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THE DEVELOPMENT OF THE TURQUAND RULE AND THE DOCTRINE OF CONSTRUCTIVE NOTICE IN SOUTH AFRICAN COMPANY LAW

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CHAPTER 1: INTRODUCTION

1.1. INTRODUCTION

A company is a separate legal person, entrusted with legal rights and has the ability to incur legal duties.[1] A company is thus a legal concept and does not have a physical existence,[2] necessitating it to act through human agents.[3] The board of directors of a company is legislatively empowered with the management and day to day business affairs of a company.[4] Therefore, there exists in normal circumstances a relationship of agency between the company and its directors and shareholders, whereby the company is the principal and the directors and shareholders are agents of the company.[5] The power to manage the affairs of the company by the directors is now an original obligation, placing a positive duty on the directors to manage the affairs, as stipulated in section 66 of the Companies Act 71 of 2008.[6] This was not the case under the old 1973 Companies Act, where this power/obligation did not come from the Act directly, but was merely delegated to the directors by the shareholders of the company through the Memorandum of Incorporation.[7]

It is to be expected in practice that the board of directors, in the exercise of their powers to manage the company, delegate these powers to other individuals, being further directors and officers of the company.[8] The principles of agency law will determine if it happens that such delegated individual enters into a contract on behalf of the company and whether such individual will be bound by such contract.[9] This will require such individuals to have authority to contract on behalf of the company[10] and give effect to the entrusted functions, within the parameters of such delegation. Such delegate is thus seen to be in the place of the board and may act as the company within such delegated parameters.[11] This is where the Turquand rule

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1 Cassim *et al Contemporary company law* (2021) 40.
2 Ibid.
3 Lehloenya and Madlela "Representation of a company when contracting with another person under South African company law" 2018 *Obiter* 547 at 547.
4 Section 66 of the Companies Act 71 of 2008. See Also Lehloenya and Madlela "Representation of a company when contracting with another person under South African company law" 2018 *Obiter* 547 at 547.
5 Cassim *et al Contemporary company law* (2021) 67.
6 Delport *Henochsberg on the Companies Act 71 of 2008* 250(4).
7 Ibid.
8 Cassim *et al Contemporary company law* (2021) 241.
9 Ibid.
10 Ibid.
11 *Tesco Supermarkets Ltd v Nattrass* (1972) AC 153 paras 174-175.

swings into action. This rule emanates from the influential case of *Royal British Bank v Turquand*[12], when Jervis CJ stated:

> "We may now take for granted that the dealings with these companies are not like dealings with other partnerships, and that the parties dealing with them are bound to read the statute and the deed of settlement. But they are not bound to do more. And the party here, on reading the deed of settlement, would find, not a prohibition from borrowing, but a permission to do so on certain conditions. Finding that the authority might be made complete by a resolution, he would have a right to infer the fact of a resolution authorizing that which on the face of the document appeared to be legitimately done."[13]

The Turquand rule was developed by the English courts to afford some sort of protection to third parties contracting with a company. This protection to third parties stemmed from them not needing to have knowledge of the internal workings of a company and that these internal workings will not adversely effect the validity and binding nature of their contract entered into with a company, when acting innocently. The Turquand rule is intended to afford protection to all outsiders dealing with a company that have no means of knowing whether the company complied with the internal formalities and procedures as required and stated in its Memorandum of Incorporation.[14] Thus, directors and other insiders of the company may not rely on the rule.[15] A distinction should however be drawn between a director acting in such capacity and a director acting as an outsider contracting with the company. Only when a director acts as an outsider contracting with a company, can reliance be placed on the rule.[16]

The rule is considered as an independent rule of company law and that the general principles of agency law is not applicable.[17] This is not the case in all law jurisdictions, as English law considers the common-law Turquand rule as inextricably linked to estoppel and ostensible authority.[18] There are however views in South Africa that support both the aforesaid

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12 (1856) 6 E&B 327; 199 ER 886.
13 *Royal British Bank v Turquand* (1856) 6 E&B 327; 199 ER 888.
14 Cassim *et al Contemporary company law* (2021) 234.
15 Ibid.
16 *Hely-Hutchinson v Brayhead Ltd* [1967] 3 All ER 98 (CA) at para 564.
17 Cassim *et al Contemporary company law* (2021) 235. Also see *Farren v Sun Services SA Photo Trip Management (Pty) Ltd* 2004 (2) SA 146 (C) at 13-14.
18 Cassim *et al Contemporary company law* (2021) 235. Also see *Freeman and Lockyer v Buckhurst Park Properties (Mangal) Ltd* (1964) 1 All ER 630 (CA), which held in English Law that the rule became interchangeable with estoppel.

considerations, but the majority leans toward the independent rule application. The Turquand Rule was historically developed to mitigate the effects of the doctrine of constructive notice.[19]

This doctrine was developed as recognition of the fundamental and continuous role representative power started to play amid the growth of commercial partnerships in England during the nineteenth century.[20] At common law, this doctrine entails a person dealing with a company to have the requisite knowledge of the constitution and other documents of a company.[21] The common law doctrine of constructive notice had an impact on the potential liability of companies for any unauthorised contracts concluded by the company's apparent agents and in particular where such authority was restricted in the company's public documents.[22]

In these cases, constructive notice would hamper outsiders wanting to rely on agency by estoppel or ostensible authority to enforce the agreement entered into against the company.[23] This results from the third party not being able to place emphasis on any ignorance that may be present pertaining to the public documents of the company.[24] The third party will have no prospects of placing reliance on estoppel or ostensible authority even insofar as the company held out the agent as having the necessary authority.[25]

This resulted in compelling third parties, when contracting with the company, to examine the public documents each time when the need arises to enter into an agreement with the company.[26] This lowered or negated the risk of lack of authority on the agent's part together with ignorance on the part of the third party pertaining to the contents of the company's public documents. Furthermore, this placed an onerous burden on third parties whenever they wished to enter into an agreement with a company.[27] This doctrine worked in favour of the company, as a person dealing with the company was deemed to have knowledge of the contents of these documents whether this was indeed the case or not.[28]

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19 Cassim *et al Contemporary company law* (2021) 231.

20 Olivier E "Section 19(5)(a) of the Companies Act 71 of 2008: Enter a Positive Doctrine of Constructive Notice?" 2017 *Stellenbosch LR* 614 at 616.

21 Cassim *et al Contemporary company law* (2021) 229.

22 Olivier E "Section 19(5)(A) of the Companies Act 71 of 2008: Enter a Positive Doctrine of Constructive Notice?" 2017 *Stellenbosch LR* 614 at 617.

23 Ibid.

24 Ibid.

25 Ibid.

26 Ibid.

27 Ibid.

28 Cassim *et al Contemporary company law* (2021) 229.

During the course of the Turquand rule's existence, the Turquand rule transgressed and found application to a wider sphere of functions within company law.[29] The purpose of this research is thus to assess to what extent these aforementioned doctrines have developed in their interpretation, reliance and application.

1.2. RESEARCH PROBLEM

What gave rise to this research study, dealing with the development of the Turquand rule and the doctrine of constructive notice in South African Company law, is the practical application of these doctrines within our South African legislative framework. This research seeks to assess the extent to which the doctrine of constructive notice has been abolished in South African company law and the application of the Turquand rule by assessing the continued practical effect thereof, as applied by the South African judiciary.

1.3. ASSUMPTIONS/HYPOTHESIS

The assumptions that this research is based on is that the doctrine of constructive notice is abolished and only finds application in very limited circumstances as detailed by the Companies Act 71 of 2008. Furthermore, the South African judiciary in recent times has leaned towards an ancillary approach by seeing and applying the Turquand rule under the same legal requirements governing the law of agency. There are however, academics that still hold true that this is not the correct application of the Turquand rule and that the Turquand rule must be seen as an independent remedy for third parties contracting with a company.

1.4. MOTIVATION

This research is significant in terms of company law due to the fact that third parties deal and contract with companies on a daily basis. Section 7 of the Companies Act 71 of 2008[30] sets out the purpose of the Act and specifically the balance that must be struck between different stakeholders of a company. The Act intends to strike a balance between all the stakeholders rights and ensure the adequate protection thereof. This has resulted in certain doctrines being developed and abolished through the years. This research will focus on the development of the doctrine of constructive notice and the Turquand rule in South African company law. Emphasis

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29 Ibid at 231.

30 Hereafter the "Companies Act" or "Act".

will be placed on how this doctrine and rule have developed and the extent of their applicability in a modern society and their interpretation and application when dealing with a company.

1.5. RESEARCH METHODOLOGY

The approach that will be followed for conducting the research for this study will be desktop research. Reliance will be placed on various sources including legislation, case law and journal articles and textbooks. A further comparative analysis will be conducted between the law applicable in the jurisdictions of South Africa and the United Kingdom, focusing on England. The United Kingdom was chosen to conduct the comparative analysis since both the doctrine of constructive notice and the Turquand rule emanates from this jurisdiction and was incorporated into South African company law. Furthermore, the South African courts on a regular basis draw comparison with the United Kingdom jurisdiction and the evolution of the United Kingdom's company law framework, specifically pertaining to corporate representation and the development of the Turquand rule.[31]

1.6. LIMITATIONS AND DELINEATIONS OF THE RESEARCH

This study will briefly examine authority in a company law context and insofar it relates to the discussion and analyses of the doctrine of constructive notice and the Turquand rule. Thereafter, the doctrine of constructive notice will be examined pertaining to the common law position, how it has developed and ultimately lead to the abolition thereof and partial codification in the Companies Act. This will be followed by examining the Turquand Rule's interpretation and development by emphasising the common law position followed by the codification thereof. Since companies are no longer restricted to a specific business activity, for purposes of this study the *ultra vires* doctrine will not be discussed and analysed and is excluded from the scope hereof. Lastly, the comparative analysis will also be restricted to the legislative framework of England, within the United Kingdom.

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[31] See *inter alia: Mine Workers' Union v Prinsloo* 1948 (3) SA 831 (A); *Legg & Co v Premier Tobacco Co* 1926 AD at 132; *Quintessence Opportunities Ltd v BLRT Investments Ltd; BLRT Investments Ltd v Grand Parade Investments Ltd* 2007 (6) SA 523 (C) at 532F; *Makate v Vodacom Ltd* 2016 (4) SA 121 (CC); *Mohamed v Ravat Bombay House (Pty) Ltd* 1958 (4) SA 704 (T); *Farren v Sun Services SA Photo Trip Management (Pty) Ltd* 2004 (2) SA 146 (C).

1.7. CHAPTER OUTLINE

In the body of this study the author will examine to what extent have the company doctrines of constructive notice and the Turquand rule been developed pertaining to the interpretation, reliance and application thereof.

Chapter 2 will in detail discuss the powers of a company, agency principles, authority and corporate contracting. The powers of a company will be discussed with reference to the artificial nature of a company which cannot act by itself. Thus, looking at the powers, the source and nature of these powers, of the board of directors entrusted with the management of a company. Thereafter, the agency principles will be discussed as laid down in South African law and the effect and binding nature of this relationship. Furthermore, the different forms of authority will be discussed, dealing with the true nature and elements of actual and ostensible authority. All this will cumulate into a discussion of how agency law and the different forms of authority forms an integral part of corporate contracting when a third party contracts with a company.

Chapter 3 will analyse the development of the doctrine of constructive notice, looking at the common law and statutory position. The reasons for its development and the final abolishment of the doctrine will also be discussed. Furthermore, this chapter will look at the continued limited application of the doctrine, as set out in the Companies Act and the criticism levied against it.

Chapter 4 is concerned with a detailed discussion and analysis regarding the development, application and reliance placed on the Turquand rule as it relates to the common law position and the codification of the rule in terms of the Companies Act 71 of 2008. This chapter will look at different views as to the continued relevance of the Turquand rule. The nature of the Turquand rule will also be discussed, looking at the two broad approaches to the rule, being an independent or ancillary approach. The codification of the Turquand rule will be discussed and how the codified version differs from that of the common law. The chapter will conclude with an analysis of whether the Turquand rule still has a place in modern company law. All the above will be substantiated by different views of academics and case law.

Chapter 5 will be the comparative chapter, setting out the position of the doctrine of constructive notice and the Turquand rule as applied and developed within the English Law jurisdiction. This will be done by assessing the development of the English Companies Act by

reviewing the relevant sections and how these sections have been amended over the years. This chapter will conclude with a view on how the English Courts interpretation of the Turquand rule has shifted to a primarily Ancillary Rule approach.

Chapter 6 provides remarks in conclusion and sets out the author's view and recommendations, after review and analysis of the discussions of academics and the practical application of the Turquand rule by South African and English courts. Furthermore, the author's views on the doctrine of constructive notice abolishment and partial codification in the Companies Act will be provided.

CHAPTER 2: COMPANY POWERS, AGENCY PRINCIPLES, AUTHORITY AND CORPORATE CONTRACTING

2.1. INTRODUCTION

This chapter will firstly focus on the source of the powers of a company. Thereafter, the agency law principles will be discussed flowing into the different forms of authority as recognised in South African law. Lastly, corporate contracting will be discussed from the view of the company and that of third parties. This chapter creates the necessary foundation and understanding pertaining to the creation and development of the doctrine of constructive notice and the Turquand rule.

2.2. POWERS OF A COMPANY

A company is regarded as being an artificial person which cannot act on its own.[32] A company acts through its directors and officers.[33] It is normally regarded that the board of directors, together with other superior management, carry out the functions of management and speak and act as the company.[34] The power of a company vests in the directors as a board and not as individuals.[35] This statutorily stems from section 66(1) of the Act which states:

> "The business and affairs of a company must be managed by or under the direction of its board, which has the authority to exercise all of the powers and perform any of the functions of the company, except to the extent that this Act or the company's Memorandum of Incorporation provides otherwise."

This section places a positive obligation on the directors to manage the company.[36] These powers in terms of section 66 will be in effect from when a director is appointed to the board of a company and the application of these powers is in terms of the board collectively acting as a unit.[37] These powers, as set out in section 66(1) are interchangeably linked to the office of a director.[38]

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32 Cassim et al *Contemporary company law* (2021) 241.
33 Ibid.
34 *Tesco Supermarkets Ltd v Nattrass* (1972) AC at 153.
35 Pretorius *et al Hahlo's South African company law through the cases* (1999) 343.
36 Delport *Henochsberg on the Companies Act* 2022 (2022) 250(5).
37 Ibid.
38 Ibid.

The importance of managing the business and affairs of the company is two-fold.[39] Firstly, this power is now original and not delegated any more as was the case under the 1973 Act.[40] Under the latter Act, these powers of directors were delegated to directors from the shareholders through the Memorandum of Incorporation.[41] Therefore, by way of example, the shareholders of the company cannot in terms of the current Act, except for where express provision is made in the Memorandum of Incorporation, take a resolution to authorise the directors to conclude and enter into a contract on behalf of the company.[42] Subsequently, the business and affairs of a company must be managed by or under the direction of its board of directors. Furthermore, the board has the authority to exercise all the powers and perform all the functions of the company, except to the extent that the company's Memorandum of Incorporation or the Act provides otherwise.[43]

2.3. GENERAL AGENCY PRINCIPLES

It is to be expected in practice that the board of directors, in the exercise of their powers to manage the company, delegate these powers to other individuals, being directors and officers of the company.[44] As a result, agency principles are unavoidable when dealing with contracting parties that consist of a company represented either by a single representative or the board contracting with a third person collectively.[45]

The principles of agency law will determine if it happens that such delegated individual enters into a contract on behalf of the company, whether such individual will be bound by such contract.[46] This will require such individuals to have authority to contract on behalf of the company[47] and give effect to the entrusted functions, within the parameters of such delegation.

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39 Ibid at 250(5).

40 Ibid at 250(5). See also *Kaimowitz v Delahunt and Others* 2017 (3) SA 201 (WCC) 12:

> "The present Companies Act has changed the source of a director's power; namely section 66 is the source of the power of a director to manage the business and the affairs of the company as opposed to a delegated power sourced in the shareholders' agreement by way of a MOI as was the case under the 1973 Act (through the then Articles of Association). As a result, the ultimate power to manage the affairs of the company resides in the directors and not in the shareholders."

41 Ibid at 250(5).

42 Ibid at 250(5).

43 Section 66(1) of the Companies Act.

44 Cassim *et al Contemporary company law* (2021) 241.

45 Van Niekerk *The development and reform of the rules regulating authority to contract on behalf of companies is South African and English Law* (LLD-Thesis, University of Cape Town, 2021) 44.

46 Ibid.

47 Ibid.

Such delegate is thus seen to be in the place of the board and may act as the company within such delegated parameters.[48]

In accordance with agency law, if an agent contracts with a third party on behalf of the company, such a contract will bind the third party and the company (principal) as if such contract is personally concluded between them.[49] The agent is seen as intermediary and the agent does not incur any liability under the contract. When the contract is concluded with the third party, the agent falls away.[50] If, however an agent contracts with a third party without the necessary authority assigned onto him/her, the agent will fail to bind the principal to the contract and incur liability to compensate the third party who suffers loss resulting from breach of warranty of authority.[51]

2.4. AUTHORITY

Authority can be divided into actual or ostensible authority. Actual authority can be expressed or implied. Actual authority is expressed when it is given in so many words, orally or in writing.[52] When referring to implied actual authority, three broad categories can be referenced.[53] Firstly, this authority is that which is reasonably incidental or a requisite for the proper execution of an agent's express authority.[54] An example is where an agent has the express authority to conclude an Offer to Purchase on behalf of his/her principal, the agent will have the implied authority to do all such things necessary and which are reasonably incidental to conclude the Offer to Purchase such as making sure that all compliance certificates are obtained and paid for.

Furthermore, implied actual authority can stem from the nature of the office or any particular position to which an agent is appointed. This is referred to as implied actual authority.[55] If an individual is appointed as a managing director of a company, he/she may have the implied actual authority to do all such things reasonably associated with such office and to conclude contracts on behalf of the company.[56] Should a board of directors appoint one member to any

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48 *Tesco Supermarkets Ltd v Nattrass* (1972) AC 153 paras 174-175.
49 Cassim *et al Contemporary company law* (2021) 241.
50 Ibid at 242.
51 Ibid at 242.
52 Ibid at 242.
53 Cassim and Cassim "The authority of company representatives and the Turquand rule revisited" 2017 *SALJ* 639 at 646.
54 Ibid.
55 Ibid at 8.
56 Ibid at 8.

executive position, they impliedly authorise him/her to do all such activities which normally falls within the scope of such office.[57] Lastly, implied actual authority may be present as a reasonable implication drawn from the conduct of a principal, where such a principal allows the activities conducted by the agent.[58]

Ostensible authority arises where an individual, by words or conduct, created the impression that someone is his or her duly authorised agent and thereby inducing a *bona fide* third party to deal with the agent within that capacity. The agent's ostensible authority is as a result of the principal's conduct or statements.[59] Ostensible authority is thus authority as it appears to others.[60] If the principle made representations, either by statement or conduct, to a third party of the agent's authority, the principal will be prevented from denying the authority of the agent.[61] If an individual dealing with an agent knows that the agent does not have actual authority to conclude any particular transaction, the individual cannot rely on ostensible authority.[62]

The courts have held that for an individual to rely on ostensible authority, there are certain requirements that need to be met namely:[63]

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57 Ibid at 8.

58 Ibid at 8. See also *Hely-Hutchhinson v Brayhead Ltd* (1968) 1 QB 549 (CA) 583.

59 See *Freeman and Lockyer v Buckhurst Properties (Mangal) Ltd* (1964) 1 All ER 503:

> "An 'apparent' or 'ostensible' authority ... is a legal relationship between the principal and the contractor created by a representation, made by the principal to the contractor, intended to be and in fact acted upon by the contractor, that the agent has authority to enter on behalf of the principal into a contract of a kind within the scope of the 'apparent' authority, so as to render the principal liable to perform any obligations imposed upon him by such contract."

60 The nature of ostensible authority and the relationship to that of actual authority was described in *Hely-Hutchhinson v Brayhead Ltd* (1968) 1 QB 549 (CA) 583 as follows:

> "Ostensible or apparent authority is the authority of an agent as it appears to others. It often coincides with actual authority. Thus, when the board appoint one of their number to be managing director, they invest him not only with implied authority, but also with ostensible authority to do all such things as fall within the usual scope of that office. Other people who see him acting as managing director are entitled to assume that he has the usual authority of a managing director. But sometimes ostensible authority exceeds actual authority. For instance, when the board appoint the managing director, they may expressly limit his authority by saying he is not to order goods worth more than £500 without the sanction of the board. In that case his actual authority is subject to the £500 limitation, but his ostensible authority includes all the usual authority of a managing director. The company is bound by his ostensible authority in his dealings with those who do not know of the limitation."

61 Cassim *et al Contemporary company law* (2021) 243.

62 *Criterion Properties plc v Stratford UK Properties LLC and others* (2004) 1 WLR 1846 (HL) 31.

63 *NBS Bank Ltd v Cape Produce Co (Pty) Ltd* 2002 (1) SA 396 (SCA); *Freeman and Lockyer v Buckhurst Properties (Mangal) Ltd* (1964) 1 All ER.

i. A representation should have taken place, whether by words or conduct;

ii. Such representation should have been made by the principal (someone clothed with actual authority), in such a manner that the principal should reasonably have expected that outsiders would act on the strength of the representation;

iii. Reliance by the third party on such representation;

iv. The reliance must have been reasonable; and

v. There must be prejudice, due to such reliance, to the third party.

A distinction needs to be drawn between implied actual authority and ostensible authority. Implied actual authority is a relationship between the principal and the agent being created by a consensual agreement to which they alone are parties. Subsequently, the third party is a stranger to this agreement.[64] As a result, should there be implied actual authority, contracts concluded by the agent will be binding on the company irrespective of the third party's reasonable reliance or good faith. In contrast, ostensible authority depends on the relationship between the principal and the third party. The agent in this instance is a stranger to the agreement.[65]

Should an implied representation be made by the principal to the third party that an agent has authority, the third party must present that he or she relied on the representation and that such reliance was reasonable, for ostensible authority to be established. Ostensible authority is thus created by a representation by the principal to the third party that the agent has the relevant authority and when acted upon by the third party, he or she may rely on estoppel, which precludes the principal from stating that he or she is not bound.[66] Taking cognisance of the above, it can be held that ostensible authority is nothing else than agency by estoppel.[67]

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64 *Freeman and Lockyer v Buckhurst Properties (Mangal) Ltd* (1964) 1 All ER at 644.

65 Ibid.

66 *Armagas Ltd v Mundogas SA (The Ocean Frost)* (1985) 3 All ER 795 (CA) 804.

67 Cassim and Cassim "The authority of company representatives and the Turquand rule revisited" 2017 *SALJ* 639 at 647. See also *NBS Bank Ltd v Cape Produce Co 2002 (1) SA 396 (SCA)* 25:

> "Our law has borrowed an expression, estoppel, to describe a situation where a representor may he held accountable when he has created an impression in another's mind, even though he may not have intended to do so and even though the impression is in fact wrong. Where a principal is held liable because of the ostensible authority of an agent, agency by estoppel is said to arise. But the law stresses that the appearance, the representation, must have been created by the principal himself. The fact that another holds himself out as his agent cannot, of itself, impose liability on

In English law it has been firmly settled that ostensible authority is based on estoppel.[68] Estoppel precludes a person, being the representor, from denying the truth of a representation that he/she made in circumstances where another person has relied on the representation made and as a result lead to prejudice being suffered by such person.[69] Estoppel is based on the principles of justice, fairness and equity stemming from the fact that a person should not be allowed to make another believe in and subsequently rely on certain facts and then later renounce those facts.[70] Estoppel is considered as a wide-ranging concept that can exist in many forms stemming from the specific circumstances of each case. One if these forms being that of agency by estoppel.[71]

This being said, the case of *Makate v Vodacom (Pty) Limited*[72] made a judgment in regard to ostensible authority and estoppel which conflicts with a plethora of South African case law[73] and the views shared by a number of authors.[74] The majority judgment of Jafta J concluded that ostensible authority and estoppel are not based on the same elements when it was stated that:

> "The same misrepresentation may also lead to an appearance that the agent has the power to act on behalf of the principal. This is known as ostensible or apparent authority in our law. While this kind of authority may not have been conferred by the principal, it is still taken to be the authority of the agent as it appears to others. It is distinguishable from estoppel which is not authority at all. Moreover, estoppel and apparent authority have different elements, barring

him." See further Swart and Lombard "Representation of Companies under the Companies Act 71 of 2008" 2017 *Journal of Contemporary Roman-Dutch Law* 666 at 674.

68 Van Niekerk *The development and reform of the rules regulating authority to contract on behalf of companies is South African and English Law* (LLD-Thesis, University of Cape Town, 2021) 67.

69 Ibid.

70 Ibid.

71 Ibid.

72 (2016) ZACC 13.

73 Hosken Employee Benefits (Pty) Ltd v Slabe 1992 (4) SA 183 (W) 190I; *Big Dutchman (South Africa) (Pty) Ltd v Barclays National Bank Ltd* 1979 (3) SA 267 (W) 282E; *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 (2) SA 11 (T) 15A; *NBS Bank Ltd v Cape Produce Co (Pty) Ltd* 2002 (1) SA 396 (SCA) 25.

74 Sonnekus "Estoppel en oënskynlike volmag van amptenare van owerheidstrukture" 2012 TSAR 593 at 596; Cassim and Cassim "The authority of company representatives and the Turquand rule revisited" 2017 *SALJ* 639 at 656*;* Oosthuizen *Die Turquand-Reël in die Suid-Afrikaanse Maatskapptyereg* (LLD Thesis, UNISA 1976) 70; Cassim *et al Contemporary company law* (2021) 236.

one that is common to both. The common element is the representation which may take the form of words or conduct.[75]

A closer examination of the original statement on apparent authority by Lord Denning, quoted below, reveals that the presence of authority is established if it is shown that a principal by words or conduct has created an appearance that the agent has the power to act on its behalf. Nothing more is required. The means by which that appearance is represented need not be directed at any person. In other words the principal need not make the representation to the person claiming that the agent had apparent authority. The statement indicates the absence of the elements of estoppel. It does not mention prejudice at all. That statement of English law was imported as it is into our law in NBS Bank and other cases that followed it."[76]

It appears from the judgment, in reaching this aforesaid conclusion, Jafta J stated three reason. The first being that in the *Hely-Hutchinson* case[77] it was stated that ostensible authority "is the authority as it appears to others."[78] Secondly, that ostensible authority only has one requirement, being a representation, whereas estoppel is subject to numerous requirements including that of prejudice.[79] Lastly, it was held that there is no case in South African law prior to the *Cape Produce* case which stated that ostensible authority is based on estoppel.[80]

It is stated, with merit, by Cassim and Cassim that this ruling may have important practical ramifications insofar as the requirement of ostensible authority is reduced. The abandonment of these additional requirements, which have been widely accepted and form an integral part to ostensible authority, is seen as a cause of concern.[81] The effect and practical implications of this judgement remains to be seen; however, a court is not obliged to follow the decision of a higher court if such decision was made without due regard to the law.[82] The confusion and uncertainty subsequent to the *Makate v Vodacom (Pty) Ltd* case has already come to the

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75 *Makate v Vodacom (Pty) Limited* 2016 ZACC 46.
76 Ibid at 47.
77 *Hely-Hutchhinson v Brayhead Ltd* (1968) 1 QB 549 (CA) 583
78 *Makate v Vodacom (Pty) Limited* 2016 ZACC 49.
79 Ibid at 46-47.
80 Ibid at 70.
81 Cassim and Cassim "The authority of company representatives and the Turquand rule revisited" 2017 *SALJ* 639 at 653.
82 *Makambi v Member of Executive of Council, The Department of Education, Eastern Cape Province* (2008) 4 All SA 57 (SCA) para 28. Also see Sharrock "Authority by representation- a new form of authority?" 2016 *Potchefstroom Electronic Law Journal* 1 at 14.

forefront. The court has held, in a case after the *Makate* judgment, that once again when reliance is placed in ostensible authority the elements of estoppel will have to be pleaded and proved.[83] Furthermore, the court in another matter proceeded to apply the requirement to the specific facts as laid down in the *NBS Bank Ltd*[84] case when estoppel and ostensible authority were pleaded.[85]

2.5. CORPORATE CONTRACTING

This section will focus on how the above principles that have been discussed relating to agency law and the necessary authority, being actual or ostensible authority, applies when contracting with a company. Actual authority is of utmost importance from a company's perspective.[86] Viewed positively, actual authority is the very essence of a company's ability to take part in corporate contracting, as it is through the necessary representatives of the company, through delegation, to contract with third parties.[87] Viewed negatively, the company can limit the actual authority given to its representatives to contract on the company's behalf and in this way attempt to control what the company representatives may do.[88]

Traditionally, the flow of actual authority from the company to one of its representatives, can be categorised in one of four ways. Firstly, the board of the company, through a general authority clause in the company's constitution, was given the power and authority to manage the company's business and affairs.[89] Secondly, the board of the company could only act as one unit, necessitating the need that the authority of the board had to be delegated to a single representative by a power to delegate clause in the company's constitution.[90] Thirdly, the ability of the company's board of directors to delegate authority to a single representative or to

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83 *Engen Petroleum Limited v AAC Agri Foods CC* 2018 JDR 0793 (FB) 18:

> "In order to prove that plaintiff acquired the claim and the right to enforce same from Engen Lesotho I am not convinced that it is good enough for plaintiff to rely on ostensible authority to do so. In relying on ostensible authority it is conceded that he did not have actual authority. Where reliance is placed on ostensible authority, the elements of estoppel have to be pleaded and proved…".

84 *NBS Bank Ltd v Cape Produce Co (Pty) Ltd* 2002 (1) SA 396 (SCA).

85 *Bothma v Chalmar Beef (Pty) Ltd* 2019 JDR 0092 (FB) 25-29.

86 Van Niekerk *The development and reform of the rules regulating authority to contract on behalf of companies is South African and English Law* (LLD-Thesis, University of Cape Town, 2021) 80.

87 Ibid.

88 Ibid.

89 Ibid. See also *Amalgamated Union of Building Trade Workers of SA v South African Operative Masons' Society* [1957] 1 All SA 451 (A) at 466.

90 Ibid. See also Swart and Lombard "Representation of Companies under the Companies Act 71 of 2008" 2017 *Journal of Contemporary Roman-Dutch Law* 666 at 676.

act as a unit could be restricted by provisions in the company's constitution being[91] either a provision that states that certain matters could not be undertaken by the company's board without the necessary shareholder consent;[92]or a provision which placed an unconditional limitation on the company's ability to enter into a specific contract or the ability of a single representative to do the same. This will be for instance where a company's constitution explicitly states that two directors need to sign a contract that is above a specific monetary threshold.[93] Lastly a company's constitution could also contain different provisions which will be incidental to the flow of authority, these being provisions pertaining to resolutions, appointments and meetings.[94]

In contrast to the above, when a third party deals with a company, the third party cannot see into the internal decision-making process of a company.[95] Furthermore, merely reading the company's constitution will not allow a third party to definitively conclude that a single representative indeed has the authority to act or deal on the company's behalf.[96] As a result, a third party when contracting with a company, relies on what the company generally protrudes to the outside world and what the single representative of the company specifically reveals to such a third party.[97] A third party is thus likely to rely on the following when dealing with a company:

I. All the facts that the company projects to the outside world, which do not relate to any specific circumstance or transaction. These being, *inter alia*, the corporate name, the offices of the company, advertisements and the company logo.[98]

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91 Ibid.

92 Ibid at 81.

93 Ibid at 81. See also *Service Motor Supplies (1956) (Pty) Ltd v Hyper Investments 1961* (4) SA 842 (A) at 469.

94 Ibid at 81.

95 Ibid at 83.

96 Ibid at 83.

97 Ibid at 84. See also *Freeman & Lockyer (a firm) v Buckhurst Park Properties (Mangal)* Ltd [1964] 2 QB 480 (CA) 503:

> "In ordinary business dealings the contractor at the time of entering into the contract can in the nature of things hardly ever rely on the "actual" authority of the agent. His information as to the authority must be derived either from the principal or from the agent or from both, for they alone know what the agent's actual authority is. All that the contractor can know is what they tell him, which may or may not be true. In the ultimate analysis he relies either upon the representation of the principal, that is, apparent authority, or upon the representation of the agent, that is, warranty of authority."

98 Ibid at 84.

II. Internal company documents. This may be provided to a third party when a prospective contract is to be entered into with the company. These internal documents of the company being, *inter alia*, the company's constitution, minutes of meetings and resolutions taken. These documents will then constitute documents where the third party will have actual knowledge of the contents thereof and not merely constructive knowledge.[99]

III. Any actions or words of individuals within the company, other than the representative himself, to which the third party is aware.[100]

IV. Actions and words of the company representative himself when dealing with the third party.[101]

In light of the above, it is clear that when a third party deals with a company, no reliance is placed on the internal actual authority of a company as stipulated in a company's constitution.[102] Therefore, a third party mainly deals with a company on the concept of ostensible authority. It is highlighted that, unless the company's constitution is brought into the public domain, the company's constitution does not feature at all and a third party relies on the other representations made by the company when dealing with it.[103]

Taking cognisance of the above elements of corporate contracting, it clearly shows that there are always two perspectives present, that of the company and that of the third party. This corporate contracting was directly affected by the two doctrines developed in the 19th century being the doctrine of constructive notice, and the Turquand rule.

2.6. CONCLUSION

In conclusion, it is now evident that the directors of a company enjoy original powers and that a positive duty is placed on them to manage the affairs of the company. The board of directors power are no longer delegated as was the case under the old Companies Act of 1973. The South African courts have laid down strict elements that need to be proved when reliance is placed on ostensible authority when contracting with someone. It is clear that agency principles and

99 Ibid at 84.
100 Ibid at 84.
101 Ibid at 85.
102 Ibid at 85.
103 Ibid at 85.

authority, as delegated, plays an integral role in the day to day running of a company and that these principles form the backbone of corporate contracting. It is however alarming that the highest court has broken away from the view that ostensible authority and estoppel are not based on the same elements, these elements that have formed an integral part of both and which have been so engrained and supported into our legal framework.

CHAPTER 3: THE DOCTRINE OF CONSTRUCTIVE NOTICE

3.1. INTRODUCTION

This chapter will examine the development and application of the doctrine of constructive notice, the abolition of the doctrine in the new Act and the criticism levied against it. The doctrine of constructive notice is considered to have entailed that when anyone was dealing with a company, it was considered that this third party knew and familiarised themselves with the important facts on the company's documents, as these documents were open for public inspection with the Companies and Intellectual Properties Commission's office. This view and assumption did not favour business convenience between a third contracting party and a company and lead to the doctrine being abolished and partially retained in the Companies Act in specific circumstances. This doctrine is important to the research as a whole, as the Turquand rule was initially developed to mitigate the adverse effects of the doctrine and to show how this doctrine will not be beneficial to modern corporate contracting.

3.2. THE DEVELOPMENT OF THE DOCTRINE

The doctrine can be explained by using the doctrine of disclosure.[104] The doctrine of disclosure is regarded as the most basic of company law doctrines as it is the flipside of corporate legal personality.[105] The origins of this doctrine is usually ascribed to the decision in *Ernest v Nicholls*[106], where the House of Lords stated:

> "All persons, therefore, must take notice of the deed and the provisions of the Act. If they do not acquaint themselves with the powers of the directors, it is their own fault, and if they give credit to any unauthorised persons they must be content to look to them only, and not to the company at large. The stipulations of the deed, which restrict and regulate their authority, are obligatory on those who deal with the company ...".

In accordance with the common-law, the effect of the doctrine of constructive notice was that a person dealing with a company was deemed to be aware of the contents of the company's

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104 Naudé "Company Contracts: The Effect of Section 36 of the New Act" 1974 91 *SALJ* first page at 317.

105 Delport "Companies Act 71 of 2008 and the "Turquand" Rule" 2011 *Journal of Contemporary Roman Dutch Law* 132 at 133.

106 (1857) 6 HL Cas 401 at 420.

constitution and all other public documents that were lodged with the registrar of companies and were open for public inspection, whether they indeed read these documents or not.[107]

This led to the doctrine being regarded as highly artificial, due to the artificial result of binding third parties to a company's constitution even if those third parties did not actually know about the provisions or contents thereof.[108] The doctrine had its effect illustrated the most in situations if the constitution of a company contained an exclusion clause.[109] The application of this doctrine meant that a third party could not state that he/she had no notice of such a clause and a representative of the company, acting in contravention thereof, would not bind the company.[110] This may be illustrated in instances where the company, in any transaction, requires two signatures of any of its directors. It may happen that only one director signs on behalf of the company pertaining to the transaction with the third party. As a result, a third party will not be able to hold the company bound and liable to the transaction, only signed by one director, as a clear reading of the company's articles states that two director's signatures are required.[111]

It has been stated that the doctrine operates negatively and unfavourably towards parties dealing with a company that did not inquire about the said documents, as the doctrine alone operates in favour of a company and not against it.[112] The doctrine of constructive notice was never intended to benefit any other person except the company itself. No other party except the company could place reliance on the doctrine and that the doctrine could not be used by any of the company's agents to escape liability or by an outsider to establish a claim.[113]

Van Niekerk aptly sums up the reasoning for why the doctrine only operates in favour of the company by stating:[114]

> "The reasoning behind this conclusion has partly to do with the origins of the doctrine. The doctrine was intended as a shield to protect shareholders –

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107 Cassim et al *Contemporary company law* (2021) 229.

108 Van Niekerk *The development and reform of the rules regulating authority to contract on behalf of companies is South African and English Law* (LLD-Thesis, University of Cape Town, 2021) 91.

109 Ibid at 92.

110 Ibid.

111 Ibid at 92.

112 *Rama Corporation Ltd v Proved Tin General Investments Ltd* [1952] 2 QB at 147, [1952] 1 All ER 554

113 Olivier "Section 19(5)(A) of the Companies Act 71 of 2008: Enter a Positive Doctrine of constructive notice?" 2017 *Stellenbosch LR* 614 at 618.

114 Van Niekerk *The development and reform of the rules regulating authority to contract on behalf of companies is South African and English Law* (LLD-Thesis, University of Cape Town, 2021) 93.

> allowing third parties to use it as a sword goes against the very basis for the doctrine. Furthermore, allowing a third party to place reliance on articles of which he/she was unaware appears contrived, not to mention that it contravenes one of the basic requirements for setting up an estoppel against a company, namely that a person setting up an estoppel must have relied on representations made by the estoppel-denier."

Therefore, the common law doctrine of constructive notice had an impact on the potential liability of companies for any unauthorised contracts concluded by the company's apparent agents and in particular where such authority was restricted in the company's public documents.[115] In these cases, constructive notice would hamper outsiders wanting to rely on agency by estoppel or ostensible authority from enforcing the agreement entered into with the company.[116] This results from the third party not being able to place emphasis on any ignorance that may be present pertaining to the public documents of the company.[117] The third party will have no prospects of placing reliance on estoppel or ostensible authority even if the company held out the agent as having the necessary authority.[118]

This resulted in compelling third parties, when contracting with the company, to examine the public documents each time when the need arises to enter into an agreement with the company.[119] This lowered or negated the risk of lack of authority on the agent's part together with ignorance on the part of the third party pertaining to the contents of the company's public documents.[120] This placed an onerous burden on third parties whenever they wished to enter into an agreement with a company.[121]

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115 Olivier "Section 19(5)(a) of the Companies Act 71 of 2008: Enter a positive doctrine of constructive notice ?" 2017 *Stellenbosch LR* 614 at 617.

116 Ibid.

117 Ibid.

118 Ibid.

119 Ibid.

120 Ibid.

121 Ibid. See also McLennan "Demise of the Constructive-Notice Doctrine in England" 1986 *SALJ* 558 at 559*:*

> *"*What it amounts to, therefore, is that it is no excuse for a person dealing with a company to say that he had not read the documents. Even in this somewhat restricted negative form, the doctrine, so far from serving any useful purpose in the field of company law, has done little else than cause unfair prejudice to third parties contracting with companies"

3.3. THE ABOLITION OF THE DOCTRINE OF CONSTRUCTIVE NOTICE

Due to modern developments in company law and trends in other common-law jurisdictions, the doctrine of constructive notice was abolished to a certain extent by section 19(4) of the Act. This section, together with section 19(5) states that:

> "(4) Subject to subsection (5), a person must not be regarded as having received notice or knowledge of the contents of any document relating to a company merely because the document—
>
> (*a*) has been filed; or
>
> (*b*) is accessible for inspection at an office of the company
>
> (5) A person must be regarded as having notice and knowledge of—
>
> (*a*) any provision of a company's Memorandum of Incorporation contemplated in section 15 (2) (*b*) or (*c*) if the company's name includes the element ''RF'' as contemplated in section 11 (3) (*b*), and the company's Notice of Incorporation or a subsequent Notice of Amendment has drawn attention to the relevant provision, as contemplated in section 13 (3); and
>
> (*b*) the effect of subsection (3) on a personal liability company."

It is thus clear that although section 19(4) has abolished the doctrine of constructive notice, section 19(5) reintroduces a muffled modern version of the doctrine.[122] As a result, section 19(5) of the Act states that a person is regarded as having the knowledge of any provision of a company's Memorandum of Incorporation containing a restrictive condition together with a restrictive method of amendment concerning the Memorandum of Incorporation or an entrenched provision that may not be amended at all.[123] All this is subject to the company's name being suffixed with the initial 'RF' and the company's Notice of Incorporation drawing the necessary attention to the aforesaid restrictive condition applicable to the company.[124] The

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122 Cassim *et al Contemporary company law* (2021) 229.
123 Ibid at 230.
124 Ibid at 230.

doctrine of constructive notice is thus dependant on the company's name being suffixed with 'RF', to alert third parties to the restrictive conditions applicable to the ring-fenced company.[125]

The doctrine of constructive notice only applies when the requirements, as set out in the Act and as mentioned above, are strictly adhered to.[126] If a company adds the suffix 'RF' to its name but in reality there is no restriction on the amendment of restrictive conditions or no prohibition on amending of clauses of the company's Memorandum of Incorporation, the benefit of the provision as stated in section 19(5) does not arise.[127] Further, if a company uses 'RF' but does not comply with the requirements in the Notice of Incorporation, section 19(5) will not protect the company.[128] The effect of preserving the doctrine in its modified form is that when the doctrine finds application, it will negate a claim based on ostensible authority of a director or other company agents or officers who have contracted on behalf of a company without having the actual authority to do so, even if the company may have held out that the said representatives of the company had the authority to contract on its behalf.[129]

The doctrine further applies in the case of a personal liability company. Persons dealing with such a company are deemed to be aware of the effect of the directors and former directors joint and several liability for debts and liabilities of the company as are or were contracted during their periods in office.[130]

When considering section 19(4) together with section 19(5), it can be regarded that a positive doctrine of constructive notice may be provided for. Unlike the common-law doctrine, the statutory doctrine may be of assistance to a third party in certain circumstances and not only to the company. Section 19(5) of the Act expressly states that "A person must be deemed to have notice and knowledge". This wording is clearly at odds with the common law doctrine which prevented outsiders from alleging ignorance of a company's public documents.[131] Previously,

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125 Ibid at 230.

126 Locke "The Legislative Framework Determining Capacity and Representation of A Company In South African Law And Its Implications For The Structuring Of Special Purpose Companies" 2016 *SALJ* 168.

126 Cassim et al *Contemporary company law* (2021) 230.

127 Ibid.

128 Ibid.

129 Ibid.

130 s 19(3).

131 Olivier "Section 19(5)(a) of the Companies Act 71 of 2008: Enter a positive doctrine of constructive notice?" 2017 *Stellenbosch LR* 614 at 621:

> "Interpreted literally, all persons must be regarded as having notice and knowledge of the relevant clauses in the MOIs of RF companies that comply with the stipulated formalities. Since the Act fails to either expressly explain the operation of section 19(5)(a), or to limit the circumstances under which it may be raised, the question as to

it was clear that the doctrine could not be used as a shield by unauthorised agents of the company to prevent personal liability but only as a rule which protected the interests of a company.[132]

The statutory doctrine can now be interpreted far more widely and the consequences of a positive doctrine of constructive notice, particularly in the context of unauthorised contracts, may be significant.[133] It is however hard to fathom that this was indeed the intention of the legislature, but it can definitely be interpreted in this way.[134] One can go further and ask the question whether an unauthorised agent of the company can rely on the statutory doctrine as a defence to a claim by a third party? The answer will ultimately depend on how section 19(5)(a) of the Act will be interpreted.[135]

Any act must be interpreted that give effect to the purpose thereof. The purpose of the Companies Act is, *inter alia*, the development of the South African economy through the promotion of responsible management.[136] Civil liability, when unauthorised agency occurs, is a recourse for third parties to hold such officers/agents of a company financially responsible for their actions.[137] Third party protection can be construed just as important as shareholder protection, as adequate third-party protection increases confidence in the economy.[138]

Ultimately, Olivier submits that section 19(5)(a) should not be interpreted as creating a positive doctrine of constructive notice. He states:[139]

> "In the first place, such an interpretation would conflict with the common-law approach to the Rule. The limitations of the common-law doctrine were well understood. Historically, the constructive notice doctrine was a Rule that could only be called upon by a company in order to protect its own interests, and was never available to any other party except the company. A positive doctrine of constructive notice would arguably conflict with other aspects of common law

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whether the Act has created a positive doctrine of constructive notice remains an open one."

132 Ibid.

133 Ibid.

134 Jooste "Observations on the impact of the 2008 SALJ 464 at 469.

135 Olivier E "Section 19(5)(A) of the Companies Act 71 of 2008: Enter a positive doctrine of constructive notice?" 2017 *Stellenbosch LR* 614 at 621.

136 S 7(j) of the Act.

137 Olivier E "Section 19(5)(a) of the Companies Act 71 of 2008: Enter a positive doctrine of constructive notice?" 2017 *Stellenbosch LR* 614 at 621.

138 Ibid.

139 Ibid at 622.

> by potentially destroying two causes of action which a third party would ordinarily have had against a purported agent for loss caused by an unauthorised contract. This interpretation could lead to prejudice for third parties contracting with RF companies. For the above reasons, it is suggested that it could not have been the Legislature's intention to create a positive doctrine of constructive notice by way of section 19(5)(*a*) of the Act."

Accordingly, the abolition of the doctrine of constructive notice by section 19(4) of the Act, brings the Act in line with other modern trends in other common-law jurisdictions.[140] As a result, third parties will not be influenced or affected by the memorandum of incorporation of a company or its public documents, unless such third parties had actual knowledge of the contents thereof.[141] The reference to a 'document' in section 19(4) of the Act will have to incorporate and refer to electronically filed documents with the Companies and Intellectual Property Commission ("CIPC").[142]

This is in stark contracts with the traditional company law logic, as laid down in chapter 2, which was that a company's constitution was in terms of legislation disclosed to the registrar and available for inspection by the public, resulting in the courts to conclude that a third party could not deny the contents thereof.[143] Currently, although companies are required to lodge their respective memorandum of incorporation with the CIPC, the only individuals that generally have access to the company's constitution are beneficial holders of the company's securities.[144] A third party no longer has the right to obtain a company's constitutional documents.[145]

The abolishment of the doctrine revolutionised corporate contracting. Consequently, the principles of agency law will continue to apply to companies. If a third party can prove the actual or ostensible authority of a company representative, the company will be liable regardless of the contents of the company's memorandum of incorporation.[146]

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140 Cassim *"The Companies Act 2008: An Overview of a Few of its Core Provisions"* 2010 *SA Merc LJ* 157 at 173.

141 Ibid.

142 Ibid.

143 Van Niekerk *The development and reform of the rules regulating authority to contract on behalf of companies is South African and English Law* (LLD-Thesis, University of Cape Town, 2021) 176.

144 See Section 26(3) and 26(7) of the Companies Act 71 of 2008.

145 Ibid.

146 Ibid at 177-178.

Given the fact that section 19(4) of the Act has abolished the obsolete and archaic doctrine, section 19(5)(a) continues with the subdued version of the doctrine.[147] This strictly applies, as discussed above, when a person's attention, while dealing with a company, has specifically been drawn to some special condition applicable to the company in the memorandum of incorporation.[148] This is achieved by the company suffixing 'RF' to its name and making the person dealing with the company aware that there are special conditions present in the company's memorandum of incorporation.[149] It is submitted that since the doctrine has been abolished and restricted to apply only to certain specific scenarios, as stipulated in the Act, third parties dealing with the company are more protected and there has been a general shift in modern company law towards strengthening the protection of third parties when dealing with a company.

3.4. CONCLUSION

It is evident that the operation of the historical common-law doctrine of constructive notice only operated to the exclusive benefit of the company when contracting with third parties. It thus cannot be stated that the existence and application of this doctrine had a positive effect on corporate contacting and encouraged outsiders to contract with a company. The author is of the view that this it is quite the opposite, that the application of this rule in the past was to the determined of all parties involved to the contracting process. Third parties would have been deterred to do business with a company which in turn will result in negative corporate growth of the company itself. The abolishment thereof is welcomed and brings the Act in line with other modern trends in other common-law jurisdictions.

147 Cassim *"The Companies Act 2008: An Overview of a Few of its Core Provisions"* 2010 *SA Merc LJ* 157 at 173.
148 Ibid.
149 Ibid.

CHAPTER 4: TURQUAND RULE

4.1. INTRODUCTION

In this chapter, the Turquand rule will be analysed pertaining to its development, application, the rule 's changed view over the years and the criticism levied against its continuous existence and place in a modern law society.

The Turquand rule was historically formulated to alleviate the severe effects brought about by the doctrine of constructive notice.[150] It was applied as an exception to the doctrine of constructive notice.[151] It has, however, developed over the years to find application and serve functions other than to merely mitigate the effect of the doctrine.[152] Had this rule not developed over the years, the rule would also have been abandoned in the same manner as the doctrine of constructive notice.[153]

This rule is derived from the *Royal British Bank v Turquand*[154] case and was later applied in *South African law in Mine Workers' Union v Prinsloo*.[155] The rule can be summarised as follows:

> "This Rule mitigates the unrealistic doctrine of constructive notice which deems anyone dealing with a company to know the contents of the company's memorandum, articles of association, resolutions and other documents recorded on the company's file with the Registrar of Companies. In its simplest form the *Turquand* Rule, or 'indoor management Rule ', entails that if nothing has occurred which is obviously contrary to the provisions of the registered documents of the company, an outsider may assume that all the internal matters of the company are regular."[156]

The rule thus essentially protects *bona fide* third parties who are not aware of any internal irregularities of the company that may affect the validity of the contracts entered into with the

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150 Cassim *et al Contemporary company law* (2021) 231.
151 Ibid.
152 Ibid.
153 Ibid.
154 (1856) 6 E & B 327; 119 ER 886.
155 1948 (3) SA 831 (A). See also *Legg and Co v Premier Tobacco* 1926 AD 132, which held that the rule forms part of the South African common law.
156 Delport "Companies Act 71 of 2008 and the "Turquand" rule" 2011 *Journal of Contemporary Roman Dutch Law* 132 at 134.

company. Thus, third parties can assume that all the internal formalities required for a valid contract has been complied with by the company. The practical effect of the rule is that it prohibits a company from escaping liability only on the grounds that an internal formality or procedure was not complied with.[157] The basis is that *bona fide* third parties should not be prejudiced in any way due to the failure by the company to comply with its own internal requirements and procedures.[158] The rule does not apply and operate if the third party is not *bona fide* or if the third party is aware of facts that would result in a reasonable person enquiring to establish whether there was compliance, or lack thereof, with internal formalities of a company.[159] Thus, a person cannot rely on the protection afforded by the rule if he/she knew that the mandate was defective or the circumstances surrounding the negotiations were suspect.[160]

Furthermore, it can be stated that the rule only applies when an agent of the company was authorised accordingly to perform a specific act.[161] If such express authority was lacking, the *bona fide* third party must show that the agent of the company had implied or ostensible authority for the company to be held liable.[162] The rule is justified on the basis of business convenience, as dealing with a company would be tedious if all third parties would first need to enquire into the internal affairs of a company and establish compliance thereof before entering into any contract.[163]

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157 Cassim *et al Contemporary company law* (2021) 232. See also Olivier "The Turquand Rule in South African Compnay Law: A(nother) Suggested Solution" 2019 *Journal of Corporate and Commercial Law & Practice* 1 at 2:

> "The Turquand rule is targeted at a situation where a company fails to fulfil one of its internal requirements regarding the authority of its agents to contract. In terms of the rule, third parties dealing with the company are entitled to presume regularity, or at least, are not to be affected by the company's non-compliance with its own internal formalities. In other words, the Turquand rule prevents a company from avoiding liability on an unauthorised contract due to non- compliance with an internal requirement. The operation of the rule will be excluded if the third party knew that the internal requirement had not been complied with. In addition, the Turquand rule cannot be used by a third party that had failed to make further enquiries in circumstances that are so suspicious that they should have prompted him to confirm the agent's authority by making further enquiries."

158 Cassim *et al Contemporary company law* (2021) 231.

159 Delport "Companies Act 71 of 2008 and the "Turquand rule" 2011 *Journal of Contemporary Roman Dutch Law* 132 at 135.

160 Cilliers et al *Corporate Law* (2018) 192.

161 Delport et al *Henochsberg on the Companies Act 71 of 2008* (2021) 108.

162 Ibid.

163 Cassim et al *Contemporary company law* (2021) 232.

4.2. NATURE OF THE TURQUAND RULE

Over the years, two clear and dominant strains of thought have emerged regarding the nature of the Turquand rule, these being the 'ancillary rule approach' and the 'independent rule approach'. The ancillary rule approach emphasises that since agency forms the foundation of corporate representation, any liability stemming from commercial contracts with a company needs to be conducted by the principles of agency.[164] This rule is focused on company liability based on ostensible authority or estoppel. Therefore, the Turquand rule is regarded as playing only an ancillary role to the greater application of ostensible authority and being of narrow application.[165] As a result, a company may not criticise its representative's ostensible authority by arguing that the third party had constructive knowledge of an internal formality contained in the company's constitution and that such formality has not been complied with.[166]

In contrast, the independent rule approach asserts that the Turquand rule is an independent rule of company law, which is considered to be a separate form of liability than that of agency law principles.[167] Therefore, if the Turquand rule is relied upon and the requirements of the rule are satisfied, the company may be held liable based on the rule alone without the need to make reference to the authority of the company's representative.[168] It should however be noted that the independent rule approach still acknowledges that the agency law principles form the general framework for corporate representation. In terms of the independent rule approach, the Turquand rule represents a company specific alteration to the principles of agency and furthermore a derivative from these principles.[169]

However the Turquand rule may be perceived, it is clear by following the independent rule approach that a third party can either rely on ostensible authority or the Turquand rule.[170] It has further been held that estoppel has substantially more difficult requirements to prove than that of the Turquand rule.[171] If the independent rule approach is applied, it is clear that there is

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164 Van Niekerk *The development and reform of the rules regulating authority to contract on behalf of companies is South African and English Law* (LLD-Thesis, University of Cape Town, 2021) 98.

165 Ibid

166 Ibid at 99.

167 Oosthuizen "Aanpassing van die verteenwoordigingsreg in maatskappyverband" 1979 *TSAR* 1 at 6.

168 Du Plessis "Maatskappygebondenheid vir die Optrede van Ongemagtigde Maatskappyfunksionarisse" 1991 *SA Merc LJ* 281 at 283.

169 Ibid. See also Oosthuizen "Aanpassing van die verteenwoordigingsreg in maatskappyverband" 1979 *TSAR* 1 at 7-10.

170 Ibid at 291. See also Oosthuizen "Aanpassing van die verteenwoordigingsreg in maatskappyverband" 1979 *TSAR* 1 at 9.

171 Cassim and Cassim "The authority of company representatives and the Turquand rule revisited" 2017 *SALJ* 660, Oosthuizen "Aanpassing van die verteenwoordigingsreg in maatskappyverband" 1979 *TSAR*

an advantage to a third party contracting with a company, since such a third party can choose between these two remedies to hold the company liable for any acts of an unauthorised company representative.[172]

Cassim strongly argues with merit in favour of the independent rule view pertaining to the application of the Turquand rule .[173] This is in line with most commentators of South African law.[174] A third party will thus be able to rely on the rule, even if all the requirements of estoppel have not been proven and furthermore without knowledge of the contents of the company's Memorandum of Incorporation.[175] This has the effect of widening the scope of application of the Turquand rule.

Further, should the rule and estoppel be treated as complementing one another, a company will not be bound by a contract where the rule applies, unless the requirements of estoppel are also proved by the third party.[176] This will have the effect of undermining the Turquand rule in South African law and reduce the protection afforded to third parties when dealing with a company.[177] This will be contrary to the interests of business convenience on which the rule is founded.[178] Accordingly, interpreting the Turquand rule as part of estoppel will undermine the common-law rule that has proven over the years to be very useful.[179]

Olivier submits that in view of the collective academic view in support of the independent rule approach of the Turquand rule in South African Law is unconvincing, merely ignores a large body of South African case law, clumsy and appears to accept legal uncertainty and potential prejudice to companies.[180]

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1 at 9, Du Plessis "Maatskappygebondenheid vir die Optrede van Ongemagtigde Maatskappyfunksionarisse" (1991) *SA Merc LJ* 281 at 291.

172 Ibid.

174 Cilliers et al *Cilliers & Benade Corporate Law* 3 ed (2000) 192-194; Oosthuizen "Aanpassing van die verteenwoordigingsreg in maatskappyverband" 1979 *TSAR* 1 at 10; Jooste 'Observations on the impact of the 2008 Companies Act on the doctrine of constructive notice and the *Turquand* rule' (2013) 130 *SALJ* 464 at 465; Du Plessis "Maatskappygebondenheid vir die Optrede van Ongemagtigde Maatskappyfunksionarisse" (1991) *SA Merc LJ* at 301-302.

175 Cassim and Cassim "The authority of company representatives and the Turquand rule revisited" 2017 *SALJ* 639 at 660.

176 Ibid.

177 Ibid.

178 Ibid.

179 Ibid.

180 Olivier "The Turquand Rule in South African Company Law: A(nother) suggested solution" 2019 *Journal of Corporate and Commercial Law and Practice* 1 at 21.

The further view, as held by academics[181] and the courts[182], is that the Turquand rule is a mere component of the doctrine of agency by estoppel. The court in *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd*[183] stated the following in support of the ancillary rule view:

> "I think it will be found, from an analysis of these and other leading authorities, that the *Turquand* Rule is simply an adjunct, in the context of companies and other entities with constitutions available to the public, of the law on ostensible authority, which is in turn a particular form of estoppel by representation."[184]

When considering that the courts have followed both the ancillary and the independent rule view pertaining to the Turquand rule, Olivier appositely summed up the position as:

> "After a reading of South African case law on this topic, the only conclusion seems to be that there is no settled and uniform approach to the Turquand rule. There has been no express statement of law on this point by an appellate level court or by the Constitutional Court. The various High Courts have often considered the Turquand rule, but there have been clear divergences in approach, and several decisions have completely ignored the supposed precedent set in the *Mine Workers' Union* case. In addition, no court has addressed whether the Turquand rule should apply to non-seal cases at all. With respect, there does not seem to be any undisputable 'weight of authority' in favour of either view of the Turquand rule, let alone the independent rule view.

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181 McLennan 'Contract and agency law and the 2008 Companies Bill' (2009) 30(1) *Obiter* 147:

> "…the so-called *Turquand* rule has no positive operation at all. Only when X has established the basic requirements of ostensible authority, may the non-compliance with internal formalities have any relevance. The indoor management rule is no substitute for any of the basic principles of the common law of agency"

Also see Van Niekerk *The development and reform of the rules regulating authority to contract on behalf of companies is South African and English Law* (LLD-Thesis, University of Cape Town, 2021) 135:

> "What mattered more was simply asking whether the third party was acting reasonably, based on the representations made to him/her, in trusting that the persons whom he/she was dealing with had authority to conclude the necessary contract. In this way, ostensible authority became the focal point of corporate contracting cases. Where a company raises non-compliance with an internal formality of which a third party has constructive notice, the Turquand rule may still have relevance, but it remains ancillary to the greater inquiry into the (ostensible) authority of corporate representatives."

182 *Insurance Trust and Investments (Pty) Ltd v Mudaliar* 1943 NPD 45 50– 54; *Service Motor Supplies (1956) (Pty) Ltd v Hyper Investments (Pty) Ltd* 1961 (4) SA 842 (A) 467; *Tuckers Land and Development Corporation (Pty) Ltd v Perpellief* 1978 (2) SA 11 (T) 15; W*olpert v Uitzigt Properties (Pty) Ltd & others* 1961 (2) SA 257 (W) 23.

183 (2015) 4 All SA 88 (WCC).

184 Ibid at 25.

> Even if there were, the recent *One Stop* decision shows that the scope of the Turquand rule is far from settled in South African law."[185]

To summarise, the fact remains that South African court have all attempted to apply the Turquand rule, but none of them seems to have taken a solid stance on what the rule is and whether or not it is an independent rule or an agency by estoppel, which creates considerable uncertainty.[186]

4.3. CODIFICATION OF THE TURQUAND RULE

It has been widely regarded that section 20(7) of the Act codifies the common law Turquand rule principles and creates a so called "statutory Turquand rule".[187] Section 20(7) of the Act states as follows:

> "A person dealing with a company in good faith, other than a director, prescribed officer or shareholder of the company, is entitled to presume that the company, in making any decision in the exercise of its powers, has complied with all of the formal and procedural requirements in terms of this Act, its Memorandum of Incorporation and any rules of the company unless, in the circumstances, the person knew or reasonably ought to have known of any failure by the company to comply with any such requirement."

There is however an irregularity created by section 20(7) of the Act, as this section does not properly align with the common law formulation of the Turquand rule. The overlap between the two forms can create uncertainty pertaining to the application thereof in practice. Section 20(7) in certain instances operates more widely than the common law rule and in other respects more narrowly.[188] The following similarities can be noted pertaining to both forms of the rule namely, both these forms prevents a company from relying on any non-compliance with specific requirements, thus upholding a fiction that there has been compliance with said

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185 Olivier "The Turquand Rule in South African Company Law: A(nother) suggested solution" 2019 *Journal of Corporate and Commercial Law and Practice* 1 at 15.

186 Mujulizi "The continued relevance of the Turquand rule under the current company law regime in South Africa" 2020 *Journal of Corporate and Commercial law & Practice* 54 at 60.

187 Delport "Companies Act 71 of 2008 And The "Turquand Rule" 2011 *Journal of Contemporary Roman Dutch Law* 132 at 136.

188 Cassim et al *Contemporary company law* (2021) 238.

requirements; and, furthermore, both rules uphold third party protection for those who acted *bona fide* and with no knowledge about any non-compliance.[189]

There are also discrepancies and conflicts that exist between the common law Turquand rule and the codification thereof. First, In terms of the common law when a person deals with the managing director of a company, he/she can assume authority has been delegated to such managing director if such delegation is possible in terms of the company's constitution. Should the company's constitution make provision for authority to be delegated to an ordinary director, a third party cannot generally assume that the internal delegation has taken place and rely on the Turquand rule.[190] In terms of section 20(7) of the Act, it is arguable that delegation of authority by the board to an ordinary director, for purposes of entering into a contract on behalf of the company constitutes "formal" or "procedural" requirements and that a third party can rely on section 20(7) by presuming that the requirements have been complied with.[191] Secondly, section 20(7) of the Act applies to a *bona fide* third party dealing with the company, but expressly exclude the categories of people seen as directors, shareholders of the company and prescribed officers i.e. insiders of the company. This is in contrast with the common law rule, which also protects and finds application to insiders in specific situations.[192] Thirdly, the common law Turquand rule will not protect a third party who knew or suspected that an internal formality is not being complied with by the company. Section 20(7) however, introduces an objective test by excluding third parties who "reasonably ought" to have known of any non-compliance with a formality by the company.[193] Fourthly, Section 20(7) states that a third party is "entitled to presume" that the procedural and formal requirements have been met. According to the common law Turquand rule, a third party is entitled to assume compliance with all internal requirements. The use of the word "presume" in section 20(7) means that it can be rebutted.[194] In other words, when a third party relies on section 20(7), a company can rebut the presumption that all internal requirements have been complied with, leaving the third party without recourse.[195] Lastly, it has been argued that section 20(7) pertains to the capacity of the

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189 Van der Linde "The validity of company actions under section 20 of the Companies Act 71 of 2008" 2015 *TSAR* 833 at 841.

190 Jooste "Observations on the Impact of the 2008 Companies Act on the Doctrine of constructive notice and the *Turquand* Rule" 2013 *SALJ* 464 at 470.

191 Ibid at 471.

192 Delport "Companies Act 71 of 2008 And The "Turquand Rule" 2011 *Journal of Contemporary Roman Dutch Law* 136.

193 Cassim et al *Contemporary company law* (2021) 238-239.

194 Delport et al *Henochsberg on the Companies Act 71 of 2008* (2021) 107.

195 Jooste "Observations on the Impact of the 2008 Companies Act on the Doctrine of constructive notice and the *Turquand* Rule" 2013 *SALJ* 464 at 473.

company rather than the authority of the directors to act on behalf of the company, since section 20(7) is organised under the same section of the Act, being section 20(1), dealing with the capacity of the company.[196]

Further confusion is created by section 20(8) of the Act. It states that the common law Turquand rule and the codification thereof applies concurrently, and that the one does not substitute the other. This will lead to uncertainty, as the scope is not the same pertaining to each form of the rule.[197] Delport highlights this by stating that, firstly the Turquand rule and section 20(7) apply concurrently and that uncertainty arises since their application differs in scope.[198] Secondly, given the fact that the common law rule is inextricably linked to the doctrine of constructive notice, the rule cannot apply following the abolition of the doctrine.[199] Lastly, it can be argued that the common law rule will only apply where constructive notice is expressly retained, in specific scenarios relating to RF companies or personal liability companies.[200]

4.4. CONTINUED APPLICATION OF THE TURQUAND RULE

It would appear, from an initial analysis, that the need for the Turquand rule disappears if a third party does not have any knowledge of the public documents of the company and that no knowledge of the public documents can be attributed to the third party as a result of the doctrine of constructive notice. This is as a result of the Turquand rule being developed to specifically mitigate the adverse effect of the doctrine of constructive notice and its close operational link with the doctrine. It has been held by some academics that the Turquand rule can still be applied, despite the abolition of the doctrine of constructive notice.[201]

Firstly, when one thoroughly analyses the Turquand rule, it becomes clear that the rule is not necessarily tied to the doctrine of constructive notice. The rule is not only available to a third

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196 Delport et al *Henochsberg on the Companies Act 71 of 2008* (2021) 111.

197 Delport "Companies Act 71 of 2008 and the "Turquand Rule" 2011 *Journal of Contemporary Roman Dutch Law* 132 at 138.

198 Ibid. See also Mujulizi "The continued relevance of the Turquand rule under the current company law regime in South Africa" 2020 *Journal of Corporate and Commercial law & Practice* 54 at 62-63:

> "…s 20(7) is broader than the common law as it expressly permits a third party to assume compliance with formal and procedural requirements under the Act, whereas the common-law rule cannot be used to assume this compliance, leaving the third party confined to assuming requirements contained in the company's memorandum of incorporation."

199 Ibid.

200 Ibid.

201 Oosthuizen "Die Turquand-reel as reel van die verenigingsreg" 1977 *Journal of South African Law* 210 at 215-216.

party where such party is prejudiced due to the attribution of knowledge regarding internal formalities pertaining to authority as outlined in a company's Memorandum of Incorporation.[202]The Turquand rule can also be relied upon in circumstances such as defective notice of meetings, defective appointment of directors or the absence of a required quorum which does not relate to the doctrine of constructive notice.[203] As a result, a third party knows that directors must be duly appointed or the requisite notice of meetings must be compliant and further that no publicity is given to these irregularities. Therefore, a third party's need for protection does not flow from the doctrine of constructive notice and will as a result of these circumstances being present be able to rely on protection afforded by the Turquand rule.[204]

Furthermore, the statement that a party can merely rely on implied or ostensible authority in the absence of the doctrine of constructive notice oversimplifies the situation.[205] Should a third party know of an internal requirement to be complied with by the company, it will be almost impossible to use estoppel as a defence against the company.[206] The third party will have to prove that the company has made a representation that a certain individual has the necessary authority to also show that the internal requirements have been complied with.[207] Since a third party has no access to the internal operations of a company, it is evident that it would be impossible for such a party to ascertain the true state of affairs. In light hereof, there is still a need for the protection of the Turquand rule.[208]

Lastly, it cannot be accepted that since the doctrine of constructive notice is abolished, the need for the Turquand rule evaporates. This will lead to unacceptable consequences and essentially means that a third party will be deprived from the protection of the rule even where such third party has no access to the internal management of the company.[209] The Turquand rule will

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202 Ibid.
203 Ibid.
204 Ibid.
205 Ibid.
206 Ibid.
207 Ibid.
208 Ibid. See also Swart & Lombard "Representation of Companies under the Companies Act 71 of 2008" 2017 *Journal for contemporary Roman Dutch law* 666 at 681:

> "The *Turquand* rule remains an independent company law principle based on equity and aiming to protect third parties against the non-compliance by representatives of companies of internal management rules or requirements. This also prevents companies from avoiding a contract based on the lack of authority of the company representative."

209 Ibid.

provide maximum protection under circumstances where the third party is not confined within the application of the doctrine of constructive notice.[210]

Taking cognisance of the above, it is submitted that there is indeed still room in certain circumstances where a third party can rely on the protection afforded by the Turquand rule, now that the doctrine of constructive notice has been abolished. Should a third party not be able to place reliance on the Turquand rule, it seems that a third party contracting with a company will be severely impeded. This flows from the fact that such a party will not be able to hold a company liable under specific circumstances where such a third party has no way of knowing whether or not the internal formalities of the company has been complied with. This will lead to business contracting being negatively affected, as the risk for a third party will be too great should there be no recourse for such a party in terms of the Turquand rule.

4.5. CONCLUSION

It is clear that the initial purpose of the Turquand rule was to merely mitigate the adverse effects brought about by the doctrine of constructive notice. The Rule has, however, developed far beyond this purpose and still has a rightful place in modern company law as a possible remedy that can be relied upon by third parties contracting with a company, without knowledge of all the company's internal requirements. Furthermore, it is submitted that the Turquand rule must be seen as an independent rule, separate from the principals of agency law. The partial codification of the rule in section 20(7) of the Companies Act has led to great uncertainty rather than clarification. In light thereof, it is recommended that the legislature should amend or repeal section 20(7) in its entirety.[211]

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210 Ibid.

211 See further recommendations in para 6.3 of Ch 6 below.

CHAPTER 5: THE DOCTRINE OF CONSTRUCTIVE NOTICE AND THE TURQUAND RULE AS APPLIED IN ENGLISH LAW

5.1. INTRODUCTION

This chapter will briefly discuss the demise of the doctrine of constructive notice in English law and further assess the continued application of the Turquand rule. It will become clear that the English courts have established the view that the Turquand rule is not an independent remedy but that the rule forms part of and is governed by the principles of agency law.

5.2. THE DEMISE OF THE DOCTRINE OF CONSTRUCTIVE NOTICE IN ENGLISH LAW

The main driver for reform in English Law, came from the United Kingdom joining the European Community in 1973.[212] As a result of the European Communities Act 1972 (c 68), the United Kingdom had to comply with the European Community's first directive on Company Law.[213] Article 9 of the Company Law Directive stated that all member states must remove any restraints attached to a company's contractual capacity in the objects clause. Article 9(1) of the Company Law Directive stated the following:

> "Acts done by the organs of the company shall be binding upon it even if those acts are not within the objects of the company, unless such acts exceed the powers that the law confers or allows to be conferred on those organs."[214]

Article 9(2) stated further that "[t]he limits on the powers of the organs of the company arising under the statutes or from a decision of the competent organs, may never be relied on as against third parties, even if they have been disclosed".[215]

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212 Nyombi "The gradual erosion of the ultra vires doctrine in English Company law" 2014 *International Journal of Law and Management* 347 at 355.

213 Ibid. See Council Directive No.68/151/EEC(OJ1968L65/8).

214 Article 9(1) of the Council Directive No.68/151/EEC(OJ1968L65/8). See also Nyombi "The gradual erosion of the ultra vires doctrine in English Company law" 2014 *International Journal of Law and Management* 347 at 355.

215 Article 9(2) of the Council Directive No.68/151/EEC(OJ1968L65/8). See also Nyombi "The gradual erosion of the ultra vires doctrine in English Company law" 2014 *International Journal of Law and Management* 347 at 355.

The Companies Act 1985 proceeded to incorporate article 9(1) and (2) of the Company Law Directive mentioned above, under section 35(1) and (2) of its provisions[216] which stated as follows:

> 35(1)-"In favour of a person dealing with a company in good faith any transaction decided on by the directors is deemed to be one within the capacity of the company to enter into and the power of the directors to bind the company is deemed to be free of any limitation under the memorandum or articles".[217]
>
> 35(2) –"A party to a transaction so decided on is not bound to inquire as to the capacity of the company to enter into it or as to any such limitation on the powers of the directors, and is presumed to have acted in good faith unless the contrary is proved."[218]

In light of section 35 of the Companies Act 1985, it is clearly evident that this section's intent and purpose was to abolish the doctrine of constructive notice and that this will result in making the corporate contracting easier for third parties when transacting with companies.[219] Section 35 further made the defining factor to establish whether a transaction falls within the section's protection that of "…a person dealing with a company in good faith…".[220]

Therefore, section 35 of the Companies Act 1985, could not be relied upon by the company itself. This section only applied if a third party dealing with a company had done so in 'good faith' and furthermore if the transaction was decided upon by the directors of the company.[221] It is now widely considered that this section was poorly drafted and only resulted in adding to the complexities of an already complex Doctrine.[222] This resulted in section 108 of the Companies Act 1989 substituting a new section 35, 35A and 35B for that of the old section 35.[223] Section 35A of the Companies Act 1985 was intended to give effect to Article 9(2) of the European Communities first directive, stating that limitations on the powers of company

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216 Nyombi "The gradual erosion of the ultra vires doctrine in English Company law" 2014 *International Journal of Law and Management* 347 at 355.

217 Section 35(1) of The Companies Act of 1985 (c 6).

218 Section 35(2) of The Compnaies Act of 1985 (c 6).

219 Nyombi "The gradual erosion of the ultra vires doctrine in English Company law" 2014 *International Journal of Law and Management* 347 at 355.

220 Ibid.

221 Section 35 of The Companies Act of 1985 (c 6). See also Cassim "The Rise, Fall and Reform of the Ultra Vires Doctrine" 1998 *SA Merc LJ* 293 at 299.

222 Ibid.

223 Delport "European Community Directives on the Harmonization of Company Law and United Kingdom Company Law: A Status Report" 1992 *SA Merc LJ* 293 at 200.

organs can never be relied upon against third parties, even if such limitations had been disclosed.[224] Section 35A was thus introduced to provide greater security to third parties.[225]

Lastly, section 711(A)(1) of the Companies Act 1985, which found application in circumstances where the third party is not protected by section 35(A), effectively abolished the doctrine of constructive notice, in that it stated that a person will not be taken to have notice of any matter merely because it is disclosed or made available for inspection.[226] Section 711(A)(1) should have been read together with section 711A(2), which made an important qualification to the abolition of the doctrine, in stating that where unusual circumstances exist which is known to a third party, it will elicit a duty by the third party to make further inquiries.[227]

5.3. CONTINUED APPLICATION OF THE TURQUAND RULE

It is evident that today English law primarily follows an ancillary rule approach when reliance on the Turquand rule comes into question.[228] This is based firstly on the fact that the courts have followed this approach as set out by the Court of Appeal in the *Freeman*[229]-case.[230] Furthermore, it is widely viewed that the statutory amendments, as stated above, have supplemented the Turquand rule to a large extent.[231]

In the *Freeman* case the court applied the ordinary principles of agency law and resulted in a company being bound to an instruction which was given by the company's managing director, stemming from the principles of ostensible authority.[232] Van Niekerk stated that the real value of this judgment in the Freeman-case is threefold. Firstly, the judgment placed corporate representation in English Law squarely within an agency criterion, in essence resulting in an

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224 Payne "Company contracts and conundrums: When is a board not a board and when is a director not a person" 2004 *European Company and Financial LR* 235 at 239.

225 Ibid at 242.

226 Cassim "The rise, fall and reform of the ultra vires doctrine" 1998 *SA Merc LJ* 293 at 304.

227 Ibid.

228 See Cassim *et al Contemporary Company Law* (2021) 235-236:

> "In English law, by contrast, the common-law Turquand Rule became interwoven with estoppel or ostensible authority as a result of the decision in *Freeman and Lockyer v Buckhurst Park properties (Mangal) Ltd*… In English law, *Freeman and Lockyer* ruled that the common-law Turquand Rule was part of estoppel in English law. This means that the rule applies only if the requirements of estoppel are satisfied."

229 *Freeman and Lockyer v Buckhurst Park Properties (Mangal) Ltd* (1964) 1 All ER 630 (CA).

230 Van Niekerk *The development and reform of the rules regulating authority to contract on behalf of companies is South African and English Law* (LLD-Thesis, University of Cape Town, 2021) 100. See also Cassim and Cassim "The authority of company representatives and the Turquand rule revisited" 2017 *SALJ* 639 at 661.

231 Ibid.

232 Van Niekerk *The development and reform of the rules regulating authority to contract on behalf of companies is South African and English Law* (LLD-Thesis, University of Cape Town, 2021) 104.

Ancillary Rule Approach to the Turquand rule.[233] Furthermore, the judgment clarified and aligned conflicting decisions preceding it pertaining to agency principles.[234] Lastly, this judgment authoritatively emphasised the agency principles relevant to corporate representation.[235]

The conflicting judgments[236] preceding the *Freeman* case in English law, pertaining to agency principles and the application of the Turquand rule, has been adequately dispensed with and explained in the *Freeman* case and this case has now laid down the settled law to be followed. This has been aptly stated in *Hely-Hutchinson*[237] when it was held:

> "The cases on this branch of the law are numerous, and until recently they were by no means easy to reconcile. They extended over more than a century and, until the recent decision of the Court of Appeal in [Freeman] were by no means easy to understand. But I am absolved from any detailed consideration of the earlier cases by the fact that in the Freeman case the Court of Appeal exhaustively reviewed and analysed those earlier cases, and laid down, in terms which are binding upon me, what the law applicable to this part of the case is."[238]

Considering the *Freeman* case in English Law, inference can be drawn that the Turquand rule only operates if the requirements of estoppel are satisfied.[239] This will lead to the practical implication of when reliance is placed on a company's Memorandum of Incorporation to establish estoppel, the third party will have to have known and relied upon the Memorandum's contents.[240]

Similarly to the considered codification of the Turquand rule in South African law under section 20(7) of the Companies Act, the rule has been codified by section 40 of the United Kingdom Companies Act , 2006.[241] This section not only supplements the Turquand rule but

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233 Ibid.
234 Ibid.
235 Ibid.
236 *Houghton & Co v Nothard, Lowe and Wills Ltd* (1927) 1 KB 246 (CA) at 266; K*reditbank Cassel GmbH v Schenkers Ltd* (1927) 1 KB 826 (CA) at 844 ; *British Thompson-Houston Co Ltd v Federated European Bank* Ltd (1932) 2 KB 176 (CA); *Clay Hill Brick and Tile Co Ltd v Rawlings* (1938) 4 All ER 100.
237 *Hely-Hutchinson v Brayhead Ltd* (1968)1 QB 549 (CA).
238 Ibid at 562E.
239 Cassim and Cassim 'The authority of company representatives and the Turquand rule revisited" 2017 *SALJ* 639 at 661.
240 Ibid.
241 Ibid at 662.

exceeds the protection that is afforded to third parties when compared to the common law Turquand rule.[242] As a result, the common law Turquand rule has not been repealed by this section, but continuous to operate alongside the statutory protection flowing from section 40.[243] Since the protection afforded to third parties by section 40, the importance of the Turquand rule has decreased.[244]

Section 40 (1)-(2) of the United Kingdom Companies Act, 2006 states that:

> "(1)In favour of a person dealing with a company in good faith, the power of the directors to bind the company, or authorise others to do so, is deemed to be free of any limitation under the company's constitution.
>
> (2)For this purpose—
>
> (a)a person "deals with" a company if he is a party to any transaction or other act to which the company is a party,
>
> (b)a person dealing with a company—
>
> (i)is not bound to enquire as to any limitation on the powers of the directors to bind the company or authorise others to do so,
>
> (ii)is presumed to have acted in good faith unless the contrary is proved, and
>
> (iii)is not to be regarded as acting in bad faith by reason only of his knowing that an act is beyond the powers of the directors under the company's constitution."

Notably, a person will not be considered as acting in bad faith merely because he knows that a certain act of the company is beyond the powers of the directors under the company's constitution or merely beyond their authority.[245] This is in contrast with the common law Turquand rule, where the rule will be negated by actual knowledge of the irregularity, thus

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242 Ibid.

243 Frantzen *The powers and authority of directors to act on behalf of a company under South African law* (LLM-Thesis, University of South Africa, 2019) 45.

244 Ibid.

245 Cassim and Cassim 'The authority of company representatives and the Turquand rule revisited" 2017 *SALJ* 639 at 661.

resulting in this section broadening the scope of protection given to third parties when compared to the common law rule.[246]

Furthermore, section 40 will only apply in instances where the contracting third party was dealing with the board of directors or an authorised agent by the board.[247] This section will not find application where the agent was not authorised by the board of directors to act on behalf of the company.[248] Should this scenario arise, the common law Turquand rule or the principles of ostensible authority should be relied upon and applied to ascertain whether the company may be held liable.[249]

5.4. CONCLUSION

The English company law framework has for all intent and purposes abolished the doctrine of constructive notice through section 9 of the European Communities first direct and later through section 35 of the Companies Act 1985. It has further become settled law that the common law Turquand rule forms part of agency law and is a mere extension thereof. The rule has also been codified in section 40 of the United Kingdom Companies Act, 2006. The codification of this rule and the protection it affords third parties has diminished the importance and reliance placed on the Turquand rule in English law.

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246 Ibid. See also Frantzen *The powers and authority of directors to act on behalf of a company under South African law* (LLM-Thesis, University of South Africa, 2019) 46:

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

247 Frantzen *The powers and authority of directors to act on behalf of a company under South African law* (LLM-Thesis, University of South Africa, 2019) 47.

248 Ibid.

249 Ibid.

CHAPTER 6: CONCLUSION

6.1. INTRODUCTION

This research study set out to address the development of the Turquand rule and the doctrine of constructive notice in South African Company law. This was done by firstly assessing the concept of authority and agency principles within company law and how these concepts are of practical importance in corporate contracting. Thereafter, an analysis was done of the doctrine of constructive notice and this doctrine's general abolishment, not just in our law but also in English law. This brought the company law legislative framework in line with modern developments.

The Turquand rule's development was discussed by assessing its continuous application in modern company law and how this rule has evolved beyond a mere remedy to mitigate the effects of the doctrine of constructive notice. The partial codification of the common law positions has also bee analysed and the extensive confusion this codification creates. Furthermore, how this rule is practically applied by the South African courts and the conflicting views of the rule against the law of agency. Lastly, this research has indicated how this rule has been interwoven with the law of agency in English Law.

The abolishment of the doctrine of constructive notice, with the exclusion of "RF" companies, and the partial codification of the Turquand rule are welcome developments that have coincided with the changing of the times to cater for a more modern approach to these company law doctrines. However, the common law Turquand rule should not be disregarded and furthermore not be applied in accordance with the ancillary rule approach to that of agency law.

It is respectfully submitted that the legislature has fell short of adequately abolishing the doctrine of constructive notice and left much debate pertaining to the partial codification of the Turquand rule in section 20(7) of the Companies Act. Furthermore, the need to read the common law positions in conjunction with the Act, rather than a substitution therefore, has created some uncertainty as discussed above.[250]

[250] See para 4.3 of Ch 4 above.

6.2. RECOMMENDATION: DOCTRINE OF CONSTRUCTIVE NOTICE

The author recommends that the doctrine of constructive notice be abolished in its entirety and must not even find application to "RF" companies, where the Memorandum of Incorporation contains some sort of restrictive condition.[251] The reasoning for this is, that in the authors view, the law has shifted to a third-party perspective and that of business convenience when contracting with a company. This has resulted in the view that a third party must be afforded as much protection as possible when contacting with a company.[252]

It is submitted that the limited continued application of the doctrine of constructive notice can be abused by companies to protect themselves when contracting with third parties. In accordance with section 19(5) of the Companies Act, companies can merely add the suffix "RF" to their name and as a result draw attention to some "considered" restrictive condition in the Memorandum of Incorporation. Alternatively, the Act should be amended to clearly state what is considered as a 'restrictive condition' as this will result in the limited application of the doctrine and will only be used for the intended purpose.[253]

The legislature, regardless of the abovementioned irregularities, should be commended for the lesser or so-called diluted version of the doctrine, as far more protection is now afforded to third parties compared to the position under the old Companies Act. Therefore, this diluted version of the doctrine should not be regarded as completely ineffective as it greatly curtails the past disposition applicable to third parties when contracting with a company.

6.3. RECOMMENDATION: TURQUAND RULE

Pertaining to the Turquand rule, the author is of the view that the rule should be seen as an independent remedy separate from that of agency law principles. The rule must still be applied to give ultimate protection to third parties when contracting with a company in certain circumstances. The recent shift in South African law, to bring it in line with the settled view in English law, that the Turquand rule is merely an extension of estoppel/agency principles is regrettable.[254] The author is of the view that this goes against business convenience and full protection afforded to third parties when dealing with companies, as the rule independently

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251 See para 3.3 of Ch 3 above.
252 Ibid.
253 Ibid.
254 See para 4.2 of Ch 4 above.

affords more protection to third parties than when the rule is regarded as a mere extension of estoppel. The reasoning behind this flows from the fact that the rule, independently viewed, has fewer requirements to be met than that of estoppel. Therefore, the author favours an independent rule approach to the Turquand rule, separate from the requirements to be established when proving estoppel.[255]

Retaining the common law Turquand rule alongside section 20(7) of the Act, as stipulated in section 20(8) of the Act, creates some confusion as it is unclear how these two rules should be integrated with one another.[256] It is clear that section 20(7) of the Act shows similarities to the common law rule, hence the partial codification, it is however unclear as to the section's scope of operation and application. The number of uncertainties, inconsistencies and discrepancies highlighted in the research above, leads to far more uncertainty by a third party than the intended protection.[257]

Accordingly, the author recommends that this section be amended by the legislature to clearly expand the application of the section in some areas to bring it in line with that of the common law rule's wider application. This will result in a third party not being deprived of the protection he would have had under the common law rule. Section 20(7) of the Companies Act, like the common law rule, should be applied wide enough and a third party should be able to rely on section 20(7) in circumstances dealing with situations, *inter alia*, where the necessary prior shareholders' approval and formalities was not adhered to pertaining to the appointment of directors, formalities pertaining to delegation by the board to a single representative and lastly formalities relating to meetings and quorums.

To dispel of the uncertainties, the legislature must, *inter alia*, define what is meant by "formal and procedural" requirements and it should be clear that this section will only apply in scenarios where the directors or agent of the company exceed their authority and not where the company's capacity comes into question. Alternatively, that the codification of the Turquand rule must be read as a substitution rather than in conjunction with the common law. The other side also holds true, by repealing the provisions pertaining to the Turquand rule and afford the common law position to develop.[258]

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255 Ibid.
256 See para 4.3 of Ch 4 above.
257 Ibid.
258 Ibid.

6.4. CONCLUSION

It is therefore respectfully submitted by the author in conclusion that the legislature fell short in adequately dispensing with the doctrine of constructive notice in its entirety and that the partial codification of the Turquand rule has created more confusion that certainty within company law. The limited application of the doctrine however should be applauded since it now creates much more protection for third parties when dealing with a company.

The author further submits that the Turquand rule must remain an independent remedy available to third parties contracting with a company, apart from that of agency law. The rule must not be established as being a form of agency law, as in English law. The rule must still enjoy its rightful independent place within company law. The rule should further enjoy continued application in South African law even in light of the doctrine of constructive notice now being abolished.[259]

Furthermore, the discrepancies that the partial codification of the Turquand rule has created cannot be left as is by the legislature and the provisions relating to the Turquand rule need to be amended. These amendments taking the form that the codified version of the rule is the only version i.e. abolish the common law rule or alternatively, repeal the provisions in their entirety as contained in the Act and let the common law continue to find application and develop accordingly.

[259] See para 4.4 of Ch 4 above.

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