New Zealand Company Contracting: The Reform of Reasonable Reliance on Apparent Authority

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In Bishop Warden Property Holdings Ltd v Autumn Tree Ltd*, the Court of Appeal acknowledged the proviso to s 18(1) of the Companies Act 1993. The Court endorsed the position that its constructive knowledge feature was only relevant to company insiders or those with an ongoing relationship to the company. The Court also suggested that constructive knowledge may still be relevant to an initial assessment of whether an arm's length third party could establish apparent authority to bind a company. This article argues that the Court of Appeal was correct on this first point. However, the second assertion is irreconcilable with s 18(1) and the purposes of its introduction. The better view is that the proviso has statutorily supplanted reasonable reliance as a feature of common law apparent authority. This original requirement was predominantly a social or normative question marking the balance of fairness between parties to a contract. Parliament shifted that balance in 1985, amid a period of heightened deregulation and reform, in favour of contracting third parties.*

I INTRODUCTION

MJ Trebilcock, writing in 1963, argued that cl 142 of the Draft Companies Code for Ghana "would achieve little that the present law … does not already achieve".[1] Additionally, the provision would:[2]

> … carry the disadvantage … [of] creat[ing] a whole new body of rules governing company contracts, which, because of their generality and indeed novelty, might well in practice give rise to almost as many problems as they solve.

The common law principles of company contracting, subtly and gradually refined, were best left untouched. Nevertheless, cl 142 found favour in the Commonwealth. The clause set out presumptions of regularity for third

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1 MJ Trebilcock "Company Contracts" (1963) 2 Adel L Rev 310 at 334.

2 At 334.

parties dealing with companies, notably codifying and extending the rule in *Royal British Bank v Turquand*.[3] The clause set down a principle of agency law that officers and agents of a company could be assumed to have the customary powers and duties of a person in that position.[4] Further, the clause was subject to a proviso that a third party could not rely on the provision where they had actual knowledge, or constructive knowledge "having regard to his position with or relationship to the company".[5] In New Zealand, cl 142 ultimately became s 18(1) of the Companies Act 1993 (Companies Act). Trebilcock's forewarning that the generality and novelty of the provision would give rise to problems proved accurate. Judicial interpretations of the s 18(1) proviso and its Australian equivalent have been wide-ranging. In *Bishop Warden Property Holdings Ltd v Autumn Tree Ltd*, the Court of Appeal helpfully summarised the law of apparent authority as it pertains to New Zealand companies.[6] However, the Court's analysis of the proviso's intended relationship to the ordinary limbs of apparent authority presents several issues.

This article argues that the s 18(1) proviso has statutorily supplanted reasonable reliance as a feature of common law apparent authority. In support of this argument, close attention is given to the section's construction and the historical context of its introduction. Part II summarises the development of company contracting at common law. Part III outlines the interpretative issues raised in the *Autumn Tree* decision. Part IV charts the competing views of the s 18(1) proviso and the extent to which the statutory wording alters the common law position. Part V examines s 18(1) and its purpose. Finally, Part VI looks at the wider implications of the adopted interpretation — particularly in the areas of agent dishonesty, breaches of fiduciary duties and guarantees.

II THE FOUNDATIONAL PRINCIPLES OF COMPANY CONTRACTING

Section 18 of the Companies Act reflects the common law and "cannot properly be understood without reference to it".[7] The development of company contracting principles necessarily informs the section's intended effect.

3 *Royal British Bank v Turquand* (1855) 5 El & Bl 248, 119 ER 474 (QB).

4 LCB Gower *Final Report of the Commission of Enquiry into The Working and Administration of the Present Company Law of Ghana* (Government Printer, Accra, 1961) at 109.

5 At 109.

6 *Bishop Warden Property Holdings Ltd v Autumn Tree Ltd* [2018] NZCA 285, [2018] 3 NZLR 809.

7 Peter Watts, Neil Campbell and Christopher Hare *Company Law in New Zealand* (2nd ed, LexisNexis, Wellington, 2016) at 302.

Corporate Legal Personality

Companies have legal personalities.[8] This means the law treats a company as a legal person "capable of enjoying most of the rights and bearing most of the duties that can be enjoyed or borne by a natural legal person".[9] Corporate personality presents a quandary: how does this incorporeal "person" enter into contractual relations with others? Some suggest that companies can directly contract without intermediaries because the board of directors can pass resolutions as an organ of the company.[10] "On this view", Professor Peter Watts QC notes, "only delegates *below* the board are agents".[11] However, Watts argues the "better" and more widely accepted view is that companies can only contract through agents and the principles of agency.[12]

Principles of Agency: Actual and Apparent Authority

A company, as principal to a contract, is bound by the actions of an agent if there is sufficient evidence of assent to the agent's actions, or if the principal has conducted itself in a way that has led a third party to reasonably believe that it has so assented.[13] Where the former condition is established, the agent has *actual* authority to act. Where the latter condition is established, the agent has *apparent* or *ostensible* authority.[14]

An agent's actual or apparent authority can be customary or non-customary (also referred to, respectively, as usual or unusual). Customary authority is concerned with "establishing the scope of authority that an agent of a *particular kind*, such as a director, would be expected to have, looking at industry norms".[15] Non-customary authority is concerned with "non-standard conferral[s] of authority" based on particular factual indications.[16] This might occur, for example, when a company continues to acquiesce to the actions of an agent exceeding the bounds of his or her actual authority.[17]

Diplock LJ's judgment in *Freeman & Lockyer (A Firm) v Buckhurst Park Properties (Mangal) Ltd* is recognised for its conceptual clarity on these principles:[18]

> An "actual" authority is a legal relationship between principal and agent created by a consensual agreement to which they alone are parties. Its

8 Companies Act 1993, s 15.
9 Watts, Campbell and Hare, above n 7, at 23.
10 At 304.
11 At 304 (emphasis added).
12 At 304.
13 At 307.
14 At 307.
15 At 307 (emphasis added).
16 At 307.
17 See *Investment Research Unit Ltd v Rada Corp Ltd* (1988) 4 NZCLC 64,547 (HC).
18 *Freeman & Lockyer (A Firm) v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 (CA) at 502–503 (emphasis added).

> scope is to be ascertained by applying *ordinary principles of construction of contracts*, including any proper implications from the express words used, the usages of the trade, or the course of business between the parties.
>
> …
>
> An "apparent" or "ostensible" authority, on the other hand, is a legal relationship between the principal and the contractor created by a representation… [which], when acted upon by the contractor by entering into a contract with the agent, *operates as an estoppel*, preventing the principal from asserting that he is not bound by the contract.

These statements indicate that actual and apparent authority may have originated from differing bodies of law. While actual authority finds its footing in the ordinary principles of contract construction, apparent authority is based on common law estoppel and prevents a principal from denying a contract. There has, however, been debate about apparent authority's proper categorisation.[19] Some have claimed that it cannot be characterised as a genuine estoppel because the detriment incurred by the representee may be small, and the representation may be very general — such as simply putting someone in a position which carries usual authority.[20] Others have gone further, assuming that apparent authority is an extension of objective analysis of contract formation.[21] This interpretation would explain the weak requirements of representation and reliance, which are difficult to reconcile with estoppel's need for an unequivocal representation.[22] Nevertheless, the authors of *Bowstead and Reynolds on Agency* refute this conceptualisation:[23]

> This logically requires that the principal must be able, without subjecting himself to the ratification rules and their safeguards, to *sue the third party for non-performance of an executory contract*, simply because the third party could sue on it under the doctrine of apparent authority.

Therefore, the best view is that apparent authority has a grounding in common law estoppel but should be regarded as "invoking a special (and weak) type of estoppel relevant only in the agency context".[24] This view

19 See Olivia de Pont "Company Contracting: Lord Neuberger and the Deprecation of Constructive Knowledge" (2013) 19 Auckland U L Rev 171 at 190, where the author succinctly outlines these range of views.

20 Peter Watts and FMB Reynolds *Bowstead and Reynolds on Agency* (21st ed, Thomson Reuters, London, 2018) at [8-028].

21 See, for example, Ji Lian Yap "Knowing Receipt and Apparent Authority" (2011) 127 LQR 350 at 354; and Rebecca Lee and Lusina Ho "Reluctant Bedfellows: Want of Authority and Knowing Receipt" (2012) 75 MLR 91 at 93–94.

22 Watts and Reynolds, above n 20, at [8-029].

23 At [8-031] (emphasis added).

24 At [8-031].

allows for nuanced legal differentiation between apparent authority and "true estoppel situations".[25]

Nevertheless, while apparent authority is best viewed as a form of estoppel, there are similarities between the requirements for establishing a representation of authority and establishing an ordinary contract. The promisee, in using the concepts of authority to *bind* a principal to a contract, has the onus of proving actual or apparent authority.[26] This allocation of the burden follows from the convention that "the onus of proving a contract always lies on the promisee".[27] Furthermore, as in principal-to-principal contracting, the parties are judged objectively "from the position of the reasonable person, with such person's knowledge of observable facts".[28] In the law of apparent authority, and indeed in true estoppel cases, this is embodied by the principle of reasonable reliance: the court may infer from circumstances that the representee "must have been suspicious to the extent that further inquiries would have been appropriate in the context".[29]

Andrew Robertson notes that the doctrine emerged as an express requirement in mid-19th century common law estoppel cases, starting with the Court of Exchequer Chamber judgment of *Freeman v Cooke*.[30] However, the author acknowledges that the principle was "implicit in some of the earliest estoppel cases at common law and equity".[31] Indeed, Professor Francis Dawson has suggested that early cases where representations were made good resulted from the equity judges carefully defining the sort of conduct by which reliance was protectable.[32] Robertson argues that the imposition of a reasonableness standard is a limiting principle, tempering the balance of fairness between representor and representee. Accordingly, reasonable reliance is not entirely, or even predominantly, a question of fact — rather, it is a "'social question' … involv[ing] the allocation of risk and responsibility" and requiring the court to take account of community standards and norms of conduct.[33]

25 At [8-029].
26 Watts, Campbell and Hare, above n 7, at 308 citing *Lysaght Bros & Co Ltd v Falk* [1905] 2 CLR 421; *Polish Steamship Co v AJ Williams Fuels (Overseas Sales) Ltd* [1989] 1 Lloyd's Rep 511 (QB) [*The Suwalki*] at 514; and *Dent v Herbert* CA243/02, 18 June 2003 at [32].
27 At 308.
28 Watts and Reynolds, above n 20, at [8-050].
29 At [8-048]. See also *Egyptian International Foreign Trade Co v Soplex Wholesale Supplies Ltd* [1985] 2 Lloyd's Rep 36 (CA) [*The Raffaella*] at 41.
30 Andrew Robertson "Reasonable Reliance in Estoppel by Conduct" (2000) 23(2) UNSWLJ 87 at 98–99; and *Freeman v Cooke* (1848) 2 Exch 654, 154 ER 652 (Exch Ch).
31 At 98.
32 Francis Dawson "Making Representations Good" (1982) 1 Canta LR 329 at 334–335.
33 Robertson, above n 30, at 95.

The Doctrine of Constructive Notice

While not expressly required by the Companies Act,[34] most companies in New Zealand have a constitution. When adopted, a copy of a company's constitution is added to the Companies Register, which is publicly accessible.[35] Under the common law doctrine of constructive notice, a person dealing with a company could not rely on ignorance of public documents that would illustrate a corporate agent's lack of authority.[36] It was a negative rule and could not be used to attribute knowledge in a third party's favour.[37]

Over time, the doctrine came to be seen as too onerous on third parties attempting to contract with companies. Parliament introduced ss 18B and 18C (the precursors to the current ss 19 and 18 respectively) into an earlier version of the Companies Act in 1985. Their introduction was intended to reform the law. No longer was a person deemed to have notice or knowledge of the contents of a company's constitution, or any other document relating to a company, merely because it was on the Register or publicly available for inspection.[38]

The Indoor Management Rule: *Royal British Bank v Turquand*

Prior to statutory reform, the common law had fashioned its own rule to temper the harshness of the constructive notice doctrine: the *Turquand* or "indoor management" rule. This rule was a presumption that a promisee was innocent of any irregularities in a company's internal procedures.[39] While third parties could not deny having notice of public documents, this did not mean they were bound to go further and inquire into *actual* compliance with internal formalities.[40] As JS McLennan notes, to hold the opposite would "lead to an impossible situation [where] no one could safely contract with companies".[41] Nevertheless, the presumption of fact enshrined in *Turquand*'s case was rebuttable on evidence that the person dealing with the company knew the company had not complied with the particular internal formality.[42] Likewise, the company could show that circumstances

34 Companies Act, s 26.
35 Sections 32–33.
36 *Ernest v Nicholls* (1857) 6 HL Cas 401, 10 ER 1351 (HL).
37 See, for example, *Rama Corp Ltd v Proved Tin & General Investments Ltd* [1952] 2 QB 147 (QB) at 147 per Slade J.
38 Section 19.
39 *Turquand*, above n 3, as cited in JS McLennan "The Ultra Vires Doctrine and the Turquand Rule in Company Law — A Suggested Solution" (1979) 96 SALJ 329 at 345.
40 At 345.
41 At 345.
42 *Morris v Kanssen* [1946] AC 459 (HL) at 475.

surrounding the conclusion of the contract were suspicious enough to put a reasonable person on inquiry.[43]

Like apparent authority generally, there has historically been disagreement about the correct classification of the rule in *Turquand*'s case. It was initially interpreted as a special rule of company law, allowing a third party to positively bind a company if that party dealt with a person purporting to have been delegated authority and the company's articles showed that such delegation was possible.[44] Over time, a "jungle of irreconcilable decisions" formed regarding the true nature and scope of the indoor management rule.[45] Gradually, it came to be understood not as a special rule of attribution, but rather as a negative rule that came into play only when the basic requirements of estoppel had been met.[46] Diplock LJ's celebrated decision in *Freeman & Lockyer* "cut the path" to this correct conceptualisation.[47] The modern understanding is that the rule in *Turquand*'s case only addresses:[48]

> ... *procedural irregularity* and does not affect the ordinary requirement that the third party show that he dealt with someone with actual or apparent authority from the company to make the contract.

Dawson J recognised this interpretation in *Northside Developments Pty Ltd v Registrar-General*:[49]

> … the indoor management rule only has scope for operation if it can be established independently that the person purporting to represent the company had actual or ostensible authority to enter into the transaction. The rule is thus dependent upon the operation of *normal agency principles*; it operates only where on ordinary principles the person purporting to act on behalf of the company is acting within the scope of his actual or ostensible authority.

Indeed, McLennan argues the rule is "nothing more than a projection of the doctrine of ostensible authority".[50] Nonetheless, while only having a negative operation, the High Court of Australia acknowledged in *Northside* that the *Turquand* rule appears to have originated from the same body

43 At 475.
44 For example, *Re County Life Assurance Co* (1870) 5 LR Ch App 288 (CA) at 293.
45 LCB Gower and others *Gower's Principles of Modern Company Law* (4th ed, Stevens & Sons, London, 1979) at 184.
46 McLennan, above n 39, at 348.
47 Gower and others, above n 45, at 184.
48 Watts and Reynolds, above n 20, at [8-050] (emphasis added).
49 *Northside Developments Pty Ltd v Registrar-General* (1989–1990) 170 CLR 146 at 198 (emphasis added).
50 McLennan, above n 39, at 352.

underlying apparent authority — estoppel.[51] Both are subject to the condition that a third party cannot rely on the rule if put on inquiry.[52]

III *BISHOP WARDEN PROPERTY HOLDINGS LTD V AUTUMN TREE LTD*

In 2018, the Court of Appeal analysed how these foundational company contracting principles interacted with s 18(1) of the Companies Act.

Facts

Autumn Tree Ltd (Autumn Tree) was incorporated to purchase, subdivide and develop a property in Auckland's Meadowbank. One party, Junjie Zhao, owned 50 per cent of Autumn Tree's shares. Another party, Gaiyu Ma, owned 30 per cent. Xiaoyuan Niu (Tina), owned 20 per cent and was the company's sole director.[53] In July 2016, Tina entered into a written agreement with Mr Zhao in which she agreed to be a "'nominal director' … 'tak[ing] no obligations, corporate and legal affairs and irregular conduct consequences in the operation of Autumn Tree'".[54] In return, Mr Zhao agreed to pay her $20,000.[55]

In January 2017, Autumn Tree obtained a valuation of the property to arrange development finance. The loan was for around $1.6 million. The valuation accounted for the fact that resource and building consents necessary for subdivision had been granted, and construction had already been commenced on one of the lots. Each lot was valued at $2.25 million on completion, rendering their combined potential value $4.5 million.[56]

On 3 August 2017, Tina purportedly met with Ms Ma's daughter, Anna. Tina wanted to surrender her 20 per cent interest in Autumn Tree and resign as director.[57] Subsequently, Anna met with Mr Zhao who instructed Autumn Tree's accountants to remove Tina as a shareholder and director of the company, record the transfer of shares to Anna and note that Anna had become a director of Autumn Tree on the Companies Register.[58] At 11.54 am, the share transfer was registered. At 1.10 pm, Anna was registered as a new director of Autumn Tree. However, the Register did not record Tina's removal as a director until 5 August 2017 at 10.21 am.[59]

51 *Northside Developments*, above n 49, at 212.
52 At 212.
53 *Bishop Warden v Autumn Tree*, above n 6, at [2]–[3].
54 At [4].
55 At [4].
56 At [5].
57 At [6].
58 At [7].
59 At [8].

On the afternoon of 3 August 2017, Tina met with Mr Blomfield of Bishop Warden Ltd (Bishop). It was their first meeting. Tina purportedly told Mr Blomfield she would prefer to sell the Meadowbank Property rather than complete the proposed subdivision. Mr Blomfield claimed he undertook a search on the Companies Office website that showed Tina as Autumn Tree's sole director. Learning this, and having conducted a QV Online search, Mr Blomfield offered to buy the property on Bishop's behalf for $1.1 million. He argued this figure reflected the building's QV rateable value of $1.17 million as at 1 July 2017. Tina accepted this offer, signing the agreement "'as director of Autumn Tree'".[60] This agreement was unconditional, and the parties recorded a $5,000 deposit and a settlement date of 3 August 2018 (one year after signing). The following day, Bishop lodged a caveat on the property.

Procedural History

Autumn Tree applied to the High Court for removal of Bishop's caveat, arguing that the agreement was invalid and Bishop, therefore, had no caveatable interest in the property. Autumn Tree argued the agreement was invalid because Tina did not have actual or apparent authority to enter into a contract on behalf of Autumn Tree.[61]

The High Court granted the removal of the caveat. Hinton J accepted that Tina did not have actual authority because Anna had been registered as a director. The sale of the property also constituted a major transaction, requiring a special resolution of shareholders.[62] Further, there was no apparent authority to enter into the transaction because, her Honour confirmed, "one out of a board of directors has little in the way of customary authority".[63] The agreement was, therefore, invalid.[64]

Hinton J briefly discussed the proviso to s 18(1) of the Companies Act. Her Honour stated that there appeared to be a "strong case" that the proviso applied because Bishop was "well aware of sufficient suspicious circumstances" such that it ought to have known of Tina's lack of authority.[65] This was the case even though the parties had "a very brief 'relationship'" with no prior dealings.[66]

60 At [9].
61 *Autumn Tree Ltd v Bishop Warden Property Holdings Ltd* [2017] NZHC 2838, [2018] NZAR 336 at [4].
62 At [37]–[38].
63 At [60]–[62].
64 At [63]–[64].
65 At [66].
66 At [66].

The Court of Appeal's Reasoning

Bishop appealed the decision. The Court of Appeal confirmed Hinton J's approach regarding the customary authority of a single director on a multi-director board. If Tina had been held out as the sole director of Autumn Tree, s 18(1) of the Companies Act would have saved the agreement.[67] However, Autumn Tree had held out two directors at the relevant time.[68] Bishop could not rely on apparent authority.

The Court differed to Hinton J in its interpretation of the proviso to s 18(1), clarifying the scope of constructive knowledge under the provision. Noting that "the type of constructive knowledge which can preclude reliance on apparent authority … arises by virtue of the person's *position with or relationship to the company*",[69] their Honours considered that *Equiticorp Industries Group Ltd (in stat man) v The Crown (No 47)* remained a correct statement of the law.[70] In that case, Smellie J viewed "position with or relationship to" as referring to those with an "ongoing relationship" with the company.[71] In *Autumn Tree*, the Court of Appeal outlined the policy rationale underlying this interpretation:[72]

> [73] The intention of the proviso, enacted by a 1985 amendment to the Companies Act 1955, was to change the common law so that constructive knowledge of a defect would not be fatal to a third party's attempt to enforce a contract. It was considered that the interests of commerce required third parties who were not insiders to be able to rely on a company having complied with its internal requirements unless the third party had actual knowledge of the defect in question.

Despite endorsing the *Equiticorp* approach, the Court of Appeal agreed there was an argument that the circumstances of the agreement made it unreasonable for Bishop to rely on Tina being held out as an agent of the company.[73] The Court held that the sale price, which was obviously below value, was "arguably inconsistent with any apparent authority to enter into the Agreement" and this was an assessment relating to "apparent authority rather than to the proviso to s 18(1)".[74] These comments suggest that constructive knowledge may still have relevance in an arm's length commercial transaction and reasonable reliance survives in its original common law form. This interpretation is supported by their Honours'

67 *Bishop Warden v Autumn Tree*, above n 6, at [52].
68 At [68].
69 At [73] (emphasis added).
70 At [74].
71 *Equiticorp Industries Group Ltd (in stat man) v The Crown (No 47)* [1998] 2 NZLR 481 (HC) at 722–723.
72 *Bishop Warden v Autumn Tree*, above n 6 (footnotes omitted).
73 At [71].
74 At [71] (footnotes omitted).

description of reasonable reliance as a necessary element of apparent authority:[75]

> [30] Apparent authority requires that the agent be held out as having authority to enter into a transaction of the kind made, the holding out must be done by a principal or someone with actual authority, the third party must know of the principal's holding out and rely on it, and the third party's reliance must be reasonable. The onus of proof is on the third party. If there is no actual benefit to a company, it may not be reasonable to rely on any holding out or apparent authority.

The Court cited *Northside Developments* as authority for the final proposition that it may be unreasonable to rely on apparent authority if there is no actual benefit to a company. The extent to which these common law principles remain unaltered by the s 18(1) proviso is uncertain.

IV COMPETING VIEWS ON THE S 18(1) PROVISO

Section 18C, introduced in 1985, amended the Companies Act to affirm and extend *Turquand*'s indoor management rule and other presumptions of regularity in company contracting. Section 18C(1) of the 1955 Act ultimately became s 18(1) of the reformed Companies Act and remained similar in substance. Paragraphs (c) and (d) of the subsection respectively address customary and non-customary apparent authority and are subject to the knowledge standards in the s 18(1) proviso. The extent to which the proviso alters the pre-1985 position has been a point of considerable debate. The disagreement has centred around the correct interpretation of three key elements:

- Who has a "position with or relationship to" the company?
- Does knowledge one "ought to have" include, or require more than, the established common law "putting on inquiry" test?
- Is knowledge "one ought to have" relevant outside of one's "position with or relationship to" the company?

75 At [30] (footnotes omitted and emphasis added).

"Position with or Relationship to"

On its introduction in 1985, it was generally understood that the proviso to s 18C(1) was intended to reform the law in favour of third parties asserting a contract. In that year, Cynthia Hawes took the view that the wording limited the constructive knowledge element to company insiders.[76] The proviso was based on Professor Laurence Gower's Draft Companies Code for Ghana, which became the model in several Canadian provinces and the New South Wales Companies Code 1981.[77] Early Australian cases adopted a similar position that the wording "connection or relationship with" only applied to company insiders.[78]

In *Bank of New Zealand v Fiberi Pty Ltd*, Kirby P took the opposite view, asserting the equivalent Australian proviso had not altered the position at common law in any material respect:[79]

> The purpose of the subsection … is not promoted by over-defining the way in which such knowledge is received or by insisting that the knowledge may only come through certain limited relationships. The words "connection or relationship with the company" should not be taken to mean a "connection or relationship" necessarily going beyond the transaction or dealings the subject of the assumptions.

A year after the judgment, Watts argued the decision ought to be explained by the specific wording in the Australian provision — particularly because the concept of a "connection" is much broader than that of a "relationship".[80] However, Kirby P's position in *Fiberi* has had some support in New Zealand: for example, Hinton J's obiter comments in the first instance decision of *Autumn Tree*.[81] Likewise, Olivia de Pont has taken the view that the difference in the Australian provision is of little consequence because the wording in s 18(1) "does not demonstrate any clear intention to constrain the circumstances in which constructive knowledge could apply".[82] She argues constructive knowledge, as a feature of the common law, must inform any interpretation of the proviso and that there are no reasons to allow an arm's length third party to "unreasonably fail to make enquiries when put on notice".[83]

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76 Cynthia Hawes "Indoor Management and the Companies Amendment Act 1985" (1985) 2 Canta LR 343 at 348–349.

77 Peter Watts "The companies amendment Acts 1983 and 1985 — the need for further reform" in John H Farrar (ed) *Contemporary Issues in Company Law* (Commerce Clearing House, Auckland, 1987) 9 at 13; and Companies Code 1981 (NSW).

78 See generally *Lyford v Media Portfolio Ltd* (1989) 7 ACLC 271 (WASC) at 281; and *Brick and Pipe Industries Ltd v Occidental Life Nominees Pty Ltd* [1992] 2 VR 279 (SCA) at 312 and 362.

79 *Bank of New Zealand v Fiberi Pty Ltd* (1993) 14 ACSR 736 (NSWCA) at 743.

80 Peter Watts "Company Contracts and the Knowledge of Persons Dealing with Companies" [1994] CSLB 50 at 50.

81 *Bishop Warden v Autumn Tree*, above n 6, at [66].

82 de Pont, above n 19, at 195.

83 At 195–196.

A middle ground between these opposing views emerged in *Equiticorp*. As noted in Part II, Smellie J took the view that the words extended the class beyond insiders but limited it to those with an "ongoing relationship" with the company.[84] The provision did not capture third parties in arm's length transactions. His Honour canvassed a range of Australian authorities with differing approaches,[85] but ultimately endorsed Gleeson CJ's view in *Story v Advance Bank Australia Ltd* that an inside or "anterior" relationship was required.[86]

Some suggest *Equiticorp* implicitly adopts the common law approach because the Chief Justice in *Story* refused to rule out the possibility of a relationship arising from "the very dealing which is putatively affected by the irregularity".[87] With respect, this proposition cannot be supported. Gleeson CJ's phrase should not be read in isolation, but rather, in conjunction with the sentence that followed — particularly where the Chief Justice refers to an "anterior" or *prior* relationship. Additionally, Smellie J explicitly stated that he interpreted *Story* as adopting an "ongoing relationship" test.[88] His Honour amply considered Kirby P's approach and chose not to adopt it. In any event, the Court of Appeal in *Autumn Tree* understood the proviso to represent a reform of the common law such that an outsider would not lose the relevant presumption merely because there were suspicious circumstances putting them on inquiry.[89]

"Ought to Have … Knowledge"

There is disagreement about whether the proviso simply reflects the common law approach, such that circumstances putting one on inquiry meets knowledge one "ought to have". Again, Kirby P in *Fiberi* considered that similar phrasing ("ought to know") codified the common law, which had "evolved in line with ... policy considerations".[90] His Honour asserted "[i]t would take language more direct and clear than s 68A of the Code" to exclude basic common law principles.[91] New Zealand authorities have expressed similar sentiments. In *Levin Meats Ltd v Perfect Packaging Ltd*, French J considered that constructive knowledge included:[92]

84 *Equiticorp*, above n 71, at 722–723.
85 *Lyford*, above n 78; *Brick and Pipe*, above n 78; and *Fiberi*, above n 79.
86 S*tory v Advance Bank Australia Ltd* (1993) 31 NSWLR 722 (CA) at 735.
87 See Watts, Campbell and Hare, above n 7, at 351, which sets out Gleeson CJ's equivocation and then claims "[t]his view has been adopted in the only New Zealand case so far to give detailed consideration to the proviso: *Equiticorp*". See also *Story*, above n 86, at 734–735.
88 *Equiticorp*, above n 71, at 722.
89 *Bishop Warden v Autumn Tree*, above n 6, at [73].
90 *Fiberi*, above n 79, at 744.
91 At 744.
92 *Levin Meats Ltd v Perfect Packaging Ltd* (2011) 10 NZCLC 264,950 (HC) at [63].

> … wilfully and recklessly failing to make such inquiries as an honest and reasonable person would make, knowing of circumstances which would indicate the facts to an honest and reasonable person, and knowing of circumstances which would put an honest and reasonable person on inquiry.

Her Honour cited John Farrar in *Company & Securities Law in New Zealand*, who had written in support of this view.[93] Farrar argued, consistently with consensus among commentators, that courts would likely adopt the five graduated knowledge categories outlined in *Baden v Société Générale pour Favoriser le Développement du Commerce et de l'Industrie en France*.[94] While the Court of Appeal in *Autumn Tree* noted that "[t]he proviso creates two classes of knowledge which preclude reliance on s 18(1): actual knowledge and a type of constructive knowledge", the Court did not go further in clarifying what that type was.[95] Following the *Autumn Tree* decision, the High Court in *TVBI Co Ltd v World TV Ltd* restated and endorsed the view in *Levin Meats* that the proviso included a "putting on inquiry" test.[96]

Conversely, in *Equiticorp*, Smellie J maintained that the "seemingly most accepted" view is that the words "differ from the common law concept … and require something more".[97] The judgment extensively considered the proviso's constructive knowledge requirement, charting Kirby P's position and other Australian authorities. His Honour noted the Victorian Court of Appeal decision *Brick and Pipe Industries Ltd v Occidental Life Nominees Pty Ltd*, which stated that:[98]

> Although s 68A was undoubtedly inspired by the rule in *Turquand's Case* and is in a sense a codification of it, the section does not incorporate the concept of being "put on inquiry" … .

Smellie J agreed, noting that if Parliament had wanted to codify the common law position, it would have simply enacted the settled proposition from *Morris v Kanssen* that the indoor management rule could not be invoked if a person was put on inquiry.[99] As Katrina Lai argues, that test was formulated in the 19th century when the number of companies and supporting agents was far more limited.[100] The drafters of the equivalent Australian proviso "opted for an entirely new form of words rather than incorporating" that

93 At [63].
94 John Farrar and Susan Watson (eds) *Company and Securities Law in New Zealand* (2nd ed, Brookers, Wellington, 2013) at 137–138; and *Baden v Société Générale pour Favoriser le Développement du Commerce et de l'Industrie en France* [1993] 1 WLR 509 (Ch).
95 *Bishop Warden v Autumn Tree*, above n 6, at [72].
96 *TVBI Co Ltd v World TV Ltd* [2019] NZHC 246 at [187].
97 *Equiticorp*, above n 71, at 724.
98 *Brick and Pipe*, above n 78, at 359 as cited in *Equiticorp*, above n 71, at 724.
99 At 725.
100 Katrina Lai "Bank of New Zealand v Fiberi Pty Ltd" (1995) 20 MULR 252 at 257.

language, suggesting a clear intent to move away from the common law position.[101] Again, Smellie J and Lai clearly take a different view as to the proviso's intended scope.

The Relevance of Constructive Knowledge Outside of Relationship to the Company

Before any New Zealand decision gave serious consideration to the proviso, Watts wrote an article canvassing the Australian authorities. He argued that the concept of a relationship arising out of a single transaction "should be treated with some circumspection".[102] Watts acknowledged the reformatory intention behind the law, noting that both the New Zealand and Australian provisions were not intended generally to be codifications or restatements of the position at common law.[103] Therefore, he endorsed the view that constructive knowledge under the proviso was limited to company insiders.[104] However, Watts maintained that:[105]

> … knowledge of facts which suggest limits on the agent's authority may in some cases *undermine the outsider's argument that the agent had apparent authority to bind the company*. That conclusion, however, does not require the construction of the proviso adopted in *Fiberi* and *Story*.

The author then claimed it was arguable that *Fiberi* could have been better decided on the basis that the bank had not met the *initial onus* on it to show that it had dealt with someone with apparent authority, which would not require the use of the proviso. Nevertheless, Watts acknowledged the difficulty with this analysis in his later writing:[106]

> … in relation to non-customary apparent authority, it is sometimes difficult to know whether some suspicious fact known to a promisee undermines the relevant agent's apparent authority, in which case the company will defeat the promisee without needing to have recourse to the proviso to s 18, or whether that fact does not undermine the agent's ostensible authority but puts the promisee on inquiry under the proviso. This is because non-customary apparent authority is always fact specific rather than based on industry practice, and although some facts might suggest that an agent has been given abnormal powers to act for a company, others may undermine that impression or may suggest that the powers have been withdrawn.

The Court of Appeal's statements in *Autumn Tree* are consistent with Watts's early assertions. As noted, the Court agreed there was an argument

101 At 258.
102 Watts, above n 80, at 50.
103 At 50.
104 At 50.
105 At 51 (emphasis added).
106 Watts, Campbell and Hare, above n 7, at 352.

that the undervalue sale price "was arguably inconsistent with any apparent authority to enter into the Agreement" and that this was an "assessment relat[ing] to apparent authority *rather than* to the proviso to s 18(1)".[107] Their Honours then clarified that "the proviso to s 18(1) does not, of course, make mention of the *circumstances* of the transaction", but rather relates to knowledge arising by virtue of the person's position with, or relationship to, the company.[108] This clarification supports the proposition that the reasonable reliance element of the test for apparent authority has not been supplanted by the s 18(1) proviso. The argument conceptually distinguishes between two features of company contracting at common law — on one side, apparent authority as a means of binding a company, and, on the other, the presumptions of fact (such as the *Turquand*'s rule) that there are no irregularities in a company's internal management.

This understanding of constructive knowledge and its place in the company contracting analysis has been criticised. John Land mounts a clear opposition. Land maintains that "the Court of Appeal's judgment in *Autumn Tree* contains an internal inconsistency which potentially undermines the Court's approach to the proviso".[109] That inconsistency is the inclusion of reasonable reliance in the test for apparent authority while also endorsing the *Equiticorp* ongoing relationship test.[110]

Land references the Court of Appeal's endorsement of the *Equiticorp* "ongoing relationship" test, and argues that the "intended law reform would be undermined if the proviso applied where a third party had constructive knowledge of a defect arising out of just the particular transaction".[111] The reform arose from a policy position that "commercial certainty" needed to be safeguarded, and a view that the common law was unduly harsh to third parties who were not insiders.[112] While the proviso did not remove constructive knowledge as a form of knowledge that could defeat reliance on apparent authority, the draftsperson substantially "narrowed the class of people" to which it could be ascribed.[113] Therefore, Land concludes that "to establish apparent authority it is no longer necessary to show that it is 'reasonable' to rely on a holding out".[114]

Professor Susan Watson also takes this view, claiming that:[115]

107 *Bishop Warden v Autumn Tree*, above n 6, at [71] (emphasis added).
108 At [73] (emphasis added).
109 John Land "Company Contracting in New Zealand after *Autumn Tree*" (2018) 24 NZBLQ 311 at 318.
110 At 319.
111 At 318.
112 At 318.
113 At 318.
114 At 320
115 Susan Watson "What Bishop knew: *Autumn Tree*" [2018] NZLJ 307 at 331 (emphasis added).

> … due to the wording of the proviso to s 18, because there was no pre-existing relationship between Autumn Tree and Bishop, the belief on which the knowledge is based *need not have been reasonable*.

Instead, the issue should have been whether the undervalue sale price rendered Bishop wilfully blind to Tina's lack of authority.[116] Indeed, the Court of Appeal recognised in *Autumn Tree* that actual knowledge under the proviso included wilful blindness.[117] Accordingly, an independent third party entering into a transaction with certain suspicious circumstances would need to be "so suspicious"[118] that they were "sufficiently aware something [was] wrong but deliberately avoid[ed] further investigation".[119] Circumstances putting them on inquiry would not be sufficient to establish wilful blindness.

V THE INTENDED SCOPE AND PURPOSE OF S 18(1)

Despite the confused picture painted by the case law and commentary on s 18(1), it is possible to carve out an interpretation that gives due regard to company contracting's foundational principles, while respecting the reform represented by the proviso. This interpretation is supported by a close examination of the provision's construction, the purpose of its introduction and its policy objectives. It shows how the proviso has statutorily supplanted and reformed reasonable reliance as it existed at common law.

The Construction of the Section

Section 18(1)(c) and (d) address customary and non-customary apparent authority. Section 18(1) prevents a company or guarantor from asserting against a promisee that, in relation to those paragraphs, "a person held out by the company" has not been duly appointed[120] or does not have authority to exercise a customary or non-customary power.[121] Arguably, paras (c) and (d) do not come into play unless a promisee can prove the existence of a "holding out" by the company. The section does not define the circumstances in which an agent is held out. The common law must provide the answer to that question. As Part II outlined, reasonable reliance has been a well-established feature of common law apparent authority — expressly since *Freeman v Cooke* in 1848.[122] On this reading, the "held out" wording may provide a gateway through which the common law "put on inquiry" test

116 At 331.
117 *Bishop Warden v Autumn Tree*, above n 6, at [72].
118 Land, above n 109, at 318.
119 *Bishop Warden v Autumn Tree*, above n 6, at [72].
120 Only in relation to para (c), dealing with customary authority.
121 In relation to both paragraphs.
122 *Freeman v Cooke*, above n 30.

finds footing within s 18(1), independently of the proviso and its ongoing relationship test.

Indeed, it is Watts's view that the ordinary principles of agency law lie behind the provisions and "nothing in the paragraphs removes from the outside party the burden of establishing such authority".[123] While the provisions are statutory estoppels, he argues that they are structured negatively and cannot positively bind a company to illegitimate exercises of power.[124] Rather, they preclude a company from "denying various defects in the exercise of power", subject to the proviso.[125] Watts sees the scope of s 18(1) as being confined to the indoor management rule and presumptions of regularity.

This interpretation of s 18(1) overlooks one important aspect of the section: the very existence of para (d). The paragraph is aimed at non-customary representations of authority, which by definition cannot be subject to a presumption of *procedural* regularity. The distinctiveness of a non-customary holding out is that it is entirely fact-specific and not based on a customary or procedural conferral of authority. As noted in Part IV, Watts acknowledges that this creates difficulties in categorisation — a suspicious fact, he suggests, may work to undermine apparent authority *or* be relevant to the constructive knowledge limitation in the proviso.[126] A simpler explanation is that the proviso, according to the construction of s 18(1), applies equally to all limbs of the subsection. Parliament could have easily avoided the ambiguity, Watts notes, by omitting reference to para (d) from the proviso so that it read:

> Unless the person has, or ought to have, by virtue of his or her position with or relationship to the company, knowledge of the matters referred to in any of paragraphs (a), (b), (c), or (e), as the case may be.

That wording would make clear that the proviso only applied to the knowledge requirement that could rebut presumptions of fact such as the indoor management rule, and *not* the knowledge making reliance on a representation unreasonable. It should be noted, however, that when s 18C was introduced in 1985, the explanatory note to the Law Reform (Miscellaneous Amendments) Bill discussed the proviso solely in the context of s 18C(1)(a), which expressly codified the indoor management rule. Specifically, it stated:[127]

> The new section provides that no dealing or transaction between a person and a company or any person who has acquired any property rights or

123 Watts, Campbell and Hare, above n 7, at 303.
124 At 302–303.
125 At 302.
126 At 349–350.
127 Law Reform (Miscellaneous Amendments) Bill 1984 (76-1) (explanatory note) at 1 (emphasis added).

> interests from a company shall be invalid, void or unenforceable on the ground that the memorandum or articles of the company have not been complied with unless he has knowledge or by virtue of his position with or relationship to the company ought to have knowledge *that the memorandum or articles have not been complied with*.

This passage may suggest that Parliament did not consider the possibility that the proviso to s 18C would alter the standard company contracting analysis as it relates to *establishing* apparent authority.

The maintenance of that analysis had been a key feature of cl 142 of Gower's Draft Companies Code, on which s 18 is based. In the Bill, Gower does not refer to non-customary apparent authority and sets out the law in a way he believes to be "in accordance with existing case law and with normal agency principles".[128] His view is that a person may lose protection under the proviso because of his or her "relationship to the company—because he [or she] is a director or other 'insider' whereas the *Turquand* rule only protects 'outsiders'".[129] The proviso was intended to change the law to avoid the situation where "circumstances, rather than the relationship to the company, put the other party on enquiry."[130] These statements of law are consistent with the foundational principles outlined in Part II. Clearly, Gower envisaged the proviso as merely codifying and constraining the rule in *Morris v Kanssen* that constructive knowledge could rebut the presumption of procedural regularity.[131]

Similarly, Watts mounts a convincing argument that no other aspects of s 18(1)(c) and (d) alter the common law position. Although the paragraphs "do not expressly state that the holding out has to be to the person dealing with the company" (the promisee), Watts suggests that this is merely an ellipsis and "[a]ll that is missing is the phrase 'to him or her'".[132] The drafter was "simply alluding to the standard requirements before moving to the proviso where the real law reform was to be implemented".[133] In this article, it is argued that the inclusion of non-customary apparent authority illustrates the reform was intended to be extensive. The explanatory note also indicates that s 18C of the 1955 Act was intended to specify "the occasions on which the actions of an officer or agent of the company are *binding* on the company in respect of dealings with third parties".[134] This language suggests Parliament intended the proviso to have a broader scope than merely constraining the knowledge that could rebut presumptions of internal regularity.

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128 Gower, above n 4, at 111.
129 At 110.
130 At 110 (emphasis added).
131 *Morris v Kanssen*, above n 42, at 475.
132 Watts, Campbell and Hare, above n 7, at 332.
133 At 333.
134 At 1 (emphasis added).

Alternatively, if Parliament had only wanted to reform the indoor management rule and other procedural presumptions, it could have removed the provision addressing non-customary apparent authority entirely. The provision had never been a feature of Gower's Draft Code. Although not explicitly stated, this may have been the view of the Law Commission when it omitted the subsection from the draft bill annexed to the *Company Law Reform and Restatement* report in 1989.[135] The omission was carried forward in two versions of the Companies Bill (1990 and 1992),[136] but the subsection was ultimately maintained when the new Companies Act came into force in 1993. If the omission had been adopted, this would have been a clear signal from Parliament that s 18 is only directed at presumptions of regularity that a company's *internal procedures* have been complied with, and that constructive knowledge may still defeat an independent third party's reliance on apparent authority at common law. Conversely, its preservation suggests Parliament intended the proviso to go beyond the scope of the indoor management rule and those presumptions.

As a further point of interest, the Law Commission suggested in a 1990 report that the proviso had created "unwarranted uncertainty in commercial transactions"[137] and removed it from the annexed draft bill.[138] This omission was not adopted in the subsequent Companies Bills. However, the proviso was amended in the Companies Act to include commas — most significantly, after the phrase "ought to have". Parliament may have intended to reform the law further so that actual knowledge (as with constructive knowledge) is only relevant where one has a "position with or relationship to the company". This reform would, in effect, render an outsider's knowledge *completely irrelevant* under the proviso. Smellie J may have taken this view before the grammatical amendments were introduced; his Honour held in *Equiticorp* that s 18C provided protection "except where, by reason of a party's position with, or relationship to, the company, it *knows* or ought to know differently".[139]

Conversely, Watts has suggested that the correct interpretation is to "ignore the offending comma" such that actual knowledge is considered independently from one's position with or relationship to the company.[140] This interpretation maintains the understood position under the 1955 Act. This argument has strength; while the reform was intended to shift the scope of protection in favour of the outsider, it was not intended to confer a complete immunity regardless of one's state of knowledge.

135 Law Commission *Company Law Reform and Restatement* (NZLC R9, 1989) at 263.
136 Companies Bill 1990 (50-1), cl 155; and Companies Bill 1992 (50-2), cl 155.
137 Law Commission *Company Law Reform: Transition and Revision* (NZLC R16, 1990) at 32.
138 At 270.
139 *Equiticorp*, above n 71, at 727 (emphasis added).
140 Watts, Campbell and Hare, above n 7, at 350.

Lastly, it is necessary to consider the legal burden inherent in the proviso. The proviso precludes a third party from relying on any of the paragraphs in s 18(1) if that party meets the specific knowledge and relationship standards. The onus of proof is on the company to show the third party is not entitled to rely on the protections in the provision.[141] A third party will not be automatically disentitled if they have knowledge of any of the matters in s 18(1), but a court will have scope to determine whether that knowledge precludes reliance. In this way, the subsection mimics the character of rebuttable presumption — which is a feature of the *Turquand*'s rule at common law.[142] This alignment was clearly Parliament's intention; when the Law Reform (Miscellaneous Amendments) Bill was at the select committee stage, it was suggested that the introductory words to s 18C be:[143]

> … recast in line with Commonwealth precedents … to say that a company cannot assert an irregularity in the actions of its officers unless the other party knew or ought to have known of the irregularity.

As the Minister of Justice Hon Geoffrey Palmer MP noted on the Bill's second reading, the former wording had "suggested that a transaction was automatically vitiated in all cases if the party dealing with the company knew or ought to have known of an irregularity".[144]

Conversely, the burden of establishing apparent authority rests on the party seeking to *bind* the company to a contract — the third party.[145] This allocation of the burden is how, in cases such as *Mustang Marine Nominees Pty Ltd v The Vessel "Tuna to Go" (formerly named "Impact")*, a promisee could plead an affirmative defence of apparent authority and *separately* rely on s 18 of the Companies Act.[146] Nevertheless, Ellis J considered reliance on s 18 "added nothing material" to the pleading because "s 18(1)(c) and (d) 'are in large part based on common law concepts of apparent or ostensible authority'".[147] Her Honour argued that the extent of the overlap was demonstrated by the fact that both arguments failed on the same facts.[148] The significance of the proviso as a reverse onus is further diminished when one acknowledges that reasonable reliance, as a feature of both common law and equitable estoppel, does not appear to require independent proof. In the Australian case *W v G*, Hodgson J said:[149]

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141 At 348.
142 See Part II of this article.
143 (4 June 1985) 462 NZPD 4469.
144 (4 June 1985) 462 NZPD 4469.
145 Watts, Campbell and Hare, above n 7, at 308. See also the discussion in Part II of this article.
146 *Mustang Marine Nominees Pty Ltd v The Vessel "Tuna to Go" (formerly named "Impact")* [2012] NZHC 778 at [114].
147 At [116], citing French J in *Levin Meats*, above n 92, at [43].
148 At [116].
149 *W v G* (1996) 20 Fam LR 49 (NSWSC) at 66 (emphasis added).

> I do not understand it to be an independent part of the plaintiff's cause of action that she establish that her reliance was reasonable and I do not consider it necessary for me to make a *positive finding* that the plaintiff's conduct was reasonable.

Therefore, while the legal onus of establishing apparent authority is on the third party, the principal company will generally seek to adduce evidence illustrating the third party's state of knowledge. Arguably, the reverse onus simply reflects this well-understood practicality. Further, reasonable reliance is best characterised as a "social question" tempering the balance of fairness between parties in estoppel cases. As Robertson notes, it is not "a factual question" in the same way as, for example, the finding of a representation.[150] It has been acknowledged that apparent authority is a weak form of estoppel, and, as such, the bearing of "true estoppel situations" like *W v G* may be reduced.[151] However, those concerns largely centre around the aspects of representation and reliance, and not the reasonableness characteristic. The authority has relevance to this limited extent.

In any event, New Zealand decisions have tended to support Robertson and Hodgson J's view. In *TVBI v World TV*, decided after the Court of Appeal's judgment in *Autumn Tree*, Associate Judge Smith did not appear to make a distinction between reasonable reliance and the proviso — interpreting the *Levin Meats* approach in the following way:[152]

> [181] Her Honour then addressed subsections 18(1)(c) and 18(1)(d) of the Act, which together broadly encompass the common law concept of apparent, or ostensible, authority, *subject to the "reliance/reasonableness" factors which are addressed (in an arguably narrower fashion) by the proviso to s 18(1)*.

This interpretation is significant given that the Associate Judge heard arguments on the relevance of *Autumn Tree*, and counsel for the promisor company explicitly outlined the Court of Appeal's statements on reasonable reliance.[153] His Honour ultimately concluded that the company had:[154]

> … not shown an arguable case that the circumstances come within the proviso to s 18(1), or that it was not reasonable for TVBI to have relied on World TV's representations … .

It should, however, be acknowledged that TVBI had a history of dealings with World TV.[155] That being so, the case differs from *Autumn Tree* where the parties were only involved in the single transaction. The Associate

150 Robertson, above n 30, at 107.
151 Watts and Reynolds, above n 20, at [8-029].
152 *TVBI v World TV*, above n 96 (emphasis added).
153 At [152].
154 At [207].
155 At [22], [133] and [195].

Judge, therefore, did not have to directly address the issue of whether constructive knowledge would defeat an arm's length party's ability to rely on apparent authority. Nevertheless, the Court's view that the proviso addresses and narrows "reasonableness/reliance" factors is significant.

The Purpose of the Section

The Court of Appeal contends that s 18 of the Companies Act "effectively codifies the common law indoor management rule".[156] Indeed, one important aspect of the 1985 amendment to the Companies Act 1955 was to recognise and affirm the principles that had developed at common law.[157] As noted in Part IV, Kirby P in *Fiberi* interpreted the equivalent Australian provisions as merely restating the common law position — sentiments that have been generally, but not totally, dispelled in the New Zealand context by *Equiticorp*. Section 18, however, goes beyond statutory affirmation of the indoor management rule. It also, as Watts notes, "effectively codifies the principles of agency law in relation to dealings with companies".[158] David Milman and Alan Evans, writing in the same year s 18C was introduced, argued "the law could be greatly simplified by according *de jure* statutory recognition to the rules laid down" by Diplock LJ in *Freeman & Lockyer*.[159] Indeed, codification was the first step in achieving that simplification.

However, while recognition of common law principles is important and necessary to give the provision effect — its ultimate aim is reform. Watts argues that:[160]

> The relevant mischief was that the common law was thought to *suppress commerce unduly* by making all outsiders inquire whenever something suggested to a reasonable person that there may be a problem on the company's side. In other words, constructive knowledge was thought inappropriate; actual knowledge should be required for persons who were dealing at arm's length.

Giving effect to this purpose requires one to accept that the reasonableness aspect of common law apparent authority has also been reformed. Some may suggest the reform was not explicit enough, and that "more direct and clear" language is needed to "exclude the operation of such basic common law principles".[161] As Part II of this article contended, reasonableness is a foundational principle of apparent authority because the third party is attempting to bind a principal to a contract. Just as in ordinary parol

156 *Bishop Warden v Autumn Tree*, above n 6, at [32] (emphasis added).
157 Hawes, above n 76, at 343.
158 PG Watts "Company Law" [1990] NZ Recent Law Review 183 at 187.
159 David Milman and Alan Evans "Corporate Officers and the Outsider Protection Regime" (1985) 6 Co Law 68 at 76.
160 Watts, Campbell and Hare, above n 7, at 349–350 (emphasis added).
161 *Fiberi*, above n 79, at 744.

contracting, where the parties' conduct is assessed from an objective standpoint, so too must be representations of authority. "It would be surprising", the authors of *Bowstead & Reynolds on Agency* argue, "to look for reasonableness in assessing whether a representation was made in the first place, but throw that over when assessing whether there were countersigns".[162] As Watts notes, contracts can be "very enriching" to those attempting to assert them, and "correspondingly impoverishing" to an alleged promisor.[163] It is difficult to balance the fault between a principal who may have been "lax in supervising" an agent, and a promisee who may have neglected to take "the easy step" of inquiring about said agent's authority.[164]

Nevertheless, reasonableness, as a feature of both equity and the common law, is predominantly a normative and social question. As Robertson argues, reasonableness represents the allocation of risk and responsibility between the parties, to "determine the circumstances in which reliance on another person's conduct is socially acceptable".[165] Traditionally, it has been the court's role in agency cases to determine where a party would lose its ability to rely on a representation. The line was drawn where a party was "put on inquiry". Upholding the spirit of the s 18(1) proviso requires understanding that the line has been shifted. Parliament, as the representative body, is best placed to set down norms of conduct both broadly and in the context of commercial relationships. A wider reform of constructive knowledge in company contracting does not, as de Pont contends, allow parties to act "unreasonably".[166] Rather, it redefines the notion of reasonableness in company contracting to achieve a desired policy goal — that being commercial certainty in arm's length negotiations.

This interpretation accords with the historical background to the 1985 s 18C amendment. The reform occurred during a time of significant change to New Zealand corporate law, with the "Government's deregulatory drive in full swing".[167] The newly established Law Commission was tasked with a "re-examination of fundamental concepts of company law".[168] It appears the aim was to stimulate economic growth by alleviating some of the burdens on third parties in the company contracting process. As Lai argues, there are strong moral and economic reasons for this position.[169] The company — acquiring the benefit from the agent, and putting them out into the world — has a greater ability to screen for trustworthiness and oversee

162 Watts and Reynolds, above n 20, at [8-050].
163 Watts, Campbell and Hare, above n 7, at 308.
164 At 309.
165 Robertson, above n 30, at 95.
166 de Pont, above n 19, at 195.
167 Peter Fitzsimons "Australia and New Zealand on Different Corporate Paths" (1994) 8 Otago LR 267 at 279.
168 At 282.
169 Lai, above n 100, at 256.

the agent's activities.[170] The position is also more economically efficient because "the outsider might only deal with an agent on a handful of occasions", and the amount of time and expense in making inquiries into their credentials is relatively high.[171] Likewise, many transactions "involve outsiders who deal with companies from an equal or inferior bargaining position" — parties who "should not be expected to untangle the convoluted web of authority in each company".[172]

This view is not universally accepted. Watts makes the apt observation that while the principal is responsible for selection and appointment of an agent, "it is the third party and not the principal who will have had the crucial interactions with [that] agent".[173] Similarly, "the principal will normally have no reason to know of the wrongdoing" in situations where "[t]he third party may well have had an opportunity of detecting signs of untruth or overselling by the agent".[174] Watts places great emphasis on the third party's ability to police the company contracting process. However, this argument loses force in light of the proviso's relationship test. Parliament, it seems, rationally intended to distinguish between company insiders who have a greater opportunity of detecting counter-signs of authority, and outsiders who have less ability (and arguably, moral responsibility) to do so. Indeed, parliamentarians understood the provision to be a significant reallocation of commercial risk — as Douglas Kidd MP, in opposition, proved during the third reading of the Companies Bill:[175]

> I wonder what advice the Minister has had about the probability of irregularity when people are easily able to enter into obligations that are binding on a company when the formality is so minimal.

This interpretation supports the view that the statute supplants reasonable reliance at common law, such that the onus is on the promisor company to prove actual knowledge of a defect in authority (including wilful blindness), or constructive knowledge of a defect arising in an "ongoing relationship". It is difficult to see how the converse proposition would operate. Reasonable reliance has not been conceptualised as an "independent part of the plaintiff's cause of action" and does not require a positive finding of reasonableness by a judge.[176] Rather, it disentitles a party from relying on a representation of authority if circumstances put them on inquiry. With a customary role, constructive knowledge of a defect could disentitle reliance

170 At 256–257.
171 At 257.
172 At 257–258.
173 Peter Watts "Some wear and tear on *Armagas v Mundogas*: the tension between having and wanting in the law of agency" [2015] LMCLQ 36 at 38.
174 At 38.
175 (4 September 1990) 510 NZPD 4295.
176 *W v G*, above n 149, at 66.

on apparent authority *or* rebut the presumption inherent in the indoor management rule. However, with a non-customary representation, that knowledge could only be relevant to the reasonable reliance limb of apparent authority. The Court of Appeal's comments in *Autumn Tree* allow for an arm's length third party, not wilfully blind under the proviso and protected by s 18(1)(d), to nevertheless be disentitled from relying on an unusual representation. This situation would occur where the circumstances surrounding a transaction put that third party on inquiry. That interpretation effectively undermines Parliament's intent to reform the law as outlined.

However, if the reform was intended to be extensive, is it also possible that inroads have been made into the other limbs of apparent authority? Watts acknowledges arguments that, on a plain reading, s 18(1)(c) and (d) could be understood as removing the requirement that a promisee *knew* and *relied* on the representation.[177] This interpretation would be a "radical change".[178] Knowledge of the holding out and actual reliance on it are essential principles forming the foundation of the parties' legal relationship. More significantly, they are not normative issues, but threshold factual questions best left to the courts. It is not suggested, in intending to reform the balance of risk between commercial parties, that Parliament wanted to make sizeable inroads into other principles of agency law. Indeed, paras (c) and (d) explicitly reference established features like the requirement of a "holding out". Parliament has recognised where the common law is best placed to fill the gaps of the Companies Act. Likewise, the "put on inquiry" test is a feature of both reasonable reliance and the indoor management rule at common law. Recall that the High Court of Australia in *Northside Developments* suggested this was because these rules had a common "genesis" in estoppel.[179] Similarly, McLennan argued that the *Turquand*'s rule was a "projection" of apparent authority.[180] The scope of the proviso's reform, therefore, ought to extend within the bounds of these parallel principles of agency, but go no further than necessary to achieve Parliament's reformatory purpose.

VI WIDER IMPLICATIONS

This understanding of the s 18(1) proviso has wider implications in the law of agent authority — particularly in cases of dishonesty and fiduciary breaches. Routine transactions like the issuing of guarantees are also affected.

177 Watts, Campbell and Hare, above n 7, at 332.
178 At 333.
179 *Northside Developments*, above n 49, at 212.
180 McLennan, above n 39, at 352.

Dishonesty and Fiduciary Breaches

Where an agent acts dishonestly, the application of the proviso becomes even more complex. Watts argues that dishonesty is an independent ground for asserting a lack of authority, and can be asserted "even where there is no question, that the agent had authority to exercise the type of power in question".[181] None of the paragraphs in s 18(1) address this situation, and for this reason, the proviso is irrelevant.[182] This interpretation relies on authorities such as *Hopkins v TL Dallas Group Ltd* that dishonesty may remove authority at law.[183] However, it is inconsistent with several Australian cases that hold dishonesty does not remove authority at law, but instead makes the transaction voidable in equity.[184] In such cases, as Watts recognises elsewhere, the level of knowledge required by the third party promisee before the promisor can disown the contract on equitable grounds remains a "vexed question".[185] As equity acts on the conscience, it may be that the "cold calculus" of constructive knowledge is an "[in]appropriate instrument", and actual knowledge ought to be required.[186] At least in the company contracting sphere, this interpretation would accord with the reform represented by the s 18(1) proviso — that being the constraint of constructive knowledge to specified "ongoing" relationships.

Additionally, the Companies Act has codified several directors' duties in Part 8 — among them the duty of directors to act in good faith and in the best interests of the company[187] and the duty to exercise powers for proper purposes.[188] Section 18(1)(a) may afford a gateway through which the knowledge tests in the proviso apply to these fiduciary duties, rather than the position in equity. The paragraph provides that a company "may not assert" against a third party that the Act has not been complied with, subject to the proviso. In the case of dishonesty by a company's directors — representing a breach of their duty under s 131 — constructive knowledge of the impropriety would possibly defeat a third party's reliance if there were an ongoing relationship. This interpretation raises two main issues. It makes little sense to differentiate the treatment of third party knowledge in the case of director dishonesty and dishonesty by some other type of agent. Why should constructive knowledge defeat the former, and actual knowledge, the latter? Third parties are much more likely to have contact with subordinate agents than the board itself. Secondly, even if equity adopted a constructive

181 Peter Watts "Relying on the register of company directors when contracting with companies" [2018] CSLB 35 at 36.
182 At 36.
183 *Hopkins v TL Dallas Group Ltd* [2004] EWHC 1379 (Ch), [2005] 1 BCLC 543.
184 *Kinsela v Russell Kinsela Pty Ltd (in liq)* (1986) 4 NSWLR 722 (CA); and *Richard Brady Franks Ltd v Price* (1937) 58 CLR 112.
185 Peter Watts "Authority and Mismotivation" (2005) 121 LQR 4 at 8.
186 *Re Montagu's Settlement Trusts* [1987] 1 Ch 264 at 273.
187 Companies Act, s 131.
188 Section 133.

knowledge standard against third party promisees, it seems strange that an ongoing relationship would be a prerequisite in the case of directors.

In light of these issues, s 18(1)(a) cannot be interpreted as a gateway to apply the proviso to directors' fiduciary breaches. Where a transaction is voidable in equity, a consistent standard must be adopted across the wide variety of company agents. That standard should be actual knowledge of the impropriety sufficient to act on the third party's conscience.

Guarantees

In *Autumn Tree*, the Court of Appeal cited *Northside Developments* for the proposition that "[i]f there is no actual benefit to a company, it may not be reasonable to rely on any holding out or apparent authority."[189] Watts notes that the presence of a benefit is not ordinarily problematic because the delivery of money or other consideration usually suffices.[190] However, guarantees present an issue because it may "not be clear that the financial accommodation … is going to a party with any connection to the guarantor".[191] In *Northside*, it was held that the third party bank (receiving the guarantee) was put on inquiry as to a defect in the authority of a rogue director because there was no apparent connection between the subject of the loan and the guaranteeing company.[192] Watts suggests this aspect of the decision was wrongly decided because "[g]uarantee obligations are undertaken for a host of reasons" that "will not always be apparent to the outsider".[193] He preferred Mason CJ's stricter formulation that the third party will only be put on inquiry where the guarantee "appears to be unrelated to the purposes of [the guarantor's] business and from which it appears to gain no benefit".[194] Likewise, where an apparent benefit is absent, together with a *demonstrable gain* to the agent, this would clearly put the outsider on inquiry.[195]

The proviso alters the balance in favour of outside third parties. Following the *Equiticorp* approach, a third party receiving a guarantee will only be put on inquiry in the context of an ongoing relationship. For example, if a lender has dealt with the agent of a company who has previously sought a loan, and the agent offers a guarantee that does not appear to benefit the company and is unrelated to its purposes, that would disentitle the bank to the protections afforded by s 18(1)(c) and (d). However, if a lender has had no prior dealings with a company's agent, it is suggested they can rely on apparent authority unless:

189 *Bishop Warden v Autumn Tree*, above n 6, at [30].
190 Watts, Campbell and Hare, above n 7, at 330.
191 At 330.
192 *Northside Developments*, above n 49, at 146–147.
193 Watts, Campbell and Hare, above n 7, at 330.
194 At 330; and *Northside Developments*, above n 49, at 165.
195 At 331.

- Section 18(1)(c) or (d) cannot be raised because the company has not "held out" the agent as having customary or non-customary authority to provide a guarantee on its behalf;
- the lender has actual knowledge that the agent has no authority to provide a guarantee on the company's behalf; or
- the circumstances of the transaction are so suspicious that the lender is wilfully blind to the agent's lack of authority to provide the guarantee (perhaps, for instance, due to a combination of factors such as the lack of an apparent benefit, and the agent receiving a demonstrable gain).

VII CONCLUSION

Trebilcock's concerns about cl 142 of Gower's Draft Companies Code, which were eventually realised in s 18 of the Companies Act 1993, were well-founded. Specifically, the proviso to s 18 — and its interaction with foundational common law principles — has been the source of considerable academic confusion. This uncertainty reached a crescendo in the Court of Appeal decision in *Autumn Tree*, which accepted the proviso's reformatory purpose but nevertheless promoted reasonable reliance in its common law form.

The proviso distinguishes between insiders who can "police" the authority of agents, and outsiders who cannot reasonably be expected to do so. It recognises that it is unduly onerous to require an arm's length third party to examine a company's complex internal affairs. The construction of the provision supports this purpose — in particular, the existence and preservation of s 18(1)(d), which addresses non-customary apparent authority. This subsection was not featured in Gower's Draft Code and cannot properly be described as a presumption of regularity in a company's internal procedures. Further, the precise wording of the proviso ("ought to have") indicates that Parliament intended a higher threshold for third party constructive knowledge.

These aspects suggest that the proviso was intended to have a wider scope than simply codifying and constraining the knowledge that could rebut the presumption of fact represented by *Turquand*'s case. The better view is that the proviso has statutorily supplanted reasonable reliance as a feature of common law apparent authority. Reasonable reliance, as originally manifested, was predominantly a social or normative inquiry that marked the balance of fairness between parties to a contract. Parliament is the superior organ of government to determine where that balance lies. This legislative recalibration does not allow parties, as some have suggested, to act

unreasonably in contracting with companies — rather, reasonableness has been redefined to facilitate changing commercial realities.