

## 3 Stone Buildings Presentation: Guilty Knowledge

### The Attribution of Knowledge

#### Andrew Twigger

1. This paper will consider the principal mechanisms by which English law attributes the knowledge of an individual to a company. It will not consider the exception to the normal principles of attribution which applies when the individual is committing a fraud on the company. That topic will be addressed by David Lord Q.C.
2. There is an important distinction to be drawn between:-
  - (1) The imputation of knowledge, whereby X is treated as knowing something even though he did not know it, because Y was acting on X's behalf and the law regards X as having Y's knowledge; and
  - (2) The attribution of Y's acts or state of mind to a company, because the company is not a real person and it can only act and think through individuals.
3. The first of these concepts, the imputation of knowledge, is an aspect of the law of agency. Knowledge of the agent is imputed, in certain circumstances, to the principal. Since a company can act through agents, the relevant rules are applicable to companies, but those rules apply equally when the principal is a human being. As will be explained below, the circumstances in which knowledge can be attributed to the principal are reasonably confined.
4. The second concept arises because of the special status of a company as having its own legal personality. When the individuals who make up the board of a company decide on a particular course of action, that is the decision of the company. This kind of attribution applies only to companies, but it applies to more than just knowledge: everything a company does amounts to something done by an individual (or individuals) which are attributed to it. The burden of this paper is that in recent years the courts have gradually extended the circumstances in which knowledge can be attributed in this way.
5. The two concepts are often confused, but the distinction between them is illustrated by the reasoning of the Court of Appeal *El Ajou v. Dollar Land Holdings* [1994] 2 All ER 685. The essential question was whether the defendant (DLH) should be fixed with the knowledge of its chairman (Mr Ferdman) that the funds which DLH had received by

way of investment were the proceeds of fraud. There were said to be two ways in which such knowledge could be attributed to DLH:-

- (1) Because Mr Ferdman was DLH's agent in the relevant transaction; or
  - (2) Because Mr Ferdman was, in relation to DLH's receipt of the assets in question, the "*directing mind and will*" of DLH and his knowledge was, consequently, to be regarded as that of DLH.
6. None of the members of the Court of Appeal thought that Mr Ferdman's knowledge could be imputed to DLH pursuant to agency principles, but they all thought that it could be attributed to DLH because he was its directing mind and will in relation to the receipt of the funds.
  7. This has always seemed to me to be an odd distinction, even if the ultimate result was right. In so far as Mr Ferdman had authority from DLH to act on its behalf in relation to the funds, there was no suggestion that his authority as agent was any more limited than his authority as its directing mind and will. If his knowledge was relevant in one capacity, it is difficult to see why, as a matter of logic, it should not be relevant in the other capacity.
  8. The reasoning of the Court of Appeal, and Hoffmann LJ in particular, turned on a long established principle of the law of agency to the effect that knowledge acquired by an agent outside the scope of his agency cannot be imputed to the principal, in the absence of any duty on the part of the principal to investigate. There was nothing to put DLH on inquiry and it had no duty to investigate or make disclosure. Consequently, Mr Ferdman's "*private*" knowledge could not be treated as the knowledge of DLH, even though he may well have owed a duty to DLH to inform it.
  9. This logic did not prevent Mr Ferdman's "*private*" knowledge being attributable to DLH on the ground that he was its directing mind and will, however. Hoffmann LJ referred to the judgment of Viscount Haldane LC in *Lennards Carrying Co. Ltd. v. Asiatic Petroleum Ltd.* [1915] AC 705, in which he used the expression "*directing mind and will*" to distinguish someone who was "*merely a servant or agent*" from someone whose actions were that of the company itself.
  10. Millett J had decided at first instance that Mr Ferdman was not the directing mind and will of DLH because he exercised no independent judgment, acting instead upon the directions of the American beneficial owners. Hoffmann LJ disagreed with this conclusion because, what mattered, in his judgment, was that Mr Ferdman

exercised powers on behalf of the company which identified him as the directing mind and will: in particular, he signed the relevant agreement, without there being any board resolution authorising him to do so. He “*committed the company to the transaction as an autonomous act which the company adopted by performing the agreement.*”

11. In *Meridian Global Funds Management Asia v. Securities Commission* [1995] 2 A.C. 500, however, Lord Hoffmann expressed some caution about the use of the expression “*directing mind and will.*” He said “*it will often be the most appropriate description of the person designated by the relevant attribution rule, but it might be better to acknowledge that not every such rule has to be forced into the same formula.*” Instead, he preferred to approach the question of attribution in that case as akin to an exercise of construction.
12. The facts were that Mr Koo was employed by the appellant investment management company. He caused the company to purchase a shareholding which triggered a reporting requirement under section 20(3) of the New Zealand Securities Amendment Act 1988. No notice was given under the section, which required the purchaser to give a notice once it knew that a relevant interest had been purchased. The company was, therefore, in breach of the section if Mr Koo’s knowledge was attributed to it, but not otherwise.
13. The Privy Council held that Mr Koo’s knowledge was attributable to the company. Lord Hoffmann reasoned as follows:-
  - (1) The law has developed “*primary*” rules of attribution which are derived either from the company’s articles of association (e.g. an article providing that decisions of the board are decisions of the company) or from company law (e.g. the unanimous decision of all the shareholders in a solvent company is the decision of the company).
  - (2) Since not every business decision can be taken by the board or the shareholders as a body, there are, in addition, rules of attribution derived from the principles of agency, which are the same rules as those applicable to natural persons.
  - (3) Furthermore, the company may become subject to liabilities as result of principles such as that of vicarious liability.
  - (4) These rules are “*usually sufficient to enable one to determine [the company’s] rights and obligations*” but this may not be the case “*in exceptional cases,*” such as where “*a rule of law, either expressly or by implication, excludes attribution on the basis of the general principles of agency or vicarious liability.*”

- (5) The example of such a rule given by Lord Hoffmann was of a rule of criminal law which speaks in terms only of the acts or state of mind of an individual. In such a case:

*“the court must fashion a special rule of attribution for the particular substantive rule. This is always a matter of interpretation: given that it was intended to apply to a company, how was it intended to apply? Whose act, (or knowledge, or state of mind) was for this purpose intended to count as the act etc. of the company? One finds the answer to this question by applying the usual canons of interpretation, taking into account the language of the rule (if it is a statute) and its content and policy.”*

- (6) Since the policy of the New Zealand Act was to compel the immediate disclosure of the identity of persons who become substantial security holders in public issuers, the person whose knowledge was to count as that of any company acquiring such shares was that of the person who, with authority of the company, acquired the relevant interest.

14. It seems to me that, whilst the result is obviously sensible, the approach raises a number of issues:-

- (1) Lord Hoffmann stresses that a special rule of attribution is to be fashioned in exceptional cases. Does this mean that knowledge which cannot be attributed to a company on the basis of the primary rules of attribution or agency principles will only rarely be attributable on the basis of the directing mind and will principle? This does not seem to be the way in which the *Meridian* reasoning has been applied in subsequent cases (see below).
- (2) The special rule of attribution envisaged by Lord Hoffmann is to be fashioned where a rule of law excludes attribution on the basis of the primary rules of attribution or agency principles. Again, this seems to contemplate a very limited scope for such a special rule, where there is some reason for thinking that the law did not intend normal rules to apply.
- (3) Lord Hoffmann’s comments about the exceptional nature of a special rule make perfect sense in the context of the interpretation of a statutory provision which is drafted by reference to the position of individuals, but was implicitly intended to apply to companies (such as the New Zealand Act considered in the *Meridian* case). But it is more difficult to see how this is to work in the case of non-statutory “rules”, such as the principles applicable to liability for fraudulent

representations, or knowing receipt, for example.

- (4) Take, for instance, the facts of *El Ajou*. Mr Ferdman's knowledge was not attributable to DLH on the basis of the primary rules of attribution, nor (as the Court of Appeal held) on normal agency principles. What was it about liability for knowing receipt which showed that such principles were excluded? What was exceptional about that case which justified fashioning a special rule of attribution? And how would one go about construing the principle of liability for knowing receipt?
  - (5) Surely, Hoffmann LJ's reasoning in *El Ajou* shows that it is always necessary to ask who is to count as the company in relation to the transaction in issue, regardless of whether primary rules of attribution or agency principles apply?
15. In *Bank of India v. Morris* [2005] 2 BCLC 328 the Court of Appeal was concerned with whether the knowledge of Mr Samant, a senior manager of the Bank of India, of the fraud carried out by BCCI was enough to fix the Bank of India with liability for fraudulent trading under section 213 of the Insolvency Act 1986. This was, obviously, a situation in which a construction of the statutory provision was appropriate and the Court held that the wording and policy behind the legislation was such that it would be wrong to limit attribution only to the knowledge of members of the board.
16. It was necessary to examine the facts of each case to determine whether the knowledge of an "agent" should be attributed for the purposes of the section, but typical factors to take into account were:-
  - (1) The seniority of the individual in the hierarchy of the company;
  - (2) His significance and freedom to act in the context of the particular transaction;
  - (3) The degree to which the board was informed and put on enquiry.
17. Mr Samant was very senior, he was given a free hand to negotiate the relevant transactions, and the board did not properly question him, despite the suspicious nature of the transactions. Consequently, his knowledge was attributed to the Bank.
18. However, in *MAN v. Freightliner* [2005] EWHC 2347 (Comm) (in which I acted for the defendant), Moore-Bick J was not concerned with the interpretation of a statute, but with the question of whether knowledge should be attributed when determining whether a fraudulent

representation had been made in a contract. He applied the *Meridian* approach to that question, without asking whether it was appropriate to fashion a special rule of attribution. He said that:

*“The essence of fraudulent misrepresentation, so far as is relevant for this case, is making a statement that is known to be untrue intending that the person to whom it is made will rely on it. Liability therefore depends on the conjunction of a false statement and a dishonest state of mind. In a case where it is said that a company has made a fraudulent misrepresentation the first step must be to see whether a false statement has been made by someone who is authorised to speak on the company’s behalf. Once that has been established the starting point in deciding whether the company acted dishonestly must be to enquire into the state of mind of the person who made the statement. However, if that person was unaware that the statement was false, it may be necessary to enquire into the state of mind of other persons who directed him to make it or who allowed it to be made.”*

19. Thus, the *Meridian* principle was, in effect, used in place of the old test of whether the relevant individual was the directing mind and will of the company for the purpose of the transaction in question. Moore-Bick J held that knowledge was not to be attributed for the purpose of the representation in the contract, since the individual with the knowledge was not a director or employee of the company, nor was he involved in the decision to commit the company to the contract. This did not ultimately avail the defendant, however, since the judge held it was vicariously liable in tort for fraudulent representations which the individual had made outside the contract.
20. In *Jafari-Fini v. Skillglass Ltd.* [2007] EWCA Civ 261 the question was whether a company had committed a “*Major Default*” as defined in a Facility Agreement by failing to disclose a bribe paid by the claimant to procure the company’s consent. The first question was whether the judge had been right to find that a bribe had been paid at all and the second question was whether, if that was so, he had also been right to find that the bribe had come to the attention of the company, which involved determining whether the knowledge of a director, Mr Webster, was to be attributed to it.
21. By a majority, the Court of Appeal decided that the judge was right on both questions. On the attribution issue, the members of the Court were unanimous as to the relevant principles, but Carnwath LJ considered that Mr Webster’s knowledge was less extensive than Moore-Bick LJ, with whom Laws LJ agreed.
22. Moore-Bick LJ followed *El Ajou* in holding that Mr Webster’s

knowledge could not be attributed on agency principles, since:-

- (1) Mr Webtser did not acquire the relevant knowledge because he was a director of the company, but because he was the claimant's friend.
  - (2) Mr Webster was not employed by the company to perform a task or transaction which required the company to investigate: he was simply a member of the board.
  - (3) Nor was the company under a duty to disclose information in the possession of its agents.
  - (4) Furthermore, the evidence pointed to Mr Webster not, in fact, having disclosed his knowledge to the board.
23. Moore-Bick LJ then applied the *Meridian* principle by interpreting not a statutory rule or a general rule of law but the provision of the Facility Agreement which required the company to make full disclosure of “*all information which comes to [its] attention.*” In Moore-Bick LJ's view, this clause extended to knowledge held by the board of directors as a whole and the only question was whether information which came to the attention of one director, but which he had not shared with the rest of the board, was to be treated as information in the possession of the company.
24. Moore-Bick LJ reasoned that:
- “In MAN v. Freightliner I expressed the view that where the board of directors is properly to be regarded as the directing mind and will of the company in relation to a particular transaction the knowledge of each is to be attributed to the company. That case, however, was concerned with the liability of the company for a false statement made in a written contract which the board as a whole had resolved that the company should enter into. The present case differs in as much as it is concerned with the acquisition by the company of information, but there are nonetheless similarities arising from the fact that members of the board can generally be regarded as collectively representing the company. In general, therefore, I think that information relevant to the company's affairs that comes into the possession of one director, however that may occur, can properly be regarded as information in the possession of the company itself.”*
25. Consequently, Mr Webster's knowledge was to be attributed to the company, even though he personally was not the directing mind and will of the company in relation to any other aspect of the transaction.

It seems to me that this comes, in effect, to saying that all the knowledge of a director will always be attributed to a company, provided only that the board as a whole can be said to be the directing mind and will of the company in relation to the transaction (which must apply in the vast majority of cases).

26. This appears to run counter to Hoffmann LJ's confirmation in *El Ajou* that "*English law has never taken the view that the knowledge of a director ipso facto [is to be] imputed to the company.*" Indeed, if Moore-Bick LJ's analysis is correct, it would not have been necessary for the Court of Appeal in *El Ajou* to find that Mr Ferdman had any role in relation to the transaction by which DLH received the funds: it would have been enough merely that the board, of which Mr Ferdman was a member, had such a role.
27. Nevertheless, in *Lebon v. Aqua Salt Co. Ltd.* [2009] BCC 425 Lord Hoffmann approved what he described as "*the general principle formulated by Moore-Bick LJ*" (emphasis added). In the *Lebon* case the issue was whether the defendant company knew that land which it had purchased was the subject of an earlier sale agreement by one of its directors, Mr Jingree, to the claimant. If so, the company had purchased the land in bad faith and, under the law of Mauritius, the claimant could assert an interest in it.
28. Lord Hoffmann, giving the opinion of the Privy Council, applied the *Meridian* principle to the general rule of the law of Mauritius that it is inequitable for a second purchaser with actual notice of the first purchase to rely on the absence of registration, because the second purchaser already has all the information which registration would give him. Lord Hoffmann said "*It is therefore necessary to ask which rule of attribution would best serve the purpose of this rule. If one of the directors knows of the previous sale at the time of the purchase but omits to tell the other directors and allows the sale to go ahead, would it be equitable for the company to be able to rely on the lack of transcription to override the rights of the earlier purchaser?*"
29. Lord Hoffmann answered that question in the negative, saying that there was no reason why Moore-Bick LJ's general principle should not apply. When he examined the facts, however, he pointed out that the company was only able to purchase the land in the first place by virtue of arrangements Mr Jingree had previously made with the vendor. Although he did not expressly say so, he was effectively holding that Mr Jingree was the directing mind and will of the company for the purposes of the relevant transaction. It is not obvious that Lord Hoffmann would have reached the same conclusion if Mr Jingree had not had anything to do with the transaction.

### Conclusion

30. The knowledge of a rogue director can be attributed to a company much more readily than the knowledge of an agent can be imputed to a principal. This can be explained by reference to the historical development of the different rules of attribution, but it is not clear why it should be so as a matter of common sense. It is possible to imagine circumstances in which a claimant may be able to have a transaction with a company set aside, for example, on the basis that one of the directors knew some nefarious detail about it, but in which the same transaction could not be set aside against a partnership because the knowledge of one partner was not attributable to the others on ordinary agency principles. How can that be the correct result?
31. The merit of Lord Hoffmann's approach in *Meridian* (notwithstanding the criticism that he explained it in terms of a special approach applicable to exceptional circumstances, when it appears to be much more general) is that it enables the court to make a principled value judgment about whether, in the circumstances of the particular case, knowledge should be attributed. But it is difficult to see why the same approach should not be applicable in all cases of attribution, regardless of whether a company is involved.
32. Furthermore, the present state of the law appears to be that, at least in some circumstances, knowledge of one director might be attributed to the company even though he had nothing whatever to do with the transaction in question and the other directors knew nothing. If this truly is a general principle, it seems to expose a company to far greater risks than might previously have been thought. There seems to be something to be said in favour of the old approach of asking whether the relevant individual is the directing mind and will of the company for the purpose of the transaction in question.
33. It is perhaps wise to bear in mind at all times the cautionary words at the conclusion of Hoffmann LJ's judgment in *El Ajou*:

*“If the persons beneficially interested in a company prefer for tax or other reasons to allow that company to be for all legal purposes run by off-shore fiduciaries, they must accept that it may incur liabilities by reason of the acts or knowledge of those fiduciaries.”*

Andrew Twigger  
25 September 2009