# CORPORATE AND COMMERCIAL

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## CAN THE AUTHORITY OF A DIRECTOR BE PRESUMED?

**The recent High Court judgment of *One Stop Financial Services (Pty) Ltd v Neffensaan Ontwikkelings (Pty) Ltd and Another* (20028/14) [2015] ZAWCHC 89 has clarified some important points around the *Turquand* rule (or the so-called "indoor management" rule) which exists in both common law and now under s20(7) of the Companies Act, No 71 of 2008 (Companies Act). The *Turquand* rule relates to the presumption of the authority of an agent of a company, and has a number of requirements and subtleties.**

The general rule is that if an agent is unauthorised, he does not validly bind the principal and accordingly no valid contract is concluded with the principal. Clearly such a rule would operate with prejudicial effects in commerce in the context of companies and other juristic persons, and thus for many decades there has existed a common law rule whereby a third party may presume that an agent of the company has followed all internal procedures and obtained all internal approvals before concluding a contract on that company's behalf. The rule emanates from the seminal English case of *Royal British Bank v Turquand* (1856) 6 E&B 327. The Companies Act has in a sense codified the *Turquand* rule in s20(7) which provides as follows (emphasis added):

> 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.

Section 20(8) then appears to preserve the common law at the same time:

> Subsection (7) must be construed concurrently with, and not in substitution for, any relevant common law principle relating to the presumed validity of the actions of a company in the exercise of its powers.

This alert by no means attempts to summarise all the aspects of the complex and extensive *Turquand* rule, and it should be noted that there are other grounds upon which a third party may rely, such as estoppel, ostensible authority, implied authority and ratification. The recent *One Stop* case did, however, make some important observations, and confirmed important legal principles, regarding the applicability of the common law and statutory *Turquand* rule in respect of individual directors who purport to bind their company:

- The point of departure is that it is the board, and not an *individual director*, that may validly contract on behalf of the company.
- Where the company's constitution (Memorandum of Incorporation) permits the board to appoint one of their number as a *managing director*, the person so appointed may reasonably be assumed to have delegated authority to conduct transactions within the usual scope of a managing director's authority.
- There may be other types of executive positions, whether held by a director or an employee, which carry with them a representation of an authority usual to that type of position (for example a financial director or branch manager) and to whom similar principles would apply.
- However, outside of those cases, a third party is not ordinarily entitled to assume that an individual director has authority to represent the company. The mere fact that the company's constitution permits the board to delegate authority to a single director does *not* entitle the third party to assume that *any* director with whom he deals has been the recipient of delegated authority.

*continued*



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The above has been relatively clear in our case law for quite some time. But what of s20(7)? Does the section extend the *Turquand* rule, and does it now allow a third party to presume the delegated authority of an individual director? In this regard, the court emphasised that s20(7) refers to a presumption of compliance with "formal and procedural requirements": If an individual director did not have delegated authority from the board in the first place, that cannot be said to be a mere "formal or procedural" defect or omission. The court did not believe that s20(7) was intended to be a radical deviation from, or modification of, the well-established common law principles around the indoor management rule. The court was of the view that:

> Another way of looking at this question is by giving due weight to the requirement in s20(7) that the third party should have been dealing with the 'company'. The section does not state that the third party may make any assumptions when dealing with a purported representative per se. This reinforces the view that in order for s20(7) to apply the third party must establish that he was dealing with someone who had actual or ostensible authority to bind the company, because only in those circumstances can he say that he was dealing with the 'company'.

In other words, there must in the first place be an agent who could bind the company, but that agent failed to follow certain internal protocols.

Thus the principles around the entitlement to presume an individual director's authority remain intact for now, but it remains to be seen how a higher court might interpret the concept of "formal and procedural requirements" as contained in the statutory *Turquand* rule when the opportunity arises, especially for instance in the context of those provisions of the Companies Act (or a company's Memorandum of Incorporation) which require shareholder approval for certain transactions.

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