ULTRA VIRES DOCTRINE IN COMPANY LAW: TRULY BEATEN, BUT NOT DEAD

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INTRODUCTION

The Ultra Vires rule represents perhaps one of the most important and enduring contribution of common law in the regulation of registered Companies. Following from the principle that a company is incorporated basically to carry on the objects laid down in its Memorandum of Association otherwise known as the main 'objects' or the 'subtraction', that is to say the company cannot act outside its purposes or objects for which it was created or exceed its powers. A registered company must therefore according to this rule confine itself within its permissible activities as provided in its memorandum of association. Where a company acts outside its business i.e. its stated purposes or objects or exceed its powers, such act is regarded as Ultra Vires.

The Ultra Vires doctrine has come a long way in company law and the long jurisprudential journey has apparently taken its toll. There have been general dissatisfaction with the Ultra Vires concept which necessitated legislatures in several jurisdictions to succumb to the calls for reform of law in this area. In the form which the Ultra Vires concept appears in Nigerian Company law it has undergone some remarkably welcome and salutary changes under the Companies and Allied Matters Act, 1990. Some opinions have however been expressed to the effect that the Ultra Vires doctrine has been abolished or killed completely by CAMA. This

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Ilaper seeks to show clearly that even though the Ultra Vires doctrine has been truly beaten by the recent provisions of CAMA, it is not completely dead after all and can still be invoked in appropriate cases to protect shareholders and check the excesses of directors. We must however first take care of preliminary matter - on this rather topical issue.

Development OTTS - Ultra Vires Doctrine

It is generally believed that the Ultra Vires doctrine was established in the SUTTON'S HOSPITAL case. According to Professor Gower:

"That case has generally been taken to establish that a chartered corporation has all the powers of a natural person insofar as an artificial entity is capable of exercising them; if it misuses its powers by exceeding the objects in the charter, it may be that proceedings in the nature of quo warranto could be taken to restrain it"

However, the first authoritative pronouncement on the point was made by the House of Lords in Ashbury Railway Carriage & Iron Co. v. Richie. In that case, a Company had been formed under the 1862 Companies Act with objects which permitted it "to make, buy and sell, or lend or hire railway Carriages and Wagons and all kinds of railway plant ... for the use of the business of mechanical engineers and general contractors", the directors entered into a contract to finance the construction of a railway in Belgium. The company received advice that the agreement might be Ultra Vires, but it was later ratified by all the members. The company subsequently repudiated the contract. The question was whether
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The company was bound by the contract. The House of Lords held that the contract was Ultra Vires the company; that the financing of the construction of a railway in Belgium cannot be brought within any of the objects. The Court stated that the contract was void ab initio and not even the unanimous consent of all the members of the company in, eral meeting could validate or ratify an Ultra Vires contract.

The Ultra Vires doctrine has been adopted and applied in decided cases in Nigeria. In Continental Chemists Ltd v. Dr. Ifekandu, the Supreme Court declared that a contract outside the objects of an incorporated company is Ultra Vires, invalid and unenforceable. In Metalimpex v. Leventis and Co., Nigeria Ltd, the court held that where the contract is Ultra Vires the company, neither the company or the other party can enforce it. And in Okoya and others v. Santilli and Others, the court stated that a company conducting its affairs otherwise than on the basis of its true memorandum and articles of association acts Ultra Vires.

Lord Cairns, L.C. in Asbury's Case explained the rationale for the application of the Ultra Vires rule to companies. First, it was meant to provide protection for investors so that they might know the objects for which their money was to be employed. Secondly, it would protect creditors of the company by ensuring that the company's fund to which alone they could look for payment, are not dissipated in unauthorized activities. In addition, the rule helps to control the powers of directors in relation to the internal management of the company. The court according to a commentator, saw the Ultra Vires rule both as the price incorporators should pay for privilege of being allowed to trade with limited liability and as a means of providing protection for the investor and public against the abuse of that privilege.

Subsequently, however, the courts realized that the rule operated to the detriment of third parties dealing with the company. The House of Lords realized that its ruling in the Asbury's case had been draconian. Thus a slight modification or mitigation of the rule was done in Attorney-General v. Great Eastern Railway Co, where the House of Lords relaxed the rule by recognizing that a company could exercise any implied powers which were reasonably incidental to the carrying out of its express objects. Apparently this decision did not completely take out the sting from its original ruling and flashes of the harsh application of the rule continue to vibrate.

5 (1966) 1 ALL NLR 1
6 (1976) 1 ALL NL.R(P+1) 94
7 (1990) 2 NWLR (P+ 131) 172
8 Asbury's Case (1875) L.R. 71 U. 653 667.
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Defects of The Ultra Vires Rule

According to Professor Gower (p. 165) at the beginning, the intention of the Ultra Vires rule was indeed salutary for the protection of creditors and shareholders. At the time it prevented trafficking in company registrations, 

an investor in a gold mining company did not find himself holding shares in a fried-fish shop. Unhappily it was capable of causing hardships as great as those which it prevented.

In practice the Ultra Vires rule failed to provide effective protection for the investor. By subscribing to a strict rule of nullity, the court rendered the purported protection of the shareholder illusory. Members are not allowed to change to new objects even when the main objects have failed and the company is facing threat of liquidation neither can they validate any transaction which may be advantageous to the company even though Ultra Vires.

The Ultra Vires doctrine also worked great injustice to the company since an Ultra Vires contract was void ab initio-in capable of giving rise to legal rights and therefore incapable of enforcement by either the company or third parties. Third parties have therefore evoked the doctrine that escape liability to the company. A company can’t recover where the act is Ultra Vires. That a stranger could rely on the doctrine sought to protect is bad. For instance in CONTINENTAL CHEMIST LTD V. DR. IFEKANDU (15), notwithstanding that the tile doctor had undertaken to work for 5 years in return for the company undertaking to give him money the contract was null.

Invasion Of The Ultra Vires Rule

Even though a slight modification or mitigation of the rule was provided in the case of A-G.V. Great Eastern Railway (17) to cover incidental powers necessary for executing the company’s objects, it still worked hardship and continued to echo.

14 LCB Gower, op. cit. p. 165

15 (1966) 1 ALL NLR 1

17 (1880) 5 APP. Cas, 473 H/L
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To avoid the harsh effects of the rule, therefore, Company promoters resorted to various devices to evade the Ultra Vires rule.

1. Proliferation of Objects
The first of these devices was the proliferation of objects clauses by s.v.-cieri ng every conceivable object, far wider than they will ever accomplish. The result was that instead of succinct objects clause, there were found objects running to more than 20 paragraphs. The courts reacted to this practice by adopting the main object rule of construction whereby in construing the memorandum the ejusdem generis rule is applied to located the main or dominant object of the company for which the members subscribed their money and treat all the other paragraphs, however generally expressed as ancillary to this main object. The main object is taken as the substratum or basis of existence of the company. If the main object fails then its whole substratum is said to have disappeared and anything done by the company in such circumstances would be Ultra Vires! In the case of RE GERMAN COFFEE DAYE the company's objects were to work a German patent for manufacturing coffee from dates, to obtain and work other inventions for that or similar purposes and to import and export all descriptions of food products. The German patent was not granted but the company bought a Swedish patent and manufactured coffee from dates in Germany without a patent. The company was quite solvent and majority of members wishes to continue. But on a petition by two shareholders it was held that the substratum had failed and since the company could not attain its main object it was just and equitable to wind it up.

20 (1918) A.C. 514 HL
21 (1966) 2 Q.B. 656 C.A.

R S. German Date Coffee Co (1882) Ch.D. 169.

See also Re Crown Bank (1890) Ch.D. 634

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3. The Subjective Objects Clause - Bell Houses Clause
A further device used in the evasion of Ultra Vires doctrine was the practice of including in the objects clause a provision for the carrying on of any business which the company or directors think fit. A typical is as follows:

"To do all such other thing as are incidental or condu ctive to the attainment of the objects specified or any of them"

In Bell Houses Ltd v City Wall Properties Ltd 1 (1966) 2 Q.B. 656 C.A. The court accepted the validity of subjective clauses without qualification. In that case the main object of the Plaintiff company was the development of Housing Estates, but one of the inflated objects authorized it:

"to carry on any other trade or business which can ill the opinion of the Board of Directors be advantageously carried on by the company in connection with or as ancillary to any of the above businesses or the general business of the company."
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The company through its chairman entered into a mortgage brokerage agreement with the defendant. The defendant refused to pay the amount charged and argued that the contract was Ultra Vires the plaintiff company.

But the court held that the clause was valid and effective to empower the company to undertake any business which the bonafide believed could be advantageously carried on an adjunct to its other business.

However, the Supreme Court of Nigeria has occasion to construe a similarly worded objects clause in Continental Chemists Ltd V. Dr. Ifekandu and held that the clause was indefinite and useless". The clause in question stated that the company can enter into any business which the directors think will increase the profits of the company...

This was the position of the law before CAMA introduced some reforms. As noted by Gower (165-169) the result of the foregoing practices was largely to frustrate the whole object of the doctrine. It ceased to be a protection to anyone and became merely a trap for the unwary third party and a nuisance to the company itself.

Reform Of The Ultra Vires Rule Under C.A.M.A

The problem or to put it more realistically the hardship and injustice created by the rigid application of Ultra Vires rule forced many common law jurisdictions to find ways to mitigate the harsh consequences of the doctrine". Indeed the Companies and Allied Matter Act has severely decapitated the Ultra Vires rule and stripped it of its sting and hardship.

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though the doctrine is still recognized and preserved in the interest of corporate activities, like in many common law jurisdictions 4

Section 39 (1) of CAMA is retaining the rule provides thus:

"A company shall not carry on any business not authorized by its memorandum and shall not exceed the powers conferred on it by its memorandum itself."

Section 39 (1) gives the company the powers of a natural person of full majority for the furtherance of its authorized business or objects, unless its memorandum or any law provides otherwise. This definitely does not mean that the company is thereby authorized to do all business which a natural person may do. The powers conferred on it are still only for the purpose of the stipulated objects and no other. As Dr. Orojo further explained the simple implication of this provision therefore is at any powers exercised by the company will be Ultra Vires if such powers were not exercised

"or the furtherance of its authorized business or objects"

Section 39 (2) strengthens this retention by providing for the protection of the rule in proceedings in court under sections 300-313 i.e for protection of minority shareholders against oppression or under subsection 4. The sub-section 4 shows clearly that this retention is only as an internal doctrine namely to enable any member or holder of any debenture secured by a floating charge to restrain the company from engaging in any unauthorized business or object or otherwise exceeding its powers. The section provides thus:

23 Both the Coehn Committee and Jenkins Committee in

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The Nigerian Law Reform Commission considered the reform of the doctrine in England, Canada, Ghana and the Caribbean and expressed a preference for the approach adopted in Canada, Ghana and the Caribbean.
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"Oil the application of (a) any person of the company; or (b) the holder of any floating charge over any part of the company's property, or by the trustees of holders of any debentures, the court may prohibit by injunction, the doing of any act or the conveyance or transfer of any property ill breach of subsection (1) of the Ultra Vires doctrine.”

However, section 39 (3) in eliminating the mischief, hardship and nuisance value of the doctrine provides that:

"Notwithstanding the provisions of subsection (1) of this section, [no act of a company and no conveyance or transfer of property to or by a company shall be invalid by reason of the fact that such act, conveyance or transfer was made or made for the time being of any contract the authorized business of the company or that the company was otherwise exceeding its objects or powers”.

Thus by the provisions of section 39 (3) the common law position that a contract which is Ultra Vires is void has been reversed. Ultra Vires acts are no longer void but valid and enforceable, Section 39 (3) depicts an apparent abolition of the Ultra Vires doctrine. This is also strengthened by the provisions of section 65 (6) to the following effect:

"If a business is being carried on by the company, the company shall not escape liability for acts undertaken in connection with that business merely because the business in question was not among the business authorized by the company’s memorandum.”

It is worthy of note however that what section 39 (3) preserves is an executed contract or transaction. Any transaction which is executory is not protected.

Section 39 (5) provides that the holder of a debenture secured by a floating charge and a member who has not voted for the Ultra Vires contract may apply to set the contract aside. If the court exercises its power to set
the transaction aside, compensation may be allowed for any loss. However, no compensation will be awarded in respect of loss of anticipated profits. This provision will ensure that a situation where a party to an Ultra Vires transaction loses everything will no longer arise. Consequently, Continental Chemists Ltd V. Dr. Ifekandu and related cases are no longer a win Nigeria.

A backbone of the Ultra Vires doctrine which is the doctrine of constructive notice has also been abolished under section 68 of the Act. This was a situation where third parties were presumed to know the contents and requirements of the company’s memorandum and Articles of Association.

With the abolition of the doctrine of constructive notice of registered documents coupled with section 39 (3) and sections 65, 66, 67 and 70 of the Act (which makes the company vicariously liable in civil and criminal law for the acts of its organs) the Ultra Vires doctrine remains of probative value only.

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CONCLUSION

The Ultra Vires doctrine, certainly, is truly beaten, it bleeds but it is not dead after all. As we have seen the deliberate erosion of the effectiveness of the Ultra Vires doctrine, as applicable to companies is that, the doctrine is regarded as a nuisance to both companies and third parties who enter into business transactions with a company in good faith. It is also considered unrealistic to expect that everyone who deals with a company has or is deemed to have constructive notice of what is in the Company's memorandum. It is therefore not surprising that section 68 of the CAMA 1990 has abolished the doctrine of constructive notice of the contents of the memorandum of a registered company, all in the bid to protect investors and create a conducive atmosphere for business.

Finally, it must be noted that whatever arguments writers have against the Ultra Vires, it is still one of the most important principles of company law, and a dependable tool for the protection of shareholders and for defining the limits of the activities of a company, as well as the powers of directors.

INTRODUCTION

As the earth now threaten sustainability, the need to devise how to prevent and resolve issues becomes more prevalent. In conventions mental law mechanisms are engaged.

Also, the institution of the memorandum of a company is crucial. It serves as a tool to protect investors and create a conducive atmosphere for business.