This book examines Section 2:7 of the Netherlands Civil Code. Section 2.7 contains a provision entitling a company – under certain circumstances – to nullify an ultra vires transaction with a third party. The study not only includes the history of the law in this area but also compares the legal position of several other European jurisdictions. The study concludes by recommending that the Netherlands legislator introduces unlimited capacity for NV and BV companies vis à vis third parties.

First it analyses the situation in England in chapters 2 through 5. England can be seen as the nursery of the ultra vires doctrine: the theory that a registered company is unable to perform ultra vires transactions. As opposed to the permission granted by the public authority to act as a legal entity with limited liability (concession theory), the contractual capacity of a company was deemed to be limited by the contents of a company’s object clause. In the famous case Ashbury v. Riche (1875) the House of Lords declared the ultra vires rule to be the law. This caused considerable criticism from the business sector, because many believed that the legal security of third parties had been sacrificed to protect company shareholders and creditors. In any event, it led to the custom of very lengthy and extended object clauses in memoranda of association.

The controversy between the judiciary and the business world about ultra vires transactions then focussed on the interpretation rules: when to deem a specific transaction to be within an object clause in a memorandum of association. An important question in extension thereof was whether a transaction conflicting with the (financial) interest of a company should be deemed to be ultra vires. Initially the judiciary did indeed apply this rule for a considerable period. However, since 1970 (Charterbridge Corporation Ltd. v. Lloyds Bank Ltd.) it withdrew from this position and ruled that the (financial) interest of a company should be distinguished from and not mixed up with the subject of ultra vires transactions. Other restrictive interpretation rules remained applicable, including the rule that an ‘independent objects clause’ could not convert something which was intrinsically a power into an object (Introductions Ltd. v. National Provincial Bank 1970).

While the courts were busy with these questions of interpretation, which caused legal uncertainty and resulting criticism from the business world,
legislator entrenched the ultra vires doctrine by a remarkable path. The
European Communities Act of 1972 opted for the possibility granted in the
second part of Section 9 paragraph 1 of the first EC Directive, maintaining
the ultra vires rule to the extent that it could be used against third parties who
acted in bad faith. However, due to the manner in which the English legisla
tor implemented this provision, the ultra vires rule could remain in full force,
diverging from the literal text of the Directive while honoring its goal of
protecting third parties. The formulation of the Act caused many differences
of interpretation between the various authors. The existing legal uncertainty,
resulting from the different interpretation rules described above, was there
to increased by the manner of implementation of the first EC Directive.
Partly as a result of criticism from the business world, the Companies Divi
tion of the Department of Trade and Industry (DTI) decided in 1985 to ap
point a review commission under the presidency of Professor Dan Prentice
to examine the legal and commercial consequences of the abolition of the
ultra vires rule.

The Prentice Report of 1986 contained numerous recommendations, includ-
ing that (i) the (external) capacity of a company should be unlimited, (ii)
with respect to private companies the mandatory obligation of an object
clause should be abolished and (iii) a public company could publish an an-
nual statement describing its prospective business activities in place of the
object clause, in fulfillment of the existing requirement based on the object
clause of the Companies Act. In the revised Companies Act of 1989, the legislator accepted
the recommendation in (i) above. However, the manner in which this new
concept was codified led again to interpretation difficulties. As a result the
subject of the abolition of the ultra vires rule reappeared on the agenda of the
broad Company Law Review in 1998 upon which DTI again reported. The
recommendation document (the Consultation Document of 1999) not only
contains proposals to secure the uninterpretable abolition of the ultra vires
rule in order to grant full capacity to companies to enter into transactions
with third parties, but also proposes making the object clause optional for
private companies.

This study then turns to the history of the Dutch ultra vires doctrine in chap-
ters 6 through 9. Following the developments in England, the ultra vires
doctrine in the Netherlands became a subject of interest to authors at the end
of the nineteenth century. If the developments in the Netherlands were not
yet a copy of those in England, they remained at least quite similar over a
long period. Tension also arose in the Netherlands between the severe ultra
vi res rule and the wish to protect third parties who had acted in good faith.

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remarkable path. The possibility granted in the Directive, maintaining against third parties which the English legislator had remained in full force, while honoring its goal of feared many differences existing legal uncertainty, described above, was there- the first EC Directive. /old, the Companies Divi- minded to fill the gap, honoring both points of departure: the applicability of the ultra vires rule and the protection of third parties who did act in good faith. In first instance a company was simply held liable when it had entered into an ultra vires trans- action with a third party in good faith (the case of the Huiden-arrest of 1928). At a later stage the Supreme Court adopted the construction whereby acts, which could have fallen under the object clause and which took place under such circumstances that a third party, acting in good faith and with reasonable care, could have assumed and was permitted to assume that those acts were not ultra vires, were deemed to be part of the object clause. In other words, in those circumstances these acts were not ultra vires (the case De Gruyter/Voorschootbank-arrest of 1942).

After the first EC Directive became applicable, the Netherlands legislator followed the English methodology. In Section 36h of the Code of Commerce, introduced in 1971 to comply with the directive, the legislator – as in England – opted for a provision whereby the ultra vires rule could be main- tained and whereby third parties in good faith were protected because trans- actions with them were deemed to be part of the object clause. In those cir- cumstances those acts were not ultra vires. A further similarity with the English situation was that the codification of the ultra vires provision caused a series of interpretation problems and led to legal uncertainty. This was not remedied by subsequent changes, up to the current Section 2:7 Civil Code; since Section 2:6 (old) the provision has been formulated in conformity with the literal text of the first EC Directive. However, in two ways the Nether- lands situation after 1970 deviated fundamentally from that in the UK.

In the first place, in our country, we have never engaged in broad discussion about the desirability of abolition of the ultra vires rule as is heard in the UK. Secondly, unlike in the UK, Dutch authors and the judiciary have even after 1970 maintained the interpretation rule that an object clause must to a certain extent be interpreted in respect of the (financial) interest of a company by the respective transaction. The literature is divided upon how this interpretation rule should be precisely defined. The judiciary has also failed to provide clear guidelines in this respect. This situation adds further legal uncertainty to the existing problems of interpretation of the codification of the ultra vires provision in Section 2:7 Civil Code.
The study explores the French situation, in chapter 10, which is similar to that of the Netherlands (and the UK until 1989) to the extent that the legislator has also adopted the exception to full abolition of the ultra vires rule allowed in the first EC Directive, choosing to maintain the rule against third parties who have acted in bad faith. Unlike in the Netherlands (or the UK), however, the ultra vires doctrine has led to little literature or case law in France. One possible reason is that the French theory of corporate interest has never been connected with the ultra vires doctrine, but has separate arrangements. In French law, the theory of corporate interest is governed by criminal law provisions.

Finally the German situation is discussed in chapter 11. Its most important characteristic was adopted in the main rule contained in Section 9 of the first EC Directive: that the capacity of a company vis-à-vis third parties is not in any respect limited by an object clause. In other words: a company has full capacity to enter into transactions with third parties.

The conclusion in chapter 12 is that it would both improve the legal certainty and harmonize our legal system with those of the UK and Germany, if the Netherlands were to abolish the ultra vires rule with respect to NV and BV companies, giving them unlimited capacity to enter into transactions with third parties.