Retrospective Effect” (1989) 106 *SALJ*, 513.

¹¹² Jooste, R “When Do Pre-Incorporation Contracts Have Retrospective Effect” (1989) 106 *SALJ*, 514.

¹¹³ 1932 TPD 48.

¹¹⁴ Jooste, R “When Do Pre-Incorporation Contracts Have Retrospective Effect” (1989) 106 *SALJ*, 514.

¹¹⁵ Jooste, R “When Do Pre-Incorporation Contracts Have Retrospective Effect” (1989) 106 *SALJ*, 510.

¹¹⁶ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 257.

3.2. LIABILITY OF PERSON ACTING AS AGENT OR TRUSTEE

Section 35 makes no provision for liability. As such, an interpretation of previous decisions is required in order to ascertain the position of the agent or trustee in respect of liability.

According to *Mccullogh Appellant v Fernwood Estate Ltd Respondent*,¹¹⁷ due to the construct of the agreement, had the company not have accepted the contract, the person contracting on the behalf of the company would have been required to accept the obligations and benefits created in terms of the agreement,¹¹⁸ the person acting on behalf of the company would be personally liable.¹¹⁹

In *Semer v Retief And Berman*,¹²⁰ the court indicated that a strict interpretation of the agreement would have resulted in no liability in event that the company is formed.¹²¹ As such, an omission to cater for liability, and in the event of the company never coming into existence, would never give rise to personal liability in respect of the agent or trustee.

Where the agent or trustee enters into a pre-incorporation contract and in addition causes a suretyship agreement to come about for the performance of the company to perform once it is registered and adopts the agreement. Should the company not come into existence and as such be unable to perform, this will not detract from the validity of the suretyship agreement and the agent or trustee will still be bound.¹²²

As is mentioned above, where a trustee represents a company to be formed, they act in the capacity as principal.¹²³ As such, if the other side wish to cancel the agreement, the trustee may sue as principal in order to ensure that the benefit of the agreement survives so that the company may adopt same.

¹¹⁷ 1920 AD 204.

¹¹⁸ *Mccullogh Appellant v Fernwood Estate Ltd Respondent* 1920 AD 204, 209.

¹¹⁹ *Mccullogh Appellant v Fernwood Estate Ltd Respondent* 1920 AD 204, 216.

¹²⁰ 1948 1 ALL SA 106 (C).

¹²¹ *Semer v Retief And Berman* 1948 1 All Sa 106 (C), 116.

¹²² *Trust Bank of Africa Ltd v Appletime Engineering (Pty) Ltd and Others* [1981] 1 All SA 102 (D).

¹²³ *Bagradi v Cavendish Transport Co (Pty) Ltd* [1957] 1 All SA 392 (D) 397.

This does not apply to liability, and although the trustee acts as principal, he is not liable on this basis. If the contract makes no provision for liability, then the trustee is not personally liable.¹²⁴

According to *Barnett And Another V ABE Swersky & Associates*,¹²⁵ the court looked at the contents of the contract and held¹²⁶ that a person must actually be a party to the contract before that person will have the right to sue on the contract. In the case at hand, the contract had made reference to the Plaintiff, being the seller's attorneys, but this was not enough to allow them to become a party to the agreement. The court stated¹²⁷ that consideration must be given to the complete contract to ascertain as to whether the parties intended to confer a benefit on the Plaintiff (The Seller's attorneys). The court ruled that this was not the case and upheld the appeal dismissing the Plaintiff's claim.

In *Indrieri v Du Preez*,¹²⁸ reference was made to *Blower v Van Noorden*¹²⁹ wherein the court examined the extent of the agent's liability. The court held that the other party would be entitled to recover full damages from an agent who acts without authority, even if the principal were bound and was unable to tender the full damages due to lack of means. The amount awarded against the agent would bear no reference to the pecuniary position of the principal.

The court¹³⁰ stated that where an agent contracted on behalf of a person purported to exist, the other party will not simply be obligated to establish what would have been payable under the contract, but how much would be recovered from the principal had the principal be bound, and, it is submitted, had the means of satisfying this amount.¹³¹ However, it is submitted that where a company has been de-registered, it will not be possible to establish what the company would have been able to pay.¹³²

¹²⁴ *Nine Hundred Umgeni Road (Pty) Ltd v Bali* [1986] 1 All SA 289 (A).

¹²⁵ [1986] 2 All SA 450.

¹²⁶ *Barnett And Another v Abe Swersky & Associates* [1986] 2 All SA 450, 450.

¹²⁷ *Barnett And Another v Abe Swersky & Associates* [1986] 2 All SA 450, 449.

¹²⁸ [1989] 2 All SA 254 (C).

¹²⁹ 1909 TS 900.

¹³⁰ *Indrieri v Du Preez* [1989] 2 All SA 254 (C).

¹³¹ *Indrieri v Du Preez* [1989] 2 All SA 254 (C), 259.

¹³² *Indrieri v Du Preez* [1989] 2 All SA 254 (C), 259.

Cassim¹³³ is of the view that the measure of damages imposed on the agent should yield an amount that would place the third party in the position he would have been in had the company ratified the contract.

In *Indrieri v Du Preez*,¹³⁴ the court pointed to authority¹³⁵ that suggested that to hold the agent liable for a principal that does not exist would be in effect to make a new contract that neither party ever intended and that this was unacceptable. The court held that it is not possible to hold an agent liable for a non-existing principal as it is impossible to determine the amount that a non-existing person would be able to pay.¹³⁶ It is submitted that the court misinterpreted *Blower v Van Noorden*¹³⁷ and what Innes CJ said. The Chief Justice states that you do not look at the principal, as such, even if it did exist, you would ignore their existence. You would look towards the agent and discuss the extent of the misrepresentation. A court will use other documents that are available in order to look at the intention of parties in order to ascertain as to whether the parties intended for personal liability to come about.¹³⁸

Section 35 does not make reference to personal liability, and this was the position under the previous Companies Act¹³⁹ as well. In *Olifants Trust Co v Pattison*,¹⁴⁰ the applicant took the stance that the acceptance of personal liability caused the representative to adopt the position of principal rather than trustee and as such the formalities, as provided for in the Act, were not met. The court disagreed and stated that a person may accept personal liability and this in no way excludes the operation of section 71 of the previous Companies Act.¹⁴¹

In terms of section 35 of the 1973 Act, the trustee's or agent's liability was not catered for in terms of the Act. As such, an omission to cater for liability, and in the event of the company never coming into

¹³³ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 374.

¹³⁴ [1989] 2 All SA 254 (C).

¹³⁵ *Nordis Constructions Co (Pty) Ltd v Theron, Burke & Isaac* 1972 (2) SA 535 (D).

¹³⁶ *Indrieri v Du Preez* [1989] 2 All SA 254 (C), 261.

¹³⁷ 1909 TS 890.

¹³⁸ *Twenty Seven Bellevue CC v Hilcove* [1994] 2 All SA 293 (A), 297.

¹³⁹ Section 71 of the Companies Act 46 of 1926.

¹⁴⁰ [1971] 1 All SA 32 (W).

¹⁴¹ Companies Act 46 of 1926.

existence, would never give rise to personal liability in respect of the agent or trustee. The only instance that the trustee or agent would be liable, is if whether the contract provided for such liability, or the surrounding circumstances indicated that it was the parties' intention to hold the trustee or agent personally liable or there was a misrepresentation by the trustee or agent.

Cassim¹⁴² is of the view that one of the instances wherein the agent should be liable under the pre-incorporation contract is wherein the promoter uses a shelf company simply to adopt the contract, which company is insolvent and without assets. Leaving the third party with a meaningless claim.

As such, the contents of the contract, both from a common law position and statutory position, in terms of section 35 of the 1973 Act, make contents more important than formality.

¹⁴² Cassim, M.F. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 380.

CHAPTER 4 - POSITION UNDER THE COMPANIES ACT 71 of 2008

4. POSITION UNDER THE COMPANIES ACT 71 of 2008

As a point of departure, in discussing section 21 of the 2008 Act, it is important to note how the legislation has decided to create a more integrated provision which is better structured. Section 35 of the 1973 Act was a single section with no subsections wherein practitioners would have a mountain of requirements all jam packed into a single section. Section 21 is clear in providing a detailed, and notwithstanding the contents below, simple provision.

Reform was needed in respect of section 35 of the 1973 Act. Cassim points out that the previous section 35 of the 1973 Act was “too restrictive and out of step not only with the modern trends but also with modern business practices”.¹⁴³ According to Ncube, the reform of pre-incorporation contracts as provided for in terms of section 21 are commendable and provide for an equal balance in the interests of the companies, third parties and promoters. And that there has been a clear policy shift towards a “more balanced and nuanced treatment of third parties”.¹⁴⁴ The policy shift was needed for a more balanced treatment of “potentially predatory promoters and third parties – possibly unsophisticated entrepreneurs”.¹⁴⁵

Furthermore, the legislature has elected to supply a definition now in respect of pre-incorporation contracts. This is helpful as Cassim indicated that the word “contract”, as used in the 1973 Act was problematic as there is “strictly speaking not a contract at all until ratified by the company”.¹⁴⁶ In order to resolve this, he suggested a definition should be provided for in the Act to define pre-incorporation contracts. According to Ncube¹⁴⁷ this is important because it clearly indicates that it only applies to promoters acting as agent and not as principal. This has the implication that where a promoter acts as

¹⁴³ Cassim, M.F. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 365.

¹⁴⁴ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 269.

¹⁴⁵ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 258.

¹⁴⁶ Cassim, M.F. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 395.

¹⁴⁷ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 259.

principal, the position will be regulated according to common law.¹⁴⁸ According to Delport,¹⁴⁹ section 21 does not exclude the position under the common law. As such, it is still possible for a person to enter into a contract for the benefit of a third party under common law.

In addressing the contents of section 21 of the 2008 Act, the legislature has drastically overhauled the statutory position on pre-incorporation contracts. Noteworthy points, which will be more fully canvassed herein, pertain to:

- The reduction in formal requirements;
- The implementation of liability on the agent;
- Incorporation of provision for retrospectivity;
- Presumptions in respect of when companies have adopted contracts;
- Statutory time limits under which a company must ratify.

4.1 THE REMOVAL OF FORMAL REQUIREMENTS

It should be noted from the outset, that unlike section 35 of the 1973 Act, section 21 has disregarded majority of the formal requirements as laid down and required in terms of section 35 of the 1973 Act. Cassim¹⁵⁰ argues that the formalities set out in the 1973 Act were burdensome and non-compliance may result in the contract falling outside of the ambit of the Act and will therefore be dealt with under common law.

Unlike section 21 of the 2008 Act, section 35 of the 1973 Act required that two copies of the contract were to be lodged with the Companies Office. Ncube¹⁵¹ points out that section 8 of the Corporate Law Amendment Act of 2006 amended section 35 of the 1973 Act, wherein the requirement of lodging two copies of the pre-incorporation contract, one of which had to be notarised, was amended in that

¹⁴⁸ Ncube, C. "Pre-Incorporation Contracts : Statutory Reform" (2009) Vol 126 Issue 2 *SALJ* 255, 259.

¹⁴⁹ Delport, P "2017-Henochsberg on the Companies Act 71 of 2008" – Notes – Common law.

¹⁵⁰ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 393.

¹⁵¹ Ncube, C. "Pre-Incorporation Contracts : Statutory Reform" (2009) Vol 126 Issue 2 *SALJ* 255, 261.

only the contract was to be lodged. Section 21 of the 2008 Act completely removed this requirement and according to Ncube is a welcome and overdue development because it is “inequitable to companies and their co-contracting parties alike”.¹⁵² However, Ncube does point out that the removal of the requirement to lodge copies of the pre-incorporation contract prioritizes the protection of companies and the third parties who enter into pre-incorporation contracts over protection of potential creditors and investors. According to Cassim, the 1973 Act requirement that “two copies of the pre-incorporation contract need to be lodged at the Companies Office” is problematic in practice.¹⁵³ The main criticism is that although its aim is to protect investors, it discloses details to the public which details third parties may wish to keep confidential. Cassim¹⁵⁴ was of the view that this requirement be wholly abolished.

Like the 1973 Act, section 21 has retained the requirement that the contract must be reduced to writing. Cassim¹⁵⁵ is of the view that the requirement that the contract must be in writing should be retained as this provides for certainty and will ensure that the company receives full and proper disclosure of the terms of the pre-incorporation contract. According to Ncube the retention of the requirement that the pre-incorporation contract must be written is commendable as it is “dictated by the need for certainty and full disclosure”.¹⁵⁶

The requirement that the company must ensure that provision is made in its memorandum for ratification of the pre-incorporated contract has been removed and the position under the 2008 Act does not require that the memorandum of incorporation requires a provision for the adoption of the pre-incorporation contract as one of its objectives. According to Ncube¹⁵⁷ this is because of section 19(1)(b) in giving companies the capacity of a natural person and as such, there is no need to list the ratification of a particular pre-incorporation contract. Ncube¹⁵⁸ indicates that there are other reasons

¹⁵² Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 261.

¹⁵³ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 394.

¹⁵⁴ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 394.

¹⁵⁵ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 395.

¹⁵⁶ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 260.

¹⁵⁷ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 260.

¹⁵⁸ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 260.

for retaining a provision in the Act that a company will be required to list in its memorandum the pre-incorporation contracts that it intends to ratify, but that this is not so much an objective of the company, but simply as a disclosure requirement. And that this would protect outsiders who wish to extend credit or invest. Despite the removal of this requirement, Cassim states that promoters would be “well advised to continue to include the ratification of the pre-incorporation contract as objects of the company as it may be prudent to ensure that a certain amount of publication and disclosure to investors”.¹⁵⁹

Ncube¹⁶⁰ is of the view that Parliament, in removing provisions that a company is not required to list the adoption of a pre-incorporation contract in its memorandum, that potential prejudice to companies outweighs outsider protection. Ncube¹⁶¹ is of the view that this stance is justifiable because outsider protection can be achieved by other means such as requesting information directly from the company.

Another provision that created problems in interpretation is in respect of how the promoter announces himself. In the 2008 Act the person entering into the pre-incorporate contract must “purport”¹⁶² that they are doing so on behalf of or in the name of an entity that is contemplated to be incorporated. Ncube¹⁶³ places emphasis on the word “profess” and has indicated that the word literally means¹⁶⁴ “to declare openly: announce or affirm: avow or acknowledge”. Ncube goes on to point out that in the case of *Sentrale Kunsmis* at 397 Trollop JA stated that the word “connotes that, whilst the person declares that he is acting as a trustee, he is in fact or in law not one”.

Ncube¹⁶⁵ states that it is noteworthy that section 21 uses the term “purports” over words such as “declares” or “states”. Ncube points out that the word “purports”¹⁶⁶ means represent intentionally

¹⁵⁹ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 394.

¹⁶⁰ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 260.

¹⁶¹ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 261.

¹⁶² Section 21 of the Companies Act 71 of 2008.

¹⁶³ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 262.

¹⁶⁴ <http://www.dictionary.com/browse/profess> - last accessed 4th of June 2017.

¹⁶⁵ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 262.

¹⁶⁶ <http://www.dictionary.com/browse/purport> - last accessed 4th of June 2017.

either expressly or by implication. However, the word “declare” is to make an expressed statement. Thus the word “purport” is wider in meaning and broadens the ambit of section 21. It would appear that the word now adopted in the Act properly reflects the intentions of the legislature in respect of authority.¹⁶⁷ Ncube¹⁶⁸ does point out that it will be difficult to prove an implied representation but not impossible. As such, each matter would have to be evaluated on its own facts.

Under section 35 of the 1973 Act, no provision in respect of time for the ratification of the contract existed. Ncube¹⁶⁹ points out that one of the biggest improvements in the New Act is section 21(4) in that the company has 3 months within which to adopt the pre-incorporated contract. As such, it is no longer necessary for third parties to state a time period under which the contract must be adopted. Furthermore, unlike section 35 of the 1973 Act, third parties will not be in limbo if they fail to provide for a time period wherein the company is to adopt the pre-incorporation contract. Ncube states that section 21(4) accords companies a fair amount of time to consider the pre-incorporated contract and third parties benefit from this provision because they will have to wait a maximum of three months for the company’s decision.

The concept of making provision in the Act to cause the company to have deemed to have ratified the contract was discussed by Cassim. Cassim¹⁷⁰ indicates that as an alternative, provision could be made that upon incorporation the company is automatically bound but that this situation should firmly be avoided in South Africa. This is because deemed acceptance by a company may remove the company’s ability to carefully peruse and consider the contract before being bound by it.¹⁷¹ Cassim¹⁷² does however point out that there are certain services which a company may have been deemed to have accepted without ratification. These could be things like remuneration to promoters for costs incurred in the incorporation of the company. Further submissions that could be made in support of such a

¹⁶⁷ *Gaybelle Investments (Pty) Ltd V Hermer* [1951] 1 ALL SA 45(W), 45.

¹⁶⁸ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 263.

¹⁶⁹ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 264.

¹⁷⁰ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 383.

¹⁷¹ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 384.

¹⁷² Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 384.

provision could be contracts alike to that of contracts of employment.¹⁷³ However, Cassim submits that even this liability and circumstance of deemed acceptance should be avoided as promoters would have other remedies available to them.¹⁷⁴

Ncube¹⁷⁵ points out that section 21(5) is novel in that a company that does not take a decision within 3 months to adopt the pre-incorporation contract is deemed to have ratified the pre-incorporation contract. In terms of section 35 of the 1973 Act and the common law, there is no deemed ratification of a pre-incorporation contract.

Ncube¹⁷⁶ indicates that section 21(5) appears to be punitive in nature. However, any penalty should be looked at in conjunction with section 21(4) and the three-month grace period under which the company is forced apply its mind to the contract. It also assists in protecting the promoters whose liability in terms of the pre-incorporation will come to an end after three months once the company is deemed to have ratified the pre-incorporation contract. Ncube¹⁷⁷ states that section 21(4) and (5) “balance the interests of the third party, companies and promoters, and as such they constitute a marked improvement on section 35” of the 1973 Act.

When drafting commentary on section 35 of the 1973 Act, Cassim¹⁷⁸ states that the dual warranty could be placed on the agent but would only be effective if time limits were put into place under when events in terms of the contract should take place. Furthermore,¹⁷⁹ the time period should be a combined period and not a separated period for incorporation and rectification to take place, as two separate periods could give rise to anomalies. It is submitted that by introducing the deemed acceptances provision in its current form, advances the solution of the “dual warranty” as placed forward by Cassim in that the promoter is not left helpless in waiting endlessly for ratification to take

¹⁷³ *Taylor v Welkom Theatres (Pty) Ltd And Others* [1954] 3 All SA 135 (O).

¹⁷⁴ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 384.

¹⁷⁵ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 265.

¹⁷⁶ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 265.

¹⁷⁷ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 265.

¹⁷⁸ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 373.

¹⁷⁹ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 374.

place. There is either an expressed decision by the company to reject the contract, or the promoter is released after three months.

4.2. LIABILITY UNDER SECTION 21

One of the most controversial topics of pre-incorporation contracts pertains to the position on liability. Assumptions in respect of liability, as per the previous two chapters, are almost non-existent. Under the common law and section 35 of the 1973 Act, a failure to provide for liability in terms of the pre-incorporation contract would mean that no such liability existed.¹⁸⁰ Section 21 has altered this position.

According to Cassim,¹⁸¹ and prior to section 21, in order to balance the conflicting rights between all parties (third party, promoter and company) involved in a pre-incorporation contract, statute should provide for an implied dual warranty by the agent that the company will not only be incorporated, but will also ratify the pre-incorporation contract. This dual warranty is referred to by Cassim as the Liability Proposal.¹⁸²

Section 21(2) provides that a person or persons that act in terms of section 21(1) are jointly and severally liable in terms of the pre-incorporation contract on two separate grounds. Firstly, a promoter may be liable on the basis that the company as envisaged in terms of the pre-incorporation does not come into existence, or secondly, after the company is incorporated, it fails to ratify the pre-incorporation contract. It is submitted that the liability of the agent is similar to that of a principal now.¹⁸³

As indicated above, Cassim¹⁸⁴ commented on section 35 of the 1973 Act and was of the view that statute should deem an agent personally liability on a pre-incorporation contract by way of a dual statutory warranty that the company will be incorporated and that upon its incorporation that the

¹⁸⁰ *Peak Lode Gold Mining Co., Ltd. V Union Government* 1932 TPD 48.

¹⁸¹ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 366.

¹⁸² Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 368.

¹⁸³ *Gompels v Skodawerke Of Prague* 1942 TPD 167, 171.

¹⁸⁴ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 372.

company will ratify the contract. Although this would be implied on pre-incorporation contracts, Cassim¹⁸⁵ does place emphasis on parties being able to expressly contract out of such liability.

In respect of the reference to being able to hold persons other than the promoter liable, Ncube¹⁸⁶ has pointed that the reference to “any other such person” as provided for in terms of section 21(2) is not clear in respect of who this refers to. And that if they are not legally appointed as such, are *de facto* occupying such positions. Ncube submits that the inclusion of the words “any other such person” could be in respect of a situation where there are two or more promoters and only one signs the pre-incorporation contract.¹⁸⁷

According to Cassim¹⁸⁸ it is equitable and efficient to burden the promoter with non-incorporation or non-ratification of the pre-incorporation contract as promoters often have a significant influence on the pre-incorporation contract being ratified. This is more so when the promoters also become the company’s directors and shareholders. Consequently,¹⁸⁹ the agent should be held liable to the third party for either non-incorporation or, upon the company’s incorporation, failure to adopt the pre-incorporation contract.

Cassim¹⁹⁰ has identified the scenario wherein more than one promoter represents a company and is of the view that liability in respect of such promoters should be jointly and severally liable and not just in respect of the promoter that signed the pre-incorporation contract.

According to Ncube¹⁹¹ section 21(7) provides protection to a promoter who finds themselves liable to a third party where a company has received some benefit in terms of a pre-incorporation contact. The promoter can then seek a joinder of the company in any litigation proceeding and obtain an order directing the company to return the goods received directly to the third party.

¹⁸⁵ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 372.

¹⁸⁶ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 266.

¹⁸⁷ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 266.

¹⁸⁸ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 368.

¹⁸⁹ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 369.

¹⁹⁰ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 377.

¹⁹¹ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *S.A.L.J* 255, 268.

Over and above the joinder of other promoters, various other considerations exist in respect of the extent of the promoter's liability. As per section 21(3), reference is made to a circumstance under which a promoter should be released from liability. Cassim¹⁹² is of the view that personal liability should be limited to various circumstance. This being, *inter alia*, firstly, wherein the promoter becomes a director of the company and elects not to ratify the pre-incorporation contract; secondly, parties should be entitled to expressly be entitled to contract out of personal liability; thirdly, where that company enters into a new contract which is similar or the same as the previous contract;¹⁹³ Lastly, Cassim¹⁹⁴ submits that the court should be given a wide discretion to determine personal liability where it is just and equitable to do so. In exercising this discretion the Court should take into consideration relevant factors such as the capitalisation of the company and control which the promoter exercised over the company being incorporated.¹⁹⁵

Cassim¹⁹⁶ points out that to impose personal liability on the agent for a pre-incorporated contract blurs the distinction between a pre-incorporated contract and the *stipulatio alteri*. This is because where the agent assumes personal liability, they are generally regarded as stepping into the shoes of the company and by the same token entitled to enforce the contract personally against the third party, acquire rights and obligations under the contract and sue the third party for performance.¹⁹⁷ Reference is further made to the interim period and Cassim¹⁹⁸ states that if an agent is not personally liable on a pre-incorporation contract during the interim period then there is in effect no contract during this period. Creating a provision that the agent is personally liable on the contract will ensure that there is a at all times an enforceable contract.¹⁹⁹

¹⁹² Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 378.

¹⁹³ Previously the Court held that the only way for a company to adopt rights in terms of agreement was on the basis that a new contract be drawn up (*Magnus Diamond Mining Co. Ltd. v Welgegund Diamond Mining Co. Ltd* 1910 ORC 22). As such the legislature has now considered and made room for both the eventuality that a pre-incorporated contract is drawn up and that a subsequent contract is drawn up on identical terms. Section 21(3) of the Companies Act 71 of 2008 has incorporated such a provision.

¹⁹⁴ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 379.

¹⁹⁵ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 381.

¹⁹⁶ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 370.

¹⁹⁷ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 370 -371.

¹⁹⁸ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 371.

¹⁹⁹ The period between the agent and third party enter the pre-incorporation contract and the time when the company ratifies the contract.

Cassim²⁰⁰ further points out that personal liability could be extended to the company's future solvency. However, Cassim states that this, in light of the current business environment in South Africa, would be an excessively heavy burden for promoters to bear.²⁰¹

4.3. CRITICISM AGAINST SECTION 35

Ncube²⁰² does point out there are deficiencies in section 21 in respect of the following points. Firstly, the section fails to state in expressed terms that ratification is retrospective in effect and instead uses a formulation that has proven to be problematic.

It was submitted in *Peak lode Gold Mining Co Ltd v Union Government 1932 TPD 48* that the contract came into operation on date of ratification or adoption and not retrospectively. According to Delpont,²⁰³ this is no longer problematic as section 21(6)(a) seems to allow ratification to operate retrospectively.

In his work on section 35 of the 1973 Act, Cassim²⁰⁴ is of the view that reform is needed in order to place certainty in that pre-incorporation contracts operate with retrospective effect. This retrospective effect must apply from "the date that the contract was made by the agent and the third party and not merely to the date that the company was incorporated". Parties should however be entitled to vary this position.

Ncube²⁰⁵ is of the view that section 21(6)(a) has attempted to provide clarity in respect of whether pre-incorporation contracts have retrospective effect. Criticism is levelled against section 21(6)(a) as the formulation of this section has proven to be problematic because it does not indisputably provide for retrospective effect. Ncube²⁰⁶ points out that some scholars have debated that the formulation

²⁰⁰ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 372.

²⁰¹ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 373.

²⁰² Ncube, C. "Pre-Incorporation Contracts : Statutory Reform" (2009) Vol 126 Issue 2 *SALJ* 255, 269.

²⁰³ Delpont, P. "2017-Henochsberg on the Companies Act 71 of 2008" – Notes - General Notices.

²⁰⁴ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 388.

²⁰⁵ Ncube, C. "Pre-Incorporation Contracts : Statutory Reform" (2009) Vol 126 Issue 2 *SALJ* 255, 265.

²⁰⁶ Ncube, C. "Pre-Incorporation Contracts : Statutory Reform" (2009) Vol 126 Issue 2 *SALJ* 255, 265.

meant ratified pre-incorporation contracts were retrospective to date of their conclusion and others arguing that they are retrospective to date of the company incorporation.

Section 21 of the new Act has the following provision in respect of retrospectivity, “the company as if the company had been a party to the agreement when it was made”. Cassim²⁰⁷ indicates, without reference to the 2008 Act, that this is an international trend of wording that is being used in respect of pre-incorporation contracts. Cassim points out that this wording has led to controversial academic debate and does “not go far enough to show a clear and unambiguous legislative intention”.²⁰⁸ South Africa should improve on the problems experienced by other jurisdictions and go further than the use of this populate wording.

Ncube submits that the section should read “pre-incorporation contracts have a retrospective effect and are binding from the date of their conclusion”.²⁰⁹ This would remove confusion and correspond to ratification at common law.

The second shortcoming that Ncube²¹⁰ identifies is that section 21 does not provide for the manner in which ratification must take place. Criticism levelled by Ncube²¹¹ is that section 21 does not provide for the manner in which ratification is to take place. He further goes onto indicate that the Close Corporations Act provided for certainty in respect of the manner in which ratification should take place. As of present, it is entirely up to the company to determine the manner of ratification or rejection.²¹²

When discussing the manner under which the ratification of the pre-incorporation contract should take place, Cassim²¹³ submits that a board resolution should generally suffice. However, an independent board should be used where the promoter constitutes majority of the board as

²⁰⁷ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 388.

²⁰⁸ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364,388.

²⁰⁹ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 265.

²¹⁰ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 269.

²¹¹ Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 264.

²¹² Ncube, C. “Pre-Incorporation Contracts : Statutory Reform” (2009) Vol 126 Issue 2 *SALJ* 255, 264.

²¹³ Cassim, MF. “Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act” (2007) 2 *SALJ* 364, 385 – 386.

ratification may be used in order to absolve the promoter from liability. The fact that board would in such a circumstance have an interest in ensuring that the company adopts the pre-incorporation contract, means that the ratification should rather be left to the company in the general meeting.²¹⁴

Cassim²¹⁵ states that ratification by conduct may enhance business efficiency and business convenience, as well as serve the interests of third parties. However, this should be avoided in South Africa because the negative consequences outweigh the possible benefit. Negative consequences as expressed by Cassim can be summed up as follow: Firstly, ratification by conduct may result in uncertainty as to when and whether a pre-incorporation contract was ratified.²¹⁶ Secondly, whether the company's silence may amount to ratification would cause further complexities.²¹⁷ Thirdly, ratification by conduct for business efficiency is arguable. A promoter turned director is under a fiduciary duty to disclose interests in the pre-incorporation contract. The formalities in disclosing such an interest may be no less formalistic than express ratification.²¹⁸ Lastly, Cassim²¹⁹ points out that where the promoter turns sole or majority director and shareholder it may be difficult to prove whether the company had knowledge of the pre-incorporation contract. It is submitted that this last point does not constitute a ground for rejection of ratification by conduct as the promoter/director would constitute the mind of the company and obviously be aware of all current dealings of the company, including the pre-incorporation contract.

The third shortcoming that Ncube²²⁰ points out is that section 21 does not apply to promoters acting as principal. Ncube²²¹ points out that section 21 does not apply to a promoter acting as principal. As such, there is no protection in terms of section 21 for third parties contracting with promoters acting as principal. Ncube²²² states that there is no convincing reason for this distinction and that section 21

²¹⁴ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 385 – 386.

²¹⁵ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 386.

²¹⁶ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364,386.

²¹⁷ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 387.

²¹⁸ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 387.

²¹⁹ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 387.

²²⁰ Ncube, C. "Pre-Incorporation Contracts : Statutory Reform" (2009) Vol 126 Issue 2 *SALJ* 255, 269.

²²¹ Ncube, C. "Pre-Incorporation Contracts : Statutory Reform" (2009) Vol 126 Issue 2 *SALJ* 255, 263.

²²² Ncube, C. "Pre-Incorporation Contracts : Statutory Reform" (2009) Vol 126 Issue 2 *SALJ* 255, 264.

should have included promoters acting a principal. Cassim²²³ is of the view that the scope of pre-incorporation contracts should be limited to instances where the promoter acts as agent and not principal.

Cassim²²⁴ is of the view that mutual cancellation between the agent and third party should be prohibited by statute. Furthermore, Cassim is of the view that unilateral withdrawal from the pre-incorporation contract by the third party should be prohibited. This is because if unilateral withdrawal was permissible, then provisions dealing with pre-incorporation agreement would be nothing more than a gentlemen's agreement. Furthermore, if promoters were liable under unratified pre-incorporation contracts, it would be unfair to allow third parties to unilaterally withdraw.²²⁵ Exception should however be made wherein an expressed provision be provided for in the contract.

In considering the unilateral withdrawal from a contract, Cassim²²⁶ discusses the interim period and states that if personal liability was incurred by the agent, for an unratified pre-incorporation contract, then the problems associated would be resolved in part as the third party would be unable to unilaterally withdraw from the contract. However, mutual cancellation would then become permissible.

Lastly, the wording of section 21 is clear in that the company must not be in existence at the time that the contract is entered into. According to Delport,²²⁷ the application of section 21 does not extend itself to companies that are already in existence. As such, on a strict interpretation, a shelf company would not fall within the ambit of section 21. Furthermore, the courts have adopted a similar stance disallowing the application of section 21 in respect of shelf-companies.^{228 229} Delport submits that this approach would lead to "insensible or unbusinesslike results".

²²³ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 367.

²²⁴ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 393.

²²⁵ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 390.

²²⁶ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364, 390.

²²⁷ Delport, P. "2017-Henochsberg on the Companies Act 71 of 2008" – Notes - General Notices.

²²⁸ *Eldacc (Pty) Ltd v Bidvest Properties (PTY) Ltd* (682/10) [2011] ZASCA 144.

²²⁹ Prior to this interpretation by the Courts, that Court ruled that where a contract made mentioned to a company to be used and a shelf company was used, the courts ruled that there was in principle no difference between a company to be incorporated and a shelf-company (*Venalex (Pty) Limited V Vighraha Property*

CHAPTER 5 - POSITION UNDER OTHER JURISDICTIONS

5. POSITION IN OTHER JURISDICTIONS

In this chapter, we explore the position and status that pre-incorporation contracts have held in the United Kingdom. Reasons for this can be attributed to the decision of *Kelner vs Baxter*²³⁰ wherein the Court ruled that it was impossible for a person to act as a trustee for a principal that did not exist at the time that the agreement was concluded.

The departure point in this chapter will lean towards the strict approach adopted by the courts wherein it was impossible for agents and trustees to represent unformed or unincorporated companies, as well as the results that followed in such instances, and will end on the adoption of section 51 of the Companies Act 2006 and its predecessor Section 36C of the Companies Act 1985.

5.1. COMMON LAW POSITION IN THE UNITED KINGDOM

In the past, despite no existing statute, the courts have taken invalid contracts into consideration in deciding the extent of damages and claims. In the case of *Rover*²³¹ the Court stated that the reason for allowing the appellant to claim instalments in terms of the void contract was due to a “total failure of consideration”. The Court ruled that recovery of the claim as a result of mistake would find equal application.²³² And that a party under a void contract would be entitled to claim expenses.²³³

Cc 5452/2014 KZN paragraph 14). In other cases that Court went even further to indicate that in a pre-incorporated contract, the third party may have a specific company in mind (*CShell 271 (Pty) Limited v Oudtshoorn Municipality* [2013] JOL 31070 (SCA) page 13). As such, it is submitted, that the requirement that the company must not be in existence may be problematic and should be extended to shelf companies and nominated companies.

²³⁰ (*L.R. 2 CP 174*)

²³¹ *Rover International Ltd and others v Cannon Film Sales Ltd* (No 3) [1989] 3 All ER 423.

²³² *Rover International Ltd and others v Cannon Film Sales Ltd* (No 3) [1989] 3 All ER 423, 434 and 443.

²³³ *Rover International Ltd and others v Cannon Film Sales Ltd* (No 3) [1989] 3 All ER 423, 435.

Regardless of being able to use a void contract to establish the extent of a claim, the courts have stated that where an agreement is void, it was not possible to rely on it through estoppel or ratification.²³⁴

However, although the contract is void, a quantum meruit for services rendered is allowed.²³⁵

However, in deciding on the amount to be awarded under a quantum meruit, the courts have ruled that there is no ceiling for the following reasons: 1) In the *Rover*²³⁶ decision it was the Respondent's that had noted the invalidity of the agreement and then pressured this point, despite the "invalidity having no practical significance for the parties' bargain", 2) the contention of a ceiling would not be in accordance with the principal, 3) that the imposing of a ceiling would have far reaching consequences in other situations which it would be impossible to distinguish in principal.²³⁷

According to Griffiths, pre-incorporation contracts should in theory comprise an element of intention that the company is to be formed.²³⁸

5.2. ARTICLE 7 OF THE FIRST EUROPEAN COMMUNITIES COMPANY LAW DIRECTIVE²³⁹ AND SECTION 9(2) OF THE EUROPEAN COMMUNITIES ACT 1972

Griffiths points out that at common law a newly formed company could not ratify or adopt the pre-incorporation contract. As such, a fresh contract or novation would be required. This was likewise the prevailing position in South Africa.²⁴⁰ Promoters would have to accept personal liability after the company had been incorporated unless novation or release took place by the third party. Equally, even after the company was incorporated, at common law, the third party would only be able to enforce the contract against the agent and not the newly-formed company.²⁴¹

²³⁴ *Rover International Ltd and others v Cannon Film Sales Ltd* (No 3) [1989] 3 All ER 423, 430.

²³⁵ *Rover International Ltd and others v Cannon Film Sales Ltd* (No 3) [1989] 3 All ER 423, 432.

²³⁶ *Rover International Ltd and others v Cannon Film Sales Ltd* (No 3) [1989] 3 All ER 423.

²³⁷ *Rover International Ltd and others v Cannon Film Sales Ltd* (No 3) [1989] 3 All ER 423, 436.

²³⁸ A Griffiths "Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985" *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241 – page 242 note 5.

²³⁹ (68/151/CEE OJ No. 1968 L6).

²⁴⁰ *Natal Land and Colonization Company, Ltd. v Pauline Colliery and Developing Syndicate, Ltd.* (1904) 25 NLR 1, 6.

²⁴¹ A Griffiths "Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985" *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241 – page 243 – 244.

In the United Kingdom, prior to any governing legislation the courts had adopted the stance where an agreement was entered into by a company prior to its incorporation, that contract was void.²⁴² This approach reflected the position in South Africa at the time.²⁴³ The Court retained the position that it was not relevant as to whether a person acted as trustee or agent, the contract would be a nullity.

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One of the first enactments that came about was Article 7 of the First European Communities Company Law Directive (Article 7).²⁴⁵ Article 7 was a directive in respect of the recognition of pre-incorporation contracts and the liability of an agent, which liability would accompany such contracts.²⁴⁶ Despite the attempt at changing the law, there were glaring shortcomings in Article 7 such as what the relationship between the agent and third party was, whether the agent was entitled to benefits under the contract in the event that the company fails to form and lastly conditions that the agent could be released from liability.

According to Griffiths the problem with pre-incorporation contracts was due to the essential “artificial nature of a company’s existence”, which existence is a matter of legal formality.²⁴⁷ Article 7 did not cater for any formalities that were to be met in entering into such a contract, whether the agent or trustee was entitled to exercise any rights in respect of the contract or if there was any limitation to the agent or trustee’s liability.

Griffiths states that the risk of nullity and the non-ratification of pre-incorporation contracts justified reform of the common law on the grounds of fairness and reducing the costs of contracting.²⁴⁸ This

²⁴² *Newborne v Sensolid (Great Britain) Ltd* [1953] 1 All ER 708.

²⁴³ *Natal Land and Colonization Company, Ltd v Pauline Colliery and Developing Syndicate, Ltd.* (1904) 25 NLR 1.

²⁴⁴ *Newborne v Sensolid (Great Britain) Ltd* [1953] 1 All ER 708, 710.

²⁴⁵ (68/151/CEE OJ No. 1968 L6).

²⁴⁶ Article 7 stated: “If, before a company being formed has acquired legal personality, action has been carried out in its name and the company does not assume the obligations arising from such action, the person who acted shall, without limit, be jointly and severally liable therefore, unless otherwise agreed.”

²⁴⁷ A Griffiths “Agents without principles: pre-incorporation contracts and section 36C of the Companies Act 1985” *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 241.

²⁴⁸ A Griffiths “Agents without principles: pre-incorporation contracts and section 36C of the Companies Act 1985” *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 244.

reform, as will be discussed below, came in the form of section 9(2) of the European Communities Act 1972 which provisions intended to give all pre-incorporation contracts legal effect thereby removing the risk of nullity.²⁴⁹ It is submitted, that all this provision did was provide for recognition and add liability to the agent.

Section 9(2) of the European Communities Act 1972 (Section 9(2)) was very similar to Article 7. One of the first decisions wherein section 9(2) found application was that of *Phonogram Ltd v Lane*.²⁵⁰ In *Phonogram Ltd v Lane* the legal question was whether the agent was required to refund the third party. The Appellant argued that section 9(2) was limited to companies that were already in the course of formation and that the word “purports”, as used in section 9(2) meant that the company must be in existence. The Court rejected this argument and held that section 9(2) of the European Communities Act 1972 was clear in that where a person contracts on behalf of a company not yet formed then that person is personally liable.²⁵¹

The court further pointed out that the wording “purports” does not mean that the company is in existence. And that a contract can purport to be made where both parties are aware that the company does not exist.²⁵²

As can be noted from the above, one of the more substantial changes had been the inclusion of personal liability for the agent. Griffiths points out that an agent can act in 2 distinct ways, firstly as an agent in the normal sense and secondly as an instrument. Griffiths points out that the courts do not enquire along these lines and make a distinction.²⁵³ The courts however have pointed out that the aspect of liability is limited to the extent expressed in the contract.²⁵⁴ As such, despite the inclusion of

²⁴⁹ A Griffiths “Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985” *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 244.

²⁵⁰ [1981] 3 All ER 182.

²⁵¹ *Phonogram Ltd v Lane* [1981] 3 All ER 182, 183.

²⁵² *Phonogram Ltd v Lane* [1981] 3 All ER 182, 186.

²⁵³ A Griffiths “Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985” *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241 – page 242 note 8.

²⁵⁴ *Phonogram Ltd v Lane* [1981] 3 All ER 182, 187.

deemed liability, this was only prima facie, and could be discharged where a contract's intention was shown. According to Griffiths, with reference to case law,²⁵⁵ this stance is correct and as such it is the intention of the parties that should be looked at and not the names of parties.²⁵⁶

The identity and name of a party used in pre-incorporation contracts may have troubling results. Griffiths further states that there may be the instance wherein a company is named in the pre-incorporation contract, which company name may have existed in the past, resulting in both the pre-incorporation contract being void and outside the scope of section 36C of the Companies Act 1985.²⁵⁷ It is submitted that this argument is flawed as it cannot be so simple to defeat the purpose provided for section 36C.

As such, the Court's indicated that in looking at the contract it is more important to consider the intentions of the parties rather than a distinction between signature.²⁵⁸

5.3. SECTION 36C OF THE COMPANIES ACT 1985 AND SECTION 51 OF THE COMPANIES ACT 2006

Following section 9(2) of the European Communities Act 1972 was the introduction of section 36C of the Companies Act 1985. Griffiths indicates that it was not entirely clear from the provision as to whether the pre-incorporation contract as mentioned under section 36C²⁵⁹ was one wherein the agent and the third party could enforce the contract, or whether this was limited to the third party.²⁶⁰ Griffiths submits that if the contract is enforceable by both the agent and third party, then the limits on the scope of section 36C should apply equally.²⁶¹

²⁵⁵ *Oshkosh B'Gosh Inc v Dan Marbel Inc Ltd* (1988) 4 BCC 795.

²⁵⁶ A Griffiths "Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985" *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 248.

²⁵⁷ A Griffiths "Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985" *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 247.

²⁵⁸ *Phonogram Ltd v Lane* [1981] 3 All ER 182, 188.

²⁵⁹ Companies Act 1985.

²⁶⁰ A Griffiths "Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985" *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 245.

²⁶¹ A Griffiths "Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985" *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 246.

The above question was considered in *Royal Mail Estates Limited v Maple Teesdale Borzou Chaharsough Shirazi*.²⁶² In this matter the Defendant adopted the stance that section 36C did not apply as the provision of the contract read that “the benefit of this contract is personal to the Buyer”.²⁶³ As such, the benefit under the contract could never be that of the agent, and as such was an “agreement to the contrary” and the Defendant was not personally liable under the contract.²⁶⁴ The Defendant argued that the exclusion of its ability to receive the benefit had the effect that it excluded the burden.²⁶⁵ In giving consideration to this, the Court considered 1) Whether it is possible to exclude the effect of section 36C by agreement, 2) if there is an agreement that excludes any part of section 36C, does it exclude it entirely.²⁶⁶

After considering the contents of the contract, the court came to the conclusion that the wording did not operate as a “contrary agreement” for the purposes of section 36C.²⁶⁷ The court however still reached a verdict that the provision of section 36C did not apply as it was not the intention of the parties.²⁶⁸

It is submitted that the judgment given in *Royal Mail Estates Limited v Maple Teesdale Borzou Chaharsough Shirazi*²⁶⁹ is flawed. The court started on the correct note in making reference to the provisions from where section 36C had its roots.²⁷⁰ The court then started drawing inferences that section 36C required that the benefit goes to the agent where the agent finds himself personally liable, and the parties required intention for the provision to apply. This simply cannot be correct. The

²⁶² Court of Appeal Chancery Division, July 02, 2015, [2015] WLR(D) 290,[2015] EWHC 1890 (Ch).

²⁶³ *Royal Mail Estates Limited v Maple Teesdale Borzou Chaharsough Shirazi*, Court of Appeal - Chancery Division, July 02, 2015, [2015] WLR(D) 290,[2015] EWHC 1890 (Ch) para 12.

²⁶⁴ *Royal Mail Estates Limited v Maple Teesdale Borzou Chaharsough Shirazi*, Court of Appeal - Chancery Division, July 02, 2015, [2015] WLR(D) 290,[2015] EWHC 1890 (Ch) para 34.

²⁶⁵ *Royal Mail Estates Limited v Maple Teesdale Borzou Chaharsough Shirazi*, Court of Appeal - Chancery Division, July 02, 2015, [2015] WLR(D) 290,[2015] EWHC 1890 (Ch) para 36.

²⁶⁶ *Royal Mail Estates Limited v Maple Teesdale Borzou Chaharsough Shirazi*, Court of Appeal - Chancery Division, July 02, 2015, [2015] WLR(D) 290,[2015] EWHC 1890 (Ch) para 35.

²⁶⁷ *Royal Mail Estates Limited v Maple Teesdale Borzou Chaharsough Shirazi*, Court of Appeal - Chancery Division, July 02, 2015, [2015] WLR(D) 290,[2015] EWHC 1890 (Ch) para 62.

²⁶⁸ *Royal Mail Estates Limited v Maple Teesdale Borzou Chaharsough Shirazi*, Court of Appeal - Chancery Division, July 02, 2015, [2015] WLR(D) 290,[2015] EWHC 1890 (Ch) para 63.

²⁶⁹ Court of Appeal Chancery Division, July 02, 2015, [2015] WLR(D) 290,[2015] EWHC 1890 (Ch).

²⁷⁰ Para 15 – Article 7 of the First Council Directive of the Council of the European Communities (68/151/EEC) – which read “if, before a company being formed has acquired legal personality, action has been carried out in its name and the company does not assume the obligations arising from such action, the persons who acted shall, without limit, be jointly and severally liable therefor, unless otherwise agreed”.

purpose of the provision is clear; the agent inherits liabilities not benefits. This is done in order to protect the third party, not ensure that a contract comes into existence. Furthermore, on a contextual interpretation, the application of the section applies only to the extent that parties expressly agree otherwise. Application of the provision is assumed and only excluded if that is the parties' intention.

Griffiths states that if a pre-incorporation contract is made by an agent using a name of company, section 36C would only apply so long as no company having that name had been formed when the contract was entered and that it is arguable that the provision requires more than the mere use of a non-existent corporate name.²⁷¹ It is submitted that this interpretation is incorrect. The name should have no bearing on the validity of the pre-incorporation contract and that the most important requirement is that the company must not be in existence at the time that the pre-incorporated is concluded. Thus, the argument would be whether the company's registration number existed or not at the time that the pre-incorporation contract was made.

Griffiths further states, with reference to case law,²⁷² that the application of section 36C is limited to companies registered in terms of the Companies Act²⁷³ and excludes foreign companies. Griffiths states that this submission is arguable in light of the context of section 36C and that the discrimination would put an "arbitrary limitation on the scope" of section 36C.²⁷⁴

However, despite the view submitted above, the English courts have in other judgments²⁷⁵ given more substantial and justified reasons for stating that the agent is entitled to receive the benefit in terms of a pre-incorporation contract. In *Braymist Ltd. & Ors v Wise Finance Company Ltd*²⁷⁶ the legal question

²⁷¹ A Griffiths "Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985" *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 246.

²⁷² *Rover International Ltd v Cannon Film Sale Ltd* (1987) BCLC 540.

²⁷³ 1985.

²⁷⁴ A Griffiths "Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985" *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 250 – 251.

²⁷⁵ *Braymist Ltd. & Ors v Wise Finance Company Ltd*. [2002] EWCA Civ 127.

²⁷⁶ [2002] EWCA Civ 127.

was whether the agent is not only liable in terms of the pre-incorporation contract but also entitled to sue on it where section 36C found application.

The Appellant made the submission that the purpose of section 36C was only to hold the agent liable and that the provision was limited in application.²⁷⁷ The Appellant stated that it was not possible to hold the agent liable as it would have a bizarre result in giving agents the ability to sue on the contract and the agent would have become a party to the agreement which may not reflect the parties intentions.²⁷⁸ The Appellant submitted that the sole effect of section 36C was to prevent the agent from denying the existence of a contract.²⁷⁹ And that a third party is protected by having someone that he can hold liable, not a deemed contract. Moreover, the Appellant argued the scenario where there are multiple parties acting as agent, and if the agents are entitled to sue on the contract, which agent would be entitled to the benefit.²⁸⁰

The Respondent made the submission that the “tailpiece”²⁸¹ abolished the common law distinction.²⁸² And that a pre-incorporation contracts required mutuality. The effect of section 36C was to make the agent personally liable and make the agent the principal.²⁸³

In ascertaining the assertions placed forward by the parties, the court first turned to the directive from where section 36C stemmed and highlighted that emphasis was placed on protecting of shareholders, creditors and third parties. However, there was no reference to allowing the agent to become the principal.²⁸⁴ As a result the court had to reference decisions in the European Court of Justice, however,

²⁷⁷ *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127 para 24.

²⁷⁸ *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127 para 25.

²⁷⁹ *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127 para 26.

²⁸⁰ *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127 para 28.

²⁸¹ The last portion of Section 36C – “and he is personally liable on the contract accordingly”.

²⁸² *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127 para 38.

²⁸³ *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127 para 41.

²⁸⁴ *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127 para 51.

this point had not be considered by the European Court of Justice and as such no authority on the subject could be found.

The court concluded that the “tailpiece” and its extend or limited application were left to general law for determination and thus the common law applied as to whether the agent can enforce the contract.²⁸⁵ In deciding this question, the court considered the various circumstances that could exist. Where the principal is identified, the agent cannot intervene, and where the principal is unidentified, the agent can only intervene if he fits such description as has been given of the supposed principal.²⁸⁶ The court further considered the position where the agent is in fact principal, and that this can happen where the third party cannot be influenced by the personal qualities of the principal and part performance has been accepted by the third party with full knowledge that the agent in the contract was real principal.²⁸⁷

Griffiths states that there may be an instance wherein a third party intends to contract with a company connected to the agent, while accepting that the contract and it obligations and rights would be with the company and that the agent would ensure that such a company would be an existing company.²⁸⁸ It is submitted that an instance like this cannot even be considered as it goes against the fundamentals of pre-incorporation contracts as the agent falls out of the contract all together once ratification takes place and the company can never be an existing company.

The Court in *Braymist* concluded that section 36C was created to comply with Article 7 of the First Directive, holding the agent liable under the pre-incorporation contract and placing the agent in the

²⁸⁵ *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127 para 59.

²⁸⁶ *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127 para 60.

²⁸⁷ *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127 para 61.

²⁸⁸ A Griffiths “Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985” *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 246.

same position in respect of enforcement as they would be at common law.²⁸⁹ As a result, the Court held that the contract was enforceable by the agent.²⁹⁰

It is noteworthy that the Canadian province of Ontario makes it clear as to who would be liable in terms of a pre-incorporation contract and whether the agent would be entitled to the benefit under a pre-incorporation contract through section 21(1) of the Ontario Business Corporate Act 1990 which read as follows: “except as provided in this section, a person who enters into an oral or written contract in the name of or on behalf of a corporation before it comes into existence is personally bound by the contract and *is entitled to the benefits thereof*” (Own emphasis).

Section 36C is far from perfect and for the most part²⁹¹ is inferior to South Africa’s section 21 of the 2008 Act. Griffiths submits that if section 36C is to be amended, non-ratification should also be addressed as well as relieving the agent of personal liability and the circumstances under which the third party can enforce the contract.²⁹²

Griffiths states, in conclusion, that the courts have limited the scope of section 36C by requiring that there must be a particular would-be contractual party whose identity and characteristics can be ascertained.²⁹³ Further limitation can be attributed to, as stated by Griffiths with reference to case law,²⁹⁴ to companies registered in terms of the Companies Act²⁹⁵ and excluding foreign companies. Griffiths states that this submission is arguable in light of the context of section 36C and that the discrimination would put an “arbitrary limitation on the scope” of section 36C and that it is not

²⁸⁹ *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127 para 62.

²⁹⁰ *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127 para 66.

²⁹¹ Failing to provide for 1) period for consideration and thereafter deemed acceptance, 2) release of agent from liability and 3) whether retrospectivity has any effect on the contract.

²⁹² A Griffiths “Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985” *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 252 – 253.

²⁹³ A Griffiths “Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985” *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 252.

²⁹⁴ *Rover International Ltd v Cannon Film Sale Ltd* (1987) BCLC 540.

²⁹⁵ 1985.

important as to where the companies are formed, but where the parties intended that the company would be formed.²⁹⁶

The United Kingdom's own Courts²⁹⁷ have recognised weakness in the provision and despite this, section 36C successor section 51 of the Companies Act 2006 uses identical wording. The position under section 51 has not altered anything at all. There is still no clarity, *inter alia*, as to whether the agent can enforce the contract, whether the agent can be released or whether retrospectivity finds application.

²⁹⁶ A Griffiths "Agents without principles : pre-incorporation contracts and section 36C of the Companies Act 1985" *The Journal of the Society of Legal Scholars* - Volume 13, Issue 2 July 1993 pages 241, 250 – 251.

²⁹⁷ *Braymist Ltd. & Ors v Wise Finance Company Ltd.* [2002] EWCA Civ 127.

CHAPTER 6 - CONCLUSION

It is submitted that the purpose of company law is to create a vehicle which has the effect of causing people to interact with one another without the fear of liability where interactions are *bona fide*. These interactions cause people to work in a commercial sense and allow various commodities, goods and services to come into existence.

Aspects that assist in giving rise to this objective have been recognised in pre-incorporated contracts and their earlier counter-part, the *stipulatio alteri*. Governments, academics and the business world have recognised this, and saw that there was a desirable effect of giving legal recognition to such contracts.

The earliest recognition was vague and failed to provide details in respect of the relationship between the promoter and the third party, manner of adoption, whether retrospectivity was applicable and liability in respect of the promoter.²⁹⁸

As pointed out, the English common law originally dictated that such pre-incorporation contracts were void and that despite wide acceptance of this form of contract, English statute has fallen behind leaving large gaps to be filled in by their courts.²⁹⁹

The short falls experienced in the United Kingdom are, *inter alia*, the failure to provide for when the promoter is released, details in respect of the relationship between the promoter and third party, whether pre-incorporated contracts have retrospective effect and the manner that is to be applied when adoption takes place, to name a few.³⁰⁰

These short comings exist despite Companies Act 1985 and Companies Act 2006 being passed and considerable amount of interpretation being required from the English courts.³⁰¹

²⁹⁸ See discussion under 3.1.3 and 3.1.5

²⁹⁹ See discussion under 5.1 and 5.3

³⁰⁰ See discussion under 5.3

³⁰¹ See discussion under 5.3

Although section 21 of the 2008 Act does not address all of the above points, it does well in addressing most. As indicated above, Ncube points out that the legislature should have done more when considering retrospectivity and the manner under which a pre-incorporation contract was to be adopted or ratified.³⁰²

It is submitted that the legislature was paying attention to Cassim's works when drafting section 21 for the most part.³⁰³

Points that are notable improvements and that are worthy of complement on the part of the legislature are in respect of the three months grace period under which the company has to consider the contract after which it is deemed to be bound. This provision deals with and solves a substantial number of problems and as such, the legislature has really applied its mind to consider all parties that are involved in a pre-incorporation contract and should be commended.

However, as per the introduction, reference is made in that section 21 has a defect, and that this defect is of such a substantial nature that it makes the entire provision superfluous. This defect lies in the fact that section 21 only deals with pre-incorporation contracts where the promoter acts as agent. It does not apply to the position of that of a trustee.³⁰⁴

As to how section 21 is superfluous can only be demonstrated by example. In example one the promoter wishes to enter into a lease for a company that he plans on incorporating, he is not too sure as to whether he will be able to attend to everything that is necessary and this is more of a side interest than a serious consideration. As such, he enters into the agreement as a trustee subjectively knowing that this capacity will result in removing the application of section 21. At the same time, the third party believes that he has an enforceable contract

³⁰² See discussion under 4.3 and footnote 205

³⁰³ Cassim, MF. "Pre-incorporation Contracts : The Reform of Section 35 of the Companies Act" (2007) 2 *SALJ* 364.

³⁰⁴ See discussion under 4.3 and footnote 220

against the promoter as he incorrectly believes that section 21 applies and that personal liability will come into place at some points.

In the second example, the promoter wishes to enter into a lease for a company that he plans on incorporating, the third party being a bit more aware of the workings of section 21 knows that the promoter must enter into the lease as agent in order to ensure that section 21 finds application.

In the above two examples, the third party finds himself in drastically different positions. The above is the actual position in law at present. There is a very real loophole that exists in law, and unscrupulous promoters will take advantage of this short coming for their own benefit.

As such, urgent amendments are required in respect of section 21. It is submitted, that this amendment should find itself in the incorporation of an additional subsection and an amendment to subsection 1. The additional subsection would read “where subsection 1 finds application, the common law position shall not find application”. Furthermore subsection 1 should be amended to include trustees.

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