Companies’ Power to Borrow at Common Law and Under Section 191 of the Nigerian Companies Act 2020: Identifying the Red Line

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Abstract
In contemporary times, the necessity of adequate capital and its relative scarcity invariably impel companies to source for funds through borrowing. At common law, the power of the company to borrow is implied, and it must be exercised in strict compliance with its business and in furtherance of such business as clearly stated in its memorandum of association, otherwise the power would be *ultra vires*, void and of no legal effect. Section 191 of the latest Nigerian Companies and Allied Matters Act 2020 (Companies Act) expressly provides for the power of the company to borrow money, mortgage or charge its property and issue securities for the purpose of its business. The company may borrow any amount of money and expend it on any business that is not even stated in its memorandum. The germane issue which this article examines is the nature and extent of companies’ powers to borrow at common law and under the provision of section 191 of the Companies Act. Quite unlike the common law position, this article finds that under the Companies Act *ultra vires* borrowing by the company is not void or invalid. But the implication of this finding does not imply that the company’s express power to borrow is absolute, inviolable, and free of legal guard rails. Significant, this article identifies the line in the Companies Act beyond which the provision of section 191 of the Companies Act is breached, including the consequences and the remedies that flow from such breach.

Keywords: Nigerian Companies Act, section 191, companies’ borrowing, Companies’ securities, *ultra vires* doctrine, loan contract

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1. Introduction
Companies are registered or incorporated with the object of carrying on business ventures for the main purpose of making profits for distribution to members and shareholders⁴. Prior to incorporation and commencement of business, the promoters of a company strive to raise adequate capital for the company’s business undertaking through such means as offering shares subscription, or concluding loan or joint venture agreements. Adequate capital is also necessary for a newly incorporated company to be able to secure office apartment or business space, obtain supply of goods and services, including service contract for essential officers. Even a company that is already a going concern may need more capital to procure new operational facilities, or even to expand its scope of business or services.

The necessity of business capital and its relative scarcity invariably impel companies to source for funds through borrowing money or issuing debentures or debenture stock as security for a debt. Determining the borrowing power of a company has become more instructive in light of many cases in Nigeria where companies take loans from financial institutions without paying back as and when due, while in some cases the loans are declared as bad debts. For instance, the high rate of loan default by most companies and its erosion of banks’ liquidity and depositors’ funds necessitated the establishment of the Asset Management Corporation of Nigeria (AMCON)². While the establishment of the AMCON is commendable, there is however a need to ensure working knowledge of the nature and limits of the borrowing power of companies in order to prevent cases of wrongful or abusive exercise of such power and its potential adverse economic consequences.

At common law, the power of an incorporated company to borrow money or issue securities is implied and incidental, unless expressly prohibited by its charter or memorandum of association which defines the company’s status, business or objects, and powers³. Through the memorandum third parties and the public at large are able to clearly ascertain the permissible scope of business undertaking of the company and its powers to enter business and legal relationships⁴. For the purpose of achieving its business or objects the company must

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¹ The only exception are companies limited by guarantee. According to section 26(3) of the Nigerian Companies Act 2020: ‘A company limited by guarantee shall not be incorporated with the object of carrying on business for the purpose of making profits for distribution to members.
² The broad mandate of the AMCON is to assume the Non-Performing Loans (NPLs) in the banking system and inject fresh funds into the financial institution thereby ameliorating the economic consequences of NPLs for Nigeria. See Ikobi-Anyali, AL, (2020). “Managing Non-Performing Loans in Nigeria: An Appraisal of the Asset Management Corporation of Nigeria (AMCON)” 7(1) Nnamdi Azikiwe University Journal of Commercial and Property Law 27-41
³ Orojo, JO, *Company Law and Practice in Nigeria* (5th Ed, Lagos: Lexis Nexis, 2008) p. 55
⁴ In contradistinction, the articles of association of an incorporated company contain the internal rules and regulations of the company, including issues relating to the internal management and administration of the company.
exercise the power as conferred on it or not prohibited by the memorandum. This also applies to the power of a company to borrow money for the benefit of the company’s business as such power must be exercised in strict compliance with the relevant clauses of the memorandum. If the power is abused or exercised wrongfully, or in a manner contrary to the stipulations in the memorandum the borrowing or any security given for the debt would be _ultra vires_ the company, that is, “beyond the power” of the company1.

Under the latest Nigerian Companies Act 2020 (the Companies Act) every incorporated company, for the furtherance of its business or objects, is conferred with all the powers of a natural person of full capacity2. However, the borrowing power of companies is not implied or incidental to its human capacity but expressly provided in section 191 of the Companies Act. Pursuant to the provisions of the section, a company may borrow money for the purpose of its business and may mortgage or charge its property and issue debentures, debenture stock and other securities for any debt. But the Companies Act also provides that a company must not exceed the powers conferred upon it by its memorandum of association or the Act3.

Thus, both at common law and under the Companies Act the power of a company to borrow money in furtherance of its business or objects is duly recognized, though such power is not absolute as it must be exercised within the confines of the company’s memorandum of association and the provisions of the Companies Act respectively. The germane issue which this article examines is the nature and extent of companies’ power to borrow at common law and under section 191 of the Companies Act. Significantly, this article identifies the line in the Companies Act beyond which the provision of section 191 of the Companies Act is breached, including the consequences and the remedies that flow from such breach.

2. **Companies Power to Borrow under Common Law**

At common law, every company that is involved in trade and commerce has an implied power to borrow money for the purpose of its business, and to give security for the loan by creating a mortgage or charge on its property even where such power is not expressly stipulated in the company’s charter or memorandum of association. This implied power of a company was recognized long ago in the case of _General Auction Estate and Monetary Co. v Smith_4 in which the charter of the company did not expressly give it any power to borrow money. The company however borrowed money from one of its directors on the security of its property to pay off depositors and creditors. Upon liquidation of the company, the liquidator sought to set aside the security as the borrowing was outside the express powers of the company. But the court held that as a trading company, the company had an implied power to borrow money for its business and to give security for such debt.

However, under common law every registered company is expected to carry on its business or objects as expressly stated in the charter or statute under which it is established as a corporate entity and conferred with necessary powers towards achieving the business or objects of its existence. Where the company engages in any business or transaction outside its objects clause it is deemed to have acted _ultra vires_ or beyond its legal powers, with the consequence that such business or transaction is void. The common law _ultra vires_ doctrine is thus applied where a company acts beyond its business or objects as set out in its charter or where it acts in a way prohibited by statute.

The applicability and consequences of the _ultra vires_ doctrine were clearly encapsulated in the case of _Ashbury Railway Carriage & Iron Co. v Riche_5 where a British company entered into a contract for the financing of the construction of a railway line in Belgium. The objects of the company had been, amongst others, to make and sell, or lend on hire railway carriages and wagons and all kinds of railway plant, and to carry on the business of mechanical engineers and general contractors within Britain. In deciding whether the company was bound by the contract, the House of Lords held that the contract to finance the construction of a railway line in Belgium was outside the scope of the objects of the company and as such the contract was _ultra vires_ the company, and therefore not binding.

The case of _Ashbury Railway Carriage & Iron Co. v Riche_ therefore laid down the rule that _ultra vires_ exercise of power by a company is void _ab initio_ and cannot even be validated or ratified by the unanimous assent of all the members of the company in a general meeting; ratification is possible only where the board of directors exceeded their power in concluding a contract or transaction that is within the object clause of the company, and not otherwise. The _ultra vires_ doctrine applies with equal ramifications when a company exercises its power to borrow money in furtherance of its business or objects. Where the power to borrow is implied in the general capacity of a trading company, the exercise of that power must be in furtherance of the permissible business or objects of the company. This means that any money borrowed by the company, with or without

1 Alili, N. (2009). “Ultra Vires Doctrine under the Nigerian Company Law” 2(1) Confluence Journal of Private and Property Law, 181
2 See section 43(1) of the Nigerian Companies and Allied Matters Act 2020. In this article, the Act is referred to as the Companies Act. Reference to any other Companies Act is clearly identified.
3 See section 44(1) of the Companies Act
4 (1891) 3 Ch. 42
5 (1875) L.R. 7 HL
security, must be for the purpose of the company’s business as stated in its objects clause.

The charter or constitution of a company may also expressly provide for the borrowing power of a company. If the power to borrow is so expressly stated in the company’s charter or memorandum of association, the company must not exceed the total sum expressly stated, or exercise such power in any manner contrary to the express stipulations in its objects clause. Therefore, if the company exercised its implied power to borrow outside its business or objects, or failed to comply with its express power to borrow, any transaction or contract to borrow money would be void and invalid. So also any security given for such borrowing would not be binding or enforceable against the company since such transaction or contract is ultra vires the company.

As Lord Cairns held in Ashbury Railway Carriage & Iron Co. v. Riche, it needs to be pointed out that the doctrine of ultra vires may apply to cases where the directors of the company exceeded the powers delegated to them in the management of the company. But the difference between the ultra vires powers of the company and its directors is that unless the company’s own power is exceeded by the directors, the ultra vires doctrine does not necessarily apply. The company retains the power to ratify its directors’ ultra vires acts if they acted within the business or objects of the company and for the benefit of the company, though they may have acted outside their authority as conferred on them by the company’s article of association. As discussed in the next section below, this distinction is important as it has significant legal implications when examining the express power of companies to borrow, and in determining the consequences where the exercise of such power is ultra vires the company.

2.1 Borrowing power ultra vires the company

As noted in the preceding section, the company’s power to borrow under common law, whether express or implied, is subject to the ultra vires doctrine which requires the company not to exceed its powers, otherwise the transaction would be void and of no effect. It follows, therefore, that where a company borrows money in excess of its borrowing power, the borrowing would be ultra vires the company. This position of common law on the ultra vires power of a company to borrow was clearly stated in the early 19th century case of Sinclair v Brougham, decided about two decades after Ashbury Railway Carriage & Iron Co. v. Riche. In the case, the House of Lords determined one of the three fundamental issues relating to companies’ power to borrow, to wit, when the power to borrow, whether express or implied, is ultra vires the company.

In Sinclair v Brougham, a Building Society established under a statute had the object of bringing together those willing to lend and those wishing to borrow money for the building of houses. The company was thus empowered to borrow money from members or shareholders for its purposes as a building society. But eventually, the company’s business extended into receiving deposits from non-members. When the company fell on hard times and was under liquidation, Viscount Haldane LC held that the power to receive deposits from the public and non-members of the company was ultra vires the company. Therefore, depositors were not entitled to recover their money under the ultra vires loan contracts. The implication of this decision has since then been that a lender to the company under an ultra vires loan contract cannot sue the company to recover the loan, and any security given for such loan is void and of no legal effect.

This is abundantly exemplified by the later case of Re Introduction Ltd in which the company business involved rendering entertainment services to foreign visitors at a seaside port. Eventually, a transfer of shares in the company led to the constitution of a new board of directors which decided that the company would be engaged in the breeding of pigs. When the company’s account was heavily overdrawn the bank demanded security and the company offered the bank two debentures secured in the company’s assets. Subsequently, the company went under, and this action turned on the issue whether the securities held by the bank were legally valid against the company. It was held that the business of pig-breeding for which the company borrowed the money was ultra vires the company hence the securities issued for that purpose were void and invalid.

Re Introduction Ltd, more than the case of Sinclair v Brougham, succinctly determined that the company’s power to borrow is subject to the business or object of the company. For instance, it was argued by the bank that since the company’s memorandum of association expressly authorized the company to borrow money and issue securities for debt, it did not matter to what business the company put the borrowed money. Rejecting this

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1 See the case of T.R. Pratt (Bom) Ltd v. E.D. Sassoon and Co. Ltd (1936) 6 Com Cases 90. In the case, there was no express limit on the borrowing power of the company while the directors could not borrow beyond the limit of the issued share capital of the company, unless with approval by the general meeting. When the directors borrowed money from the plaintiff beyond their powers the borrowing was held not to be ultra vires the company since the company has the power to ratify same.

2 [1914] AC 398

3 The other two are: determining whether the business for which the company borrowed the money was within the powers of the company and; determining when the power to borrow exercised by company directors is ultra vires the company. These are discussed below.

4 (1969) 1 All. E.R. 887

5 A sub-clause of the company’s memorandum of association had authorized the company; “To borrow or raise money in such manner as the Company shall think fit and in particular by the issue of debentures or debenture stock perpetual or otherwise and to secure the repayment of any money borrowed or raised by mortgage charge or lien upon the undertaking and the whole or any part of the company’s property or
argument, Harman L.J held that it is necessarily an implied addition to the power to borrow, express or implied, that the lender should obtain knowledge as to the purpose for which the company was borrowing the money. And since the borrowing by the company was not for its business stated in its memorandum, the bank could not hold the debentures against the company. This case therefore made it clear that unless the objects clause in the company’s memorandum is satisfied, companies’ power to borrow and issue securities may become ultra vires the company even where the company is expressly so empowered.

The nullity of ultra vires loan contracts and the consequential evasion of liability by the company is strengthened by the common law rule of constructive notice which considers the company’s memorandum and article of association as public documents. The implication of this rule is that lenders and other third parties contracting with the company are assumed to have a fore-knowledge of the company’s business and powers as contained in those documents. In the Re Introduction Ltd case, the rule of constructive notice defeated the argument of the bank that having known of the company’s express power to borrow, it was under the impression that the borrowing would be for the business of the company. From the decision in the case, knowledge of the express power of the company to borrow does not suffice. The lender needs to be fully aware whether the borrowing is in fact for the business or object of the company as spelt out in the company’s memorandum.

The rule of constructive notice is also applied in the determination as to whether or not the power to borrow is ultra vires the company when such power is exercised by a managing director or board of directors of the company. From the cases, if the borrowing is within the power of the company but outside the authority of the directors the borrowing is voidable and the company can dodge liability. But the company may decide to ratify the unauthorized borrowing since it is within its own borrowing power, in which case it would become liable for it. The right of the company to avoid liability is borne out of the rule of constructive notice which deems the lender as having notice of the extent or absence of the borrowing power of the directors in the company’s articles of association. Consequently, any unauthorized borrowing by directors is at best ratifiable, otherwise it is voidable and ultra vires the company. The only possible exception is where the unauthorized borrowing is evidently applied to the business benefit of the company.

2.2 Remedies for companies’ ultra vires borrowing

From the foregoing discourse, the common law power of companies to borrow is inevitably subject to the ultra vires doctrine which has been described as “an illusory protection for the shareholders and a pitfall for third parties dealing with the company”13. This is rightly so in the opinion of this author since any transaction that is ultra vires the company is non-enforceable by a third party as well as by the company. In terms of the borrowing power of companies, it is difficult how a lender is able to ensure that the borrowed money is actually put into the stated business or objects of the company. Therefore, the effect of the doctrine does not only jeopardize the interest of the lending party to an ultra vires loan contract, it also constitutes huge business risk and loss of investments for shareholders where the company is short-changed or defrauded under such contract. It creates a strong disincentive to lenders and potential investors in the company’s securities, especially in situations where the company is in dire need of funds to stay afloat, break even, and remain viable as a going concern.

It has to be pointed out that there are some remedies for the injured party in ultra vires borrowing by the company. Since ultra vires borrowing is void ab initio and cannot even be ratified by a unanimous resolution of the company’s members in general meeting5, the remedies exist only to provide equitable relief against total loss of money by the lender. For instance, one remedy is that if there is evidence that the borrowed money has not been spent the lender may obtain an injunctive order to restrain the company from parting or dissipating the money. The lender may also apply for a declaratory order for the company to hold the money in trust, thereby creating a trustee/beneficiary relationship between the company and the lender. Where the ultra vires borrowing has already been used to settle the company’s existing debt, the lender’s remedy may lie in an order to take the place of the discharged creditor under the principle of subrogation; the company’s debt remains the same and there is a mere replacement of one debt by another of the same amount5.

However, the principle of subrogation does not entitle the lender to any security held by the original

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1 See the common law foundational cases of Re Wrexham Mold C. Ltd (1899) 1 Ch. 440; T.R Pratt. (Bom) Ltd v E.D. Sassoon and Co. Ltd (1936) 6 Com Cases 90; Equity Insurance Co. Ltd v Dinshaw & Co. AIR 1940 Oudh 202; Lakshmi Ratan Cotton Mills Co. Ltd v J.K Jute Mills Co. Ltd (1957) 27 Com Cases 660; AIR 1957 All 311; V.K.R.S.T.Firm v Oriental Investment Trust Ltd AIR 1944 Mad 532.
2 See the case of Equity Insurance Co. Ltd v. Dinshaw & Co., AIR 1940 Oudh 202 decided in colonial India under the common law jurisdiction of Britain. It was held in the case that; “Where the managing agent of a company who is not authorised to borrow has borrowed money which is not necessary, neither bona fide, nor for the benefit of the company, the company is not liable for the amount borrowed.”
3 The Cohen Committee Report on the Company Law Amendment, Cmd. 6659, 9 12 (1945), para 12. As far back as 1945, the Committee recommended the abolition of the ultra vires doctrine for these reasons.
4 See Lord Cairns holding in Ashbury Railway Carriage & Iron Co. v Riche (1875) L.R. 7 HL
5 See Re Wrexham Mold C. Ltd (1899) 1 Ch. 440; Orakpo v Manson Investments Ltd (1977) 3 W.L.R. 22
creditor or to any priority that the original creditor may have had over other creditors of the company. There is the remedy for the lender to *ultra vires* borrowing by the company to retain any securities given by the company for the borrowed money. Depending on the market value of the securities, the lender may be able to recoup part or equal amount of the borrowed money. The equitable remedy of tracing may also avail the lender if the money borrowed by the company can be traced in the possession of the company in its original form, or in a particular property of the company acquired with the borrowed money. But where the money has become mixed up with that of the company and can no longer be traced, the lender may be entitled to claim a parri passu distribution of the company’s assets with the shareholders, especially when the company is undergoing a winding up process.

With respect to borrowing that is within the power of the company but contracted by directors without authority, the lender’s situation may be remedied if the company decides to ratify the borrowing. If not, the lender would be hard put to contend that the borrowing is not *ultra vires* the company based on the common law indoor management rule. The rule, derived from the case of *Royal British Bank v Turquand*, implies that the company cannot employ, as a defence against the unauthorized borrowing, the failure of the directors to comply with the internal rules and regulations of the company which could have prevented the unauthorized borrowing. But if this contention is defeated by the rule of constructive notice, the lender may hold the directors personally liable for the *ultra vires* borrowing. The lender may therefore claim damages against the directors for breach of the implied warranty of authority to borrow on behalf the company.

The old case of *Firbanks Executors v Humphereys* remains apposite to the lender’s remedy of damages against directors’ personal liability for unauthorized borrowing that is *ultra vires* the company. In the case, it was agreed that a worker was to be compensated with the company’s debentures for the construction work executed for the company. But all the debentures which the directors were authorized to issue had already been issued and the company had no assets to satisfy the worker’s claim on the debentures over-issued by the directors without authority. While holding that the over-issuing of the debentures by the directors was *ultra vires* the company and void, the court ruled that the directors were personally liable for breach of the implied warranty of authority. The directors were therefore ordered to pay the worker the par value of the debentures he ought to have received. It must be reiterated that the available remedies for a lending party to *ultra vires* loan contract with the company are only potentially equitable reliefs that do not guarantee the potency and certainty which the common law *ultra vires* doctrine commands.

Therefore, the far-reaching effect of the *ultra vires* doctrine on companies’ power to borrow under common law remains. The “incoherent logic of *ultra vires* doctrine and its ghostly relics” have led to statutory modifications of the doctrine in Companies acts in most common law jurisdictions like Nigeria. As discussed in subsequent sections, companies’ power to borrow and its nugatory rules under common law have been largely modified in the Companies Act due to the unsatisfactory nature of the available remedies and the imperatives of modern business undertakings. For example, the Companies Act has abolished the rule of constructive notice, and made the objects clause in companies’ memorandum of association to be unrestricted in scope. The next section examines how these and other provisions of the Companies Act have amended the common law companies’ power to borrow, the effect of *ultra vires* borrowing by the company, and the remedies for borrowing that is *ultra vires* the company.

### 3. Companies’ Power to Borrow under the Companies Act

It is instructive to point out that prior to the enactment of the Companies Act the common law position on companies’ power to borrow and the effect of the case of *Ashbury Railway Carriage & Iron Co. v Riche* applied in Nigeria to a full extent. For example, in *Metalimpex v Leventis & Co. Nigeria Ltd* the court held that where the power to enter into a contract is *ultra vires* the company such contract cannot be enforced by both the company and the other party to the contract. In *Okoya v Santilli* it was held that if the company acted and exercised power outside its memorandum of association it would be *ultra vires* the company. Both cases followed the precedence set by the Nigerian Supreme Court in *Continental Chemist v Ifeakandu* where the apex court fully adopted the common law position by affirming that any contract the company made outside its

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1. See the judgment of Lord Diplock in *Orakpo v. Manso Investments*, ibid, at p. 32
2. *In Sinclair v Brougham* (1914) A.C. 398
3. *In Ashbury v Riche* (1914)
4. *In Metalimpex v Leventis & Co. Nigeria Ltd*
5. *In Continental Chemist v Ifeakandu*
6. *In *Okoya v Santilli**
7. *In *L.C.B. Gower, The Principles of Modern Company Law* (Paul L. Davies ed., 6th ed. 1997) p. 233
8. See section 92
9. See section 35(1)
10. See section 35(1)
objects as stated in its memorandum is *ultra vires* the company, and therefore invalid and unenforceable\(^1\).

One way the Companies Act has modified the *ultra vires* doctrine is that all the types of business and objects which the company may lawfully undertake need not be expressly stated in the company’s memorandum. The Companies Act provides that “unless a company’s articles specifically restrict the objects of the company, its objects are unrestricted”\(^2\). Instead of expressly stating the business and objects of the company as required under common law, the Companies Act empowers the company to engage in any business provided such business is not specifically prohibited in the company’s memorandum. Accordingly, section 44(1) provides that a company shall not carry on any business expressly prohibited by its memorandum and shall not exceed the powers conferred upon it by its memorandum or the Companies Act. With particular respect to companies’ power to borrow, it is provided in section 191 thus;

A company may borrow money for the purpose of its business or objects and may mortgage or charge its undertaking, property and uncalled capital, or any part thereof, and issue debentures, debenture stock and other securities whether outright or as security for any debt, liability or obligation of the company or of any third party.

From the above provision, it is clear that the Companies Act gives express power to companies to borrow money, to charge property and to issue debentures. There is no provision in the Companies Act that constrains or imposes any conditions on the power of companies to borrow. The provision of section 191 simply requires the borrowing to be for the business or objects of the company. And since the business a company may undertake is open-ended, by virtue of section 35(1), the implication of the provision of section 191 is that the company may borrow any sum of money and for whatever business purposes it deems fit. But it has to be examined whether if the company’s power to borrow is untrammelled by the provisions of the Companies Act, can the company exceed its borrowing power, and if it does, would it be caught by the *ultra vires* doctrine?

### 3.1 Companies’ power to borrow and ultra vires doctrine under the companies act

As has been noted in the preceding sections of this article, the common law position on companies’ power to borrow is that the *ultra vires* doctrine curtailed the borrowing power of companies and rendered *ultra vires* loan contracts or transactions void and of no legal effect. The memorandum of association of companies determined when and to what extent the doctrine would apply: if borrowing power is exercised outside or contrary to the objects clause in the companies’ memorandum, it is *ultra vires* the company; if it is exercised by directors without authority, it is voidable at the instance of the company. In comparison, the provision of the Companies Act is that the company cannot carry on any business that is “expressly prohibited” by its memorandum, and must not exceed the powers conferred upon it by its memorandum or the Act itself\(^3\).

Consequently, where there is no prohibition of any specific business, or the company steers clear from the prohibited business, in its memorandum then the company would not exceed its power as conferred on it by its memorandum. The Companies Act does not provide for any way in which the company may exceed its power to borrow under the Act. But one scenario in which the company may possibly act beyond its power to borrow as provided in section 191 is when the borrowed money is applied to any business specifically prohibited in its memorandum. While the Companies Act does not expressly provide for the *ultra vires* doctrine to apply in the event that the company engages in a prohibited business or exceeds its power to borrow, it is submitted that the Act actually avoids the applicability of the *ultra vires* doctrine.

Going by the Companies Act’s marginal title for section 44 as, “Effect of *ultra vires* acts”, it does not appear that the legal effect on the company for acting beyond its power to borrow may be a nullity of the borrowing or loan contract. According to the Companies Act, if the company engages in a prohibited business or exceeds its borrowing power such breach may only be asserted in any proceeding of personal and representative action, including during investigation of the company either upon its own application or that of its members\(^4\). The Companies Act empowers any member of the company or the holder of any debenture secured by a floating charge over the company’s property, or by the trustee of the holders of any such debentures, to apply to the court for an order of injunction to prohibit the doing of any act, conveyance or transfer of any property which would

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\(^1\) This case remains the *locus classicus* on the *ultra vires* doctrine in Nigeria. In the case, the company's memorandum of association stated its object as: “To import and export drugs; To buy and sell drugs; To manufacture drugs; To compound drugs; To enter into any business which the directors think will increase the profit of the company as may be incidental and conducive to the attainment of the above objects and powers of any of them”. The company entered a contract to sponsor the respondent through medical school, and upon becoming a medical doctor, to work for the company for a certain salary and number of years. After becoming a medical doctor their relationship broke down and the company sued for breach of contract. The Supreme Court held the contract unenforceable as it was *ultra vires* the company, being outside the objects of the company as stated in its memorandum.

\(^2\) See section 35(1)

\(^3\) Section 35(1)

\(^4\) Section 44(2); it provides that, “A breach of subsection (1) may be asserted in any proceeding under sections 344 - 358 of this Act or under subsection (4) of this section”.  

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amount to a prohibited business or the company exceeding its power to borrow\(^1\).

But where it is a completed act of the company, the Companies Act provides that no such act, conveyance or transfer of property to or by a company, shall be invalid by reason of the fact that such act, conveyance or transfer was not done or made in furtherance of any of the authorized business of the company, or that the company was otherwise exceeding its objects or powers\(^2\). The unambiguous meaning of this provision is that “\(\text{ultra vires}\)” acts or borrowing by the company is not void or invalid under the Companies Act. This should not imply that the company is immune against any breach of the clauses in its memorandum or the provisions of the Companies Act. The combined effect of the provisions of sections 44 and 191 only saves such breach from nullifying or invalidating the act which manifested the breach\(^3\). This is further evident from the statutory provisions on the effect of restrictions in the company’s memorandum.

From the provisions of the Companies Act, where there is a clause in the company’s memorandum restricting the powers and capacity of the company to carry on its authorized business or object, a breach of the restriction does not invalidate the act or business transaction. For instance, according to section 45 any such breach may only be relied on and have effect only for the purpose of proceedings: (a) against the company by a director, member of the company, or a debentures holder secured by a floating charge or the trustee for the debentures holder; (b) by the company or a member of the company against the present or former officers of the company for failure to observe any such restriction; (c) by the Commission or a member of the company to wind up the company\(^4\); or (d) for the purpose of restraining the company or other person from acting in breach of the memorandum or directing the company or such person to comply with same\(^5\). Thus, breach by the company of its memorandum and the provisions of the Companies Act is not without liability and remedy, but such breach does not, \(\text{ipso facto}\), go directly to void a completed act or transaction of the company the same way the \(\text{ultra vires}\) doctrine apply under common law.

3.2 Liability and remedy for breach of companies’ power to borrow

It can be stated in categorical terms that the power of companies to borrow under the Companies Act is no longer subject to the effect of the common law position; the authority of Ashbury Railway Carriage & Iron Co. v Riche and the \(\text{ultra vires}\) doctrine. This is not to imply, however, that the company’s express power to borrow is absolute, inviolable, and free from all legal constraints. The Companies Act imposes two guard rails: the company’s power to borrow must not be exercised for the purpose of any business or object which is specifically prohibited in the company’s memorandum, and it must not go beyond the scope of the provisions of the Companies Act. This is where the Companies Act draws the line between how the company must exercise its power to borrow, and the consequences of not complying with the statutory provision.

If the company falls off the guard rails by abusing its borrowing power, the Companies Act provides a remedy for parties whose interests are likely to be injured; members and creditors of the company. According to the provisions of the Companies Act, any member of the company or the holder of debentures secured by a floating charge over any of the company’s property may initiate legal proceedings to prohibit or set aside any transaction by the company which constitutes or would constitute abuse of its borrowing power\(^6\). By virtue of the provisions of section 44(5), if the transaction sought to be prohibited in the proceeding is being, or is to be performed or made pursuant to any contract to which the company is a party, the court may, if it deems it to be equitable for all the parties to the contract, set aside and prohibit the performance of such contract.

Section 44(5) provides further that upon setting aside and prohibiting the performance of the contract, the court may allow compensation to the company or to the other parties to the contract for any loss or damage sustained by them by reason of the setting aside or prohibition of the performance of such contract\(^7\). The Companies Act does make the remedy of compensation available to parties, particularly lenders in loan contracts or investors in the company’s securities that may incur loss or suffer any damage due to the setting aside and prohibition of any transaction or contract which may violate the company’s memorandum or the provisions of the Companies Act. Therefore, the company may be held liable to pay compensation to its members and creditors, including debentures holders, if and when it abuses its express power to borrow under the Companies Act.

In addition to the company’s liability for wrongful or abusive use of borrowing power, the Companies Act imposes liability on directors and officers of the company where the company (a) receives money by way of loan

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\(^1\) See section 44(4)

\(^2\) Section 44(3)

\(^3\) And as noted below, there is a remedy and liability for the breach of the company’s memorandum and the provisions of the Companies Act.

\(^4\) The “Commission” means the Corporate Affairs Commission which is responsible for the administration of the Companies Act, including the registration, regulation and supervision of the formation, incorporation, management, striking off and winding up of companies in Nigeria. See section 8(1).

\(^5\) See section 45

\(^6\) See section 44(4) and (5).

\(^7\) But no compensation shall be allowed for loss of anticipated profits to be derived from the performance of such contract. See section 44(5).
for specific purpose; (b) receives money or other property by way of advance payment for the execution of a contract or project; or (c) with intent to defraud, fails to apply the money or other property for the purpose for which it was received. Every director or other officer of the company who is in default is personally liable to the party from whom the money or property was received for a refund of the money or property so received and not applied for the purpose for which it was received1.

This liability of company directors goes beyond directors’ fiduciary duty to avoid conflict of interests and exercise care, diligence and skill which a reasonably prudent director would exercise in the management of the business of the company as provided in sections 306 and 308 of the Companies Act. According to the provisions of these sections, it would constitute a ground for an action for negligence and breach of duty where directors fail to exhibit reasonable care and skill in the conduct of the company’s business; or where their personal interests conflict with any of their duties and as a result make any secret profit or achieve other unnecessary benefits which they fail to account to the company2.

But the provisions of section 316 specifically refer to where the company borrows money by way of loan for a particular business but diverts it to other purpose, or where it receives money or other property by way of advance payment for the execution of a contract or project which it fails to perform. These are instances of where the company borrows money and applies it to a business expressly prohibited in its memorandum, or in violation of the provisions of the Companies Act with respect to restrictions on the power of the company as contained in the Act. In any of these situations and pursuant to the provisions of section 316, there is a presumption of an intent to defraud, and every director of the company who is involved in the transaction is personally liable to refund the money or property so received and diverted, misapplied or embezzled.

4. Conclusion
Companies’ power to borrow as provided in section 191 of the Companies Act is different in nature and ambit than the position under the common law. The power is expressly provided and its exercise is not dislodged in the same way and with the same effect as exemplified by the case of Ashbury Railway Carriage & Iron Co. v Riche. At common law, borrowing by the company that goes beyond its power or for the purpose other than as contained in its memorandum is ultra vires the company and of no legal effect. The borrowing or loan contract can neither be enforced by or against the company, and the available remedies for the lender are only equitable in nature, with a high degree of uncertainty in terms of a favourable outcome.

But quite unlike the effect of the case of Ashbury Railway Carriage & Iron Co. v Riche and its concomitant ultra vires doctrine, under the Companies Act borrowing by the company in breach of its memorandum cannot be void in itself. The company may borrow any amount of money and expend it on any business that is neither stated nor prohibited in its memorandum. This is important for companies of this 21st century when business imperatives require that corporate decisions are based on market trends and not necessarily dictated by the fine prints in the company’s memorandum. The statutory remedies for any loss or fear of loss as a result of such flexible and unilateral business decisions of the company are able to remove any disincentives to lenders and secured creditors of the company.

Consequently, it is permissible for the company to borrow money for a specified business and thereafter apply it for another it decides would best serve its interest and increase its profit. And provided it is in its corporate interest and business profit, the company does not have to look over its shoulders in entering any contract relating to a business or object outside its memorandum, since it can legally enforce such contract when circumstance demands. Significantly, however, just as the Companies Act expressly provides for the company’s power to borrow, it also expressly imposes liability on both the company and its directors for any abusive and wrongful borrowing. This is the red line in companies’ power to borrow as provided in section 191 of the Companies Act.

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1 See section 316
2 See sections 306(2) and 308(2)