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Ultra vires

Elmer D. Hays

ULTRA VIRES

By Elmer D. Hays.

The phrase "Ultra Vires" as used in this thesis means any act which the corporation is not authorized to do, either by its expressed or its implied powers. Much confusion has arisen in the application and use of this term. Some writers have used it to mean acts not only beyond the expressed and implied powers of the corporation as given in the charter, but also acts which are contrary to public policy, and are void whether done by individuals or corporations. Such acts are now called "illegal acts" when they are done by corporations and such "illegal acts" are not included in ultra vires as now used.

This term "ultra vires" has also been applied to those acts which are beyond the power of the directors, but within the power of a majority of the stockholders. This confusion in the meaning of the term has caused a great deal of trouble and worry to the courts and has been a most unfortunate thing in the development of the branch of the law on this subject.

The proper use of the term is the rule stated at the first of this article and which definition is also found in Cook's work on corporations. (Vol. 2, p. 1989.)

There are two rules laid down by the courts in this country on the doctrine of "ultra vires." One is the Federal Court rule, or the strict rule, and the other is the State Courts rule, or the rule of estopped. The Federal Court rule has the soundness of logical reason on its side, but it cannot always be said to have justice. Especially does this seem to be true when innocent third parties become involved.

The strict rule is: A contract of a corporation which is either unatuhorized by, or in violation of, its charter, or governing statutes, or which is entirely outside of the scope of the powers of its creation, is void in the sense of being no contract at all, because of the lack of power in the corporation to enter into it; that such a contract cannot be enforced by any kind of action in a court of justice; that being void ab initio, it cannot be made good by ratification, or by any renewals, and that no performance on either side can give validity to it so as to give a party to the contract any right of action upon it.

Under this rule no action can be maintained on such a contract, although there has been part performance, or expenses incurred, on the faith of the ultra vires promise.

Most of the cases decided by the Federal Courts and the Supreme Court of the United States follow this rule. The following cases will affirm these statements. Pittsburg, etc., R. Co. v. Keokuk, etc., Bridge Co. 131 U. S. 371, 33 L, ed. 157, 9 Sup. et. 770, Day v. Spiral Springs Buggy Co., 57 Mich. 146, 23 N. W. 628, 58 Am. 352. Central Transp. Vo. v. Pullman Palace Car Co. 139 U. S. 24. 35 L. ed 55. 11 Sup. et. 478

The reasons upon which the courts rests their opinions in the application of this strict rule are: That the stockholders be protected; that everyone is supposed to know the law; that the corporation shall not transcend the power granted by the state and that the public must be protected. Where the acts are plainly and openly beyond the powers these rules are good ones, but where the acts are of on extrinsic nature of which the party had no notice then justice demands the innocent third party be protected in some way.

In the case of the Central Transportation Co. v. the Pullman Car Co. we have a fine illustration of the effect of the strict rule. In this case the Central Transportation Co. sold all of its cars and fixtures to the Pullman Palace Car Co. for and in consideration of a certain amount of money to be paid each year as a royalty. After the use of the cars for two years the Pullman Palace Car Co. refused to pay the royalty. The court held that this contract could not be enforced because it was ultra vires. As a result we have to-day the greatest monopoly in the railroad business. The Central Transportation Co. because it could not re-stock with fixtures had to go out of business and the Pullman Car people received all of the benefits and became a great monopoly.

We might say that this has given rise to the more liberal doctrine or the State Courts Rule. The strict rule may have been reasonable at the beginning, but in the last few years the field of corporations has taken the most important position in our business world. Since the field has had such a large development the best rule seems to be that of estopped. Moreover, the strict rule seems to have been originallly applied to quasi public corporations and not to private corporations.

The state courts enforce the rule that the law which gives a corporation the power to act as a corporation is of necessitv required to hold them to all their obligations and in this way make justice and right the measure of all corporate as well as individual actions. When I say State Courts I mean also Kentucky Courts for this is the rule as laid down in our State to-day. If the parties have reached such a position as that it would be inequitable and unjust to allow the plea of "ultra vires," the doctrine of estoppel will be applied so as to prohibit the party who wishes to make this his defense from so doing. Where the contract is executory on both sides, or executed on both sides, the courts both state and federal, will leave the parties just as it found them.

The following cases will illustrate the state courts rule set out above:

Whitney, etc. Co. v. Barlow, 63 N. Y. 62, 20 Am. 504. Kadish v. Garden City, etc., Bldg. Assn. 151 Ill. 531, 38 N. E. 336, 42 Am. St. 256. Union Pacific R. Co. v. Chicago, etc. R. Co. 163 U. S. 564, 604, 41 L. ed 265. Holmes, etc., Mfg. Co. v. Homes, etc. Metal Co. 127 N. Y. 252, 27 N. E. 831, 24 Am. St. 448. Parris v. Wheeler 22 N. Y. 494. Manchester, etc., Co. v. Concord, etc., R. Co., 66 N. H. 100, 20 At. 383, 49 Am. St. 582, 9 L. R. S. 689. Wright v. Highes 119 Ind. 324, 21 N. E. 907. Dewey v. Toledo, etc., R. C., 91 Mich. 351, 51 N. W. 1063.

A suit for the specific performance of an ultra vires contract cannot be maintained in any court. This rule is without a single exception. Where there has been a part performance of the contract and a suit is brought to compell the completion of a material part of the contract the

courts will not hear such a cause. For to do so would be to give a void contract life after an immaterial part has been executed. The courts and the law of the land makes it the duty of the corporation to rescind the ultra vires contract at the earliest possible moment, and when a corporation does rescind the contract it is the duty of the court to uphold the corporation and to leave the other party to get relief in an action for damages or the recovery of the property already given as a consideration.

The state is the only one who can raise the question of ultra vires against a corporation. It is the duty of the officers of the state to proceed against a corporation by and warrants if the terms of the charter have been violated.

If the party wishes to avail himself of the plea of estappel he cannot do so unless he surrenders the benefits which he has received from the contract. No state court will allow one to enter this plea and at the same time retain all of the benefits which he would receive from the contract.

There is another distinction between "Ultra Vires" contracts which it might be well to notice. Contracts which are malum in se and malum prohibitum.

Not much can be said of contracts of this first class. A contract which is malum in se, that is, the illegality adheres to the contract itself, can never be enforced in any court.

Contracts which are malum prohibitum are those agreements which the state by statute has made illegal. In these contracts there is nothing illegal which address to the contract itself, but they are illegal because, of and by reason of, the statute. An act which has however been made illegal may be enforced upon certain grounds. As a general rule where the statute makes the act illegal, and an action is brought on this contract, because of the illegal basis it will not be enforced, unless it can be shown that the real purpose of the act is not to declare the contract void but to punish if the act is committed. In other words if the statute states what the punishment shall be; or if the prohibition was imposed for a certain class or to adjudge the contract void would clearly defeat the purpose of the statute then the courts will proceed to sit in judgment on the merits of the particular case. A great number of the cases have involved the last principal and this seem to be the rule under which most of the last class of cases have arisen.

This is a statement of what have now become the fixed and settled rules on the points discussed in this paper.