Limits on Corporate Power under Ethiopian Law: Does the Ethiopian Commercial Code Recognize the Doctrine of Ultra Vires?

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Abstract

It is normally expected that companies to act within the contours of predetermined purposes as stipulated in the purpose (object) clause of memorandum of association. Any attempt to go beyond the scope of the delineated purposes is ultra vires. In accordance with the classic doctrine of ultra vires a dealing or a transaction which is beyond the legitimate power of company is devoid of legal effect. In Ethiopia however it is not clear whether the Commercial Code recognizes the doctrine of ultra vires or not. The Ethiopian Commercial Code simply states that business organizations cannot engage in unpermitted ventures. If this prohibition is taken as ultra vires, then its possible effect has to be determined. Nowadays in advanced systems the doctrine of ultra vires has been dwindling. The Ethiopian Commercial Code appears not in line with the global trend. The article attempts to expose the on-going global development on corporate ultra vires, and suggests the Ethiopian law to reconsider its stance by aligning with the changing global business milieu. After brief discussion on the rationale behind limitation of the contours of corporate powers expressed in the purpose clause of memorandum of association, this article explores the possible effects of ultra vires transactions in Ethiopia by applying doctrinal research methodology.

Keywords: commercial law, commercial code, ultra vires, company, corporate

I. Introduction

Since the time of *Fetha Nagast* Ethiopia has commercial laws that meant to regulate the emerging commercial activities. The then fragmented commercial legilsations were either discarded or recodified in the Commercial Code of 1960.[1] The Commercial Code of 1960 was designed to modernize the Ethiopian commerce by facilitating the creation and sustenance of capital. With a view to modernize commercial institutions and commercial regulation, the Imperial Government relied on the acumen of the renowned international comarative lawyers. Consequently, the rules enshrined in the Commercial Code of 1960 were

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1 Comm. Code of the Empire of Ethiopia, Proc. No. 166 of 1960 *Neg. Gaz.* Estraordinary Year 19th May 1960, A.A..

crafted in comparative perspectives. The Code incorporated rules developed elsewhere in the globe in comparative approach. The rules of the Commercial Code of 1960 were very progressive and designed in projection of the future Ethiopia. It was not simply a transplant of one system, but reflected both continental and common law approaches. However, the ever advancing digital technology and virtual transaction rendered some of the rules of the Code obsolete. Consequently, the Commercial Code of 1960 had been under revision for a decade, and finally revised Book I and Book II of the Commercial Code of 1960, including bankruptcy provisions incorporated in the Commercial Code of 2021.[2] Like its predecessor, the Commercial Code of 2021 does not specifically use the expression ultra vires. It simply copied the old provisions prohibiting running unauthorized ventures. This necessarily triggers doubts whether the Ethiopian Commercial Code recognizes the doctrine of ultra vires or not.

The government, as a guardian of public interest, has a mandate to regulate the operation of business organizations. Needless to say the regulation of commercial transactions and commercial instituiuons is vital in economic governance. In line with the nations economic policy, commercial laws set forth rules governing the kind of business organiaiton that can be set up, the formation requirements and procedures that have to be followed, and in some cases the overall scope of operation. Business regulations starts with preliminary works of founding a business entity, scrutiny during business registration, business licensing and periodic follow up by an appropriate government agency. Though companies can engage in any economic activity that can usher profit, they have to act within the bounds of mandatory regulations by confining their activities within the ambit of the business license granted. Generally, though there is constitutional freedom to engage in a trade of ones choice, the freedom is not completely unstrained -- companies can operate only ventures with the permission of the regulatory agency. The regulatory agency controls corporate ventures through registration and deposit of foundational documents. During registration of the company regulators assess the commercial transactions to be carried out in line with the nations economic priorites. Companies are expected to list down all conceivable venture to be carried out in their preformaiton document – the memorandum of associaiton. In this regard, the Commercial Code of 2021 follows the rules of the Commercial Code of 1960. Both the

[2] Comm. Code of 2021, Proc. No. 1243 *Fed. Neg. Gaz, Extra Ordinary*, Year 27 No. 23 A.A. Apart from the some speicific changes in the form of companies, substantial rules of the Com. Code of 1960 forwarded to the Com. Code of 2021. The Com. Code of 1960 recognized three partnerships, a joint venture, and two companies. The Com. Code of 2021, has scrapped ordinary partnership, and introduces limited liability partneship, and single person private limited company. There is little change in regulation of share company and the traditional private limited company

Commercial Code of 1960 and the Commercial Codes of 2021 declare that no busienss organization can carryout an activity that is not permitted to do so.[3] Does this prohibiton mean recogniziton of the doctrine of ultra vires? If so what is the extent of the doctrine and its current effect? Now in most jurisdicitons the classical doctrine of ultra vires is either abolished through judicial pronouncment or its scope has been diminishing consideerablly, but the Ethiopia's stance is not clear. This short work attempts to assesses whether the Ethiopian Commercial Code recognizes corporate ultra vires by applying doctrinal research methodology.

II. The Power and Function of Company: what companies can do and cannot?

Normally, founders/promoters determine the kind of company to be constituted, specific ventures to be carried out and the scope of business purposes to be carried out. As do in other cases, the freedom of business is not absolute. The right to carrryout a business activity is controlled by the mandatory rules of law. Subject to mandatory provisions of the commercial code, companies can decide on the nature and scope of activities to be carried out. Meaning, within the limites of law, companies are free to list down any conceivable venture in their constitutional document. Traditionally companies are confined to carryout activities enumerated in the purposes/objects clause of memorandum of association. A purpose is a goal that founders/promoters wish to achieve by the instrumentality of the company. Literally, it is a compendium of activities that a company intends to accomplish. Choice of the purpose depends upon the interest of founders/promoters. The present trend in drafting purpose (object) clause is to craft it in a widest possible terms, enumerating every possible activity in which the company might run at any time or wishes to engage in the future. To list down activities in the purpose clause, the drafter has to know the activities that promoters/founders of the company desire to operate. The drafter of memorandum of association is expected to counsel the promoters/founders and take note of whatever legal venture that the promoters aspire to operate.

Though rarely accepted in Ethiopia, a purpose clause of memorandum of association may hold a provision that allows non-enumerated but related ventures. English and some Anglo-Saxon laws allow companies to state a general object that may be implicit in the expressed objects. Incidental ventures are activities or business transactions having some nexus with the

[3] Comm. Code of 2021. Art. 25. This provision is a cut and paste of art. 26 of the Comm. Code of 1960, Art. 26.

expressed ventures. The implied doctrine permits to operate ventures necessarily implicit in the explicitly enumerated activities in the purpose clause of the memorandum of association. The last object of memorandum of association expresses the possibility of running activities incidental to the expressed ventures. This catch-all enumeration would entitle the company to run activities that are possibly incidental to the main ventures that are expressed in the purpose clause. In other words, the last enumeration often expressed in general terms in a way it allows the company to carry out all conceivable activities having nexus with the activities expressly enumerated in the purpose clause. Thus, express purposes in the purpose clause may be supplemented by "incidental objects clause," which align with the expressed purposes. This enables companies to run closely related ventures that are conducive to the attainment of the company's main objects.

One may question the purposes of purpose clause. In this fast-changing business milieu, why companies are not permitted to flexibly run whatever activity they wish to run without the need to rigidly fix it in the memorandum of association or get permission by the regulating agencies? The purpose clause has practical significance. First, incorporation of purpose clause in the memorandum of association helps regulating agencies verify the legality of the company's venture. The office of registration uses the business purpose clause to assess whether the company can legally engage in a particular business activity. The purposes enumerated in the purpose clause of the memorandum of association should be of a nature that can be legally carried out. Thus, if anyone or more of purpose is illegal or immoral, the office of registration may require rectification or in the worst case may deny registration. Second, a purpose clause shields investors' interest. The capital of a company (either share company or private limited company) is a money contributed by individual shareholders.[4] Contributors (investors) should know the purpose for which the investment will serve. The money raised from shareholders (investors) cannot be spent in a purpose which is not known to the investors at the time of subscription of shares or later added through amendment. The purpose clause therefore gives some assurance to the investors that the fund that was raised for one purpose cannot risk another undertaking. The business purpose (object) clause of memorandum of association safeguards the interest of shareholders by confining the company to run a predetermined venture. Shareholders of a company may be attracted by the

[4] A single – person company is almost similar to a sole-proprietorship. The single member decides the purpose of the formation of the company, shares are not offered for public subscription, and so forth. In reality thus the capital of the company belongs to the single member. As the liability of the company is limited, creditors of the company can also check the purpose of the company.

business that the company actually carries out or plans to operate. Thus, if the company were permitted to run whatever venture it views good without seeking the consent or knowledge of the shareholders, investors may not be attracted to invest. Investors may not be interested to subscribe shares of a company that would potentially compete with the investor's private business. Investing in a potentially harmful company is just like standing at the side of an enemy. Investment in a company should not serve as a backfire. The enumeration of specific activities to be carried out thus affords enormous benefit to prudent entrepreneurs.

An investor may also be interested in the venture expressed in the memorandum of association. An unlimited power to change the venture thus would inflict unexpected harm. The purpose clause of the memorandum of association assures shareholders that money contributed to the company cannot be spent in a field that is not mentioned in the purpose clause of the memorandum of association. Thus, "… an investor in a gold mining company did not find himself holding shares in a fried fish shop…."[5] Moreover, potential investors give priority to certain business activities that would benefit their own private business[6] or contribute to the venture that the investor values.

Further, purpose clause assists potential subscribers to determine whether to invest in the company. Before subscribing shares, investors often appraise the feasibility, profitability of the venture, and in some cases the side effects of the ventures of the company in investor's personal business. Thus if the purpose of the intended project is detrimental to the economic or other interests of the investor, he/she may not dare to invest in a company whose venture is prejudicial to the private interest of the investor.

Thirdly, purpose clause affords protection to creditors. The fact that a company cannot engage in an activity that is not specified in the purpose clause creates a sense of security to the creditors. Creditors, when lending money to a company, assess the objectives for which the company was set up and would like to know how the money loaned may be spent. This helps the creditors appraise whether the loaned money can be paid back. Financial institutions, when lending money, are guided by the object clause of the memorandum of association to release fund, as they have to consider priority sectors. The creditors would be

5 J. Beaston et al (eds.) *Anson's Law of Contract*. (30th ed. 2016) p. 248.

6 For instance, if the company plans to produce raw materials that would be consumed by investors private business or plans to consume products of the potential investor, he/she may be motivated to subscribe shares of the proposed company.

assured that the debtor company cannot run an unknown and risky businesses. If the company attempts to transcend the limits of the purpose clause of the memorandum of association, creditors can stop the company by instituting injunctive suit or demand payment or get some kind of assurance for payment of the debt. If companies were freely permitted to run an activity that is not predetermined, without any limitation, there is possibility that the company may spend its capital in a speculative venture. This would obviously jeopardise the interest of creditors – normally the company's capital is the only security available to the creditors. Thus, anything that may drain company's capital endangers the interest of creditors. Creditors, in addition to getting back the loaned money, may have interest in particular venture. The purpose clause may attract the creditors not only in possible profitability, but also may advance the creditors personal or business interest. If the debtor company does or plans to do an activity that would compete with the private business, the creditor may deny the application for loan.

Finally, purpose clause, by confining corporate activities within defined field, serves public interest. As a general rule, the company should stick to the objects stated in the purpose clause of the memorandum of association. The purpose clause, by confining the company only to the predetermined ventures, serves public interest. It prevents the concentration of economic power in one company – avoids or limits monopoly. Monopolization hurts the public in various ways. A company with monopolistic power may not worry about quality or efficient customer care. Further, in monopolistic holding customers have little or no choice – the public may be forced to pay high price. This undoubtedly hurts the public. Competitive market, on the other hand, enhances welfare system. Besides, if the company carries out only pre-determined activities it would get specialization in fixed ventures that would possibly boost productivity. This in turn increases customers' taste, which will encourage further investment. Specialization also reduces production cost thereby dropping selling price. But if the company were allowed to frequently change its venture, without any restriction, the company would remain unproductive – this hurts public interest. The law thus by confining the company to operate only predetermined businesses serves public interest.

III. Purpose/object clause and the doctrine of ultra vires

The purposes specified in the purpose clause of memorandum of association serve as restrictive fence that limits the power of company management to act only within the contours of the defined landscape. Traditionally, any attempt to transcend the enumerated purposes or engage in a venture that is not expressly or implicitly stated in the purpose clause is violation of the law. In accordance with the classical theory, engaging in a venture that is not expressed or implicit in the purpose clause of memorandum of association is *ultra vires*.[7] Literally, the expression, "ultra vires" is "beyond power."[8] Thus, if representatives of company attempt to carry out an activity that is not expressly or implicitly stated in the purpose clause of the memorandum of association, the activity is beyond power of the company. As a representative's power naturally cannot exceed the power of the principal, the maximum limit of power of personnel is the power of the principal. Therefore, either the directors or managers who act on behalf of company, cannot legitimately work beyond the purposes specified in the purpose clause. Thus, unless predetermined purposes are modified through legally sanctioned procedures, no one could act beyond the specified purposes. In accordance with the strict application of the traditional ultra vires doctrine, even a general body of shareholders could not approve a beyond power venture.[9] This was based on the rationale that the company has got legal personality to carryout purposes it is empowered to engage in and has got business license. Artificial personality is not absolute – companies can execute only predetermined ventures. This aligns with the classic doctrine of ultra vires. In the words of Eisenberg:

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7 The doctrine of ultra vires is different of *intra vires*. The company may have power to act in some ways, but the authority of its officers may be limited. If the company representatives act beyond the granted power, unless third parties act in bad faith, an intra vires transaction cannot affect the interest of third parties. The doctrine of ultra vires is Anglo – Saxon concept but it also introduced to civil law nations such as France, Germany and Japan. The Japanse Civil Code use the expresssion purpose calsue, which is also true in Ethiopia. See Akio Takeuchi, "How should we Abolish the Ultra Vires Doctrine in Corporation Law?" Law Japan (Dan Fenno Henderson (trans.)1968) p. 140.

8 See W. "Ultra Vires in Modern Company Law." *The Modern Law Review*, vol. 46, no. 2, 204 (1983), *JSTOR*, www.jstor.org/stable/1095493. Accessed 1 Dec. 2020.

9 L.C.B Gower *Principles of Modern Company*, (Paul L. Davies (ed.) 6th ed. 1997) P. 203. Lord Cairns in *Ashbury Railway Carriage and Iron Co. v. Riche* remarked: "… if the shareholders of this company could not abante have authorized a contract of this kind to be made, how could they subsequently sanciton the contract after it had, in point of fac, been made?" L.R. & H.L. 653 (1875) noted in H.R. Hahlo & M.J.Trebilcock, *Hahlo's Casebook on Company Law* (2nd ed. Sweet & Maxwell 1977) p. 158. In the words of eisgenberg, " … under classical English law even unanimous shareholder ratifcation wouldnot be a bar to an ultra vires defense if the trnsaciton was outside the objects of the coroporation." Mervin A. Eisgenberg, *Corporations and Other Business Organizations Cases and Materials (9th Foundation Press*, 2005) p. 122.

> … the corporation is regarded as a fictitious person endowed with life and capacity only insofar as provided in the charter [now memorandum of association]. Early corporate charters tended to narrowly circumscribe the activities in which a corporation could permissibly engage. Transactions outside that sphere were characterised by the courts as ultra vires (beyond the corporation's power) and unenforceable against the corporation….[10]

The doctrine of ultra vires shields creditors and investors from unauthorized use of company's fund. As liability of the companies is limited, its fund is the only security to creditors and third parties who deal with the company. In this sense, company's capital cannot be used to run a venture in respect of which the company is not licensed. Eisenberg shares this view stating: "The original purpose of the ultra vires doctrine seems to have been to protect the public or the state from unsanctioned corporation activity."[11] This dictates company management to run only predetermined ventures. Creditors or investors release loan or investment in the company in reliance of facts stated in the purpose clause of the memorandum of association, and other pertinent clauses that reveal the financial position of the company. The need to confine to the predetermined purposes that are enumerated in the purpose clause of memorandum of association restricts corporate management to avoid speculative ventures that would destroy the wishes of creditors and investors. If anyone or more of the purposes of company has to be modified, investors or creditors who invested or lent fund in assumption of the old purpose, should give their consent or get paid.[12] In this regard the classic illustration, "… an investor in a gold mining company did not find himself holding shares in a fried fish shop, and to give those who allowed credit to [a] limited company some assurance that its assets would not be dispatched in unauthorized enterprise,"[13] best explains how unexpected change in venture is detrimental to the interest of creditors.

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10 *Id*.
11 *Id.*
12 Art. 463 of the Comm. Code *supra* note 1.
13 J. Beaston *et al supra* note 5.

The governing rule of the doctrine of ultra vires was first demonstrated in seminal English case *Ahbury Rail Way Carriage and Iron Co. Ltd v. Riche.*[14] The purpose/object clause of the memorandum of association of the company enumerated the following objects:

1. "To make and sell or lend or hire railway carriage, wagons and all kind of railway plants,
2. To carry on business of mechanical engineers, and genral contractors,
3. To purchase, lease work and sell mines, minerals, land, and buildigs,
4. To purcahse and sell, merchants timber, coals, metals or other materials,
5. To buy and sell materials on commission or as agents,
6. To acquire, purchase, hire, contruct or erect works or buildigns for the purpose of the company, and
7. To do all such other things as are necessary, continent incidental or conductive or any such objects."[15]

The Company with these chartered purposes concluded a contract with the Plaintiff (Riche), to finance construction of railway project in Belgium. Based on the financing agreement, Riche contracted with Ashbury Railway Carriage & Iron Company to construct the said railway. After Riche performed some of the stated works, Ashbury repudiated the contract claiming it was ultra vires. Riche brought action requiring Ashbury to respect the terms of the contract. The issue was whether financing construction of a railway in a foreign country was within the ambit of the power of the company. With the intention to release directors involved in the contract from the claim of abuse of power liability, shareholders of the defendant company unanimously approved the transaction. Disregarding this formal ratification of the unauthorized transaction the case was lodged in court of law. The "House of Lords held that the contract was ultra vires, on the ground that it lacked the power under the charter,"[16] therefore altogether void. If a transaction is void, then it cannot be ratified even by unanimous consent of all of the shareholders.

It is vividly evident that financing construction of railway in a foreign country was not specified in the purpose clause of the charter of the company. Financing a contract in a

[14] L.R. & H.L. 653 (1875) SeeHahlo and Trebilocock *supra* note 9.
[15] *Id*.
[16] *Id.*

foreign country cannot be easily followed up by the investors and creditors of the lending company. As a general rule, directors of the company have to confine themselves to carryout activities expressed in the purpose/object clause. In *Ashbury*, the House of Lords concluded that financing a construction contract abroad was ultra vires.[17] Though not stated in the judgement, it is equally doubtful to consider the legality of financing had the contract been not in a foreign country. Similarly, a company should have an express power to guarantee performance of an obligation. Unless it is a surety company, guarantee cannot be implicit. For example, In *Bringson v. Mill Supply Co*.,[18] it was held that guarantee given for performance of an obligation was ultra vires. [19]

The purpose clause of memorandum of association of Ashbury Railway Company appears very vague and may be subject to multiple interpretations. In Ethiopia a purpose expressed in general terms cannot be accepted for registration.[20] Further, in practice the office entrusted with registration of companies, in Ethiopia, denies registration of a memorandum of association with implied powers, or expressed in general terms. In Ashbury's case, the seventh purpose is a catch-all box that can beef up unexpressed but incidental objectives. In Ethiopia, with a view to cut litigation, registering clerks advise companies to stipulate only express purposes. However, inclusion of incidental objects would enable companies to run all related ventures without the need to amend the memorandum of association. This in turn effectuates business thereby contributing to the economy and boosting job creation. If we choose to avoid litigation at the cost of efficiency, the avoidance of implicit purposes is preferable. With a view to mitigate harsh effects of the decision of *Ashbury*, English courts devised the implicit power doctrine.

The Indian Companies Act follows the traditional effect of ultra vires transactions. If an activity or a transaction is ultra vires, then it is null and void. It cannot be ratified at all. It is true void transaction is non-existent and cannot get life at all. The first Indian case in this regard is *Jahangir R Modi vs. Shamji Ladha*.[21] In this case the company purported to

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17 *Id.*

18 219 N.C. 498; 14 S. E. 2nd 505 (1941) noted in Eisenberg *supra* note 9.

19 *Id*.

20 Though not enunciated in the Code, the office of registration denies registration of a company with purposes stated in general terms enabling the company to run unexpressed but related ventrues. The prevailing global trend that suggest for abolition of the doctrine of ultra vires would change the Ethiopian stance. The law revision should consider the ever changing global trajectory.

21 4 Bomb. H.C. Report 185(1866 – 67).

subscribe stock of another company though this power was not expressed or implicit in the object clause of the memorandum of association. The then Bombay (now Mumbai) High Court held the transaction was ultra vires and hence void.[22] Is being a partner of partnership without express authority in the purpose clause of memorandum of association beyond power of company? Assume a company engaged in detergent factory. Running detergent factory was within the ambit of the power of the company. Is it ultra vires if the company invests in another detergent factory to operate it in partnership with another company? According to Eisenberg "[e]arly cases often held that a corporation had no power to enter into a partnership unless that power was explicitly granted by a statue or by the certificate of incorporation."[23] Similarly, the fate of entering into a joint venture business with another company is also questionable. Given restriction to devise an implied power in the purpose clause of memorandum of association, the possibility of implying unexpressed powers in Ethiopia is doubtful. Currently, in United States company laws expressly authorize corporations to enter into partnership or joint venture agreements even if the articles of association is silent on the issue,[24] but in Ethiopia implication is uncertain.

An ultra vires transaction is void – assumed non-existent. Consequently, persons involved in an ultra vires transaction may suffer loss or may be prejudiced in some way. Who is responsible for adverse effects of ultra vires ventures that are declared null and void? Normally a company is responsible for transactions carried out in its name. It is a person in law, but its personality is limited to carry out activities that it can legally carryout. Conversely, the company has no power to engage in an activity that it is not legally empowered to operate. On the same token, ultra vires generates duty on the company. Thus, if an ultra vires activity is rendered null and void, primarily managers involved in the transaction may be jointly and severally liable to redress the effects of ultra vires transaction. The directors or other personnel of company who acted beyond the legitimate power of the company are liable for the effects of ultra – vires transactions. The problem however is that the managers or other persons who represented the company in an unauthorized transaction/ venture may be not economically able to make the damage good. Is there any way to seek compensation from the company that has repudiated an ultra vires transaction? Unless

22 *Id*.
23 Eisgenberg *supra* note 9 at 123.
24 Sel. Gen. Corp. Law Section 122(11), N.Y. Bu. Corpo. Law Section 202(15) Model bus. Corp Act. Section 3.02(9) noted in Eisenberg *supra* note 9 at 123.

otherwise expressly provided by the company law, an innocent third party can seek compensation from the company by invoking the rules of unauthorized/apparent agency.[25]

Thus, if a company attempts to engage in an activity/ transaction that is not permitted to carryon, the illegal activity/ transaction generates double consequences: internal and external effect. Internally, shareholders may restrain the company from running an ultra vires activity by instituting injunctive action. The court may order the company to stop acting beyond its legal power. The external effect is an ultra vires activity is null and void. A null and void act cannot produce any legal effect. This rule was true in England before its incorporation into European Communities Law. After incorporation into the European Communities, the second effect of ultra vires transaction was changed. "Section 9(1) of the European Communities Act 1972 … attempted to dispose of all problems…." Accordingly, third parties we deal with directors of company in good faith were allowed to presume full power of directors in respect of all activities on behalf of the company they direct. This safeguards the interest of innocent third parties. Third parties may be said to be innocent if they were not actually aware of the limitation of the power of the company. In this case ultra vires transactions are viewed as valid and enforceable contractual link is created between the company and the innocent third party. The English company law did not absolutely abolish the doctrine of ultra vires but it rather establishes a presumption of good faith. The company still can set up the defence of ultra vires against a person who deal with it in bad faith, and where he seeks to enforce an ultra vires transaction against third party, the third party can still plead the defence of ultra vires. Shareholders can still be able to restrain a company from embracing on proceedings on or proceeding with a course of action, which is ultra vires.

The other consequence of ultra vires transaction is injunction. Shareholders or interested third parties can restrain the company from operating a "beyond power" activity by instituting action for injunction. In this regard too, the purpose clause of memorandum of association serves as a protective tool to safeguard interest of shareholders and the company from speculative businesses.

[25] See Art. 2195 of the Civ. Code. This point is brielfy dicussed in later section.

IV. The Dwindling Effecct of Doctrine of Ultra Vires

Initially the doctrine of ultra vires, by confining the company to engage in certain predetermined venture, meant to safeguard the interest of the public, creditors and investors, but the confinement backfired at all concerned because the company was barred from running profitable ventures flexibly aligning with the rapidly changing business world. In the words of Leacock:

> The doctrine [of ultra vires] did not effectuate its goals. Rather than serving as a reliable and effective shield for shareholders and creditors as anticipated, on the contrary, it became a troublesome barrier to the conduct of legitimate business activities. It was unscrupulously exploited to invalidate otherwise legally valid contracts, and thereby prevented companies from pursuing potentially profitable activities. Companies were legally disabled from pursuing business activities not stated in the objects clause….[26]

In a situation where constitutional documents of company cannot be freely alterable,[27] deprivation of an ability to carry on a profitable business backfired on the very people that the doctrine of ultra vires was meant to protect. Needless to say, if the company is profitable, the value of shares will rise, the ability to pay debt would be enhanced, and the public would get better service etc. Further, declaration of voidness of an ultra vires transactions and non-responsibility of the company had harmed innocent third parties. This had negative effect in transactions involving registered companies. Consequently, nations and commercial entities took several actions that had steadily diminished the traditional effects of the doctrine of ultra vires. The introduction of plethora of purposes in the memorandum, the limitation of constructive notice rule to situations of bad faith, and the implied power doctrines diminished the classical effect of the doctrine of ultra vires.

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[26] Stephen J. Leacock, "Rise and Fall of the Ultra Vires Doctrine in United States, United Kingdom, and Commonwealth Caribbean Corporate Common Law: A Triumph of Experiancew Over Logic" *Depaul Business and Commercial Law Journal* Vol. 5 Issue 1(2006) p. 78.

[27] For instance until 1948 in England memorandum of assocaiiton of companies were not freely amendable. Before 1948 English companies could amend object clause of memorandum of association only after securing court authorization.

First, with a view to mitigate or possibly avoid ultra vires, companies drafted long list of powers that apparently meant to allow companies run wide spectrum of ventures. Companies started to list down plethora of powers even if the company does not invoke it. The long list of purpose/object clause, long list of power of the company could not help the company to escape from the invocation of the doctrine. Courts often ignored powers that did not relate with the expressed purposes. This subjected the companies with the unwarranted lengthy litigations.

Second, after five years of the decision of *Ashbury Rail Way Carriage and Iron Co. Ltd v. Riche,*[28]the Court recognized implied powers doctrine. The introduction of implied power doctrine has further diminished the doctrine of ultra vires. The House of Lords in *A. G. v. Great Eastern Railway Co,*[29]sanctioned the practice of using implied powers doctrine. By referring to the implied powers companies are allowed to run business having some kind of nexus to the enumerated purposes and goals of the company. For instance, a Florida company whose purpose under its charter was to run a railroad was allowed to operate leasing and running a resort hotel.[30] The Supreme Court of United States concluded:

> "Undoubtedly the main business of a corporation is to be confined to that class of operations which properly appertain to the general purposes for which its charter was granted. But it may also enter into and engage in transactions which are auxiliary or incidental to its main business.[31]

But what is an implied power and how can we distinguish it from other ventures having no nexus with the expressed purposes/objects? Any legal activity that "… may fairly be regarded as incidental to, or consequential upon, the specified objects ought not be ultra vires."[32] The implied doctrine authorized companies to run all conceivable ventures that align with the main purpose/object of the company. An incidental business should have some nexus with the main object. If a company runs cattle breeding business for example, running non-enumerated veterinary clinic or veterinary school or cattle food factory may be viewed as ventures that are fairly incidental to the main business. But running completely unrelated

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28 L.R. & H.L. 653 (1875).

29 *A.G. v. Great E. Rt.* Co. (1880) 5 App.Cas. 473 (H.L) noted by Leavock *supra* note 26 at 79.

30 Leavock *supra* note 26.

31 The Supreme Court of United States in *Jacksonville, Mayport, Pablo Ry & Nvaviation Co. v. Hopper*, 160 U.S.514, 526, 16 S.Ct. 379, 40 L.Ed. 515 (1896) cited in Eisenberg *supra* note 9 at 123.

32 A.G. v. Great E. Rt. Co. (1880) 5 App.Cas. 473 (H.L) noted by Leavock *supra* note 26 at 79.

business is violation of law and ultra vires. For example, in *Introduction Ltd v. National Provincial Bank,*[33] the Company (Introduction Ltd) was formed in 1951 to provide accommodation and service to overseas visitors for long period of time but after change of board of directors, the new directors started running pig breeding. With a view to expand the business the Company borrowed money from National Provincial Bank. Before releasing the loan, the bank took copy of the memorandum of association that contained the original objects, but released the fund. In suit for challenging the legality of the loan, the court declared that the loan was ultra vires. Pig breeding was neither expressed in the purpose clause nor incidental to the main purposes expressed in the purpose/object clause of the memorandum of association.

Further the authorization of board of directors to run any business that is beneficial to the interest of the company,[34] and its incorporators is another progressive measure that has further diminished the significance of the doctrine of ultra vires. In United States, unless restricted by articles of incorporation, corporations are free to run all lawful business activity.[35] This has virtually relieved companies from the obligation to specify purposes in the articles of association.[36] Unless unwanted ventures are specified in the articles of incorporation, the document need not have a clause labelled as purpose/object clause.[37] This may appear as complete avoidance of the doctrine of ultra vires in United States, but actually not. First, if a United States Corporation runs an illegal venture, the venture may be viewed as ultra vires. Next, if articles of incorporation holds restriction in conducting business, violation of an express prohibition is ultra vires.

Finally, in United States the doctrine of ultra vires is not accepted as a defence that would relieve the company from corporate tort nor criminal responsibility. The theory of vicarious liability in this case works. A beyond power transactions may be invalidated but the company is responsible for acts or failures of its directors and officers. This protects the security of business transaction and builds public confidence to deal with a registered company. Thirdly,

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33 *Introduction Ltd. v. National Porvincial Bank*, Ch 199 (C.A. 1970).

34 *Bell House Ltd. v. City Wall Properties Ltd.* 2 Q.B. 656, (Eng. C.A. 1966)

35 In United States, states have their own company law. Though there is possibility to have a totally distinct corporation law, state corporaiton law aligns with the Model Corporation law.

36 In effect this has virtually weakened application of the doctrine of ultra vires in United States. Some may even argue that in United States the doctrine of ultra vires is practially dead.

37 This affords companies to flexibly run business activity. Though this may allow running a speculative business, its economic benefits outweighs the side effects.

if a company has already benefited from the effects of ultra vires transaction it cannot refuse to discharge its part of obligation claiming ultra vires. This assertion is based on the doctrine of estoppel. If a person has promised to act in some way, he/she should keep the promise and discharge it. If the other has discharged his/her part of obligation in reliance of the promise, the debtor is legally estopped to refuse his/her part of performance. Fourthly, in United States unanimous shareholder approval can bar the application of the ultra vires defence unless the action would be prejudicial to the interest of creditors. Finally, in United States the effect of certificate of registration is in a diminishing state. Thus, there is a possibility for companies to venture flexibly without the need to seek regulator's approval or control. This makes companies to run whatever business transaction without limitation simply based on business judgement rule. Though the practice may not be uniform in all companies, absence of limitation in corporate power practically diminishes the classical effects of the doctrine of ultra- vires.

Finally, the diminishing effect of the doctrine of ultra vires has a deteriorating effect in application of the doctrine of constructive notice. What is the doctrine of constructive notice and how it works in conjunction with the doctrine of ultra vires?

The law requires documents defining the power of company to be registered and deposited in the public office – the Office of Registration or uploaded on the website of the regulatory agency. The Office Registration is not simply Document Authentication and Registration Agency (DARA). DARA does not regulate companies or nor specifically authorized to register corporate documents. DARA however assists the Regulatory Agency – the Ministry of Trade and Industry and relevant regional agencies – by authenticating corporate documents. The Regulatory agency ascertains the legality of the purposes enumerated in the purpose/object clause of the memorandum of association or its constitutional charter. The memorandum of association should be available to the public. It has to be kept at a place where the public can see and even take copy of the registered documents. If the memorandum of association and accompanying documents are registered and deposited at a place where the regulatory agency (the Ministry of Industry and Commerce or uploaded in the web page) manages, the law assumes everyone knows the contents of the registered documents. This presumed notice is known as constructive notice. The doctrine of constructive notice is thus a legal supposition that the public is aware of the registered documents.

The strict application of the doctrine of ultra vires dictates persons who wish to deal with a registered company to inspect public documents and make sure that the dealing confirms with the purpose clause of the memorandum of association. Before contracting with a registered company third parties were expected to know the limits of the capacity of the company. This was unnecessary burden and imposition of duty on third party dealers. Failure to observe the voluntary duty may generate sever legal consequences. An ignorant dealer would suffer if the transaction is ultra vires and devoid of legal effect. The availability of the documents to the public and possibility to know the limits of the power of the company creates a legal presumption – a presumption that everyone who deals with a registered company is not only aware of the facts of the company, but also presumed to understand the contents of the registered documents. As the public may not necessarily have notice of the registered documents, the assumption of knowledge of registered document is harmful to unwary dealers.[38] Nowadays, company documents are available online, but still dealers should search the documents online to comprehend the legality of company's venture. Getting access to registered documents and understanding long list of purposes may not be easy to busy entrepreneurs. In this increasingly competitive business world, the 'duty" to comprehend the capacity of a company would create a hurdle that would stagnate business decision making.

Consequently in most advanced economies, there was tremendous dissatisfaction with classical effects of the doctrine of constructive notice and the theory of ultra vires. The classical theory of ultra vires is unsound to ever changing business activity. Rigidity would hinder advancement. Companies should be able to bend to cope with the fast-changing customer taste and advancing technology. The classical effect of ultra vires transaction had caused additional hardship to third parties. If a transaction is declared ultra vires, the interest of innocent third parties may be prejudiced. If the company assumes as if no transaction took place, and not responsible for effects of nullity of ultra vires transaction -- only third-party dealers bear the brunt of nullity of ultra vires transaction. Third parties are required to take precautionary measures by checking the true power of company. Thus, the doctrine of constructive notice and strict application of the doctrine of ultra vires is very detrimental to the interest of third parties.

[38] In lieu of observing registered documents dealers may ask the representatives of company regarding the legality of dealing and the capacity of the company, but in big companies this may not be feaible. In multinational companies, where thousands of dealers make business transaction, it would be hard, if not impossible to explain the contours of the power of the company to everyone who wish to transact with a registered company.

On account of various justifications, the traditional effect of the doctrine of ultra vires has been steadily diminishing. First, in most jurisdictions innocent third parties are protected from the effects of doctrine of constructive notice.[39] The basic objective of constructive notice is creation of the presumption of knowledge of the contents of registered documents (constructive notice). However, the doctrine is bad to unwary outsiders who cannot take precautionary measures before dealing with the company.[40] The public therefore is forced to be vigilant by taking note of registered documents as a precautionary measure to know the power and objects of a registered company. This made dealers reluctant to transact with a registered company. Innocent dealers who cannot understand the technicality of longwinded objects clause may be easily jeopardised. This obviously hurts past changing business milieu thereby affecting national economy by hampering the tempo of fast-moving business transaction.

With a view to halt the constraints of the constructive notice and reduce harsh effects of the doctrine of ultra vires, nations took remedial measures. English company law abrogated the doctrine of constructive notice except in situation of bad faith.[41] Leacock views the doctrine of ultra vires as a sword against innocent persons.[42] If the doctrine simply stands to relieve the company against acts of its representative who are supposedly aware of the limits of the power of the company, it is of course a sword that cuts the throat of unwary third parties who rely on words or acts of company representatives. Nowadays, in United States, UK[43], Canada and the Caribbean commonwealth, there is presumption of good faith.[44] Mere awareness of registered documents cannot affect the interest of third parties.[45] Third parties are assumed aware of the contents of registered documents if assisted by professional lawyers who understand the technicality of the registered documents. To establish bad faith claimants of ultra vires, presumably, the company should prove such awareness.

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39 In England since incorporaltion into the European Community strict application of the doctrine of constructive notice was changed. Companies are prohibited to use the doctrine of ulta vires as a "sword" against innocent third parties (Sections 108 and 109 of the 1989 English Company Law.)

40 Accordingly revier of English Company law suggested for total elimination of the doctrine of consturctive notice on justification that third party dealer are busy to get note of constitutional documents of compnay. See Leacock, *supra* note 26 at 87.

41 *Id* at 91; Section 108 of the 1989 English Company Law.

42 *Id.*

43 Section 35(2) of the1985 English Company Law provides the presumption of good faith thereby be shiting the onus of proving bad faith on the persons claiming the application of ultr vires.

44 Leavock *supra* note 26 at 41.

45 *Id.*

Is the doctrine of constructive notice applicable in the Ethiopian company law? Proclamation No. 980/2016[46] is silent on this issue. The Ethiopian law simply requires registration and deposit of company documents. It is however implicit that registration is not simply record -- keeping of company documents in the public office or webpages of the Office of Registration of the Ministry of Trade and Industry or pertinent regional offices, but the very purpose of registration and deposit of documents is creating public awareness regarding the power and activities of registered company. Interested parties can see registered documents or upon payment fee can take copy of the registered documents. This rule should apply to access webpages in which company documents stored or download it with the permission of the webpage owner. Nowadays, before a document submitted for registration and deposit of documents in the Ministry of Trade and Industry or in regional offices, the memorandum of association is required to be registered and deposited in the Office of Document Authentication and Registered Authority (DARA). In accordance with Article 18(3) any interested party can "… get a copy of information about a document in the hands of the notary…"[47] Upon payment of a prescribed fee (usually nominal service fee), the notary gives a copy of the document.[48] Therefore, the public has apple possibilities to know facts stipulated in the registered documents. As there is no obligation to see the contents of registered documents, the law presumes knowledge. Thus, the Ethiopian law implicitly recognizes the doctrine of constructive notice. Apparently, the Ethiopian law appears to recognize the classical effects of constructive notice. In Ethiopia thus everybody is presumed to know and even understand the contents of registered documents. Currently, in Ethiopia it does not matter whether a person is actually aware of the facts of registered document or not– the defence of ignorance of the registered facts is not acceptable. With a view to know the capacity, and business purposes of a registered company, prudent dealers should take note of registered documents.

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46 Commercial Registration and Licensing Proc. No. 980/2016, *Fed. Neg. Gaz*. 22nd year No. 101 Aug. 2016 A. A.

47 Authentication and Registration of Documents' Proc. No: 334/2003 Fed. *Neg. Gaz* 9th Year, No. 54 A.A 8th May 2003, Art. 18(3).

48 *Id*.

V. Effects of Ultra Vires Transactions under Ethiopian Company Law

The Ethiopian Commercial Code does not expressly provide possible effect of ultra vires transactions. But can we infer the application of the doctrine of ultra vires and its effects from the prohibitive words of Article 25 of the Commercial Code of 2021? Article 25 of the Commercial Code of 2021 states: "No business organization shall carry on a trade which is not permitted to carryon or which is subject to specific requirements with which the said business organization has not complied."[49] This prohibition extends to all forms of unauthorized ventures, which include corporate ultra vires. Before granting the permission the Ministry of Trade and Industry or regional offices of trade and industry or other relevant government offices may requires pertinent agencies to assess professional competence of running an expressed venture. If the professional competence of candidate company is positively assessed, the license may be granted. When the venture sought to operate does need competence assessment, by examining the legality of enumerated ventures, the Ministry of Trade and Industry or relevant regional offices register the company, and the company acquires separate legal existence. The company is expected to run only the registered ventures. The personality and power of the company depends upon the carrying out of the permitted ventures.

Though it is arguable to take Article 25 of the Commercial Code of 2021 as a provision meant to regulate ultra vires transactions in Ethiopia, the classical effect of ultra vires transactions and the consequences of operating an unpermitted venture is congruent. In both cases an unauthorized transaction is devoid of legal effect.

One may fairly question whether an unpermitted transaction is really an ultra vires transaction. As pointed out above an ultra vires transaction is a transaction which is beyond the power of the company. If a company purports to operate an activity that is not mentioned in the purpose clause of the memorandum of association, the activity is unpermitted and hence beyond the power of the company. Then why not such an authorized dealing is ultra vires? It is not the use of a matching expression that matters, but the effect of the transaction. An ultra vires engagement is not only violates company's constitution, but also it transgresses company law. Thus, engaging in an unpermitted business is not only illegal but also it

[49] Com. Code of 2021, Art. 25.

prejudicial to the public interest, which holds the interest of shareholders, creditors and innocent customers. Synonymizing an "unpermitted" venture with the expression "ultra vires" may not be a puzzling equivalence – in effect the two notions appear identical. An However, the notion of "unpermitted" business is broader in scope. It holds some transaction that need not be ultra vires. For example, a company may commence business without having its constitutional document registered or getting business license. In this scenario the whole venture is unpermitted and hence unlawful but not ultra vires. The issue of ultra vires raises only in respect of companies that are legally constituted. With respect to companies formally incorporated fulfilling the requirements of law there is no apparent difference between ultra vires transactions and unpermitted transactions.

Operating an unpermitted transaction affects public interest as it is prejudicial to the interest of shareholders, creditors and innocent third parties. Similarly, ultra vires transactions also affect public interest (the interest of shareholders, innocent third parties or creditors may be summed as public interest. This work suggests that Article 25 of the Commercial Code of 2021 may be invoked to apply the doctrine of ultra vires in Ethiopia. Thus, until the legislator takes its silage hammer that defines effects corporate ultra vires or direction offered by the Cassation Division of Federal Supreme Court, it is suggested to invoke ultra vires transaction as a competent of unpermitted transaction.

If a given form of activity (purpose) is listed down in the purpose clause of the memorandum of association and business license is granted on the basis of the enumeration, it is assumed that the company has got permission to operate the expressed activities. Before registering the company the registrar at the Ministry of Trade and Industry or regional offices, checks the enumerated purposes. If one or more of the enumerated purposes is of a nature that cannot be permitted, the officer will deny registration. On the contrary, if the enumerated purposes are acceptable and the company is registered and business license is granted the company is permitted to carry out the registered businesses. Engaging in anyone or more of the licensed and registered ventures is not only legal, but also within the legitimate power of the company (not ultra vires).Conversely, if a company attempts to engage in a transaction that is contrary to the enumerated objects, the transaction is impermissible by virtue of Article 25 of the Commercial Code of 2021. Meaning, an unpermitted venture is illegal and cannot be enforced in courts. As the doctrine of constructive notice is a governing rule, third parties who involved in the illegal transaction cannot be protected. The effect of such transactions is

no different from the effects of classic ultra vires transactions. Hence, though both the Commercial Code of 1960 and the Commercial Code of 2021 are silent on corporate ultra vires transactions, the overall effect of running unpermitted transaction in Ethiopia, and the classical effects of ultra vires transaction appears congruent. In line with the foregoing discussion on the nature and legal effects of ultra vires, it appears possible to conclude the Ethiopian Commercial Code, in effect, recognizes the doctrine of ultra vires.

Article 25 of the Commercial Code of 2021 does not provide the legal consequences of transgression of the prohibition, but Article 23 offers some clue. Article 23 of the Commercial Code of 2021 expresses possible effect of carrying on an activity without getting permission, like unregistered and unlicensed 'traders." In the sense of Article 23 of the Commercial Code of 2021, running an unpermitted business/transaction generates penal and civil effects. Further, the company cannot exercise the rights of legal trader in respect of ultra vires transactions, but when it comes to liability, the law enforcement by consider the illegal or unpermitted transaction as one of the commercial activity. Thus, undoubtedly the company may be forced to pay tax in respect of the revenue earned through unpermitted (ultra vires) transaction.

The rationale for unenforceability of ultra vires transactions is based on the nature of personality of companies. Juridical persons are mere creations of law. The contour of their personality is limited. Artificial persons are have got legal personality to carry out only activities that are expressed or implicit in the purpose clause of the constitutional document. Thus, if an artificial person engages in an out of power venture, the transaction is void. This assertion aligns with the rules of Indian and English company law. In India, for example, if a company engages in a venture that is not explicitly or implicitly envisaged in the object clause of memorandum of association, the ultra vires transaction is void and cannot be enforced. Consequently, any attempt to carry out an activity that is not explicitly or implicitly stated in the memorandum of association is violation of law – ultra vires. Literally it is beyond the legitimate power of the company. Consequently, if a company ventures in a transaction that it is not permitted to carry out or that is beyond its purpose clause as outlined in the memorandum of association, the transaction produces no legal effect.

It is not arguable that Ethiopian companies are not allowed to run unpermitted or unlicensed ventures. What does this actually mean, or what would happen if a company runs unpermitted

venture? Is the transaction null and void or may be invalidated at the request of interested parties? Can the company or its officers, or third-party dealers petition for nullity of the unpermitted transaction? The Commercial Code does provide a clear solution. The term "not permitted," or "not licensed" signifies running a venture in violation of law. Literally a venture in violation of law is an illegal activity/transaction or contract. It is a basic rule of law of contract that an illegal dealing is devoid of legal effect – null or void.[50] If an act is illegal or carried out in violation of law, any interested party can petition for declaration of voidness. As pointed out above, an ultra vires transaction need not be an illegal transaction in sense of general law, but it may be declared void if the transaction is beyond the power of the company. This may be justified in absence of power or capacity. If corporate managers execute an ultra vires, either the company, its officers, third party dealer or regulatory agencies can require declaration of voidness. This assertion aligns with the classical effects of ultra vires transaction.

General nullity of 'unpermitted' transaction would affect smooth functioning of commerce and sanctity of market. Categorical declaration of voidness of an ultra vires transaction would motivate the public to take strict precautionary measures that would in turn hamper quick business decision making -- hesitation to enter into business transaction stagnates commerce thereby backfiring the company. Automatic nullity of an ultra vires transaction releases the company from unwarranted transaction but it is detrimental to innocent third parties. But what is the standard for gauging innocence? If a person honestly believed that the company has capacity to enter into the transaction without getting notice of the limitation, he/she may be viewed as innocent. If third party dealers are required to check the purpose clause of the memorandum of association, the failure to comply with the law may strain the innocence. This prompts a question on application of the doctrine of constructive notice under Ethiopian law. Is there duty to check company documents to know the limitations in the power of the company? The doctrine of constructive notice appears unfairly dictating the public to take further actions when dealing with a limited liability company. As pointed out above, the old English law that strictly applied the doctrine of constructive notice has been changed – nowadays, innocent third parties are protected. Innocence in this case is unawareness of the actual limitation of the power of the company, but not failure to check and understand the contents of the registered documents. In this case, the onus to prove non-innocence goes to

[50] Civ. Code, Art. 1714

the company. Therefore, unless the company proves that the dealer had actual knowledge of the limitation of the company, third party dealers are presumed innocent. This actually makes the doctrine of constructive notice ineffective.

If an ultra vires transaction is unenforceable, what possible remedies are available to innocent third parties against the company? In accordance with the classical theory, if a transaction is ultra vires, the company cannot be obligated to do anything in respect of an ultra vires activity. This is based on the rationale that an ultra vires transaction is void and generates no right and obligation. However, to avoid unjust enrichment, things delivered under the guise of a void transaction shall be restituted.[51] Third parties can invoke the doctrine of unlawful enrichment to get things delivered to the company.

Further, in certain cases, innocent third parties can sue persons who represented the company in the unauthorized transaction. Unauthorized agents are personally responsible for the unauthorized representation. Third parties can also join the company in the suit against the person who acted on behalf of the company without having an authority to do so. As agents may not sufficiently compensate the third-party joinder of the company may the best option to get compensated. As a rule, a representative who acted beyond the legitimate power granted by the company or exceeded the power of the company is responsible for the effects of ultra vires transaction, but in exceptional cases, the principal company may be sued together with the person who acted on behalf and in the name of the company.[52] If the board of directors or other officers of the company have exceeded the power of the company they represent the representation is ultra vires, but innocent third parties may invoke the benefit of appearance of authority and join the company in a suit for reinstitution.[53] The company is not required to honor an out of power (ultra vires) transactions but may be forced to compensate innocent third parties for the ostensible authority. The benefit of appearance of authority is not always available. To invoke the benefits of appearance of authority certain minimum requirements set forth in the Civil Code shall be fulfilled.[54]. On account of conduct or words of the apparent principal third party dealer may honestly believe that the representative had actual authority. First, if the principal (the company) had informed third parties that the agent

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51 *Id*, Art. 1808(2).
52 See *Id*, Art, 2195.
53 *Id*.
54 *Id*.

had power to act in certain way[55], and later revoked this power but not informed revocation of the authority, the agent may deal with the third party in respect of the revoked power. If the third party is unaware of the revocation of the power, he/she considers the agent was authorized to represent the company. The innocent third party dealer can invoke the benefit of doctrine of apparent authority. This is a situation not so usual in respect of ultra vires transaction, but a company may alter its expressed or implied power amending the purpose clause of memorandum of association and get it registered and deposited in accordance with requirements of Proclamation No. 922/2015.[56] The informed third party may actually be unaware of the alteration of the informed power and deal with the company's representative. This is ultra vires transaction and may be declared null. The third party may join the company in a suit against the agent for compensation on account of appearance of authority. If the prior power of the company was communicated to third parties, the alteration has also to be communicated. The non-existent power but the already created appearance of authority make the company responsible to the innocent third parties. The transaction was ultra vires but the innocent third may consider the company continuously having the power. If the transaction was rendered null and void on account of ultra vires, the principal company may be jointed in a suit for compensation. [57]

Though the strict application of the doctrine of constructive notice makes it practically ineffective, appearance of authority can be created by conduct of principal.[58] For example, if the board of directors or a top-level manager or managing director of the company keeps silent when a person representing the company acts beyond the scope of his/her power which is also beyond the power of the company, an innocent third party may assume as if the company had power to conclude an ultra vires contract. In respect of ultra vires transactions, appearance of authority by conduct is arguable but it is still possible. Appearance of authority cannot make the company liable because exact legal power of the company are registered and

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55 If the principal is a physical person this rule undoubtedly works but in case of juridcal persons this rule may promt an issue regarding the person who may inform third parties. As an artificial person the compnany cannot inform its powers. It should be the represenative of the company. Managers of company are assumed having full power regarding acts of management. (Art. 33 of the Com. Code of 1960) If the managing director or chairman of board of directors inform thrid partie the limits of the power of the company, any change in actual power shall be informed, otherwise, innocent third paries can invoke appearnce of authority. A related question is whetehr oral communication of the power of the company suffices for appearnce of authority. As Art. 2195 does not make distinction in this, it appears possible to apply the rule if the informant is authorized to make such statement.

56 Authentication and Registration of Documents, Proc. No. 922/2015 , *Fed. Neg. Gaz.* 22nd Year No. 39, Feb. 2016, A.A., Art. 9(1).

57 *Id*, Sub-art. a.

58 *Id*, Sub-art. c.

assumed known. The conduct of the company officials has no power to override the effects of doctrine notice (actual or presumed). Appearance of authority may also be created if the company had furnished document to the agent regarding the limits of power on the basis of the power of the company and later changed the purpose clause of the memorandum of association by amendment which was registered and deposited, but the agent acts on the basis of altered power, the company is responsible for its failure to change the written power of agency.[59] If the purpose on the basis of which the agent was authorized is changed through amendment that was validly registered and minutes of the meeting that had amended the purpose was registered accordingly, the representation conducted on the basis of the lapsed purpose and lapse power is ultra vires. The company can possibly invoke the doctrine of ultra vires, the innocent third party can invoke the doctrine of appearance of authority and fault on the part of the company by allowing the agent to continue representation with a lapsed power. In this case, the unauthorized agent is responsible to the third party, but the law allows joinder of the apparent principal. Thus, the company may be forced to compensate the third party even if the transaction is ultra vires. 1)

When an unpermitted venture is permitted or unremunerated purposes is included in the list of purposes clause through amendment, the venture falls within the legitimate power of the company. Owing to the nature of the company, or otherwise due to public policy measures, inclusion in the purpose clause by itself cannot legalize operation of the activity. In this case, the regulatory agency may not accept the amendment. But where the amendment is within the bounds of law, the company can run any form of venture by presenting the amended memorandum of association to the attention of the regulatory agency (the Ministry of Trade and Industry or regional offices or other pertinent offices, like National Bank of Ethiopia, where memorandum of association of banks is amended). The amendment has to comply with the legal and procedures requirements of the Commercial Code.

VI. Conclusion

A company is expected to operate its business within the confines of predetermined ventures. The activities that the company may engage in or transactions it may execute are normally listed down in the purpose clause of the memorandum of association. The enumerated

[59] *Id*, Sub-art. b.

purposes are viewed legally permitted when the memorandum of association is registered and business license is granted. It is generally believed that the company is powerless to engage in an activity that is not enumerated in the purpose clause of the memorandum of association. Any activity that exceeds the power of the company is ultra vires. The Commercial Code of 2021 or its predecessor kept silent regarding the recognition of the doctrine of corporate ultra vires or its effects. The legislative silence however cannot usher Ethiopian company lawyers to take the silence as non-recognition of the rule of ultra vires. To allow a company exercise unlimited power appears inherently wrong. Thus, though the doctrine of ultra vires is not expressed in the Ethiopian Commercial Code, the requirement that company cannot engage in an activity that is not expressed in the purpose clause of the memorandum of association implies that exceeding the legitimate power or engaging in an unenumerated activity is ultra vires. Companies being artificial creations generally enjoy predetermined powers. The limits of powers of Ethiopian companies are required to be expressed in the purpose clause of memorandum of association. The company is required to carry out only the activities that are expressed or with necessary precaution implied from the nature of business. It is often viewed that the company got permitted to carry out activities for which it is licensed by the regulatory agency. This is line with Article 25 of the Commercial Code of 2021, which obligates companies to engage in only permitted ventures. The prohibition of operating an unpermitted business is a legislative dictate, while the need to confine to the powers enumerated in the memorandum of association is a corporate duty. If a purpose is enumerated in the purpose clause of the memorandum of association and the memorandum of association is registered in accordance with the requirements of business registration and licensing proclamation, it is generally assumed that the company is permitted to engage in anyone or more of the purposes expressed in the memorandum of association. Conversely thus unremunerated venture is unpermitted venture that the regulatory agency is not aware of it. By implication thus if engaging in non-enumerated business is ultra vires, the same goes to operation of unpermitted business or transaction. Hence, though not expressly stated in the Commercial Code of Ethiopia, it is possible to invoke doctrine of ultra vires through purposive construction.

Traditionally companies are expected to act within the defined contours of business activity, but the confinement backfired to incorporators by restraining the company not to engage in profitable ventures. The restriction not to go beyond the delineated ventures affected not only the very people who designed the company but also national economy and corporate clients.

This called for judicial and legislative intervention. Consequently, numerous changes have been made. In some jurisdictions, companies are permitted to carry out any legal business activity; while, others provide flexibility approach that extended the power of board of directors. The doctrine of ultra vires is not however dead in all advanced system. In some jurisdictions the doctrine is still alive, and can be enforced but it has been considerably deteriorating.

The changing global situation indicates that the doctrine of ultra vires in its traditional sense is outdated and prejudicial to the interest of corporate clients and the national economy. Ethiopian companies also should be permitted to carryout whatever legally possible ventures upon their choice without the need to amend the purpose clause of memorandum of association. The business license should be designed in a way Ethiopian companies can flexibly operate profitable business. Further, innocent third parties should be protected from harsh effects of the doctrine of constructive notice. Thus, unless bad faith is proven against corporate clients, mere failure to get awareness of the content of registered documents, should not a basis for liability.