

*These notes refer to the Companies Act 2006 (c.46)
which received Royal Assent on 8 November 2006*

COMPANIES ACT 2006

EXPLANATORY NOTES

TERRITORIAL EXTENT AND DEVOLUTION

Part 4: a Company's Capacity and Related Matters

121. This Part replaces various provisions in the 1985 Act about a company's capacity and related matters, including in particular those in Chapter 3 of Part 1 of that Act.

Section 39: A company's capacity

122. This section provides that the validity of a company's acts is not to be questioned on the ground of lack of capacity because of anything in a company's constitution. It replaces the present section 35(1) and (4) of the 1985 Act, which made similar provision for restrictions of capacity contained in the memorandum.
123. The section does not contain provision corresponding to section 35(2) and (3) of the 1985 Act. It is considered that the combination of the fact that under the Act a company may have unrestricted objects (and where it has restricted objects the directors' powers are correspondingly restricted), and the fact that a specific duty on directors to abide by the company's constitution is provided for in section 171, makes these provisions unnecessary.
124. *Subsection (2)* indicates that the section, like section 35 of the 1985 Act, is modified in its application to charities.

Section 40: Power of directors to bind the company

125. This section provides safeguards for a person dealing with a company in good faith and restates section 35A and 35B of the 1985 Act. The power of the directors to bind the company, or authorise others to do so, is deemed not to be constrained by the company's constitution. This means that a third party dealing with a company in good faith need not concern itself about whether a company is acting within its constitution.
126. *Subsection (2)(b)(i)* of the section replaces part of section 35B of the 1985 Act: an external party is not bound to enquire whether there are any limitations on the power of the directors. The first limb of section 35B (which refers to the memorandum) has not been carried forward. This is concerned with restrictions in a company's constitution that limit a company's ability to act and consequently the powers of the directors to bind the company (the so called "ultra vires rule"). Under the Act, the objects no longer affect the company's capacity to act and so this limb is not necessary.

Section 41: Constitutional limitations: transactions involving directors or their associates

127. This section restates section 322A of the 1985 Act. It applies to a transaction if, or to the extent that, its validity depends on section 40 and provides that where the party to a transaction with a company is an "insider" (for example, a director of the company or person connected to such a director – see *subsection (2)(b)(i) and (ii)*), then the

protection afforded by that section will not apply. Instead, the transaction will be voidable at the instance of the company.

128. Irrespective of whether the transaction is avoided, the “insider” and any director who authorised the transaction is liable to account to the company for any gain he has made as a result of the transaction and to indemnify the company for any loss or damage that the company has incurred (see *subsection (3)*). However, where the “insider” is not a director of the company, it may be possible for him to avoid liability if he can show that at the time he entered into the transaction with the company he was unaware that the directors were exceeding their powers (see *subsection (5)*).
129. As now, under *subsection (4)*, a transaction will cease to be voidable in certain circumstances, for example, if restitution is no longer possible.

Section 42: Constitutional limitations: companies that are charities

130. This section restates section 65 of the Charities Act 1993. It is a qualification of the rules in sections 39 and 40.
131. It provides that the protection afforded to an external party by sections 39 and 40 will not apply where the company in question is a charity, unless:
- the external party was unaware (at the time that the act was done) that the company was a charity; or
 - the company has received full consideration in respect of the act done, and the external party was unaware that the act in question was beyond the company’s capacity or beyond the powers of the directors.
132. Corresponding provisions for charities that are registered in Scotland can be found in section 112 of the Companies Act 1989 (see *subsection (5)*).

Section 43: Company contracts

133. This section restates the provisions of section 36 of the 1985 Act.

Section 44: Execution of documents

134. This section largely restates section 36A of the 1985 Act. It provides that a company may execute a document under the law of England and Wales or Northern Ireland by affixing the company seal or by signature by two directors or by one director and a secretary (or joint-secretary) or (for the first time) by a single director if that signature is witnessed and attested.

Section 45: Common seal

135. This section replaces the provisions of sections 36A(3) and 350 of the 1985 Act. It permits but does not require a company to have a common seal. If a company has a common seal, it requires the seal to include the company’s name: failure to do so is an offence.

Section 46: Execution of deeds

136. This section restates section 36AA, inserted into the 1985 Act by the [Regulatory Reform \(Execution of Deeds and Documents\) Order 2005 \(SI 2005/1906\)](#). The only change is to extend the application for the purposes of the law of Northern Ireland.

Section 47: Execution of deeds and other documents by attorney

137. This section replaces section 38 of the 1985 Act. The 1985 Act does not require the appointment of the attorney to be by deed nor does it say anything about deeds executed on behalf of the company in the United Kingdom. This section provides that a company

may appoint, under the law of England and Wales or Northern Ireland, attorneys to execute deeds or other documents on its behalf, and that documents executed in this manner, whether in the UK or abroad, have effect as if executed by the company. It also makes clear that the method for a company appointing an attorney is by instrument executed as a deed, which is the same method by which an individual appoints an attorney.

Section 48: Execution of documents by companies

138. This section restates section 36B of the 1985 Act. It makes clear that no seal is required regardless of any other statutory provision. The only change is the addition of *subsection (1)* which makes clear that this section forms part of the law of Scotland only.

Section 49: Official seal for use abroad

139. This section replaces section 39 of the 1985 Act. It sets out the circumstances and manner in which a company may use its common seal outside the UK.

Section 50: Official seal for share certificates etc

140. This section restates section 40(1) of the 1985 Act. It enables a company that has a common seal to have an official seal for sealing securities issued by the company and for sealing documents creating or evidencing securities so issued.

Section 51: Pre-incorporation contracts, deeds and obligations

141. This section restates section 36C of the 1985 Act. A company is not bound by a contract purportedly made on its behalf before it came into existence unless the obligations are novated, i.e. a new contract must come into existence after incorporation on the same terms as the old one. Novation may be express or implied.

Section 52: Bills of exchange and promissory notes

142. This section restates section 37 of the 1985 Act. A bill of exchange is an unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand or at a fixed or determinable future time a sum certain in money to or to the order of a specified person, or to its bearer. A promissory note is an unconditional promise in writing made by one person to another, signed by the maker, engaging to pay, on demand or at a fixed or determinable future time, a sum certain in money to, or to the order of, a specified person or to its bearer. Where someone acting under a company's authority makes, accepts, or endorses such an instrument in the name of the company, or on its behalf, this section treats this as if these actions had been done by the company.