

# LL.B IV SEMESTER

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## **SUBJECT- COMPANY LAW**

### **TOPIC- DOCTRINE OF ULTRA VIRES**

The object clause of the memorandum of the company contains the object for which the company is formed. An act of the company must not be beyond the object clause otherwise it will be ultra vires and therefore, void and cannot be ratified even if all the member wish to ratify. This is called the doctrine of ultra vires. The expression “ultra vires” consists of two words: ‘ultra’ and ‘vires’. ‘Ultra’ means beyond and ‘Vires’ means powers. Thus, the expression ultra vires means an act beyond the powers. Here the expression ultra vires is used to indicate an act of the company, which is beyond the powers conferred on the company by the objects clause of its memorandum. An ultra vires act is void and cannot be ratified even if all the directors wish to ratify it. Sometimes the expression ultra vires is used to describe the situation when the directors of a company have exceeded the powers delegated to them. Where accompany exceeds its power as conferred on it by the objects clause of its memorandum, it's not bound by it because it lacks legal capacity to incur responsibility for the action, but when the directors of a company have exceeded the powers delegated to them. This use must be avoided for it is apt to cause confusion between two entirely distinct legal principles. Consequently, here are restricting the meaning of ultra vires objects clause of the company's memorandum.

#### **Protect to Creditors & Investors**

Doctrine of ultra vires has been developed to protect the investors and creditors of the company. This doctrine prevents a company to employ the money of the investors for a purpose other than those stated in the objects clause of its memorandum. Thus, the investors and the company may be assured by this rule that their investment will not be employed for the objects or activities which they did not have in contemplation at the time of investing their money in the company. It enables the investors to know the

objects in which their money is to be employed. This doctrine protects the creditors of the company by ensuring them that the funds of the company to which they must look for payment are not dissipated in unauthorized activities. The wrongful application of the company's assets may result in the insolvency of the company, a situation when the creditors of the company cannot be paid. This doctrine prevents the wrongful application of the company's assets likely to result in the insolvency of the company and thereby protects creditors. Besides the doctrine of ultra vires prevents directors from departing the object for which the company has been formed and, thus, puts a check over the activities of the directions. It enables the directors to know within what lines of business they are authorized to act.

### **Origin of Doctrine of Ultra Vires**

Doctrine of ultra vires has provides protection to the investors and creditors o the company. The doctrine of ultra vires could not established its roots. It established its roots in 1875 when the Directors, and Company, of the Ashbury Railway Carriage and Iron Company (Limited) v Hector Riche, (1874-75) L.R. 7 H.L. 653 as decided by the House of Lords. A company called "The Ashbury Railway Carriage and Iron Company," incorporated under the Companies Act, 1862.

### **Ashbury Railway Carriage and Iron Company (Limited) v Hector Riche, (1874-75) L.R. 7 H.L. 653**

A company called "The Ashbury Railway Carriage and Iron Company," incorporated under the Companies Act, 1862. The objects listed in the object clause of memorandum of association were :

1. to make, and sell, or lend on hire, railway carriages and waggons,
2. and all kinds of railway plant, fittings, machinery, and rolling-stock;
3. to carry on the business of mechanical engineers and general contractors ;
4. purchase, lease, work, and sell mines, minerals, land, and buildings;
5. to purchase and sell, as merchants, timber, coal, metals, or other materials,
6. and also to buy and sell any such materials on commission or as agents.

The directors agreed to enter into contract to construct a railway line in Belgium. The contract was between The Ashbury Railway Carriage and Iron Company and Hector Riche. The contract was for supplying the materials required for construction of Railway lines.

The objects under the object clause of this company were to supply and sell the materials required to construct railways. It does not cover construction of railway lines. The contract here was to construct a railway. That was contrary to the memorandum of association. So the contract was Ultra Vires to the company.

As held by House of Lords that this contract was ultra vires not only of the director but also of whole company. Even if majority of shareholder ratify it, then to it can not change. It will still remain ultra vires of the whole company.

This doctrine got its roots firm in 1875 in case of Ashbury Railway Carriage and Iron company Ltd. v. Riche. Thus the expression ultra vires means an act beyond the powers. An ultra vires act is void and cannot ratified even by majority of shareholders. Even if special resolution passed by shareholder with majority of votes, then also its ratification cannot happen. Where a company exceeds its power as conferred by objects clause, its not bound by it because it lacks legal capacity to incur responsibility for the action.

**Basic principles included the following:**

1. An ultra vires transaction cannot be ratified by all the shareholders, even if they wish it to be ratified.
2. The doctrine of estoppel usually precluded reliance on the defense of ultra vires where the transaction fully performed by one party
3. A fortiori, a transaction fully performed by both parties could not attacked.
4. The contract fully executory, the defense of ultra vires might also raised by either party.
5. If the contract partially performed, and the performance held insufficient to bring the doctrine of estoppel into play, a suit for quasi contract for recovery of benefits conferred available.
6. If an agent of the corporation committed a tort within the scope of his or her employment, the corporation could not defend on the ground the act was ultra vires.

**Exceptions-**

Following are the exceptions to Doctrine of Ultra Vires:

1. An act intra vires of the company but outside the authority of the directors may be ratified by the shareholders.
2. An act intra vires of the company but done in an irregular manner. It can turn into valid by shareholders consent.
3. If the company has acquired any property through an investment, ultra vires of the contract, the company's right over such a property shall still be secured.
4. While applying doctrine of ultra vires, the effects incidental or consequential to the act shall not be invalid unless they are expressly prohibited by the Company's Act.
5. There are certain acts under the company law, which though not expressly stated in the memorandum, are deemed impliedly within the authority of the company and therefore they are not deemed ultra vires. For example, a business company can raise its capital by borrowing.
6. If an act of the company is ultra vires the articles of association, the company can alter its articles in order to validate the act.