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Contributor

A NEW APPROACH TO PRE-INCORPORATION CONTRACTS

In commercial life people who are entering into business ventures and who are in the process of incorporating a company, (promoters) often enter into contracts, called pre-incorporation contracts. Those contracts are intended for the benefit of the company to be incorporated but the company to be incorporated cannot enter into a contract because it does not become a legal entity until the certificate of incorporation is issued. Even after it is incorporated it cannot "ratify" or "adopt" a contract ostensibly made on its behalf because the promoters are unable to act for a principal which does not exist.

However promoters are often anxious to take advantage of a business opportunity while their attorneys are incorporating companies on their behalf. They may for example wish to buy or sell, a business, equipment, a restaurant or do a deal which must be "clinched" immediately.

What does the law say about the obligation of the promoter who enters into a contract of this nature? As the company is not in existence, the promoters may or may not be liable personally, and whether they are depends on the capacity in which they purport to sign the contract. If the contract was signed by the promoter "for and on behalf of ABC

Co. Ltd”, the promoter is personally liable, but where he signs “ABC Co. Ltd. per John Black” then there is no contract. In the first example, the promoter has signed in his personal capacity, while in the second he has signed on behalf of a company which does not exist.

Fine distinctions such as these created uncertainty and hardship in the law for both promoters and persons entering into contracts with them.

The modern approach to the law is to be enacted in Jamaica when the new Companies Act is passed. It will provide that:-

1. A promoter is personally liable when he enters into an oral or written agreement or a contract on behalf of a company which does not exist, unless he expressly states in the agreement that he is not to be personally liable. The promoter may also enforce this contract for his own benefit;
2. Within a reasonable time after incorporation (no time limit provided) the company may adopt the contract, and when it does, the company is liable under the contract as if it were incorporated at the time the pre-incorporation contract was created;
3. The promoter is not liable under the contract nor can he take the benefit of the contract, once it is adopted by the company. However, whether the contract is adopted or not by the company, a party to it may apply to the court for an order fixing liabilities and apportioning obligations between it, the promoter and the company. The court will be vested with wide discretionary powers to make such orders as it deems fit.

This new approach in the law reflects the modern position enacted in Canada under the

Canadian Business Corporation Act. Barbados and Trinidad and Tobago have adopted the provisions of the Canadian Act. Our proposed provision differs from our Caribbean partners, in that the provision covers “an oral or written agreement or contract” whereas theirs covers “a written contract” only.

The earliest reform of the common law occurred in South Africa as early as 1926 where it was provided that the company which is subsequently incorporated must be empowered in its memorandum to adopt the pre-incorporation contract and the contract must be lodged with the other company documents at the time of incorporation.

New Brunswick and Ontario have included oral contracts as we will in our new Act and in England the Companies Act 1986 refers simply to “contracts”. Presumably this applies to oral and written contracts. The UK legislation provides that promoters are personally liable on pre-incorporation contracts, a reform of the common law position which made liability of the promoter dependent on the manner in which the contract was signed. However the UK reform does not address the difficulty of making the company once incorporated adopt the contract, a situation which one leading commentator has described as “lamentable”. Presently the only way in which the company can adopt a pre-incorporation contract is to enter into a post incorporation agreement in the same terms. Until the new Act becomes law the old common law position is, of course, our position.

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