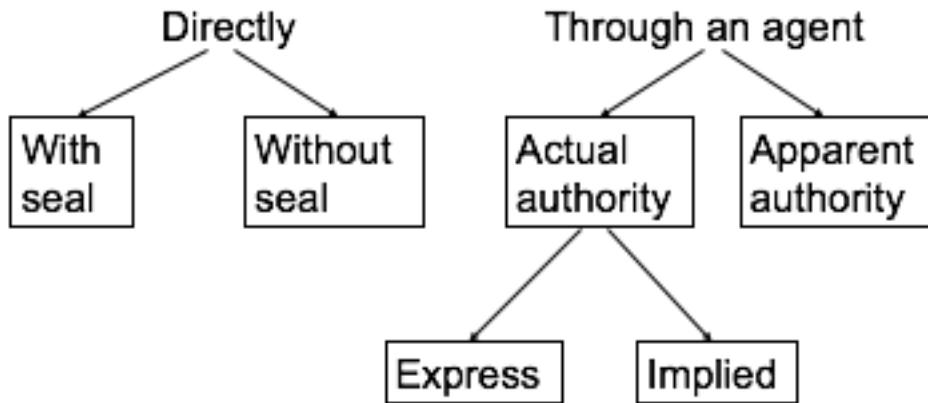


TOPIC 3: CONTRACTS WITH OUTSIDERS

HOW DO COMPANIES CONTRACT WITH THIRD PARTIES?



EXECUTION WITHOUT A SEAL S 127 (1)

A company may execute a document without using a common seal if the document is signed by:

- 1) 2 directors of the company
- 2) a director and a company secretary or-
- 3) For a proprietary company that has a sole director who is also the sole company secretary- that director

DIRECTLY

- Traditionally: by using its “common seal”
- Seal no longer required (see page 512 for example of company seal)
- Three ways possible now
 - Execute the document with seal, and necessary witnesses – s127(2)
 - Execute the document without seal – signed as required by s127(1)
 - Use procedure set out in constitution
- As well as proper signing/sealing procedure, there must also be authority for the company to enter the contract
 - Normally comes from the board
 - Resolution #1 approves company entering the contract (“substantive authority”)
 - Resolution #2 authorizes the execution of the documents in a specified way (“formal authority”)

AGENT

The Law of Principle and Agent

Three parties

- Principal
- Agent
- Third Party

Two contracts

- Principal and Agent
- Principal and Third party
 - Subject to powers and authority of agent.

Generally, the Board of Directors collectively, is the agent of the company.

Also includes senior employees and directors acting alone

The issue is depending on the level of the person what authority they have to enter into contracts on behalf of the company

ACTUAL AUTHORITY

- Where the principal has actually agreed that the agent can act on the principal's behalf
- Actual Authority can be express or implied

EXPRESSED

Where the principal says (verbally or in writing) that the agent can act for the principal, the agent has express actual authority. Power of directors in the corporations Act or in constitution says you have authority of Board of Directors by resolution give you authority. Can arise by way of oral or written statement.

- Can arise from a provision in the Corporations Act or the company's constitution e.g. s198A
- Can also arise when a company agent (e.g. the board) who has actual authority delegates some of their own actual authority e.g. appoint a CEO with certain authority
- By statute e.g. s198A (RR) Power of directors in the Corporations Act
- Can arise by way of oral or written statement, e.g. The Constitution of the company says *'Board may make contracts up to \$100,000, but above that, shareholder approval is required'*.
- - The Board to MD
 - 'Managing director may make contracts up to \$10,000 in value, but above that value, Board approval is required'*

IMPLIED

Implied: although not expressly stated, it is

implied by courts in the circumstances as being reasonably necessary to carry out express authority (flows naturally from express authority). The position or title you have
Managing Directors:

Indirect statements made by the principal and from principal's conduct. Implied actual authority can arise by implication from things the principal says and does. Included in "things the principal does" are:

- a) appointing someone to a certain position
- b) otherwise acting to give the person, include through 'acquiescence'

although not expressly stated, it is implied by courts in the circumstances as being reasonably necessary to carry out express authority (flows naturally from express authority).

Manage the daily affairs of the company

'To do all things as fall within the usual or customary scope of that position': Hely- Hutchinson v Brayhead Ltd [1968]1 QB 549.

What is the usual scope?

Dealing with everyday matters; running the company; supervising others; and being in charge: Entwells Pty Ltd v National and General Insurance Co Ltd (1991) 5 ACSR 424 but NOT selling the company's business!

APPARENT AUTHORITY

- Agent appears or seems to have authority from the perspective of the outsider because the company has held out or represented the person as having the necessary authority (even if they do not have express/implied authority) :
Implied from the conduct of the parties and the circumstances
- When agent is placed in a particular position by the principal
- e.g. appointed to manage the business and therefore authority
- to make contracts that a person in that position customarily
- has. (*Hely-Hutchinson v Brayhead Ltd.*)
- *In Brick & Pipe Industries Ltd v Occidental Life Nominees Pty Ltd*
- the court held that a director was taken to have implied authority

INDOOR MANAGEMENT RULE

Persons dealing with a company in good faith may assume that acts within its constitution and powers have been properly and duly performed and are not bound to inquire whether acts of internal management have been regular. Therefore, the outsider can assume that the company has followed its internal processes.

Royal British Bank V Turquand-

Where Royal British Bank was entitled to assume that Turquand's internal process had been followed and the bank did not know or suspect there had been a failure to Turquand to follow its internal procedures.

EXCEPTIONS TO IMR

An outsider is prevented from relying on the indoor management rule when:

- - The "actual knowledge exception" applies: If the outsider actually knows that the purported agent lacked express actual authority, or that the contract was defective in some other way, then the outsider will be unable to enforce the contract on the basis of apparent authority, implied actual authority or the indoor management rule. Also, if the court finds that the outsider deliberately "kept his or her eyes shut" in order not to discover the irregularity that they thought existed, the actual knowledge exception applies. Or
- - The "put on inquiry exception" applies: (a) The outsider has failed to make inquiries that would usually or customarily be made by someone in the outsider's position or (b) a reasonable person in the outsider's position would have been "put on inquiry" about a possible irregularity, and would have investigated, but the outsider has either not investigated at all or not investigated sufficiently.

s128(1) – a person is allowed to make the assumptions in s129 in relation to dealings with a company. s129 (1) – A person may assume that the company's constitution and any provisions of this Act that apply to the company as replaceable rules, have been complied with/statutory indoor management rule BUT EXCEPTION s128 (4)

s129 (2) and (3) – What is customarily, note type of authority E.g. MD can borrow money, make contracts related to the day to day operations of the company, cannot sell the business of the company, can't enter contracts that are not in the normal course of the company's business

s128 (3) – the assumption may be made even if an officer or agent of the company acts fraudulently, or forges a document, in connection with the dealings. s128 (4) – a person is NOT entitled to make an assumption in s129 if at the time of the dealings they knew or suspected that the assumption was incorrect.

Under common law, the indoor management rule doesn't apply if fraud is present making

contract invalid.

However, under statute law the indoor management rule does apply even if fraud exists under s128 (3) which REPLACES the common law.

NORTHSIDE DEVELOPMENTS VS REGISTER GENERAL

Northside Developments Pty Ltd V Register General – Where the company was not bound by the mortgage as Barclays Bank should have made further enquiries of the full company board suspecting irregularity but didn't.

EXCEPTION TO INDOOR MANAGEMENT RULE

1. Knowledge of rules and not met
2. Know person had no authority
3. Contract unusual and suspicious
 - Liability and asset must go to principal
 - If not --> unusual