Capacity and authority considerations in commercial financing transactions from a Bahrain law perspective

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In commercial financing transactions, generally, a formal legal opinion is sought by the lender to give them certainty on the capacity and authority of the borrower and/or any obligor as well as the enforceability of the transaction including the transaction documents. This article considers particular issues relating to capacity and authority in Bahrain.

Express versus implied powers

It is common in Bahrain for directors or managers to be granted general powers under the company's memorandum and/or articles of association. Such powers are expressed in generic terms, referring to the power to 'do all acts and deeds for and on behalf of the company' or to 'manage the company and do all things necessary to achieve its objects'. While useful for the management of the day-to-day operations of the company, relying on such generic powers when borrowing money, granting security or providing a guarantee can be risky.

Generally, the law does not imply powers of a company. There is no concept of ostensible authority under the laws of Bahrain. Accordingly, explicit authority where the company has provided a certain representative (be it a manager, director or otherwise) to do that specific act for and on behalf of the company will be required. General management powers granted to the directors or managers in the company's memorandum and/or articles of association are unlikely to be sufficient for the purposes of establishing the capacity of a company to enter into finance transactions.

Therefore, the express terms of its constitutional documents of the company would need to be considered. By way of example:

- when opening an account, the constitutional documents must contain the right/power to open bank accounts, deal with financial institutions or similar wording;
- when borrowing money, the constitutional documents must contain the right/power to borrow, obtain finance, obtain credit or finance facilities or similar wording. If the term of the loan is more than three (3) years, the constitutional documents must clearly specify that the directors have the power to borrower for more than three (3) years. If this is not clearly stated, then under Article 182 of the Law No. 21 of 2001 promulgating the commercial companies law (as amended) ("**Companies Law**") a shareholders' resolution is required;
- when granting security, the constitutional documents must contain the right/power to mortgage, pledge or grant security interests over the company's property to secure the debt; and
- when giving a guarantee, the constitutional documents must contain the right/power to guarantee a third party's obligations.

When assessing the power of individuals to sign on behalf of a company the first place to start is the constitutional documents of that entity. The appropriate power or authority should be given to the individual in the constitutional documents. For example:

- if the constitutional documents clearly authorise an individual to perform the relevant activity, nothing further is required;
- if the board of directors are authorised in the constitutional documents to perform the relevant activity, a directors' resolution approving the transaction and authorising a certain individual or individuals to sign is acceptable;
- a notarised power of attorney from the company to the individual(s) giving them the power to enter into that particular type of transaction is acceptable (including renewal of facilities granted to the corporate entity); or
- if an individual is authorised (with the power to delegate), a notarised power of attorney from the authorised individual to that individual(s) giving them the power to enter into that particular type of transaction (including renewal of facilities) is acceptable.

If none of the above apply, a shareholders' resolution should be obtained.

Please note that according to Article 183 of the Companies Law, in relation to joint stock companies (public and private) and limited liability companies (limited liability) "*the chairman of the board is the head of the company who represents it before third parties. His signature shall be considered as a signature of the board of directors before third parties. He shall implement the decisions of the board and comply with its recommendations. The vice-chairman shall replace the chairman in the latter's absence and have the same powers of the chairman of the board*". Accordingly, if a board of directors' resolution is obtained from joint stock companies (public and private) and limited liability companies (limited liability) that is only signed by the chairman of the board of directors, this can be considered as a signature of the entire board of directors based on Article 183 of the Companies Law (subject to no contrary provision being contained in the constitutional documents of the company).

Whatever the case, there should be a clear chain of authority from the constitutional documents to the relevant individual.

Conclusion

If the company does not have the capacity and authority to enter into the transaction and transaction documents, the company would be acting outside its powers (i.e. ultra vires) and as such, its entry into the transaction and transaction documents could be challenged.

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