

# The Ultra Vires Doctrine in Joint Stock Companies and under the New Turkish Commercial Code

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The prohibition against ultra vires, actions beyond permitted powers, in existing regulations provides that a transaction conducted with an outside party is not binding if the party acted outside of their field of operation. Accordingly, companies are to acquire rights and accept obligations only in specific matters which are written in the articles of incorporation.

Transactions outside the field of activity of a company are deemed nonexistent. This creates two problems in daily life. First, companies keep their fields of activity and scope wide to avoid being blocked by this regulation. Furthermore, they will add their potential fields of activity to the articles of incorporation for future enterprises. It is acceptable for companies to shift from one sector to another but in this way it reduces their transparency and damages their credibility. Related to this, companies which are not experts in their sector conduct business in more than one branch of industry while being inactive in others. Second, if a transaction conducted by a company outside their field of activity directly or indirectly is voided, it will affect the reliability of transactions and markets.

While the operations inside a company are considered within the scope of management, external affairs are considered under the scope of the representation authority. In joint stock companies, the board of directors and other managers conduct transactions and manage the company by performing their duties, which stem from the law and the articles of incorporation, and represent the company in agreements and transactions conducted with third parties and the company's employees. These competences belong to the board of directors and the board members in principle.

The board of directors can transfer its managerial powers and duties to members, establish various committees consisting of members, and/or transfer their duties to one or more members or even a person who is not a member of the board. A person who assumes the powers of the board of directors is called

the executive director if also a member, and the executive manager if not. Besides the executive or non-executive directors, other persons such as commercial agents and representatives can be authorized to represent the company. In terms of limiting the power of representation of these persons, the TCC states that all managerial and representative powers are delegable, while limiting the power of representation. Delegation of the exclusive powers of the board is forbidden, and such delegation of representative powers is limited by person (co-signatory) and location (confined to head or branch office transactions).

Thus, imposing restrictions on the power of representation of third persons in terms of subject or amount is ineffective. For this reason, while some management authorizations are valid, restrictions related to representation, like a 500 TL monetary limit or a subject restriction to wholesale issues is not valid.

Although its origins relate to power of attorney, the doctrine of ultra vires applies to transactions that take place outside of a company's field of activity. According to Article 137 of the TCC, as long as a company's field of activity is written in the main agreement, commercial corporations are competent regarding all rights and obligations. Article 137 of the TCC is as follows: "Having legal personality, trade companies shall be entitled to acquire all rights and undertake all obligations provided that such rights and obligations fall within the scope of activities indicated in their articles of association. Statutory exceptions regarding this matter shall be reserved."

One can easily infer the essence of what is called the ultra vires doctrine from the above: Any company

established in Turkey may carry out only the activities specified in its articles of association. The ultra vires doctrine restrains the ability of a company to enter into a contract or perform an operation that is beyond its corporate powers, the limits of which are determined by its articles of association. Accordingly, any ultra vires act concluded by a company is considered invalid and thus does not confer any rights and/or obligations on either the company or third parties. Also, Article 321 of the TCC includes the provision that representatives should stay within the company's scope and fields of activity. Therefore, transactions that differ from the field of operation are regarded as nonexistent.

The Judicial Council's court decisions reflect this principle. "In a written statement that is done on behalf of a company, it is required that in addition to the company's name there must also be the managers' signatures." (Yargıtay 11. HD 2005/13952). "A company's board of directors or representative is authorized to make legal transactions only in accordance with the company's scope and field of activity, if they only have special permission from the general assembly, they would be conducting legal transactions or business outside the scope of purpose and subject."

Another Judicial Council decision is as follows; "Despite being signed by the chairman of the board and two members of the board of directors, since it is related to the limitation of amounts which is also related to a company's internal affairs, even if it has been published in the Trade Registry Gazette, it is not binding on third parties. The court must decide to overrule the objection since the chairman of the board, who has the right of representation and to bind the company singly as written in the articles of incorporation, and thus the company, will be responsible for the bill of exchange he/she signed on behalf of the company. According to the Çamoğlu decision, in Turkish doctrine the words intent and subject were included mistakenly due to a lack of attention by the legislature. The author also believes that the word subject should be interpreted widely, considering the operations within the scope of a partnership which are acquiring profits and distributing this profit. [ÇAMOĞLU (Poroy/Tekinalp), 2009, s.318]" (Yargıtay 12. HD, 2004/10762).

This principle has been amended in the New Turkish Commercial Code (**NTCC**). It's appropriate to explain the topic through Articles 125, 331 and 371. In the second clause of Article 125 of the second section of the NTCC, which covers commercial companies and general provisions, companies have rights and obligations in the framework of the Turkish Civil Code Article 48, which gives companies legal entity except for statuses specific to natural persons. Article 331 of the NTCC emphasizes that joint stock companies should be established for all economic aims and fields of activity which are not forbidden by law.

The first sentence of Article 371 of the NTCC has determined all transactions that are within a company's scope and field of operation should be done on behalf of the company by the person who has the authority to represent the company. The second sentence of Article 371 specifies that transactions made with third parties by people who have representation authority shall be binding for the company. Still, such authority can be refuted if it can be proven that the third party already knew the circumstances or if the third party should have deduced and foreseen that the articles of incorporation would be declared inadequate to support the situation. However, as mentioned in Article 371/1, if a company suffers a loss due to transactions that are made in violation of the articles of incorporation and law, it should revoke the authority of the relevant representative. This amendment emphasized the departure from the ultra vires doctrine in the legislative intention of Article 371 and other articles.

However, this should not be misinterpreted to mean company managers may now make transactions outside of the scope and fields of activity. Instead, the amendment should be interpreted to mean that transactions that are outside a company's scope and field of operation shall not be regarded as nonexistent, but rather shall be regarded in the framework of responsibility of the representative who made the transactions that were contrary to law and the articles of incorporation in order to protect third parties who made a transaction with the company in good faith.