IN THE SUPREME COURT OF THE DEMOCRATIC SOCIALIST REPUBLIC OF SRI LANKA

In the matter of an appeal under Section 5(1) of the High Court of the Provinces (Special Provisions) Act No. 10 of 1996 read together with Section 6 thereof, Sections 754(1), 755(3) and 758 of the Civil Procedure Code and Article 128 of the Constitution of the Democratic Socialist Republic of Sri Lanka.

SC (CHC) Appeal No. 37/2011
Commercial High Court of Colombo
Case No. HC (Civil) 285/2006(1)

Pan Arch Architecture (Pvt) Limited,
19-D, Ocean Tower, Station Road,
Colombo 4.

Plaintiff

vs

(1) Neat Lanka (Pvt) Limited,
47A Prince Street, Colombo 11.

And also at
No. 50 1/11, Colombo Plaza, Wellawatte.

(2) Neat Property Developers (Pvt) Limited,
51, Vipulasena Mawatha,
Colombo 10.

Defendants

And now between

Pan Arch Architecture (Pvt) Limited,
19-D, Ocean Tower, Station Road,
Colombo 4.

Plaintiff – Appellant

vs

(1) Neat Lanka (Pvt) Limited,
47A Prince Street, Colombo 11.

And also at
No. 50 1/11, Colombo Plaza, Wellawatte.

(2) Neat Property Developers (Pvt) Limited,
51, Vipulasena Mawatha,
Colombo 10.

Defendants – Respondents

Before: **Vijith K. Malalgoda, PC, J**
Mahinda Samayawardhena, J
Arjuna Obeyesekere, J

Counsel: Geoffrey Alagaratnam, PC with Suren Fernando for the Plaintiff – Appellant

Argued on: 29th May 2023

Written Submissions: Tendered on behalf of the Plaintiff – Appellant on 7th June 2023

Decided on: 13th October 2023

Obeyesekere, J

The Plaintiff – Appellant [the Plaintiff] instituted action in the High Court of the Western Province exercising Civil jurisdiction and holden in Colombo [the Commercial High Court] on 7th December 2006 against Neat Lanka (Private) Limited, the 1st Defendant – Respondent [the 1st Defendant] and Neat Property Developers (Private) Limited, the 2nd Defendant – Respondent [the 2nd Defendant], claiming that the Defendants are jointly and severally liable to pay the Plaintiff a sum of Rs. 10,200,000 for the architectural and consultancy services provided by the Plaintiff to the Defendants and seeking to recover

the said sum of money together with interest from 28th September 2006. While each of the Defendants filed answer denying liability, the 2nd Defendant preferred a claim in reconvention against the Plaintiff, necessitating the filing of a replication by the Plaintiff denying the said claim.

Admissions and Issues having been raised on behalf of all parties, the case proceeded to trial with the Plaintiff leading the evidence of two witnesses, namely Kumudu Munasinghe, its Managing Director and Lakkana Abeynayake, who had served as the Chief Executive Officer of the 2nd Defendant at the time relevant to the impugned transaction. Sanjeeva Senaratne, a director and shareholder of the 1st and 2nd Defendants gave evidence on behalf of the Defendants. On 16th September 2011, the learned Judge of the Commercial High Court entered judgment in favour of the Plaintiff but only against the 1st Defendant.

Aggrieved, the 1st Defendant filed an appeal in this Court against the said judgment. The Plaintiff too filed an appeal complaining that the learned Judge of the Commercial High Court erred when he failed to hold against the 2nd Defendant, as well, in spite of having answered the issues relating to the 2nd Defendant in a manner favourable to the Plaintiff. Both appeals were taken up together for argument on 29th May 2023, on which date the learned President's Counsel for the Defendants informed this Court that he has received instructions from the Defendants that both companies are presently defunct and for that reason, the 1st Defendant is not interested in pursuing with the appeal filed by it and the 2nd Defendant will not participate in the appeal filed by the Plaintiff.

The learned Counsel for the Plaintiff, Geoffrey Alagaratnam, PC informed this Court that he has received instructions to proceed with the appeal of the Plaintiff. Accordingly, this Court proceeded to hear Mr. Alagaratnam, PC, who submitted that while the findings of the Commercial High Court against the 1st Defendant are no longer in issue, the principal issue that is left to be determined is whether the learned Judge of the Commercial High Court erred when he did not hold the 2nd Defendant jointly and severally liable for the payment of the aforesaid sum of money to the Plaintiff.

Background to the transaction

I shall commence by setting out as briefly as possible the background events relating to the transaction that culminated in the filing of action in the Commercial High Court.

The Plaintiff, a limited liability company incorporated under the provisions of the Companies Act, was engaged in the business of architecture, engineering, project management and safety consultancy. According to its Managing Director Munasinghe, discussions had taken place in November and December 2005 with Senaratne, Suminda Perera, who was the other director and shareholder of the 1st Defendant, and Lakkana Abeynayake who did not hold any position in either of the Defendants at that time, relating to the construction of a luxury mixed development project [the Project] on a land situated on Galle Face Terrace, Colombo 3, which land was said to have been owned by the 1st Defendant.

There are three matters that must be noted. The first is that Abeynayake was appointed as the Chief Executive Officer of the '*2nd Defendant*' by the 1st Defendant with effect from 2nd January 2006 by letter dated 3rd January 2006 signed by Senaratne and Perera [P26]. The second is that the 2nd Defendant was not in existence at this point in time and was incorporated only on 26th January 2006. The third is that the intention of the aforementioned Directors of the 1st Defendant was to incorporate the 2nd Defendant as a special purpose vehicle for the purpose of carrying out the said Project, which meant that the 2nd Defendant too was to be a contracting party. Senaratne confirms this position in his affidavit which served as his evidence-in-chief before the Commercial High Court where he states that, "*The 2nd Defendant Company was incorporated to engage in a Project for the development of a land situated in Kollupitiya and for the construction of a condominium building thereon and for the 2nd Defendant to sell or lease condominium units therein to prospective buyers and lessees.*" With the 2nd Defendant being a shell company with no assets of its own, the Project was to be funded by the 1st Defendant.

Offer and acceptance

Pursuant to the aforementioned discussions and at the invitation of the 1st Defendant, the Plaintiff had submitted its written offer dated 28th December 2005 [P4] for the provision of consultancy services for the said Project, addressed to Suminda Perera, in his capacity as a Director of the 1st Defendant. The said proposal sets out the scope of services to be performed by the Plaintiff, the fee that was payable for the said services and the payment milestones linked to six design stages. P4 had been followed by another letter from the Plaintiff the next day [P5], addressed in the same manner as P4, amending the fee proposed in P4 from 6% to 4%. It is noted that the receipt of P4 and P5 have been acknowledged in writing by P6, to which I shall refer in detail, later.

Although no formal written agreement was executed between the Plaintiff and the 1st Defendant relating to the provision of services by the Plaintiff for the Project, the acceptance by the 1st Defendant of the offer of the Plaintiff contained in P4 and P5 is borne out by the payment of a sum of Rs. 1,500,000 that the 1st Defendant made as an advance by a cheque dated 5th January 2006 drawn on its account [D5]. While this payment served as a promise from the 1st Defendant to the Plaintiff that payment for the work that was to be carried out by the Plaintiff was to be made by the 1st Defendant, it also demonstrated the intention on the part of the 1st Defendant to contract the services of the Plaintiff for the said Project and create a legal relationship between the parties. The receipt of the said sum of money has been acknowledged by the Plaintiff by an invoice dated 6th January 2006 [P10] issued in favour of "Suminda Perera, Neat Developers (Pvt) Limited" which is not the corporate name of either the 1st or the 2nd Defendant. Be that as it may, by making this payment, and especially in the absence of any written correspondence to the contrary, the 1st Defendant has clearly undertaken to be financially responsible and contractually liable for payment for services that the Plaintiff was to provide in terms of P4, read with P5.

Appointment of the Plaintiff

P4, P5 and the aforementioned payment were followed by letter dated 17th January 2006 [P6] titled, '*Letter of appointment for Consultancy Services for new Luxury Mixed Development Project at No. 27A, Galle Face Terrace, Colombo 3*', addressed to the Plaintiff. Although the 2nd Defendant was yet to be incorporated, P6 was on a letter head of the 2nd Defendant and signed by Abeynayake, in his capacity as the Chief Executive Officer of the 2nd Defendant.

P6 reads as follows:

> "***On behalf of Neat Property Developers (Private) Limited****, I am pleased to appoint your company, Pan Arch Architecture (Private) Limited as the Consultancy Company for the provision of a Consortium service for our prestigious new luxury development project at No. 27A, Galle Face Terrace, Colombo 3,* ***on the terms and conditions as set out in your letters dated 28th and 29th December 2005*** *except that the Consortium Fee is 3.5%, as was subsequently agreed between our Directors, Mr. Sanjeeva Senaratne and Mr. Suminda Perera and yourself.*
>
> *Further, as approved and confirmed by our Directors, Mr. Sanjeeva Senaratne and Mr. Suminda Perera,* ***Neat Lanka (Private) Limited will be responsible for all payments/expenses with regard to the Project****, since both Directors, Mr. Sanjeeva Senaratne and Mr. Suminda Perera are also directors of Neat Lanka (Private) Limited and the project site at No. 27A, Galle Face Terrace, Colombo 3 is also owned by Neat Lanka (Private) Limited.*
>
> *We look forward to a successful outcome to this project and a long and happy association with Pan Arch Architecture.*" [emphasis added]

There are three important matters to be noted with regard to P6. The first is that even though P6 had been written on behalf of the 2nd Defendant, the 2nd Defendant had not been incorporated as at the date of P6. The second is that in between P4 and P6, negotiations had taken place between the 1st Defendant and the Plaintiff which resulted in the consortium fee being reduced by a further 0.5% to 3.5%. The third is that even

though the Plaintiff was required to provide the consultancy services to the 2nd Defendant, the 1st Defendant had undertaken the liability to make the payments for the work that was to be carried out by the Plaintiff.

Pre-incorporation contracts

I must at this stage advert to the legality and the consequences of a contract entered into by a company prior to its incorporation, known as pre-incorporation contracts, and thereby place P6 in its proper perspective.

In **Gower's Principles of Modern Company Law** [by Paul L. Davies and Sarah Worthington, 10th ed., 2016, Sweet & Maxwell] the position in England with regard to pre-incorporation contracts has been laid down in the following manner [pages 111 to 113]:

> "*As already noted, these contracts cannot bind the non-existent entity, and the company, once formed, cannot ratify or adopt the contract. Prior to statutory amendments driven by the UK's entry into the EU, the legal position as between the promoter and the third party seemed to depend on the terminology employed. If the contract was entered into by the promoter and signed "for and on behalf of XY Co Ltd" then, according to the early case of Kelner v. Baxter [(1866) L.R. 2 C.P. 174], the promoter would be personally liable. But if, as is much more likely, the promoter signed the proposed name of the company, adding his own to authenticate it (e.g. XY Co Ltd, AB Director) then, according to Newborne v. Sensolid (Great Britain) Ltd., [(1954) 1 Q.B. 45 CA] there was no contract at all. This was hardly satisfactory.*
>
> *The statutory rule took a clear if rather dramatic stand. The relevant provision is now CA 2006, s. 51, which reads:*
>
> > *"(1) A contract which purports to be made by or on behalf of a company at a time when the company has not been formed, has effect, subject to any agreement to the contrary, as one made with the person purporting to act for the company or as agent for it, and he is personally liable on the contract accordingly."*

The obvious aim of the provision is to increase security of transactions for third parties by avoiding the consequences of the contract with the company being a nullity. The provision imposes contractual liability on the promoter, and applies even if the new company is never formed. To avoid the promoter's personal liability under the statute, the third party must explicitly agree to forego the protection – consent cannot be deduced simply from details of the contract which, interpreted widely, would be inconsistent with the promoter accepting personal liability, such as the promoter signing as agent for the company.

The presence of the statutory provision has had an effect on the courts' perception of the common law in this area. In Phonogram Ltd v. Lane [(1982) 1 Q.B. 938 CA], Oliver LJ said that the "narrow distinction" drawn in Kelner v. Baxter and the Newborne case did not represent the true common law position, which was simply: "does the contract purport to be one which is directly between the supposed principal and the other party, or does it purport to be one between the agent himself – albeit acting for a supposed principal – and the other party?" ***This question is to be answered by looking at the whole of the contract and not just at the formula used beneath the signature****. If after such an examination the latter is found to be the case, the promoter would be personally liable at common law, no matter how he signed the document.*

On this analysis the difference between s. 51 and the common law is narrowed, but not eliminated. At common law, if the parties intend to contract with the non-existent company, the result will be a nullity and the third party protected only to the extent that the law of restitution provides protection. Under the statute, a contract which purports to be made with the company will trigger the liability of the promoter, unless the third party agrees to give up the protection. ***In other words, the common law approaches the question of the third party's contractual rights against the promoter as a matter of the parties' intentions****, with no presumption either way, whereas the statute creates a presumption in favour of the promoter being contractually liable. The common law is still important in those cases which fall outside the scope of the statute."* [emphasis added]

In **Attygalle and Another v Commercial Bank of Ceylon Ltd**. [(2002) 1 Sri LR 176], the Court of Appeal observed that the Companies Act, No. 17 of 1982 does not have a provision similar to Section 36(c) of the Companies Act of England 1975 which was in force at that time and which was similar to Section 51 referred to earlier. In **Company Law** by Kanag-Isvaran and Wijayawardana [2014, at page 79], it has been pointed out that prior to the enactment of the present Companies Act in 2007, and in the absence of any provisions in the Companies Act, No. 17 of 1982, " *… it was the common law that governed pre-incorporation contracts in Sri Lanka. The common law, as it stood, that governed pre-incorporation contracts was simple. A company had no capacity to contract before its incorporation, for one cannot act before one comes into existence. This was based on the principle that an act which cannot be done by a non-existent principal, cannot be done through an agent. It was also a settled principle in common law that after a company was incorporated it could not ratify pre-incorporation contracts, for the reason that a contract purported to be made by a company which did not exist was considered a nullity in the eyes of the law.* "

The issue that had arisen in Kelner v Baxter (supra) and Newborne v Sensolid (Great Britain) Ltd. (supra), was however laid to rest by some legislative wizardry in the form of Sections 23 to 25 of the Companies Act, No. 7 of 2007, of which Sections 23 and 24 are re-produced below:

Section 23

"*(1) For the purpose of this section and sections 24 and 25 of this Act, the expression "pre-incorporation contract" means –*

(a) a contract purported to have been entered into by a company before its incorporation; or

(b) a contract entered into by a person on behalf of a company before and in contemplation of its incorporation

(2) Notwithstanding anything to the contrary in any law, a pre-incorporation contract may be ratified within such period as may be specified in the contract or if no such period is specified, within a reasonable time after the incorporation of such company, in the name of which or on behalf of which it has been entered into.

(3) A pre-incorporation contract that is ratified under subsection (2), shall be as valid and enforceable as if the company had been a party to the contract at the time it was entered into.

(4) A pre-incorporation contract may be ratified by a company in the same manner as a contract may be entered into on behalf of a company under section 19."

Section 24

"*(1) Notwithstanding anything to the contrary in any law, in a pre-incorporation contract, unless a contrary intention is expressed in the contract, there shall be an implied warranty by the person who purports to enter into such contract in the name of or on behalf of the company –*

(a) that the company will be incorporated within such period as may be specified in the contract, or if no period is specified, within a reasonable time after the making of the contract; and

(b) that the company will ratify the contract within such period as may be specified in the contract or if no period is specified, within a reasonable time after the incorporation of such company.

(2) The amount of damages recoverable in an action for breach of an implied warranty referred to in subsection (1), shall be the same as the amount of damages that may be recoverable in an action against the company for damages for breach by the company of the unperformed obligations under the contract, if the contract had been ratified by the company.

(3) *Where after its incorporation, a company enters into a contract in the same terms as or in substitution for, a pre-incorporation contract (not being a contract ratified by the company under section 23), the liability of a person under subsection (1) shall be discharged*."

Thus, had this transaction taken place after the Companies Act, No. 7 of 2007 was enacted, the Plaintiff could have resorted to the above provisions in pursuing its legal rights.

Continued involvement of the 1st Defendant

The evidence of Abeynayake was that P6 had been prepared on the instructions of Senaratne and Perera. With the 2nd Defendant not having been incorporated by the time P6 was written, I must emphasise the fact that P6 to my mind, served as much more than a mere comfort letter to the Plaintiff that payment would be made by the 1st Defendant, especially since the 2nd Defendant was being incorporated for the specific purpose of carrying out the Project and did not possess the necessary financial resources at the beginning of the Project to meet the advance payment of 10% which was due upon the Plaintiff undertaking the Project. The fact that the 2nd Defendant did not have any assets or for that matter even a bank account after its incorporation has been confirmed by Abeynayake in his evidence, thus demonstrating that it is the 1st Defendant who had the financial strength to execute the Project and that the 1st Defendant was very much an integral part of the Project, and was to continue as a contracting party to the transaction, in spite of the fact that the services were to be provided to the 2nd Defendant. This is further confirmed by the email dated 24th January 2006 [P9], by which the Plaintiff had forwarded the Preliminary Construction Cost Estimate to Abeynayake, with the 1st Defendant being referred to as the Client.

Entry of the 2nd Defendant

The 2nd Defendant was incorporated two days after P9 – i.e., on 26th January 2006 [P8a], with Senaratne and Perera being the only shareholders and directors of the 2nd Defendant. While the correspondence tendered do not indicate as to what transpired

between the parties immediately thereafter, by letter dated 24th February 2006 [P12] addressed to Abeynayake in his capacity as Chief Executive Officer of the 2nd Defendant, the Plaintiff had sought the payment of a sum of Rs. 3,400,000 being the balance of the advance payment and a further Rs. 9,800,000 being the percentage due for the schematic design which the Plaintiff claims it had completed for the 2nd Defendant after its incorporation. The fact that the Plaintiff called for payment from the 2nd Defendant demonstrates that in its mind, the 2nd Defendant too was a contracting party and an integral part of the transaction.

This is confirmed by the reply to P12 which is a letter dated 2nd March 2006 [P13] sent by Abeynayake in his capacity as Chief Executive Officer of the 2nd Defendant on a letter head of the 2nd Defendant, where, under the title of "*Consultancy Fees for new luxury mixed development project at No. 27A, Galle Face Terrace, Colombo 3,*" he has stated as follows:

> "*We have received your letter dated 24th February 2006 setting out the payments due for the advance and the schematic stage of design.*
>
> ***Our directors**, Mr. Sanjeeva Senaratne and Mr. Suminda Perera **have approved and agreed to release the balance money from Neat Lanka (Pvt) Limited**, as soon as possible, **since the payments due are in order**.*
>
> *Thank you for sending me a copy of the schematic design drawings.*" [emphasis added]

P13, quite apart from not contesting the fact that services have been and are being performed by the Plaintiff for the 2nd Defendant and that payments are due, contains a promise on the part of the 2nd Defendant that the payments would be made by the 1st Defendant, thus ensuring the continued presence of the 1st Defendant in the transaction. I must perhaps emphasise that the transaction that had developed since December 2005 and which was still evolving in the months of January and February 2006, saw the involvement of both Defendants, with work being carried out by the Plaintiff initially at the request of the 1st Defendant and after its incorporation, for the 2nd Defendant, with the 2nd Defendant acknowledging that the work has been carried out to their satisfaction,

and the 1st Defendant taking financial responsibility for the said work, thus giving rise to a tri-partite transaction. One cannot argue that the 2nd Defendant stands removed from the relationship between the Plaintiff and the 1st Defendant as, had that been the case, there need not have been any involvement from the 2nd Defendant at all and, it certainly should not have made any representations as to the contract terms, like those that one sees from P13.

Further payments by the 1st Defendant

Pursuant to P13, the 1st Defendant had made two further payments of Rs. 1,500,000 by cheque drawn on its account in favour of the Plaintiff, the first being on 20th March 2006 [D8] and the second being on 27th March 2006 [D9]. The two payment vouchers [D6 and D7] prepared by the 1st Defendant however state that the monies are being given by way of a loan to the 2nd Defendant. By stating so, the 1st Defendant has confirmed that the work is being carried out for the 2nd Defendant. The invoices for these two payments [P14 and P15] have been issued by the Plaintiff in favour of the 2nd Defendant, thus confirming the intention of the Plaintiff to create a legal relationship with the 2nd Defendant, as well.

By letter dated 8th May 2006 [P16] addressed to Senaratne in his capacity as Director of the 2nd Defendant, the Plaintiff had requested that the balance sum of Rs. 10,200,000 be paid. It appears that the relationship between the parties had deteriorated by this time, probably due to the failure to make payment for the work already done. Two reminders to P16, both addressed to the same person as in P16, had been sent to the 2nd Defendant on 31st May 2006 [P17] and 25th July 2006 [P18], with the receipt of both letters having been acknowledged by the 1st Defendant. In between P17 and P18, i.e., on 14th June 2006, Abeynayake had resigned as Chief Executive Officer of the 2nd Defendant. P17 and P18 have been followed by letters of demand dated 28th September 2006 to both the 1st Defendant [P20] and the 2nd Defendant [P21]. As the Defendants had failed to respond to any of the aforementioned letters P16, P17, P18, P20 and P21 and pay the money claimed therein, action had been instituted on 7th December 2006, on the basis that the 1st and the 2nd Defendants are jointly and severally liable for the payment of the balance sum for the work performed by the Plaintiff.

Relationship between the parties – *vide* the pleadings

The question whether it is the 1st or the 2nd Defendant that is liable or whether both Defendants are liable depends on the relationship that developed between the parties, the promises they made to each other and the intention of each party that can be gathered from the evidence, both oral and documentary.

In paragraph 12 of its plaint, the Plaintiff had stated that, "*at all times material the* ***Defendants are jointly and severally liable*** *to the Plaintiff on the written agreement entered into between the parties, especially as* ***the contract was between the 2nd Defendant and the Plaintiff*** *and the* ***holding out of the 1st Defendant as being also liable for payments*** *was for the convenience of the 2nd Defendant and in any case in addition to the liability of the 1st Defendant.*" [emphasis added]

Thus, the pleaded position of the Plaintiff was that the agreement is not only with the 2nd Defendant but with the 1st Defendant as well, as the 1st Defendant had undertaken the obligation of making payment for the services carried out by the Plaintiff, thus making both Defendants liable to the Plaintiff, jointly and severally. It must be stated that the Plaintiff did not claim that part of the contract had been novated in favour of the 2nd Defendant.

The position taken up by the 1st Defendant in its answer was of course a complete denial of liability with its position being that it only provided the necessary finances to the 2nd Defendant to enable the 2nd Defendant to make the necessary payments to the Plaintiff. The 1st Defendant alleged that Abeynayake, who had worked with Munasinghe on another project prior to assuming office as Chief Executive Officer of the 2nd Defendant, had colluded with the Plaintiff and committed the 2nd Defendant to certain obligations without the knowledge of the 1st Defendant. While a similar position has been taken by the 2nd Defendant in its answer, a claim in reconvention had also been made by the 2nd Defendant for the refund of the monies paid so far on the basis that the schematic drawings prepared by the Plaintiff, for which payment was being claimed by the Plaintiff, had not been accepted by the Defendants. The allegation of collusion has been denied by the Plaintiff in its replication, and remained unsubstantiated during the trial.

The principal issues between the parties

There are two principal issues that were raised at the trial by all parties which remains to be answered by this Court. The first is, was there an agreement between the 1st and/or 2nd Defendant/s on the one hand, and the Plaintiff, on the other?

In **Noorbhai v Karuppan Chetty** [27 NLR 325] it was held by the Privy Council that "… *the very elementary proposition of law [is] that a contract is concluded when in the mind of each contracting party there is a consensus ad idem* ..."

Weeramantry in "**The Law of Contracts**" [1967, Volume I, paragraph 84] has pointed out that the constituent elements of a contract can be reduced to the following basic essentials:

(a) Agreement between parties;

(b) Actual or presumed intention to create a legal obligation;

(c) Due observance of prescribed forms or modes of agreement, if any;

(d) Legality and possibility of the object of the agreement;

(e) Capacity of parties to contract.

Weeramantry goes on to state as follows:

> "*An agreement is a manifestation of mutual assent by two or more persons to one another. In simpler terms, therefore, an agreement would mean a state of mental harmony regarding a given matter between two persons, as gathered from their own words or deeds. Contract generally connotes among other things an actual or notional meeting of minds, for in general without such a meeting of minds a contract does not come into being. Agreement on the other hand, primarily denotes such meeting.* [paragraph 86]

The view is commonly held that in addition to the other requisites ***for the formation of a valid contract there should also be present, on the part of the parties, an intention to enter into legal relations****. It follows from this view that this requirement must be superadded to the fact of agreement if the agreement is to be productive of legal results.* [paragraph 158; emphasis added]

Whether two minds are in actual or real agreement not even the parties themselves can say for no man can fathom the thoughts of another; and in the realm of actual intention no man can speak for anyone but himself. ***The law consequently views the question of intention objectively****. Unable to plumb the depths of intention, it proceeds upon the external manifestations of such intention, whether by words or by deeds. From these external manifestations the law ascertains the presumed or notional intentions of parties.* [paragraph 86; emphasis added]

Agreement, which is so important to the formation of contract, depends in its turn on the intention of the contracting parties. The inner or true intention of a person is, however, not generally capable of ascertainment with any degree of assurance by another, if indeed it is capable of ascertainment at all. ***The law therefore always adopts an objective test in determining the intention of the parties to a contract****, and is guided by their manifestations of intention whether by words or by acts. From such words or acts it draws its inferences regarding intention on the basis of a reasonable person's assessment of them in the context in which they were uttered or performed.* [paragraph 104; emphasis added]

It would therefore be more correct to say that in all cases where the law requires an actual intention to enter into legal relations, what is required is either an intention which actually exists or one which, ***having regard to all surrounding circumstances, it will by a fiction deem to exist in the minds of the parties****."* [paragraph 158; emphasis added]

The second issue that needs to be answered in this appeal is whether the 1st and 2nd Defendants are jointly and severally liable towards the Plaintiff. Several liability arises when two or more persons make separate promises to another, whether by the same instrument or by different instruments. On the other hand, joint liability arises when two or more persons jointly promise to do the same thing, with their being only one obligation. Joint and several liability arises when two or more persons jointly promise to do the same thing and also severally make separate promises to do the same thing.

Relationship between the parties – *vide* the evidence

Munasinghe, having referred to the background facts that I have already referred to, has stated as follows in his affidavit which served as his evidence-in-chief:

a) Upon its incorporation, the 2nd Defendant acted on the offer reflected in P4 and proceeded with the Project subject to the terms and conditions specified in P4 and P5;

b) The 1st Defendant undertook the financial responsibility for the payments – vide P6 and P13 – although the agreement was formally to be entered into with the 2nd Defendant;

c) The 1st and 2nd Defendants agreed to be jointly and severally liable to the Plaintiff in respect of all monies due to the Plaintiff.

In cross examination, Munasinghe stated as follows:

a) The initial negotiations were with the 1st Defendant which was followed by an offer of services [P4 and P5] to the 1st Defendant;

b) The 2nd Defendant came into the transaction in addition to the 1st Defendant, as the 1st Defendant *wanted a separate company for the project*;

c) Accordingly, the 2nd Defendant was incorporated for the execution and implementation of the Project, as admitted by Senaratne in his affidavit;

d) After its incorporation, the Plaintiff corresponded with the 2nd Defendant as it was the intention of all parties that the 2nd Defendant too would be a contracting party. Accordingly, there is an agreement between the 2nd Defendant and the Plaintiff;

e) The work was carried out by the Plaintiff at the request of the 1st Defendant for the 2nd Defendant;

f) By making three payments to the Plaintiff, the 1st Defendant has accepted the terms and conditions of the offer that the Plaintiff had made to the 1st Defendant by P4 and P5;

g) The receipts for the payments however were issued in favour of the 2nd Defendant;

h) Even though there was no written agreement with the 1st Defendant, the 1st Defendant was nonetheless liable because it is the 1st Defendant who initiated the discussions, had negotiations with the Plaintiff, extended the promises and acted upon such promises by making the payments.

Viewed objectively, it is evident from the oral and documentary evidence that what had emerged was an agreement between the 1st and 2nd Defendants on the one side, and the Plaintiff on the other, thus giving credence to the position taken up by the Plaintiff that both Defendants are jointly and severally liable to the Plaintiff.

Relationship between the parties – *vide* the evidence of Senaratne

It would perhaps be relevant to refer to the affidavit of Senaratne at this stage. I must say at the outset that most of the matters averred in the said affidavit, especially as to the discussions that took place during February to April 2006 between the directors of the 1st and 2nd Defendants and the Plaintiff and what transpired at such discussions were not suggested to Munasinghe in cross examination, thereby reducing the evidentiary value of Senaratne's affidavit.

The fact that the 2nd Defendant was incorporated for the sole purpose of the Project is made clear by Senaratne's statement that, "*in the month of December 2005, steps were taken to incorporate the 2nd Defendant to engage in the development of this land by constructing a Condominium Building thereon and selling or leasing Condominium units therein to prospective buyers and lessees.*"

I am of the view that the transaction that took place between the parties must be viewed from the perspective of the above explanation of Senaratne. When a company already in existence is keen to commence a new project and takes on the role of the promoter, an option that is open to the promoter of the new project would be to incorporate a separate corporate entity with limited liability for that project, thus making the newly formed entity a special purpose vehicle. Quite apart from separating or isolating the entity to be formed from the existing promoter entity for commercial and financial reasons, and gaining the advantage that a limited liability company with a separate legal personality has to offer, considerations of tax benefits and fiscal concessions for entities engaging in specific kinds of activity too demand that the activity relating to the new project be kept separate.

However, on the other side of the table is an entity – the Plaintiff in this case – who is entering into the transaction on the financial strength of the already existing promoter company and which therefore seeks some form of comfort from the promoter in order to ensure that payments are made for the services provided. It is therefore important that these transactions are structured properly with the rights and liabilities of each party correctly identified. Unfortunately, in this appeal, that has not been done, with the result that:

(a) the evidence, similar to pieces of a jigsaw have to be put together by Court to form the complete picture and determine the intention of the parties; and

(b) for reasons to which I have already adverted to and shall advert, both Defendants have exposed themselves to liability.

In his affidavit, Senaratne, for the first time stated as follows:

(a) P4 and P5 were unsolicited proposals;

(b) The parties were only having preliminary discussions to explore the possibility of the 2nd Defendant employing the Plaintiff as architect for the Project;

(c) There were no dealings whatsoever between the Plaintiff and the 1st Defendant;

(d) The Plaintiff did not submit a detailed Project proposal acceptable to the 2nd Defendant;

(e) No firm contract was entered into between the Plaintiff and the 2nd Defendant for the employment of the Plaintiff as the architect.

I must say that the above, quite apart from not being suggested to Munasinghe during cross examination, was contrary to the documentary and oral evidence that the Plaintiff had already placed before the Commercial High Court.

Senaratne has stated further that:

> "***We advised the Plaintiff*** *that in the event the Plaintiff company being in fact employed as Architect,* ***the related contract would be between the Plaintiff and the 2nd Defendant*** *which was then under incorporation and would not be between the Plaintiff and the 1st Defendant as the 2nd Defendant was to be responsible for all aspects of the Project and the 1st Defendant was unconnected with the Project and was engaged in an entirely different field of business.*"
>
> "***Although the Plaintiff and the 2nd Defendant had discussions regarding the 2nd Defendant employing the Plaintiff as architect****, no firm agreement or contract was entered into by which the 2nd Defendant in fact employed the services of the Plaintiff as architect. "* [emphasis added]

Although Senaratne took great pains to explain that the 1st Defendant had no liability towards the Plaintiff, he was confronted by the fact that not only had an assurance of payment been made by the 2nd Defendant on behalf of the 1st Defendant but that payments had in fact been made by the 1st Defendant. Even if his explanation that, "*as the 2nd Defendant was pending incorporation at that stage, the payment was lent and advanced to the 2nd Defendant by the 1st Defendant and the cheque in payment was issued by the 1st Defendant*" could be accepted for the first payment in January 2006, it cannot be accepted for the balance two payments as the 2nd Defendant had been incorporated by then. Thus, in my mind, the 1st Defendant had contractually bound itself to the Plaintiff by making all three payments.

Referring to the payments made to the Plaintiff, Senaratne has stated as follows:

> "*The payments aggregating Rs. 4.5 million* ***made by the 2nd Defendant*** *to the Plaintiff* ***were by way of an advance payment to cover the cost of preliminary work*** *said to have been done by the Plaintiff such as the initial project appraisal and the cost of preliminary studies on the obtaining of the necessary approvals from the Urban Development Authority and the Colombo Municipal Council and liaising with these two authorities and the checking of the electricity, water and sewerage connections etc. which were to be carried out by the Plaintiff.*"
>
> "*No agreement was reached for the appointment of the Plaintiff as the architect and no agreement was reached as to the fees that were payable to the Plaintiff other than the* ***aforesaid Agreement for the 2nd Defendant to pay the Plaintiff a sum of Rs. 4.5 million to cover the cost of preliminary work*** *said to have been done by the Plaintiff.*" [emphasis added]

It is clear to me that Senaratne was blowing hot and cold. On the one hand, he states that there was no agreement at all with the 2nd Defendant and on the other he admits that payment was made to cover the cost of preliminary work carried out by the Plaintiff but adds a rider by saying that the work was *said to have been done* by the Plaintiff. None of these explanations were made at the time payment was demanded in writing nor were these matters suggested to Munasinghe during cross examination.

Failure to respond to business correspondence

Mr. Alagaratnam, PC has invited this Court to draw an adverse inference against the 2nd Defendant for its failure to respond or deny the contents of the letter of demand [P21] or for that matter, most of the other letters sent, although the receipt of such letters was admitted by Senaratne.

In **The Colombo Electric Tramways and Lighting Co. Ltd v Pereira** [25 NLR 193 at page 195], Jayawardena, A. J, quoted with approval the following dicta of Lord Esher in **Wiedeman v Walpole** [(1891) 2 Q. B. 534], which has been cited in many later cases:

> "*Now there are cases – business and mercantile cases – in which the Courts have taken notice that, in the ordinary course of business, if one man of business states in a letter to another that he has agreed to do certain things, the person who receives that letter must answer it, if he means to dispute the fact that he did so agree. So, where merchants are in dispute one with the other in the course of carrying on some business negotiations, and one writes to the other, "but you promised me that you would do this or that," if the other does not answer that letter, but proceeds with the negotiations, he must be taken to admit the truth of the statement*."

Dias, J in **Saravanamuttu v De Mel** [49 NLR 529 at page 542] held that, "*In business matters, if a person states in a letter to another that a certain state of facts exists, the person to whom the letter is addressed must reply if he does not agree with or means to dispute the assertions. Of course there are exceptions to this rule. For example, failure to reply to mere begging letters when the circumstances show that there was no necessity for the recipient of the letter to reply can give rise to no adverse inference against the recipient*."

Having considered *inter alia* the above cases, my brother, Justice Samayawardhena has stated as follows in **Disanayaka Mudiyanselage Chandrapala Meegahaarawa v Disanayaka Mudiyanselage Samaraweera Meegahaarawa** [SC Appeal No. 112/2018; SC minutes of 21st May 2021]:

"*However, I must add that although it is a general principle that failure to answer a business letter amounts to an admission of the contents therein, this is not an absolute principle of law. In other words, failure to reply to a business letter alone cannot decide the whole case. It is one factor which can be taken into account along with other factors in determining whether the Plaintiff has proved his case. Otherwise, when it is established that the formal demand, which is a sine qua non for the institution of an action, was not replied, Judgment can ipso facto be entered for the Plaintiff. That cannot be done. Therefore, although failure to reply to a business letter or a letter of demand is a circumstance which can be held against the Defendant, it cannot by and of itself prove the Plaintiff's case. The impact of such failure to reply will depend on the facts and circumstances of each case*."

I am in agreement with Samayawardhena, J and wish to reiterate that the failure to respond to a business letter must not be looked at in isolation of the other facts and that its impact would depend on the facts and circumstances of each case. Having said so, I am in agreement with the learned President's Counsel that this Court is certainly entitled to draw an inference against both Defendants arising from their failure to deny the existence of a contract with the Plaintiff to provide consultancy services upon receipt of the several letters referred to earlier. I am therefore of the view that the Defendants cannot deny that the Plaintiff in fact provided the relevant services, thus requiring this Court to consider whether the Defendants are jointly and severally liable to make payment for the said services.

Judgment of the Commercial High Court

The learned Judge of the Commercial High Court, having taken into consideration the following circumstances of this case, concluded that the 1st Defendant is the *alter ego* of the 2nd Defendant and thereby the 1st Defendant is liable to the Plaintiff:

(a) The initial discussions were with the 1st Defendant;

(b) The invitation to submit bids was extended by the 1st Defendant;

(c) The directors and shareholders of both the 1st and the 2nd Defendant are identical;

(d) The land on which the Project was to be implemented belonged to the 1st Defendant;

(e) P6 was prepared by Abeynayake in consultation with the Directors of the 1st Defendant who later became the shareholders of the 2nd Defendant and took up appointment as directors of the 2nd Defendant;

(f) At the time P6 was written, the 2nd Defendant was yet to be incorporated and the acceptance of P4 and P5 by Abeynayake who had been appointed by the 1st Defendant as the Chief Executive Officer of the company that was to be incorporated is binding on the 1st Defendant;

(g) By P6, it was represented to the Plaintiff that the payment obligation has been undertaken by the 1st Defendant which was the only existing entity at that time and the payments were in fact made by the 1st Defendant, even after the incorporation of the 2nd Defendant.

I must add to the above list, the fact that, (a) the negotiations prior to and post P4 and P5 were with the 1st Defendant; (b) P17 and P18 by which payments were demanded from the 2nd Defendant were acknowledged by the 1st Defendant.

Lifting of the corporate veil

The learned President's Counsel for the Plaintiff did not seek to argue before us that the 2nd Defendant would be liable simply in view of the above conclusion of the Commercial High Court, and hence, the necessity for me to consider if the said conclusion is correct does not arise. I must however state the obvious. A limited liability company is a separate legal entity, has an existence of its own and is organised to do business in its own right. Each such entity has legal rights and liabilities distinct from its shareholders and the corporate veil between them would not be disturbed lightly.

Of course, there are circumstances where the corporate form will be disregarded and the corporate veil will be pierced to hold individual officers or shareholders personally liable for the acts of the corporate. In '**Gower's Principles of Modern Company Law**' [supra; at page 198], the authors, having stated that, "*When analysing the judicial decisions on lifting the veil, it is crucial to distinguish between those situations where the court is applying the terms of a contract (other than legislation relating to companies) or, less often, a contract, from those where, as a matter of common law, the veil is lifted. The reason is that the justification for lifting the veil in the former group of cases is to be found in the wording of the statute or the contract*," proceeded to state as follows [at pages 205 and 206]:

> "*The doctrine of lifting the veil plays a small role in British company law, once one moves outside the area of particular contracts or statutes. Even where the case for applying the doctrine may seem strong, as in the under capitalised one-person company, which may or may not be part of a larger corporate group, the courts are unlikely to do so. As Staughton LJ remarked in Atlas Maritime Co SA v Avalon Maritime Ltd, The Coral Rose [1991] 4 All ER 769 at 779*:
>
> > "*The creation or purchase of a subsidiary company with minimal liability, which will operate with the parent's funds and on the parent's directions but not expose the parent to liability, may not seem to some the most honest way of trading. But it is extremely common in the international shipping industry and perhaps elsewhere. To hold that it creates an agency relationship between the subsidiary and the parent would be revolutionary doctrine*."

The above passage from Gower and Davies, albeit from the 8th edition, has been quoted by Saleem Marsoof, PC, J in **DFCC Bank v Weliwita Don Kushmitha Mudith Perera** [SC Appeal No. 150/2010 – SC minutes of 25th March 2014]. Merely because one company is a parent and another is its subsidiary does not mean that their rights and liabilities – and their fates – are inextricably intertwined in law. And, to introduce a wide and easily accessible route, via which the distinctness in corporate personalities between the parent and the subsidiary can be flouted, would be to shake the very foundations of company law. This does not mean, however, that by virtue of being separate corporate entities, an

impassable gulf exists between the parent and the subsidiary. In exceptional circumstances, our Courts are indeed empowered to lift and/or pierce the veil of incorporation, and have done so in the past, though of course cautiously. It bears repeating therefore that it would be a rare occasion indeed for the veil to be lifted and/or pierced.

The factual circumstances – revisited

While reiterating the aforementioned factual matters relied upon by the learned Judge of the Commercial High Court as to why the 1st Defendant is liable to the Plaintiff, the learned President's Counsel for the Petitioner submitted that the 2nd Defendant too must be held liable for the reason that (a) the work was to be performed for the 2nd Defendant; (b) the contract was for the benefit of the 2nd Defendant; (c) the 2nd Defendant too has extended promises to the Plaintiff; and (d) therefore the contract was not only with the 1st Defendant but with the 2nd Defendant, as well. In other words, his position was that there was a clear intention on the part of all parties to create legal relations in respect of the Project which gave rise to a contract where both Defendants are jointly and severally liable to the Plaintiff.

It would be well at this stage to recapitulate the factual circumstances in order to decide whether there existed an agreement with the 1st and 2nd Defendants on the one hand, and the Plaintiff on the other. The starting point of course would be the initial discussions held in December 2005 between the Plaintiff and the 1st Defendant, with the 1st Defendant being represented by its two directors and shareholders, namely Senaratne and Perera, and Abeynayake who became the Chief Executive Officer of the 2nd Defendant a few days later.

The discussions were followed by the initial proposal of the Plaintiff [P4 and P5] made to the 1st Defendant. In my view, P4 and P5 fortify the position of the Plaintiff that they had discussions with the 1st Defendant and were invited to submit its proposal. This is followed by the 1st Defendant making the first payment of Rs. 1,500,000 [D5], which was prior to the incorporation of the 2nd Defendant. Thus, the cumulative effect of the above is the

intention of the 1st Defendant to enter into an agreement with the Plaintiff for the provision of consultancy services for the Project.

The '*entry*' of the 2nd Defendant to the transaction takes place on 6th January 2006 by P6. Although not incorporated as at that date, P6, which according to Abeynayake was prepared in consultation with Senaratne and Perera, is signed by Abeynayake on behalf of the 2nd Defendant and not only refers to and accepts P4 and P5 but seeks to appoint the Plaintiff as the Consultant for the provision of a Consortium service for the Project on the terms and conditions set out in P4 and P5 and provides a specific assurance that payments would be made by the 1st Defendant, with a payment of Rs. 1,500,000 being made almost simultaneously. While P6 does not make the 2nd Defendant liable for the reason that the 2nd Defendant was not incorporated as at that date, it certainly gives context to the intention of the parties to have the 2nd Defendant involved in the entire transaction.

The next document after P6 is P9 dated 24th January 2006, by which the Plaintiff forwarded the Preliminary Construction Cost Estimate to Abeynayake, with the 1st Defendant being referred to as the client. The incorporation of the 2nd Defendant followed two days thereafter on 26th January 2006.

The next two letters are crucial. The first is letter dated 24th February 2006 [P12] addressed to Abeynayake in his capacity as the Chief Executive Officer of the 2nd Defendant. By P12, the Plaintiff requested the 2nd Defendant to pay a sum of Rs. 3,400,000, which was the balance sum of money outstanding on the advance payment of 10%. Thus, by P12, the Plaintiff acknowledged the presence and involvement of the 2nd Defendant in the transaction. What followed thereafter – P13 – cements the contractual involvement of the 2nd Defendant for the reason that the 2nd Defendant not only confirmed that the payments are in order but also stated that "…*our directors, Mr. Sanjeeva Senaratne and Mr. Suminda Perera have approved and* ***agreed to release the balance money from Neat Lanka (Pvt) Limited****, as soon as possible...*". Thus, P13 confirms the position of the Plaintiff that there existed an agreement between the parties with both Defendants promising to do the same thing.

Pursuant to P13, the 1st Defendant continued to make two further payments by cheques drawn on its account [D8 on 20th March 2006 and D9 on 27th March 2006], even though the 2nd Defendant had been incorporated by then and payments were called from the 2nd Defendant. The explanation of Senaratne was that even though it is the 1st Defendant that made the payments, it was only a loan made to the 2nd Defendant. While this confirms that the services were being performed for the 2nd Defendant, it must be noted that the payments were made directly by the 1st Defendant to the Plaintiff and not through the 2nd Defendant. Thus, the position is that the work was carried out for the 2nd Defendant, with the invoices and receipts issued to the 2nd Defendant and for payments to be made by the 1st Defendant.

Conclusion

Based on the above discussion, it is clear to me that both the 1st Defendant and the 2nd Defendant have been present on one side of the table and made separate promises to the Plaintiff but with the same objective – i.e., to contract the Plaintiff to provide consultancy services for the Project. Adopting an objective test, the promises the Defendants had made to the Plaintiff through the entire course of the transaction point to the two of them acting together. This being so, the liability must surely fall on both of them, not just on the 1st Defendant.

The learned Judge of the Commercial High Court has appreciated the fact that the evidence was sufficient to hold the 1st Defendant liable. It appears from the answers given by the learned Judge of the Commercial High Court to the issues raised by both parties that he was of the view that the 2nd Defendant too is liable. This is borne out by the answers given to Issue Nos. 3, 4, 9 and 10 raised by the Plaintiff and issue No. 19 raised by the Defendants, as set out below.

Issue No. 3 – Was there a written agreement between the 1st and the 2nd Defendants and the Plaintiff? – P6 න් P13 න් හා ගෙවීම් කිරීමෙන් ගිවිසුම්ගත පැවැත්ම සංස්ථාපනය වේ.

Issue No.4 – Are the 1st and 2nd Defendants liable jointly and severally under the said Agreement? පෙනි යන ගිවිසුම අනුව මුදල් ගෙවීමේ වගකීම 1 වන විත්තිකරු වෙතය. ඒ අනුව 1 විත්තිය වග කිව යුතුය.

Issue No. 9 – Has a cause of action arisen to the Plaintiff to sue the Defendants jointly and severally for the recovery of Rs. 10,200,000? ඔව්. නඩු පැවරීමට නඩු නිමිත්තක් පැනනැගී ඇත. ගෙවීමේ වගකීම 1 විත්තිය වෙතය.

Issue No. 10 – If one or more of the above issues are answered in favour of the Plaintiff, is the Plaintiff entitled to the relief prayed for? ඔව්. ගිවිසුම්ගත බැඳීම් අනුව එය ගෙවීමට බැඳෙන්නේ 1 විත්තිය වේ.

Issue No. 19 – Did the Plaintiff and the 2nd Defendant not enter into the purported contract claimed by the Plaintiff? ගිවිසුමකට ඇතලු වූ බව සාක්ෂි අනුව පෙනේ.

However, the learned Judge of the Commercial High Court has failed to undertake a closer look at the liability of the 2nd Defendant and appears to have overlooked the fact that the 2nd Defendant is liable. It is on this point alone that the learned Judge of the Commercial High Court has erred in an otherwise correct and exhaustively analysed judgment.

Taking into consideration the totality of the above circumstances, I am of the following view:

(a) The findings of the learned Judge of the Commercial High Court in respect of the 1st Defendant are correct and therefore are affirmed;

(b) The learned Judge of the Commercial High Court erred when he failed to consider that the 2nd Defendant too has made promises to the Plaintiff and that the correspondence establish that the 2nd Defendant and the Plaintiff had an intention to create legal relations in respect of the work performed by the Plaintiff in respect of the Project, and the 2nd Defendant is therefore jointly and severally liable towards the Plaintiff;

(c) The learned Judge of the Commercial High Court erred in law when he failed to answer Issue Nos. 4, 9 and 10 in favour of the Plaintiff against the 2nd Defendant. The said three issues are accordingly answered in favour of the Plaintiff and the Plaintiff shall be entitled to relief as prayed for in the plaint against the 2nd Defendant, as well.

The Commercial High Court is directed to enter decree accordingly.

I make no order for costs.

JUDGE OF THE SUPREME COURT

Vijith K. Malalgoda, PC, J

I agree.

JUDGE OF THE SUPREME COURT

Mahinda Samayawardhena, J

I agree.

JUDGE OF THE SUPREME COURT