NOTES AND COMMENTS

Corporations and the Doctrine of Ultra Vires.

Discussion in this and the last issue of *Res Judicatae* of problems arising from the application to bodies corporate of the doctrine of *ultra vires* tempts one to speculate in what respects improvements might be made in this branch of the law. As the life of the community tends to become dominated more and more by the activities of corporations, State and private, trading and non-trading, the importance of ensuring that the law relating to them is adjusted as closely as possible to social and economic requirements is obvious.

What, then, are the social interests involved? The cardinal interest is that, vested in the community as a whole, which arises out of the fact that the development of industry and commerce has called for the replacing of the individual capitalist by the large corporation—whether it be set up by the State or by private enterprise. This interest broadly put is that the law should give ready recognition to and should facilitate the formation and functioning of bodies corporate. Let us concede for the present that this need has been sufficiently met, at any rate in the industrial and commercial spheres (with which these comments are chiefly concerned), by the Companies Acts of last century. There still remain, however, further interests to be considered. These may be regarded as of two classes. First there are the interests of the public generally which has to deal with and finds itself affected by the operations of corporate bodies. Secondly there are the interests of the members or shareholders themselves who have invested capital in corporations.

Both these interests have claims to the protection of the law. The problem is to correlate them. Although one might have thought that of the two the first was that deserving of the law's most anxious protection the tendency in fact has been to sacrifice it to the second. Thus where one is injured by the *ultra vires* torts of a corporation he may find himself without remedy against it,[1] the courts having tended to emphasize the importance of safeguarding the shareholders from liability in respect of an undertaking which theoretically they could not authorize (though they may be reaping the benefit of it) rather than the need for adequately protecting the public against tortious acts.

In reality, however, the two interests referred to are not necessarily conflicting, and it is submitted that solutions are available which effectively safeguard both.

The solution here suggested has two aspects. In the first place it requires that in relation to the public a corporation should be regarded in all respects as a natural person with the full legal capacity of a natural person and subject to the same degree of liability. Secondly it requires that as between the corporation and its members the activities of the corporation should be strictly controllable in accordance with the objects for which it is incorporated.

1. *Poulton* v. *London & South Western Railway*, L.R. 2 Q.B. 534.

The first aspect involves the frank recognition by the Courts of the "real" as opposed to the "fictional" nature of corporate personality. In particular it means that the theory according to which the legal capacity of a corporation (and so its legal liability) is defined and limited by its Act, Charter, or Memorandum of Association must give way to a recognition that its conduct whether, within its objects or not, does very really affect the public. From the point of view of the public generally there is no practical justification for treating a corporation differently from a natural person. It acts in the main in a similar fashion to a natural person. The practical consequences of its actions are not different. Why should those actions, then, have a different legal consequence?

It is obvious, of course, that the gravest flaw arising out of the application to corporations of the doctrine of *ultra vires* is in the sphere of tort. Where one contracts with a corporation it is at least possible, though it is increasingly impracticable, to ascertain by searching whether the company has power to enter into the contract. But it seems unreasonable to throw on to the public the burden of ascertaining what is often a difficult question of interpretation—namely whether a particular undertaking is within the company's powers or not. Accordingly it is suggested that the same principles should apply in respect both of contract and tort.

This first aspect of the proposed solution in fact involves little more than the application to statutory corporations of what appears to have been the general practice of the Common Law in relation to the corporations known to it.[2] At Common Law a corporation has power as was determined in the *Sutton's Hospital* Case,[3] to do all such acts as a natural person can do. Even a direction in the Royal Charter by which it is created limiting its powers by express negations, though its breach may be a ground for annulling the Charter, cannot derogate from the plenary power with which the Common Law endows it.[4]

Writing of corporations at Common Law Holdsworth[5] remarks that it would seem that "so far as criminal or civil liability is concerned, the courts have always been prepared to hold that a corporation is as capable of being held liable as a natural person." It is interesting to notice that he regards the bursting of the South Sea Bubble as the point from which the application of the doctrine of *ultra vires* gains ground.

The second part of the suggested solution involves on the one hand a strengthening of the requirements regarding the definition of the Company's objects so that persons becoming members may know at least what its main objects are, and on the other hand the provision of an effective procedure by which they may, if they desire, confine its activities accordingly. The need for the former is forcibly expressed by Lord Wrenbury in *Cotman* v. *Brougham*.[6] After em-

2. c.f. Holdsworth: *History of English Law*, Vol. IX, pp. 49-70.
3. (1612) 10 Co. Rep. 30b.
4. Palmer: *Company Law*, 15th Edn. p. 3 c.f. per Bowen L.J., *Baroness Wenlock* v. *River Dee Company*, 36 Ch. D. 685, n.
5. Holdsworth: loc. cit. p. 53.
6. [1918] A.C. 514 at 522 and 523.

phasizing the distinction between the objects of a company and its powers for effecting those objects, and stating that powers are not required to be, and ought not to be, specified in the memorandum of association he proceeds: "There has grown up a pernicious practice of registering memoranda of association which under the clause relating to objects, contain paragraph after paragraph not specifying or delimiting 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 included somewhere within its term."

The need for machinery to enable the members of a corporation to confine its activities to the objects so stated arises mainly in respect to the interests of a dissentient minority. If a majority disapproves of the company's activities it can, as a rule, enforce its view by direct methods. A minority, however, must rely on the aid of the Court to protect its interests. In the Act at present there exists machinery which can be used for the purpose. The Court, relying on its powers to wind up a company where it is just and equitable so to do[7], can and on occasions will, order a company to be wound up where its main object—its substratum—has vanished.[8] But the remedy might in conjunction with measures for tightening up of the practice relating to Statement of Objects be made more readily available.

In any such measures, however, the dangers of inelasticity must be carefully borne in mind. Industrial and commercial conditions and needs are apt to change rapidly, and it is in the interest of the community at large as well as of the shareholders, that a company should be able to adopt new objects and so satisfy new social needs so long as no substantial injury is done thereby to a minority. Probably the existing provisions of the Act enabling the objects to be altered with the consent of the Court[9] are, if liberally applied, sufficient for the purpose.

It is submitted that reform in the directions mentioned would alleviate many of the major defects involved in the application to corporations of the doctrine of *ultra vires*. Whether such reform is now possible without legislative action is beyond the scope of these comments, but one is tempted to find in recent years an increasing tendency for the Courts to adopt a wide construction of the objects clauses as between the company and the public, while suggesting that as between it and its members only it may still be necessary to construe the memorandum in the more restricted light of the company's "main objects."

J.B.H.

7. Companies Act 1928, Sec. 137.
8. e.g., German Date Coffee Co., 20 Ch. D., 169.
9. Companies Act, 1928, Sec. 17.