following, p 802).

[32] But note, eg, *Conway v Ratiu* [2005] EWCA Civ 1302, [2006] 1 All ER 571, where the corporate veil was lifted, and *Diamantides v JP Morgan Chase Bank* [2005] EWCA Civ 1612 where that was considered.

[33] A second appeal concerned a charge based upon similar facts against the Monkwearmouth Conservative Club Ltd, which was incorporated under the Companies Acts. The cases were treated as indistinguishable and disposed of together.

[34] (1882) 8 QBD 373.

[35] This principle was applied to penetrate an elaborate network of some 80 interlocking trusts and companies in *Re a Company* [1985] BCLC 333, CA, and strikingly illustrated by diagrams which are reproduced in the report of the case.

[36] Contrast this with a finding that a particular *transaction* is a sham: see the discussion in *Secretary of State for Business, Enterprise and Regulatory Reform v Neufeld*[2009] EWCA Civ 280, [2009] BCC 687, noted in the Note following *Lee*'s case **[2.04]**, p 43.

[37] An alternative ground for the decision of the court was that DHN did have a sufficient interest in the land, on the basis of either an irrevocable licence or a resulting trust, to claim compensation for disturbance in its own right.

[38] This was not strictly a 'group enterprise' case. The occupier of the shop premises which were compulsorily acquired was a company of which W held 999 shares and his wife the remaining one. Part of the land was owned by W personally and the rest by a second company in which, again, W and his wife held all the shares. The judgments leave little doubt, however, that *DHN* would not have been followed even if the facts had been identical.

[39] The case went to the House of Lords on grounds which did not involve this point.

[40] See also *The Maritime Trader* [1981] 2 Lloyd's Rep 153, [1981] Com LR 27, in which the court refused to order the arrest of a ship owned by the defendant company's subsidiary.

[41] [1977] AC 774 at 807.

[42] *Revlon Inc v Cripps and Lee Ltd* [1980] FSR 85.

[43] *Istituto Chemioterapico Italiano SpA and Commercial Solvents Corpn v EC Commission* (Cases 6 and 7/73) [1974] ECR 223.

[44] 1978 SLT 159.

[45] Of course, in an appropriate case a parent may be held liable on the basis of a contractual promise or a representation that it would support its subsidiary: a plea which failed in *Kleinwort Benson Ltd v Malaysia Mining Corpn Bhd* [1989] 1 All ER 785, [1989] 1 WLR 379, CA, where the 'comfort letter' given by the parent company was construed as excluding an intention to create legal relations. If the subsidiary has gone into insolvent liquidation, the parent may be liable as a party to fraudulent trading under IA 1986 s 213, or (as a 'shadow director') liable for 'wrongful trading' under IA 1986 s 214. See 'The functions, powers and duties of the liquidator', pp 804ff.

[46] At present, this can be done in England only with the approval of the prescribed statutory majorities of the creditors concerned, by a scheme of arrangement under CA 2006 ss 895ff, or, in special circumstances, under the 'power to compromise' conferred on liquidators and the court by IA 1986 s 167(1) and Sch 4. For an example of the latter, see *Re Bank of Credit and Commerce International SA (No 3)* [1993] BCLC 1490.

[47] *ICI v EC Commission* (Cases 48, 49, 51–57/69) (the *Dyestuffs* case): [1972] ECR 619, where the CJEU held that anti-competitive behaviour of a subsidiary company within the EU, acting on the instructions of its parent company outside the EU, was attributable to the parent so as to enforce successfully EU competition rules. In *Provimi Ltd v Roche Products Ltd* [2003] EWHC 961 (Comm), [2003] 2 All ER 683 it was held that because a group does not have legal personality, the Commission must select a specific company within the latter as an

addressee of its decision, and be responsible for payment of the penalty.

[48] For further reading on this topic, see T Hadden, *The Control of Corporate Groups* (1983); DD Prentice, 'Groups of Companies: The English Experience' in KJ Hopt (ed),*Groups of Companies in European Laws* (1982), p 99; CM Schmitthoff and F Wooldridge (eds), *Groups of Companies* (1991); K Hofstetter, 'Parent Responsibility for Subsidising Corporations: European Trends?' (1990) 30 ICLQ 576; IM Ramsay, 'Holding Company Liable for the Debts of an Insolvent Subsidiary: A Law and Economics Perspective?' (1994) 17 *University of New South Wales Law Journal* 520.

[49] *Collins Steward Ltd v Financial Times Ltd* [2005] EWHC 262 (QB), eg, held that a corporation cannot have hurt feelings.

[50] See Companies Act 1967 (CA 1967) s 68(5) (now, alas, repealed): 'An insurance company which contravenes subs (1) or (2) above shall be guilty of an offence and liable on conviction on indictment to imprisonment for a term not exceeding two years.'

3. Corporate Activity and Legal Liability

Chapter: **(p. 81)** 3. Corporate Activity and Legal Liability
Author(s): Len Sealy and Sarah Worthington
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Introduction

The previous chapter considered what it means to say that a company is a legal person. This chapter looks at how the company *acts* as a legal person: in particular, how it enters into binding contracts, commits torts and crimes, makes gifts, sues and is sued.

Rules of attribution: how does a company act?

A company must act through human agents. The principal issue to be addressed in every problem in this area is: *which acts of which people will count as acts of the company*, so that we can say that the *company* has entered into a binding contract, or the *company* has committed a tort or a crime?

Once we have established what the *company* has done, or knows, or intends, then we are usually in a good position simply to apply the normal rules of contract, torts or crime to assess whether rights have been created or infringed.

The most significant contribution to answering the question, '*Who acts for the company?*', comes from the next case. The fundamental principles that it set out are extracted here, but a longer extract, in context, appears later in this chapter (see **[3.29]**).

[3.01] Meridian Global Funds Management Asia Ltd v Securities Commission [1995] 2 AC 500 (Privy Council)

The facts are immaterial at this stage, but see **[3.29]** for more detail.

> The opinion of their Lordships was delivered by LORD HOFFMANN: … Any proposition about a company necessarily involves a reference to a set of rules. A company exists because there is a rule (usually in a statute) which says that a persona ficta shall be deemed to exist and to have certain of the powers, rights and duties of a natural person. But there would be little sense in deeming such a persona ficta to exist unless there were also rules to tell one what acts were to count as acts of the company. It is therefore a necessary part of corporate personality that there should be rules by which acts are attributed to the company. These may be called 'the rules of attribution'.
>
> The company's primary rules of attribution will generally be found in its constitution, typically the articles of association, and will say things such as 'for the purpose of appointing members of the board, a majority vote of the shareholders shall be a decision of the company' or 'the decisions of the board in managing the company's business shall be the decisions of the company'. There are also primary rules of attribution which are not expressly stated in the articles but implied by company law, such as 'the unanimous decision of all the shareholders in a solvent company about **(p. 82)** anything which the company under its memorandum of association has power to do shall be the decision of the company': see *Multinational Gas and Petrochemical Co v Multinational Gas and Petrochemical Services Ltd* **[7.39]**.
>
> These primary rules of attribution are obviously not enough to enable a company to go out into the world and do business. Not every act on behalf of the company could be expected to be the subject of a resolution of the board or a unanimous decision of the shareholders. The company therefore builds upon the

primary rules of attribution by using general rules of attribution which are equally available to natural persons, namely, the principles of agency. It will appoint servants and agents …

The company's primary rules of attribution together with the general principles of agency, vicarious liability and so forth are usually sufficient to enable one to determine its rights and obligations. In exceptional cases, however, they will not provide an answer. … For example, a rule may be stated in language primarily applicable to a natural person and require some act or state of mind on the part of that person 'himself', as opposed to his servants or agents. … In such a case, the court must fashion a special rule of attribution for the particular substantive rule. This is always a matter of interpretation: given that it was intended to apply to a company, how was it intended to apply? Whose act (or knowledge, or state of mind) was *for this purpose* intended to count as the act etc of the company? One finds the answer to this question by applying the usual canons of interpretation, taking into account the language of the rule (if it is a statute) and its content and policy. …

The 'primary rules of attribution' as set out in the Model Articles, Arts 3 and 4 (for both limited and public companies), provide as follows:

Directors' general authority

3. Subject to the articles, the directors are responsible for the management of the company's business, for which purpose they may exercise all the powers of the company.

Members' reserve power

4.

(1) The members may, by special resolution, direct the directors to take, or refrain from taking, specified action.
(2) No such special resolution invalidates anything which the directors have done before the passing of the resolution.

A company may choose its own 'primary attribution' rules, but these model provisions are common. In addition, if permitted by the company's constitution, the board may delegate its powers. See, for example, Model Articles, Arts 5 and 6. If the board then delegates in a manner permitted by the articles, the delegate(s) will have actual authority to bind the company as long as their actions are within the scope of the delegation.

Contractual liability: general issues

The issue to be addressed here is whether a contract between the company and an outsider is binding. The company and the outsider will only be able to enforce the contract (or be sued on it) if the contract is binding. The Companies Act 2006 (CA 2006) s 43 provides that a company can enter into a contract either in writing under its common seal, or through an authorised agent acting on behalf of the company.

(p. 83) A company is a legal person, and the principles which determine the validity of contracts between legal persons are already familiar. A contract is valid and binding only if the:

(i) contracting parties have the *capacity* to contract (or are deemed or presumed to have that capacity); and
(ii) agents effecting the transaction on behalf of the parties have the *authority (real or apparent)* to do so (or are deemed or presumed to have that authority).

Notice that the first question relates to the *company*, and the second to its *directors* (or other agents). The first question now creates few problems (although it used to create enormous ones); the second is often critical.

For completeness, three further points should be noted. First, under the normal rules of agency just described, the acts of an unauthorised agent (ie an agent without actual authority, statutorily deemed authority or common law ostensible authority) will not bind the company (the principal) to the third party in contract. The contract will be void. But if the unauthorised agent has dealt with the third party explicitly as agent, then the principal (the company) may choose to *ratify* the unauthorised transaction, effectively adopting it and rendering it binding on the third party.[1] Secondly, and alternatively, if the unauthorised agent has dealt with the third party explicitly as agent and the company does *not* ratify, then the third party can sue the *agent* for breach of warranty of authority. Finally, even if the contract is void, its terms may nevertheless have been carried out, and assets transferred (and effectively transferred) between company and intended counterparty. In these circumstances each party has the right to recover the assets it has mistakenly transferred (mistakenly in the assumption that there was a contractual obligation to transfer).[2]

Corporate capacity

A company's capacity may be constrained by provisions in its articles. For example, a charitable company may expressly limit its activities (its '*objects*') to particular types of charitable activities in a nominated field. Commercial companies can do the same, although they have less reason, and no obligation, to be so restrictive (CA 2006 s 31(1)). These legal limitations in the company's constitutional documents limit the company's *capacity* —although now to little external effect.

Historically, purported acts outside such nominated objects were void. Neither party could enforce the contract, and any benefits transferred were subject to restitutionary claims aimed at restoring the parties to their pre-contractual positions. This created great disincentives for outsiders dealing with the company, and could wreak unfair and unexpected consequences on transacting parties. The advantage, if there was one, was for the members: they could be sure (if the directors acted properly) that their investments were confined to selected types of ventures.

In the end, the commercial disadvantages and unfairness to outsiders were seen as a price too high to pay for members' security, and the legislature stepped in with statutory provisions protecting third parties. These provisions do not go so far as to provide that every company actually *has* the capacity to do anything, but they prevent the validity of any act being called into question on the ground of lack of capacity arising from anything in the company's constitution (CA 2006 s 39(1)). This is just as beneficial for outsiders, but preserves the right **(p. 84)** of insiders (particularly the company, or the members by derivative action, to sue their directors (or other agents) for breaches of the company's constitution (ie for acting outside the powers given to the directors: CA 2006 s 171), and for causing loss to the company (eg arising from the prohibited transaction). This is why the 'capacity issue' is no longer a problem for outsiders, but it also explains why it remains necessary—even if only for insiders—to know how 'objects clauses' should be interpreted.

These issues are explored in more detail at 'Agency and authority in corporate contracting', pp 95ff.

Authority of the company's agents

Even if the company does have the capacity to enter into a particular type of contract (or is deemed to have the necessary capacity), this does not mean that anyone and everyone can decide that the company *will* commit itself. For example, a national petroleum company certainly has the capacity to sell to customers, but not everyone (not even every company employee) can decide that the company *will* sell to a particular customer or enter into a transaction above certain value limits. Only those employees (or company *agents*) with *authority* to make a sale can commit the company in this way.

The issue of authority raises its own problems. The *actual authority* of an agent cannot extend to the doing of anything that is not permitted by the company's constitution (eg a company that may only perform charitable works, or only publish English monographs, cannot give *actual* authority to its agents to transact other types of business). So all the analytical work that went into interpreting a company's constitutional documents for the purpose of determining a *company's* capacity, could possibly go into the same task for the purpose of determining the limits of an *agent's* actual authority.

In practice, the end result might then have been a 'vicious circle': having removed the impediment to outsiders arising from the objects and their impact on corporate capacity, they reappear in another guise, with the same effect, because of their impact on agents' authority. Again, the legislature intervened, and, in favour of third parties 'dealing with a company in good faith, the power of the directors to bind the company, or authorise others to do so, is deemed to be free of any limitation under the company's constitution' (CA 2006 s 40(1)). Note the good faith limitation.

This is not all. A company's objects are not the only constraint on actual authority. Even where the proposed dealing *is* within the company's objects, only certain people will be given actual authority to transact the particular business on behalf of the company. So, in the earlier example, some employees will have *actual authority* to sell bulk supplies of petroleum to wholesalers or large retailers, perhaps within certain value limits depending on seniority, others only to sell petrol to the public at domestic outlets. Employees in the latter group are unlikely to have actual authority to transact the former types of business for the company. But appearances are sometimes misleading. An employee at head office may appear to outsiders to have the necessary authority to sell supplies to wholesalers, but the company's own internal rules and organisational structure may provide otherwise. Once again, the legal rules protect the outsider in these types of cases. They do that by common law mechanisms, not statutory ones. These are the legal rules on *ostensible or apparent authority* and the '*indoor management rule*'.

Clearly all these protective rules in favour of third parties are based on an underlying policy assumption that it is only reasonable, in the circumstances, for the outsider to believe, and rely on the fact, that the company's agent has the necessary authority to transact the business in issue. Where such assumptions are *not* reasonable, the protective provision falls away.

In particular, in relation to the statutory assumptions, CA 2006 s 41 specifically provides that directors and connected persons cannot rely on s 40 to assert the validity of a transaction **(p. 85)** (although the company can, at its option, affirm the transaction).[3] This section also imposes remedies that go beyond those available at common law: the contract is voidable (subject to certain exceptions); and the parties to the transaction *and* any directors of the company who authorised the transaction are liable to account to the company for any gain made, and compensate for any losses caused.

Binding contracts between the company and third parties

When these various rules are put together, it can be seen that a contract between the company and an outsider will be binding if:

(i) the company has the capacity to enter into the contract, *or* that capacity can be assumed (using s 39(1)); *and*
(ii) the director (or other agent transacting the deal) has *either* actual authority to transact the deal (or can be deemed to have that authority using s 40), *or* has*ostensible authority*. And, in cases of either actual or ostensible authority, if the impediment to successfully demonstrating the particular form of authority is an issue of internal company procedure, then the *indoor management rule* allows the third party to assume that the internal procedures are regular.[4]

Each of these elements is examined in the sections that follow.

Capacity: what is a company legally entitled to do?

The modern relevance of a company's capacity to act was summarised at 'Corporate capacity', p 83. The rather odd conclusion seems to be that a company is legally *able*to do, and accept obligations to do, a good number of things that are beyond its capacity. The statutory deeming provisions which lead to this conclusion are extracted in the following section.

Statutory provisions protecting third parties (outsiders) from the consequences of constitutional limitations on corporate capacity

Companies Act 2006 s 39

39 A company's capacity

(1) 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.
(2) This section has effect subject to section 42 (companies that are charities).

(p. 86) **Companies Act 1985 s 35**

35 A company's capacity not limited by its memorandum

(1) 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 memorandum.
(2) A member of a company may bring proceedings to restrain the doing of an act which but for subsection (1) would be beyond the company's capacity; but no such proceedings shall lie in respect of an act to be done in fulfilment of a legal obligation arising from a previous act of the company.
(3) It remains the duty of the directors to observe any limitations on their powers flowing from the company's memorandum; and action by the directors which but for subsection (1) would be beyond the company's capacity may only be ratified by the company by special resolution.

A resolution ratifying such action shall not affect any liability incurred by the directors or any other person; relief from any such liability must be agreed to separately by special resolution.

First EU Directive No 68/151/EEC

Article 9

1. Acts done by the organs of the company shall be binding upon it even if those acts are not within the objects of the company, unless such acts exceed the powers that the law confers or allows to be conferred on those organs.
However, Member States may provide that the company shall not be bound where such acts are outside the objects of the company, if it proves that the third party knew that the act was outside those objects or could not in view of the circumstances have been unaware of it; disclosure of the statutes[5] shall not of itself be sufficient proof thereof.
2. The limits on the powers of the organs of the company, arising under the statutes or from a decision of the competent organs, may never be relied on as against third parties, even if they have been disclosed.
3. If the national law provides that authority to represent a company may, in derogation from the legal rules governing the subject, be conferred by the statutes on a single person or on several persons acting jointly, that law may provide that such a provision in the statutes may be relied on as against third parties on condition that it relates to the general power of representation; the question whether such a provision in the statutes can be relied on as against third parties shall be governed by Article 3.[6]

The history surrounding statutory intervention on corporate capacity

Before CA 2006, an old-style memorandum of a company was required to state the company's objects. CA 2006, by contrast, drops the requirement for a memorandum in this form, and makes a statement of the objects optional

for companies registering after the Act came into force (s 31(1)).[7] In other words, if a statement of objects is made it will be contained in the **(p. 87)** articles; if none is made then the company's objects are unrestricted.[8] Much of the following discussion is irrelevant to companies with unrestricted objects. These companies avoid all the risks of having their actions classified as *ultra vires* (to the extent that there are such risks, given CA 2006 ss 39 and 40).

History of the development of objects clauses

The reasoning behind objects clauses was that those who invest in a company are entitled to know what type of enterprise it is. An equity investor in a gold-mining company, it has been said, would not wish to see his savings 'frittered away' in a fish and chip business; equally, those who give credit to a company may reasonably expect some indication of the scope of the activities of the enterprise with which they are dealing. But the objects clause did not survive long merely as a statement for the information of investors and creditors. It soon became the basis for the development of the '*ultra vires*' doctrine, which dominated the thinking in important areas of company law for over a century. The reforms made over the past 30 years (now reflected in CA 2006 ss 39 and 40) have deprived the doctrine of its central role, but it has not disappeared altogether.

The *ultra vires* doctrine was a rule concerned with the *capacity* of the company. It imposed artificial limitations on the acts and things which a company was regarded, in law, as capable of doing. Of course, as we saw in an earlier chapter, there are some acts which in the nature of things a company, or any other kind of corporation, simply cannot perform (eg marry or commit the crime of rape). But the *ultra vires* doctrine declared that, in addition to these natural limitations on a company's capacity, it was also to be regarded as incapable of doing anything which was not within the scope of its objects clause, or reasonably incidental thereto. The doctrine, in other words, restricted the powers of the company to matters covered by its stated objects, and any act which was outside those objects was not simply beyond the authority of the directors as a corporate organ, but beyond the capacity of the company itself—and, in the eyes of the law, a nullity having no effect whatever. It followed that not even the unanimous decision of the members could authorise or ratify such an act, as the House of Lords established in the leading case of *Ashbury Railway Carriage & Iron Co Ltd v Riche*[1875] LR 7 HL 653, HL.[9]

Although the doctrine was concerned to confine the activities of a company within its stated *objects*, it necessarily had the effect also of restricting the company's *powers*. The line between objects and powers is a difficult—perhaps an impossible—one to draw. The courts did make the concession that a company should be deemed to have implied powers to do anything reasonably incidental to its declared objects (*AG v Great Eastern Rly Co* (1880) 5 App **(p. 88)** Cas 473, HL) so that, for instance, a trading company could borrow money for the purposes of its trading business, but even then the position was not always clear. Could a company with surplus funds invest them in the shares of another company? Was this something which it had power to do, incidentally to its main business, or did it need to state in its memorandum that investing in shares was one of its objects?

The draftsmen of company memoranda, confronted with such uncertainties, chose to mini-mise the risk that outsiders might attack the company's actions for lack of capacity. They tried to put the matter beyond doubt by enlarging the objects clause and specifically including the making of investments as one of the objects of the company. Naturally, objects clauses become longer and longer.

The judges saw it as their role to fight a rearguard action against these attempts to undermine the *ultra vires* doctrine, perhaps seeing it as the strongest weapon they had to cope with cases of blatant corporate wrongdoing. They protested frequently at the length and prolixity of the drafting—a futile gesture, and a rather unbecoming attitude for them to take, since most of them must, as counsel, have spent much professional time earlier on in their careers in drafting and settling the very terms which they now sought to condemn!

By contrast, the insiders consistently aimed to ensure that the capacity of their companies should be as nearly unfettered as possible. Besides enumerating objects at great length,[10] draftsmen adopted other devices, such as: (i) specifying what are essentially powers as *objects* of the company (*Re Introductions Ltd* [1970] Ch 199, CA (indicating that the courts might not always be persuaded and might, despite the express words, construe the powers as merely incidental) and *Rolled Steel Products (Holdings) Ltd v British Steel Corpn* [1986] Ch 246, CA); (ii) including clauses designed to ensure that no listed object should be construed restrictively by being read as merely ancillary to some other object (an all objects are 'main objects' clause: see *Cotman v Brougham* [1918] AC 514, HL[11]); and (iii) authorising the company, or its directors, to determine any extensions to the company's

objects as may seem warranted (a 'subjective objects' clause: see *Bell Houses Ltd v City Wall Properties Ltd*[1966] 2 QB 656, CA): that is, 'To carry on any other trade or business whatsoever which can, in the opinion of the board of directors, be advantageously carried on by the company in connection with or as ancillary to … the general business of the company.'[12] Despite attracting judicial complaints, these drafting devices went a considerable way to mitigate the harshness of the *ultra vires* rule by minimising the occasions when it could be invoked.

The judges, too, assisted in this process. In the *Rolled Steel* case **[3.04]**, the Court of Appeal drew a distinction between a company's power or *capacity* to do an act (absence of which would render the contract *void*), and the exercise of that power or capability for improper ends. This distinction was used to save many transactions with third parties that had previously been regarded as beyond capacity, when it was thought that the company's powers could not (at law) be exercised for improper ends.

(p. 89) Calls for reform

As a result of the approaches previously described, the *ultra vires* doctrine struck most infrequently, but then with such random effect, that it was a hazard for the very people it was supposed to protect. These were the company's own members or shareholders and its unsuspecting creditors, who might naturally enough assume that a company with a properly drafted objects clause would have the power to do anything at all. Accordingly, the case for abolishing the doctrine altogether was for decades an unanswerable one.

It was suggested very early on by the Cohen Committee (Cmd 6659, 1945, para 12) that every company 'should, notwithstanding anything omitted from its memorandum of association, have as regards third parties the same powers as an individual. Existing provisions in memoranda as regards the powers of companies … should operate solely as a contract between a company and its shareholders as to the powers exercisable by the directors'. This recommendation was not implemented because the government at the time recognised that to abrogate the *ultra vires* principle without at the same time modifying the rule that all those dealing with a company were deemed to have constructive notice of its memorandum ('Constructive notice and its abolition', p 128) would be pointless. The outsider would simply be deemed to know that the *directors*had no *authority* to contract on a matter not covered by the objects clause (rather than that the *company* had no *capacity*). The constructive notice rule was thought too important to jettison without further consideration, so the *ultra vires* doctrine was left in place.

The Jenkins Committee (Cmnd 1749, 1962, para 42) recommended a different reform, which would have replaced the constructive notice doctrine with an elaborate set of statutory rules, but rather oddly did not urge the abolition of the *ultra vires* doctrine itself. Nothing came of that recommendation, either.

Meantime, countries all around the Commonwealth were taking steps to discard both doctrines by one technique or another, such as enacting comprehensive lists of statutory objects applicable to all companies, declaring companies to have the full legal capacity of a natural person, allowing 'unlimited objects' clauses, making the objects clause optional, and even (in the case of the Isle of Man) banning the registration of objects clauses altogether.

When the UK acceded to the Treaty of Rome in 1972, it was finally necessary to make modifications to the doctrines of *ultra vires* and constructive notice in order to comply with Art 9 of the First EU Company Law Directive (see the previous extract). Article 9 was concerned (inter alia) to ensure that a third party dealing with a company should not be disadvantaged by the possibility that the company was acting beyond its capacity. In the UK, this was effected by s 9(1) of the European Communities Act 1972 (later consolidated as Companies Act 1985 (CA 1985) s 35, in its original form, then CA 1985 ss 35, 35A and 35B, and now CA 2006 ss 39 and 40). The drafting of the very first of these provisions was defective in a number of respects. There were suggestions it did not even meet the demands of the Directive. The result was most unsatisfactory: the harshest effects of the *ultra vires* doctrine were undoubtedly avoided in part, but the doctrine itself was allowed to survive.

Further reform came in 1989, following recommendations made by Professor Prentice in his Report, published in 1986. These recommendations also dealt with the doctrine of constructive notice ('Constructive notice and its abolition', pp 128ff) and the apparent authority of corporate representatives ('Summary of agency principles', pp 95ff). Section 35 of CA 1985 was recast, so as to prevent the validity of any act done by a company from being

called into question on the ground of lack of capacity (see 'Statutory provision protecting third parties (outsiders) from the consequences of constitutional limitations on corporate capacity', p 85). But, once again, the *ultra vires*doctrine itself was not abolished.

CA 2006 is in many respects the same. The *ultra vires* doctrine therefore survives for some internal purposes; has been used as a justification for imposing a disqualification**(p. 90)** order on a director (*Re Samuel Sherman plc* [1991] 1 WLR 1070); and continues to apply to charitable companies (s 35(4)), and to bodies not governed by the Companies Acts. On the 'internal purposes', the abolition of the traditional connection between a company's objects clause and its capacity does not mean that those acting on behalf of the company now have carte blanche to do what they like in the company's name. A member has always had a right to seek an injunction to prevent the company from entering into what would have been an *ultra vires* transaction. And directors must observe any limitations on their powers flowing from the company's constitution (s 171), and will be liable to the company for any breaches.

The problem now is to decide just how much of the massive body of case law which the doctrine generated in its heyday it remains important to know. It will still be necessary at times to construe a company's objects clause, particularly in the context of directors' duties when it is necessary to know the proper scope of the directors' activities, so knowledge of some, at least, of the old cases will be required for this purpose. A small number of these cases are therefore noted in the following section.

Finally, remember that objects clauses are contained in the company's articles (if they are included at all), and unless these provisions in the articles are entrenched, the articles can be changed by special resolution (ss 21 and 22, and see 'Alteration of the articles', p 219); and special resolutions can, it would seem, be passed informally (see ss 29, 281, 283, and 'Informal decision-making—the "*Duomatic*" principle', p 206).

Interpreting objects clauses

As noted earlier, it is usually no longer necessary for outsiders to concern themselves with limitations in the corporate constitution: see CA 2006 ss 39 and (noting the good faith requirement in the latter section) at 'Authority of the company's agents', p 84. But if the directors successfully commit the company to a contract which is outside the company's objects, and thus outside the directors' *actual* authority and therefore in breach of CA 2006 s 171, then the company may be in a position to seek a remedy from its defaulting directors. In pursuing that claim, the company will have to prove that the company's constitution prohibited the directors' actions, and that will involve construing the objects clauses, perhaps using the following cases.

Some powers—such as the power to borrow—may be construed restrictively by the court as incidental powers, even though declared by the memorandum to be objects.

[3.02] Re Introductions Ltd [1970] Ch 199 (Court of Appeal)

The litigation concerned the validity of a secured loan. Before the loan was granted, the bank was given a copy of the company's memorandum and articles, and was expressly aware that the company was carrying on the business of pig breeding, which was *ultra vires*. The bank unsuccessfully argued that the company nevertheless had the power to borrow, even for this purpose, because the company's objects included the power to borrow, and made that power an 'independent' object.

> HARMAN LJ: [After outlining the facts.] There is also in this memorandum a form of words which is common enough, and has been for many years; the words at the end of the objects clause are these: 'It is hereby expressly declared that each of the proceeding sub-clauses shall be construed independently of and shall be in no way limited by reference to any other sub-clause and that the objects set out in each sub-clause are independent objects of the company.' Of course, the original idea of that form of words was to avoid the old difficulty, which was that there was a main objects **(p. 91)** clause and all the others were ancillary to the main objects; and many questions of ultra vires arose out of that.
>
> It was argued, therefore, that the only obligation of the bank was to satisfy itself that there was an express power to borrow money, and that this power was converted into an object by the concluding words of the

> objects clause which I have read. It was said that, if this was so, not only need the bank inquire no further but also that it was unaffected by the knowledge which it had that the activity on which the money was to be spent was one beyond the company's powers.
>
> The judge rejected this view, and I agree with him. He based his judgment, I think, on the view that a power or an object conferred on a company to borrow cannot mean something in the air: borrowing is not an end in itself and must be for some purpose of the company; and since this borrowing was for an ultra vires purpose, that is an end of the matter.
>
> Mr Walton, I think, agreed that if sub-clause (N) must in truth be construed as a power, such a power must be for a purpose within the company's memorandum. He says that it is 'elevated into an object' (to use his own phrase) by the concluding words of the objects clause in the memorandum, and this object, being an independent object of the company, will protect the lender and that that is its purpose. I answer that by saying that you cannot convert a power into an object merely by saying so …
>
> I agree with the judge that it is a necessarily implied addition to a power to borrow, whether express or implied, that you should add 'for the purposes of the company'. This borrowing was not for a legitimate purpose of the company: the bank knew it, and, therefore, cannot rely on its debentures. I would dismiss the appeal.

➢ Notes

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1. The approach of *Re Introductions Ltd* to the construction of objects clauses, including the 'demotion' in appropriate cases of 'objects' to 'incidental powers', has been endorsed in later cases. However, in *Rolled Steel Products* it is suggested that the decision in *Introductions* should be seen as resting not on *ultra vires* but on the basis that the directors had abused their powers or exceeded their authority. See the discussion at 'Failure to act for proper purposes', p 331. What difference does this make to the relevant legal analysis and to the practical outcome for the various parties potentially affected?

2. One type of corporate 'object' which sometimes calls for particular attention in this connection is that of making gifts and paying pensions and gratuities. *Re Horsley & Weight Ltd* **[4.30]** illustrates that such provisions can be legitimate substantive objects of a company, although it is now possible that such transactions might be open to attack under IA 1986 s 238, as being 'at an undervalue'.

3. By contrast, in the Court of Appeal in *Brady v Brady* **[10.08]**, Nourse LJ expressed views which suggest that the *ratio decidendi* of *Re Horsley & Weight Ltd* may have a restricted application. He said:

> In its broadest terms the principle is that a company cannot give away its assets. So stated, it is subject to the qualification that in the realm of theory a memorandum of association may authorise a company to give away all its assets to whomsoever it pleases, including its shareholders. But in the real world of trading companies, charitable or political donations, pensions to widows of ex-employees and the like apart, it is obvious that such a power would never be taken. The principle is only a facet of the wider rule, the corollary of limited liability, that the integrity of a company's assets, except to the extent allowed by its constitution, must be preserved for the benefit of all those who are interested in them, most pertinently its creditors.

The House of Lords reversed the decision of the Court of Appeal in this case without commenting on these remarks.

(p. 92) ***An act which comes within the scope of a power conferred expressly or impliedly by the company's constitution is not beyond the company's capacity by reason of the fact that the directors entered into it for some improper purpose.***