ATTYGALLE AND ANOTHER
v.
COMMERCIAL BANK OF CEYLON LTD.

COURT OF APPEAL
TILAKAWARDANE, J. AND
UDALAGAMA, J.
CA NO. 401/94
DC COLOMBO NO. 1905/M
AUGUST 23, 2000 AND
MARCH 30, 2001

Companies Act, No. 20 of 1982 – Account opened with Bank by sole Directors – Facilities obtained by the Directors – Company not incorporated – As the company was non-existent is the contract a nullity? – Liability of the "Directors"

The plaintiff-respondent instituted action against the defendant-appellants for the recovery of a certain sum with interest. The defendant-appellants entered into an agreement with the plaintiff-respondent Bank to open an account between the plaintiff Bank and A. D. R. Products, the 1st and 2nd defendants-appellants were named as Directors and they signed as Directors. The company was never formed and the Bank was not informed of this fact; overdraft facilities have been requested for and obtained by the 1st defendant-appellant purporting to act as the Director on behalf of A. D. R. Products. It was contended that since no company was formed, the contract was a nullity and could not be enforced. The District Court held in favour of the plaintiff-respondent.

On Appeal –

Held:

(1) In pursuance of the agreement monies were released and accepted by the defendant-appellants.

(2) Sums of money released from time to time into the account was released only because the defendants-appellants had duly completed and handed over the document P1, holding out that a company was in the process of being registered.

(3) These monies had been depleted or used by the defendant-appellants, both had the sole authority and were the authorised signatories duly recognised by the Bank.

'When a person contracts on behalf of a non-existent company he was personally liable.'

Per Tilakawardane, J.

"Once monies were received there was an accountability on those actually receiving the monies to repay the same, and they could not seek protection under legal fiction to avoid payment."

(4) The rights and obligations of the parties to the contract, the Bank on the one hand and the defendant-appellants on the other cannot be transferred to a non-existent company, which in any event was not bound by the terms of the contract at the time it was made.

(5) Notwithstanding the introduction of the words "Director", "Chairman" the defendants-appellants were personally responsible and liable to pay the monies outstanding on the account.

(6) The corporate veil, which would have shielded them from liability cannot be availed of as admittedly the body corporate A. D. R. Company Ltd., was non-existent.

APPEAL from the judgment of the District Court of Colombo.

Cases referred to :

1. *Newborne v. Sensolid* – (GB) 1954 QB 45, 1953 1 ALL ER 708.
2. *Kelner v. Baxter and Others* – 1866 LR 2 Court of Common Pleas.
3. *Ex parte Hartop* –12 Ves 349 at 352.
4. *Furnivall v. Coombes* – 6 Scott NR 522.

Lalanath de Silva for defendant-appellants.

Ajantha Coorey with *Nuwan Kodikara* for plaintiff-respondent.

Cur. adv. vult.

May 23, 2001

SHIRANEE TILAKAWARDANE, J.

This appeal has been preferred by the defendant-appellants against the judgment of the Additional District Judge, Colombo, dated 31. 03. 1994, wherein he had held in favour of the plaintiff-respondent and granted the reliefs prayed for with costs.

The plaintiff Bank instituted action against the defendants who were husband and wife, jointly and severally for the recovery of a sum of Rs. 858,065/70 together with interest thereon at 30% per annum from 1st May, 1986, until full and final settlement and turnover tax on such interest at 5% and costs.

Parties admitted the Contract (P1) which was an agreement dated 22. 06. 1979 to 'comply with the rules for the time being for the conduct of such accounts' and to open an account between the plaintiff Bank and A. D. R. Products. 1st and the 2nd defendant-appellants were named and they signed as the *sole Directors* of that company. The 1st defendant-appellant admittedly signed this agreement as *'Director' on page (1) of the contract but on its reverse signed as the Chairman.* The agreement also purported to carry a certification on its reverse that a Board meeting of the Board of Directors of A. D. R. Products had been held on 20th, June, 1979, resolving : "that a Banking Account in the name of the Company be opened with the Commercial Bank of Ceylon Limited and that the said Bank be and is authorised to honour Cheques, Bills of Exchange and Promissory Notes drawn accepted or made on behalf of the company by any one of the Directors and to act on any instructions so given relating to the account, whether the account be overdrawn or not, or relating to the transactions of the Company". This Board resolution had also been

signed by the 1st defendant-appellant (as Chairman) and the 2nd defendant-respondent (as Director).

This agreement P1 had been tendered with P7 which was a letter dated 22. 06. 1979 sent by the 1st defendant-appellant signed by him as Director of A. D. R. Products. This letter was a request to open the account in the name of company A. D. R. Products, and informs the Bank that "The Company is under incorporation and no sooner we receive the Certificate of Registration and Articles of Memorandum will be forwarded to you".

Admittedly, this company was never formed (vide admissions at page 106 of the brief) and the Bank was not informed of this fact by either of the Directors/Chairman. The reasons for not forming the company were never given as neither the 1st nor the 2nd defendant-appellant had given evidence at the trial although, they had both admittedly signed the aforesaid agreement P1 with the Bank, as well as the purported resolution of the Company. (contained in the reverse of P1).

Nevertheless, by letters dated 14. 09. 1981 (P6) and 15. 07. 1983 (P5) repeated overdraft facilities have been requested for and obtained by the 1st defendant-appellant purporting to act as the Director on behalf of A. D. R. Products.

The Bank had by letter dated 24. 01. 1984 (P4) addressed to the 1st defendant-appellant in his personal capacity, informed him that the overdraft facilities of several accounts including the aforesaid account maintained in the name of A. D. R. Products were unsettled and requested him to regularise the accounts. The letter also referred to an earlier letter dated 10. 01. 1984 which had been sent to the 1st defendant-appellant on the same subject. The letter P4 sent under

registered post had been addressed to the 1st defendant-respondent in his personal capacity. He had not informed the Bank that he was not liable or that such amounts were not due from him.

Two further letters dated 17. 07. 1987 were sent under registered post to both the 1st and the 2nd defendant-respondents by the said Bank demanding settlement but neither letter had been answered nor had the Bank been informed that the company had not been registered.

The document P2, which was also admitted, was an extract of the statement of accounts relating to the account bearing No. 269 in the name of A. D. R. Products for the period 1. 10. 1981 to 27. 05. 1986. The statements revealed that the account had been overdrawn in a sum of Rs. 858,065.70 of 30. 04. 1986. The fact that this amount was outstanding to the Bank at all times and has not been settled to date was not challenged. Most importantly, the fact that these monies *had been received personally by both the 1st and 2nd defendant-appellants* had been admitted by admission (2) recorded on 16. 08. 1993. (vide page 105 of the brief).

According to the evidence of the witness for the plaintiff Bank, B. Y. Ranjith Sebasthian, monthly statements had been sent to the two defendant-appellants. (page 113 of the brief). Neither of the defendants had ever testitied that they had not received these statements nor that they had no knowledge of the monies paid out on the accounts. The evidence by this witness that neither of the two defendants had ever denied receiving these monies therefore went unchallenged (page 114).

Counsel for the defendant-appellants submitted that this witness had ". . . . plainly admitted that the 2nd defendant was not involved

at all" (page 124). This is incorrect, as the question that had been put to the witness Ranjith Sebasthian was that there was no connection between the personal accounts and the account that was the subject-matter of the case. It was to this question that the witness had replied that no monies from the impugned account had been paid into a personal account of the 2nd defendant-respondent (page 124). The witness did not testify that 'the 2nd defendant was not involved at all'. Even an inference on this reply alone that the 2nd defendant was not involved at all cannot be made.

Importantly, this witness stated that unless both the Directors had signed the agreement the loan would not have been given pending the formation of the company, and the loan was granted to both of them jointly (page 115). The witness further stated that every change in address of the defendant-appellants had been informed to the Bank, and accordingly similar change in the address of the purported company had also simultaneously been requested (page 127). This witness also stated that there was transference of monies between this account and the other personal accounts of the 1st defendant-appellant (pages 128 and 129). Significantly, in spite of the abovementioned evidence of the witness for the Bank even the 2nd defendant-appellant did not give any evidence disclaiming her accountability or liability.

The position of the defendant-appellants was that in considering the privity of the contract, the Court must bear in mind that the defendant-appellants had at all times acted as Directors/Chairman of the "A. D. R. Products Ltd.". Since no company by that name was formed, they claimed that A. D. R. Products Ltd. was non-existent and therefore the contract was a nullity and could not be enforced. Counsel cited the case of *Newborne v. Sensolid*[1] in support of his proposition that an unformed company was not liable. In that case a contract for the sale of goods by a company was signed by the

sellers as "yours faithfully, Leopold Newborne (London) Limited", after which the name of Leopold Newborne was written. The Courts held that the contract could not be enforced because the company had never been formed, as evidently the contracting party was the company. Leopold Newborne could not prove that he was the seller of the goods and therefore he could not sue the buyer for non-acceptance of the goods. The legal principal enunciated by Lord Goddard was that he could not enforce his contract when he purported to sell not his goods but goods belonging to a company. He could not claim it to be "his contract", "when he never signed on behalf of the company or as an agent of the company but as the company. The document on which he was suing was held to be a nullity. The nexus of Leopold Newborne to the goods he claimed could not be established. The legal principal contained in that case was different and has no relevance to the present case.

In England the law relating to non-existent companies was altered by legislative intervention in 1972 by section 9 (2) of the European Communities Act of 1972. Now Companies Act of Engalnd 1975 section 36 (*c*). This section reads as follows :

> "Where a contract purports to be made by a company or by a person as agent for a company, at a time when the company has not been formed, then subject to any agreement to the contrary the contract shall have effect as a contract entered into by the person purporting to act for the company or as agent for it and *he shall be personally liable* on the contract accordingly."

The Sri Lanka Companies Act, No. 17 of 1982 does not have a similar provision.

In the present case in pursuance of the agreement P1 monies were released and accepted by the defendant-appellants. The sums of

money released, from time to time, into the account P2 was so released only because the defendant-appellants had duly completed and handed over the document P1, holding out that a company was in the process of being registered. (P7) These monies had been depleted or used up by the defendant-appellants. Both had the sole authority and were the authorised signatories duly recognised by the Bank. No tangible evidence had been given that anyone of them had not operated the account or did not receive any benefit. Even though the opportunity was afforded to the defendant-appellants neither gave evidence.

The case of *Kelner v. Baxter and Others*[2] had set down the principle that when a person contracts on behalf of a non-existent company he was personally liable.

In the same case (page 180) reference had been made to *ex parte Hartop*[3] at 352 where Lord Erskine stated that ". . . The mere fact of a person professing to sign a contract for or on behalf of or as an agent for another *will not per se prevent responsibility* as a contracting party to attach to the former".

In the case of *Furnivall v. Coombes*[4] a clause to exclude personal responsibility was included and was held to be repugnant and void, even though the company could not be held liable due to its non-existence.

The principle that underlay these cases was that once monies were received there was an accountability on those actually receiving the monies to repay the same, and they could not seek protection under legal fiction to avoid repayment.

On the face of P1 it was clear that the intention of the parties who signed it was to be liable for the monies that had been received.

There was no doubt that the monies were received and spent by defendant-appellants and no others. The rights and obligations of the parties to the contract, the Bank on the one hand and the defendant-appellants on the other cannot be transferred to a non-existent company, which in any event was not bound by the terms of the contract at the time it was made. The defendant-appellants were personally bound under the obligations created in terms of the contract P1 signed by them. Notwithstanding, the introduction of the words "Director", "Chairman" the defendant-appellants in the circumstances of this case were personally responsible and liable thereto. The defendant-appellants were therefore personally liable to pay the monies outstanding on the account.

The corporate veil which would have shielded them from liability, cannot be availed of, as admittedly the body corporate A. D. R. Company Ltd. was non-existent. I see no reason to interfere with the findings of the Additional District Judge holding them liable to repay the said monies.

Accordingly, the appeal is dismissed with incurred costs payable by the defendant-appellants to the plaintiff-respondent Bank.

UDALAGAMA, J. – I agree.

Appeal dismissed.