Comparative Analysis of the Evolving Status of *Ultra Vires* under Company Law and Practice

Peter K. Enimola*

1. Introduction

Ultra Vires is a Latin expression used to describe acts undertaken beyond the legal powers of those who have purported to undertake them.[1]The *ultra vires* rule enjoins a company from undertaking acts not expressly or impliedly authorized by its constitution[2] as well as the law. Companies, being essentially creations of law, are governed for the most part by the law, now largely of common law origin and statutory derivation.[3] An important component, nevertheless, of the ordering of relationships within the company is still said to be the contract.[4] While statutes increasingly intervenes to regulate the minutiae of corporate life, company lawyers still speak in terms of the nexus of contracts that form the corporate environment and govern its affairs.[5] Where statute is silent, reference may often be made to the pacts and agreements that surround the company and that determine the extent to which members of the company may enforce dealings with each other.[6] As the company's constitution is often the reflection of the private contract between its founding shareholders and the basis of future contracts between the company and aspiring investors, this

* Peter K. Enimola, LL.M, BL, Doctoral candidate, University of Aberdeen, UK.

1 K. Aina: "*Ultra Vires* Doctrine is Dead," (2004) *University of Ibadan Journal of Private and Business Law* Vol. 4, p. 18; *Gower's Principles of Modern Company Law*, (6th edn.), (London: Sweet and Maxwell, 1997), p. 202.

2 D.A. Obadina: "The New Face of *Ultra Vires* and Related Agency Doctrine in the Commonwealth and USA," (1996) *Lawyers' Bi-Annual Journal of Nigeria and Comparative Law.* Vol. 3, No. 1, June. p.22.

3 P.J. Omar: "Powers, Purposes and Objects: The Protracted Demise of the *Ultra Vires* Rule", Available at: http://epublications.bond.edu.au/cgi/view content, visited 21/02/2011.

4 See P. Ireland: "Property and Contract in Contemporary Corporate Theory", (2003) 23 *LS*, 453.

5 Omar, *loc. cit.,* note 3 above.

6 *Ibid.*

question straddles the divide between private ordering and public intervention through regulation.

Hence, there was need for investors to be assured that the company was being run according to its constitution or memorandum and articles of association and thus in line with what they had expressly authorized. The best way of achieving this was to limit the boundaries of corporate activity through stipulating objects or purposes, so that activity deviating from these purposes could be challenged through the imposition of duties and sanctions for failure to observe them. Subscribers at formation would be able to control this process because of the requirement that they signify their assent to the constitutional documents through signing the memorandum.[7] With respect to future participants, this process becomes useful as it assists in identifying, in advance of any contract, whether the purpose of company matches the investment requirements of the prospective shareholders.[8]

It is from the foregoing that the doctrine of *ultra vires* comes to play. Over the years, the courts and statutes have played roles in the existence of the doctrine. This paper therefore, shall critically examine the origin of the doctrine of *ultra vires*, its justification, defects, the doctrine of constructive notice and its abolition, attempted evasion of *ultra vires*, the application and reform of *ultra vires*, etc. from a global and comparative perspective.

2. Historical Evolution of *Ultra Vires*

It is said that chartered companies were regarded as enjoying the same legal capacity as the adult at common law.[9] Put differently, at one stage, it was thought that on the analogy of chartered companies, registered companies were immuned from the *ultra Vires* rule.[10] In theory, they were unfettered as regards their transactions, even in areas

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7 *Ibid.*

8 *Ibid.*

9 See H. Rajak: "Judicial Control: Corporations and the Decline of Ultra Vires," (1995) 26 *Camb. LR.*, 9 at p. 12, citing the case of Sutton's Hospital (1612) 10 Co. Rep. 1a, 23a.

10 Obadina, *loc. cit.* at p. 1

not expressly authorized by the charter, although they ran the risk that the Crown, displeased by an abuse of this concession, could act so as to revoke the charter.[11] The provisions of the statutory model changed matters in so far as the exercise of restraint was concerned. Commentators are united in agreeing that statutory companies came into being at a time of great economic fever, when the laying down of infrastructure works in the shape of canals, railways, roads and services meant that there was a real risk of substantial infringement of private rights, notably the possibility of expropriation of property, which often occurred for the purposes of carrying out these great projects.[12]

Statutory companies were comparatively rare until the Railway Mania of 1845.[13] However, judgments in the wake of the explosion in their numbers demonstrated that the courts would examine the statutes creating these companies so as to ensure that they adhered to their purposes as well as by closely scrutinizing the extent of their powers and resolving disputes with individuals in favour of private rights.[14]

The advent of registered companies in 1844, in the wake of the Gladstone Commission of 1841[15] did not at first raise the issue of capacity. The assumption was made that this type of company related in form to the partnership model, enjoyed the contractual capacity of the business partnership. This capacity was co-extensive with that of its members and ratification by unanimity of any contractual act was said to be possible[16] The deed of Settlement Company, which came into vogue following the passing of the *Bubble Act*, enjoyed a similar

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11 See also L. Sealy, *Cases and Materials in Company Law* (London: Butterworths, 2001), p.145, who states that charter companies were only limited in instances where powers had been conferred on them by statute, c.f. *Hazell v Hammersmith and Fulham* LBC [1992] AC 1 (HL).

12 See R. Pennington, *Company Law (*London: Butterworths, 2001), p. 105; H Rajak, *op. cit.* at p. 15.

13 Gower, *op.cit.*, note 1 above at p. 203.

14 Omar, *op. cit.*, note 3 above.

15 This Commission was instituted to deal with the problem of certain heavy industries that did not have access to the mechanism of incorporation through Act of Parliament.

16 See S. Griffin: "The Rise and fall of the *Ultra Vires* Rule in Corporate Law". (1998) 2 *MJLS* 5 at 6.

partnership-like structure and consequently any question of capacity was decided as for a partnership whose members were free to elect to change the constitutional arrangements applicable to their affairs.[17] There was no provision on alteration of the Deed of Settlement and it was generally agreed that the business or purpose of the company could be altered or enlarged by the unanimous consent of the shareholders and that they could also ratify *ultra vires* act of the directors.[18]

The legislature responded in the shape of the *Joint Stock Companies Act,* 1856 (UK), whose passage was stated as being necessary to protect the interests of existing and prospective investors against the misuse of corporate capacity.[19] The Act replaced the deed of settlement with new constitutional documents called the memorandum and the articles of association. Part of the requirements for the memorandum was that it should contain an objects clause, delineating the purpose for which the company was founded.[20] Once a company formally stated its objects, it became possible for control to be exercised by the courts, in so far as a business transaction fell outside the powers the company enjoyed to fulfil these objects. There were, nevertheless, problems with the stipulation, particularly the omission of any faculty to alter the objects once stated or to prohibit amendments, a situation that seemed to undermine the object of the exercise.[21] Some reliefs came in the shape of the *Companies Act* 1862 (UK), a piece of consolidating legislation that stated conclusively that a company's memorandum could not be altered save in limited instances.[22] Nevertheless, the new Act did not resolve the remaining ambiguity over the scope of the objects clause and whether extensive

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17 Sealy, *op. cit.*, note 11 above at p. 145.

18 Aina, *loc. cit.*, note 1 above at p. 19.

19 Griffin, *op. cit.*, note 16 above at 6.

20 This provision is the ancestor of the modern day section 2(1) (c), Companies Act 1985.

21 See Griffin, *op. cit.*, note 11 above at pp. 6-7.

22 To effect a change of name or a reorganization of share capital (Section 12). These restrictions remained until the passing of the *Companies (Memorandum of Association) Act* 1890.

objects clauses were effective at clearly communicating the capacity of the company to would be transacting parties.[23] The inevitable result was that the courts would have to provide guidance, which arrived in the shape of the ruling in *Ashbury Carriage Company v Riche* (1875).[24]

In *Ashbury's Case,*[25] the objects of the company were:

> To make and sell, or lend or hire railway carriages and wagons and all kind of railway plant, fittings machineries and rolling stocks and to carry on the business of mechanical engineers and general contractors; to purchase, lease, work and sell, mines minerals, timber, coal, metals or other materials, to buy and sell any such material on commissions agents; to acquire purchases and erect works, building for the purposes of the company and to do such other things as are necessarily contingent, incidental or conducive to all or any of such objects.

The company having obtained a concession granted by the Belgian Government, contracted with Riche, a railway contractor, to build a railway between Anvers and Tournai. Following part performance of the contract and having paid Riche some moneys, the company experienced financial difficulty and sought to palliate this by allowing some of the directors to take over the contract in a personal capacity.[26] When the company wanted to disclaim the contract, Riche sued for breach of contract.

The company pleaded lack of capacity rendering the contract void *ab initio,* pointing to the terms of its own memorandum. Riche counterclaimed that the wording of the memorandum, which used the

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23 Griffin, *op. cit.*, note 16 above at p. 7.

24 (1875) LR 7 HL 653, (1875) LR 9 Ex 224. There had been two previous occasions on which courts considered the *ultra vires* rule, for which Rajak, *op. cit.* at 21, citing *Taylor v Chichester and Midhurst Railway Company* (1870) LR 4 HL 628 and *Eastern Counties Railway Company v Hawkes* (1855) 5 HLC 331, in both of which the transactions were held within the powers of the company.

25 *Supra.*

26 Presumably, because they were willing to invest when other participants were not, making it impractical for funds to be channelled through the company in the absence of unanimity.

term "general contractors" was wide enough to cover the transaction and, further, that the shareholders had approved the contract and accordingly must be taken to have ratified it.

The House of Lords was being asked to choose effectively between rival interpretations of the 1862 Act, the first being that companies should be deemed to have all the natural powers unless restricted, a construction similar to that applying to charter companies, and the second, that only those matters expressly or by necessary implication authorized could form the basis of the company's capacity.[27] The House of Lords held that the contract was indeed void as being *ultra vires* the company and that the ratification, if indeed it could take place, was ineffective.

There were two other consequences of the decision, notably the reliance in the House of Lords on a point of construction using the *ejusdem generis* rule meant that extensive objects clauses would be construed, not literally, but to give effect to a primary purpose (the substratum of the company) and, further, the decision confirmed that the type of *ultra vires* to be applied to the company was of the wide variety. This point was of considerable import because the Act's prohibition on altering the objects clause seemed to reflect a policy viewpoint that incorporation was a legal privilege to be conceded only in respect of objects.[28]

The doctrine was adopted and applied in Nigeria and it has been applied in the cases of *Ifekandu v Continental Chemists Ltd*,[29] *Metalimpex v A. G. Leventis and Co. Ltd.,*[30] *Okoya and Ors. v Santili and Ors;*[31] etc.

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27 See Griffin, *op. cit.*, note 16 above at pp. 7-8. See also Rajak, *op. cit.*, note 9 above at pp. 21-22, who states that the opposing interpretations rest on the divergent approaches taken by Mr. Justice Blackburn, who saw the question from the viewpoint of the common law, and Lord Cairns, who took as his starting point the statute.

28 Omar, *op. cit.*

29 (1966) All NLR, 1.

30 (1976) All NLR, (Pt.2), p.94.

31 (1990) 2 NWLR (Pt. 131) 172.

3. Justification of the Doctrine

Various reasons have been adduced for the adoption of the *ultra vires* doctrine in company law. The doctrine of *ultra vires* was developed at common law to ensure that the company keeps to the limits of its authorized objects listed in the memorandum in the interest of the creditors and investors. One view of the decision in Ashbury's case was that the courts recalled abuses stemming from trafficking in obsolete charters following the *Bubble Act, 1720 (UK)* and wished to prevent similar abuses in respect of registered (and statutory) companies.[32]

Ostensibly, there were also elements of a desire to protect various classes of participants, particularly shareholders and creditors and public interest.[33] It is possible to see that shareholders, actual or prospective, are protected by the existence of objects which make it possible to ascertain the consequences of any decision to invest and that creditors would be assured that transactions with the company could only be used in connection with the purposes mentioned in documents that are available for inspection.[34]

There seems to be consensus among writers[35] and even the courts that the doctrine was intended to offer protection to investors as well as other persons dealing with the company.[36] Although the risk of transactions being declared *ultra vires* encouraged promoters to make "credible commitments" to would-be transacting partners to avoid transactions lying outside the company's powers, this was not effective because parties remained unable to negotiate optimal contracts because of the difficulty in foreseeing changes in circumstances that would

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32 See Sealy, *op. cit.*, note 11 above at p. 145; Gower, *op. cit.*, note 1 above at p. 203.

33 See J. Farrar and B. Hannigan, *op. cit*. at 100.

34 Griffin, *op. cit.*, note 16 above at p. 8, where he argues that this protection is illusory because creditors, unless secured, could not obtain injunctions to restrain *ultra vires* transactions nor could they apply for winding up based on a failure of the company to adhere to its 'substratum.'

35 Gower, *op. cit.*, note 1above at p. 161; A.O.O. Ekpu: "The *Ultra Vires* Doctrine Lives on under the new Companies and Allied Matters Decree", *Bendel State University Law Journal.* (1991/1992), Vol. 1 No.1 at p. 76.

36 *Ibid.*, at p. 75.

require alterations in the nature of business for efficiency purposes.

4. Effects/Defects of *Ultra Vires* Rule

The effect of an *ultra vires* act is that it is void and is not binding on the parties as pointed out by Russel L.J. in the case of *York Corporation v Leetham & Sons Ltd.*[37] yet, these changes were not possible because the alteration of objects and ratification of transactions not in compliance with the constitution were not possible.[38] *Ashbury's case* was also an instance where judicial intervention had an undesirable commercial by-product because it permitted the company to evade an obligation by disclaiming capacity to contracts thus putting its contractual partner in the worst position possible of being unable to enforce its rights, except in limited instances.

For instance, if a person lent his money to a company on *ultra vires* business, he could not recover it.[39] Even if an action is brought for recovery of money, the company could raise the defence of *ultra vires* and would go away without liability as demonstrated in the cases of *Re Introductions Ltd*[40] and *Re Jon Beauforte (London)*.[41]

The strict application of *ultra vires* doctrine hampered commercial activities.[42] The protection that the *ultra vires* doctrine

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37 (1924) 1 Ch.557 at537 where he said: "An *ultra vires* contract cannot become *intra vires* by reason of estoppel, lapse of time, ratification, acquiescence or delay' See also M.O. Sofowora, *Modern Nigerian Company Law,* (Lagos: Soft Associates, 1992), p. 67.

38 See Gower, *op. cit*., note 1 above at pp. 206-207. For an instance, the constructive notice doctrine applying in a manner that produced an inequitable result, see also *Re Jon Beauforte (London) Limited* [1953] Ch 131.

39 E.P. Ohio: "The Effect of Section 39(3) of the Companies and Allied Matters Act, 1990", (1999/2000) *University Benin Law Journal.* Vol. 5 No. 2 at p. 4.

40 (1970) Ch. 199.

41 (1953) Ch.131.

42 Sofowora, *op. cit*., note 37 above at p. 67.

provided investors and businessmen soon became frustrated and lost.[43] The doctrine then could be described as "an ill-wind that blew nobody any good."[44]

5. The Doctrine of Constructive Notice Examined

Under the common law a person dealing with the company is presumed to have read the public documents of the company and to have made certain that any proposed transaction he intended to enter with the company was not prohibited by or inconsistent with the objects of the company. Any act therefore which is inconsistent with any of these documents would not bind the company and was void. The unfortunate effect of the rule came to play in the case of *Re Jon Beauforte (London),*[45] where a company was authorized by its memorandum of association to carry on the business of fashion designers. The company decided to undertake the production of veneered panels, which was *ultra vires*. A company supplied it with fuel for the factory, which was built to make the panels and tried to prove on liquidation that the supply was for legitimate purpose. Their claim failed and the court held that they ought to have actual notice of the business of the company.

Therefore, a person cannot raise a defence that he did not know that the transaction was *ultra vires* the company.[46] The case of *Royal British Bank v Turquand*[47] has come to whittle down the harsh effect of the doctrine. In that case, the board of Directors was authorized to borrow money on bond as the company might from time to time authorize in its general meeting. The directors borrowed money on sealed bond without any resolution passed and the company afterwards refused to acknowledge the indebtedness, the court held that the company was bound since there was nothing to suggest that the authority was wanting and no fact to put the outsider on notice. By the rule in *Turquand's case,* a person dealing with a company is not bound

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43 D. Sasegbon, *Companies and Allied Matters Law and Practice*, (Lagos: Dsc Publications Ltd, 1990), p. 69.

44 *Ibid.*

45 (1953) Ch. 131.

46 Sofowora, *op. cit*., note 37 above at p. 72.

47 (1856) 6 E&B 327.

to ascertain the public documents to see that the proposed transaction is not *ultra vires*.[48] He is not to be bothered by the indoor management rule of the company.[49] However, where the party is aware or ought to have known of the irregularity or where the irregularity results in the third party relying on forged document or where he failed to carry out investigation after being put on enquiry by usual circumstances, the rule in *Royal British Bank v Turquand* will not become applicable.

6. The Evasion of *Ultra Vires*

The immediate consequence of *Ashbury's Case* was careful consideration in respect of the drafting of objects clauses. The memoranda were eschewed and there grew instead the practice of specifying a profusion of all the objects and powers that the ingenuity of company advisers and promoters could dream of.[50] In response, however, the courts would use two techniques to set limits on the proliferation of clauses. The first was to distinguish between objects and powers and to state, in an application of the *ejusdem generis* rule, that powers could only be used in furtherance of the objects.[51] The second was to locate, even where only objects were concerned, the paragraph, which appeared to the courts to contain the main or dominant object and to construe all others as ancillary to this main purpose.[52]

The first technique certainly maintained the primacy of objects and the need to specify them in the company's documents, but did not necessarily avoid prolix and confusing drafting, as was later stigmatized by Lord Wrenbury in the case of *Cotman v Brougham.*[53] The second technique is reminiscent of the approach in *Ashbury's Case* with respect to the context in which the substratum rule operated. Both seem, however, to be redundant distinctions to make in light of

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48 Aina, *op. cit*., note 1 above at p. 23.

49 Sasegbon, *op. cit*., note 43 above at p. 124.

50 Gower, *op. cit*., note 1 above at pp. 203-204.

51 *Ibid.,* at p. 204.

52 See Farrar, *Farrar's company law*, (London: Butterworths, 1998), p. 101, citing the authority of *Re Haven Gold Mining Company.*

53 (1918) AC 514.

the decision in *Attorney-General v Great Eastern Railway Company.*[54] In this case, the House of Lords extended the wide view of *ultra vires* to statutory companies. On the facts, which concerned whether the company had the capacity to undertake a transaction involving the manufacture, sale or lease of railway stock, the court was of a view that the company was expressly empowered. There, the obiter of Lord Selborne LC declared that the doctrine of *ultra vires* should be:

> …reasonably understood and applied and that whatever may fairly be regarded as incidental to, or consequential upon, these things, which the legislature has authorized, ought not… to be held, by judicial construction to be *ultra vires*.[55]

Although the distinction between powers and objects dates back to *Cotman's case*, the use of the "incidental and consequent" qualification does not seem to materially require that they be distinguished. The point is made that to require, in the case of the pursuit of any particular activity, whether it is a means to an end (a power) or an end in itself (an object) to be identified, would give rise to commercially damaging distinction(s).[56] Similarly, with respect to the second technique, this requires that the courts identify what they consider to be the main purpose, which might be a factual exercise, based on evidence, or a fortuitous finding, based on a chance selection.[57]

7. "Independent Objects" or "Cotman" Clauses

The inevitable response to the advancement of these techniques was the development of what came to be called "Independent Objects" or "Cotman" Clauses.[58] This was the device of inserting a clause at the end of the memorandum specifying that each objects clause was to be construed as a separate and independent object and that clauses were

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54 (1880) 5 App Cas 473.

55 *Attorney-General v Great Eastern Railway Company* (1880) 5 App. 478.

56 See Rajak, *op. cit.*, note 9 above at p. 24.

57 *Re German Date Coffee Company* (1882) 20 Ch D 169.

58 See Farrar, *op. cit.* Note 52 above at p. 102, where the authors trace the development of this practice to Sir Francis Palmer in 1891.

expressly stated as not to be treated as ancillary to each other[59]as demonstrated in the case of *Cotman v Brougham*.[60] The case involved the activities of the Essequibo Rubber and Tobacco Estates Company, which agreed to underwrite shares in the Anglo-Cuban Oil Company. When both companies subsequently became insolvent, the respective liquidators, Cotman for Essequibo, Brougham for Anglo-Cuban Oil, went to court.

To determine whether or not Essequibo should be placed on the list of contributories for the other company, Cotman's argument being that the transaction was *ultra vires* the company. The House of Lords unanimously held that the transaction was indeed within the capacity of the company. Although the House of Lords disapproved strongly of the independent objects clause,[61]the fact that the Registrar of Companies had granted a certificate of incorporation based on the memorandum was held to conclusively bind the court.[62] Nevertheless, the practice was described as "pernicious" by Lord Wrenbury and Lord Finlay LC was of the view that the relevant Act, the *Companies (Clauses) Consolidation Act* 1908 (UK), should be amended to prevent what the court saw as an abuse of the legislation. In an instructive passage outlining the struggle between the draftsmen and the court, Lord Wrenbury stated:

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59 A typical clause would read: "None of the sub-paragraphs of this paragraph and none of the objects therein specified shall be deemed subsidiary or ancillary to any of the objects specified in any other such sub-paragraph, and the Company shall have as full a power to exercise each and every one of the objects specified in each sub-paragraph of this paragraph as though each such sub-paragraph contained the objects of a separate Company."

60 [1918] AC 514 at 521.

61 In *Stephens v Mysore Reefs (Kangundy) Mining Company Ltd* [1902] 1 Ch 745 a similar clause had apparently been ignored by Mr. Justice Swinfen-Eady.

62 See Griffin, *op. cit.*, note 16 above at p. 10, where he is of the view that the consequences of such an acceptance are that the case impliedly abolished the application of the substratum rule, albeit not through any judicial concern for its potentially adverse effect on commercial practice.

> There has grown up a pernicious practice of requiring memoranda of association which under the clause relating to objects contain paragraph after paragraph not delimiting or specifying the proposed trade or purpose, but confusing power with purpose and indicating every class of act which the corporation is to have power to do. The practice is not one of recent growth. It was in active operation when I was a junior at the Bar. After a vain struggle I had to yield to it, contrary to my own convictions. It has arrived now at a point at which the fact is that the function of the memorandum is taken to be, not to specify, not to disclose, but to bury beneath a mass of words the real object or objects of the company, with the intent that every conceivable form of activity shall be found included somewhere within its terms. The present is the very worst case of the kind that I have seen.[63]

A consequence of the case was to again throw into focus the distinction between powers and objects, Lord Wrenbury being of the view that:

> Powers are not required to be and ought not to be specified in a memorandum. The Act intended that the company, if it be a trading company, should by its memorandum define the trade, not that it should specify the various acts which it should be within the power of the company to do in carrying on the trade.[64]

Contention over the distinction between powers and objects persisted for many years. A view might be taken that, while Cotman-style clauses remained in vogue, as indeed they have done till the present day, the confusion between power and object was likely to continue. Increasingly, however, the courts have taken a pragmatic approach, reminiscent of the technique used by the courts to set limits on the proliferation of clauses in the wake of *Ashbury's Case*. This

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63 *Cotman v Brougham* [1918] AC 514 at 521.

64 *Ibid.*, at p. 522.

occurred in *Re Introductions Ltd* (1970),[65] where it was held that a faculty to borrow money could not of itself be treated as an object but constituted an incidental power, and in *Rolled Steel Products (Holdings) Limited v British Steel Corporation*,[66] where Mr. Justice Vinelott opted for a rule of construction, stating that:

> The question whether a stated 'object' is truly an independent object or purpose is always a question of construction. Even borrowing and lending moneys are activities capable of being pursued as independent objects… but commonly, where a sub-clause of the memorandum… states that one of the objects of the company is 'to lend or advance' or 'to borrow and raise' it is artificial to construe the sub-clause as anything other than a power conferred for the furtherance of what are in truth its "substantive objects" or purposes.[67]

The same question of construction is evident in the case of, *Re Horsley and Weight Limited,*[68] where in holding that the payment of a pension to a former director could constitute a separate object of the company, Lord Justice Buckley stated that:

> It has now long been common practice to set out in memoranda of association a great number and variety of 'objects', so called, some of which… are by their very nature incapable of standing as independent objects which can be pursued in isolation as the sole activity of the company. Such 'objects' must, by reason of their very nature, be interpreted merely as powers incidental to the true objects of the company.[69]

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65 *Re Introductions Ltd* (1970) Ch 99. For a critique of this approach, see Lord Wedderburn: "Unreformed Company Law", (1969), 32 *MLR* 563.

66 (1982) Ch 476.

67 *Ibid.,* at p. 497.

68 [1982] Ch 442.

69 *Ibid.,* at 445.

8. "Subjective Objects" Clauses or Bell Houses Clause

A further development, which some authors state predated Cotman Clauses,[70] was what came to be known as the "subjective objects" clause. This is provided, usually by a sub-clause at the end of the recital, that the carrying on of any business, which in the view of the directors was beneficial to the company, would be authorized.[71] Although, an early case expressed doubt that the use of such a clause came within the prescription of the constituting Act,[72] because of the practice of the Registrar of Companies in accepting memoranda, the courts felt themselves constrained, just as in *Cotman, Case*, in having to accept their essential validity. In *Bell Houses Limited v City Wall Properties Limited*, [73] where the issue at stake was whether commission was payable for information as part of a property development transaction and whether it was *ultra vires* for the plaintiff to request it, is modern authority for the proposition that these clauses are acceptable, provided that the directors honestly form the view that the advantage in pursuing the transaction is in connexion with and ancillary to the main business of the company. *Bell Houses' Case* is viewed as sounding the death-knell for the *ultra vires* doctrine, the use of these drafting devices appearing "to destroy any value that the *ultra vires* doctrine might have had as a protection for members or creditors; it had become instead merely a nuisance to the company and a trap for unwary third parties."[74]

Apart from the battle of the forms, represented by the drafting techniques employed and the responses the courts gave to them, the

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70 Farrar, *op. cit.*, note 52 at p. 102, citing *Re Peruvian Railways Company* (1867) 2 Ch App 617.

71 A typical clause would read: "To carry on any other business or activity of any nature whatsoever which is in the opinion of the directors capable of being advantageously."

72 *Re Crown Bank* (1890) 44 Ch D 634. 68 *Bell Houses Limited v City Wall Properties Limited* [1966] 2 All ER 674. 69.

73 [1966] 2 All ER 674.

74 See Gower, *op. cit.*, note 1 at p. 204, who suggests that, although companies could readily change their objects, omission to do so could still have fatal consequences for all parties to a transaction.

retreat from *Ashbury* is also represented by the qualification on the use of the *ultra vires* doctrine to limit this to issues of capacity and not to include the mere exercise of powers by directors, even if wrongful or mistaken. The courts later interpreted *ultra vires* narrowly to envelop only the question of capacity and left issues of what were in effect excess of authority or illegal exercise of powers to be decided by reference to the ordinary law governing directors' breach of duty to act bona fide in the interests of the company. This episode is illustrative of the unsatisfactory state of the *ultra vires* doctrine that "doomed it to a slow and sometimes painful demise almost from the time of its strongest judicial support."[75]

9. Reformation of *Ultra Vires* Doctrine

From the attendant defects inherent in the *ultra vires* doctrine as identified above, it became imperative for the doctrine to be reformed. Therefore, the foregoing consideration of the judicial attitude to the application of the *ultra vires* rule and to the practices developed to environment came to reveal that the courts have not been following consistent principles.[76] Since the *ultra vires* doctrine no longer stood the test of time, there were views that it should either be abolished or reformed to remove the bottlenecks it created.[77]

The Cohen committee in England (1945) recommended that as regards third parties, a company should have all the powers of a natural person and the memorandum should operate solely as a contract between a company and its shareholders as to the powers exercisable by the directors,[78] while Jekins Committee in England recommended that the *ultra vires* doctrine be retained but advocated for the abolition of the doctrine of constructive notice among others. Professor Gower lent his support to the recommendations of the

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75 Gower, *op. cit.*, note 1 at p. 205.

76 Sasegbon, *op. cit.*, note 43 at p. 71.

77 *Ibid.* See also Sealy, *op. cit.*, note 11 at p. 114.

78 Sasegbon, *op. cit.*, note 43 at p. 71

Jenkins Committee;[79] while Pennington on his own called for complete abolition of the *ultra vires* rule.[80]

In Nigeria as well as in other places the doctrine was also attacked. For instance, the Law Reform Commission observed:

> The result of these developments is that the *ultra vires* doctrine no longer protects the interest of shareholders or the creditors.[81]

Nigeria Law Reform Commission recommended an outright abolition of the doctrine.[82]

In purported compliance with the Directive of the European Economic community, S. 9(1) of the European Communities Act 1972 which was re-enacted in England as S.35 of the Companies Act, 1985 provides that in favour of a person dealing in good faith, any transaction decided on by the directors is deemed to be free of any limitation under the memorandum or articles and that the third party is relieved of any obligation to inquire about internal matters.[83]Without further statutory intervention S.35 of the Companies Act 1985 cannot be said to have checked against ultra vires act or transactions.

Reforms introduced by the Companies Act, 1989,[84] which modify the old section 35 of the Companies Act, 1985 further pursuant to the requirements of the Fires E C directives also confer on companies option of opting out of external ultra vires.[85]

Under section 2 (a) of the amended Act Companies are still required to state their objects. However, section 3 now provides that:

> Where the company is to carry on a business as a general commercial company: (a) the object of the company is to

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79 *op. cit.*, note 1 above.

80 *Pennington's Company Law* (4th edn.), (London: Butterworths, 1995), p. 106.

81 Reports on the Law Reform of Nigerian Company Law (1988) vol.1 p.71.

82 *Ibid.*, p.75.

83 Aina, *op. cit.*, note 1 at p. 33, see also Obadina, *op. cit.*, note 2 at p.40.

84 See Gower, *op. cit.*, note 1 at pp. 172 – 193.

85 Obadina, *op. cit.*, note 2 at P. 39-40.

> carry on any trade or business whatsoever, and (b) The company has powers incidental or conducive to the carrying on of any trade or business by it.

The difficulties in question arises from the fact that the 1985 Act fail to equip companies with all powers necessary to enable them to operate as bodies with unlimited contractual capacity.[86]

The final analysis that can be drawn from the above provision is that general commercial companies may carry on any trade or business and may state any object incidental or conductive to the carrying on of any trade or business by it thereby doing away with the *ultra vires* rule without any declaration to that effect[87] This is a step forward but it certainly does not go far enough in that it only enables the other party to an *ultra vires* transaction to enforce it against the company if certain conditions are fulfilled.

Furthermore, by Companies Act of 1989 which substitute new section 35 and inserts SS. 35(A) and 35B into the Companies Act, 1985.[88] In that context, section 35 of the 1989 operates to prevent any transaction undertaken outside the memorandum being called into question on ground of lack of capacity by reason of anything in the memorandum. Thus, by virtue of the provisions both the company and third parties are precluded from relying on *ultra vires* defence.

However, the third party protection is subject to two limitations:

(1) Section 35 allows a member to institute proceedings to restrain a company's act, which but for section 35(1) would be beyond the company's capacity. The right of the shareholder to challenge ultra vires transaction will be extinguished once the company has assumed legal obligation under the transaction.

(2) Where the board of directors enters into a transaction in violation of a constitutional limit on their powers and the other party to the transaction includes a director in the

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86 *Ibid.*, at p. 40.

87 Aina, *op. cit.*, note 1 at p. 34.

88 Sasegbon, *op. cit.*, note 43 at p. 71, See also Aina, *op. cit.*, note 1 at p. 34.

> company or its holding company, or a person connected with such a director or an associated company, then the transaction is voidable at the company's option, without regard to the state of knowledge of the other party.

The conclusion from above are that the *ultra vires* doctrine under the 1989 Act operates internally and applies in respect of acts that have been executed and not on acts that are still executory. In other words, *ultra vires* cannot be said to have effect on a concluded act. In this regard, Aina[89] submits that the section may seem to preserve the second exception to the rule in *Foss v. Harbottle*[90] that a member may sue to prevent *ultra vires* Act.

It is instructive at this point to give a highlight of the 2006 Companies Act of the United Kingdom.[91]

The Companies Act 2006 aims at simplifying the company law of the United Kingdom, and in doing so removed the requirements for an objects clause, leaving the memorandum as a simple statement of certain facts relating to the company. Any limitation on capacity will thereafter be contained in the company's articles of association and will, if breached, be a purely internal matter potentially making directors liable to shareholders for any loss caused by the breach but not invalidating the act itself.

Section 39(1) of the 2006 Act provides that*:*

> The validity of an act done by a company shall not be called into question on the ground of lack of capacity by reason of anything in the company's constitution.

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89 Aina, *ibid*., at p. 35.

90 (1843) Hare 461.

91 The Companies Act 2006 (c.46) is a statute of the United Kingdom regulating companies within that jurisdiction. The Act received Royal Assent on November 8, 2006. The Act also has the distinction of being the longest in British Parliamentary history, with 1,300 sections and containing not less than 15 schedules.

A company's articles of association will become its main constitutional document, and the company's memorandum will be treated as part of its articles.

Section 31(1) of the Companies Act of U K., 2006 provides: "Unless a company's articles specifically restrict the objects of the company, its objects are unrestricted."

That is, under the new Act, a company's capacity will be unlimited unless its articles specifically provides otherwise.[92] Hence, the last vestiges of the *ultra vires* rule will be removed to ensure that challenges could not be brought to the acts of any company on the basis of the powers being exceeded. The intention is that the effect of an illegal act will be governed by the rule or statute that creates the illegality. It is also the intention that companies will no longer be permitted to include objects in a constitution that serve to limit its capacity.

It is further provided in Section 40 of the Companies Act, 2006 that:

(1) In favour of a person dealing with a company in good faith, the power of the directors to bind the company, or authorize others to do so is deemed to be free of any limitation under the company's constitution.

(2) For this purpose—
(a) a person "deals with" a company if he is a party to any transaction or other act to which the company is a party,
(b) a person dealing with a company—
(i) is not bound to enquire as to any limitation on the powers of the directors to bind the company or authorize others to do so,
(ii) is presumed to have acted in good faith unless the contrary is proved, and
(iii) is not to be regarded as acting in bad faith by reason only of his knowing that an act is beyond the powers of the directors under the company's constitution.

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92 *Ibid.*

(3) The references above to limitations on the directors' powers under the company's constitution include limitations deriving—

(a) from a resolution of the company or of any class of shareholders, or
(b) from any agreement between the members of the company or of any class of shareholders.

(4) This section does not affect any right of a member of the company to bring proceedings to restrain the doing of an action that is beyond the powers of the directors.
But no such proceedings lie in respect of an act to be done in fulfilment of a legal obligation arising from a previous act of the company.

(5) This section does not affect any liability incurred by the directors, or any other person, by reason of the directors' exceeding their powers.

Other commonwealth jurisdictions were not left out in the attempt to stamp the corrosive tide of the *ultra vires* rule. Nigeria,[93] Ghana[94] Mauritius,[95] Fiji,[96] Singapore,[97] Malaysia,[98] and Papua New Guinea[99] have enshrined statutory provisions with slight variations to others on the reform of the *ultra vires* doctrine.

Section 38 of CAMA, which is in *pari materia* with section 24 of the Companies Code Act of Ghana, provides that:

> Except to the extent that the company's memorandum or any enactment otherwise provides, every company shall for the

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93 The Companies and Allied Matters Act, Cap C20, Laws of Federation of Nigeria, 2004 (hereinafter abbreviated to CAMA), SS.38 – 40, 68-69.
94 Companies Code 1963 [Act 179], SS. 24 – 26; 137-142.
95 Companies Act, 1984, S.22-23 and 25.
96 Laws of Fiji, Cap 247 Rev. 1985, SS.7 and 8.
97 Companies Act, 1970 (Cap. 185), section 19.
98 S.20, Companies Act, 1965 (No 125).
99 Section 37, Companies Act (chapter No.146) Revised Law of Papua New Guinea Vol. 5.

> furtherance of its authorized business or object, have all the powers of a natural person of full capacity.

Though Bakinbinga[100] opined that the provision has effects on abolition of ultra vires doctrine, Obadina,[101] has argued *per contra* that the powers implied by the section come into play only where the company is engaged in the pursuit of authorized business and those powers are capable of being exercised only in pursuit of such objects. An example of a contrary statutory provision is included in S.38 (2), CAMA which provides that a company shall neither have nor exercise power to make a donation or gift of its property or fund to a political party or political association or for any political purpose. Also, sections 24 and 38 are expressed to be subject to contrary statutory provisions imposing restrictions on the powers of the company.[102]

In most jurisdictions, however, the reformer set down the long list of specific powers deemed to be possessed by all companies unless they are expressly excluded, with the object of ensuring that the companies have all the powers necessary to enable them to pursue their authorized objects. In some cases, however, the statutory list includes provisions, which will enable companies to pursue substantive business object outside those expressly enumerated in the memorandum. For instance, S.7 of the Fiji companies Act vests Companies with the capacity to undertake business activities which are calculated to directly or indirectly enhance the value of or render profitable any of the company's property or right. Section 25(2) of the Singapore's Companies Act is in similar terms but also permits a company to undertake transactions "which may seem to the Company to be conveniently carried on in connection with its business''.[103]

It must however be noted that this formula does not endow companies with unlimited capacity because any business carried on by

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100 Bakinbinga, "The Reform of Company Law in Nigeria". *The Jurist* (Nigeria) Vol.3, (August, 1990) p.55-61.

101 Obadina, *op. cit.*, note 2 at p. 30.

102 S. 27(1) (d) CAMA.

103 See also Section 23(c) and the third schedule.

virtue of the provisions must, in point of fact bear the prescribed relationship of the existing business of the company.

Also, the Bermuda Companies Act, 1981 in Section 11 provides:

> A company limited by shares shall without reference in its memorandum have powers set out in first schedule unless any of such powers are excluded by its memorandum.

Some jurisdictions have also adopted the unrestricted capacity formula to abolish the ultra vires rule. Taking the lead is Canada. In other words the Canadian Business Corporation Act (BCA) was one of the first legislative measures to provide for the abolition of external operation of the *ultra vires* rule.[104]. The BCA has also served as a model for reforms in Barbados[105] New Zealand,[106] and Zambia.[107]In these jurisdictions, the companies' legislations endow companies with either 'full capacity to undertake any business or activity'[108] or with the "capacities and powers of a natural person."[109]

It is stated in clear terms under section 39(1) of CAMA that:

> A company shall not carry out any business not authorized by its memorandum and shall not exceed the powers conferred upon it…

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104 Companies Act 1985 (Cap 308), ss.17-22. This is a Federal Act under the constitution of Canada. It is its provinces who have the predominant role in incorporation of companies, nevertheless, the Business Corporation Act becomes a prototype for new Business Corporations Acts in Alberta, Saskatchewan, Manitoba, New Brunswick and Ontario. For Commentary of on Business Corporation Act, See J. Sziegal (Ed) studies in Canadian Company Law (1973) pp.17-18

105 Companies Act, 1985.

106 The Companies Act, 1993.

107 Companies Act, 1994 (No 26) and Zambia (Companies Act 1994).

108 Section 16 (1) (b), New Zealand Companies Act, 1993.

109 Barbados: *op. cit.* Section 17 Dominica: *op. cit.*, s. 17 (1) Australia *op. cit.* Sec 161(1) (b) Zambia: *op. cit*, Sec. 22(1).

From the face of it, the section appears to have codified the *ultra vires* rule[110] that section 39(1) is unnecessary and it is a wrong assertion of a position that no longer exists but it may be to save the exceptions to the rule in *Foss v Harbottle*.[111]

It is further provided in section 39(2) CAMA that a breach of the provision of S. 39(1) may be asserted in any proceedings under sections 300 to 313 of CAMA or under S.39 (4). The foregoing is the approach adopted in Company Code Act Ghana, 1963 to offer protection to the third parties dealing with the company. That is to say, both the Ghana Company Code and CAMA enable designated parties to rely on breach of the *ultra vires* rule in proceedings for relief against "oppressive conduct" on the part of the company.

The high water mark of the innovations brought by CAMA on effect of *Ultra vires* rule is contained in section 39(3). The subsection validates acts of a company conveyance or transfer of property to, or by a company where such act, conveyance or transfer was not done or made for the furtherance of any of the authorized business of the company or that the company was otherwise exceeding its objects or powers.

Similarly, it is stated in clear terms in Section 39 (1) of the Companies Act, UK, 2006 that:

> The validity of an act done by a company shall not be called into question on the ground of lack of capacity by reason of anything in the company's constitution.[112]

Also, both Sections 17 and 23 of the New Zealand and Zambia Companies Act respectively provide that:

> No act by a company shall be invalid merely because the company did not have capacity or the power to undertake it.

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110 Aina, K., *op. cit.*, note 1 at pp. 35 – 36.

111 *Supra.*

112 The 2006 Act substitutes the word "memorandum" as contained in the 1985 Act with "constitution."

Section 18 of the Canadian Business Corporation Act also states:

> No act of the company shall be invalid merely because it is contrary to the articles.

Looking at these sections and section 39 (3), CAMA, in particular, *ultra vires* transactions involving a company now has legal force whether the act or transaction done by the company is *ultra vires*, it or the same is in excess in the exercise of the powers it has in the memorandum, an enforceable claim can be brought in respect thereof.[113] It then follows that for all purposes, no declaration or judgment of a competent court of law can render invalid the acts of or by a company which are *ultra vires* it or exceeds the powers of the company when already done or executed or concluded.

Section 39(4) CAMA entitles any member of a company or the holder of any debenture secured by a floating charge over the company's property to bring an application to the court for an injunction to prohibit breach of S.39 (1) or *ultra vires*. An analogous section to this is section 218 Companies Code Act of Ghana. It must be noted that *ultra vires* act may also be restricted to only proposed actions not executed or concluded acts.

By the provisions of section 39(5) CAMA, on proceedings brought under section 39(4) CAMA, whereby the court prohibits or sets aside the performance of a contract which involves *ultra vires* transactions, compensation may be paid for any loss or damage suffered by the parties to the contract by reason of such order of the court. The transaction giving rise to the proceedings should not have been concluded. This remedy appears to be limited in that the company can quickly swing into action calling for the majority to alter its objects to accommodate the *ultra vires* act or transaction.

Other reforms worthy of note are the abolition of the doctrine of constructive notice and the provision for alteration of the object clause in most jurisdictions. Section 68 of CAMA is to the effect that except as mentioned in section 197 of CAMA, regarding particulars in the register of particulars of charges, a person shall not be deemed to

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113 Sasegbon, *op. cit*., note 43 at p. 72-72.

have knowledge of the contents of the memorandum and articles of a company or of any other particulars, documents, or the contents of documents merely because such particulars or documents are registered by the Commission or referred to in any particulars or documents so registered, or are available for inspection at an office of the company. There exist similar provisions in Section 35 of the Companies Act of England, Section 771 A of the 1989 Act and Section 40(1) of the Companies Act of U K, 2006.

Furthermore, under section 69 of CAMA, there exists the provision for presumption of regularity to the effect that any person having dealings with a company or with someone deriving title under the company shall be entitled to make the assumption, among others, and the company and those deriving title under it shall be estopped from denying their truth that the company's memorandum and articles have been duly complied with. Hence, a person dealing with the company is no longer deemed to have notice of the memorandum and articles or other registered documents of the company just because such is available for inspection.

On alteration of object clause, a company may, at a meeting, by special resolution alter the provisions of its memorandum with respect to the business or objects of the company.[114] The effect of alteration therefore is that an *ultra vires* act or transaction can be made intra vires by amending the constitution or memorandum of the company to suit it.

9. Conclusion

Ultra vires started as a judicial innovation when judges were faced with the need to protect parties to transactions engendered by corporate activities. Companies then were at the infancy stage and there was the need for legislations to supplement the contractual nature of the company with the requirement for objects in the memorandum, to enabling parties transacting with the companies not to end up losing their investments. However, the evolution of the doctrine later turned

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114 Sections 45 and 46, CAMA; ss. 16 and 17, English Companies Act, 1985, S. 31(2), Companies Act of UK, 2006.

out to create undue hardship to investors, leading to the reform of the doctrine in various jurisdictions. It is instructive that in most jurisdictions, the *ultra vires* doctrine has been amended, restricted or avoided in some form. In many of these jurisdictions, the legislatures have gone as far as enacting provisions granting full capacity to companies, marking the last stage of the slow death of *ultra vires*, first predicted in 1966.[115]

Nevertheless, the reforms that did occur in Nigeria did not seem to be effective and frequently raised more questions than they resolved. The reform of company law is certainly long overdue in Nigeria. Steps should be taken to ensure that the company law in Nigeria remains up to date and can serve usefully as an example to other jurisdictions, seeking to modernize their regulatory regimes for companies with a view to effectively meeting up with modern trends.

There is need to abolish the restrictions inherent in the *ultra vires* rule by granting full capacity to both private and public companies. It is recommended that removing the requirements to state objects will enhance the use of the constitution or the memorandum and articles of association as mechanisms for control by the shareholders. The process of legislative reforms should put into consideration the views of jurists, academicians and practitioners capable of injecting new values in Company Law and Practice.

115 See Lord Wedderburn, "Death of *Ultra Vires*" (1966), 29 *MLR.* 673.