FROM *ULTRA VIRES* TO AGENCY: A COMMENT ON THE RECENT MODIFICATIONS TO THE *ULTRA VIRES* DOCTRINE*

This article deals with the many deficiencies in the new model *ultra vires* doctrine introduced by the recent English Court of Appeal decision in the *Rolled Steel* case. This article also assesses the impact of this decision on Section 25 of the Singapore Companies Act.

I. INTRODUCTION

SECTION 25(1) of the Singapore Companies Act[1] modifies the harsh common law rule that *ultra vires* transactions are absolutely void, and provides in effect that no act of a company is to be invalid by reason only that the company was without capacity or power to do the act.[2] Unfortunately, the circumstances under which the company is deemed to be acting without capacity or power are undefined by the Act. In this connection, one needs to rely on common law and, especially, the English *ultra vires* doctrine for the definition of the circumstances under which a company is deemed to be acting without capacity or power. It follows that the scope of section 25(1) is, perhaps undesirably, affected by the changes in the development of the English *ultra vires* doctrine. To assess the impact of these changes on the section it is necessary to trace the recent development in this common law doctrine.

The English *ultra vires* doctrine has long suffered from deficiencies in that the bases upon which it operates lack consistency and rationality. It is thought to be fundamental to the doctrine that a distinction be maintained between objects and powers in a company's memorandum so that any corporate transaction that falls within the scope of an object is necessarily *intra vires* whereas a corporate transaction that falls within the scope of a power is *intra vires* only if it is exercised for a purpose ancillary or reasonably incidental to the pursuit of the objects. Any transaction that falls within the scope neither of an object nor a power is of course *ultra vires.* But, in 1871, Sir

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1 The full text of section 25(1) of the Companies Act, Cap. 185, 1970 Rev. Ed. (Reprint, 1985) is as follows: "No act or purported act of a company (including the entering into of an agreement by the company and including any act done on behalf of a company by an officer or agent of the company under any purported authority, whether express or implied, of the company) and no conveyance or transfer of property, whether real or personal, to or by a company shall be invalid by reason only of the fact that the company was without capacity or power to do such act or to take such conveyance or transfer."

2 See commentary on a similar Australian provision in Wallace and Young, *Australian Company Law And Practice,* (1965) p. 98.

G. Mellish LJ. decided in *Re Marseilles Extension Railway Company,*[3] the first in a line of cases, that the validity of an exercise of power depended upon whether the outsider had notice of the improper purpose behind the transaction in question. In 1932, there was a further deviation from the established norms in that Eve J, in the now infamous case of *Re Lee, Behrens & Company Ltd.*,[4] decided that whether a transaction was binding or not was dependent upon whether it satisfied a three-limb test with different criteria, one of which was whether the transaction is entered into for the benefit of the company.

Recently, in the case of *Rolled Steel Products v. British Steel Corporation,*[5] the English Court of Appeal decided that the purpose behind a transaction should not be the determining factor in deciding its legality. If a transaction falls within the scope of a power expressly or impliedly conferred by the company's memorandum it remains binding regardless of the purpose behind the transaction because the company has through its memorandum held out its directors as having ostensible authority as agents of the company to enter into that transaction.

It is the intention of the writer to argue that this attempt to graft the concept of ostensible authority under the law of agency on to the *ultra vires* doctrine is undesirable as it does not remove or resolve the existing confusion. The paper also attempts to explain the reasons giving rise to the conflicting bases in the *ultra vires* doctrine. The rest of the paper assesses the impact of the *Rolled Steel* decision on section 25 and recommends that the decision be rejected. An additional reason for recommending its rejection is that many of the problems inherent in the *ultra vires* doctrine have been avoided in the Singapore context because section 23 and the third schedule of the Singapore Companies Act have comprehensively set out many specific powers of a company.

II. THE ORIGIN OF THE CONCEPT OF LIMITED CAPACITY AND A NORMATIVE MODEL OF THE ANCILLARY *ULTRA VIRES* DOCTRINE

In the legal context, a power is the ability to effect a particular change in a given legal relation.[6] In this regard, an individual has the natural legal power to enter into any binding contractual relationship. In contrast, companies are endowed with these capabilities and powers by the law.[7] It follows that unlike an individual, a company may only legitimately exercise powers that have been endowed by law.[8] A company's legal competence and capacity is thus limited because

3 [1871] L.R. 7 Ch. 161.
4 [1932] 2 Ch. 46.
5 [1984] B.C.L.C. 446.
6 See Hohfeld, "Some Fundamental Legal Conceptions as Applied in Judicial Reasoning", (1913-14) 23 Yale L.J. 16, 44-45.
7 See Wolff, "On The Nature Of Legal Persons", (1938) 54 L.Q.R. 494, 496.
8 This state of affairs resulted because the House of Lords in the case of *Ashbury Railway Carriage And Iron Co.* v. *Riche* (1875) L.R. 7 H.L. 653 declared that a company incorporated under the Companies Act ought not to be regarded as a common law corporation endowed with full powers, but as a statutory corporation endowed with limited powers only.

the Companies Act would normally require a company to state in its memorandum the objects of the company.[9]

The justification for the creation of a limited capacity company is that it offers greater protection to investors and creditors alike as company assets are prevented from being dissipated in unauthorized activities. However, this strict and uncompromising definition of the early *ultra vires* rule has to be somewhat relaxed because whilst the Companies Act requires a company to state the powers necessary for the accomplishment of these objects, it inevitably follows that the powers necessary for the attainment of these objects must be impliedly created. Buckley L.J. in *Re Horsely & Weight Ltd.*[10] has justified this need for implied powers in the following words:[11]

> "... for it is the practical need to imply the power in order to enable the company effectively to pursue its authorised objects which justifies the implication of the powers."

As noted by an author, "the strict rule is also to be applied reasonably so that whatever is fairly incidental to the objects expressly authorized by the memorandum or statute will, unless expressly prohibited, be *intra vires.*"[12]

Today, the modern expression of this rule is that an exercise of power is *intra vires* if it is ancillary or reasonably incidental to the pursuit of an authorized object.[13]

It is interesting to note that section 23(1) of the Companies Act expressly provides that the powers of a company shall include the power to make donations for patriotic or for charitable purposes; the power to transact any lawful business in aid of Singapore in the prosecution of any war or hostilities in which Singapore is engaged; and more pertinently the powers set forth in the Third Schedule to the Act.

It also follows from the above discussion that the distinction between objects and powers is important. The reason is that true objects are in substance well-defined business activities or purposes which are capable of being pursued in isolation as the sole activity of the company.[14] Such objects are therefore truly capable of defining and limiting a company's capacity. Powers, on the other hand, are mere abilities which may be exercised for any purpose including those purposes that are neither ancillary nor incidental to the pursuit of authorized objects. For example, having the power or ability to walk will lead one astray unless one is walking towards a predetermined destination. Therefore to treat what is in essence a power as an object because it has been illegally included in the memorandum is dangerous as its operation would render a company's limited capacity limitless!

[9] The relevant provision here is in section 22(1) of the Singapore Companies Act, *supra,* note 1.
[10] [1982] Ch. 442.
[11] *Ibid*., p. 448.
[12] See L.C.B. Gower, *Gower's Principles of Modern Company Law* (4th Ed., 1979) p. 165.
[13] *Per* Buckley L.J. in *Re Horsley & Weight Ltd.,* [1982] Ch. 442, 448.
[14] *Ibid.*

The role of the *ultra vires* rule is therefore to prevent this insidious enlargement of a company's capacity as a result of indiscriminate exercises of powers for purposes that are neither ancillary or reasonably incidental to the pursuit of authorized objects by rejecting such exercise of powers as being null and void. Although this may result in a very harsh treatment of an outsider who is a *bona fide* purchaser dealing with the company in good faith without notice,[15] this remains necessary if the whole rationale of the *ultra vires* doctrine is to be preserved. In summary, a normative model of the *ultra vires* doctrine which should serve as a reference point may be expressed in the following sub-rules:

(i) a distinction must be drawn between objects and powers;

(ii) an express power is a power that is found in the objects clauses of a memorandum;

(iii) an implied power is created by a process of implication on the ground that a company must necessarily possess powers to do acts for purposes that are either ancillary or reasonably incidental to the pursuit of the authorized objects;

(vi) a transaction that is entered into in direct pursuance of an object in the memorandum is valid and binding;

(v) a transaction that falls within the scope of an implied or express power is valid and binding only if it is exercised for a purpose ancillary or reasonably incidental to the pursuit of the authorized objects in a company's memorandum.

It can be noted from steps (iii) and (v) that the requirement that a power must be exercised for a purpose ancillary or reasonably incidental to the objects is used not only as a touchstone for the implied creation of powers but also as a control mechanism to ensure that powers are exercised within the bounds or capacity of the stated objects.

However, in this age of a complex and fast changing economic environment, a company's dexterity to switch or undertake new business activities may be vital for its survival. Also businessmen today prefer to operate a group of companies rather than a sole company in order to take full advantage of limited liability. The concept of a limited capacity company therefore fetters rather than facilitates business expediencies of the above nature. As a result, evasion techniques abound. The other serious shortcoming of the *ultra vires* doctrine is that it operates harshly on innocent outsiders who constantly run the risk of their transactions with the company being rendered null and void if the purpose of the transaction is outside the scope of the memorandum. As a result, conscious judicial efforts have been made to counter evasion of the *ultra vires* doctrine and also to ameliorate its inherent harshness. The recently developed *ultra vires* doctrine therefore reveals marked deviations from the normative model.

[15] See Gregory, "*Rolled Steel Products (Holdings) Ltd.* v. *British Steel Corp.* — Only Swarf for Liquidators", (Jan/Feb 1985) Insolvency L. & P., 17, 18.

III. DRAFTING TECHNIQUES TO OVERCOME THE *ULTRA VIRES* DOCTRINE

It is fundamental to the normative model of the *ultra vires* doctrine that a distinction be maintained between objects and powers. The reason is that any corporate transaction that falls within the scope of an object is necessarily *intra vires* whereas a corporate transaction that falls within the scope of a power is *intra vires* only if it is exercised for a purpose ancillary or reasonably incidental to the pursuit of the objects. To evade these rules it is now a common practice to masquerade powers as objects. Company powers are not left to a process of restrictive implication and are instead expressly provided for in a company's memorandum. This measure creates what a writer has described as "the baffling express powers"[16] that greatly confuse the distinction between objects and powers.

Apart from the above, other drafting techniques are also employed to produce results that would obfuscate the clear distinction between objects and powers. For example, it is a widespread drafting technique to enumerate the objects clause in the memorandum at great length so as to render a company's limited capacity almost limitless! The courts initially responded by construing only one of these objects as the main object and regarded the rest as only ancillary powers. This caused the business community to insert what is now known as the *Cotman* v. *Brougham* clause which is an express declaration in the objects clause to the effect that each of the specified objects or powers should be deemed to be independent and not ancillary or subordinate to any other objects. The House of Lords in *Cotman* v. *Brougham*[17] approved of such a clause and Lord Parker of Waddington justified the result on the ground that:[18]

> [a] person who deals with a company is entitled to assume that a company can do everything which it is expressly authorised to do by its memorandum of association....

Subsequently, it was felt that if the effect of such a clause remained unchecked it would seriously undermine the *ultra vires* doctrine. Several judges began to express the view that where objects were really mere powers they must be so treated notwithstanding the presence of a separate objects clause.[19]

This view was also affirmed by Slade L.J. in his judgment in the recent *Rolled Steel* case where he accepted the argument that full force must be given to the *Cotman* v. *Brougham* clause unless the power in question is by nature incapable of constituting a substantive object.[20] Clearly, an independent clause would not elevate what is essentially a power into an object. However, what is more interesting is that in *Rolled Steel,* Slade L.J. actually subjected the *Cotman* v. *Brougham* clause to one more restriction. He took the view that a construction of the memorandum as a whole might show

16 See Shapira, *"Ultra Vires Redux",* (1984) 100 L.Q.R. 468, 469.
17 [1918] A.C. 514.
18 *Ibid*., at p. 521.
19 See for example Buckley L.J.'s judgement in *Re Horsley & Weight,* [1982] 1 Ch. 442 at p. 448.
20 [1984] B.C.L.C. 446, at p. 501.

that the sub-clause, whether containing a power or an object, was intended as an ancillary power only.[21]

IV. THE DEVIATIONS PRIOR TO THE *ROLLED STEEL DECISION*

The above discussion reveals the extent to which attempts have been made to evade the *ultra vires* rule and how judges have tried to contain these efforts. We should next examine how judges in trying to ameliorate the harshness inherent in the doctrine are themselves responsible for introducing rules that are in conflict with those sub-rules in the normative model of the *ultra vires* doctrine.

First, Eve J. in the case of *Re Lee, Behrens & Company Ltd,*[22] decided that whether a transaction is binding or not is dependent upon whether it satisfies a three-limb test as follows:[23]

(i) Is the transaction reasonably incidental to the carrying on of the company's business?

(ii) Is it a *bona fide* transaction? and

(iii) Is it done for the benefit and to promote the prosperity of the company?

It is submitted that these sub-tests represent serious deviations from the body of normative *ultra vires* sub-rules. Under the orthodox *ultra vires* doctrine the first question to ask in deciding whether a transaction is valid is whether the company has the power to enter into the transaction in question in the sense that if the power were not expressly provided it is one that could be implied as being ancillary or reasonably incidental to the pursuit of the authorized objects. The second question is whether the transaction falls within the power in question. Having cleared the first two hurdles, the third question is whether the transaction is entered into for a purpose that is also ancillary or reasonably incidental to the pursuit of the authorized objects. In contrast, the first limb of Eve J.'s test is tantamount to suggesting that a company has the power to enter into any transaction so long as it can be vaguely justified as being reasonably incidental to the carrying on of the company's business. In this regard, the whole rationale of the *ultra vires* doctrine, namely to limit the creation and the scope of a company's powers and then to control the purpose of a particular transaction is completely ignored.[24] As regards the *bona fide* transaction and benefit to the company requirements which respectively constituted the second and third limb of Eve J.'s test, they are clearly irrelevant considerations, under the normative *ultra vires* doctrine. Under this doctrine it is the purpose behind the transaction that matters and neither the subjective good faith of the directors nor the element of benefit to the company should count. By not taking the purpose of the transaction into account except for the requirement that it must be for the benefit of the company, the control mechanism under the normative *ultra vires* doctrine which requires

21 *Ibid.*
22 [1932] 2 Ch. 46.
23 *Ibid.*, at p. 51.
24 *Supra,* note 15.

that the purpose of the transaction must be ancillary or reasonably incidental to the pursuit of authorized objects is bypassed.

A second serious deviation to the normative *ultra vires* doctrine came about as a result of Sir G. Mellish L.J.'s decision in *Re Marseilles Extension Railway Company Ltd,*[25] where he held that the validity of an exercise of express power depended upon whether the outsider had notice of the improper purpose behind the transaction in question. This is absurd as the only ground on which a company may validly exercise a power is if it is for a purpose that is ancillary or reasonably incidental to the pursuit of a company's objects.[26] The issue of notice should have been totally disregarded.

In the light of these deviations and controversies the recent Court of Appeal judgment in *Rolled Steel Products* v. *British Steel Corporation*[27] on an *ultra vires* issue deserves close scrutiny, especially as the judgment has been described as an attempt by one of the judges to remodel the *ultra vires* doctrine.[28]

V. THE *ROLLED STEEL* "NEW MODEL" *ULTRA VIRES* DOCTRINE

The facts of the case are that there were four companies involved in a chain of indebtedness. One SSS Ltd. owed some £860,000 to a C Ltd. On the other hand, SSS Ltd. was a creditor of Rolled Steel Products (Holdings) Ltd (RSP) and had lent to RSP a sum of £400,000. However, both SSS Ltd. and RSP were owned and controlled by the Shenkman family. Subsequently, C Ltd was taken over by the British Steel Corporation (BSC) which continued to press SSS Ltd for the repayment of its debts to C Ltd.

To ensure that SSS Ltd would finally repay its debt, BSC pressed for a personal guarantee by Mr. Shenkman as well as a company guarantee by RSP which owned sufficient assets to meet the debt. Although Mr. Shenkman acceded to the demand, RSP could not readily do so as the payment under the guarantee by RSP to BSC which was in excess of RSP's debt of £400,000 to SSS Ltd might subsequently have been attacked as a fraudulent preference over RSP's creditors and perhaps even as an act of misfeasance on the part of the directors.

(1) *The Scheme*

The solution to this problem was that C Ltd would lend a further £401,448 to RSP before RSP issued the guarantee to BSC. This money would then be used to extinguish RSP's debt to SSS Ltd and SSS Ltd would, in turn, use the same partially to reduce its debt of £860,000 to C Ltd. Having transferred, in effect, a portion of SSS Ltd's debt to RSP, RSP would then agree to guarantee the balance of SSS Ltd's debt to C Ltd and failing that, RSP was to issue a debenture in favour of C Ltd.

25 [1871] L.R. 7 Ch. 161.
26 See Baxter, *"Ultra Vires and Agency Untwined",* [1970] 29 C.L.J. 280, 281.
27 [1984] B.C.L.C. 446.
28 See Gregory, *"Rolled Steel (Holdings) Ltd.* v. *British Steel Corporation",* (1985) 48 M.L.R. 109, 110.

(2) *The Approval of The Scheme By RSP's Board of Directors*

A disquieting feature of the scheme was that Mr. Shenkman had earlier personally guaranteed SSS Ltd's indebtedness to C Ltd. The transfer of a portion of SSS Ltd debt to RSP served to benefit him as it would reduce his liability under his guarantee. In contravention of Article 17 of RSP's Articles of Association, Mr Shenkman subsequently approved of the scheme without any declaration of his self-interest in this series of transactions.

(3) *The Causes of Action*

On 25 March 1975, RSP brought an action against BSC, the receiver, the trustees in bankruptcy of Mr Shenkman, and his father on the following grounds:—

(i) neither the guarantee nor the debenture was the deed of RSP, because it was not duly executed by RSP. The reason was that Mr Shenkman was personally interested in the arrangements and because he had not declared his interest in accordance with Article 17 and 18(a) of the Articles of Association of RSP he was not entitled to guarantee the debenture. In short, there had been no proper quorum of directors voting on the resolution;

(ii) if contrary to the plaintiff's submission, the guarantee and the debenture were the deeds of RSP, each of them was *ultra vires* and void because the arrangements were made not for the purposes or benefit of RSP, but for the personal benefit of Mr Shenkman;

(iii) if contrary to the plaintiff's submission, the guarantee and the debenture were the deeds of RSP and were *intra vires* RSP, the directors were acting in breach of their fiduciary duties because these transactions were entered into in bad faith and not for the purposes of RSP. It followed that BSC and the receiver, having received the moneys with actual or constructive knowledge of this breach, took them as constructive trustees.

(4) *The Defences*

In defence, the defendants sought to rely on the rule in *Turquand's* case[29] in that although the resolution was defective the defendants were entitled to rely on it as a formally valid resolution. They also argued that the shareholders by having unanimously consented to the execution of the guarantee and debenture ratified and made binding the transaction in question.

(5) *The Decision*

With regard to the shareholder consent point, Slade L.J. took the view that as this argument was raised after the close of evidence, it came too late to be heard. Slade L.J. also confirmed an important factual finding that C Ltd and BSC knew that the guarantee and the debentures were not entered into by RSP for any purpose of

[29] It is interesting to observe that the "indoor management" rule or the rule in *Royal British Bank* v. *Turquand* (1856) 6 E. & B. 327 provides that outsiders are not required to inquire into the regularity of a company's internal proceedings such as the due execution of documents, the passing of authorizing resolutions, and the regularity of directors' appointments.

RSP, but were a gratuitous disposition of the property of RSP and were entered into by RSP for the benefit of SSS Ltd and Mr Shenkman personally.[30]

This knowledge was imputed to C Ltd and BSC because legal advice given to RSP's solicitor that the proposed transactions were probably *ultra vires* and constituted a misfeasance by its directors was reported to the head of the legal services department of C Ltd.

The finding of this knowledge on the part of the defendants was fatal to their appeals for the following reasons:

(a) if the transactions were found to be *ultra vires,* they could not rely on the rule that as *bona fide* purchasers without notice the transactions remained binding;

(b) If the transactions were found to be *intra vires,* they alternatively constituted a breach of directors' fiduciary duties. The same transactions could be set aside at the instance of the company and the directors would be liable as constructive trustees because they had assisted with knowledge in a breach of trust;

(c) If the transactions were held to be *intra vires* and to be treated as instances of directors exceeding their authority as agents, this knowledge on the part of the defendants would disentitle them from relying on the doctrine of apparent authority to validate the transactions.

Slade L.J. also held that the judge in the lower court had erred in allowing the defendants to amend their defence so as to plead the defence of the *Turquand* rule because this was unduly prejudicial to the plaintiff, since the plea was one of mixed fact and law and the amendment was only sought after the hearing of the evidence was closed. This technical defect was in fact relied upon by Slade L.J. in disposing of the case.

VI. THE NEW MODEL *ULTRA VIRES* DOCTRINE

This brings us to the most important "academic" issue in this case, that is, whether the transactions were also *ultra vires.* Slade L.J.'s efforts to answer this question in effect amounted to a restructuring of the *ultra vires* doctrine, resulting in a modified new model *ultra vires* doctrine being introduced. Described below are the steps taken by Slade L.J. to arrive at his new model *ultra vires* doctrine.

(i) First, Slade L.J. decided that a sharp distinction must be maintained between objects and powers. The explicit reason given to justify such a distinction was that section 2(1)(c) of the English 1948 Companies Act requires only objects to be stated in the memorandum.[31] The implicit justification for maintaining the distinction seems to be that only objects which are in their nature an activity which a company could pursue in isolation could delineate a company's capacity. Powers are, on

[30] *Supra,* note 20 at p. 492.

[31] A similar requirement is imposed by section 22(1)(b) of the Singapore Companies Act, *supra,* note 1.

the other hand, mere abilities and may be exercised only within the scope or confines of the true objects. It follows that powers ought not to be inserted in a company's memorandum and the exercise of any implied or express powers should also be controlled so that a company is treated as having implied powers only to do acts for purposes which are reasonably incidental to the attainment or pursuit of any of its express objects.[32]

(ii) Following from the above, Slade L.J. also stated the proposition that once a clause is capable of subsisting as an independent object of the company it cannot be *ultra vires* for it is by definition something which the company is formed to do and so must be *intra vires.* This same principle should apply even if a company has adopted as its object the giving away of corporate property gratuitously. In this context, Slade L.J. declared that the *Lee, Behrens* principle, developed to provide a test as to whether a company's gratuitous disposition of property comes within a company's capacity, ought to be recognized as being misleading and of no assistance.[33] And in his opinion, this is so especially in the light of the observations of Buckley L.J. in *Re Horsley & Weight Ltd,*[34] of Pennycuick J. in *Charterbridge Corporation Ltd.* v. *Lloyds Bank Ltd.*[35] and of Oliver J. in *Re Halt Garage (1964) Ltd.*[36]

(iii) Having disposed of the *Lee, Behrens* principle as being misleading and irrelevant the distinction between objects and powers became all-important. Slade L.J. now had to decide whether the sub-clause in RSP's memorandum that authorized it to give guarantees for any persons, firms or companies was in the nature of a power or object. The sub-clause in question read:

> Clause 3(K): To lend and advance money or give credit to such persons, firms, or companies and on such terms as may seem expedient, and in particular to customers of and others having dealings with the company, and to give guarantees or become security for any such persons, firms or companies.

It is interesting to note that Slade L.J. did not employ Buckley L.J.'s test of whether the sub-clause in question could be pursued in isolation as the sole activity of the company to decide the matter although he did concede that a sub-clause could not be treated as an object if it was by nature incapable of being so. He took the view that even if a sub-clause might exist as a substantive object, a construction of the memorandum as a whole might show that it was intended to constitute an ancillary power only. The presence of a *Cotman* v. *Brougham* clause should not elevate what were essentially powers into objects. However, Slade L.J. did express the view that wherever possible the *Cotman* v. *Brougham* clause should be granted its full impact.[37] In

32 *Supra,* note 20, at p. 500.
33 *ibid*., at p. 501.
34 [1982] Ch 442, 452.
35 [1970] Ch 62, 69-71.
36 [1982] 3 All E.R. 1016, 1028-30.
37 See earlier discussions at pp. 21-22.

construing this sub-clause Slade L.J. came to the conclusion that this was meant to be an ancillary power not because it was in nature incapable of constituting an independent substantive object but because the sub-clause imposed the condition that the company might lend or advance money as might "seem expedient". This condition necessarily implied that there was some criterion by which expediency was to be tested and the only possible criterion could be "as may seem expedient for the furtherance of the other objects of the company." In this regard, the sub-clause could only be regarded as an ancillary power. In further support of such a conclusion Slade L.J. pointed out that the specific direction in clause 3(k) that credit be given only to customers of, and persons having dealings with, the company made it abundantly clear that the sub-clause in its context was intended to comprise merely a series of ancillary powers.[38]

(iv) Since the sub-clause was in the nature of a power, Slade L.J. expressed the view that strict logic might require that any exercise of such a power whether implied or express would be beyond the company's capacity if the resultant transactions were in fact performed for purposes other than those of its incorporation.[39] However, Slade L.J. modified this rule on the ground that the practical difficulties resulting from such a conclusion for persons dealing with a company carrying on a business authorized by the memorandum would be intolerable.[40] To solve the problem, Slade L.J. relied on Buckley J.'s unsatisfactory judgment in *Re David Payne & Co. Ltd.*,[41] as stating the proper alternative approach.[42] Under this approach, an act that is *ultra vires* would not be so regarded and it follows that the act would become voidable but not void. Such an act would instead be treated as an act of impropriety on the part of the directors who have exercised the power in question. Since this only raises questions of equity between the directors and the shareholders it does not affect the legal quality of the act *vis-a-vis* the outsider without notice of the impropriety. In Slade L.J.'s view, directors' authority as agents is limited by the implied condition that they must exercise their powers only for the purposes of the company and therefore any such express restrictions found in the sub-clauses in a memorandum merely reinforced such a condition. Slade L.J. was therefore suggesting that every general power contained in a company's memorandum was subject to the express or implied restriction that it must be exercised for the purposes of the company. Thus, every exercise of power outside the condition ought not to be treated as *ultra vires* but as an instance of directors exceeding their authority.[42] Slade L.J. then put forward the proposition that an outsider acting without notice of the impropriety of the transaction in question may invoke the independent "indoor management rule" and the agency doctrine

38 *Supra,* note 20 at p. 502.
39 *Ibid.*
40 *Ibid.*
41 [1904] 2 Ch. 608.
42 See subsequent discussion at pp. 37-40.
43 For a critique of such a proposition see subsequent discussion at pp. 42-43.

of apparent authority[44] in their favour. Slade L.J. was able to cite Harman LJ.'s judgment in *Re Introductions Ltd.*[45] as a supporting decision because in this judgment Harman L.J. had upheld the rule that the validity of an exercise of power for purposes other than the company's corporate purposes depended upon whether the outsider knew that the directors had exceeded their authority.[46] Also in support was Pennycuick J.'s statement in *Charterbridge Corporation Ltd.* v. *Lloyds Bank Ltd.*,[47] where he declared that:

> Where directors misapply the assets of the company that may give rise to a claim based on breach of duty. Again, a claim may arise against the other party to the transaction, if he has notice that the transaction was effected in breach of duty. Further, in a proper case, the company concerned may be entitled to have the transaction set aside. But all that results from the ordinary law of agency and has not of itself anything to do with the corporate powers of the company.

This brings us to the end of Slade LJ.'s valiant efforts to remodel the *ultra vires* doctrine affecting ancillary "objects" and powers. In the main, Slade L.J. justified his results on policy grounds as well as on the ground that the *Re David Payne* and *Re Introductions* decisions were not authorities on *ultra vires* but were merely authorities on directors' agency powers.[48] In this remodelling process, Slade L.J. stated some extremely controversial propositions deserving our close scrutiny. The first of these is the proposition that the *Lee, Behrens* principle should be laid to rest.

VII. PROPOSITION I: THAT THE *LEE, BEHRENS* PRINCIPLE SHOULD BE LAID TO REST

It is respectfully submitted that the real reason why the *Lee, Behrens* principle is objectionable is not that it causes confusion between the *ultra vires* doctrine and the standard of directors' fiduciary duties but that it has been developed as an alternative touchstone to the objects in a memorandum for the implied creation of a company's powers. The reason for this necessity is that the concept of a limited capacity company is based on the premise that objects contained in a company's memorandum exhaustively define the range of purposes for which a company's impliedly created or express powers may be legitimately exercised. But quite naturally there must be occasions where a company would like to pursue a business activity which unfortunately has not been included as an object in the memorandum or it would like to exercise a power which it possesses for a purpose outside the scope of the memorandum. Both acts would be *ultra vires* and void even if they were clearly for the benefit of the company and even if the company would be seriously disadvantaged if they

[44] For a review of how the agency doctrine of apparent authority is applied in the company law context see subsequent discussion at p. 41.

[45] [1970] Ch. 199.

[46] *Ibid.*

[47] [1970] Ch 62, 69.

[48] See Gregory, *"Rolled Steel Products (Holdings) Ltd.* v. *British Steel Corporation",* (1985) 48 M.L.R. 109, 110.

were prevented from being done. In this context, an interesting question that arises is whether a company may within reasonable bounds be allowed to enlarge its capacity. Although most companies' articles of association lay down detailed procedures for the alteration of the objects in a memorandum,[49] they are seldom utilized because most companies are unaware that what they have proposed to do could be *ultra vires* in the first place.

This proposal to enlarge a company's capacity on the spot is not as radical as it sounds. The Australian "omnibus clause"[50] that operates to permit a company to undertake vertical or horizontal business expansion and the similar English *Bell Houses* clause[51] which operates to allow a company to pursue any activities which the directors consider to be advantageous to the company are both means of showing how a company may in effect expand its limited capacity. Therefore, it is this writer's belief that the decisions in the line of 'gift' cases culminating in the *Lee, Behrens* principle represented a deliberate effort on the part of judges to put forward an alternative *ultra vires* doctrine that enables the court to adopt a more flexible approach in determining the limits of a company's powers and capacity. More specifically, it allows the court to validate transactions that are reasonably incidental to the carrying on of the company's business rather than the stricter requirement that they must be for purposes ancillary or reasonably incidental to the pursuit of authorized objects in the memorandum. And in conjunction with the above criterion, the court may also take into account any objective benefits which the proposed transaction may confer on the company and the subjective good faith of the directors in entering into the transactions in question. Given the cogency of those considerations, it is indeed unfortunate that they

[49] See section 33 of the Singapore Companies Act, *supra,* note 1.

[50] An example of such a clause is found in the Australian case of *H.A. Stephenson & Son Ltd.* v. *Gillanders Arbuthnot & Co.* [1931] 45 C.L.R. 476. Dixon J. in this case construed the clause permitting the company in question to "carry on any other business whether manufacturing or otherwise as the company may deem expedient" as an object rather than a power on the ground that although "the definition is a wide one it does not appear to be considered too indefinite to pass muster as a lawful object." In his opinion, the true meaning of the object read in the context of the memorandum would appear to be to authorize the company to carry on not any business the company might subjectively choose to carry on, but only such business as it might consider convenient to carry on because it was connected with or arose out of the course of business adopted by the company. This was in effect an objective test. Having formed the preliminary view that an omnibus clause ought to be treated as an object, Dixon J. then rejected the main object rule as this sub-clause ought not to be construed as ancillary or subservient to the main or predominant object of the company in question to trade as a produce merchant. In his view, trading as a produce merchant was only an initial and an immediate purpose of the company but the other objects including the "omnibus clause" were nevertheless potent and ranked equal with and independently of the first and immediate object. An "omnibus clause" therefore has the effect of permitting a company to undertake vertical or horizontal business expansion.

[51] The English *Bell Houses* clause *(Bell Houses Ltd.* v. *City Wall Properties Ltd.,* [1966] 2 QB 656) authorized the company "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 ancillary to any of the objects of company". This as noted by Ford imposes a subjective test of honest belief on the directors. See H.A.J. Ford, *Principles of Company Law,* (1982, 3rd Ed.) p. 96.

were unappreciated by all the judges who attempted to castigate the *Lee, Behrens* principle.

To substantiate my thesis the reader's attention must be drawn to the case of *Henderson* v. *Bank of Australia.*[52] In this case, a valued officer of the bank was killed in a railway accident. At an annual general meeting after his death a resolution was passed authorizing the directors to grant to the family of the deceased an annual pension of £1,500 for a period of five years. One of the disgruntled shareholders sought a declaration that the resolution was *ultra vires.*

In the absence of express authorization, the question before North J. was whether the company had the implied power to authorize the gratuitous payment. North J. held that a company might exercise such a power if it were done *bona fide,*[53] was incidental to the business of the company,[54] and was for the benefit of the company.[55] Interestingly, North J. stated that in applying the last two criteria one needs to look at what was done by other companies of a similar character and position engaged in the same pursuit,[56] irrespective of whether these other companies are acting within their powers or not.[57] At this point, it is important to note that North J. intended to apply the "incidental to" and "for the benefit of the company" requirements in an objective manner as stated above. The reason might be that North J. appreciated the fact that this principle created a new source of company powers that needed to be justified in its own right. North J. tried to legitimize this new principle by suggesting that it did not deviate from the normative *ultra vires* doctrine as the new set of criteria also indirectly served to promote the achievement of the company's objects. He said:[58]

> It seems to me here that what has been done has been done for the purpose of giving effect to the objects of the company, and promoting the prosperity of the company.

And more specifically, he said:[59]

> The principle of those cases, as I understand is this, that here there are directors of a trading company, those directors necessarily have incidentally the power of doing that which is ordinary and reasonably done in every such business, with a view to getting either better work from their servants, or with a view to attract customers... In the present case the reason suggested is that it secures a better class of officials who are willing to take service with the company, *an object of equal importance of course for carrying on its legitimate business.* (emphasis added)

North J. probably felt that there were occasions where a company's memorandum could not exhaustively define what was good

52 (1888) 40 Ch. D 170.
53 *Ibid*., at p. 173.
54 *Ibid*., at p. 174.
55 *Ibid*., at p. 173.
56 *Ibid*., at p. 175.
57 *Ibid.*
58 *Ibid.*
59 *Ibid*., at p. 179.

for the running of the business of a company and this justified the introduction of a more flexible touchstone in place of the rigid *ultra vires* doctrine. If one agrees with North J. that there is a need for a more flexible source of company powers than the rigid *ultra vires* doctrine then such a rationale in fact provides cogent support for what he was hoping to achieve.

In line with these developments, what Eve J. did in the *Re Lee, Behrens Case*[60] was to split North J.'s principle into a three-limb test. He suggested that the validity of a gratuitous grant is to be tested, as is shown in all the authorities, by the answers to three pertinent questions:[61]

(i) Is the transaction reasonably incidental to the carrying on of the company's business?

(ii) Is it a *bona fide* transaction? and

(iii) Is it done for the benefit and to promote the prosperity of the company?

It is interesting to note that in *Henderson's* case, except for the *bona fide* requirement, North J. essentially applied the test in an objective way. He indicated that to apply the principle one must first objectively determine the ordinary mode of carrying on the business in question, and to do that one must also look objectively to what is done by other companies of a similar character and position engaged in the same pursuit.[62] Eve J. was handicapped in his ability to apply the test in an objective way due to a lack of evidence which might show whether the grant was made for the benefit or to promote the prosperity of the company or was reasonably incidental to the carrying on of the company's business.[63] As a result Eve J. erroneously applied the test in a subjective way as the only available evidence pointed to the fact that the predominant, if not the only, consideration operating in the minds of the directors, was a desire to provide for the widow and that the question what, if any, benefit would accrue to the company never presented itself to their minds.[64] The ensuing damage following this subjective application of the principle was that the state of mind of the directors now became all important to decide the question of whether the proposed grant was for the benefit of the company. This is wrong and also undesirable as it closely resembles the *Smith* v. *Fawcett*[65] test that directors are under a duty to act *bona fide* in what they subjectively consider to be the interests of the company.[66] Eve J. should not have allowed himself to be pressured into applying the principle in a subjective manner due to a lack of evidence as regards the objective benefit of the grant to the company. This approach paved the way for commentators to criticize the *Lee, Behrens* principle on the ground that it confuses the capacity issue with that of directors' breach of fiduciary duties

60 *Supra,* note 22.
61 *Ibid*., at p. 51.
62 *Supra,* note 52, at p. 175.
63 *Supra,* note 22, at p. 52.
64 *Ibid.*
65 [1942] Ch. 304.
66 *Ibid*., at p. 306.

and to ignore the more important issue of whether a more flexible touchstone for the implied creation of company powers is needed to soften the rigidity of the normative *ultra vires* doctrine.

It is indeed unfortunate that the case of *Re Lee, Behrens & Co. Ltd.* has been regarded as the case that established the "distinctive principle" rather than *Henderson's* case where North J. had a clear grasp of the special role of this "distinctive principle".

The further blunder committed by Eve J. was that instead of relying upon *Henderson's* case alone to formulate his principle he had also drawn support from two other cases that were really concerned with the exercise of power by directors and majority shareholders rather than the issue of whether a company has the capacity to do a certain act. This further discredited the *Lee, Behrens* principle unnecessarily.

The first case was *Hampson* v. *Price's Patent Candle Co.*,[67] which was actually a decision on whether the directors had properly exercised the powers of management delegated to them when they proposed to pay a gratuity to each worker in the factory. It is therefore puzzling as to how Eve J. sought support from such a decision to formulate a new principle to determine the boundaries of a company's capacity.

The next case relied upon by Eve J. was *Hutton* v. *West Cork Ry* Co.,[68] a case which has been severely criticised in a recent decision by Oliver J., *Re Halt Garage,*[69] on the ground that the case is a case concerning the control of majority shareholders' exercise of voting power and not the issue of whether the company has the capacity to do a certain act.

The facts were that a railway company which had no provision in its articles for paying remuneration to directors sold its undertaking, pursuant to an Act of Parliament, to another company. Section 14 of the same Act provided that on the completion of the transfer the company should be dissolved except for the purpose of regulating its internal affairs and winding up the same and of dividing the purchase-money. After the completion of the transfer a general meeting of the company was held at which a resolution was passed to apply £1,050 of the purchase-money in compensating the paid officials of the company for their loss of employment, although they had no legal claim for any compensation, and £1,500 in remuneration to the directors for their past services.

One of the two issues raised as a result was whether the company had the capacity and power to award gratuitous compensation to the paid officials who were essentially employees of the company. Cotton L.J. distinguished *Hampson's* case on the ground that in that case the company was a going concern and it had the powers to award gratuitous payment to its workers for the purposes of carrying on the business if this would induce the workers to work harder. Since

67 [1876] 45 L.J. (Ch.) 437.
68 [1876] 23 Ch. D. 654.
69 [1982] 3 All E.R. 1016.

the company in the instant case existed only for the purpose of winding-up it followed that it did not have the power to do so. It is respectfully submitted that such a view is erroneous. The criterion should not be whether the company is or is not a going concern but whether power to do the act in question had been provided for either expressly or impliedly by the company's memorandum. To rely on the factor of whether the company is a going concern or a winding-up concern to decide whether the company has the power to do the act in question is specious as it is tantamount to suggesting that a company may freely enlarge its capacity merely on the ground that the additional powers are necessary for the purposes of carrying on a business. If Eve J. had actually drawn support from this aspect of Cotton L.J.'s judgment in order to formulate his principle he would have been misled.

If Cotton L.J. had been guilty of leading Eve J. astray, Bowen L.J. was even more blameworthy. Like Cotton L.J., Bowen L.J. preferred to deviate from the *ultra vires* doctrine and put forward the embryonic *Lee, Behrens* principle which later and for some inexplicable reason was credited as being formulated by Eve J. Bowen L.J. believed that the power to make a gratuitous award to employees and directors may be impliedly created if the award is *bona fide,* done within the ordinary scope of the company's business and reasonably incidental to the carrying on of the company's business for the company's benefit.[70] On these erroneous premises, it was not difficult for Bowen L.J. to say that the awards to the employees and the directors were not incidental to the carrying on of the company's business as it was a dying concern.

To draw further support for my thesis that the *Lee, Behrens* principle was actually introduced to provide a more flexible alternative touchstone for the implied creation of company powers we should consider the subsequent treatment of the principle by the English judges.

The first case in this line of cases is *Charterbridge Corporation Ltd.* v. *Lloyds Bank Ltd.*[71] In this case, a director of C company entered on behalf of the company into a guarantee to a bank to secure the debts owed by D company to the bank. The background to this arrangement was that C company was a constituent member of a group of closely associated companies headed by D company.[72] The interesting feature in this case was that one of the clauses in C company's memorandum actually empowered it to guarantee by mortgages or charges the performance of any obligations of another corporation or persons "with whom or which the company has dealings or having a business or undertaking in which C company is concerned or interested whether directly or indirectly."[73] For reasons which we will discuss later[74] Pennycuick J. drew no distinction between objects and powers and held that any act that is within the scope of a power expressed in the memorandum is an act within the com-

70 *Supra,* note 68, at pp. 672-3.
71 [1970] 1 Ch. 62.
72 *Ibid.*
73 *Ibid.*, at p. 65.
74 See subsequent discussion at p. 38.

pany's memorandum.[75] Pressed by counsel's argument to determine the validity of the exercise of borrowing power and conscious of the importance of this question, Pennycuick J. reacted by stating categorically that he thought it was contrary to the whole function of a memorandum that objects stated unequivocally and set out in it should be subject to a validity test that depended upon the directors' state of mind.[76] He further criticized Eve J. for having confused the issue of ratification of directors' power by the general meeting with the issue of company's capacity and power.[77] And he felt that the *Lee, Behrens* principle was at best relevant only to implied powers, and inappropriate to the scope of express powers. This view of Pennycuick J. is most interesting as it in fact accepts and confirms the role of the *Lee, Behrens* principle as an alternative touchstone for the implied creation of company powers.

Having taken such a hard line Pennycuick J. quickly retreated with cold feet as he realized that a fellow high court judge had held in *Re Introductions Ltd.* v. *National Provincial Bank Ltd.*[78] that an express power which is a power in nature rather than an object is incapable of ranking as a separate object. He conceded that if he were wrong in his view of *ultra vires* and if the intention of the directors were relevant to the question of *ultra vires* then in his opinion a modified form of the *Lee, Behrens* principle should be applied! Taking the view that it was legitimate for the interest of the group of companies to take precedence over the individual member company if that also ultimately benefitted the individual company, he suggested that the proper test was:[79]

> Whether an intelligent and honest man in the position of a director of the company concerned, could, in the whole of the existing circumstances, have reasonably believed that the transactions were for the benefit of the company.

It must be recalled that although the test that was formulated and applied by North J. in *Henderson's* case included a *bona fide* requirement, the test as a whole was applied essentially in an objective manner. And we have already noted that the mistake made by Eve J. was to over-emphasize the *bona fide* requirement so that the subjective state of mind of the directors became all important. In this context, what Pennycuick J. did to correct the mistake of Eve J. was minimal as he had merely introduced a measure of objectivity in determining the state of mind of the directors, which unfortunately still remains the all important criterion in determining the validity of a corporate transaction. What Pennycuick J. achieved was that he confirmed the role of the *Lee, Behrens* principle as an alternative test of company capacity and power. In this regard, it is indeed puzzling as to how Slade L.J. could possibly have relied upon the "observations" of Pennycuick J. to justify the proposition that the *Lee, Behrens* principle should be laid to rest.

75 *Supra,* note 71, p. 69.
76 *Ibid*., see also Baxter, *supra,* note 26 at p. 286.
77 *Ibid.*
78 [1968] 2 All E.R. 1221, *per* Buckley J. at p. 1225.
79 *Supra,* note 71, at p. 74.

If the reason for Slade L.J.'s reliance on Pennycuick J.'s observation in the *Charterbridge* case is puzzling, his reliance upon Oliver J.'s observations in *Re Halt Garage (1964) Ltd.*[80] is even more mystifying. Although Oliver J. began promisingly in criticizing the confusion in the *Lee, Behrens* principle he unexpectedly held that the principle should continue to apply to cases involving the gratuitous dispositions of company assets.[81] Thus, *Re Halt Garage (1964) Ltd.* can hardly be cited as an authority for the proposition that the principle should be laid to rest. It was only due to fiscal considerations that Oliver J. chose not to apply the principle to the instant case.

In summary, it can be noted that although the judges so far mentioned did criticize the *Lee, Behrens* principle, none of them actually proposed that the principle should be laid to rest. On the contrary, Pennycuick J., for example, confirmed the role of the *Lee, Behrens* principle as an alternative test of company capacity and power. And Oliver J. actually decided that it should be applied with full force with regard to cases involving gratuitous disposition of company property.

Given the cogency of the arguments that favour the role of the *Lee, Behrens* principle as an alternative touchstone for the implied creation of company powers it is disappointing that Slade L.J. had totally failed to address these issues.

VIII. PROPOSITION 2: THAT THE HARSH *ULTRA VIRES* DOCTRINE NEEDS TO BE MODIFIED TO PROTECT OUTSIDERS

At this juncture, it is useful to recall that the basic justification for the concept of limited capacity is that it protects shareholders and existing creditors by rejecting as null and void transactions between the company and an outsider if the purpose of that transaction is outside the scope of the memorandum. It follows that an outsider whose transaction with the company is now being challenged as *ultra vires* runs the risk of his transaction being rendered null and void. Theoretically, this system of protection is thought to be a fair system because a company's limited capacity is ascertainable by its memorandum which is a constitutional document of the company freely available for inspection. But commercial realities have shown that the system may work oppressively for the following reasons.

(i) Businessmen have neither the time nor the resources to study a company's memorandum in order to acquaint themselves with its legal capacity.

(ii) They may not appreciate the significance in the distinction between objects and powers.

(iii) Even if they can distinguish a power from an object they might be unable to find out the purpose behind the exercise

[80] [1982] 3 All E.R. 1016, (decided in 1978 but not reported until 1982).
[81] *Ibid*., at p. 1032.

of a particular power. To illustrate the problem, Buckley J. in *Re David Payne & Co. Ltd.* said:[82]

> … I think the matter is to be treated in this way — that the lender cannot investigate what the borrower is going to do with the money; he cannot look into the affairs of the company and say, "Your purposes do not require it now, this borrowing is unnecessary; you must show me exactly why you want it, and so on."

(iv) Assuming that they have knowledge of the purpose behind the exercise of a power and could reasonably decide for themselves whether the purpose is ancillary or reasonably incidental to the pursuit of the company's authorized objects, the presence of the *Lee, Behrens* principle has greatly confused the proper criteria that should be employed to decide the validity of an exercise of power.

(v) It is also extremely unjust that that the company which has solicited the interest of the outsider in the transaction now, for its own reasons, turns round and invokes the *ultra vires* doctrine arguing that the transaction should be set aside as being null and void.[83]

The plight of an unwary outsider was first revealed to an unsympathetic Sir James Bacon V.C. in *Davis' Case.*[84] The facts were that the directors of a building society borrowed money from a Mr Joseph Davis and employed the amount in a loan to another society. The first mentioned society was eventually wound up and Mr Davis, the innocent outsider, sought to recover his debt by proving his claim to the official liquidator. Speaking in an unsympathetic voice, Sir James Bacon, V.C. ruled that the loan was not for the purpose of enabling the members of the society to build anything and the borrowing was a totally unauthorized act, and a transaction wholly illegal between borrower and lender.[85]

However, barely five months later, Sir G. Mellish L.J. reached a contrary decision in *Re Marseilles Extension Railway Company,*[86] a case which preceded the *David Payne's* case and basically provided the rudiments of the *David Payne's* solution. The facts were in the main similar to *Davis' Case* and also raised the issue of whether the company had validly exercised its power to borrow money which was expended for an unauthorized purpose. Oblivious to this main issue, the judge considered the question of whether the lender had notice that the loan would be employed for an unauthorized purpose. The significance of this course of enquiry was only revealed when he later said:[87]

> But in my opinion there is no evidence at all… that the Credit Foncier (the lender) had notice of any of these transactions, so as to make this loan… an invalid loan.

82 [1904] 2 Ch. 608, 613.
83 See Paterson and Ednie, *Australian Company Law* (3rd Ed. 1982) Vol. 3, at p. 53, 108
84 [1871] L.R. 12 Eq. 516.
85 *Ibid*., p. 520.
86 [1871] L.R. 7 Ch. 161.
87 *Ibid*., at p. 167.

It appears that the validity of an exercise of express power now *depended upon whether the outsider had notice of the unauthorized purpose behind the transaction.* Since the lender company had not had notice of the unauthorized purpose the judge said that it could recover its loan. This is absurd as a company may only validly exercise a power if it is ancillary or reasonably incidental to the objects of a company as stated in its memorandum and, as noted by a writer, its power can neither be limited nor extended save by matters expressly alluded to therein.[88] Mellish, L.J., however, admitted that he could only justify the decision on policy grounds for he said:[89]

> After all, the real question is, which of two innocent sets of shareholders is to bear the loss? It appears to me that if the directors of the Marseilles Company have been guilty of an improper application of the funds of the Marseilles Company, it would be more just that the shareholders of the Marseilles Company whose directors improperly applied this money, should bear the loss, than the innocent shareholders of the Credit Fonder, whose directors appear to have done what it was a perfectly legitimate thing for them to do; it being a part of their business to lend money, and the other company having power to borrow it.

Mellish, LJ.'s effort to protect the outsiders should be appreciated but his method of doing so by literally burying alive the doctrine of *ultra vires* is wrong. Unfortunately, successive cases basically followed Mellish, LJ.'s lead and could, at best, only provide further policy justifications. For example in *Re David Payne & Co. Ltd.*,[90] which was again a case of *ultra vires* lending by an innocent lender, Buckley J. merely echoed Mellish, L.J. and said that the lender could not investigate what the borrower was going to do with the money.[91] Secondly, he expressed the view that if a director had exercised his express power improperly this might well have resulted in a breach of fiduciary duty but that was, in his opinion, a matter between the shareholders and directors.[92]

In holding as he did, Buckley J. received the unanimous support of the Court of Appeal where Vaughan Williams L.J. approved of the *Re Marseilles* decision and expressly overruled *Davis' case.*

It is interesting to note that in *Charterbridge Corporation Ltd.* v. *Lloyds Bank Ltd. and Another,*[93] Pennycuick J. detected some inherent contradictions in Buckley J.'s judgment in *David Payne's* case and noted that he found it difficult to reconcile Buckley J.'s earlier statement that[94] "a corporation cannot do anything except for the purposes of its business and everything else is beyond its power, and is *ultra vires"* with his later statement that:[95]

[88] See Baxter, *"Ultra Vires and Agency Untwined",* (1970) 29 C.L.J. 280, 281.
[89] *Supra,* note 86 at p. 168.
[90] [1904] 2 Ch. 608.
[91] *Ibid.*, at p. 613.
[92] *Ibid.*
[93] [1970] 1 Ch. 62.
[94] *Supra,* note 90, at p. 612.
[95] *Ibid.*, at p. 613.

> If this borrowing was made, as it appears to me at present it was made, for a purpose illegitimate so far as the borrowing company was concerned, that may very well be a matter on which rights may arise as between the shareholders and directors of that company. It may have been a wrongful act on the part of the directors. But I do not think that a person who lends to the company is by any words such as these required to investigate whether the money borrowed is borrowed for a proper purpose or an improper purpose. The borrowing being effected, and the money passing to the company, the subsequent application of the money is a matter in which the directors may have acted wrongly; but that does not affect the principal act, which is the borrowing of the money... I think here the power to borrow is a power resting in the directors...

The contradiction is that how could an *ultra vires* act be regarded as a breach of director's fiduciary duties so that it could remain binding. Having pointed out the anomaly, Pennycuick J. rather disappointingly retreated from his criticism of the *David Payne* solution giving the excuse that the Court of Appeal had in any event unequivocally decided that the transaction was not *ultra vires*[96]

There is, however, a legal possibility of rectifying the absurdity in the *David Payne* solution and this was meekly attempted by Pennycuick J. in the *Charterbridge* case. Appreciating the principle that a transaction that falls within the scope of an object as distinct from a power in a company's memorandum must be infra *vires,* he held the view that the way to help the outsider is not to draw any distinction between objects and powers, but to regard an express power in the memorandum as an object. The result of such an exercise is that the issue of capacity is thereby pre-empted. The matter could then be treated as an abuse of power by the director in which case it would give rise to a claim based on a breach of director's fiduciary duty.[97] As against the other party to the transaction a claim might arise based on the law of agency if he has notice that the transaction was effected in excess of the director's powers, and, in a proper case, the company concerned may be entitled to have the transaction set aside.[98] On these grounds, Pennycuick J. declared that:[99]

> Apart from authority, I should feel little doubt that where a company is carrying out the purposes expressed in its memorandum, and does an act within the scope of a power expressed in its memorandum, that act is an act within the powers of the company.

Pennycuick J.'s views were unfortunately thwarted by Buckley J. and Harman L.J.'s efforts of carefully distinguishing objects and powers in the case of *Re Introductions Ltd.* in order that the integrity of a limited capacity company be preserved.

The facts of *Re Introductions Ltd.* were that a company was formed with the object of providing various facilities for foreign

96 *Supra,* note 93.
97 *Ibid*., at p. 69C.
98 *Supra,* note 93, at p. 69.
99 *Ibid.*

visitors. The objects clause in its memorandum was widely drafted, but it did not authorize it to carry on the business of pig breeding. To finance this *ultra vires* activity the company had obtained overdraft facilities from the defendant bank by issuing two debentures on the company's assets as security. Although the bank conceded that the pig-breeding business activity was *ultra vires* it argued that the loan was nevertheless *intra vires* because a sub-clause in the company's memorandum expressly authorized the company to borrow or raise money in such manner as it thought fit. Furthermore, this power was converted into an object by the concluding words of the memorandum which provided that each of the preceding sub-clauses should be construed independently of and should be in no way limited by reference to any other sub-clause and that the objects set out in each sub-clause were independent objects of the company. Faced with these arguments, Harman L.J. and the rest of the Court of Appeal judges who were conscious of the need to preserve the integrity of the limited capacity company said:[1]

> It has always been the ambition apparently of the commercial community to stretch the objects clause of a memorandum of association, thus obtaining the advantage of limited liability with as little fetter on the activities of the company as possible. But still you cannot have an object to do every mortal thing you want, because that is to have no object at all…

Construing the sub-clause that empowered the company to borrow, Harman L.J. felt that this clause had in truth to be construed as a power. He approved of Buckley J.'s view in the lower court that "a power or an object conferred on a company to borrow cannot mean something in the thin air: borrowing is not an end in itself and must be for some purpose of the company."[2] He added that if it was a power such a power must be for a purpose within the company's memorandum.[3]

As regards the arguments that the power had been elevated to an object by the concluding words in the memorandum, Harman L.J.'s terse reply was that one could not convert a power into an object by merely saying so.[4]

If the distinction between objects and powers must be maintained and contracts entered into pursuant to the exercise of a power must be subjected to the rigour of the *ultra vires* doctrine, then the irksome absurdity in the *David Payne* solution remains unmitigated.

The reason why in the *Rolled Steel* case, Slade L.J. had more success in removing the irksome absurdity was that he used and extended the policy reasons that favour protection for innocent outsiders not to justify the abolition of the distinction between objects and powers but to suspend the consequences that flow from it. In fact, this is one of a few "innovative" aspects of his judgment. Thus, having formed the opinion that the sub-clause in question was in the nature of a power he suggested that:[5]

1 [1970] 1 Ch. 199, 209.
2 *Ibid.*, at p. 210.
3 *Ibid.*
4 *Ibid.*
5 *Supra,* note 20, at p. 502.

> Strict logic might therefore appear to require that any act purported to be done by a company in purported exercise of powers ancillary to its objects conferred on it by its memorandum of association, whether express or implied (eg. a power to borrow) would necessarily, and in every case, be beyond its capacity and therefore wholly void if such act was in fact performed for purposes other then those of its incorporation. However, the practical difficulties resulting from such a conclusion for persons dealing with a company carrying on a business authorised by its memorandum, would be intolerable.

It is fair to infer from the above that Slade L.J. was advocating that the consequences that flow from the object/power distinction ought to be suspended in the interest of the innocent outsiders. It also logically follows that in the absence of an outsider who has contracted with the company, for example, as in the case of a corporate gratuitous disposition, this justification for the suspension is absent. It follow that under such circumstances, the consequences that flow from the object/power dichotomy ought to be given their full effect. This last inference is especially important to us because in the event that the *Rolled Steel* case is accepted as good law in Singapore, this inference has important bearing on the determination of the scope of section 25(1) of the Companies Act.[6]

IX. PROPOSITION 3: THAT IN PLACE OF THE STRICT *ULTRA VIRES* DOCTRINE AGENCY PRINCIPLES SHOULD PROVIDE THE LEGAL BASIS TO DETERMINE WHETHER A TRANSACTION WITH AN OUTSIDER SHOULD BE SET ASIDE

Having adopted the rule in *David Payne,* Slade L.J. believed that the "anomalous," "puzzling," or "absurd"[7] rule therein could be explained using agency principles. In his opinion, an outsider was entitled to rely on the fact that as a general rule, a company incorporated under the Companies Act held out its directors as having ostensible authority to do on its behalf anything which its memorandum of association, expressly or by implication gave the company the capacity to do.[8] It followed that if a sub-clause in the memorandum authorized a company to borrow for the purposes of the company, its directors would have the power to do so, as long as the outsider had no notice of their ulterior motive to use the borrowed money for a "foreign" purpose. Because the company through its memorandum held out its directors as having the apparent authority[9] to borrow, then not only is the *ultra vires* issue pre-empted but the express condition that the borrowing must be done for the purposes of the company would also be construed not as limiting a company's

6 See subsequent discussion at p. 46.

7 See Baxter, *supra,* note 26, at p. 280.

8 *Supra,* note 20, at p. 507.

9 Slade L.J. was not alone in suggesting that agency principles should be used for the protection of outsiders. Two writers have documented that "a much more potent weapon in the armoury available to protect outsiders is the concept of apparent or ostensible authority by virtue of which the company will be bound by certain transactions of its offices which have not been expressly or implicity authorised." See Milman and Evans, "Corporate Offices and the Outsider Protection Regime", (1985) 6 Co. Law. 68, 70.

capacity but simply as limiting the authorities of the directors.[10] Although the outsider had constructive knowledge of the memorandum, including any condition that was attached to the sub-clause, he nevertheless had no notice of the breach of the condition because he was entitled to assume that its directors were properly exercising such powers for the purposes of the company as set out in its memorandum.[11] In the opinion of Slade L.J., three factors actually operated to legitimize this particular assumption. The first factor has already been stated, that is, a company holds out its directors as having the apparent/ostensible authority to bind the company to any transaction which falls within the powers expressly or impliedly conferred on it by its memorandum of association.[12] It is subsumed within such a proposition that Slade L.J. considered that the four requirements laid down in *Freeman & Lockyer* v. *Buckhurst Park Properties (Mangol) Ltd.* as necessary for establishing this apparent/ostensible authority had been satisfied. These requirements are:[13]

a) a representation that the agent has authority to enter on behalf of the company into a contract of the kind sought to be enforced was made to the contractor;

b) that such representation was made by a person or persons who had 'actual' authority to manage the business of the company either generally or in respect of those matters to which the contract relates;

c) that he (the contractor) was induced by such representation to enter into the contract, that is, that he in fact relied upon it; and

d) that under its memorandum or articles of association the company was not deprived of the capacity either to enter into a contract of the kind sought to be enforced or to delegate authority to enter into a contract of that kind to the agent.[14]

The second factor is based upon policy considerations and is reflected in the rule that an outsider is under no duty to investigate and inquire into the purpose behind a transaction. And in this connection, Slade L.J. cited Buckley J.'s words in *Re David Payne & Co. Ltd.* that:[15]

> A corporation, every time it wants to borrow, cannot be called upon by the lender to expose all its affairs, so that the lender can say, "Before I lend you anything, I must investigate how you carry on your business, and I must know why you want the money, and how you apply it, and when you do have it I must see you apply it in the right way." It is perfectly impossible to work on such a principle.

Slade L.J. also cited Harman L.J.'s words in *Re Introductions Ltd* that:[16]

[10] *Supra,* note 20, at p. 507.
[11] *Ibid.,* at p. 508.
[12] *Ibid.,* at p. 507.
[13] [1964] 2 Q.B. 408, *per* Diplock L.J. at 506.
[14] For the latest discussion on the application of these criteria in the company law context see Milman and Evans, *supra,* note 9.
[15] [1904] 2 Ch. 608, 613.
[16] [1970] Ch. 199, 210.

> I would agree that, if the bank did not know what the purpose of the borrowing was, it need not inquire...

And finally Slade L.J. also cited Lord Parker of Waddington's words in *Cotman* v. *Brougham* that:[17]

> A person who deals with a company is entitled to assume that a company can do anything which it is expressly authorised to do by its memorandum of association, and not investigate the equities between the company and its shareholders.

Slade L.J. further commented that this last passage was in his opinion "an expression of the rule in *Turquand's* case.. .".[18] This conveniently brings us to Slade L.J.'s third factor and that is that an outsider is entitled to assume on the authority of the principle in *Turquand's case* that the directors of the borrowing company were acting properly and regularly in the internal management of its affairs and were borrowing for the purposes of the company's business.[19] With due respect to Slade L.J., it is submitted that *Turquand's case* or the "indoor management rule" could not furnish the support claimed by him.

The first thing to note about this "rule" is that it is a rule based on commercial convenience and its application is independent of the agency principle.[20] The second point is that the "rule" applies only to cure defects in authority arising out of irregularities in the procedures of internal management, for example, in the execution of documents, in the appointment of directors and officials and in the passing of authorizing resolutions conferring authority on them.[21] Thus, the rule has no application in a situation where the director has already been properly appointed and the issue is only whether in acting as he did he has exceeded the authority conferred upon him by the memorandum of association.[22] It follows that Slade L.J. could not rely on *Turquand's* rule as a justification that an outsider could assume that the purpose of the transaction is one within the scope of the memorandum.

Another difficulty that confronted Slade L.J. in his attempt to invoke agency principles was that he held in the *Rolled Steel* case itself that an express condition that restricts the scope of a power should be construed not as a limitation on the company's capacity but as limiting the authority of the directors so that a breach of the condition should be regarded as an instance of directors exceeding their authority. In any case, Slade L.J. also claimed that every general power contained in a company's memorandum was subject to the express or implied condition that it had to be exercised for the purposes of the company. The difficulty in this approach is that if a power is subject to the express or implied condition that it must be exercised for the purposes of the company then the condition is hardly

[17] [1918] A.C., 514, 521.
[18] *Supra,* note 20, at p. 505.
[19] *Ibid.,* at p. 504.
[20] See J.H. Farrar, *Company Law,* (1985) p. 300.
[21] See L.S. Sealy, *Cases and Materials In Company Law,* (1985, 3rd. Ed.) p. 218.
[22] *Ibid.*

a restriction, in fact, the condition is so general that it should be construed as conferring wide discretion on the directors. If this is the case then the directors who improperly exercise their power for purposes other than those of the company have not exceeded their authority in the sense that they have usurped a power which they do not have but they have instead utilized a power which they have for an improper purpose. They are thus guilty of a breach of fiduciary duty rather than of acting without authority. The reason why the distinction is important is that under general law the consequences that flow from an abuse of power and acting without power are different. For example, an act performed without authority is void whereas an act in breach of the director's fiduciary duties is voidable at the instance of the company. The former is so because it is a principle of the law of agency that where an agent enters into a transaction without authority that transaction is void and no property can pass under it irrespective of the state of the third party's knowledge.[23] The reason why such drastic consequences were avoided in *Rolled Steel's* case was that Slade L.J. countered it by suggesting that an outsider might rely on the ostensible/apparent authority of the directors as held out by the company's memorandum to validate the transaction in question. On the other hand, an abuse of power results in a voidable but not void act because an exercise of power for an improper purpose is effective at common law in conferring rights and may be set aside only in equity.[24] For it is a principle of equity that where a party entering into a transaction with one in a fiduciary position has notice that by entering into that transaction the other was committing a breach of duty, the company may have that transaction set aside and recover any property passing under it.[25] On the other hand, if the third party dealt with him in good faith and without notice of the abuse the company would have no power to set the transaction aside.[26]

The above demonstrates that contrary to what Slade L.J. suggested, the legal basis to justify the rule that whether a transaction be set aside depends on whether the outsider has knowledge of the impropriety behind the transaction rests more appropriately on the law of trusts than the law of agency. It is submitted that the law of agency could be more appropriately invoked only if the directors acted in breach of a specific condition that had been attached to a general power so that they could properly be regarded as acting without authority. But it is inconceivable that a company would on its own volition choose to fetter its capacity and powers by attaching such specific conditions to its general powers. In this sense, Slade L.J.'s solution appears academic.

Another reason why the law of trusts provides a better justification for the rule is that under trust principles a person who assists another who is in a fiduciary position to commit what he knows to be a breach of trust cannot legitimately complain if the transaction is subsequently set aside.[27] As noted by a writer, the Court of Appeal

[23] See Baxter, *supra,* note 26, p. 297.
[24] See Ford, *supra,* note 51, p. 369.
[25] See Baxter, *supra,* note 26, p. 296
[26] See Ford, *supra,* note 51, p. 361.
[27] See Baxter, *supra* note 26, p. 284.

in *Re Marseilles Extension Railway Co.*[28] was in effect being asked to determine not whether the borrowing was *intra vires,* but whether the directors had been guilty of a breach of trust.[29] And in his opinion,[30] a breach of fiduciary duties was what Buckley J. in *Re David Payne & Co.* meant when he said:[31]

> If this borrowing was made, as it appears to me at present it was made, for a purpose illegitimate so far as the borrowing company was concerned, that may very well be a matter on what rights may arise as between the shareholders and the directors of that company. It may have been a wrongful act on the part of the directors. But I do not think that a person who lends to the company is by any such words as these required to investigate whether the money borrowed is borrowed for a proper purpose or an improper purpose. The borrowing being effected, and the money passing to the company, the subsequent application of the money is a matter in which the directors may act wrongly; but that does not affect the principal act which is the borrowing of the money.

Another reason why the law of agency compares unfavourably with the law of trusts is that the law of agency is unable to discriminate against multi-purpose transactions where although the apparent purpose of the transaction was within the purposes of the company it was also planned to confer benefits to the directors. In this connection, the law of trusts as applied in the company law context is much more discriminating as a director is under a duty not only to act in good faith in the interests of the company but is also required not to act for any collateral purpose.[32]

Another advantage of the law of trusts is that its application is not pre-empted if the transaction is also found to be *ultra vires.* They may co-exist. In contrast, the law of agency cannot be invoked if the act in question is also *ultra vires.* In fairness, it should be pointed out that Slade L.J. did appreciate the relevance of the law of trusts and had in fact in his judgment utilized the constructive trust remedy to provide for the plaintiff's relief.

In summary, the gist of Slade L.J.'s judgment is that any act that falls within the scope of a company's powers is *intra vires.* From now on the strict logic of the *ultra vires* doctrine will continue to have impact only in cases where the act in question does not even, to begin with, fall within the scope of the company's powers. An interesting comment on this development was expressed in the following words:[33]

> On this rather narrow view, few activities will fall outside the corporate capacity of the modern limited company. With the standard multifarious list of object/powers, a *Cotman* v. *Brougham*

28 *Supra,* note 86.
29 See Baxter, *supra,* note 26, p. 284.
30 *Ibid.*
31 [1904] 2 Ch. 608, 613.
32 See *Smith* v. *Fawcett,* [1942] Ch. 304, *per* Lord Greene at p. 306.
33 See Clark, *"Ultra Vires* after *Rolled Steel Products",* (1985) 6 Co. Law 155, 158.

and a *Bell Houses* sub-clause, a company's contractual capacity will be close to that of a natural person. By the decision in *Rolled Steel* the court has abandoned the *ultra vires* doctrine as the appropriate vehicle for implementing the prime policy aim of protecting shareholders and creditors. In order to strike down an unreasonable depletion of corporate assets, such as in *Rolled Steel, Introductions* and *Re David Payne,* other means — including breach of duty and the law of agency — will be used.

The relevance of the above analysis depends, of course, on *Rolled Steel's* acceptability as an authority in the Singapore courts. As noted by a commentator, it may be doubted whether *Rolled Steel* represents the law of England let alone, in our context, that of Singapore.[34]

We have by now completed a thorough examination of the *ultra vires* doctrine with its latest developments as contained in the *Rolled Steel* case. It is proposed that we now assess the impact of the *Rolled Steel* decision on section 25 of the Singapore Companies Act.[35] The reasons for this exercise might be academic as it is inconceivable that English common law would be permitted to change or abrogate a statutory provision in force in Singapore. Nevertheless it is hoped that the exercise will provide pointers as to the direction which the Singapore law should take.

X. THE IMPACT OF THE *ROLLED STEEL* DECISION ON SECTION 25 OF THE SINGAPORE COMPANIES ACT

As earlier mentioned, the doctrine of *ultra vires* existed for the protection of shareholders and creditors and not for the protection of outsiders. As discussed, the plight of the innocent outsiders has forced the common law courts to introduce the rule that the validity of such transactions is dependent upon whether the outsiders concerned have notice of the foreign purpose behind the transaction.[36] The impact of the *Rolled Steel* decision lies in Slade L.J.'s efforts to provide a conceptual basis for this later rule. Slade L.J. unequivocally suggested that the *ultra vires* doctrine when applied in relation to outsider's interest must be modified on policy grounds.[37] In his opinion, acts that fall within the scope of an implied or more particularly an express power must be *intra vires* and can only be impeached on other legal grounds.

This common law regime for the protection of outsiders set up by Slade L.J. is perhaps unnecessary in the Singapore context. The reason is that a statutory regime for the protection of outsiders has already been provided for by section 25 of the Singapore Companies Act.[38] In essence, the section provides that no act or purported act of a company and no conveyance or transfer of property, whether real or personal, to or by a company shall be invalid by reason only of the fact that the company was without capacity or power to do such act or execute or take such conveyance or transfer.

34 *Ibid., p.* 159.
35 *Supra,* note 1.
36 See earlier discussion at pp. 36-40.
37 See earlier discussion at pp. 39-40.
38 *Supra,* note 1.

Since *Rolled Steel* has decided that acts falling within the scope of an implied or express power should be regarded as *intra vires,*[39] it follows that it is no longer possible to argue that such an act has been performed without capacity or power and is therefore *ultra vires.* If this is so, then the purpose of section 25(1) to protect such a transaction from being set aside on the ground that it was entered into by the company without capacity or power becomes defunct. If this is the necessary consequence of importing the *Rolled Steel* decision it is unlikely that the case will be regarded as stating the law here as it would partially abrogate the scope and effect of section 25. The reason why it is only partial and not total abrogation is that the scope of the *Rolled Steel* decision is limited and arguably excludes cases that do not involve the interests of outsiders.[40] It also excludes cases where the corporate acts in question do not even fall within the scope of the implied or express powers and are therefore clearly *ultra vires.* Such cases should remain governed by the strict logic of the original *ultra vires* doctrine and section 25 should continue to perform the legislative role of providing the much needed relief to outsiders.

Perhaps, it is also desirable to reject the *Rolled Steel* decision because, as we shall see, the protection conferred upon an outsider under the *Rolled Steel* regime is inferior to that conferred under the statutory regime. The reason is that under the statutory regime the *ultra vires* transaction remains binding regardless of the outsider's state of knowledge as to the purpose behind the transaction. This interpretation is supported by writers commenting on an equivalent Australian provision and they have expressed the view that:[41]

> The cases dealing with deemed notice by a person dealing with a company of its public documents, with the rights of third parties and with such activities as *ultra vires* borrowing are it is conceived no longer of practical import.

Thus an outsider such as a bank could make detailed investigation into a company's affairs without the anxiety that it might be fixed with actual knowledge of directors' impropriety and thus lose the statutory protection in the process. In contrast, under the *Rolled Steel* regime, a bank which has notice of the impropriety would most certainly lose the protection it might get. Although it was stressed in *Rolled Steel* that an outsider is under no duty to inquire into the purpose behind a transaction[42] and therefore could avoid being put on notice of the impropriety of the transaction, this suggestion does not accord with commercial realities as it is inconceivable that a bank would not first inquire into the affairs of a company before lending money to it. Therefore, the common law regime of protection for outsiders is inferior to the statutory regime as the whole regime was premised on the ground that the outsider has not been put on notice of the impropriety that affects the transactions whereas under the statutory regime the knowledge element is irrelevant.

39 *Supra,* note 20, at p. 507.

40 See earlier discussion at p. 40.

41 See section 20 of part III, Division 2 of the 1961 Australian Uniform Companies Act, and Wallace and Young, *Australian Company Law and Practice,* (1965) at p. 99.

42 See earlier discussion at pp. 41-42.

On the other hand it might be argued that the *Rolled Steel* regime confers more protection in some other manner in that it makes it extremely difficult for minority shareholders to challenge the transaction between the company and outsider as being *ultra vires.* Since such transactions would be invariably regarded as *intra vires,* their only remedy is to sue the directors for a breach of trust and to do so they would have to contend with the *Foss* v. *Harbottle*[43] rule. To add to their misery, since the *Rolled Steel* decision has to a great extent abolished the *ultra vires* doctrine it is now open to the majority of the members to affirm the directors' action leaving the minority with no right of action at all.[44]

In contrast, section 25(2) (a) retains the right of minority shareholders to restrain the company from doing any act or acts or the conveyance or transfer of any property on the ground that the company lacks capacity or power to do so.[45] However, it must be emphasized that proceedings under section 25 (2) (a) will not automatically result in the outsider being denied the benefit of the general validating effect of section 25(1).[46] The reason is that section 25(3) provides that:

> If the authorised act, conveyance or transfer sought to be restrained in any proceedings under subsection (2) (a) is being or is to be performed or made pursuant to any contract to which the company is a party, the Court may, if all the parties to the contract are parties to the proceeding and if the Court deem it to be just and equitable, set aside and restrain the performance of the contract and may allow to the company as to the other parties to the contract, as the case requires, compensation for the loss or damage sustained by either of them which may result from the action of the Court in setting aside and restraining the performance of the contract but anticipated profits to be derived from the performance of the contract shall not be awarded by the Court as a loss or damage sustained.

It can be gleaned from the above provision that although section 25(2) (a) has retained the right of the minority shareholder to challenge the transaction entered into by the company with an outsider, the rights and interests of the outsider have been carefully balanced under subsection (3) against these rights. Gone are the days when an outsider might suddenly find himself confronted with a declaration that the contract he had entered into earlier was now null and void as being *ultra vires* and hence incapable of conferring any rights on him.[47] Commenting on how the Australian equivalent of section 25(3) balances an outsider's interest, Street J. in the Australian case of *Hawkesbury Development Co. Ltd.* v. *Landmark Finance Pte. Ltd.* declared that:[48]

> In effect, where pursuant to Section 20(2) (a) [25(2) (a) in Singapore's Companies Act] a shareholder brings proceedings against

43 (1843) 2 Hare 461.
44 See Clark, *supra,* note 33, at p. 159.
45 Wallace and Young, *Australian Company Law and Practice,* (1965) at p. 98.
46 *Hawkesbury Development Co. Ltd.* v. *Landmark Finance Pty Ltd.* [1969] 2 N.S.W.R., *per* Street J. at p. 122.
47 *Ibid.*
48 *Ibid.*

> his company and a stranger in respect of an existing *ultra vires* contract, the court is given wide power under Subsection (3) to achieve justice and equity as between the company and the stranger. In some cases the court might decline to intervene under Subsection (3), thus permitting performance of the contract to go forward, alternatively, the court might deem it to be just and equitable simply to set aside and restrain performance of the contract, in other cases, the order to set aside and restrain might be coupled with an order that the company pay compensation to the stranger; and in yet other cases the setting aside and restrain might be accompanied by an order that the stranger pay compensation to the company. The court is given a wide charter by S20(3).

Thus, an outsider is not seriously disadvantaged by the fact that the statutory regime has retained the right of the minority shareholder to challenge the validity of the transaction.

It is also interesting to note that the most poignant illustration of the inferiority of the *Rolled Steel* regime to the statutory regime is demonstrated by the result of the *Rolled Steel* case itself. As may be recalled, the outsider in that case lost at the end of day on a mere technicality. As the board of directors that had purported to authorize the transactions in question was inquorate because one of its directors had failed to disclose his interest in them, the resultant transactions were rendered void *ab initio* because they could not be regarded as being deeds of the company. It was also fatal to the outsiders that they had notice of the impropriety involved.[49]

If *Rolled Steel* were to be decided under the section 25 regime the result might be different. A similar argument to the above could be made on the ground that section 25(1) operates to validate an act only when there has been an act of a company. It follows that under the factual circumstances of the *Rolled Steel* case there was no act of the company to speak of, as the act had not been properly authorized. And this fact was at least within the constructive notice of the outsider. What was done was therefore not an act of the company as such and such an act must be regarded as void *ab initio.* It is submitted that this argument is not tenable under section 25(1) because it expressly provides that an act of a company includes any act done on behalf of a company by an officer or agent of the company under any "purported" authority.[50] These words strongly suggest that an act of a company under section 25(1) includes an act that has not been duly authorized and, as already noted, the knowledge element on the part of the outsider is irrelevant. Thus section 25(1) might still be successfully invoked to validate the guarantee and the debenture given by the company.

On balance, it seems that the *Rolled Steel* regime displays sophistry in every aspect of its conception. The decision reveals little appreciation of the real issue in the *Lee, Behrens* principle and it is fair to say that the attempt to remodel the *ultra vires*

[49] See Sealy "*Ultra Vires* and Agency Untwined", (1985) 44 C.L.J. 39, 41.
[50] See section 25(1), *supra,* note 1.

doctrine is nothing more than an over-zealous attempt to help the outsider. In this regard, it is difficult to hail the decision as being a step in the right direction.

XL CONCLUSION

It is submitted that the *Rolled Steel* decision ought not be accepted as good law in Singapore and that section 25(1) of the Companies Act should continue to apply with all the attendant advantages in favour of the outsider. It is further submitted that it is perhaps unnecessary to receive the English Court of Appeal decision as law here for the reason that section 23(1) and the attendant Third Schedule of the Singapore Companies Act have comprehensively set out the powers of a company to safeguard the interests of any innocent outsiders.

With regard to the *Lee, Behrens* principle, it is submitted that since very few of the English judges actually understood the special role of the principle as an alternative yardstick for the implied creation of powers, it is open to the Singapore Courts to decide whether the principle ought to be received into the local law, especially in cases involving gratuitous disposition of company assets. Given the ineffectiveness of the *ultra vires* doctrine as a whole to protect shareholders and creditors, the real issue is whether we should follow the example of the Australians who, on 1 January 1984, abolished the *ultra vires* doctrine altogether.[51] However, it is interesting to note that the new provisions in the Australian Companies Act[52] did not abolish the doctrine of *ultra vires* in relation to those companies which retain, or elect to have, stated objects in their memorandum.

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[51] See Paterson and Ednie, *supra,* note 83, at p. 53, 101.

[52] See section 67 and 68 of the 1981 Australian Uniform Companies Act.

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