

# IMPLICATIONS OF *ULTRA VIRES* DOCTRINE ON BUSINESS TRANSACTION IN NIGERIA

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## ABSTRACT

*Companies are formed for the purpose of doing business to make profits. Such businesses are restricted by the object clause in the Memorandum of Association. This research work aimed at showing the effects of ultra vires doctrine on Business transaction in Nigeria. But the law at times validates the act of a company notwithstanding that it was done for the furtherance of the company's authorized business (or that if otherwise exceed the company's powers).*

*Keywords: Ultra vires doctrine, business transaction, memorandum of association, company*

## INTRODUCTION

Ultra vires are a common law doctrine. It simply means beyond the powers of the company to carry on a business. It is predicted upon the doctrine of constructive notice of registered documents. The doctrine can be said to represent perhaps one of the most important and enduring contributions of common law in the regulation of the existence and activities of registered companies in Nigeria. It was principally propounded in order to protect the investors and creditors to companies in Nigeria on their investment. By this restriction, an investor is placed in a position to know precisely the purpose which his money was used, and a creditor is ensured that the company' funds are not expended on activities that are not authorized by the object clause. See Section 39(1) of Company and Allied Matters Act (CAMA) 1990, which provides as follows:

*"A Company shall not carry on any business not authorized by its memorandum and shall not exceed the power conferred upon it by its memorandum on this Act".*

However, if an act of transaction carried out by a company which is legal in itself, but not authorized by the object clause in the Memorandum of Association or by statutes, it is ultra vires, that is void and cannot be ratified by members at an Annual General Meeting. It follows therefore from the principle that a company is mainly to carry on the objects laid down in its object clause. Any one dealing with a company may have to ask himself not only whether the officer of the company acting in the transaction has authority to do so, but also whether the company itself had the capacity to enter into the transaction. This was the position before the enactment of Company and Allied Matters Act 1990, because this position of law in Nigeria was a reflection of the position in England, as seen in the celebrated case of ASHBURY RAILWAY AND IRON CO. V. RICHE (1875) LRH. 1653.

In this case, the company was formed for the purpose of

making and selling railway wagons. The Company secured a contract to build a railway system in Belgium. Riche was made a sub-contractor. The Company went into difficulties and thereby attempted to put an end to the contract between it and Riche. The English House of Lords held that:

*"The contract which the company has made to construct a railway system and of which Riche was a sub-contractor was void, since this was not included in the company's object clause".*

The Nigerian Supreme Court also adopted the same attitude in CONTINENTAL CHEMIST LTD V. DR. IFEKANDU (1966) ALL. MLR 11, here a drug dispensing company purported to train medical Doctors for the purpose of setting up and running hospitals. Though the memorandum has a clause, which allowed it to carry on any other business which could be conveniently carried on with its main objects, the transaction was declared ultra vires and therefore void. Furthermore, on the competency and power of the company to enter into the contract, Lord Claims Said in ASHBURY RAILWAY CARRIAGE AND IRON CO. V. RICHER (SUPRA) that:

*"The question is not as to the legality of the contract, the question is to the competency and power to make the contract... I am clearly of the opinion that this contract was entirely beyond the objects in the memorandum of association... it was thereby placed beyond the powers of the company to make the contract... if it was void at the beginning it was void because the company could not make it a contract".*

The restriction of registered companies to the ultra vires rule by the courts is no more than a restraint, aimed at confining them within the territory of the memorandum and thereby denying them of the commercial freedom enjoyed by natural persons of full capacity.

It should be noted that the doctrine under consideration also is applicable to statutory companies, but not to chartered companies members of chartered companies may apply to the court for an

injunction to restrain the company's freedom exceeding its stated objects. A part from carrying out the objects of the company, a company may however be expected to also carry out every thing which is reasonably necessary to enable it achieve the purpose for which it was formed. This shall require a wider interpretation of the doctrine, for the companies to at least diversify into other areas that may be considered incidental to the main objects of the company. Qualifying the application of the doctrine, LORD SELBORNE in ATTORNEY GENERAL V. GREAT EASTERN RAILWAY CO. said of the doctrine of ultra vires that:

*"It ought to be reasonable and not unreasonably understood and applied and whatever may fairly be regarded as incidental to or consequential upon those things which the legislature has authorized, ought not (unless expressly prohibited) to be held by judicial construction to be ultra vires"*

It is apparent from the statement of Lord Selborne that company may carry on an additional business where that business is incidental to the company's main objects so long as it is beneficial to the company. This position was demonstrated in DUECHAR V. THE GAS LIGHT AND COKE CO. LTD. Where a company formed to extract gas from coal had the power to manufacture and supply gas, deal with and sell by-products and converts the by-products into marketable state. The plaintiff, a Secretary to the company which supplied the defendant with caustic soda chlorine by the defendant and the erection of a factory for that purpose was ultra vires. The company used the caustic soda to convert certain residuals of gas-making into chlorine; a by-product of caustic soda was converted into bleaching power. It was held that the manufacture of both products was fairly incidental to the company's power or objects. However, where an act which by its nature is expressed to be, and is capable of being an independent object to the company is in issue, the act will be ultra vires. In RE-HORSELY AND WEIGHT LTD. A company's objects include the power to

grant pensions to its present and past employees and to its directors. The company is consequence purchased a pension policy for the director and employee who were almost retiring. After his retirement, the company was wound up and the liquidator sought a declaration that the payment was ultra vires. It was held that the power to grant pensions was a substantial object of the company and was therefore valid.

It should be noted that in spite of the fact that incidental or consequential objects may sometimes be implied. The danger of same unspecific acts being declared ultra vires is a real one for where the company foes an act which is ultra vires, no legal relationship or effect will, as a general rule emerges there from. Such act is void and therefore cannot be ratified even if all the shareholders agree, as the act was void abinitio. This was the position taken by Lord Cains in ASHBURY'S case while dealing with the validity of the contract when he said intia alia that: "If it was a contract void at the beginning, it was void because the company could not make the contract".

## **THE EFFECTS OF ULTRA VIRES ON BUSINESS TRANSACTIONS**

The ultra vires doctrine asserts that registered companies and statutory ones have a limited capacity to enter into legal relationship. In line with this, Section 38(1) CAMA endows every company with all the powers of a natural person. But this is limited to power exercised to further its objects. The doctrine was made for the protection of the general public, the creditors to the company and also the company's shareholders. The truth is that the statement of a company's objects in its memorandum is intended to serve a double purpose. In the first place, it gives protection to subscribers who learn from it the purpose to which their money can be applied, in the second place it gives protection to person who deal with the company and who can infer from it the extent of the company's powers. The narrower the objects expressed in the memorandum

the less are the subscriber's risk, but the wider such objects the greater is the security of those who transact business with the company. This was said by Lord Parker in the case of COTMAN V. BROUGHMAN (1918) A.. C. 514. Where it was held that:

*"A company could engage in a variety of objects at will provided its objects clause consisted of a list of such objects and concluded with clause to the effect that each and every one of the aforementioned clauses are separate and independent objects of the company".*

Subsequently in the case of BELL HOUSE LTD V. CIT WALL PROPERTIES LTD (91962) 2. QBD. 656, the court accepts that an additional paragraph properly worded, could be added, which could give directors acting in good faith power to change the company's business and when they so choose, to carry any other business whatsoever, which can in the opinion of the Board of Directors advantageously be carried on by the company.

## **CONCLUSION AND RECOMMENDATIONS**

The doctrine of ultra vires which restricts the powers of a registered company to carry on business within the object clause is meant to protect investment of those who do business with the company. The company shall not exceed the powers conferred upon it by its memorandum see section 39(1) of the Companies and Allied Matters Act. It should be noted that the rule that ultra vires contracts are void ab initio is no longer the law in Nigeria. Section 39(4) and (5) of the Act has moderated the position in S. 39(3). These two sub-sections entitle the court upon application of a member or creditor to validate an ultra vires contract. Ultra vires contracts however are now not void but voidable. The rationale of the doctrine is to protect members, creditors and the general public.

The positions of the study therefore are: that a member of a company is allowed by law to alter the object clause in the memorandum by simple majority of an annual general meeting of

the company; that a company can include in its object clause a number of businesses it can undertake; that if even an act of the company is not stated in its object clause, a company be allowed to carry on with such business if it is related to the kind of business allowed in its object clause. That the powers of Directors to the commit the company to contract be extended to cover businesses closely related to those authorized by the memorandum. Any members of a company can seek court injunction, compelling the company to engage on such business its benefits. These recommendations will go along way in making business transactions much easy in Nigeria.

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