Agents Behaving Badly

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Chief Justice, Judges, colleagues, ladies and gentlemen.

A. Introduction – macro and micro problems in corporate attribution

My talk tonight is on agents – in particular, agents behaving badly.

I've chosen this topic because of its importance. Modern business is routinely transacted by agents. That is inevitably so when the transaction involves a company. The relevant legal rules on attribution and agency are thus an indispensable element of modern commerce. They are well established, well used and, one might expect, well settled. It might then seem preposterous to suggest that in England these rules on corporate contracting are descending into an unholy muddle. But that is the thesis of my lecture tonight.

I know this talk would be controversial if presented in the UK. Perhaps it will be so here. And yet I don't think I'm about to say anything which deviates very much from what I was taught – or what I *thought* I was taught (I do appreciate the difference) – as an undergraduate at the University of Queensland some time ago.

These modern English problems are neither trifling nor tangential.

I've divided my lecture in two, looking at both macro and micro issues.

<u>First</u>, at the macro level there are problems with the very foundations of attribution in corporate law.[1] The key attribution question is easy: whose acts will count as the acts of the company?[2] But arriving at the right answer is sometimes extraordinarily difficult. This is especially so when the

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[1] *Moulin Global Eyecare Trading Ltd (In Liq) v Commissioner of Inland Revenue* [2014] HKCFA 22 (HKCFA), [61] (Lord Walker): 'Attribution means, in this context, the process of legal reasoning by which the conduct or state of mind of one or more natural persons (that is, human beings) is treated as that of a non-natural person (that is, a company) for the purpose of determining the company's legal liability or rights in civil proceedings (in particular, its liability or rights in contract, in tort or for unjust enrichment) or its criminal liability'.

[2] *Meridian Global Funds Management Asia Ltd v Securities Commission* [1995] 2 AC 500 (PC), 507 (Lord Hoffmann).

company is in the grip of fraudsters, but the problems extend more broadly. This is forcefully illustrated by two famous (or infamous) English cases: *Stone & Rolls Ltd (in Liq) v Moore Stephens (A Firm)*[3] and *Safeway Stores Ltd v Twigger*.[4] In the first, the House of Lords denied a one man company the right to sue its negligent auditors; in the second the English Court of Appeal denied a UK supermarket chain the right to sue its wrongdoing directors and employees. The special facts are significant, but the unadorned outcomes look startling.[5] They suggest something fundamental has gone awry in the law on corporate attribution. I suggest the company is being penalised by unwarranted identification with its misbehaving agents, and will use the *Stone & Rolls* case to develop that idea.

Secondly, at the micro level, there are serious problems in applying the elementary rules of agency in the corporate context. Take actual authority. The modern English position is that an agent has actual authority to do only those acts which are in the company's interests. Acts which are contrary to the corporate interest are unauthorised. In these circumstances contracts with outsiders can only be based on ostensible authority. The result is that outsiders dealing with agents, even an agent such as the company's CEO, may have to turn to estoppel and prove reliance on an effective representation that the CEO can indeed act.[6] That seems odd. It is true, of course, that no principal would *actually authorise* an agent to act contrary to the principal's interests, but that is not the real question in issue in these contracting cases. Or it should not be.

I want to cover both these macro and micro strands. I also want to be critical. Diplomacy suggests I should therefore focus on English cases – or at least on English judges – not Australian ones. I will leave you to make the relevant comparisons yourself.

Turning first to the macro issues – these are the big picture issues in corporate attribution.

B. Big picture issues – the macro problems in corporate attribution

Any modern discussion of corporate attribution invariably begins with Lord Hoffmann's analysis in *Meridian Global Funds Management Asia Ltd v Securities Commission*,[7] and his description of 'the rules of attribution' which enable a company to function in the real world. His classification of these

[3] *Stone & Rolls Ltd (in Liq) v Moore Stephens (A Firm)* [2009] UKHL 39; [2009] 1 AC 1391 (HL).
[4] *Safeway Stores Ltd v Twigger* [2010] EWCA Civ 1472 (CA).
[5] Earlier this year the Supreme Court conceded the outcome in the first case (obiter) and did not overrule the second, although some judges expressed doubts: *Bilta (UK) Ltd (in liq) v Nazir* [2015] UKSC 23 (SC).
[6] *Thanakharn Kasikorn Thai Chamkat v Akai Holdings Ltd* (2010) 13 HKCFAR 479 (HKCFA).
[7] *Meridian Global* (n 2), 506-7 (Lord Hoffmann).

rules as primary,[8] general[9] and special,[10] his elucidation of their content, and the toppling of the mythology surrounding a company's 'directing mind and will',[11] all repay meticulous re-reading. But for current purposes what is crucial is the single question that all these rules of corporate attribution seek to answer: 'Whose act (or knowledge, or state of mind) was *for this purpose* intended to count as the act etc. of the company?'[12] This is not an easy question.

Testing the macro issues: *Stone & Rolls*

Stone & Rolls Ltd (in Liq) v Moore Stephens (A Firm)[13] provides a dramatic illustration. As noted earlier, the House of Lords denied the claimant, a one man company, the right to sue its negligent auditors.

I use this particular illustration with some hesitation. I am conscious that Justice Jackson ran his 2014 WA Lee Lecture on the theme of why little is decided by cases where the plaintiffs don't win. In my defence, I hope he is right, and that little is considered to have been decided by this particular case!

The case is difficult.[14] Lord Neuberger, the current President of the Supreme Court, thinks it should be put to one side, not to be looked at again.[15] But that would be premature. The Supreme Court

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[8] These are mandatory, company-specific rules found in the company's constitution (typically in its articles of association) and also in specific company law rules developed by judges (eg the rule that the unanimous intra vires decision of the shareholders in a solvent company will bind the company: *Multinational Gas and Petrochemical Co v Multinational Gas and Petrochemical Services Ltd* [1983] Ch 258): ibid, 506.

[9] These are further rules of attribution which are 'equally available to natural persons, namely, the principles of agency': ibid, 506. Note that these general rules of attribution do *not* include estoppel or ostensible authority in contract, or vicarious liability in tort. These doctrines are not rules of attribution: they do not indicate whose acts count as the acts of the company. Instead, they impose liability (estoppel-based or public policy-based) on the company for the acts of others (whose acts are not acts of the company). As Lord Hoffmann said: 'And having done so [ie having identified and empowered specific agents], it will *also make itself subject to* the general rules by which *liability for the acts of others* can be attributed to natural persons, such as estoppel or ostensible authority in contract and vicarious liability in tort.' (emphasis added): ibid, 506.

[10] This category probably causes more concern than is warranted. Lord Hoffmann's attribution question is key: 'Whose act [is] … *for this purpose* intended to count as the act … of the company?' If this question is not answered explicitly by either the primary or the general rules of attribution, then it must be answered by seeking inferences. These inferences must be such as to indicate whose act will count as the act of the company in the particular circumstances in issue. As such, they are most likely to emerge from a close examination of the particular operating structure of the target company (as they did in *Meridian* itself, and indeed as they did in *Lennard's Carrying Co Ltd v Asiatic Petroleum Co Ltd* [1915] AC 705: see the discussion in *Meridian* at pp 509-511). There is nothing magic about this. If something must exist (ie a person whose acts count as the acts of the company), but that thing has not been described expressly, then the courts must examine the relevant circumstances and find the implicit explanations. That is exactly what Lord Hoffmann did in *Meridian*.

[11] See especially *Meridian Global* (n 2), 509-510.

[12] ibid, 507 (Lord Hoffmann). The emphasis is his.

[13] *Stone & Rolls* (n 3); *Safeway Stores Ltd v Twigger* (n 4). But also see *Bilta v Nazir* (n 5), [86], where Lord Sumption favours attribution applying 'regardless of the nature of the claim or the parties involved', but would then invoke public policy exceptions to permit company claims against directors. To the contrary, Lord Mance, at [36]-[37], favours a 'simpler and more principled analysis.' Who would disagree?

earlier this year appeared to accept the outcome of the case on its special facts, and certainly did not put its judicial finger on the essential problems with the reasoning.[16] Without that guidance, the risk of resurrecting the same dubious thinking remains high. Rather than ignoring the case, the latent difficulties need to be nailed.

The facts are deceptively simple. Mr Stojevic was effectively the sole director and sole shareholder[17] of Stone & Rolls, a company set up for the express purpose of defrauding banks. By the time the frauds were discovered, both the money (~$US174m) and the fraudster had disappeared.[18] The claims by the defrauded banks put the company into liquidation, and the liquidator then sued Moore Stevens, the company's auditors, for their allegedly negligent failure to discover the fraud over several years.

The auditors successfully sought to strike out that claim on the basis of the 'illegality defence' (*ex turpi causa*), insisting that the court should not allow its processes to be used by the company to enable it to benefit from its *own* illegal conduct.[19] Whether Stone & Rolls *was* seeking to benefit from its *own* wrong was key. The House of Lords found the question exceptionally difficult, and in the end split 3:2 to hold that the company could <u>not</u> sue its auditors. In the majority were Lords Phillips, Walker and Brown; the dissenters were Lords Mance and Scott. In short, both sides had hefty proponents.

The scope of the *ex turpi* defence is controversial,[20] and its use in these corporate contexts was novel. Here it produced a perverse result: it permitted an admittedly culpable auditor (or one assumed so for the purposes of the strike out) to escape liability for negligent audit practices to the detriment of the defrauded company and its innocent creditors.[21]

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[14] The judges in the case thought it so, and one of them, Lord Walker, reiterated that in *Moulin Global* (n 1), see especially [101], [106], [133].
[15] *Bilta v Nazir* (n 5), [30] (Lord Neuberger). Also see the cautious approach to *Stone & Rolls* in *Moulin Global* (n 1).
[16] Although there are a good number of thoughtful commentaries on the case: see especially E Ferran, 'Corporate Attribution and the Directing Mind and Will' (2011) 127 LQR 239; P Watts, 'Stone & Rolls Ltd (In Liquidation) v Moore Stephens (A Firm): Audit Contracts and Turpitude' (2010) 126 LQR 14.
[17] Sole beneficial shareholder and controlling shadow director.
[18] In claims of fraud, the individual cannot insist that he was acting *only* as the embodiment of the company and not in a personal capacity: *Standard Chartered Bank v Pakistan National Shipping Corp (No 2)* [2002] UKHL 43, [2003] 1 AC 959 (HL). Contrast the assumption of responsibility for negligent statements: *Williams v Natural Life Health Foods Ltd* [1998] 1 WLR 830 (HL).
[19] The Queen's Bench Division decided the company could sue, but that view was unanimously overruled by the Court of Appeal, and also by the House of Lords by a majority of 3:2 (Lords Phillips, Walker and Brown in the majority; Lords Scott and Mance dissenting).
[20] See *Bilta v Nazir* (n 5), [15] (Lord Neuberger), indicating the issue needed urgent Supreme Court resolution before a seven or nine member tribunal.
[21] See the strong dissents of Lords Mance and Scott.

It is impossible to distil a coherent ratio from the case, and that is not the point of the analysis in this lecture. Nevertheless, a starting point is needed, and to varying degrees the three majority judgments seemed to subscribe to the following logic:

(i) Stone & Rolls was <u>personally</u> liable for the fraud on the banks, not merely vicariously liable;

(ii) in its action against its auditors, <u>this</u> was the wrong from which Stone & Rolls sought to benefit;

(iii) even in an action *against* the auditors (as distinct from an action *by* the banks), Stone & Rolls remained personally liable for this fraud – it was not assisted by an odd principle known as the *Hampshire Land* principle;[22]

(iv) it followed that since Stone & Rolls was seeking to benefit from its personal wrongdoing, the *ex turpi causa* defence applied to deny the claim; and

(v) in any event, the auditors, even if negligent, were not liable to the one man company, because in these particular circumstances there was either no duty or no causal loss.

Although the judgments made nothing of it, this last point is a knock-down argument, rendering steps (i)-(iv) immaterial. Certainly on this logic, if each step can be made out, then Stone & Rolls' claim must fail.

But the issue for this lecture is the extent to which the analysis which delivered these conclusions failed to pay due regard to the macro issues in corporate attribution: first, to the company's separate legal personality; and secondly to the simple but vital qualifier, '*for this purpose*', in Lord Hoffmann's key attribution question.

Each is considered in turn. Each is important.

I will undoubtedly appear critical of the outcomes in this case. I am. But I am not critical of the obvious erudition in the judgments: to use an apt Australian analogy, it is invariably easier to see the lie of the land after a track to the summit has been hacked through the undergrowth.

Turning first to the issue of paying due regard to the company's separate corporate personality.

[22] *Hampshire Land Co (No 2), Re* [1896] 2 Ch 743 (Ch).

1. Due regard for the separate corporate personality of companies

Corporate attribution is all about ascribing acts, knowledge and intention to companies. It is clearly crucial to pay due regard to the separate personality of companies.

There is evidence that the House of Lords failed on this front at three particular stages in its analysis: first, in ascribing special status to one man companies; then in analysing the duties of auditors to such companies; and finally in considering the particular harm suffered by such companies at the hands of the auditors.

1. The 'one man company' exception found in **Stone & Rolls**

First – the special status of one man companies. Notice that the steps in the logic just ascribed to the House of Lords can be set out quite coherently without any mention of the fact that Stone & Rolls was a one man company owned and controlled by the fraudster, Mr Stojevic. Yet this fact was crucial at every step along the way in the majority's judgments, and their conclusion was expressly limited to that context. Had there been innocent directors or shareholders, their conclusion would have been otherwise.[23]

That distinction immediately sounds alarm bells. The core concern of the illegality defence is with what the company is *doing* in the litigation in issue: is it seeking to benefit from its own illegal conduct? That question can only be answered using the rules of corporate attribution, and those rules do not suffer a sea change depending on whether the company is owned and controlled by wrongdoers. With or without a few innocent directors or shareholders, Stone & Rolls could still be directly responsible for its own illegal conduct, and could seek to litigate to advantage.

Despite this, the House of Lords held that only one man companies would be regarded as taking advantage of their own wrong and barred from litigating. The irresistible inference is that the corporate veil has been ignored:[24] the implicit logic is that because the fraudster himself cannot sue,[25] then nor can his puppet company.[26] This will not do. There is no simple equivalence between the 'one man' and the 'one man company'. That is the very first lesson of corporate attribution.

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[23] At various points throughout the judgments, but see, eg, *Stone & Rolls* (n 3), [174], [203]. Lord Phillips' judgment is harder to characterise; he held that the auditors owed no duty in these circumstances of a one man company run by the fraudster, but also that in these circumstances (which, precisely?) the *ex turpi* defence applied: [18].

[24] The risk of inappropriately equating the fraudster and his company is high in all these cases. Nevertheless, ibid seems to suffer from the problem more than most: eg [18], [61], [131], [183], [174], [184], [195], [196], [199], [201]. By contrast, see Lord Mance at [206]-[207].

[25] Ibid, invariably assumed without argument. If the *ex turpi causa* defence did not stand in the way, the claim may fail in any event at the causation stage, or be limited on the grounds of contributory negligence.

2. Separate personality and the scope of auditor liability

The same slippage between 'the company' and 'the individuals behind the company' is seen in the court's analysis of auditor liability. Tonight I will not elaborate on the shortcomings in the analysis which led to the conclusion that the company could not sue,[27] or at least not a one man company in the grip of a fraudster, but will simply note that it worryingly misconceives auditor liability and, more importantly, again relies on an unacceptable simple equivalence between the 'one man' and the 'one man company'. Indeed, if the House of Lords were right, then audits of misbehaving one man companies would be pointless exercises, mere arid technicalities.

3. Separate personality and the company's particular claim against its auditors

The third indication that the House of Lords paid too little attention to the corporate form lies in their assumptions about the claim being made by Stone & Rolls against its auditors. The court – indeed *everyone* – assumed that the wrong from which Stone & Rolls sought to benefit was Stone & Rolls' fraud against the third party banks. But this is not true.[28] Quite how the court could have been so blindsided is not clear. The company's complaint was <u>not</u> that its auditors failed to detect that funds were coming *into* the company as a result of the company's fraudulent deception of the banks. That did not cause loss. The company's complaint was that the auditors failed to detect that funds were going *out* from the company, without any justification, to the fraudster, Mr Stojevic, and his associates.[29]

Viewed this way, the company's claim is clearly not one where the company sought to benefit from its own wrongdoing. If this is right, it would have demolished *ex turpi causa* argument in a single blow.

The distraction was a failure to pay due attention to the distinction between the 'one man' and the 'one man company' in the quite different contexts of the company's distinct relationships with the banks, the fraudster and the auditors.

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[26] *Stone & Rolls* (n 3), [118] (Lord Scott, dissenting) makes this precise point about the majority judgments.

[27] Some of the muddle may have been generated by a failure to isolate the auditor liability argument from the *ex turpi causa* argument. Lord Mance (dissenting) certainly thought so: ibid, [265]. And he maintained his criticisms in *Bilta v Nazir* (n 5), [46]-[47].

[28] See especially *Stone & Rolls* (n 3), [10] (ie even counsel for the company) and [27] (Lord Phillips).

[29] As recognised in ibid, at [102], by Lord Scott.

In short, as these three issues indicate, failure to pay due regard to the separate corporate personality of the company may have distracted the court from clear analysis of the issues.

Instead, the judges persuaded themselves to make special rules for one man companies both generally and in the context of auditors' duties, and they assumed that the company's wrong against the banks was the same corporate wrong which was material against the auditors. None of these conclusions holds water.

2. The machinery of corporate attribution – whose act counts '*for this purpose*'?

Turning now to the second macro issue. It follows directly from the first. Where the first focused on the separate personality of the company, the second focuses on the particular corporate allegation in issue. If the company is to be liable to a third party in some way, then what precisely must the company be shown to have *done*, or *intended*, or *known*? Only with that answer very clearly in mind can the specific attribution question be asked: whose acts, or intention or knowledge will count as the company's *for that purpose*? Generalisations are impossible. An individual within the corporate structure may act, or intend or know a wide variety of things, but her actions, intentions and knowledge will not count as the company's for all purposes. Ignoring that fact can derail the analysis.

The slippage is between 'attribution *for this purpose*', and 'attribution judged generically'.

Again, three points are made. These are the most important points in this first half of my lecture. They relate to the hierarchy of Lord Hoffmann's attribution rules; the troubling *Hampshire Land* principle; and the ex turpi defence as it applies to companies.

First, the corporate attribution rules generally.

1. Corporate attribution generally – no hierarchy of rules

All the judges in *Stone & Rolls* concluded that the company itself was directly or personally liable to the banks for defrauding them.[30] There is no complaint with this.

But the path to that conclusion in *Stone & Rolls* was not simple. Far too much was made of the generic feature that Mr Stojevic was the 'directing mind and will' of the company. This is not significant. It would not have mattered if there had been innocent directors and shareholders, or if

[30] Also see *Lloyd v Grace, Smith & Co* [1912] UKHL 1, [1912] AC 716 (HL); *Morris v CW Martin & Sons Ltd* [1966] 1 QB 716 (CA). And see *NSW v Lepore* [2003] HCA 4, [127] (in quite a different context) expressing a preference for findings of direct liability rather than vicarious liability for legal and policy reasons. This is eminently sensible.

Mr Stojevic had had a less senior role. Once Mr Stojevic was identified as the person whose acts and intentions count as the company's, precisely the same consequences would follow.

Put generally, there is no magic hierarchy in Lord Hoffmann's primary, general and special rules of attribution, and certainly no special significance accorded to the primary rules. *All* are simply rules describing how to identify the person (or persons) whose acts count as the company's for some particular purpose. This *is* how the company acts.

2. *The troubling* **Hampshire Land** *principle: an exception to what?*

Secondly, the troubling Hampshire Land principle and what it stands for. As an aside, naming a 'principle' by its case name rather than by its function is all too often an implicit admission that the principle is not properly understood. So it is here.

In *Stone & Rolls*, the Hampshire Land principle was described this way: the 'knowledge of the agent will not be attributed to the principal when the knowledge relates to the agent's own breach of duty to his principal.' A moment's thought suggests this cannot possibly be true as a general principle. Misbehaving agents are invariably in breach of duty to their principals. If their guilty knowledge, and perhaps their acts too, cannot then be attributed to the company, the law of corporate attribution would unravel completely. Almost all the cases go the other way.

The problem lies in stating the Hampshire Land rule generically. Attribution rules <u>cannot</u> be stated generically. Lord Hoffmann's attribution question is very particular – whose acts or knowledge count as the company's acts or knowledge *for <u>this</u> purpose?*

Pursuing this line, it is clear that the Hampshire Land principle does not protect companies when they are suing or being sued by outsiders. In either context the company is infected with the acts, knowledge or intentions of its fraudulent directors or employees.

But the Hampshire Land principle does have *some* life in it. I suggest the principle is only relevant when *the company sues its insiders*, and even then only for limited purposes. Wrongdoing defendants sued by claimant companies cannot escape liability by the ruse of claiming that *their own* acts or knowledge, attributed to the company, deliver the result that the company has waived, or shared, or conspired in the defendant's liability. Such assertions seem so contrary to common sense that, whatever our general rules, they cannot lead to this end.[31]

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[31] *Bilta v Nazir* (n 5), [42]. Also see generally [37]-[44].

The cases support this. This is regardless of whether *Hampshire Land* is cited. Typically it is not. All that is necessary is to ask the attribution question specifically, permitting no slippage between the precision of 'attribution *for this purpose*', and the sloppiness of 'attribution judged generically'.

3. *The ultimate test: thinking clearly about the ex turpi causa defence and its application to companies*

Finally the *ex turpi* rule. This provides that courts will not enforce illegal contracts, nor assist claimants to recover benefits from their own wrongdoing.[32]

In *Stone & Rolls*, the House of Lords denied the company's claim against its auditors, but confined its conclusion to one man companies.[33] If there had been innocent directors or shareholders, then the majority suggested that the company <u>would</u> have been able to sue, and *ex turpi* would not have prevented that.

This instinct is right, I suggest. And indeed the one man finding is wrong. The very premise of the *ex turpi* rule, as accepted by the House of Lords, indicates why.

The explanation is simple. Take two steps back. There is a difference between the two limbs of the *ex turpi* rule, and the difference turns out to be crucial in the context of companies.[34] While the court will *never* enforce an illegal contract to which the company is a party,[35] it will only prevent claimants from recovering the benefits of their wrongdoing when the unlawful conduct is that of the claimant (it is his *own*), and is 'not conduct for which he is vicariously liable[36] or which is otherwise attributed to him under principles of the law of agency'. That was the concession made by counsel for the auditors, Mr Sumption QC (as he then was), and it would hardly have been made lightly.[37] It was a proper concession, in complete accord with the public policy supporting the rule.

[32] See especially *Stone & Rolls* (n 3), [26].
[33] ibid, [63] (Lord Phillips), [192] (Lord Walker), [203] (Lord Brown), [241] (Lord Mance (dissenting), suggesting *ex turpi* would only defeat a solvent one-man company, [120]-[121] (Lord Scott (also dissenting), seemingly suggesting *ex turpi* was never needed or appropriate to deny a company's claim).
[34] ibid, at [24], [26]-[28].
[35] And *Ashmore, Benson Pease & Co Ltd v AV Dawson Ltd* [1973] 1 WLR 828 (CA) may be seen as such a case, although it needs to be treated with a great deal of caution, since not one of the three judgments makes *any* reference to the fact that the contracting parties were companies. The only concern was with what the individual employees or managers knew, and the outcome was treated as being the same as if the contract had been between those individuals. If the case stands for anything, it might be that a contract which is illegal in its performance, and known to be such by both sides, will also not be enforced, even though the same contract might have been carried out perfectly legally.
[36] This point is now open after *Bilta v Nazir* (n 5), [29] (Lord Neuberger), [48] and [50] (Lord Mance), and contrast [80] (Lord Sumption) seeing *Stone & Rolls* as confining the defence to instances where the company is primarily liable.
[37] *Stone & Rolls* (n 3), [8]. As noted earlier, Watts (n 16), 17, says this is 'simply wrong', but the authorities cited do not seem to support the assertion, and it is doubted.

Consider cases involving individuals rather than companies. With individuals, the real import of the personal nexus requirement is plain: the court will not assist an individual to recover benefits from her *own* wrongdoing, but it will not deny her that right when *another individual* is the source of the allegation that she is a wrongdoer. In those circumstances she is permitted to advance her claim to recover benefits, or compensation or an indemnity. Whatever the scope of the *ex turpi* rule, its public policy reasons are not called into play in circumstances where X is only a wrongdoer because of the acts of others. With individuals, the only way that X can be treated as a wrongdoer because of the acts of others is via agency or vicarious liability. When these rules apply, the result is that X will have to bear legal liability to others for those wrongful acts, regarded as her acts or her liability, and made so by the rules of agency or vicarious liability: ie she can be sued by third parties. *But* she can in turn sue others, and her claim will not be barred by *ex turpi* rule. She is of course most likely to sue those who actions rendered her a wrongdoer, but she may also sue others who are more remotely involved, for contribution, etc.

The impact of this approach on companies is obvious. A company cannot do <u>anything</u> unless it is through the act of another individual. That is the essence of *Meridian*. Unlike an individual, a company cannot act in its own person, for it has no person in that sense; it must of necessity act by its agents.[38] If the second limb of the *ex turpi* rule does not apply where the company is merely liable vicariously or via the agency rules, then this limb <u>never</u> applies to companies. This is the radical consequence of the personal nexus test.

But even if the consequence is radical, is it unacceptable? Its result is that companies made liable by attribution can sue their badly performing directors and auditors, and any third parties associated with these wrongs. But the company does not get off scott free. Attribution means the company itself can sued. And as Lord Scott noted in his dissent in *Stone & Rolls*, this makes the *ex turpi* rule unnecessary in this particular corporate context.[39] I might add that of course a rule of public policy should not be used when it is unnecessary.

3. Summary: key macro concepts in corporate attribution

This brings to a close discussion of the big picture issues in corporate attribution. Before we move on to the little picture issues, I should summarise the points made so far. They are these.

[38] *O'Brien v Dawson* [1942] HCA 8, (1942) 66 CLR 18, 32 (Starke J), cited by Edelman J in *Perpetual Trustee Company Ltd v Burniston (No 2)* 2012 WASC 383 (WASC), [210]. Also see *Ferguson v Wilson* (1866) LR 2 Ch App 77, 89 (Sir H M Cairns LJ).
[39] *Stone & Rolls* (n 3) [120]-[121].

My headline: the key insight from *Meridian Global* is Lord Hoffmann's question: 'Whose act (or knowledge, or state of mind) was *for this purpose* intended to count as the act etc. of the company?'[40]

Analytical rigour in answering this question demands that courts pay due regard to the separate personality of the company and the detailed workings of the machinery of corporate attribution.

In doing that, and using *Stone & Rolls* as a platform for discussion, three specific claims were advanced.

First, there is no necessary hierarchy between the different rules of corporate attribution. All are directed at answering the attribution question.

Secondly, the *Hampshire Land* principle should be abandoned as a distracting and not particularly useful label for a simple principle of corporate attribution which applies when wrongdoers seek to shed liability by claiming that *their own* acts count as corporate acts so as to give them a defence.

Thirdly, and perhaps most dramatically, the *ex turpi* defence, insofar as it prevents claimants from suing to recover benefits from their own personal wrongdoing, will never apply to companies.

Turn now from those macro issues to the detailed workings of the machinery of corporate attribution. These are the micro issues of corporate attribution.

C. Infrastructure issues – micro problems in corporate attribution

This is a move from the structure and general machinery of corporate attribution to its nuts and bolts. In corporate contracting, that typically means a move to the general rules of agency.

The practical problem I want to address is simple but controversial: what are the limits to an agent's actual authority?

In answering that question I suggest the courts have failed to distinguish between questions which are appropriate as between principal and agent and questions which are appropriate as between principal and third party. They have also fallen into the trap of assuming that because something should not be done, then the doing of it should have no effect.

But to the problem for this section.

[40] *Meridian Global* (n 2), 507. The crucial importance of context in answering attribution questions is now being properly recognised: see, eg, *Moulin Global* (n 1), [41] (Lord Walker); *Bilta v Nazir* (n 5), [41] (Lord Mance), [191] (Lords Toulson and Hodge); P Watts and FMB Reynolds, *Bowstead & Reynolds on Agency* (20th edn, Sweet & Maxwell, 2014), [8-213].

1. The boundary between actual authority and ostensible authority

1. The problem

The question is disarmingly simple. Does a corporate agent have *actual* authority to act contrary to the company's interests? Take a simple example. If an agent has authority to transact publishing deals on behalf of the company up to a value of $1m, and purports to bind the company to a publishing deal which is worth only $0.5m but is not in the company's interests, should the outcome as between the company and the third party be analysed on the basis of actual authority or only on the basis of ostensible authority, there being no actual authority to act contrary to the company's interests?

Modern English orthodoxy suggests the latter. It holds to the view that a corporate agent has *no* actual authority to act contrary to the company's interests. A third party wanting to prove a contract with the company in those circumstances must do so on ostensible authority grounds. That calls into play the rules so clearly set out by Diplock LJ in *Freeman & Lockyer v Buckhurst Park*.[41] If that route through ostensible authority is not available, then the contract will be void since the agent has no actual authority. In practical terms, *if* there has been a valid representation, and *if* the third party's reliance is bona fide and reasonable, then the third party will have her contract. Otherwise she will not.[42] <u>This is the 'no actual authority' approach.</u>

By contrast, an analysis founded on actual authority would approach the problem by holding the transaction to be within the *scope* of the agent's actual authority, but in breach of the agent's duty to the company. The agent would be *abusing* her authority, but not *exceeding* it. The contract with the third party would therefore be binding on the company, being within the scope of the actual authority of the agent, but voidable by the company as against third parties who are not bona fide purchasers for value without notice of the company's equitable rights. On this analysis, the deal with the innocent third party is prima facie binding, and the company's remedies are exclusively against the defaulting agent unless the third party is complicit in some way in the agent's wrong. <u>This is the 'within scope, but in abuse of authority' analysis.</u>

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[41] *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* (1964) 2 QB 480 (CA), 503-506, especially the familiar summary at 506.

[42] Unless the company ratifies the contract, and who has the power to do that, and in what circumstances, can be a nice question: S Worthington, 'Corporate Governance: Remedying and Ratifying Directors' Breaches' (2000) 116 LQR 638. Clearly ratification could and would not be contemplated unless the market had turned so that the initial breach was no longer so. That then perhaps begs other questions – was the agent simply prescient?

Put like this, it is evident that the practical outcome is often the same on either analysis, although the onus of proof lies in different places and that can be important in practice.

Which is the better analysis?

I suggest the 'within scope, but in abuse of authority' analysis is preferable. Nevertheless, I advance this view tentatively. It runs counter to the current analysis in *Bowstead & Reynolds on Agency*[43] and to a good number of respectable cases in England and Australia.[44] In its defence, however, the earlier editions of *Bowstead* adopted this alternative view, and on close reading some of the leading cases are more ambivalent than their isolated extracts might suggest.

I start with an outline of the support for both views.

2. The orthodox view vs. the preferred view: lining up support

The orthodox view – 'no actual authority'

Mr J Lightman is credited with leading the UK charge to adopt the modern orthodoxy. In *Hopkins v TL Dallas Group Ltd,* he endorsed the proposition in the 17th edn of *Bowstead & Reynolds*, to the effect that:[45]

> "the agent is simply not authorised to act contrary to his principal's interests: and hence … an act contrary to those interests is outside his actual authority. The transaction is therefore void unless the third party can rely on the doctrine of apparent authority" (Bowstead para 8–218).

[43] Watts and Reynolds (n 40), Article 23: 'Unless otherwise agreed, authority to act as agent includes only authority to act for the benefit of the principal'.

[44] *Lysaght Bros & Co Ltd v Falk* [1905] 2 CLR 421 (HCA), 439 (O'Connor J), although also noting that the act was void only if not a dealing with innocent parties, which is typically the 'voidable' test; *Hopkins v TL Dallas Group Ltd* [2005] 1 BCLC 543, [87]-[91] (Lightman J); *AL Underwood Ltd v Bank of Liverpool and Martins* [1924] 1 KB 775 (CA), 791-2 (Scrutton LJ); *Heinl v Jyske Bank (Gibraltar) Ltd* [1999] 1 Lloyd's Rep Bank 511; *Parti v Al Sabah* [2007] EWHC 1869 (Ch), [45]-[46] and [49]-[50] (Peter Smith J); *Rubin v Cobalt Pictures Limited* [2010] EWHC 2240 (Ch), [53]-[54] (Snowden J); *GHLM Trading Limited v Maroo* [2012] EWHC 61 (Ch), [170]-[171] (Newey J); *Bass Jarrington Limited v The Royal Bank of Scotland plc, HQ Chester Limited* unreported 2014 WL 6633457, 7 November 2014, [24]. See too the important analysis in *Akai Holdings* (n 6), [77] (Lord Neuberger NPJ). Also see R Nolan, 'Controlling Fiduciary Power' (2009) 68 CLJ 293, 296; M Conaglen and R Nolan, 'Contracts and Knowing Receipt: Principles and Application' (2013) 129 LQR 359; R Nolan and M Conaglen, 'Good faith: what does it mean for fiduciaries and what does it tell us about them?' in E Bant and M Harding (eds), *Exploring Private Law* (CUP, 2010).

[45] *Hopkins v T L Dallas Group Limited* [2004] EWHC 1379 (Ch), [88], and see generally [87]-[91]. The quotation from Bowstead is preceded by this: 'The grant of actual authority to an agent will not normally include authority to act for the agent's benefit rather than that of his principal and therefore, without agreement, the scope of actual authority will not include this. The grant of actual authority should be implied as being subject to a condition that it is to be exercised honestly and on behalf of the principal: *Lysaght Bros & Co Ltd v. Falk* (1905) 2 CLR 421 . It follows that, if an act is carried out by an agent which is not in the interests of his principal … then the act will not be within the scope of the express or implied grant of actual authority. As a result there cannot be actual authority: [then citing Bowstead]' The language of 'scope', which must in this context mean 'aim or purpose' rather than its more natural meaning of 'opportunity for operation', is apt to be misunderstood.

This is the approach which now holds sway in England, but one of the clearest illustrations of its operation comes from Hong Kong.

In *The Thai Bank v Akai Holdings Ltd*,[46] Mr Ting, the chief executive and executive chairman of Akai, entered into a US$50m pledge and loan agreement with the Thai Bank. On its face this agreement was patently damaging to Akai – it was not in the company's interests – and it was to the benefit of both the Bank and a second company under the direction of Mr Ting. Lord Neuberger NPJ delivered the only reasoned judgment, basing his analysis entirely on this orthodox 'no actual authority' view, and concluding that the impugned contract was void, the CEO, as agent, having no actual or ostensible authority to do the deal.

The alternative/preferred view – within the scope of actual authority, but in abuse of it

The alternative view, the 'within scope but in abuse' view, is best expressed by Millett J (as he then was) in *Macmillan Inc v Bishopgate Trust (No 3)* [1995]:[47]

> English law … recognises the distinction between want of authority and abuse of authority. … In particular …under English law:
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> > "an act of an agent within the scope of his actual or apparent authority does not cease to bind his principal merely because the agent was acting fraudulently and in furtherance of his own interests:" see *Bowstead on Agency,* 15th ed. (1985), p. 279, art. 74.
>
> The fact that this rule applies to actual authority as well as to apparent authority, and that it may therefore be relied upon by a third party to whom the authority of the agent has not been held out by the principal, was laid down in England …[in] *Hambro v.Burnand* [1904] 2 K.B. 10

This view is expressed with Lord Millett's usual clarity and precision. Despite that, both this case and *Hambro v Burnand* are now given short shrift by Bowstead & Reynolds as impossible to accept unless limited to ostensible authority.[48] But neither case can be so easily dismissed: Millett J could

[46] *Akai Holdings* (n 6).
[47] *Macmillan Inc v Bishopsgate Investment Trust Plc (No 3)* [1995] 1 WLR 978 (Ch), 984.
[48] *Hopkins v T L Dallas Group Limited* (n 45), [89] (Lightman J) making reference to *Macmillan* only; Watts and Reynolds (n 40), [3-009], limiting both cases.

not have been more explicit; and even on the most sceptical reading, *Hambro* is clearly not concerned with ostensible authority.[49]

Other judges have also taken Lord Millett's line.[50] I mention in particular *Grimaldi v Chameleon Mining NL (No 2)*,[51] where the relevant law was laid out in plain words in line with Lord Millett's approach.

The list of authorities could be extended for both camps, but the battle is not won by counting the strength of the forces on either side. The real question is which analysis is more persuasive?

3. The problems with the orthodox approach

The orthodox (and currently favoured) 'no actual authority' approach suffers from a number of weaknesses. I think there are four particularly glaring problems.

First, the orthodox approach muddles two quite different contexts. It accurately describes the agent's authority, or what the agent is allowed to do, as being a matter of contract or consent between principal and agent. It adds the uncontroversial rider that no principal consents to its agent acting contrary to the principal's interests. Indeed, there are typically other limits, both explicit and implicit. As *between principal and agent*, the agent will be in breach of duty to the principal if any of these lines are crossed; appropriate remedies will follow.

But as *between the company and its outsiders*, the question is different. It is 'whose act will count as the act of the company for the purpose of making this contract?' The answer is surely not, no one whose acts are in breach of duty to the company. The acts of agents count as the acts of the company even though the agents are doing what the company,[52] or the general law,[53] has prohibited them from doing.

Going back to my earlier example, if the contact is a publishing contract for less than $1.0m, then the nominated agent *is* the person whose acts count as the acts of the company, regardless of whether the contract turns out to be against the company's interests, motivated by improper purposes, negligent or disloyal.[54]

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[49] *Hambro v Burnand* 2 KB 10 (CA), especially 19-20 (Lord Collins MR); 23-25 (Romer LJ); and 26 (Mathew LJ).
[50] Eg *Clark v Cutland* [2003] EWCA Civ 810, [2004] 1 WLR 783 (CA), [26]-[27] (Arden LJ); *Robins v Incentive Dynamics Pty Ltd (in liq)* (2003) 175 FLR 286 (NSWCA), [82] (Giles JA) and [65]-[67] and [73]-[74] (Mason P).
[51] *Grimaldi v Chameleon Mining NL (No 2)* [2012] FCAFC 6 (FCA), [254], and see generally [276]-[281].
[52] Eg, *Safeway Stores Ltd v Twigger* (n 4).
[53] Eg, *Stone & Rolls* (n 3), so far as its liability to the defrauded banks was concerned.
[54] And unless the third party is implicated in the breach, these are matters exclusively between the principal and the agent.

By contrast, if the purported contract is a canal-building contract, then this is *not* the person whose acts count as the acts of the company for the purpose of contracting.

The confusion arises from assuming that conclusions which apply in the principal/agent context will also apply in the principal/third party context.

Secondly, the way in which the orthodox approach then relies on ostensible authority does not make sense. The detailed analytical steps are typically ignored,[55] but notice what is required. The approach set out in *Freeman & Lockyer* remains the law. On that basis, a contract founded on estoppel against the company must be based on a representation to the third party of the authority of the 'unauthorised' agent, and that representation must be made by someone with *actual* authority to make the representation.[56] That is typically but not inevitably grounded in the fact that the authorised representor is *actually* authorised to do the deal in question. Just stating this requirement immediately reveals the nonsense which must then go on. According to the orthodox view, *no* corporate agent has actual authority to act contrary to the interests of the company. It follows that there is no one who can make the required representation on which ostensible authority can then be built.

Thirdly, the orthodox analysis cannot explain a large number of key cases. According to the orthodox view, if a contract is not for the benefit of the company and the third party is aware of that fact, then the contract is void. But in just this situation contracts are typically held to be voidable, not void.[57] This is true of self-dealing transactions,[58] contracts made for improper purposes,[59] and contracts involving bribed agents.[60] These contracts are all voidable. Have the judges in all these cases simply missed a trick?

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[55] *Akai Holdings* (n 6) is a rare exception.

[56] *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* (n 41), 504 (Diplock LJ). See Lord Neuberger NPJ struggling with this issue (in the context of a discussion of the likely practical impossibility of self-authorising agents) in *Akai Holdings* (n 6), [68], [70], [71].

[57] This is especially evident in older cases dealing with promoters: eg, *Erlanger v New Sombrero Phosphate Co* (1878) 3 App Cas 1218 (HL); *Cape Breton Co, Re* (1887) 12 App Cas 652 (HL).

[58] *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549, 585-6 (Lord Denning MR), 589-591 (Lord Wilberforce) and 594 (Lord Pearson); *Guinness plc v Saunders* [1990] 2 AC 663, 692-3 (Lord Templeman). Also see Watts and Reynolds (n 40), [6-068] and [8-220]. But see D O'Sullivan, SB Elliott and R Zakrzewski, *The Law of Rescission* (OUP, 2008), [1.65]-[1.69].

[59] *Hogg v Cramphorn* [1967] Ch 254; *Bamford v Bamford* [1970] Ch 212 (CA); *Richard Brady Franks v Price* [1937] HCA 42; *Harlowe's Nominees Pty Ltd v Woodside (Lakes Entrance) Oil Company NL* [1968] HCA 37, (1968) 121 CLR 483, 500 (Barwick CJ, McTiernan and Kitto JJ); *Winthrop Investments Ltd v Winns* [1975] 2 NSWLR 666, 697; *Whitehouse v Carlton Hotel Pty Ltd* [1987] HCA 11, (1987) 162 CLR 285.

[60] *Parker v McKenna* (1874) LR 10 Ch App 96, 118, 124-125 (James LJ), 118 (Lord Cairns LC); *Panama and South Pacific Telegraph Co v India Rubber, Gutta Percha, and Telegraph Works Co* (1875) LR 10 Ch App 515, 528-9; *Armagas Ltd v Mundogas SA* [1986] AC 717, 742-743; *Shipway v Broadwood* [1899] 1 QB 369 (CA), 373 (Chitty LJ); *Logicrose Ltd v*

Fourthly, the test is difficult to apply. Should a transaction be judged 'not in the interests of the company' if that is what the agent believes, or only if that is what a reasonable person would believe? The former leaves too much in the agent's hands, which seems odd with fiduciaries. The latter requires third parties to be unduly wary of attractive bargains. That too seems inappropriate.

In short, the orthodox analysis, despite its popularity, does not really seem tenable. But is the 'actual authority' approach any better?

4. The arguments favouring the actual authority approach

The approach based on 'within scope but in abuse' seems to meet these various criticisms without attracting more of its own.

First, it does not muddle contexts. It separates principal/ agent and principal / third party contexts.

Secondly, in the principal/third party context, the analysis starts with the appropriate question: 'Whose acts will count as the acts of the company in this contractual dealing with the third party?'.

Thirdly, it deals with ostensible authority properly. Ostensible authority is relevant only when the deal is outside the scope of the agent's authority. Then the company can say the purported deal is void; no one whose acts count as the acts of the company has engaged with the third party. But if the company has itself (through its properly authorised agents) represented that the agent *does* have the necessary authority, then the company will be estopped from denying that fact as against any third parties who have reasonably relied on its truth.[61]

Fourthly, the required analysis is quite different if the purported deal is within the scope of the agent's authority, but in abuse of it. Take the contracts with the banks in *Stone & Rolls* and *Akai*: both were entered into by CEOs, and both were contrary to the interests of their respective companies. An analysis based on 'scope of actual authority' would simply hold that in both cases the agents had acted within the scope of their authority, but had abused it. As a consequence, the companies in both instances would have had remedies against their defaulting agents, and third parties who knew the deal was in breach of duty would take their contractual benefits subject to the company's equities – ie the contract would be voidable. That analysis would have delivered the benefit of the contract to the banks in *Stone & Rolls* but not in *Akai*. Moreover, it would require precisely the same investigation of the third parties as took place in *Akai* and would deliver in

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Southend United Football Club Ltd [1988] 1 WLR 1256, 1260-1261, and 1262 (Millett J); *Wilson v Hurstanger Ltd* [2007] EWCA Civ 299, [39]; *Tigris International NV v China Southern Airlines Company* [2014] EWCA Civ 1649, [143].

[61] *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* (n 41).

practical terms precisely the same remedy. But it would not require the difficult and seemingly unnecessary loop required to dismiss actual authority and somehow manage to find ostensible authority on the orthodox model. Lord Neuberger NPJ in *Akai* clearly found that added loop analytically testing.[62]

Finally, the 'actual authority' approach simplifies the legal analysis. The only necessary distinction is between *scope* and *abuse*. That is a line which is very easy to draw.

5. Conclusion

That is all I want to say about the problem of actual authority. My conclusion may seem odd. It seems, rather perversely, and reversing the current Bowstead and Reynolds assertion, to insist that an agent may indeed have actual authority to act contrary to the company's interests.[63] But that is not quite right. It muddles contexts. Just because something *should not be done* (as between principal and agent), it does not follow that the doing of it *should have no effect* (as between principal and third party).[64] This slippage is fatal to clear and defensible legal analysis.

D. Conclusion

Now I have reached my conclusion. This lecture set out to explore some of the current problems in the law of corporate attribution and agency in England.

In doing that I have advanced some propositions which may seem controversial. You may disagree with the detail, but I hope you will agree that a clear understanding of the relevant legal principles is imperative. In applying these principles, the various difficult questions must addressed rigorously.

If that is done, then all will be well.

Thank you for inviting me here tonight and for listening so attentively. I started with an indication that tonight I was mostly repeating what I thought I had been taught at UQ. That was not by way of trying to shift any blame. Brisbane is where I first discovered my passion for the law. In particular,

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[62] *Akai Holdings* (n 6), [68], [70], [71].

[63] Ie the agent may well be is acting within the scope of his authority, even though he is acting in abuse of it.

[64] Making the same point, see *In re Halt Garage (1964) Ltd.* [1982] 3 All ER 1016, 1029-1030 (Oliver J). The point has also been roundly addressed in the analogous context of limitations on corporate capacity: see *Charterbridge Corporation Ltd v Lloyds Bank Ltd* [1970] Ch 62, 69 (Pennycuick J); *Rolled Steel Products (Holdings) Ltd v British Steel Corporation* [1986] Ch 246 (CA).

I’ve always valued the intellectual excitement and analytical rigour it showed me. If I’ve lost some of the shine, then clearly I’ve been away far too long.

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