EFFECTIVE CORPORATE GOVERNANCE AND MANAGEMENT IN NIGERIA: AN ANALYSIS

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DECLARATION

I hereby declare that this work is the product of my own research efforts; undertaken under the supervision of Professor J.M. Nasir and has not been presented elsewhere for the award of a degree or certificate. All sources have been duly distinguished and appropriately acknowledged.

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CERTIFICATION

This is to certify that this thesis has been examined and approved for the award of the degree of DOCTOR OF PHILOSOPHY IN LAW

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This thesis is dedicated to the followings:

1. My God Almighty for His mercies upon my life.
2. My wife for her love, encouragement, prayers and understanding.
3. My mother for her love and constant prayers.
4. My children for their untiring love.

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NIGERIAN LEGISLATIONS

ABBREVIATIONS

NIGERIAN REPORTS

A.N.L.R.	All Nigerian Law Reports (Reprints)
ALL. N.LR	All Nigerian Law Reports
C.C.H.C.J.	Certified Copies of High Court Judgements
F.R.C.R.	Federal Revenue Courts Reports
F.S.C.	Federal Supreme Court
L.L.R.	Law Reports of the High Courts of Lagos State
N.C.L.R.	Nigerian Commercial Law Reports
N.C.R.	Nigerian Law Reports
N.S.C.C.	Nigerian Supreme Court Cases
N.W.L.R.	Nigerian Weekly Law Reports
Pt.	Part
R.M.L.R.	Royal Monthly Law Reports
S.C.	Judgements of the Supreme Court
U.L.L.R.	University of Ife Law Reports

UNITED KINGDOM REPORTS

A.C.	Appeal Cases
All.E.R.	All England Reports
App. Cas	Law Reports, Appeal Cases
B.C.C.	Brown's Chancery Cases
B.C.L.E.	Butherworths Company Law Cases
Ch.	Law Reports Chancery
Ch. App.	Chancery Appeal Cases

Ch.D.	Law Reports, Chancery Division
C.P.D.	Law Reports, Common Pleas Division
E.R.	English Reports
Ex.D.	Law Reports, Exchequer Division
Hare	Hare
K.B.	Kings Bench
C.R.Ch. Appp.	Law Reports Chancery Appeal
CR. Eq.	Law Reports Equity Cases
L.R.H.L.	Law Reports House of Lords
L.R.N.S.W.	Law Reports, New South Wales
L.T.	Law Times
N.S.W.S.R.	New South Wales Law Reports
N.S.W.S.R.	New South Wales State Reports
Q.B.	Queens Bench
Q.B.D.	Queens Bench Division
S.C.	Session Cases
S.C. (HL)	Session Cases, House of Lords
T.C.	Tax Cases
T.L.R.	Times Law Reports
W.L.R	Weekly Law Reports
W.N.S.C	Weekly Notes, Session Cases

OTHER REPORTS

A.C.L.R.	African Commercial Law Reports

A.L.R.	Australian Law Reports
A.L.R. Comm.	African Law Reports (Commercial Series)
At. K	Atkyns
C.L.R.	Commonwealth Law Reports
D.L.R.	Dominion Law Reports
Dr. & Sm	Drewry and Small
F.R	Federal Report
F. Supp	Federal Supplement Reports
I.R.L.R.	Industrial Relation Law Reports
Ir. R	Irish Reports
Ken.	Kensas Reports
N.J.Eq	New Jersey, Equity Reports
N.Z.L.R.	New Zealand Law Reports
S.E.C.	Securities and Exchange Commissions Reports
S.L.R.	Scottish Law Reports
S.L.T.	Scots Law Times
T.R.	Term Reports
Tex-Civ-App.	Texas Civil Appeal Reports
W.A.C.A.	Selected Judgements of West African Court of Appeal
Wis.	Wisconsin Reports

OTHER SOURCES

A.B.U.L.R.	Ahmadu Bello University Law Review
Adelaide L.R.	Adelaide Law Review

Bus.L.R.	Business Law Review
C.L.R.	Cambridge Law Review
Cal. L.R.	California Law Review
Can. B.R.	Canadian Bar. Review
Col. B.R.	Columbian Law Review
Camb. L.R.	Cambridge Law Journal
CLEAN (N)	Continuing Legal Education Association (Nigeria)
Co. Law	Company Lawyers
Harv. L.R.	Harvard Law Review
L.Q.R.	Law Quarterly Review
M.L.R.	Modern Law Review
M.U.L.R.	Minnesota University Law Review
Mich L.R.	Michigan Law Review
Mod. L.R.	Modern Law Review
N.B.L.	Nigerian Bar Journal
N.S.C.L.	Nigerian Journal of Contemporary Law
N.L.J.	New Law Journal
N.Z.U.L.R.	New Zealand University Law Review
S.A.L.R.	South African Law Review
Y.L.J.	Yale Law Journal
Yale L.R.	Yale Law Review

ABSTRACT

Recent events worldwide concerning high profile corporate failures necessitated the imperative need to determine the efficacy of corporate governance and management oversight devises. It is in this regard that this thesis has assessed the performances of important stakeholders engaged in policy formulation, day-to-day running of the affairs of the companies as well as those persons or organs charged with oversight responsibilities. The thesis critically analysed and evaluated the conceptual foundation of corporate governance and management in Nigeria as well as the global trend on the development of modern corporate government and management principles. The research work is anchored on primary and secondary source materials in addition to the carrying out of oral interview and the administering of designed questionnaires. The research work presented an opportunity for a thorough and comprehensive analysis and evaluation of the roles of corporate governance and management instruments against the background of the legal climate in which they operated. The thesis position is that corporate bureaucrats charged with the onerous task of effective governance and management of companies in Nigeria as well as the various inbuilt monitoring devises have failed to perform their assigned roles thus raising a critical questions of the necessity for reforms and a concomitant change of attitude amongst stakeholders. Thus, the thesis has noted among other things that the legal regime regulating directorial conducts needs to be revisited in the form of amendments to make the obligations more defined, focused and deterrent.

CHAPTER ONE

INTRODUCTION

1.1 GENERAL BACKGROUND

In the past few years, the Nigerian commercial terrain has witnessed not only tremendous growth and expansion but also vigorous legislative activities, particularly in the area of Company Law. For instance, the Law Reform Commission carried out a far-reaching law revision exercise in 1990 with the aim of producing a much more appealing and comprehensive code. The recommendations of the Law Reform Commission, most of which have been codified have changed the outlook of much of our Company Law. It is important to point out that the revision exercise was necessitated by the acute problems which arose with the rapidly developing economic activities of the nation and which the 1968 Company Act found difficult to cope. Essentially, the primary aim of the reform was to facilitate business activities in the country and ensure that the tripatite interests of the investing public, the general public itself as well as that of the nation were protected.[1]

The law revision activities of the Law Reform Commission soon culminated in three major company enactments in 1990. These are the Companies and Allied Matters Decree (Now Act), the Banks and Other Financial Institutions Actand the Insurance Act of that year. These enactments revolutionised Corporate Law, management and governance in the country. But it is a sad note however that despite the laudable efforts of the Law

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[1] The Working Paper on the Reform of Nigerian Company Law Vol. 1 p. 3 para. 9.

Revision Exercise of the Law Reform Commission, company failure continues to be on the increase. Many corporate entities have failed to thrive or survive since 1990, despite these enactments.

Though company failure is a universal phenomenon, in the case of Nigeria, the situation has been quite alarming. For instance, with respect to the Banking Industry between 1986 and 1994, most banks lost some of the confidence which had returned to the Banking Industry after the 1950s situation when between 1930 and 1954 many indigenous banks failed. On a specific note, it has been reported that seven banks were distressed in 1989; nine in 1990; eight in 1991; thirteen in 1992; twenty four in 1993 and four in outright liquidation in 1994;[2] five in 1995 and an all time alarming highmark of twenty six banks as at January 16, 1998.[3] Distress and Liquidation did not spare the operations of primary mortgage institutions either. Thus in 1997 alone, ninety seven primary mortgage institutions were liquidated in one fall swoop by the Central Bank when it revoked their operational licences.[4]

Two main factors can be suggested as responsible for company failure and distress generally. These are the macro-economic (external) factors and the micro-economic (internal factors). The macro-economic factors border on structural imbalances in the economy and the economic system, inappropriate economic policies, international factors or a combination of all or some of

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2 Mamman H.; *"Banks Management Issue and Restoring the Health of Nigerian Banks through Improving the Quality of Management/Employees"* N.D.I.C. Quarterly *Vol.* 4 No. 4 at p. 57.

3 Nigerian Deposit Insurance Corporation *(N.D.I.C.) Yearly Report* 1999; See also Chigbo, Ejiofor, "Liquidation Banks in Nigeria", *in Body and Soul Weekend Paper* Vol. 1 No. 9 dated 31st October 1999 at p. 12 and 13.

4 Nigerian Deposit Insurance Corporation *(N.D.I.C) Yearly Report* 1998, at p. 3.

these. Thus for instance, deregulation as an economic policy may change the business environment and make things difficult for the company's management to take the right managerial steps. Globalization and huge foreign debts have adversely affected many world economies especially the developing economies of the third world. Appropriate decision making becomes more sophisticated and most often difficult to take under such a debilitating business environment.

The micro-economic factors on the other hand advocates that external factors are merely secondary and that the principal factors lie in managerial deficiency. It has been pointed out in this direction that:

> … A bank headed by weak management… is usually the first one to fall prey to deteriorating economic (macro-economic) condition… adequate management (i.e. good or qualitative management) is more adept at dealing with changing macro-economic conditions… applying only macro-economic remedial actions… without simultaneously addressing the management side may prove ineffective or even counter-productive.[5]

It is submitted that quality management is undeniably, an important factor which draws a distinction between a solvent and an insolvent corporate entity. The efficiency of a corporate entity is reflected in the effectiveness of its management and governance.

The management of a company is essentially the collective responsibility of both the directors and the shareholders, while that of governance belongs to the Board of Directors. This is understandably so, since the directors

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[5] See Mamman, H. op. cit. at p. 58. The problems most banks had started with management inattention to the details of loan functions which created credit weaknesses and ultimately macro-economic changes.

constitute the organs through which the company as a fictitious legal person acts. They constitute the directing mind and will of the corporation.

The decision making powers is divided between two primary organs, namely, the shareholders in general meeting and the directors acting either as a Board of Directors or through delegates.[6] While the director hold the primary powers of management, that of the shareholders is residual in nature.

Due to the importance attached to the position of directors as agents and managers of the company, the law in most jurisdictions including Nigeria has imposed some stringent statutory duties and obligations on directors aimed at ensuring prudence in the management of corporate entities.[7]

The need for an efficient management and governance culture amongst managers of business concerns is more than ever before imperative in this age of social responsibility. This is so since the old fashioned concept of company as an instrument meant solely for the maximization of profit for the benefit of shareholders has given way to that which recognises that as an economic unit, it consists of a combination of a series of factors, namely, those of the investors as the providers of capital, of the employees as providers of labour and of the creditors and the public at large.

Even in Britain, which for a considerable period of time had shown a traditional dislike for formal institutionalism, the new concept of modern company was recognised by all the political parties. The then British

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6 63 (3) CAMA 1990.

7 Sections 279, 280, 281 and 287, 622 of the Companies and Allied Matters Act 1990; sections 20(5), 24(5); 44(3) and Banks & Other Financial Institutions Decree BOFIA etc.

Conservative Government in July 1973 published a white paper on Company Law Reform and stated as follow:

> In formulating… Proposals, the Government are specifically recognising in the context of the Company Law, the generally accepted fact that ownership involves responsibilities as well as rights. This requires company directors on behalf of the shareholders to discharge their social responsibilities as well as to protect their legitimate interest. The Board of Companies and their management, thus have a manifest obligation towards those with whom they have dealings – and none more so than the employees of the company.[7a]

The laudable concept has for long in America received judicial recognition, in a number of cases. For instance in *Theodore Holding V Henderson*[8] in 1969, and later in *Emith V Balow*.[9] both courts gave tacit recognition to corporate social responsibilities of companies. In Nigeria this new philosophy has not gone unrecognised. Thus according to Ahmed Abdullai:

> … It is generally accepted that companies have several responsibilities involving non-profit seeking activities or activities in which profit is moderated for some socially useful purpose…[10]

It is important to note however that this social responsibility which is moral in nature, does not confer any formal right on the employees or workers to participate in decision making or exercise effective control in the manner in which a company shares its profits.

7a Schmitthof M.C., *"Commercial Law in a changing climate"* 2nd ed, (London: Sweet & Maxwell, 1988) at p. 37.

8 275 A. 2nd Pel. Cha. (1969) 398.

9 S.C. of New Jersey 38 A. 2058 (1983).

10 Abdullahi, A.; *"The Company in a Changing Environment."* Nigerian Business Law & Practice. Journal Vol. 2 No. 2 (1990) p. 29. See also Adewale, T., *"Companies and Social Responsibilities"* (Vanguard, August 3, 1995) at p. 12.

The researcher firmly holds the belief that in Nigeria, various internal corporate governance and management monitoring devices aimed at checking the directors so as to ensure effective corporate management and governance have not been effective. The result is that management in many large public companies has become an uncontrollable monster and "self perpetrating Oligarchy."[11a] The researcher further believes that effective management and governance is attainable in corporate entities in Nigeria. It is therefore imperative that an identification of the problems militating against the existing corporate governance monitoring devises and an application of a prescriptive approach to these problems will do justice to this research work.

It is needless to emphasis that this research work is imperative at this critical stage of our national development. Those companies that will continue to survive and prosper in this new millennium, in the face of deregulation, economic liberalization, increased competitiveness and globalization are those that will fully imbibe the complement of effective Corporate Governance and Management in Nigeria. This is the unenviable task of this research work.

1.2 STATEMENT OF RESEARCH PROBLEM

The alarming rate of company failures, and distress due to misgovernance and mismanagement in Nigeria and the apparent failure of inbuilt corporate governance and management devices to arrest the phenomenon made this research work imperative.

[11a] Lord Denning, M.R. in *Northwest Holdt Ltd. V. Department of Trade & Others (1973) 3 All E.R. 280, (1978) Ch. 201.*

It is the expectation of most, if not every shareholder who has chosen to invest in companies that there will be return on his or her investment. The snag however is that not every investor has the opportunity of taking part directly in the governance or management of the business which he has invested. This is due to the complex structure of the modern company as a business organization. Thus quite often, those in charge of governance or management are either those who have no personal investment at all or those who are in control of majority shares in the company. This sort of scenario thus necessitates that there should be adequate safeguards in place not only to discover and check improprieties in companies but also to deter those seeking to perpetrate them.

In the Nigerian corporate setting, shareholders are mostly dispersed and have small holdings. This problem is compounded by lack of interest and collective action to challenge those in governance and management positions. This apathy on the part of shareholders to perform their oversight responsibilities have rendered ineffective other internal corporate governance oversight devices such as the proxy machinery, non-executive directors, auditors and derivative suits that depend on them for their efficacy.

The governance and management style of corporate bureaucrats has brought out a quantum of problems of ineffective corporate governance and management in corporations that are more of micro-economic nature. Is the self serving interest of the directors responsible for corporate distress and collapse in Nigeria? And to what extent? Could it have been possible to stem

the tide of corporate distress and collapse in Nigeria if the shareholders had effectively exercised their residual or concurrent power of management? What about the Board of Directors – the policy making organ? Where the boards qualitative enough to perform their assigned responsibilities in the governance of corporations in Nigeria? Were they also victims of external influence and interference? Have non-executive directors who are usually expected to bring to bear their special knowledge, and skill faired as important mechanisms for effective corporate governance? What impediments did they contend with in discharging their governance and management functions in Nigeria. From the external source is the company external auditors whose duty it is to act as the watchdog of the financial aspect of corporate governance by establishing the credibility or otherwise of financial statements. Has the auditor performed satisfactorily his watchdog role? What has been responsible for the auditors apparent lack of will? What lessons do we derive from the governance and management of companies in Nigeria by the non-executive and executive directors? What are the lessons from the performances of those responsible for checks and balances in the company set up? Considering our understanding and experience of the roles and performances of the various stakeholders in corporate governance and management in Nigeria, do they provide the required platform for judgement and recommendations for effective governance and management of corporations? These are pertinent problems which this research has addressed.

1.3 RESEARCH AIMS AND OBJECTIVES

The lingering problem of company failure in Nigeria in recent times has been a matter of grave concern to many. There is no denying the fact that effective management and governance is the central force and the most critical factor in economic and social development the world over. But in Nigeria, as events have so far shown, the secrets of effective corporate governance and management have eluded quite a large number of managers of commercial concerns. Thus the real problem of company failure in Nigeria cannot be attributed to macro-economic factors alone but equally to that of mismanagement. And this includes ignorance of management knowledge, lack of management ability, discipline and vision, absence of entrepreneurial and managerial initiative and innovativeness, and absence of appropriate legislative framework. The above problems are compounded by the fact that legislative responses to them have not been successful. It is these reasons that have necessitated this research aims and objectives.

1.3.1 Research Aims

(a) To provide insights into the relationship between governance and management mechanisms and companies financial performances in Nigeria.

(b) To examine the extent to which corporate governance and management devises may assist in ameliorating the agency problem posed by corporate bureaucrats.

1.3.2 Research Objectives

The objectives of this research work which flows from its overall aims are several. In particular, the specific objectives are as follows:

1. Investigate the relationship between quality board of directors and a company's performance
2. To examine the extent to which the prevailing corporate governance and management legal regime may be related to effective governance and management of corporations.
3. To examine whether or not maintaining a distinct separation of the position of Managing Director and Chairman of the Board of Directors plays a crucial role in ensuring effective corporate governance and management.
4. To examine whether the appointment of an effective and independent external auditor, assist in the companies performance.
5. To ascertain the influence of the composition of the board of directors on effective corporate governance.
6. To examine whether the nature of insider shareholdings is related to quality of governance and management.
7. To examine whether there is a positive relationship between vigilant and unapathetic shareholders and quality governance and management.
8. To contribute to and expand the scope of knowledge in corporate governance and management.

1.4 SCOPE AND LIMITATION OF STUDY

The scope of this research work has been appraise various enactments both local and foreign that are relevant to the governance and management of companies in Nigeria. In so doing, cognizance was taken of the prevailing socio-political environment as well as the state policies in which these enactments operated.

The scope of the study therefore revolve around corporate bureaucrats such as directors acting individually or as a group as well as those whose responsibilities it is to perform oversight functions.

The scope of the study does not however encompass an extensive examination of the theory and practice of management save those aspects of the subject matter that are necessary in establishing a link between it and governance.

1.5 RESEARCH METHODOLOGY

This research work is both doctrinal and non-doctrinal. To this extent both the primary and the secondary sources of materials has been used. This entails textbooks, journals, articles, magazines, newspapers, legislative enactment and judicial decisions emanating from Nigeria and other jurisdictions relevant to the Nigerian situation. Opinions contained in such materials will be of much assistance.

From the non-doctrinal angle of this research opinions of directors of corporate entities, board members of companies both past and present,

shareholders of companies, company external auditors etc. has been sampled through oral interview and the administering of questionnaires.

1.6 LITERATURE REVIEW

Professor Gower[12] carries out an extensive discussion on directors' duty to the company. He classifies them into two broad categories, namely, the fiduciary duties and the duties and skill which are a derivation of common law. Professor Gover's approach suggests that the standard of duty under common law is regrettably low unlike the fiduciary duties that are quite strict. He carried out a painstaking analysis of the English Insider Dealing Act of 1985 as to the origin of the general equitable principles that mandate directors to desist from having interest and where they have such interest to make appropriate disclosures concerning such transactions to their companies. Professor Gower has commended the prohibition of directors from dealing in securities of their companies without a concomitant corporate responsibility to disclose pricesensitive informations at their disposal to the shareholders.

Professor Gower also examined the ramifications of the majority rule principle contained in *Foss v. Harbottle* which he considers an inhibition to minority shareholders right to challenge corporate wrongs. The learned scholar asserted that a company has two primary organs charged with the governance and management of companies. These, he says, are members in general meeting and the directorate. He attempts an analogy in constitutional law, noting that just as in a constitutional democracy where legislative sovereignty

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[12] See Gower's Principles of Modern Company Law, 5th ed; (London: Stevens & Sons, 1998). See also the 4th edition.

and administration resides with parliament and executive government respectively, the rule making authority rests with the general meeting of members, while the governance and management resides with the directorate either as a board or the individual director. The shortcoming of this work is that it has not captured specific governance issues from Nigerian perspective.

The learned authors of Boyle & Birds, Company Law,[13] examine the theory and practice of "proxy voting machinery" in corporate governance. They noted that contrarily to the generally held notion that the proxy instrument is a monitoring device, it is a potent instrument in the hands of an overbearing and collaborative board that is unsympathetic to shareholders cause. They provide an explanation for this apparent weakness, as the inability or failure or apathy of the majority of individual shareholders to attend company meetings. They observed that though the growth of institutional shareholders could have been an antidote to the shareholders inefficiency, by redressing the imbalance, the usual practice of institutional shareholders not wanting to contest issues at company meetings have swayed the advantage in favour of management. The contributions of the learned authors is quite commendable but falls short of suggesting remedial measures.

The work of C.D. Thomas "Company Law for Accountants"[14] devoted four chapters on directors duties and majority rule and minority protection. The chapters restated the fiduciary duties of directors to act honestly and in the best interest of the company and to be bound by the provisions in the

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13 See Boyle, A.J. (ed.) Boyle & Birds Company Law, 2nd ed. (Bristol: Jordan & Sons 1987).

14 Thomas, C.D.; *Company Law for Accountants*, 3rd ed. (London, Butterworths, 1992).

company memorandum and articles of association on one hand, the duty of care, skill and diligence and the ambit of the majority rule and the circumstances under which the rule would be sidetracked. The authors observed that the right of a minority shareholder to initiate a corporate action derivatively where such a company is facing a winding up proceeding has ceased to exist. But they noted further that the greatest obstacle to minority right to challenge a corporate wrong is that of compensation for the cost of litigation by successful litigants, which usually is given to the company. The advantage of author's contribution lies in the lucidity and simplicity in which they discussed the subject matter. The drawback of their contribution is that of brevity in several essential areas.

Also of some importance to this research work is S.C. Shepherd's text "The Law of Fiduciaries"[15] published in 1981. This work dealt with the importance of human activity and trust. The work examined the fiduciary concept, and its historical antecedents. The author submits that it is unclear whether it is right to assert with the force of finality whether the law relating to fiduciaries is part of the law of restitution or a subject matter that overlaps with the principles of restitution. The author explained that the reason for this dilemma is more of a reflection of the present stage of development of law of fiduciary.

The work also attempted a classification of the fiduciary principle into three major compartments, namely, properly holders, representatives and

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[15] Shepherd, J.S.; "The Law of Fiduciaries" (Toronto Canada: The Casswell Co. Ltd. 1981).

advisers. The author however warns that there are no identifiable classes of relationship that exhibit predominantly a fiduciary component and that these classifications are just rough guides. The work also unveiled the philosophical problem in the understanding of the fiduciary concept. The work noted that the English legal system has two distinct roots the common law and equity.

In relating the application of the fiduciary principle to modern day corporations, the author observed that the application of the fiduciary principle is much more complex in modern corporations, due to the number and interrelationships of the fiduciary relationships between various participants in company setting. This book is an important source material that has laid a solid historical and theoretical foundation for the present day corporate obligations of corporate bureaucrats.

Farrah's Company Law,[16] is another source material that sheds much light on some aspects of this research work. At chapter 21 the author discussed the strategic importance of the board. The authors observed that though in the nineteenth century management was viewed as an agent of the corporation in general meeting and as such controlled by it, the situation is no longer the case. The present day increase in the power and influence of the Board is seen by authors as a result of the change of wording in the standard form of article in the early twentieth century. The learned authors noted the inability of the corporate law to grasp sufficiently the plethora of management structures and practices as well as the unsatisfactory state of the law in

[16] See Farrah, J.H.; Furrah, N.E. and Hannigan, B.M.; (London: Buttersworths 1991).

relation to the authority of an individual director to bind the company. The issue of the distribution of corporate power within the corporate setting is given some consideration. The author discussed the division of corporate power between the company in the general meeting and the board of directors. The authors analysed the theoretical nature of this division and concluded that it is not a realistic view of what happens in practice. The authors have also applauded the legal recognition of the concentration of power in the hands of management and considers it as being in consonance with separation of ownership and control hypothesis and the idea the corporation for raising large amount of capital. The author further identified the legal instrumentalities for curbing possible abuses such as the various fiduciary obligations, the disclosure principles, entrenching shareholders power in general meeting, and the reform of the board structure. This work is also an important foundational material that provides a solid platform for this research work.

Pennington,[1725] examined the principle of judicial non-interference inherent in the principle of majority rule and the exceptions to it. He considered the effect of the breach of directors fiduciary duties which he said may lead to an invocation of a derivative action if certain conditions are complied with. Pennington examined the ramifications of the overriding power of the board of directors to ratify directorial improprieties arising from the breach of fiduciary obligation in the absence of fraud. Pennington also

[1725] Pennington, R.R., Company Law, 5th ed. (London: Buttersworths 1985).

discussed the circumstances under which a derivative action may be premised on the negligence of directors. He however asserted while disagreeing with Professor Gower that where a plaintiff requires a board to call a general meeting for the purpose of commencing action against directors and the director either refuses to call the meeting or call the meeting to defeats the resolution by utilising the votes of shareholders, the only remedy the court can give is by calling the meeting and not by allowing the plaintiff to commence the action as suggestion by Professor Gower. Pennington made an elaborate contribution to the requirement of directorial control of the affairs of the company as a precondition for derivative action. He analysed the concept of directorial control but debunked the assertion that the mere fact that a member who institutes a derivative action holds share of a class that has no voting rights and as such disadvantaged to call a meeting, does not mean that the directors are in control of the company affairs. Pennington further observed that the requirement of control has not been a rigid requirement under English law not only with respect to unincorporated common law companies but even with limited liability companies. This work though quite enriching only examined the subject matter from a narrow perspective of the English legal system.

The learned authors of Charlesworth and Geoffrey Morse,[18] see considerable wisdom in the majority rule principle in corporate litigation which

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[18] Geoffrey M. (ed.) *Charlesworth & Morse Company Law* 14th ed. (London: Sweet & Maxwell 1999).

emphasizes that the wishes of the majority prevail over those of the minority in the absence of fraud. They contended that the principle avoids multiplicity of suits and prevent the company from being the subject of a long and expensive litigation but conceding that the action limiting rule is by no means an inflexible rule since it can be trampled upon under certain situations. The authors also attempted a justification for the strict approach of the law in ascribing both the trusteeship and the fiduciary tag on directors to make them accountable to the company even where there is no economic loss or common law fraud is established. Inspite of the lucidity with which the learned authors analysed the subject matter, the treatment of other important matters such as directors duties, for instance is just a rehash of the general principles governing directors duties. The work failed to capture and bring to the fore major critical issues and complexities of corporate governance.

Professor Irukwu in his book "Insurance Management in Africa"[19] has made an illuminating contribution which has important bearing to the research work. He examined the concept and responsibilities of management as opposed to governance generally. More importantly, he examined the composition and functions of a typical insurance company operating in Africa comprising shareholders, board of directors, the management, staff and the various technical departments and policy makers. But the learned authors apparently fell into an inadvertent error when he said the management of a

[19] Irukwu, J.O. "Insurance Management in Africa" (Ibadan: Heinemann Educational Books Nigeria 1977).

company is entrusted to the board of directors, instead of the managing director. The author discusses the importance of quality boards in insurance companies encompassing a mixture of part-time and workers directors as obtained in developing countries. The material offers considerable insight into the operations of the mode of governance and management of insurance companies in Nigeria. This material is therefore restrictive in its approach to the issues of corporate governance and management.

Kiser Barnes book on "Cases and Materials on Nigerian Company Law"[20] examined the various components of corporate management from the legal perspective. He submitted that the general meeting of the company as a vital organ of the company provides an occasion for shareholders to air their views on company maters and take effective action with respect to company policies. But he is quick to add that the reality of the division of powers between the board of directors and the shareholders in general meeting is that the power to call general meeting vested in the board of directors arms them with dictatorial power to decide whether to call a general meeting or whether a meeting shall be held or not.

The learned author carried out a critical analysis of Section 282 of CAMA 2004 with regards to directors duty of care, skill and diligence and concludes that unlike the pre-1990 era when the courts were obviously non-interventionist concerning the directors duty of care whereby directors were

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[20] Barnes, K.D.; Cases and Materials on Nigerian Company Law, (Nigeria: Obafemi Awolowo University Press Ltd. 1992).

judged by their qualifications, attributes and personal skills, Section 282 of CAMA 1990 is an objective standard which admits of no discrimination by imputing the same degree of common intelligence on company directors. Inspite of the contribution of this work to the research work, it did not provide answers to the post 1990 distress syndrome and collapse of many a corporate entity in Nigeria.

Professor G.A. Olawoyin book "**The Status and Duties of Company Directors**",[21] has devoted the entire eleven chapters on company directors. Essentially, the book is a commendable attempt at discussing comprehensively, the principles pertaining to duties of directors, and the historical and fiducial basis for the principles. The author also unearthed the difficulties entails in practicalising the principles within the confines of commercial entities. The book captured the attitudes of the courts to the problems posed by the application of the principles. The author made an important finding when he noted that the trusteeship concept of fiduciary duties applicable to directors breaks down at various points in its application to contemporary directors. He further observed that the lack of effective control over directors was a result of the inability of the legislative authorities to introduce far-reaching reforms. The book brings out clearly some of the root causes of ineffective corporate governance by directors in corporations. The book no doubt identified some of the basic problems of ineffective governance

[21] Olawoyin, G.A.: "Status and Duties of Company Directors" (University of Ife, Ile-Ife – Nigeria 1977).

and management but failed to proffer solutions capable of addressing same. This material which was published in 1977 though still of immense relevance falls way behind in terms of current happenings in the corporate terrain.

Dr Olakunle Orojo, in his book "**Company Law and Practice in Nigeria"**,[22] examined the position of directors in the governance and management of companies. He considered the theoretical bases for the various positions ascribed to company directors. He submitted that despite the attitude of the law, their true essence is that they are merely commercial men managing a trading concern for the benefit of themselves and the shareholders. The learned author also discussed at length the duties of directors and the mechanisms for enforcement. He noted that directorial obligations imposed on directors are of serious considerations since in the final analysis the court will always intervene to set aside a transaction. He considered the practical difficulties posed by the powerful administrative machinery of the company at the disposal of directors in enforcing directorial obligations. He noted further that the fact that directors are in most cases controlling shareholders makes their removal a Herculean task despite the availability of remedies. The limitation of this material however lies in the lack of indept treatment of the subject matter. The learned author is rather casual in his analysis.

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[22] Orojo, J.C.; Company Law and Practice, 3rd ed. (Lagos: Mbayi & Associates Ltd. 1992).

The book "**Essays on Company Law"** published in 1990,[23] contains several contributions from personalities who have made incisive analysis on wide ranging subject matters in company law. Particularly, relevant to this research work are the contributions of Professors Akanki, J.O. Anifalaje, and Osarheimen Osumbor.

Professor Akanki,[24] whose contribution is on "Protection of the Minority in Companies" observed that the action limiting rule in *Foss v. Harbottle* was designed to preserve the ideals of democracy in companies by shutting out vexatious and multiplicity of actions though in the process renders the minority vulnerable victims of the companies majority shareholders. Professor Akanki sees the enlargement of the concept of oppression to encompass unfairly prejudicial; unfairly discriminatory and disregard of interest as commendable innovation to protect the minorities in companies as well giving them considerable room to manouvre while instituting minority shareholders action. He applauded the removal of judicial barrier as to competent litigants that hitherto encouraged the majority to perpetuate fraud on the minorities in companies. He remarked further that the elongation of the concept of *locus standi* to encompass a director, officers past or present, a creditor and the Corporate Affairs Commission, and any other person the court considers fit and proper, is a legislative weapon capable of minimizing rather than encouraging frivolous litigations.

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23 Akanki, E.O. (ed.) "Essays on Company Law" (Lagos: University of Lagos Press 1992).

24 Ibid. at p. 276.

Professor Anifalaje's contribution is on **"Current Principles and Policies on Company Accounts Annual Returns and Audit"**.[25] He sees the concept of corporate financial reporting as emphasizing financial probity and accountability. The author emphasised the fact that the three concepts of company accounts, annual returns and audits are interrelated concepts which individually and collectively serve as reliable index of corporate financial information for the consumption of shareholders, creditors, investors and the Corporate Affairs Commission. He condemned the repeal of Section 352(3) of the CAMA which hitherto requires the legal practitioner to countersign the auditors report as hasty. He noted that the requirement of countersigning was to ensure that two reasonable heads were better than one. The author recommended the creation of a corporate supervision department to carry out constant surveillance on companies financial statements.

Professor Osumbor[26] in examining the duties and powers of director decried the decision to codify the fiduciaries duties as well as the duty of care and skill. He noted that though the decision to codify was courageous, the exercise has made CAMA 2004 an embodiment of too many defects, irritating drafting, printing errors, imprecion in the nature of the duties and powers of directors as well as the lumping together of too many issue of different origins. The writer however noted with satisfaction the attitude of CAMA in emphasizing among other things, disclosure of director's shareholding; duly to

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25 Ibid. at p. 200.
26 Ibid. at p. 130.

give notice of personal matters of directors; particulars of directors in trade catalogue, substantial property transactions concerning directors; prohibition of secrets payments, gifts or bribes to directors, probity in the conduct of company directors who take protective cover under limited liability to perpetrate improprieties in companies. The author singled out Section 290 of the CAMA which is directed at the company directors for the purpose of holding them accountable personally for the money or property received by way of loan, advance payment for the execution of contract or project. But he quarreled with the requirement of intent to defraud on the part of a director before such director can be held liable. The contributions of these authors are no doubt enriching but one sided for not anticipating the post 2000 development in the corporate terrain.

The book "**Board Room Management: A Book of Reading"**,[27] edited by Ronald Eguonu, is also an outstanding contribution to corporate governance and management. Particularly of relevance are the articles of Ronald Eguonu, Chris Atoki, Professor G.O. Nwankwo, Chief John Ebhodaghe, Chief J.A. Odeyemi and Professor Peter Umoh.

In chapter one of the book, Ronald Eguonu, in his contribution titled **"Introduction to the Board Room"[28]** identified four categories of Nigerian boards. He noted that the quality of appointees to the Board and what actually transpires there affects the quality of corporate governance which impacts

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27 Eguonu, R. (ed.) "Board Room Management: A Book of Readings." (Ikeja Lagos: Strides Associates Ltd. 1994).

28 Ibid. at p. 1.

seriously on the success or otherwise of the organization. The author compared the advantages and disadvantages of multiple directorship and came to the conclusion that it should be discouraged since it heightens greed. He identified traditional areas of conflict among Board members. He noted further that the problem of Nigerian Boards is a mix grill in which government policy including that of Central Bank, the Nigerian factor especially that of endless manouvring, the explosion in the number of banks and the consequent inexperience of staff and boardmen accentuated ineffective governance and management.

The authors contribution is quite commendable but surprisingly fails to provide remedial measure to the problems identified.

Chris Ade Atoki in his article **"Outside Directors: Duties, Rights, Privileges and Liabilities"**,[29] examined the ethical and legal implications of being a company director which he says must be considered from the standpoint of directorial powers and the discharge of directorial powers and responsibilities. The author considered the specific constraints that inhibit the performances of non-executive directors in ensuring effective management of their enterprises. He further commended the practice in foreign countries where appointees to the Board is based on competence and individual area of specialization. The authors contribution in the chapter clearly portrayed some of the problems that inhibit directors in effective discharge of their corporate responsibilities. The authors inability to point out imperfections in the legal

[29] Ibid. at p. 35.

regime regulating directorial conduct of outside directors is a drawback in the authors contribution.

Professor G.O. Nwankwo in chapter six made a brilliant and invaluable contributions. In his piece titled **"Making the Nigerian Board Work"**,[30] the learned professor, examines the corporate scene in Nigeria and comes out with the findings that the problem with corporate governance and management in Nigeria is that of managing the environment. This, he breaks down into the internal and domestic environment, the legal and regulatory environment, the socio-political environment as well as societal expectations. The author approached his analysis from the perspective of the banking industry. On the internal environment, the writer noted that a pre-condition for success in any organization is the effectiveness of the internal audit whose function it is to carry out an analysis of the internal financial environment of the institution and ensure that the right thing is done. He identified a second component of the internal environment to mean the need to balance the conflicting obligations that exist within the banking industry.

On the domestic front, the author identified the macro-economic and political factors such as the institutional, regulatory and socio-political environment as capable of impacting negatively on effective corporate governance of corporations. On the legal and regulatory environment, the author considered how the Central Bank of Nigeria, Nigerian Deposit Insurance Company, the Companies and Allied Matters Act, the Structural Adjustment

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30 Ibid. at p. 48.

and deregulation measures or policies could impact either positively or negatively on effective governance and management of corporations. The crucial nature of the political, economic and social environment is further identified by the writer. He identified a link between effective governance and appropriate political and government structure as well as friendly political philosophy. The author submitted that the external environment is dominated by the volume and direction of trade flows, external debt profile and the effect of globalization which are critical and weighty enough to shape positively or negatively the effective governance of banks in Nigeria.

"Crisis Management at the Board of Insured Banks",[31] is the caption of John Ebhodaghe's piece in chapter seven of the book. Ebhodaghe took a surveillance of the crisis situation in the Boards of Nigerian banks and identified lack of understanding of directors roles, inaccurate and unreliable information by management for Board use in decision making, violation of legal provisions and rules regulating the Board; lack of regular and adequate legal guidance and counselling at the Board and multiple directorship as factors responsible for Board room crises. Though he sees the bank management as the primary organ capable of resolving crises at bank Boards, he noted however that where this becomes impossible, the regulatory and supervisory authorities have the obligation to take necessary action to protect the interest of interested parties such as depositors, creditors, and the general pubic. The contribution of Ebodaghe is a pointer to the unhealthy happenings

[31] Ibid. at p. 64.

at Nigerian boards and together with the contributions of Professor Nwankwo, Eguonu, Atoki, the deep seated problems affecting Nigerian Boards are laid bare. But fails to suggest appropriate remedial measures.

Chief J.A. Oduyemi's contribution touched on "**Corporate Accountability**",[32] in corporate entities in Nigeria. He examined accountability from the standpoint of not only the prevention of fraud and misappropriation but also ensuring high performance of corporate bureaucrats arising from the perfection of corporate goals and objectives through reliable and regular management information flow system. He considered the role of auditors, audit committees, and accounting standard Boards in ensuring effective corporate reporting and accountability. The author recommended strong internal control departments; effective and independent audit committees, as Leeways towards ameliorating the problems of ineffective corporate governance and management and the nagging problem of inflation accounting. The contribution of this author though commendable has not addressed the problems associated with distress syndrome in the corporate terrain in Nigeria which more than ever before has become complex.

Professor Peter Umoh is also one of the contributors in the book under reference, in his article "**The Problems of Corporate Governance in the Nigerian Banking Industry"**[33] he identified pressures for unwarranted favours, government negative actions, in exemplary Board and management

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[32] Ibid. at p. 75

[33] Ibid. at p. 100.

relationship, ownership crises, inadequate funding and a host of other factors as the root causes of ineffective corporate governance in the Nigerian banking industry. The author is however unable to examine the problems associated with Nigerian Boards structures as currently obtained and what should be done to ensure the Boards relevance as the engine room for effective corporate governance.

Richard Smerdon's book "**A Practical Guide to Corporate Governance"**,[34] is an all encompassing work that has touched on major corporate governance and management issues though mainly from the perspective of United Kingdom companies. The author in chapter one examined the objectives of effective corporate governance from the view point of 'shareholder' value and 'stakeholder' theory. But he admitted that these objectives have been assailed by other writers who have argued that there is polarization of theories as between 'shareholder value' and 'stakeholder' protection. The author noted that effective corporate governance is judged mainly in terms of the performance of the firm but debunks the generally held view that there is an overwhelming convincing link between performance and effective governance. He observed that the presence of directors with large personal shareholdings and an effective chairman have positive bearing on the performance of the corporation rather than the presence of large number of independent directors. The author drew a correlation between effective

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[34] Smerdon, R. A Practical Guide to Corporate Governance (2nd Ed.) (London: Sweet & Maxwell, 2004)

corporate governance and high culture of disclosure; strong rights and equal treatment for shareholders; and a significant number of 'independent' directors including financial specialists on the Board.

In chapter two, the author suggested benchmarks for determining the effectiveness of the Board as embodied in the combined code on corporate governance, and the Higgs Review. He considered the qualities of an ideal board which he said consist of a group of experience and talented individuals.

The author evaluated the duties and liabilities of directors and noted that the whole essence of corporate governance rests on the shoulder of directors. The chapter emphasized the objectivity and subjectivity test for determining the liability of directors with respect to the duties of care and skill, but concluded that the current leaning and preponderance view and evidence in many jurisdictions is to ignore the subjectivity test in favour of the objective one.

Chapter five which is titled "**The Non-Executive Director"** discussed the peculiar and unique position of non-executive directors in corporate governance as well as the qualities required of him as a director within the context of Cadbury, Hampel, Higgs and the combined codes of best practices. The contributions of the executive directors to the development of company strategy as well as scrutinizing the performance of management is considered. The chapter captured the unsatisfactory situation where most non-executive directors and chairman of corporations lacked training or development. The

authors observed the fact that non-executive directors as the custodians of the governance process should be reserved for the professionally minded persons.

The "**ROLE OF THE CHAIRMAN"** in corporate governance is the focus of chapter 6. The author dwelt on the corporate interrelationship between the chairman and important stakeholders, such as shareholders, and the managing director from the standpoint of the combined code.

In Chapter 12, the role of the Company Auditor and the Audit Committee is given some prominence. The author traced the history of the corporate scandals that have trailed the heals of the company auditor in the 1980, 90s and the early part of the 21st century and fingered the unhealthy affinity between the auditor and management as one of the impediments hindering the auditors performance. The author discussed the various mechanisms suggested by the 1998 combined code, the government and the accounting profession, the Cadbury and the Hampel Committee which unanimously and substantially agree that "a periodic change of audit partners should be arranged in order to bring a fresh approach to audit". The chapter captured most of the inhibiting factors militating against the auditors performance. The essence of the chapter is the author's position that the framework and the legal environment in which the auditor has operated has not been conducive to provide him the objectivity which shareholders and the public require of him in discharging his functions. The author reviewed the role of the Audit Committees which among other things is to ensure integrity in financial reporting and the audit process. The only limitation to this work is

that it has not the benefits of considering the subject matter from the perspective of Nigeria and possibly other less developed countries.

Mamman Hassan and Oluyemi Sunday,[35] see the major causes of banking crises and failures from the angle of mismanagement and illegal activities such as fraud and embezzlement. They traced the poor state of some banks to a complex set of interrelated factors such as the micro-economic and the macro-economic factors. They identified the significance of interrelated factors such as human asset resources in banks, capital adequacy, asset quality, management quality, earning capacity and liquidity as indices for determining the viability of banks but are quick to assert that management quality underlined all other factors. In their analysis, they argued that the reasons for poor quality performance by banks are traceable to lack of adequate inspection unit, inadequate Internal Audit Department, inadequate co-ordination of banks activities and rampant fraud and forgeries. They also identified possible situations to include a review of the existing policies on appointment to the board's improvement in the selection of banks key management staff, sound training programmes for management, constant banks staff/management audit programmes. This is an important research material which has examined the problems of ineffective corporate governance from the perspective of the banks. The article, regrettably took a less than cursory look at the Nigerian legal environment and the boards structure in

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[35] Mamman, H; "Banks Management Issues and Restoring the Health of Nigerian Banks through Improving the Quality of Management/ Employees" N.D.I.C. Quarterly Vol. 4 No. 4 1997.

their analysis and treatment of the subject matter thus robbing their contribution of much of the balance required in the process.

Suzan Chua in her own article titled: **"The Auditors Liability in Negligence in Respect of the Audit Report"**[36] discussed the statutory and professional basis for directors and auditors obligations to prepare and audit corporate accounts, and the standard and duty of care expected of company auditor. An attempt is made to review extensively existing case law and common law position and highlighting in the process the palpable low standard of care expected of auditors. The authors approach has however ignored regrettably the human aspect of the auditors problems.

Dr. Ahmed Abdullahi, article captioned "**The Company in a Changing Environment",**[37] evaluated the significance of Annual General Meeting in corporations but noted that it is now more of a stage managed event and an event of little value. The writer called for a review of CAMA in order to ensure greater and meaningful participation of shareholders in companies affairs. The authors contribution in his write up can at best be said to be an abridged commentary on the role of general meetings in corporate governance. No attempt is made by the writer to explore the ramifications of the subject matter. This, no doubt has robbed the treatment of the subject matter of some relevance.

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[36] Chua, S., "The Auditors Liability in Negligence in respect of Audit Report" (1995) Journal of Business Law.

[37] Abdulai, A.; "The Company in a Changing Environment". The Nigerian Business Law and Practice Journal Vol. 2 No. 2 1990.

CHAPTER TWO

CONCEPTUAL FOUNDATIONS OF CORPORATE GOVERNANCE AND MANAGEMENT IN NIGERIA

2.1 INTRODUCTION

This chapter examined some fundamental aspects of Company Law generally. This, the chapter examined the meaning, kinds and types of companies operating in Nigerian commercial landscape and the necessary conditions for establishing them in Nigeria. It also embarked upon the historical analysis of the background of Nigeria Company Law. The close affinity between Nigeria as a former colony of Britain and Britain itself, and the resultant influence which it had on Company Law in Nigeria is explored. Again, important but often misunderstood terms such as 'Shareholder' and 'Member' of companies will be dealt with.

The Memorandum and Articles of Association of a company are two most important documents in the life of a company as a commercial organization. While the former defines the powers and duties of a corporate entity, the latter regulates internal management matters of a company. The importance of these two documents, their relationship to one another, and their combined effect upon incorporation, will be thoroughly analysed.

Finally, the chapter examined the legal and practical implications of the all-important concept of corporate personality in Company Law. In summation, the chapter's significance lies in laying the foundation for the subject matter of this thesis.

2.2 THE MEANING OF THE TERM "COMPANY"

The word "Company" is a phrase that is commonly used and abused especially, in relation to business concerns. For instance, a sole business enterprise or even a partnership are sometimes loosely called a company, though, not a limited liability. Thus, the definition of the Word Company has not been quite an easy task. Most authors have tended to avoid a comprehensive definition of the term. This is not unconnected with the close affinity between registered companies and other business concerns. Allied to this, is the need to avoid some practical problems which an attempt at a comprehensive definition might engender.

Nevertheless, in the modern sense, the traditional legal definition of a company is that it is an association of a number of persons for a common purpose and usually for the principal reason of carrying on a business with a view to making profit or gain. Essentially therefore, a company is an association of persons known as the company's members, who have teamed up with the purpose of conducting its business or carrying on other activities in the company's name or association, by whatever name it is known. This definition is on all fours with that provided by Professor L.C.B. Gower,[1] a leading and distinguished English author on Company Law. In Gower's opinion, while the word 'Company' may not have an all exclusive legal meaning, the word connotes an association of a number of people for some common

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[1] Gower, L.C.B. "Principles of Modern Company Law", 5th Ed. (London: Stevens & Sons, 1998) p. 3.

object(s) solely for economic reasons. Gower's definition is not quite different from others.[2] Section 19 of the Company's and Allied Matters Act, (hereinafter called the CAMA) appears to have statutorily recognized Gower's definition from the perspectives of "profit", "gain", "business" and "association".

It is however important to point out that the three main features of the definition i.e. membership, object and profit are also true of entities like unincorporated businesses. But the main attribute, which distinguishes a limited liability company from unincorporated ventures, is that of registration. Even then, it has been recognized that these definitions are still deficient in many essential aspects. For instance, the idea that a company is incorporated for economic or profit purpose is not realistic. A company could be incorporated for the sole purpose of charity without any regard for profits. Again, the CAMA, recognizes Guarantee Companies which are non-trading companies and for which members are barred from sharing profits.

Another observation is the fact that the definition has failed to take cognizance of the all-important distinction between members of a company and the management. Though admittedly, these observations have some basis in truth, it is submitted that rather than being unduly troubled by this problem of definition, it would suffice to retain the existing ones as working definitions rather than running into the temptations of attempting a definition that is inelegant, and superfluous, in all its ramifications.

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[2] For instance, see Burke, John "Osborns Concise Law Dictionary", 6th Ed. (London: Sweet & Maxwell, 1976). P. 83, where it is defined as "An association of persons formed for the purpose of some business or undertaking carried on in the name of the association each having the resort of assigning his shares subject to the regulation of the company.

Most companies are incorporated under the provisions of the CAMA, but it is equally possible legally to incorporate a company by an act of the National Assembly or the States House of Assembly. A company possesses a legal personality which makes it quite distinct from those of its members as well as a partnership.

Generally, the idea of the company as a strictly legal entity had its genesis under the English legal system under which companies were either categorized as chattered companies – those brought into being by the grant of a special chatter from the British Crown, or Statutory Companies – those formed under an Act of Parliament. Statutory Companies derive their existence from the Parliament either under a general enactment or a specific enactment.

All the aforementioned types of companies share basic similarities in terms of legal framework, organization and consequences. In Nigeria however, owing to the increasing ascendancy and importance of registered companies, both statutory and chattered companies have assumed a less significant role in modern times.

It is quite pertinent to highlight some of the distinctive qualities of registered companies which partnerships, as a form of business organizations lack. Both partnership and registered companies are the most popular business organizations the world over. They share some striking features. For instance, both emphasize group of persons carrying on business in common and for economic reasons; the only difference being however that while

registered companies are registered and incorporated under the CAMA, a partnership is ordinarily not registered unless it is a limited partnership.[3]

In specific terms, the differences may be looked at firstly from the point of view of formation requirements. Here, a partnership is implied by law with little or no formality. In the case of a company however, the formation requirements are somehow rigid. For instance, registration is filing of the Articles and Memorandum of Association in addition to other important documents.

Secondly, a company upon registration acquires a separate and distinct corporate personality different from its members. Thus, it can hold property, sue and be sued in its own corporate name. But a partnership has no independent existence apart from its partners. However, it can be sued in the name of the partnership.

Thirdly, inspite of the fact that both partnership and company have the same legal minimum membership of two, members or partners in a banking business shall not be less than 10 and for other partnership 20. In the case of public companies however, it has no maximum membership while for private companies, the maximum is 50.

Again, the liability of partners is unlimited in the case of partnership whereas in the case of companies limited by shares, the liability of members is limited to the amount of shares subscribed for by a member.

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[3] S. 1(a) of the Partnership Act 1890 and S. 19 of the CAMA

Furthermore, while the *ultra vires* doctrine is dominant in company law, it has no place in partnership law since partnership agreements are alterable by the consent of the parties.

Another distinctive feature which draws, a demarcation between a company and a partnership is that an interest in a partnership is not transferable without the prior consent of all the partners. In the case of companies however shares are freely transferable subject however to some restrictions that might be imposed by the articles of association in the case of private companies.

The issue of the right to participate in management constitute another high point in the distinction between partnership and incorporated companies. While every partner has the right to take part in management except otherwise agreed, in the case of companies, the power of management is that of the Board of Directors.

Other features peculiar to companies are the consequential right of perpetual succession, the right to give securities on assets both fixed and floating; the right to raise capital in open market; and the mandatory requirement to fulfil rigorous statutory formalities such as filing of annual returns with the Corporate Affairs Commission. As for partners, except otherwise agreed, the death or insanity or bankruptcy of partners automatically brings to an end the partnership and in the case of statutory formalities the partnership does not make provision for such. Finally, with regard to securities, a partnership can only provide securities on fixed assets.

2.3 HISTORY OF NIGERIAN COMPANY LAW

2.3.1 The Evolution of the Modern Company

Before the 18th century, trading concerns were of two forms, one being by way of a Royal Charter of Incorporation which was regarded as time consuming and difficult, the second, through the process of unincorporated associations or partnership, as it is now known. Both however lacked the incidence of incorporation. Most companies at that period adopted the looser and less controllable unincorporated association. The consequences and disadvantages of such associations was seen in 1720, when a company known as the South Sea Company attempted an ambitious and speculative scheme[4] involving the acquisition of the British National debt, a scheme which crashed disastrously causing thousands of investors unquantifiable loses. The result was the subsequent enactment of the Bubble Act of 1720 which then sought to compel trading companies to avail themselves of the corporate form of business organizations rather than the unincorporated version. But the Bubble Act turned out to be a legislative disaster. Thus instead of restricting the proliferation of unincorporated associations, it actually promoted them. The reason was not unconnected with the fact that Royal Chatters had become increasingly more difficult to obtain than the pre-bubble Act era.

By the middle of the 18th century, the Deed of Settlement Company[5] as the most visible form of domestic company came into the business horizon. This was a system whereby members of a company were all required to append their signatures to such deed. The practical effect of the deed, upon

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4 It is also commonly known as the South Sea Bubble of 1720

5 This was used to avoid the Bubble Act but proved unsuccessful.

signing was that, the members were deemed to have agreed to carry on business in common and settle assets of the company on thrust for the same reason. The deed of settlement also made provision for a set of Governors (later known as Director) to take charge of the company's affairs and a set of trustees who have to manage the company's properties. Inspite of the obvious advantages of the Deed of Settlement type of companies, it lacked certain basic incidences of incorporation, as it could not sue and be sued. Thus stripped of the most basic attributes of incorporation, it was clear that investors were in a serious dilemma. They therefore agitated for a repeal of the Bubble Act. This clamour finally yielded dividend in 1825. The repeal of the Act necessitated the enactment of a much more simple and amenable registration procedure. This came in the form of the Joint Stock Companies Act of 1844 and the disappearance of the deed of settlement company.

Though the company was now a legal person following the enactment of the Joint Stock Company Act of 1844, the court still held on to the partnership analogy in its approach to business enterprises,[6] a tendency that was clearly at variance with the distinct legal personality of a company. This sordid state of affairs had a telling effect on the relationship between shareholders and directors. Thus, the General Meeting was synonymous with the company while the directors were merely the agents of the company and subject to the control of the company at the General Meeting. This ran counter

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6 Shephard, J.S. "The Law of Fiduciaries", (Toronto Canada: The Casswell Co. Ltd. 1981), p. 350.

to the incidence of distinct legal personality which the law fostered on the company.

This was the unsavoury position until 1906 when the English courts came up with the indoor management rule, a rule which sought to explain the fact that a company being an artificial legal person, has distinct powers which are shared between directors and shareholders,[7] and each serving as the watchdog over the other.

2.3.2 Development of Company Law

What is now known as the entity of Nigeria was a former colony of Britain. Thus most of the laws including Nigerian Company Law in operation in Nigeria today were influenced by laws derived from Britain.

Prior to 1876 however, there were companies operating in Nigeria, although there was no legal framework under which such companies operated. Such companies were all foreign in nature and enjoyed foreign rights and privileges. This was the position until 1879 when the Supreme Court Ordinance of that year was promulgated. With its promulgation, the Common Law, the doctrines of equity, the statutes of general application that were in force in England on the 24th day of July 1874 were received and made applicable in Nigeria. Thus those aspects of the English Common Law, the doctrines of equity and the statutes of general application which were relevant to and

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7 Shaw Ltd V. Shaw (1935) 2 K.B. 113 (CA) of p. 134.

concerning any area of company law in Nigeria were received and made applicable in Nigeria.[8]

The Companies Ordinance (Act) of 1912[9] was the first indigenous enactment in respect of companies in Nigeria. This enactment was initially limited in its operation to the Colony of Lagos, but was subsequently amended and extended in its operation to the entire country.[10] One essential attribute of this enactment was the fact that it was able to provide the necessary guide and procedure for the incorporation of companies in Nigeria. Another discernable feature was the fact that it was a derivation of the English Companies Act of 1908. Initially, the ordinance applied only in the Colony of Lagos until 1917 when it was amended and its territorial jurisdiction enlarged to cover other parts of the country.

The Companies Ordinance of 1922 followed. This consolidated and reenacted the Ordinance of 1912 and that of 1917. The Act witnessed series of amendments in 1929, and 1954 respectively and was eventually incorporated into the 1958 edition of the Laws of the Federation.[11]

Prior to 1968, the Ordinance of 1922 governed corporate business in Nigeria. But its subsequent inability to cope with surging economic activities after independence necessitated its repeal with the promulgation of the Companies Act 1968.[12]

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8 An example of such Statute is the Companies Act 1862.

9 Vol. VIII of 1912: S. 626(C) of the CAMA.

10 Companies (Amendment and Extension) Act 1917.

11 As Cap. 37.

12 S. 396(1) of the 1968 Act. See also Adaptation of Laws (Redesignation of Decrees) Order 1980 by which all Decrees are to be cited as Acts.

The 1968 Act was tailored after the 1948 English Companies Act and the Jenkins Committee Report.[13] The problem with the Act was that it could not deal effectively with the problems which emanated from the nations economic activities due to the upsurge of a number of companies. Secondly, the Federal Government's overriding need to promote the indigenisation of enterprises in Nigeria through an appropriate legal framework further accentuated the need to repeal the 1968 Act with a view to ensuring that the law responds effectively and efficiently to the problems associated with the rapid development of the nations economic activities as well as protecting the interests of the investors, the public and that of the nation as a whole. [14] Consequently, the Federal Government mandated the Law Reform Commission to carry out a far-reaching review and reform of Nigerian Company Law as well as the registration of Business Names Act of 1961 and the Land (Perpetual Secession) Act Cap. 98.[15]

The CAMA 1990 which was the product of the reform efforts was originally meant to commence on 2nd January 1990, but could not until October 1990 when the Federal Government enacted the companies and Allied Matters (Amendment Decree) No. 32 of 1990. The Act applies to all companies formed and registered under it; all existing companies; all companies incorporated, formed or registered under other enactments as well as

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13 See Jenkins Committee Report Cmnd 1749 (1962) and Tables 1 and 2 of the Act 1968.

14 See Working Papers on the Reform of Nigerian Company Law, Vol. 1, p.3, para. 9.

15 Some of areas which the reform highlighted for instance are the establishment of Corporate Affairs Commission to administer the Company Act and other counterpart statutes such as the Registration of Business Names Act; the incorporated trustees Act (i.e. the Land Perpetual Succession Act Cap. 98), Abolition of Non-voting Shares and Weighted votes; prohibition of guarantee company with share capital and unlimited company without share capitals etc.

unregistered companies.[16] Under Section 624 however, Trade Unions and employees of such trade unions are expressly excluded from the operational scope of the Act.

2.4 PRESCRIPTIONS FOR ESTABLISHING A COMPANY UNDER NIGERIA LAW

Under the CAMA, a minimum of two persons is required for the purpose of establishing a company irrespective of whether it is a public or private company.[17] Under the Company's Act of 1968, the Act required a minimum of seven persons for the purpose of establishing a public company and a minimum of two for private companies. The limitation placed on public companies has now been done away with under the CAMA.[18]

The 1968 Company's Act was silent on the capacity of persons who desire to establish a company or become or remain as members of a company. The Common Law was the only relevant law regulating the subject. The Common Law recognizes a person under the age of 21 years as an infant. The infants' contractual rights are circumscribed under Common Law. The Nigerian Law Reform Commission took cognizance of this limitation as constituting an obstacle to the running of business through the medium of companies. Where the Articles of Association permits, an infant can enroll as a member of a company by either subscribing for the company's shares or by outright purchase of such shares. Where the infant becomes a member by virtue of subscription or purchase he thereby becomes bound by the general common

16 Part 1 and 2 of CAMA.
17 S. 93 of CAMA
18 S. 18 of CAMA.

law rules of contract. Any contract of allotment or purchase of shares is voidable at the instance of such infants, since shares are not necessaries. Thus an infant may avoid such contracts within a reasonable time after attaining majority or avoid it before attaining majority.[19] The infant however cannot legally recover any price paid under such a contract except there is a complete failure of consideration. In the event of an infant acquiring shares from an owner and failing to repudiate liability for calls[20] on such shares, the company cannot generally repudiate the transaction though the transaction will be liable for the calls. But where a company is in the process of being wound up and the buyer of shares is an infant, the liquidator can exercise the infants' rights to avoid the transaction on his behalf. This was the position until the Law Reform Commission critically analysed the problem posed by infants participation in company investment and came out with some far reaching recommendations. In doing so, the Commission also examined critically the contractual capacity of mentally disordered persons, undischarged bankrupts and persons convicted of offences against corporations.[21] An aspect of the report of the Law Reform Commission found expression under Section 20 of the CAMA which now severely restricts the capacity of individuals who are to incorporate companies. Thus, those ineligible to form a company are:

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19 Steinberg V. Scala Leeds Ltds (1923) at p. 450.

20 A call is a demand upon the holder of partly paid up shares in a company for payment of the balance or an instalment of it by the company itself or of the company i.e. in Liquidation by the Liquidators. See also Lumsden's case (1868) L.R. 4 Ch. App. 31.

21 Working papers on the Reform of Nigerian Company Law, pp. 21 – 22.

(a) an infant who is less than 18 years of age. But such an infant will not be disqualified if other persons not disqualified have subscribed to the Memorandum of Association;[22]

(b) an individual adjudged to be of unsound mind;

(c) an undischarged bankrupt;

(d) any individual disqualified under Section 254 of CAMA from being a director of a company. Thus where a person is convicted by a High Court of certain corporate offences, such a person stands to be restrained in accordance with Section 254 from participating in the management of a company for a period not more than 10 years;

(e) a corporate body in liquidation.[23]

Generally speaking, an alien or foreign company can incorporate a company in Nigeria except where he is or it is inhibited by certain disabilities as may be imposed by an existing law at any point in time.[24] The various statutory restrictions imposed by law are aimed at protecting the national economy as well as availing Nigerians the opportunity of engaging profitably in economic activities. The 1999 Constitution of the Federal Republic of Nigeria has given tacit recognition to this fact by empowering every citizen of Nigeria to carry on any business of his or her choice either as an individual or as a member of a group, though subject to such restrictions as may be imposed by any relevant law.

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22 S. 20(2) of the CAMA.

23 S. 20(1) (3) of CAMA.

24 For instance, The Immigration Act 1990; The Investment and securities Act 1999; The National Investment and Promotion Act, 1995.

The relevant statutes which impose restrictions on aliens may now be briefly examined.

(a) **Immigration Act 1990**[25(a)]

Section 8(1) (b) of the Act provides that any foreigner or alien wishing to practice a profession or establish or take over any company with limited liability in Nigeria either on his own account or in partnership with any other person must seek and obtain the consent of the Minister of Internal Affairs in writing. The consent is mandatory where amongst other things, the alien intends to go into a joint venture with a Nigerian citizen or association; intends to subscribe to the Memorandum of Association of a company; wants to acquire shares or have shares transferred to him. The consent is also required where a Nigerian based company seeks to employ the services of an alien as an employee.

The permit is categorised into three viz:

(i) Residence Permit: This permits the foreigner the right to reside in the country where by the nature of the business he is going to transact in Nigeria he must reside in Nigeria to do the business.

(ii) Business Permit: This allows a foreigner to carry on business in Nigeria.

(iii) Expatriate Quota: This requirement entails that the number of foreigners to be employed by any company or partnership must receive the permission of the Minister of Internal Affairs in

25(a) Cap. 171 1990.

writing. The initial expatriate quota is normally obtained along with the business permit.

Expatriate quota are of two types, viz:

(iv) Temporary expatriate quota: Under this category, the group of Foreigners affected are Directors and other allied employees of companies and partnership where such employees are given an initial grant of five years subject to a further renewal period of two years.

(v) Permanent Unit Reviewed (PUR):

Under this category the employees of the business enterprise such as chairmen of the Board of Directors, the Managing Director and Chief Executive Officer are the beneficiaries.

(b) **Foreign Exchange (Monitoring and Miscellaneous Provisions) Act 1995**

This Act repealed the Exchange Control Act of 1967. Before any foreigner or multinational corporation can fully do business in the Nigeria market, it must do so through the instrumentality of the foreign Exchange Market. Under the 1995 Act, there is no need to ask for the approval of the Minister of Finance before an alien can import capital into Nigeria to invest in any enterprise. All that is needed is for the alien to apply to a licenced capital agent called an authorised dealer under the Act and a certificate is issued under the autonomous foreign exchange market.

The Act provides guidelines in dealings of the foreign exchange market. The principal aim of the Act is the promotion and protection of foreign and local investments in the Nigerian economy. The Act thus authorises the operation of foreign currency domicilliary account which mandates any person based in abroad or Nigeria, whether a citizen or foreigner to trade, deal in and invest in securities in the Nigerian capital market or by private placement in Nigeria.

(c) **Investments and Securities Act 1999.**

The Investment and Securities Act repealed the Securities and Exchange Commission Act 1988. The Act requires all transfer of shares or allotment of shares to be registered with the Commission. Thus where an alien participates in an enterprise in Nigeria by virtue of the fact that he is a shareholder of that enterprise, be it public, private, unlimited or even partnership, no security shall be issued, sold or transferred unless the prior permission or approval of the Commission is sought and obtained. The essence of this is to ensure that Nigerians are not unduly used as fronts by aliens.

(d) **National Office of Technological Acquisition and Promotion Act 1990.**

Under this Act, any agreement between aliens and Nigerians involving transfer of technology must be registered within six months of the agreement otherwise it shall be devoid of legal force. Matters relating to transfer of technology include:

(a) The supply of the use of trade mark.

(b) The right to use patented inventions.

(c) The supply of technical expertise.

(d) The supply of basic or detailed engineering.

(e) The supply of machinery and parts; and

(f) The provision of operating staff or managerial assistance and the training of personnel.

(e) **Industrial Inspectorate Act 1990**

This Act provides for the registration and evaluation of all plants, machinery or equipments to be imported into Nigeria by a foreign investor. The objectives of the Act is to ensure that such foreigners obtain the relief of capital allowance as well as preventing the over-valuation of imported capital equipment into the country.

(g) **National Investment Promotion Act of 1995**

This Act repealed the Nigeria Enterprises Promotion Act of 1989. The 1989 Act had also replaced the 1977 indegenization Act. Under the 1977 Act enterprises were grouped into the followings:

i. Category A: Enterprises under this head were received exclusively for Nigerians.

ii. Category B: Enterprises falling under this head were divided in the ratio of 60% for Nigerians and 40% for foreigners.

iii. Category C: Under this head enterprises were shared out in the ratio of 60% for foreigners and 40% for Nigerians.

The 1989 Act came to remove the restrictions thus making it possible for aliens to invest in any enterprise where the paid up share capital is not less than ₦20 million. However, the 1995 Investment and Promotion Act has removed the requirement of ₦20 million and there is no restriction any more except enterprises listed on the negative list such as production of military uniforms, narcotics and drugs, arms, ammunitions as well as petroleum enterprises.[25(b)]

The Act established a commission known as National Investment Promotion Commission. All foreign enterprises or investment must register with the Commission and the Commission is expected to keep such a register.[25(c)] The registration enables such foreign investors to freely transfer any funds in respect of any transaction abroad through an authorised dealer bank in free convertible currencies.

Section 25 of the Act also provides to the effect that no such enterprise shall be nationalised or expropriated.

2.5 CLASSIFICATION AND TYPES OF COMPANY

Under the 1968 Companies Act, now repealed, companies were mainly categorized into public and private. Then, a public company must have at least seven members. In the case of private companies, the minimum number was two. With regard to legal maximum, there was none for the public companies, whereas in the case of the private companies, it was fifty. While the 1968

25(b) S. 32 of the Act.
25(c) S. 19 of the Act.

repealed Act did not define comprehensively what constitutes a public company; it did in the case of private companies. For instance, under Section 28(1) of the Act a private company was one which its Articles *inter alia*, restricted the right to transfer its shares; limited the number of its members to fifty (excluding present and past employees of the company); prohibited any invitation to the public to subscribe for any shares or debentures of the company. These provisions were sacrosanct with respect to private companies, though it was possible to convert a private company to a public one by altering the articles to sidetrack the compulsory provisions of Section 28(1).

2.5.1 Public and Private Companies

With the enactment of the CAMA, the same statutory minimum number of membership for both private and public companies was introduced but the CAMA still maintained the distinction between public and private companies. Section 22(1) of the CAMA states that a private company is one stated in the memorandum to be a private company and that its Articles shall restrict any transfer of its shares. The maximum number of its members is fifty excluding bona fide employees. But where two or more persons jointly hold one or more shares, they are treated as a single member.[26]

A private company is prohibited from inviting the public to either subscribe for any shares or debentures of the company or deposit money for fixed periods or payable at call whether or not it bears interest.[27] These

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[26] S. 22(3) (4) of CAMA.
[27] S. 22(5) of CAMA.

requirements are mandatory since they constitute the very essence of the status of the private company. Default in this regard may lead to such private company forfeiting its privileges and exemptions.[28] In such a situation, the Act will apply to it as if the company were not a private company. However, the court reserves the right to hold otherwise where it is satisfied that the reason for such default was either accidental or due to inadvertence or to some other reasonable cause, or that viewed from another angle, it is unjust and inequitable to strip such private company of such privileges once an application is brought before it by an interested party.

2.5.2 Company Limited by Shares

A company limited by shares may be either a public or private company. Generally however, these types of companies constitute the largest type of companies. It is so called in that the liability of members in these companies are limited by the memorandum to the amount, if any, unpaid on the shares respectively held by them.[29]

2.5.3 Company Limited by Guarantee

This type of company is normally set up for purposes of promoting commerce, art, science, religion, sports, culture, education, research, charity, or other similar objects.[30] This type of company cannot be incorporated with

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28 S. 23 of CAMA where the court may relieve the company from such repercussions.

29 Liability may however be extended where a company carries on business with less than the minimum numbers of members or the authorize minimum share capital. See generally, SS. 93 and 99 CAMA.

30 See S. 20(1) of CAMA.

the purpose of carrying on business with a view of making profits and paying dividends to members.

The liability of a member is limited by the memorandum to such amount as the member may respectively undertake to contribute to the asset of the company in the event of its being wound up.[31] One important limitation as far as guarantee companies are concerned is the provision of Section 26(5) of the CAMA which prohibits the registration of the Memorandum of Association unless the consent of the Attorney General of the Federation is obtained.

Under the 1968 Companies Act, a guarantee company may or may not have a share capital. One of the innovations brought about by the CAMA is the prohibition of guarantee companies from being registered with a share capital.[32]

2.5.4 Unlimited Company

Under the 1968 Act, an unlimited company may or may not have a share capital.[33] But under the CAMA an unlimited company must be registered with a share capital which must not be below the statutory minimum of ₦10,000.00.[34] It thus becames mandatory that any existing unlimited company not having a share capital shall alter its memorandum to comply with the above requirement.

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31 S. 26 of the Act provides that the total liability of members to contributes to the assets of the company in the event of its being wound up should not at any point in time be less than N100,000.

32 S. 26(2) of CAMA.

33 Ss. 1(2); 2; 3; and 4 of the 1968 Act.

34 S. 25; S. 650, S. 99, and S. 27(2) of CAMA.

An unlimited company though a body corporate, essentially resembles a partnership since every member is personally liable in full for the debts of the company while still retaining its membership. From all indications, an unlimited company looks unattractive and therefore not a preference for investors.

2.5.5 Incorporated Trustees

An important innovation under the CAMA is the allowance of non-profit making organizations to be registered by the Corporate Affairs Commission[35] without necessarily going through the rigours of registration provided under Section 19 of the CAMA. Prior to 1990, such registration was only permitted under the Land Perpetual Succession Act of 1958. Though incorporated trustees enjoys the status of a body corporate and thus have perpetual succession upon registration, this has a limited effect since the corporate status is only enjoyed by the trustees and not the association.

2.5.6 Unit Trust

A Unit Trust is a kind of business organization, by which individuals agree to pool their resources together under a trust. Under such an arrangement members are each given units of shares to be managed by experts who are themselves under the control of Board of Directors. Before 1990, the consent of the Minister of Finance was required before a Unit Trust could be ventured into. The Corporate Affairs Commission has however down played this requirement and a Unit Trust must now be registered with the Commission. A Unit Trust is a block of investment carried on by incorporated

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[35] Ss. 673-695 of CAMA.

companies. The investment is usually vested in trustees under a trust deed and divided into beneficial ownership by way of shares which are described as units. One remarkable difference between an incorporated company and a unit trust is that in the case of the latter, they do not make their own investment decision, instead, they allow the trustees in whose lands they place their capital to invest on their behalf. But the unit holders as providers of capital are entitled to dividends or capital appreciation from time to time. Most investment companies today are classical examples of unit trust.

The unit trust kind of business organization is often the instrumentality by which public officials engage in blind trust arrangement concerning their private business interests. A blind trust arrangement is a legal arrangement where a public official puts his private business interest in the hands of trustees who protects and shields him from day to day business decision thereby avoiding potential conflict of interest with government decisions. It is thus tremendous importance to public servants in particular.

2.6 MEMBERSHIP OF A COMPANY

Some relevant sections of the CAMA clearly state the category of persons that are disqualified from being members of a company. For instance, Section 80 provides that a person of unsound mind or an undischarged bankrupt is not qualified to be a member of a company. However where such an insane or bankrupt person already held shares before the time of such disability, such shares shall become vested in his committee or trustee. This instrument of trusteeship or committeeship cannot translate to that of a

member of a company. To become a *bonafide* member of the company, the committee or trustee must take the required steps to do the necessary registration as the proprietor of the shares.[36]

Disability in the nature of unsoundness of mind deprives a member of the right to vote. In such a situation, his committee, when registered becomes vested with such right on his behalf.[37]

A corporate entity in liquidation is also disqualified from being a member of a company. Although, a company can be a member of another company, it is disqualified from being a member of itself. Thus a company is disqualified from dealing in its shares.[38] But it can purchase its own shares only under certain conditions[39] provided the necessary provision is made in its Articles and Memorandum of Association. Where such conditions are complied with the purchase must be made out of the profits of the company which would ordinarily have been available for purpose of dividend.[40]

As previously noted,[41] certain persons are disqualified from being members or subscribers of the Memorandum of Association, while on the other hand an alien or a foreign company may participate in forming a company for

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36 *Morgan V. Gray* (1963) Ch. 83 at p. 87.

37 The difference in attitude can perhaps be explained by the fact that while a bankrupt member is still in possession of his senses, and so can reasonably be expected to exercise it judiciously, the same cannot be said of the person of unsound mind.

38 See Trevor V. Whitworth (1887) 12 App. Cas. 409 where the rule was enunciated; see also S. 160 of CAMA which subsequently codified the rule.

39 For instance, where the purpose is to settle or compromise a debt of claim assented by or against it; elimate fractional shares; fulfil the terms of non-assignable agreement under which the company has an option; satisfy the claim of a dissenting shareholder to comply with court order.

40 S. 1161 of CAMA.

41 Supra at pp. 15-18 of this chapter. See generally S. 20 CAMA.

the purpose of trade or business in Nigeria subject to certain laws regulating the rights and capacity of aliens to carry on business in Nigeria.

The next focus is about what it takes to become a bonafide member of a company. Section 79 of the CAMA succinctly states with regard to the above that subscription to the Memorandum of a company is a clear undertaking that one has agreed to be a member of a company. Specifically, Section 79(1) of the CAMA provides that once a person has subscribed to the Memorandum of Association of a company, he is deemed to have become a member of the company as soon as it is registered. Section 18 also provides that at least two persons must subscribe to the Memorandum of a company, be it private or public company.[42]

Section 27(2) of the CAMA provides that subscribers to the Memorandum must take a certain number of shares whose value must not be less than 25% of the authorized share capital. But it is implicit in the decision *Onwuka v. Taymani*[43] that in a situation where a subscriber acquires the whole or any part of the shares subscribed for by him, not as beneficial owner but on trust for another person, he must disclose in the Memorandum that fact including the name of the person. Subscription to the Memorandum therefore constitutes the first method of becoming a member of a company.[44] It is important to emphasis that once the act of subscription is completed, such subscribers are deemed to have agreed to be members of the company. The

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42 This has clearly done away with the old distinction between a public and private company pertaining to minimum number of members needed to incorporate a company under the 1968 Companies Act which requires a minimum of seven in the case of public company and two in the case of private company.

43 (1965) L R 62 at p. 73.

44 Starcola (Nig.) Ltd. V. Adeniji (1973) 1 SC at p. 202.

act of subscription also automatically confers on such person full membership status.

The rule that mere subscription to Memorandum of Association gives right to both company membership and share holding is qualified under two situations. First, where the company fails or refuses to allot shares to subscribers which such subscribers had already signed for, they cannot be held liable for such shares.[45] For this exception to apply however[46] such shares must have been allotted to some other persons and there is nothing for the subscribers to take.

Another method of becoming a member of a company is by allotment and registration. Mere allotment of shares without registration does not give one the right to membership. Membership means entering ones name on the register of members.[47]

The generally held view is that the terms 'shareholder' and 'membership' are synonymous. Section 79(3) of the CAMA however contradicts this general view by providing that with regard to a company having a share capital that each member shall be a shareholder of the company and shall hold at least one share. The implication here is that mere entering of ones name in the register of members without allotment of shares will not entitle such a member to legal protection.[48] Both acts of acquisition and registration are

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45 See Gower, *Principles of Modern Company Law*, Supra at 427.
46 Odumody v. Mohammed (1973) NCLR 452 at p. 460.
47 Barleth Nig. Ltd. V. Mordi Francis (1987) NWLER 613.
48 S. 79(2) CAMA.

important except in the rare situations already seen where membership is acquired by subscription only.

From the above, it is clear that a member of a company with a share capital is a person who has proprietary interest called shares in a company and whose name has been firmly inscribed on the register of members. In the case of a company without share capital, it is clear that such members may not possess proprietary interest. For purposes of definition therefore, it would suffice to narrow the definition down to membership without reference to shareholding.

Where a person seeks, to acquire membership through transferred shares, until the transferees name is registered in the register of members, such a person cannot be regarded as a member of the company. An agreement to transfer is only valid as between the parties and not the company so much so that the shareholder whose name is on the register remains the shareholder notwithstanding that an agreement to transfer shares has been concluded.[49] But when the transferee's shares is eventually entered on the register of members it appears that rights and obligations begin to run from the date of transfer rather than the date of registration of such shares.[50]

A person may also become a member of a company on transmission, on death and registration in the company's register of members. [51] Usually such

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[49] See the observation of Lindley L.J. in Societe Generale de Paris V. Tranway Co. Ltd. (1844) 14 Q BD at p. 424.

[50] See Aouad & Kuma Tin Mines Ltd. V. Kessrwani (1956) 1 F.S.C. 35.

[51] See Tira Tore Press Ltd. V. Abina & Others (1973) 4 S.C. 63, where the court considered the legal status of representative who acquired shares by transmission.

persons are personal representatives. The personal representative has the right to determine whether or not he wants to be a member of a company. Where he elects to be a member of a company, he must send or deliver to the company a signed notice to that effect. On the other hand, he may choose to have another person registered. But to be effective, he must execute the transfer in the name of that person seeking the transfer of the share in his name. The validity of shares so transferred may be unaffected inspite of the fact that it was executed by a non-member personal representative.

Membership of a company confers certain rights and liabilities on a member. These rights are well spelt out under Section 81 of the CAMA. The section specifically provides that a member has the right to attend any general meeting of the company; to speak and vote on any resolution and this includes the right to receive notice. Thus failure to serve notice on a registered member render such meeting if held, a nullity.[52] Other ancillary rights of membership include the right to dividends; the right to seek redress against oppressive and unfair treatment and the right to apply to court or the Corporate Affairs Commission where possible. On the issue of member's liability, this may be looked at from two perspectives, namely, a viable company and a company in the process of being wound up. The issue of member's liability has already been dealt with.[53] It will suffice therefore to merely add that under certain circumstances a member's liability may be

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52 Musselwhite V. C.H. Musselwhite & Sons (1962) Ch. 964.

53 Supra at pp. 19-21 of this chapter.

increased where he personally consents to such increase,[54] or by carrying on business with less than two directors and doing so for more than 60 days [55] or by receiving dividends from capital.[56]

2.7 THE MEMORANDUM OF ASSOCIATION OF A COMPANY

The Memorandum of Association of a company is a document which determines what a company is empowered to do. A Company owes its existence and survival to it since it determines its capacity and responsibilities as a legal entity. The Memorandum as the constitution of the company can be altered to the extent permitted by the CAMA.[57]

The Memorandum of Association of a company normally contains the following, namely:

(a) The name of the company;

(b) That the registered office of the company shall be situated in Nigeria;

(c) The nature of the business or businesses that the company is authorized to engage in and in case the company is not incorporated for business purposes, the nature of the object or objects for which it was formed;

(d) The restriction if any, placed on the powers of the company;

(e) Whether the company is a private or public company;

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54 See S. 49 of CAMA. A member may agree in writing to be bound to accept increased liability.

55 See S. 246(3) CAMA. This liability can also arise where a company carries on business without having at least two directors. To be liable a member must be aware of this fact. In such a case the member is liable for all debts incurred by the company during the period.

56 Where a shareholder is aware of this fact and he receives dividends out of capital, he will be liable to return such amount paid out of capital. The company intending to recover this may sue him or directly from the directors who may in turn recover it from such a member by way of indemnity. See S. 386(2) CAMA.

57 For instance, Ss. 44(i) and 625(i) of CAMA.

(f) Whether the liability of its members is limited by shares, or by guarantee or unlimited in accordance with Section 271 of the CAMA.

Where a company has a share capital, the memorandum is further required to state that:

(a) The amount of authorized share capital shall not be less than N10,000 in the case of a private company and N500,000 in the case of a public company with which the company intends to be registered and the division of such amount into shares of fixed amount;

(b) The subscribers to the memorandum shall allocate amongst each of them a number of shares whose monetary value shall not be less than 25% of the authorized share capital; and

(c) That each subscriber shall write opposite to his name the number of shares he is taking, and where the subscriber is a trustee of the shares he is holding, he must also disclose such facts including the name of the beneficiary, in accordance with Section 27(2) of the CAMA.

Apart from the foregoing, the Memorandum must, where the company is a guarantee company, furnish such other additional informations to the effect that:

(i) The income and property of the company shall be applied only in respect of the promotion of its objects and that no portion of it shall either be paid directly or indirectly to the members of the company except with the permission of the CAMA. Section 26(4) states that Guarantee companies must not be set up with the sole object of making

profit or for purposes of distribution by way of dividends. In the spirit of Section 26(1) such companies are set up for the promotion of commerce, art, science, religion, sport, culture, education, research, charity or other objects of a similar nature. Any provision in the memo entitling such members to share in the profits of the company is void in accordance with the provision of Section 26(3). A breach of the aforementioned provisions creates liability jointly and severally on all such members and officers who are aware of the breach.[58]

(ii) Each member undertakes to contribute to the assets of the company in the event of its being wound up while he is a member or within one year while he ceases to be a member for payment of the debts and liabilities of the company and of the cost of winding up, such amount as may be required not exceeding a specified amount and the total of which shall not be less than N10,000.[59]

It is important to note that a new sub-section to Section 26 of the CAMA has been introduced by an amendment to the original Act to the effect that the Memorandum of Association of a company limited by guarantee cannot be registered unless prior approval is given by the Attorney General of the Federation.[60]

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58 Such members and officers will be liable to pay and discharge all the debts and liabilities of the company. Additionally, such member and officer will be liable to a fine not exceeding N100/00 for everyday during which it carried on business in accordance with Section 26(6) of CAMA.

59 S. 26(7) of CAMA.

60 S. 26(5) of CAMA.

Finally, every Memorandum of Association shall be signed by each subscriber in the presence of at least one witness who shall attest to the signature.[61] The Memorandum is also required to be executed as a deed.[62]

2.7.1 Name of Company

According to Section 29 of the CAMA, the name of a company must be stated in the memorandum. Specifically, the section requires that the name of a company must end with certain words, namely:

(a) Private company limited by shares must end with the words "Limited" or the abbreviation "Ltd".

(b) Public company limited by shares must end with the word "Public Limited Company" or the abbreviation PLC".

(c) Company Limited by guarantee must end with the words "Limited by Guarantee" or the abbreviation "Ltd/Gte".

(d) Unlimited company must end with the words 'Unlimited" or "Ultd". This distinctive ending words for the different kinds of companies were absent under the 1968 Act.

Where a person trades or carried on business under any name or title without adhering to the above requirements, he shall be liable for penalty to the tune of N50 for every day during which such name or title was used.[63]

Section 30(1) of CAMA, however provides that no company shall be registered if the name it sought to be registered is,

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61 S. 26(5) of CAMA.
62 S. 26(6) of CAMA.
63 S. 642 of CAMA.

(i) identical with that by which a company in existence is already registered, or so nearly resembles that name as to be calculated to deceive except where the company in existence is in the course of being dissolved and signifies its consent in such a manner as the Commission requires; or

(ii) contains the words "Chamber of Commerce" unless it is a company limited by guarantee; or

(iii) in the opinion of the Commission is capable of misleading as to the nature or extent of its activities or is undesirable, offensive or otherwise contrary to public policy; or

(iv) in the opinion of the Commission would violate any existing trade mark or business name registered in Nigeria unless the consent of the owner of the trade mark or business name has been obtained.[64]

Again, there are certain identifiable words the use of which is also seriously restricted by the CAMA owing to the fact that they are capable of misleading people into believing that such companies enjoy government patronage, favour or connection or that special privilege has been granted it by the government. These words are only restricted and could be used with the necessary approval of the government.

Section 30(2) of the CAMA clearly provides that no company may be allowed to be registered with such name unless the permission of the Corporate Affairs Commission is obtained. The words include:

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[64] S. 30(11) of CAMA.

(a) The words "Federal", "National", "Regional", "State", "Government" or any other word in which in the opinion of the Commission suggests or is calculated to suggest that it enjoys the government patronage or Government Department in the country; or

(b) Contains the word "Municipal" or "Chattered" or in the opinion of the commission suggests or is calculated to suggest connection with any municipality or other local authority; or

(c) Contains the word "Co-operative" or the words "Building Society", or

(d) Contains the word "Group" or "Holding".[65]

A company is also permitted to change its name under the CAMA. The two situations under which a company can change its name are:

(a) Where there is an inadvertent registration under a prohibited name;

(b) By passing a special resolution to change the name.

In the first instance, the registration may be the first of its kind or subsequent registration under a new name. As long as the registration is done under a name that is identical with that by which an existing company is previously registered or so nearly resembling it as likely to deceive, the approval of the Corporate Affairs Commission may be obtained by the defaulting company to change the offensive name. Sometimes, the quest to change after such inadvertent registration may be initiated by the Corporate Affairs Commission. The Commission may within 6 months of the default, after the defaulting company had registered the offending name direct it to effect

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[65] S. 30(2) of CAMA

the change.[66] The Commission may take the initiative and direct a company to change its name where such name is in conflict with an existing trademark or business name registered in Nigeria before the registration in issue. This is especially so where the consent of the trademark or business name owner was not obtained.[67]

In the latter case i.e. the second circumstance under which a company can change its name, Section 31(3) of CAMA provides that this can be done by passing a special resolution which must be approved by the Corporate Affairs Commission. The approval is subsequently followed by a notification in writing that the name has been changed. The Commission's approval may however be dispensed with where what is required to be changed is the substitution of the words "Public Limited Company" for "Limited" or vice versa or the conversion of a private company into a pubic company or vice versa. Usually a resolution of the Board of Directors is required before change of name can be effected.

A company is also entitled under the CAMA to preserve its name. Obviously, this is to prevent a situation where an intending name becomes unavailable in the process of incorporating such a company. The CAMA prescribes a maximum period of 60 days for which such a name can be preserved.

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66 In such a case the company must within 6 weeks from the date of that directive or such longer period as the commission may permit comply.

67 The Commission's directive is mandatory. Non-compliance subjects the company to a fine of N25,000 for every day during which the default persists. See generally, S. 31(2) of the CAMA.

2.7.2 Statement of Share Capital

Apart from the name of the company, the Memorandum of Association of a company limited by shares must state the amount of share capital which the company intends to be registered with and the value of each share into which the share capital is divided. This nominal/authorized share capital must not be less than the statutory minimum share capital.[68] In the same vein, the subscribers to the memorandum must take not less than 25% of the authorized share capital. A further requirement is that the issued shares capital of a company registered with a share capital shall not be less than 25% of the authorized share capital. Section 103 of the CAMA clearly fortifies the above requirement by further providing that where a company passes a resolution to increase its authorized share capital, the increase will be in vain except:

(a) Within 6 months of giving notice of the increase to the commission, not less than 25% of the share capital including the increase has been issued;

(b) The Directors have delivered to the commission a statutory declaration, verifying that fact.[69]

A company having a share capital may if it so wishes reduce, alter or increase its share capital. A company seeking to reduce its share capital can do so by special resolution which is subject to court's confirmation. Reduction of capital must however be authorized by the Articles of Association.[70]

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68 This is N10,000 in the case of a private company and N500,000 in the case of a pubic company.

69 S. 99 of CAMA stipulates stringent penalties for non-compliance with these requirements.

70 S. 106 of the CAMA

Similarly, a company may in a general meeting alter its share capital through various processes, namely, consolidation, division, conversion, reconversion, sub-division etc.[71] or increase it by new shares of such amount as it deems it.[72]

2.7.3 Object of the Company

The Memorandum of Association is also required to contain the nature of the business or businesses, which the company is permitted to engage in. Where the company is not incorporated for business purposes, then the nature of the object(s) must be clearly provided in the Memorandum. In accordance with Section 38(1) of the CAMA a company upon registration becomes vested with the powers of natural person while pursuing its authorized objects or businesses subject, however to any restriction which might be imposed by the Memorandum.[73]

The essence of disclosure of the object of a company is to ensure that the company is restricted to those objects in the interest of the creditors, and the corporation itself. Thus a company can only perform such acts that are authorized. The doctrine of *ultra vires* was developed to serve this end.[74] An act though legal in itself may be caught by the *ultra vires* doctrine if it is not authorized by the object clause in the Memorandum. Once an act of a company comes within the object clause, it cannot be invalidated on the basis

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71 S. 100 of the CAMA

72 S. 102 of the CAMA

73 A company however lacks the power to exercise either directly or indirectly, to make donation, give gifts of its property or donate fund to a political party or association as for any political purpose. See S. 38(2) of CAMA.

74 S. 39(1) of the CAMA which codifies the *ultra vires* doctrine.

that it was not made in furtherance of the business of the company.[75] The only leeway out of such a problem is for any member of such a company or a debenture holder, or his trustee to apply to court to restrain a company from doing an act that is not in furtherance of the object of the company under Section 39(4) of the CAMA.

A company's object can also be altered. Before such alteration, the company must give a notice in writing to all its members. Upon such a notice being given, such alteration can be done at the general meeting of the company upon the passing of a special resolution to that effect.

Where some members for whatever reason(s) apply to the court for the cancellation of an alteration, the court must equally confirm it otherwise, it is invalid. As a matter of procedure, an application for alteration is required to be made to court within 28 days after the date on which the special resolution was passed. Such persons entitled to apply are:

(a) The holders of not less than 15% in nominal value of the company's issued share capital, or a class thereof, or

(b) In the case of a company not limited by shares, by not less than 15% of the company's members; or

(c) The holders of not less than 15% of the company's debenture holders which entitles such debenture holders to object to alteration of its objects.

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[75] S. 39(3) of the CAMA.

Once a member has consented to or voted in favour of an alteration he can no longer be heard to oppose such alteration by a court action.

2.8 ARTICLES OF ASSOCIATION OF A COMPANY

The role of the Article of Association of a company is to provide detail regulations bordering on the internal affairs of a company. The Article of Association principally regulates the rights of the members inter se and clearly sets out the mode of conducting the company's affairs or business.

Under the 1968 Companies Act, the filling of the Articles of Association was optional. A company was required to either adopt the articles in the relevant tables or file a new one entirely. This is no longer so, as the CAMA now makes it mandatory.

In terms of form and content, Section 34 of the CAMA specifically provides that the Articles of Association shall be printed (not typewritten) and signed by each subscriber to the Memorandum of Association in the presence of at least one witness who shall attest to the signature. Under the said section, the Articles shall also be executed as a deed.[76]

There are four specimen Articles in Table A of Schedule 1 to the CAMA[77] depending on the nature and type of company concerned. But these are merely to act as a guide and no more.[78]

Where a company desires its name to be listed on the Nigerian Stock Exchange, the company must comply with special listing requirements while

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[76] See specifically S. 34(3) (4) of the CAMA.

[77] See S. 34(1) CAMA.

[78] S. 34(1) clearly states that they may be used with such "additions, omissions, or alteration as may be required in the circumstances".

preparing its Articles. The Articles contains such information as the classes of shares, commission and brokerage, alteration of share capital, meetings, voting, the seal of a company, notices, restriction on transfer of shares, pre-emptive rights of shareholders, membership of a company and so forth.

Under Section 34(2) of the CAMA a company limited by guarantee is specifically required to state in the Articles the number of members with which the company intends to be registered to enable the Corporate Affairs Commission determine the appropriate fees payable on registration.

Like the Memorandum of Association, the Articles is also subject to alteration or addition by special resolution. An alteration or addition is valid as if it was originally contained in the Articles.[79] An agreement to amend the Articles is ordinarily *intra vires* the company.[80]

The CAMA contains conditions, which must be complied with before any alteration by a company can be valid. The company cannot provide in the Articles to oust itself the power to alter the Articles. Any such purported regulation would be illegal since it would be contrary to the provision of the CAMA. The act of alteration must not conflict with any provision of the CAMA.

The power to alter the Article is generally depended on the conditions stated in the Memorandum. Hence, where both conflict the Memorandum would prevail having regard to the conflict.[81] The reason is that the

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79 S. 48 of the CAMA.

80 Cave v. Jones (1981) 1 All E.R. 533; Re Duomatic (1969) 2 Ch. 365; Re Oxford Motors Co. (1921) 1 K.B. 32.

81 Guinness v. Land Corporation of Ireland (1882) 22 CL.D. 349, Per Cotton L.J. Re Duncan Gilmour & Co. Ltd. (1952) 2 All E.R. 874.

Memorandum is the dominant document out of the two. Aside from areas of possible conflicts, both documents are contemporaneous which must be read together.

Generally speaking, alteration, or notices must be for the company's benefit. It is the company's prerogative to decide that fact and not the court except however it is shown that a purported alteration is expropriately or discriminatory in a given circumstance. In such a case such alteration may be declared invalid by the court.[82]

2.9 THE EFFECT OF MEMORANDUM AND ARTICLES OF ASSOCIATION OF A COMPANY

Upon registration with the CAC, both the Memorandum and the Articles of Association become public documents to be kept by the Commission. Thus any person may inspect them at the Commission's office and obtain necessary copies of them as the case may be in accordance with Section 634 of the CAMA.

Certified copies of both documents by the Commission are admissible in evidence in any proceeding.[83]

Before 1990, the doctrine of constructive notice, a common law rule, applied to ensure that any person that transacted a business with a company was deemed to have prior notice of both the Memorandum and Articles of Association of that company, and to have read and understood them. However, under the CAMA, the doctrine is no longer part of Nigerian Law,

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82 Brown v. British Abrasive Wheel (1919) 1 Ch. 290.

83 S. 634 of the CAMA.

obviously due to the inherent injustice in the doctrine.[84] Under Section 41 of the CAMA, upon registration, the Memorandum and the Articles create two types of contracts under seal. They are:

a. a contract between the company and its members and officers,

b. a contract between the members and officers themselves, whereby they agree to observe and perform the conditions contained therein, as altered from time to time.

As could be gleaned from the provision of Section 41 of the CAMA, the Articles and Memorandum of Association cannot impute a contract between the company and a third party. This is however a general statement. But a third party may be able to act as though a contract exist between him and the company, where for instance, the Memorandum and Articles empower a third party to appoint or remove any director or other officer of the company. In such a situation, the third party may be in a position to enforce such power, pursuant to Section 41(3) of the CAMA. Again, Section 41(4) provides that a third party or any person seeking to enforce any obligation owed to him under the Memorandum and Articles may bring a representative action to enforce such an obligation. This section is in material particular with Section 20 of the English Companies Act of 1948.

A number of cases have been decided to explain the situation in which the contractual rights created by Section 41 may be enforced by the courts. One of such cases is *Hickmen v. Ken or Romney Marsh Sheepbreedes*

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[84] S. 68 of the CAMA.

Association,[85] where the Articles provided that in the event of any dispute between the company and the members, the dispute must first be referred to an arbitration before it can go to court. The plaintiff, who did not comply with the above condition, when a dispute arose, was held bound by the Articles.

A member who complied with such a condition in *Woods v. Odesse Water Works Company*,[86] was held entitled to challenge a resolution passed by the company to pay dividends declared in the form of debenture instead of cash payments provided in the Articles.

The type of contract contemplated under Section 41 is enforceable amongst the members inter se. As explained by Professor Gower,[87] the principal occasion in which the right may be of practical significance arises when an Articles grants members a right of pre-emption or refusal when another member nurses the intention of selling his shares. In such a situation, Gower explains that a duty is imposed on other members to buy such shares of a retiring member. In *Borland's Trustee v. Steel Brothers & Co. Ltd*.[88] the above principle was exemplified. There the Articles provided that where a member becomes bankrupt, his shares should be sold at the current market value to certain named persons. A member subsequently became bankrupt and his trustees in bankruptcy refused to sell his shares to the named persons. The named persons successfully challenged the matter in court.

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85 (1915) 1 Ch. 881.

86 (1889) 42 Ch. 636; See also *Johnson v. Lyttle Iron Agency* (1877) 5 Ch. At p. 667, where a member successfully challenged the irregular forfeiture of assets contrary to the companies articles.

87 Gower, L.C.B, "Principles of Modern Company Law", Supra at pp. 316-317.

88 (1901) 1 Ch. 279.

Before now, it was the law that the rights and obligations of members provided in the articles must be exercised as a member qua member. The implication of this is that where a member is given a right in a capacity different from that of a member, such a right cannot be enforced in that other capacity. In *Eley v. Positive Government Security Life Association*,[89] the Articles provided that a member should be appointed as a life solicitor of a company. When the plaintiff was appointed, he was not a member of the company. He later became a member subsequently and his appointment was terminated. He relied on the provisions in the Article to sue the company. The court dismissed his action on the premises that he was attempting to sue to enforce his rights as an outsider. This is no longer the case. The correct position is that both a member and officer can now enforce contracts contained in the Memorandum and Articles of Association of the company in their capacities as qua member and qua officer respectively.

2.10 THE DOCTRINE OF CORPORATE PERSONALITY

Upon incorporation of a company, and the issuance of a certificate of incorporation, the company becomes a body corporate or a corporation. The necessary implication is that in the eyes of the law it is a person distinct from its members. It becomes a person with rights and liabilities in law. In the words of Lord Selbourne in *G.E. Railway v. Turner*,[90] upon incorporation a company becomes a legal entity "a mere abstraction of law".

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89 (1897) AC 299. See also S. 16 of the Companies Act 1968. But S. 41 CAMA finally settled once and for all the hitherto controversy surrounding the interpretation of S. 16 of the 1968 Act.

90 (1872) 8 Ch. 149 at p. See also Cotton, L.J. in Filterofts case (1882) 21 Ch. 519.

This concept of independent corporate personality which comes into effect upon the registration of a company is recognized statutorily under Section 37 of the CAMA, which provides that upon the date of incorporation, the subscribers of the Memorandum including such other persons who shall become the members of the company from time to time shall be a body corporate by the relevant name stated in the Memorandum of Association of that company.

The concept of independent corporate existence of a company was explained and emphasized by the House of Lords in the celebrated case of *Solomon v. Solomon & Co. Ltd.*,[91] which has since remained the *locus classicus*. In that case, Solomon had for years carried on a prosperous business as a leather merchant. In 1892, he decided to convert the business into a Limited Liability Company. He then formed Solomon & Co. Ltd. with himself, his wife and his five children as members. Solomon became the Managing Director of the newly established company. The company bought the business as a going concern for £33,000. The price was satisfied by £10,000 in debentures, conferring a charge over all the companies' assets, £20,000 in fully paid shares and the balance in cash. Seven shares were subscribed to in cash by other members. Consequently, Solomon held 20,001 out of the entire 20,007 shares that were issued and each of the remaining shares was held by a member of his family apparently as a nominee on his behalf. Shortly, thereafter, the company went into liquidation. Though the

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[91] (1897) ACC 22 at p. 51.

assets of the company were sufficient to discharge the debentures, there was nothing left for the unsecured creditors. The liquidator contended that since in reality, Solomon was in control of the company's business, the company was a mere sham designed to avoid his debt obligation while carrying o n the leather business. The liquidator further argued that Solomon be ordered to indemnify the company against its debt and that the payment to Solomon of the debenture debts owed him be halted until after the satisfaction of the company's other creditors. Both the High Court as well as the Court of Appeal upheld the Liquidators submissions but the House of Lords in contrast held that Solomon was not under any liability to the company or its creditors and that the debentures were valid against the company. The principle of corporate personality has been further applied and approved in a long line of cases some of which are, namely, *Lee v. Lee Air Farming*,[92] the Nigerian cases of *Marina Nominees Ltd. v. FBIR*,[93] *Dunlop Nigerian Industries Ltd. v. Forward Nigeria Enterprises Ltd. & Anor*.[94] to mention just a few.[95]

However, the House of Lords decision in Solomon's case has been subject to vitriolic attacks. While Professor Gower considers it as "Shocking", Professor Kahn Freund called it "Calamitous". It will be recalled that in *Inroad Haulage Executive v. Elrick*,[96] Lord Asquith's attempt at casting serious doubt on the ratio in Solomon's and other similar cases in the House of Lords in 1953

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92 (1961) AC 12 P.C.

93 (1986) 2 NWLR pp. 20-46.

94 (1976) A.C.R. Comm. 243.

95 See also Nigerian cases of *Olufasoye v. Fakorede* (1992) NWLR (Pt. 272) at p. 747; *Malafia v. Veritas Insurance* (1986) 4 NWLR (Pt. 38) at p. 802; *Kurubo v. Zach. Motison (Nig) Ltd* (1992) 5 NWLR (Pt. 239) at p. 102.

96 (1953) AC 337 at 345.

was unsuccessful. Thus, the Privy Council, it appears, deliberately ignored it in Lees case[97] few years later. The concept is thus well accepted in most legal systems today including Nigeria.

The concept has been extended to the realms of labour law. In line with the corporate personality principle, it has been held that when two companies amalgamate, contracts of service, which are essentially personal in nature, cannot be transferred and that the workman does not automatically become the employee of the transferee company.[98]

The fundamental principle of independent corporate personality has other consequences flowing from it. These may now be briefly examined.

a. <u>Limited Liability</u>

One of the most obvious advantages of the corporate personality principle is the concept of limited liability. The members are not as such liable for the company's debts and obligations. Liability depends on the type of company. Where the company is limited the liability of the members is narrowed down to the amount remaining unpaid on the shares, which such members had taken. If unlimited, then, there is no limitation as to such member's liability for the company's debt obligations.

A major distinction between unincorporated companies and incorporated companies is that unlike the former, the liability of members of

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97 Supra.

98 *Nokes v. Doncaster Amalgamated Colleries* (1940) AC 1014, per Lord Atkin at p. 1026.

the latter is narrowed down either to the full nominal value remaining unpaid on the shares taken by him or such amount that is personally guaranteed.[99]

b. <u>Capacity to Sue and be Sued in Proceedings</u>

A company upon incorporation acquires the legal capacity to initiate proceedings in the company's name. Similarly, it can also be sued in its name. The decision in *Foss v. Harbottle*,[100] states the position clearly. The case established the principle that the proper plaintiff in an action pertaining to a wrong alleged to be done to a company or association of persons is *prima facie* the company or association. It must be emphasized that only the company has the right to act in legal proceedings, enter and enforce rights and obligations belonging to the company. This rule covers all manner of actions by and against the company. Therefore, where an individual member of the company seeks to arrogate to himself the right of action which belongs to the company as a legal entity such an action would fail.

The rule which is codified under Section 299 of the CAMA applies to both incorporated and unincorporated bodies.[101] But because of the hardship and injustice that may arise from its application, exceptions were originally created under common law but now codified under Section 300 of the CAMA. The circumstances under which the exceptions could come into play and a minority shareholders action allowed are where shareholders at a meeting decides to do something which is either *ultra vires* or illegal; where the

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99 This is where a company is a guarantee company.

100 (1843) 2 KB 461; see also S. 229 CAMA.

101 S. 300(9) of CAMA. See also *Hitton v. Westcork Rly* (1883) 33 Ch.D. 654.

company purports to do by ordinary resolution an act that could be properly done or is required to be done by special resolution whether by the CAMA or by its constitution;[102] where it is alleged that the personal rights of a plaintiff is infringed or about to be infringed;[103] where those that control company affairs are perpetrating fraud against the company or the minority shareholders;[104] where the company's meeting cannot be called in time to be of practical use in redressing a wrong perpetrated against a company or minority shareholders[105] or where directors are likely to undeservedly derive a profit or have profited from their negligence.[106]

c. <u>Capacity to Owe Property</u>

Another incidence of incorporation is that upon incorporation, the property of such company becomes clearly distinguished from that of a member or shareholder. A company thus become a beneficial owner of its own property, not as an agent or trustee for its members. In consequence, shareholders cannot exercise rights in respect of such company property, just as the company has no legal interest in a member's property. In the Nigerian case of *Bozak (Nig.) Ltd. v. Zeregbe*,[107] the court restated the principle that shareholders cannot exercise the right of ownership over their company's property. Logically flowing from the above is the attendant principle that a shareholder, not having a legal or equitable interest in the company's

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102 See 300(b), see also Edwards v. Halliwell (1950) 2 All ER 1064 at 1067.
103 See 300(c), see also Pender v. Lushington (1877) Ch.D. 70; Obikoya v. Ezenwa (1973) US. CC 509
104 See 300(e), see also Cooks v. Deeks (1916) A.C. 534.
105 See 300(e), see also Holdson v. National & Local Government Officer (1972) WLR 130.
106 See 300(f), see also Daniel v. Daniel (1978) 2 All ER 89
107 (1973) 4 FRCR 83. See also Macaura v. Marketing Assurance Co. (1925) AC 619.

property, cannot also proceed to insure such property.[108] The principle that a company has exclusive beneficial ownership of its property and so can only insure such property is relaxed in the case of debenture holders. Thus a debenture holder can insure the property of a company if the debenture is secured on the company's property.[109]

d. <u>Perpetual Succession</u>

Incorporation guarantees the continuity of business of the company. The life span of the company can only be terminated by the process of winding up of the company. Notwithstanding, changes that may occur in the company's membership, it has perpetual succession. As Green L.J. pointed out in *Stepney Corporation v. Osofsky*,[110] "a corporate body has no soul to be saved or body to be kicked …" The reason is not far fetched. A Corporation is an artificial person and so cannot be susceptible to natural shocks that the human flesh is prone to. Thus illness whether mental or physical cannot ground an incorporated company. A partnership on the other hand, is totally devoid of these attributes. Death, retrenchment, incapacity of a partner automatically brings a partnership to an end. Incorporation thus brings several advantages, one of which is perpetual succession.

e. <u>Capacity to Transfer Shares</u>

Incorporation, apart from the consequences already discussed, also has the effect of facilitating the transfer of a member's interest. In the absence of

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108 Macaura v. Northern Assurance Co. Supra.

109 Westminister Fire Office v. Glasgow Provident Investment Society (1888) 13 App. Cas. 699.

110 (1973) All ER 289 at 291.

any restriction in the Memorandum and Articles of Association, a share is a commodity that is freely transferable since it is a personal estate or personal proprietary interest of an individual. Upon such a transfer, the transferor drops out of the stage and the transferee steps in to take his place.

Though, a partner seemingly stands on the same legal platform since he can be held liable as a partner, usually partnership interest depends on the express agreement of all the partners concerned, apart from its being subject to other legal and practical limitations.[111]

f. <u>Capacity to Borrow Money</u>

An incorporated company also has the right to borrow money. This is also an incidence of incorporation. Practically speaking, though both incorporated companies and a partnership have the right to borrow money, incorporated companies find it easier to raise money by borrowing. A company is often more capable to provide the required collateral securities to secure its indebtedness. The usual type of security granted by companies in this regard is known as floating charge. The floating charge security device enables a lending company to obtain an effective security on the undertakings and assets of the company both present and future either alone or alongside a fixed charge on its landed property.

The floating charge is important where a business has no fixed asset such as land which can be included in a normal mortgage but has a large

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[111] Like a partner, the right to transfer shares in private companies is equally limited.

chunk of valuable stock-in-trade. A floating charge cannot be granted to either a sole trader or a partnership.

2.11 GROUNDS FOR DISREGARDING THE CORPORATE PERSONALITY OF A COMPANY

Despite the practical contributions of the corporate personality principle to the development of modern company law, it became obvious that it was being unduly manipulated and bastardized by unscrupulous investors so as to protect certain selfish interests thereby making nonsense of the original objective of the law. The need therefore arose to stem the tide of such abuses. An attempt at providing viable solutions came in the form of creating exceptions to the corporate personality principle, under exceptional circumstances. According to Professor Gower,

> it has always been recognized that the legislature can forge a sledge hammer capable of cracking open the corporate shell ...[112]

The intervention of the law in this regard is normally referred to by writers as the "lifting of the veil of incorporation". Some of the grounds under which the concept can be disregarded are provided under statute and others by the courts.

(a) Reduction of Membership below Statutory Minimum

One of the grounds for disregarding the corporate personality of a company is provided under Section 93 of the CAMA. The section provides that:

> If a company carries on business without having at least two members and does so for more than 6 months, every director or officer of the company during the time that it so carries on business after

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[112] Gower L.C.B. "Principles of Modern Company Law", Supra at p. 112.

> those 6 months who knows that it is carrying on business with only one or no member shall be liable jointly and severally to the company for the debts of the company contracted during the period.

The import of this section is to convert a limited liability company into one that is unlimited and thereby making the members of the firm liable personally as if it were operating under a partnership set up. Thus the members may become personally liable to the creditors directly and severally. But it is important to note that it is those members that remain after the six months period that will be liable to the creditors. Secondly, their liability depends on whether they had knowledged that the number has so reduced. Thirdly, they are liable only in respect of debts contracted after the extinction of the six months period. This shows clearly that the creditors' rights against the members are severely limited.

(b) Reckless or Fraudulent Trading

The circumstances under which this ground comes into operation is when a company is wound-up or is in the process of being wound-up. In either case, once the court is satisfied that a company's business has been run with the intention of defrauding its creditors or the creditors of another person or for any fraudulent purpose, the court may upon the application of the official receiver or the liquidator or any creditor or contributor of the company, declare that any person who was knowingly party to the carrying on of the business in that manner shall be personally liable without any limitation of

liability for the whole of company's debts or other liabilities of the company as the court may direct.[113]

It is important to point out that Section 506 of the CAMA which is the relevant provision dealing with reckless and fraudulent trading is limited in its operational scope despite its seemingly wide and far reaching outlook. Thus the section can only aid a creditor when the persons responsible for managing the business of the company are guilty of dishonesty which they commit while participating in the company's business.[114] Thus, active participation in the company's management is the basis for liability. A shareholder cannot be held liable for the debt of the company on account of his large shareholding or simply because he nominated or was instrumental to the appointment of directors who have been found wanting of fraudulent trading.[115]

Section 506 is only relevant when a company is being wound-up and a creditor seeking to take advantage of the section has to discharge the heavy burden of establishing fraud.[116] No doubt, this provision is a potent restraining influence against delinquent directors.

(c) Misdescription of Company

Section 631(4) of the CAMA mandates every company to ensure that its name be mentioned in legible characters in all its bills of exchange, promissory notes, endorsements and cheques issued by the company. Usually, an officer of a company is required in the process of issuing, or authorizing the issue of

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113 S. 506 of the CAMA
114 Re Gerald Cooper Chemicals Ltd (1978) 2 All E.R. 49.
115 DPP v. Schidkamp (1971) AC 1 HL.
116 Re Patrick & Lyon Ltd (1933) Ch. 786

any bill of exchange, promissory notes, cheques, or other negotiable instruments to do so with the name of the company clearly mentioned. Failure to do this subjects an officer responsible to liability to the holder of such bill of exchange, promissory notes, cheques, or other negotiable instruments except where the company acknowledges and pays the amount thereof.[117] But where the holder of a company's document is responsible for such misdescription, he will be barred from enforcing the company's liability.[118]

It is sufficient misdescription under Section 631(4) if the word "Limited" is omitted to create liability for any person found responsible.[119] But it has been held that where an abbreviation like "Ltd." is used instead of "Limited", this would not be tantamount to a misdescription.[120] This provision does ensure that the name of a company appears wherever it does business, on its seal and on all business documents and letters.

(d) Holding and Subsidiary Companies

Section 336 of the CAMA governs interrelated or associated companies within the same group enterprises, otherwise called holding and subsidiary companies. This has become a common feature in modern times. In theory, each of these interrelated companies is a separate company of its own but in reality, it is a component part of the same group of companies. The group company is usually referred to as the Holding Company while the interrelated company is called Subsidiary Company. But Section 336 of the CAMA provides

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117 Nathaniel Abiodun Adeniyi v. The State (1992) 4 NWLR p. 248.
118 Durham Fancy Goods Ltd. v. Michael Jackson Fancy Goods Ltd.
119 Pentrose v. Martyr (1858) E.B 2 E 499.
120 S. 29(65) of CAMA.

that the account and balance sheet of a holding or parent company reflect the necessary matters related to that of its subsidiaries; and the account of such subsidiary must show the aggregate amount of its indebtedness to and from other companies belonging to the group. As an addendum to the above, reports on assets, liabilities, profits and losses of subsidiaries must be annexed to the statement of the companies prospectus or statements in lieu of prospectus which must be presented in the general meeting.

Section 336(2) of the CAMA however provides that under certain circumstances, the above requirements may be dispensed with. This is, where it is impracticable or where what is involved is so insignificant, or where it will occasion a lot of expenses or where the result would be misleading or where the business of the holding company is not the same with that of the subsidiary.

The practical importance of the section is to prevent the publication of misleading information in relation to the financial position of a group of companies controlled by its holding company. This serves some practical importance where fraud is suspected as between the parent and subsidiary. The essence of the provision is that the act allows the accounts of both holding and subsidiary companies to be laid together, thus disregarding separate corporate personalities of the companies in the group and emphasizing their economic unity. The veil is thus lifted where the separate personality is disregarded below.

(e) Reduction in the Number of Directors

Section 246(3) of the CAMA deals with the circumstances under which the veil of incorporation of a company will be lifted. It provides that where the number of directors of a company is less than two and the company continues to carry on business after sixty days of such depletion, every director or member of the company that is aware that the company so carries on business after that period shall be held personally responsible for all the liabilities and debts incurred by the company during that period when the company carried on business.

Ordinarily, Section 246(1) of the CAMA provides that every registered company must have a minimum of two directors while companies that came into being before the extinction of a period of two months from the commencement of the CAMA have a minimum of two directors. But where for whatever reason the number of directors of a company becomes depleted thus falling below the minimum of two, such a company must within a period of one month appoint a new one, otherwise, it ceases to carry on business. It is when the mandatory provisions of Section 246(1) and (2) are not compiled with that Section 364(3) comes in to apply the statutory hammer to lift the veil of incorporation.

(f) Personal Liability of Directors and Officers

It is now a common feature in most corporate entities that loans or advances granted for specific projects or contracts are diverted for other purposes. Section 290 of the CAMA provides in respect of such occurrences

that where such diversion is carried out with intent to defraud, every director or other officer of the company who is in default will be personally liable to the party from whom the loan, or advances was received in the first place.

The key emphasis under Section 290 is the intent to defraud. It thus obviously appears that a diversion actuated by good intention; something in the nature of misapplication of funds will be outside the ambit of Section 290 of the CAMA.

(g) Liability Under the Failed Bank Act 1994

It appears that the veil of incorporation can be lifted under other statutes apart from the CAMA. Section 3 of the Failed Banks (Recovery of Debts) and Financial Malpractices in Banks Act 1994 provides that a Tribunal established under Section 1 of the Act shall have power to disregard the corporate veil of an incorporated entity if it is necessary to reveal its members for purposes of determining whether such members are guilty of an offence under the Act or liable jointly or severally for the debts owed by the corporate body to a failed bank.

(h) By the Courts

Where the courts is of the opinion that the corporate personality principles is being used as an agent or instrument of fraud, it will not hesitate to disregard it. An example is where a company is incorporated with the sole object of facilitating the evasion of a legal obligation. The case of *Gilford*

Motors Co. Ltd. v. Horne,[121] provides a vivid example. Horne, an ex-employee of the plaintiff company entered into an agreement not to solicit for its customers within a given time frame after leaving its employment. He later sought to avoid this obligation by incorporating a company and passing over the responsibility of doing the soliciting indirectly. The former employer succeeded in obtaining an injunction against Horne. In its judgment the court described the company as "a devise, a stratagem and a mere cloak or sham".

A similar decision was reached by the court in the Nigeria case of *Akande v. Omisade*,[122] where it was observed that where a company is established for the express purpose of doing an unlawful act or a wrongful act, the individuals as well as the company are those persons whom liability is legally owed. It further held that a person who is accountable as a fiduciary in his capacity as a director of a company cannot avoid liability by incorporating another company for the purpose of obtaining profits which would have accrued to the company in respect of which he is acting as a director.

(i) Trust

There has been fewer attempts and even less successful attempts at relying on trust as a tool for piercing the corporate veil. Nonetheless, the position is that where a company in its Articles and Memorandum of Association discloses its members to be trustees of the company, such members will be personally liable for the debts and liabilities of the

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121 (1933) Ch. 935

122 Suit No. FCAL/108/80 of 4/5/83 unreported.

company.[123] In *Littlewoods Stores v. I.R.C. Littlewoods*,[124] the holding company had purchased a capital asset and vested it in a property holding company which was its wholly owed subsidiary. It sought to obtain a tax advantage by relying on the fact that the subsidiary was a separate legal personality. The court held that:

> … the subsidiary is the creature, the puppet of Littlewoods in point of fact: and it should be so regarded in point of law.

It must be pointed out that the above decision which states that a company can hold its property on trust represents a considerable departure from the established principle that a company does not hold its property on trust for its members.[125] A pertinent observation and reflection on the points discussed so far is that the courts appear rather conservative in their protection of a company's creditors. The legislature appears to have adopted a much more aggressive approach.

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123 See Abbey Malven Wells Ltd. v. Ministry of Local Government Planning (1951) Ch. 728.

124 (1969) 1 WLR 1241.

125 See the dictum of Evershed L.J. in Short v. Treasury Commissioners (1948) 1 KB at p. 122.

CHAPTER THREE

MANAGEMENT OF COMPANIES

3.1 INTRODUCTION

This chapter seeks to identifies with the expanded theory of company organs and in the process, disproves the old and outdated concept that the general meeting alone is the primary organ of the company. Also examined and analysed is the meaning of the term "company director," as well as the legal status and conditions of his appointment.

3.2 ORGANS OF A COMPANY

A company as an artificial legal person cannot act on its own except through certain organs. These are its human organs, officers and agents. It is through all these that it exercises its rights and carries out its duties as set out in the Memorandum of Association of the Company. Though a company is endowed with all the powers of a natural person, it has no mind of its own; its directing mind and will can only be found in human persons.[1] Viscount Haldane, L.C. eloquently highlighted the artificial nature of a company when he observed in the celebrated case of *Lennard's Carrying Co. v. Asiatic Petroleum Co Ltd*, as follows:

> My lords, a corporation is an abstraction. It has no mind of its own, any more than it has a body of its own, its active and directing will must consequently be sought in the person of somebody who for some purpose may be called an agent, but who is really the

[1] See the observation of Cains, L.J. in Ferguson v. Wilson (1866) L.R. 2 Ch. 77 at 89, that "a corporation itself cannot act in its own person, for it has no person".

> directing mind and will of the corporation, the very alter ego and centre of the personality of the mind.[2]

In Nigeria, the limitation of corporate entity was emphatically recognised by the Supreme Court in *Trenco Nig. Ltd. v. African Real Estate & Investment Co. Ltd.*[3] when the court observed that "a company although having a corporate personality is deemed to have a human personality through its officers and agents".[4] This was further confirmed in *NNSC v. Subana & Anor.*[5] where the Supreme Court while overruling both the trial court and the Court of Appeal stated that:

> A company, it has been said is an abstraction. It therefore acts through living persons. But it is not the act of every servant of the company that binds the company. Those whose acts bind the company are their alter ego – Those persons who because of their positions are the directing mind and will of the company …

The power of corporate decision making is divided between two primary organs, namely, the shareholders in the general meeting and the directors, either acting as a board or through delegates.[6] Towards the end of the 19th century, the apparently held view was that shareholders in the general meeting occupied a more prominent position in the company. The Board of Directors was merely an agent of the company, subject to the control and direction of the members. Thus members in the general meeting were seen as the supreme

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2 (1915) A.C. 705 at p. 713.

3 (1978) 1 LRN 146

4 Ibid at p. 153.

5 Per Nnaemeka Agu, JSC at p. 58

6 S. 63(3) CAMA 1990.

decision making authority. The control of a company resided with the members in the general meeting since the most important functions of the company were required to be performed at the general meeting. Even the memorandum and articles, the basic constitutions of the company are only alterable by the general meeting. The influence and power of the general meeting extends to such other matters relating to the alteration, increase and reduction of company's share capital, for, it is only through the general meeting that such matters can be decisively handled. Again, it is the general meeting that appoints, and removes a director by ordinary resolution. It must be pointed out however, that the issue of whether it is the general meeting or the Board of Directors that controls the company has not been an easy one to determine.

The case which clearly explains the old concept of the supremacy of the shareholders at the general meeting is that of *Isle of Wright Rly Co. v. Tohourdin.*[7] There the English Court of Appeal re-emphasised that the general meeting was the company whereas the Board of Directors was an ordinary agent of the company subject to the control of the general meeting. In that case the directors wanted to restrain the holding of a general meeting scheduled for the purpose of appointing a committee to reorganise the management of the company. As observed by Collon, L.J. in the course of his judgement:

> It is a very strong thing indeed to prevent the shareholders from holding a meeting of the company, when such a meeting is the only way in which they can interfere if the majority of them think

[7] (1883) 25 Ch.D. 320 C.A.

> that the course taken by the directors on a matter *ultra vires* the directors or is not for the benefit of the company …

The supreme controlling authority of the general meeting was however disputed at the commencement of the 20th century, when in the later case of *Automatic Self-Cleansing Filter Syndicate Co. v. Cunnigham,*[8] the court held that the division of powers between the Board of Directors and members of the company in general meeting is predicated on the construction of the articles of association especially in relation to limited liability companies. In the case, the directors of the company, relying heavily on the powers of management delegated to them by the articles of association, refused to carry out a sale agreement which the company had approved at the general meeting. The directors refusal was hinged on the premise that the sale agreement was not in the best interest of the company. On the other hand, the members argued that the provisions of the articles of association are subject to the agency theory which mandates the directors, as agents to be subordinated to the authority of the general meeting, the principal. The Court of Appeal refused to be swayed by this line of thinking and held that the resolution of the general meeting was null and void. Professor Gower's[9] opinion with regards to this matter is that:

> ... the old idea that the general meeting alone is the company's organ and the directors are merely the company's agents and servants and at all times subservient to the general meeting, seems no longer to be the law as it is certainly not the fact.

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[8] (1906) 2 Ch. 34 CA; See also Gramophone and Typewriters Ltd v. Stanley (1908) 2 KB at 105, 106.

[9] Gower, L.C.B, "Principles of Modern Company Law", 5th Ed. (London: Stevens & Sons, 1998), p. 152.

What is apparent from the foregoing analysis is that where the power of management is vested in the Board of Directors, the general meeting cannot interfere with the Board's exercise of such powers. The members in the general meeting cannot say how the affairs of the company should be run or even overrule a decision of the Board of Directors. The Board's power of management also encompasses the power to act in respect of all matters not specially reserved for the general meeting by the companies articles.[10] This postulation does ensure that the directors are given ample opportunity to manage the business of the company specially in relation to the day to day management of the affairs of the company excepting however small scale companies where it is possible to appoint all the shareholders as directors for the purpose of running the company.

This position persisted under the 1968 Companies Act.[11] It must be pointed out however that the allotment of powers between the general meeting and the Board of Directors was not reflected in the main body of the Act itself (in contrast with the CAMA) but in the preamble.[12] Under the CAMA, it appears that the members in general meeting stand on a higher pedestal in contrast to the Board of Directors. First the CAMA in Article 80 adopts the position under the 1968 Act. Secondly, it goes a step further to make the Board

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10 Where members are however dissatisfied with the character or performances of a director, the company can always remove him by ordinary resolution.

11 See Article 80 of Table A of the 1968 Companies Act which is identical to Article 80 of the English Companies Act of 1948.

12 See Article 80 Companies Act 1968.

of Directors the agent of the members in general meeting. For instance, in Section 63(1) it provides that:

> A company shall act through its members in general meeting, or its Board of Directors or through officers or agents appointed by or under authority derived from the members in general meeting or the Board of Directors.

Thus, the shareholders in the general meeting retain the supreme controlling authority with the Board reduced to the role of an agent. Even though the Board still retains the power of management, this is now seriously circumscribed at least in theory. What obtains in practice may be completely different. The reason is that despite the fact that company directors are appointed by the shareholders, they are usually unable to operate effectively as a united entity. This informs the reason why Directors in large corporations always occupy a predominant position during conflict between ownership and managerial control.

But under certain situations, the shareholders in general meeting can exercise all the powers of the company which the Board of Directors usually exercises as the company's agent. As explained by Chukwuemeka Idigbe J.S.C. in *Okeowo v. Migliore*,[13] "agency is based simply on the principle expressed in the maxim - *quiper altum facit per seipsum fecere vide ture* - He who does an act through another is deemed in law to do it himself ... It is implicit in the maxim that the principal can always act if the agent will not." Thus, where the relevant articles vest managerial powers on the Board of Directors and the Board

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[13] (1979) 11 SC at 136.

refuses or cannot exercise the power due to breakdown in the management of the company, the general meeting may exercise such powers.[14]

Under the common law the circumstances under which the general meeting may validly exercise such inherent powers are:

(a) Where there was a deadlock on the Board;[15]

(b) Where there was no directors;[16]

(c) Where an effective quorum could not be formed;[17]

(d) Where the directors were disqualified from voting;[18]

(e) Where the directors fail to commence proceedings;[19]

(f) Where the directors have purported to borrow in excess of the amount authorised by the articles.[20]

Under the CAMA however, Section 63(5) provides that the general meeting could act in any matter if the members of the Board is disqualified or is unable to act because of a deadlock of the Board or otherwise.[21]

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14 Barrow v. Porter (1914) 1 Ch. 895 at 903 Per Warrington J.

15 Barron v. Potter (1914) 1 Ch. 895; Okenwo v. Mighove (1979) 12 NSCC 210.

16 Alexanderward v. Samyank (1975) 1 WLR 673 at 683.

17 Foster v. Foster (1916) 1 Ch.D. 532.

18 Grant U.K v. Switchbank (1880) 40 Ch.D. 135.

19 Marshalls Valve v. Manning (1901) 1 Ch.D. 267.

20 Irvie v. Union Bank of Australia (1977) 2 App Cas. 366.

21 S. 265 of CAMA.

3.3 LEGAL STATUS OF A COMPANY DIRECTOR

Company directors have acquired different status overtime primarily due to the desire of the courts to curtail not only their powers but also to impose duties and liabilities on them with the aim of ensuring that corporate assets and investors funds are duly protected. Because of the complexity of company management, most corporate entities have opted for two types of directorships, namely, the executive or service directors and the non-executive directors. The executive or service directors are normally, the employees of the company. They comprise the Managing and Executive Directors. The non-executive directors are usually experts drawn from important or specialised fields.

Under the law the company director has acquired a number of legal status. First, he is regarded as trustee of the company's money and property. The conception of directors as trustee can be traced to the later part of the eighteen century when most joint stock companies were largely unincorporated and the only force of legality which they had was the deed of settlement which vested on the trustees the property of the company. During this period most company directors were also regarded as trustees. And in those rare situations when they were not trustees in fact, they were regarded as directors in equity once they dealt with trust property.[22] This view has the support of Professor Keeton who has observed that once a company was formed by a deed of settlement and the property of the firm put in charge of the directors, they were regarded as trustees.[23]

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22 Gower (5th ed) op. cit. at 550.

23 Keeton, "The Director as Trustee (1952) 5 C.L.R. 11 at 13 and 15.

In Searly's opinion, it was wrong to conclude that the concept of directors as trustees gained prominence with companies with deed of settlement. He premised his assertion on three planks. First, he says that, it was in respect of corporations and not companies formed by the deed of settlement that directors were regarded as trustees and for which they could be held liable as trustees of company property. Secondly, he opined that there was a clear distinction between directors and trustees of companies with deed of settlement to the extent that the same persons could not be directors and trustees of their company's property as well. Finally, he posited that there is no support for the view that in the early cases concerning directors' obligation they were in fact held out to be trustees.[24]

In the opinion of Professor Olawoyin,[25] it was not in all cases that the deed of settlement vested company property on directors, though it did vest in some cases but that was sufficient to cloth company directors with the garb of trusteeship.

Directors are not only trustees in equity but also in law. In *York and North Midland Rly v Hudson*[26] Romely, M.R. pertinently alluded to the above position when he observed that company directors who are appointed to manage the affairs of a company for the benefit of shareholders are deemed to occupy a trusteeship position.

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24 Searly, "The director as trustee" (1967) Camb L.J. 83 at 84.
25 See Olawoyin, op. cit. at pp. 4-5.
26 (1853) 16 Bear 485

But it may not be completely correct to assert with the force of finality that the position of directors as trustees of the companies' property was not free from controversy. For instance in *Re-city Equitable Five Insurance Co*,[27] Romer, J. observed as follows:

> It has sometimes been said that directors are trustees. If this means no more than that directors in the performance of their duties stand in a fiduciary relationship to the company, the statement is true enough. But if the statement is meant to be an indication by way of an analogy of what those duties are, it appears to be wholly misleading.

In Nigeria, the question whether it is right to regard company directors are trustees of company properties has been affirmatively answered in *Yalaju-Amaye v. A.R.E.C Ltd*[28] where the Supreme Court of Nigeria per Nnaemeka-Asu, J.S.C ascribed to company directors the dual status of trustees and agents. Any further doubt about the trusteeship position of company directors, is now completely cleared under the CAMA. First, Section 279(1) of the Act provides that "a company director stands in a fiduciary relationship towards the company and shall observe the utmost good faith towards the company in any transaction with it or on its behalf". More specifically section 283(1) provides:

> Directors are trustees of the company's moneys, properties and their powers and such must account for all the moneys over which they exercise control and shall refund any monies improperly paid away and shall exercise their powers honestly in the interest of the company and all the shareholders and not in their own or sectional interest.

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27 (1925) 1 Ch. At 426

28 (1990) 4 N.W.L.R (Pt. 145) 422

It may not be completely right to ascribe the tag of trustee to company directors. This is because there is a difference between a trustee under law of trust and directors as trustees of company properties. The law of trust adopts a very strict position in terms of a trustee's liability to trust property by making him liable personally for any damage to property arising from personal risk or misjudgement, no matter how well intentioned. The company law on the other hand adopts a relaxed position by only subjecting the director to liability where the business risk is unreasonable especially where the act itself apart from being *ultra vires* the company, was engaged in without prior approval of the company. Another notable area of difference is that trust law makes the trustee the owner of that property and accordingly allows the trustee the liberty of dealing with it as the principal, though the liability to account to the beneficiary always remains. In company law, trust property belongs to the company.[29]

In view of all the analyses above, it is submitted that it would be more appropriate to regard a company director as a corporate fiduciary rather than a trustee. This will eliminate the inherent confusion in the use of the term. The artificiality of the legal personality of the company does makes it impossible for the company to act for itself in business transactions. Hence, the directors are appointed to act on behalf of the company.[30] Thus in the discharge of his responsibilities as agent, a director must put into consideration, the overall

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[29] See Wilson v. Lord Bury (1880) 5 Q.B.D 518 per Story J. at 530; Re-Williams (1897) 2 Ch. 2 at p.19; Smith v. Anderson (1880) 15 Ch.D 247, Re-Kingston Cotton Mill (No 2) (1896) 1 Ch.D. 331.

[30] S. 283(2) of CAMA 1990.

interest of the company, its shareholders, employees and the customers whom the survival of the company depends. As an agent, a company director must act prudently and in good faith while discharging his official functions. As long as the director is acting within the scope of his authority and on behalf of the company, he will incur no personal liability, though he remains accountable for any secret profit made. He will however incur personal liability in the circumstances where he exceeds his authority as an agent or contracts in his own name or assume personal liability.

Equating a company director as an agent has not gone down without attracting some of disapproval. While in *Ferguson v. Wilson,*[31] the court observed that the status of a company director is that of an agent, In *Re Imperial Hydropathic Hotel,*[32] Bowen, L.J. was of the view that directors are not exactly agents and that the appellation is used only for a particular moment or the particular purpose intended to be considered. In Nigeria, the Nigerian Supreme Court in *Trenco Ltd v Africa Real Estate*[33] adopted the reasoning in *Ferguson v Wilson.*

While, it may be true that the relationship between the company director and the company may not entirely fit into the compartment of a principal and an agent,[34] for purposes of accountability to the company, the director is nevertheless seen as an agent. A careful reading of sections 63(1)

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31 (1866) L.R 2 Ch. 77; see also the statement of Lord Hardwicke in Charitable Corporation v. Sutton (1742) 2 At K. 400 at 405, that directors are "most properly agents to those who employ them in this trust and who empower them to direct and superintend the affairs of the Corporation"

32 (1882) 23 Ch. D. p.1 at 12 and 13

33 (1978) 4 S.C. 9.

34 See Re Imperial Hydropathic Hotel Supra

and 283 (2) of the CAMA would suggest that a company director in the eyes of the law is an agent on behalf of the company for certain purposes and may be regulated by the relevant principles of principal and agent. Section 63 (1) of the CAMA provides that:

> A company shall act through its members in general meeting or its board of directors or through officers or agents, appointed by or under authority derived from the members in general meeting or Board of Directors.

Section 283 (2) also provides:

> A director may when acting within his authority and the powers of the company be regarded as agents of the company…

However, professor Olawoyin prefers to steer a middle course in his own contribution to the debate. In his view, the position of a company director in relation to his company is that he is an agent in certain circumstances and would be insulated from personal liabilities to third parties when acting on behalf of a company,[35] though he may be held liable in situations where he has undertaken personal liability.[36]

It is humbly submitted that it may not be strictly appropriate to assert that company directors are agents of the company in the mode of the traditional relationship of principal and agent. An unwavering insistence on this point will serve no useful purpose especially if considered against the background that where under the memorandum and articles of association of company, a director is expressed to be the agent of company, such director

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35 Olawoyin, op. cit. See also Adenyi v State (1992) 2 N.W.L.R. pt. (234) 248; Co-operative Bank Ltd v Obokhare (1996) 5 N.W.L.R. (pt. 468) 579

36 See Olawoyin op. cit. at p. 10; See also Yesufu v. Kupper (1996) 5 N.W.L.R. (pt. 446).

will be liable for the debt of the company, upon a winding up of the company pursuant to the lifting of the veil of incorporation.[37]

The point has also been made that a company director may be regarded as a servant or employee when considering the rights of the employee in the company[38] or where in the event of a corporate takeover, or winding up of a company, the issue of payment of renumeration or compensation to employees arises.

In the early days, the attitude of the courts were that directors were neither servants nor employees of a company but persons who run the company's business upon certain important terms.[39] In *Normandy v Ind. Cooper & Co*;[40] the court held that a company director or managing director is not a person in a company's employment and so not entitled to pension payable to employees.[41] In *Re Breeton & Co.*[42] Neville J. emphatically said that within the meaning of section 209 (1) (6) of the U.K. Companies Act 1908, a director qua director was not a servant of the company that appointed him. Subsequently, there was a need for a rethinking, especially with the realization that many directors were performing more than one role in relation to their

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37 See Nigarite Ltd v Dalami (Nig Ltd) (1992) N.W.L.R. (pt. 253) per Salami J C A at 304; Kate Enterprises Ltd v Daewoo (Nig) (1985) 2 N.W.L.R. (pt. 5) 116; Rainham Chemical Works Ltd v Belvedre Fish Guuno Co (1921) 2 A C. 465 at 475; Solomon v Solomon (1879) A C. 22

38 See Olaja v Kaduna Textiles Ltd (unreported) NCH/37/96 of 14th March, 1970, where Bello J (as he then was) held that a manager is not a 'worker' within the meaning of S. 2 labour Law, Cap. 9 (LFN) 1958; Lee v Lee Airfarming Ltd (1960) 3 All. E. R. Rep 420, where a governing director was held to be a worker or servant of a company within the meaning of S. 2 of New Zealand Workers compensation Act 1922.

39 See Holton v West Cork Railway Co (1883) 23 Ch. D. 654 at 652 AC per Bowen L.J.

40 (1908) 1 Ch. 84 at 104.

41 At this period no distinction was drawn between directors and managing directors; See Re Newspapers Proprietary Syndicate (1906) 2 Ch. 349; Re Dunston Imperial Gas Light & Coke Co. (1852) 3 B & Ad. 125.

42 (1913) 2 Ch. 279 at 285

companies. The managing director for instance performed dual roles in the company. Though he may not be subject to a service contract as a director, he was usually a party to a contract of employment with his company.[43]

The leading authority which shows the gradual leaning of the courts towards the acceptance of directors as servants or employees of the company they manage was the judgement of Cohen J, in *Trussed Concrete Co Ltd v Green*.[44] In the case, pursuant to an agreement dated March 25, 1936, the defendant was appointed, managing director of the Plaintiff Company for a period spanning seven years. The contract of service required the defendant to devote his time and energy to the company's business as well as carrying out the directions of the Board of directors. Additionally, the defendant was estoped during the period of his service to the company from engaging in any other business without the company's permission. The defendant was later dismissed as managing director of the company. In an unsuccessful action filed by the defendant to challenge his dismissal, his Lordship while delivering the judgement of the court remarked interestingly that:

> When I find a man who is bound to devote his whole time to the affairs of the company, to do all in his power to develop and extend the business of the company, not to engage in any other business and who is engaged on the term that his employment may be determined by the company by notice in writing. I find it impossible to say that he is not employed by the company.[45]

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43 See Lord Nermand in Anderson v James Suther land (Peterhead) Ltd (1914) S.C. 203 at p. 218; per Jekins, LJ in Godwin v Bwester (1951) 52 T.C. 80 at 96.

44 (1946) 1 Ch. 115

45 Ibid at p. 121; Anderson v James Sutherland (Peterhead) Ltd. Supra at p. 248.

After critical evaluation of the above judgement, Olawoyin opined that though the court was right in holding that the defendants were employees of the company, the judgement was based on a faulty premise. He specific grouse with the judgement is predicated on the fact that the court was unduly swayed by the existence of an agreement between the plaintiff company and the defendant which required the defendant to devote his entire time to the company's affairs. This he considered restrictive, opining that the court should have placed more premium on two facts, namely, the nature of duties performed by the director as well as the amount of time which he devoted to the company's affairs.[46]

It is respectfully submitted that rather than being unnecessarily restrictive, it would be preferable if a broader criteria is laid down for the determination of the issue. Thus where, a director devotes most of his time to the company affairs; has a service contract with the company and the nature of his duties to the company shows that he is bound to obey the instructions of the company he should be regarded as a servant or employee of the company. It is further submitted that the issue whether the director in question is performing a full time job which includes other duties outside the functions of a director should not arise.

Having regard to the various positions ascribed to the company director from the perspective of the company law, the questions that now remain to be answered are: first, what is the correct status of the company director? What

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[46] See Olawoyin op.cit. at p. 15

is the practical significance of these multifarious appellations which the company director has come to be identified with?[47] Pertaining to the first, Olawoyin pertinently observed that "the true position of a director is *sui generis* in that it neither fits in completely with that of an agent, nor of a trustee, nor of any of the other positions…"[48] This means that, directors are to be seen in the light of the specific positions of their office or appointment. In some occasions they may properly be called trustee, while in some other occasions, the right description may be that of agents, so on and so forth! The various appellations identified with them do not suggest that they belong exclusively to any of such categories. Thus, the importance of the various descriptions lie in the fact that they are useful only for the particular purpose which the court wishes to emphasis with regard to a particular sets of facts and principles. In fact in certain situations it is actually difficult to classify directors within a specific order since they occupy a unique position as one of the key stakeholders of corporate governance.

Under Nigerian Law one relevant issue for consideration is whether the general meeting really exercises control over directors as to make them

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47 Smith V. Anderson (1880) 15 Ch. D. 247 at 280; Charitable Corporation V. Sutton (1742) 2 Atk. 400, 405; Re Kingston Cotton Mill Co. (No. 2) [1896] 1 Ch. 331, 345; Ferguson V. Wilson (1866) CR. 2 Ch. App. 77, 89; Re Lands Allotment Co. (1894) 1 Ch. 616m 631, 638; Flitcroft's case (1882) 21 Ch. 579, 535; The Lady Greendolas (1965) 2 All E.R. 283, 295; Boulting V. ACTAT (1963) 2 Q.B. 606, 624, 646; Lenard's case (1915) A.C. 705, 713, 715; Re Faure Electric Accumulator Co. (1888) 40 Ch. D. 141; Liver Brothers Ltd. V. Bell (1931) 1 K.B. 557, 586, 586, 593; Trussed Steel Concrete Co. Ltd. V. Green (1946) 1 Ch. 115, 121; Regal Hasting V. Gulliver (1942) 1 All. E.R. 378; Yalaji Amaye V. AREC Amaye; Adeniji V. State, Supra, Oladejo V. State, Supra.

48 See Olawoyin, op. cit. at p. 28-29.

servants or employees of the company. It would appear that is not the intention of section 63(4) of the CAMA which states that:

> Unless the articles shall otherwise provide, the Board of Directors when acting within the powers conferred upon them by this Decree or the articles shall not be bound to obey the directions or instructions of the members in general meeting: Provided that the director acted in good faith and with due diligence.

Before the advent of the CAMA, the judicial attitude tended to favour the position that directors are intricate servants or employees of the company in the relationship between the general meeting and the board of directors of the company. For instance in *Isle of Wright Railway v Tahourdin*[49] the Cutton LJ had observed as follows:

> It is very strong thing indeed to prevent the shareholders from holding a meeting of the company when such a meeting is the only way in which they can interfere if the majority of them think that the loans taken by the directors, in a manner intravires of the directors is not for the benefit of the company.

By refusing the directors an injunction to restrain the shareholders from the holding of a general meeting which was for the sole aim of appointing a committee to re-organise company management, the court tended to create the impression that the general meeting had absolute control over the Board of Directors. This decision did not survived for long as subsequent decisions followed a contrary pattern. Thus in a latter court of Appeal judgement in *Automatic Self Cleansing Filter Syndicate v Cunninghame*[50] the court held that where the article of association of a company confers management powers on

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49 Supra

50 (1906) 2 Ch. 34. CA

the directors of a company, the article evidences a contract by which the members have agreed that only the directors shall have the powers to manage the company's affairs. This decision was followed by a host of other decisions which reiterated the same approach that the general meeting cannot control the directors exercise of management powers.[51] The basis for the decisions being that the both the general meeting and the Board of Directors have distinctive powers which are separate. Lord Wilberforce while emphasizing this point in *Howard Smith Ltd v Ampol Petroleum Ltd*,[52] said that:

> …it is established that directors within their management powers, may take decision against the wishes of the majority of shareholders and indeed that the majority of shareholders cannot control them in the exercise of these powers while they remain in office.[53]

In the *Gramaphone & Typewrite Ltd v Stanley*[54] Buckley J was also of the opinion that directors are not subject to the control of the general meeting since "…they are not agents appointed by and bound to serve the shareholder as their principal."

But can the shareholders control the directors exercise of managerial powers by altering the articles? Though Greer LJ. alluded to this in the

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51 Salmond v Quin & Axtens Ltd (1909) 1 ch.. 311. CA. Affirmed by House of Lord (1909) AC. 442. H.C.

52 (1974) A.C. 821

53 This principle of seperation of powers has attracted criticisms in the academic arena. See for instance Shisky, B,; "The relationship between the Board of Directors and the shareholders in general meeting (1968) UBC. Law Rev. Vol. 3. No. 3, 81-95; Golberg GD.; Article 80 of Table A of the companies Act 1948 (1970) 3 M.L.R. 177; Cohen, C.J, 'The distribution of powers in a company as a matter of law' (1973) 90 S.A.L.J 262; Blackman, M.S.; 'Article 59 and the distribution of the powers in a company (1975) 92 S.A.L.T 286; Mackenzie, J.A; "Who controls the company? The interpretation or Table A' (1983) 4 Co. Law Review. 99;.

54 Supra at p. 105-106

affirmative in *Shaw & Sons Sulford Ltd v Shaw,*[55] it is submitted that alteration of the article for the sake of removing a director or even refusing to reelect him is clearly out of the question as the process does not explain the subject of control in the delicate relationship of master and servant as between the general meeting and the Board of Directors. The proper approach, it is suggested is that looking at the relevant company law provision or company's article of association, can it be said or inferred that the directors are subject to the control of the general meeting so as to make them employees or servants of the company. Anything short of this, will tantamount to a deviation from the real issue. The correct starting point therefore is to examine the relevant company article of Association and see how it settles the issue.

In the United Kingdom Article 80 of Table A of the Companies Act 1968 then formed the basis for Company Article of Association. The said Article 80 Table A provided in the main that:

> The business of the company shall be managed by the directors who… may exercise all such powers of the company as are not by the Act or by these regulations, required to be exercised by the company in general meeting subject, nevertheless, to any of these regulations, being not in consistent with the aforesaid regulations or provisions, as may be prescribed by the company in general meeting.

This provision is verbose and lacks precision. As Pennington[56] rightly observed the provision apart from not empowering the general meeting to dictate to the directors as to how they shall exercise their powers in given situations, does

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55 (1935) 2 KB 113 CA at 136

56 Penington's Company Law op. cit. at 525

not also stripe the directors of the powers which the articles have conferred on them. The power to prescribe regulation, in Pennington's view, are mainly narrowed down to procedural matters usually bordering on when board meetings should take place and not about matters to be transacted at such meetings.

Perhaps it is the desire to sidetrack the ambiguity contained in Article 80 Table A that prompted the Law Reform Commission to canvas for section 63(4) CAMA referred to above.

A careful reading of subsections 3 and 5 in addition to subsection 4 of section 63 will bear testimony to the fact that the company director, especially the non-executive director is not a servant. For instance subsection 3 reads:

> Except as otherwise provided in the companies articles, the business of the company shall be managed by the Board of Directors who may exercise all such powers of the company as are not by this Act or the articles required to be exercised by the members in general meeting.

Furthermore, subsection 5(d) states that:

> Notwithstanding the provision of subsection 3 of this section the members in general meeting may make recommendation to the board of directors regarding action to be taken by the board.

Since the Board of Directors are not bound to obey the directions or instructions of the members in general meeting they thus appear to assume the position of a master under section 63(4). Secondly, since the general meeting can only merely make recommendation to the Board of Directors under section 63(5)(d), the doctrine of separation of powers is preserved, thus

clearly erasing the wrong notion that a company director is a servant or an employee of the company.[57]

The above analysis that a director qua director is not a servant or an employee of a company is true in respect of a non-executive director. But this cannot be said in respect of an executive director such as a managing director of a company. A managing director's functions and responsibilities are clearly distinct and different from those of a non-executive director. Being an appointee of the Board of Directors, he is subject to their control and bound to obey their instructions and directions. Section 263(5) CAMA actually stated the true position of the executive director by providing that:

> The directors may delegate any of then powers to a managing director or to committees consisting of such member or members of their body as they think fit and the managing director or any committees so formed shall, in the exercise of the powers so delegated conform to any regulations that may be made by directors.

The provision speaks for itself. The Board of Directors retain and exercise absolute control over the managing director or committee members while exercising the powers delegated to them by the directors. Usually the contract of service appointing an executive or managing director would state the nature of duties and powers to be exercised by them when appointed. The Board thus putting itself in a vantage position to control the executive or managing director.[58] It is the contract of service that form the basis of control of the

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57 See the decision Neville S. in Re Breeton & Co (1913) 2 Ch. D. The court hold that a director qua director is not a servant of the company.

58 See Gower (5th ed) op. cit. at 161

managing director. In *Harold Holdsworth & Co (Wakefield) Ltd v Ceddies*.[59] The appellant company appointed the respondent as the managing director. The contract of service provided that the managing director shall perform the duties and exercise the power in relation to the business of the company including those of its subsidiaries as may be assigned to him from time to time by the Board of Directors. Subsequently the respondent was directed to devote his attention to one of the subsidiaries alone. The respondent dissatisfied with this development sue the appellant company for breach of contract. The action was dismissed. An interesting aspects of the judgement is the concurring judgement of Earl Jowitt, L.C.[60] which in part said:

> … I am of the opinion that the appellant company had by … the agreement expressly preserved their right to call on the respondent to devote his time to the affairs of the (subsidiary company) if they judge this course desirable.

Also in the later case of *Lee v Lee's Air Farming Ltd*.[61] all the important criteria that distinguishes a servant and an employee director from a director qua director were brought out clearly. In that case Lee held 2,9,9,9 shares out of 3000 ordinary shares of the company. Lee was subsequently appointed the governing director as well as the chief pilot under the contract of service. Lee was able to exercise a firm control over the company affairs as well as taking all decisions relating to the company business in his position as governing director. Lee died unexpectedly while working for the company. Lee's personal representatives subsequently brought an action against the insurers for

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59 (1955) 1 WLR 352 H.L: (1955) SC (H.C) (1955) 1 ALL ER. 725

60 Ibid at 733 L

61 (1960) 3 All E. R. Rep 420.

compensation. The main question for determination was whether Lee was a worker or a servant under the New Zealand's workers' Compensation Act of 1922 which defines a worker as:

> Any person who has entered into or works under a contract of service…with an employer, whether by way of manual labour, clerical work or otherwise, and whether remunerated by wages, salary, or otherwise.

While reversing the judgement of the court below, the House of Lords held that Lee was a worker; or servant of the company. In a well considered judgement, the court held that:

> … The real issue … is whether the position of the deceased as sole governing director made it impossible for him to be the pilot of the respondent company in the capacity of chief pilot of that company. …There was no such possibility. There appears to be no greater difficulty in holding that a man acting in one capacity can give orders to himself in another capacity than there is in holding that a man acting in one capacity can make a contract for himself in another capacity. The respondent company and the deceased were separate legal entities. The respondent company had the right to decide what contracts for aerial top – dressing it would enter into. The deceased was an agent of the respondent company in making the necessary decisions… If the respondent company entered into a contract with a farmer then it can within its rights and power to direct its pilot to perform certain operation. The right to control existed even though it would be for the deceased, in the capacity as agent for the respondent company to decide, what order to give. The right of control existed in the respondent company.[62]

In this case the extreme application of the corporate personality principle was brought to the fore. But, nevertheless the message is not lost.

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62 Ibid at p. 420

3.4 DIRECTORS AS ORGANS OF A COMPANY

We have previously noted that a company director may under certain situations be called an agent of his company. But this leads to another problem. There cannot be an agent except a principal is in existence. A Company is an artificial person that lacks some of the characteristics of a human being. It is the lack of these qualities that denies it certain essential attributes. For instance a company cannot initiate anything for itself since it is not a physical entity. In the *Abbey Malvern Walts Ltd v Ministry of Local Government & Planning*.[63] Dankwerts, J. pertinently observed that:

> The first fact is that this company is an artificial person. It is first as much, though formed under the Companies Act, an artificial person as a corporation formed by statute or by royal Charter or in any other manner. It is certain, that if it is a person which exists in the eye of the law, it is not a physical entity, and can only operate by means of human being. Therefore, one must ascertain the person who operate the company and see what their position is.

According to Professor Gower[64] the initial attempt by the court to tackle the above problem which took the form of taking solace in mere formalism, by regarding the acts of a company as those that have been duly authenticated by its common seal, was unrealistic. In any case, the seal must be affixed by a natural person lawfully authorised or permitted to do so. Otherwise, the company was not liable. Furthermore it was only in contractual relationship that a seal was regarded as appropriate. In other areas of the law, notably, tort and criminal law which require the proof of the blameworthy state of mind

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63 (1951) Ch. 728 at 738

64 See Gower (th ed); op. cit. at p. 126

of the person in question, it would be impossible to impute liability on such companies. In view of these short comings the requirement of seal was discarded in 1845 in England as far as both statutory and registered companies were concerned. Subsequently, the law was completely abrogated.[65]

An acceptable and more appealing manner of resolving the above problem consisted in the courts regarding company directors as organs of the company. In so doing, the decision of the majority of the members of a company at a general meeting was deemed to be the decision of the company itself. In *Attorney-General v Davy*,[66] the above principle was clearly exemplified. The issue for determination was whether two out of the three members of a corporation were justified in appointing a chaplain, such appointment having been vehemently opposed by the third person. The court held that the action of the majority was proper. The main highlight of Lord Hardwicke L.C. judgement was that:

> … whenever a certain number are incorporated, a major part of them may do a corporate act; so if all are summoned, and part appear, a major part of those that appear may do a corporate act;… it is not necessary that every corporate act shall be under the seal of the corporation.

Implicit in the above judgement is the principle that a majority of members of a company present at the company meeting can initiate action on their behalf as well as for the company. It is the majority that now constitute the organ of

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65 See Companies Clauses Consolidation Act 1845, 5 97; and restored in (U.K) Companies Act 1948 S. 32; also S. 37 of 1968 Companies Act as well as 577 CAMA 1990.
U.K. Corporate Bodies Contracts Act 1960.

66 (1941) 2 Atk. 212

the company. In this perspective therefore when a company finds it necessary to appoint an agent, the members as the alter ego were put in a position to do the appointment. This approach did not achieve complete success since it would be impracticable for every member to be involved in the management of the company. This necessitated that a more effective and satisfactory solution was yet to be found especially if the correct position of the company director in corporate management is critically analysed. It is important to note that the powers of a company were divided between the general meeting and the directors,[67] while management powers were specifically the exclusive preserve of the directors, something which gave them the right to exercise the powers aforesaid. The members were not expected, nor competent[68] to challenge management in the exercise of the powers so delegated. The consequence of all these is that directors were the instruments as well as the organs that propel the company. In the celebrated case of *Lennard's Carrying Co v Asiatic Petroleum,*[69] the court succinctly stated the principle that should guide the courts in deciding the categories of officers that are capable of binding the company in respect of acts committed by them. His Lordship, Viscount Haldane observed in these words:

> My lords, corporation is an abstraction. It has no mind of its own more than it has a body of its own; its acting and directing will must consequently be sought in the person of somebody who for some purposes may be called an agent, but who is really the

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67 S. 64(1) of the CAMA

68 S. 63(3) of the CAMA

69 Supra. See also Bath v Standard land Co (1910) 2 ch. 408 at 419

> directing mind and will of the corporation, the very ego and centre of the personality of the corporation…[70]

Thus not every officer can bind the company with his act. An officer who is a "mere servant or agent" cannot bind the company, except on the principle of respondent superior. But a servant or agent who is an organ of the company itself, such as a director or Board of Director can bind the company.

The ambit of the organs of the company has been expanded to encompass the delegates of directors powers who has complete discretion to act independently of such instruction from the directors.[71]

Apart from delegates of directors, the scope has even been further widened to accommodate other officers or servants of a company that carry out responsible and sensitive responsibilities.[72] This new development was ably demonstrated in the *Lady Gwendolen's case*[73] where the court held that an assistant managing director of a shipping company was an alter ego or organ of a company. Thus, in the words of Professor Olawoyin, as long as such officers "enjoy a formerly delegated authority over some aspect of the companies business, on the basis that such actions are those of the company itself…" a company would be liable for the action of such officers.[74]

In Nigeria, the principle of organic theory has been tested by the courts. For instance in *NNSC v. Sabana & Anor*.[75] The 2nd respondent bought a cargo

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70 At 713-714; See also SC Houthon & Co v Nothard Lowe & Wills Ltd (1928) AC 1 H.L. at 10; HMS Truculent (1952) 22 11 ER 968; The Lady Gwendolen (1965) 2 AILRE. 283

71 See Tesco Supermarkets Ltd v Nattress (1972) AC 153.

72 See Daimler Co Ltd v Continental Tyre & Rubber Co Ltd (1916) 2 AC 307 at 340

73 (1965) 2 All E. R. 283 per Winn

74 See Olawoyin op.cit at p. 25

75 (1988) 2 NWLR (PT. 74) 23.

of rice on board a ship M.V. Eastern Maid at high sea. The 2nd respondent subsequently sold it to the 1st respondent but without delivery at the time. On the basis of the sale, the 1st respondent collected money from many of its customers and deposited same with the Nigerian Merchant Bank. But unable to get delivery of the rice from the 2nd respondent, it filed a suit against the appellant and the 2nd respondent. Subsequently, the 1st respondent obtained an order of exparte restraining the appellant and the 2nd respondent from selling the cargo of rice pending the determination of the motion of notice. Prior to the hearing of the motion on notice, the counsel to the appellant applied to court for an adjournment to enable him take further instruction from the appellant. He however entered into an undertaking that the consignment of rice would be preserved before the next adjourned date. One Mrs. Ige, an employee of the appellants company was in court the day the undertaking was made. It was however found out that at the time the undertaking was being executed, the appellant had taken delivery of the cargo of rice and distributed it to various warehouses throughout Nigeria for purposes of its being redistributed as essential commodity to the public. The basic issue for determination before the Supreme Court was the effect of the undertaking considering the status of the said Mrs. Ige. The Supreme Court held while overruling both the trial court and the Court of Appeal that:

> It cannot be forgotten that the appellant is a company, a very big company … which had … delivery points in twenty five towns and locations scattered all over the country. There is nothing to show that Mrs. Ige was of a status and position to know the true position assuming she was consulted.

3.5 NEED FOR COMPANY DIRECTORS

As stated under Section 224(1) of CAMA, directors of a company are persons duly appointed by the company to direct and manage the business of the company. This is the most important need and responsibility which the law places on company directors. But while the need for company directors is primarily that of overseeing the day to day management of the company, the need of the Board of Directors, is policy formulation.

Though the shareholders are the legal owners of the company, they cannot all be involved in the actual daily running of the company. As such, they delegate the powers of managing the company to a select group of people known as Board of Directors. The Board of Directors in turn delegate some of their authority to the chief executive known as managing director. For any corporate entity to succeed the relationship between the directors and management must operate on a smooth and cordial atmosphere. Each group must be alive to its duties and responsibilities and the company's needs.

The chief need for directors is effective corporate governance and management. Towards the attainment of this goal, directors acting collectively as a Board need to put themselves in an effective position to arbitrate between competing and hostile interest and major stakeholders. Where the company in question is family owned, it must be able to ensure the development of an effective succession plan and put in place competent management team.

The company also needs the directors to play the role of crisis managers. This entails arranging immediate replacement and ensuring continuity of

management in the event of death of the chief executives of the organization. Directors acting collectively as a Board have the added responsibility to compel company chief executives or other management to resign, where fraud is perpetrated or call in the audit committee to handle the situation.

Establishment of corporate policies and objectives constitute another necessity for Company Board of Directors. Thus, it is the responsibility of directors to fashion out what business an organization is into and what it has to do to attain its policies and objectives. Allied to this is the need to assist management in reaching appropriate decisions, and in implementing them.

A company with well connected and respected directors give credibility to the organization in the corporate world. Above all, the central need and responsibility of company directors is that of trusteeship. The company needs the directors to safeguard and manage the company's corporate assets (i.e. the human, physical and material) in the best interest of the shareholders. In discharging this need of the company, the directors must strive to ensure a balance between their responsibility to the shareholders and other constituent segments in the society.[76]

3.6 MEANING OF COMPANY DIRECTOR

The English legislature, as far back as 1948, gave a statutory definition of the term "Company Director", but in the process created some confusion. For instance, Section 455(1) of the English Companies Act of 1948 defined a

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[76] See generally, Varr, B.B.A. "Distinction Between Direction and Management", Being a paper presented at the National Workshop on Corporate Governance and the Rights and Responsibilities of Shareholders in Nigeria (28-29 November, 1994) .

Company Director to include any person occupying the position of a director by whatever name called. Even Section 741 of the subsequent English Companies Act 1985 as well as Section 395 of the Nigerian Companies Act of 1968, similarly defined a company director in the same vein. These definitions go further to include shadow directors defined as persons in accordance with whose directions or instructions the directors of a company are accustomed to act but excluding persons who give directions or instructions in their professional capacities.

Apparently, the above definitions do not offer a realistic guide as to what constitute a company director. The courts therefore came in to fill this *lacuna* by looking at the meaning of the term from the functional point of view, that is as a person who directs or controls the affair of a company.[77] In *AREC Ltd. v. Yalloju Amaye*,[78] the Nigerian Supreme Court adopted this reasoning and conception of a company director. According to Anaemeka Agu JSC, company directors are:

> … those men or women who, because of their unique position in the company, are usually referred to as its alter ego; that is to say, those men and women who, because a company is an abstraction and so cannot do anything of its own, constitute the head and thinking brain of the company.

What the CAMA has however done with regard to the definition is to harmonise both the previous statutory and judicial definitions of the term. Thus, under Section 244(1) and (2), a director is defined as a person duly appointed by the company to direct and manage the business of the company.

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[77] See McCardie, J. in Mariarty v. Regent Engineering (1921) 1 K.B. 423

[78] (1966) NWLR 653. See also S. 245(1) and (3) CAMA.

The definition further includes any person on whose instructions and directions, the directors are accustomed to act. However, this does not include all such professionals who give professional advise to directors and which is acted upon by them.

Section 650 of the CAMA appears to give an all embracing definition. It states that a "director" includes any person in accordance with whose directions or instructions the directors of a company are accustomed to act.[79] The section, apart from harmonising the definitions in both Sections 244 and 245, has clearly avoided the punitive traps inherent in Section 244(3) and (4) which completely prohibits appointment of directors by way of the doctrine of estoppel or holding out.

Directors generally take the following forms, namely:

i) Directors per se already explained,

ii) Shadow directors already explained,

iii) Alternate Directors,[80]

iv) Workers Directors,[81]

vi) Executive and non-executive directors.

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79 See also S. 271 of the CAMA.

80 This occurs where the articles allow a director who is legally appointed as such to appoint another director to act in his stead and performs all such function of his appointer.

81 These are directors appointed to represent companies employees e.g. in Germany and most EEC countries.

3.7 APPOINTMENT OF COMPANY DIRECTORS

A company director, as an important functionary in the corporate set up is appointed or elected to office by the shareholders at a general meeting,[82] or by the Board of Directors in the first time. Where the articles clearly provide that the subscribers to the memorandum should name its first directors, it must be strictly adhered to, otherwise any deviation will render any purported appointment invalid. The appointment of directors is strictly regulated by the CAMA.

3.7.1 Capacity to be a Company Director

It is not every person that can act as company director. The CAMA clearly sets out certain disabilities[83] that may disqualify a person from becoming a company director. Those category of persons lacking capacity to be so appointed are:

(a) infants, i.e. persons below the age of 18 years;

(b) lunatics or persons of unsound mind;

(c) insolvent persons, fraudulent persons and bankrupts;[84]

(d) A corporation except its representatives appointed to the Board for a given term.

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82 S. 248 of the CAMA.

83 S. 257 of the CAMA.

84 Ss. 253, 254 and 258. These sections debar both insolvent as well as fraudulent persons. Similarly, a person who vacates office due to bankruptcy, insanity, resignation and loss of share qualification are disqualified from becoming directors. It is thus a criminal offence to act while lacking capacity in this regard.

It appears however that disqualification on the bases of lunacy must be premised upon the finding of a criminal court to that effect. Though the CAMA is mute on this, it cannot be otherwise because only a criminal court can adjudged a person to be of an unsound mind.[85]

The court can also make an order pursuant to Section 254 of the CAMA on application by a receiver, liquidator, a member or a past or present creditor asking that certain categories of persons be banned from being concerned with or acting as a company director for a specific period not exceeding 10 years. At least ten days notice must be given to the person against whom such an order is sought. These comprise any person –

(a) convicted of an offence in connection with the promotion, formation or management of a company; or

(b) convicted of an offence pertaining to the winding up of a company; or

(c) found guilty of fraud or breach of duty to the company while an officer of the company.

Furthermore, any person who is appointed or being proposed to be appointed as a director of a public company must disclose this fact upon a special notice circulated to members of the company in general meeting.[86] Again, under the provisions of section 253(1) an insolvent person may be disqualified from acting as a director of a company. Finally, where the articles

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85 See S. 28 Criminal Code and S. 51 of the Penal Code respectively.

86 Ss. 252 & 256 CAMA.

make provision requiring shareholding as necessary precondition for the appointment of directors, a person seeking appointment must obtain the required shares.

3.7.2 Appointment of First Directors

By the provision of Section 246 of the CAMA, every company must have at least two directors from the commencement date of the Act, i.e. 2nd January, 1990. Any company registered prior to this date, must not later than 6 months from that date, have at least two directors. Where for any reason the number of directors is reduced below the legal minimum of two, the company must make up the shortfall within a period of one month otherwise it shall not carry on business any further.[87]

The subscribers normally appoint the first directors. In this regard, Section 247 provides that the number of first directors and their names shall be determined in writing by the subscribers to the memorandum or a majority of them or the directors could be named in the memorandum.

3.7.3 Subsequent Directors

Section 248 of the CAMA regulates the appointment of subsequent directors. This states that at a general meeting of the company, the members shall have the power to re-elect, or reject and appoint new directors. Implicit in this provision is the fact that it is the exclusive preserve of the shareholders to exercise the powers of re-election or appointment of subsequent directors. In the event of a casual vacancy arising by reason of either death, resignation, retirement or removal, Section 249(1) provides that the Board of Directors is empowered to fill such vacancy subject to

[87] Section 246(1) of the CAMA.

approval at the next annual general meeting. This means that a director appointed pursuant to Section 249(1) holds office for a limited period i.e. until the next annual general meeting when he may be re-elected or confirmed or rejected, as the case be.

Some curious provisions relating to appointment of directors are those of Sections 244, 245 and 650 of the CAMA which relate to directors who may be "duly appointed" by the company and others that may not be so appointed. Though the sections do not state what constitute due appointment of directors, it is apparent what that means is express appointment which must be brought to the notice of the CAC. But what happens if a director is appointed under an express contract but for certain reasons the appointment is not communicated to the Commission? Would such omission render the appointment null and void? Certainly this cannot be the motive of the sections. A clearly worded additional provision in this regard is therefore welcomed. It is also submitted that the provision of Section 244(3) and (4) which outlaws appointment by estoppel or holding out be completely deleted as it runs counter to the relevant company law principle that agency relationship may be created through the doctrine of holding out.[88]

3.8 VACATION OF OFFICE BY A COMPANY DIRECTOR

A director may vacate office in two ways, namely, by retirement or removal. Section 259 of the CAMA governs the retirement of directors from office by vacation. This states that unless otherwise provided by the articles, at the First Annual General Meeting of the company all the directors shall retire

[88] Freeman & Lakyer v., Buckhurst Park Properties (Mangal) Ltd. (1964) 2 Q.B. 48; S. 250 Act.

from office. At the Annual General Meeting in every subsequent year $^{1}/_{3}$ of the directors for the time being, or if their number is not 3 or a multiple of three, then the number nearest $^{1}/_{3}$ shall retire from office.

Usually, longevity in office is the yardstick in the consideration for determining retirement. Where two or more directors are due for retirement and it appears that the company has no plans to retire all of them, the CAMA prescribes the casting of lot or the tossing of a coin. It is submitted that the issue of retirement is a very serious one which should not be left to the fate of the tossing of a coin. It would be preferable, if the company uses the performance charts of the directors in such a situation as basis for a decision. It is suggested therefore that a clear worded provision concerning this be inserted into the CAMA as soon as possible. This is long overdue.

The power of removal of a company director from office is governed by Section 262 of the CAMA.[89] This provides that a company which wishes to remove a director may do so by ordinary resolution before the expiration of the period of his office notwithstanding a contrary provision in the articles or a subsisting agreement between the director and the company.[90] Section 259 however protects the director sought to be removed by stating that appropriate notice of the resolution to remove the director be served on him. Besides, the shareholders are also required to point out vividly and make available to the company the unsavoury circumstances warranting his removal.

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89 It was formally regulated by S. 175 of the 1968 Companies Act.

90 Under the 1968 Act, it was not possible to remove a life director but this is now possible under S. 262 of the CAMA.

The act of removal of directors is one of the rare privileges which the law confers on the shareholders to exercise their right of ownership. In exercising the right the shareholders may have regard to the conducts of the director. Where a particular conduct is unbecoming of a director, or is not in the best interest of the company, this may give room or provide cause for removal. It is not out of place to make a cursory remark here about the role which the Nigerian Shareholder Association organised on zonal basis could play in the removal of a company director for proven misconducts. The essence of the organization is effective corporate governance and management. In an attempt to actualise this aim, the organization has the responsibility to make representation to the Board of Directors and attend meetings of public companies; act as proxy holders of company meetings for shareholders who are members, make representations to government or any authority whose activities jeopardise the interest of shareholders. In short, the chief responsibility of the organization is to protect minority shareholders. One way of removing a company director or changing the entire management structure of a company by the association is by soliciting for proxy votes from alliances developed overtime and at company meetings. In fact the Shareholders Association of Nigeria has all it takes to use the platform of the general meeting as an avenue to probe and subject the conduct of the directors and management to scrutiny.

The procedure for the removal of a director would usually involve certain steps. The first step is the calling of an ordinary general meeting. Secondly, an ordinary resolution is prepared. Thirdly, a special notice is prepared and given to the company of the ordinary resolution. Once the

company receives notice of an intended resolution to remove a director, the company shall forthwith send a copy of it to the director involved who shall be entitled to be heard on the resolution at the meeting;[91] where a director makes representation in writing to the company with respect to the notice of intention to pass a resolution to remove him, the company shall unless the representations are received by it too late for it to do so, in any notice of the resolution given to members of the company, state the facts of the representations to every member of the company to whom notice of the meeting is sent.

Where a copy of the representation is not sent because it is too late or because of the company's default the director may (without prejudice to his right to be heard only) require that the representations shall be read out at the meeting. But it may not be necessary to send out or read out at the meeting copies of the representation if the company or an aggrieved person applies to court to stop the circulation and the court is satisfied that the right conferred on the director is being abused. In such situation the court may order the director to pay to the company the cost incurred in preparing such an application despite the fact that he is not a party to the application.[92]

Where a resolution to remove a director contravenes the above procedure the purported removal is null and void. The act of removal of a director does not vitiate or extinguish the right to receive compensation or damages for contractual breach if the director satisfies the court to that effect.

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91 S. 262(2) of the CAMA.

92 S. 262(3).

There are however some obstacles that could effectively defeat any planned removal of a company director. It may be defeated for instance, where the removal procedures are not complied with under the relevant Act.[93] Secondly, the issue of removal is generally governed by the principles of equity. Thus, the exercise of the right of removal may back fire and achieve a contrary intention where it is inequitably used.[94]

` However, a declaration by the court that a director has been improperly removed is not enough to foreclose his subsequent removal. The Court of Appeal emphasised this in *A.R.E.C. Ltd. v. Amaye*,[95] thus:

> A director who was unlawfully removed could still be removed properly despite the improper notice and procedure adopted earlier since the company has a statutory right to remove anybody from its board …

This is in affirmation of the legal position that one cannot force a servant on an unwilling master. This principle holds good provided the proper procedure is followed.

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93 Eronini v. Harbour (1957) 2 TSC 43.

94 See Re Westbourne Galleries Ltd. (1972) 2 WLR 1289.

95 Supra at p. 653.

CHAPTER FOUR

DUTIES OF COMPANY DIRECTORS

4.1 INTRODUCTION

The law in recognition of the nature of office of company directors has found it necessary to foster enormous responsibilities on them with a view to ensuring that they put in their best in the discharge of their functions. Within the company setting the directors possess management powers,[1] which the law expects them to use in the best interest of the company. The attitude of the law towards company directors has been a very strict one, having ascribed to them different status, as discussed in the preceding chapter.[2] Thus, as trustee and agents of the company, they are corporate fiduciaries who are required to act bonafide and in the best interest of the company. Professor Olawoyin lucidly states the true position when he observed thus:

> Directors have certain management powers vested in them … powers of this sort must necessarily force certain duties upon directors.[3]

The common law rules regarding directors' duties are tailored towards the unbridled exercise of directorial powers considering the fact that as trustee of trust property of the company they have the tasking responsibility to discharge their functions creditably in the interest of the company and investors alike.[4] The point must be made that the duties of company directors

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1 S. 63(3) of the CAMA.

2 See the statement of Lord Selburn in Great Eastern Rly. V. Turner (1872) L.R. 8 Ch. 149 at 152.

3 See Olawoyin, Status and Duties of Company Directors, (Ile-Ife, Nigeria: University of Ife Press, 1977) p. 103.

4 York and North Midland Rly. V. Hudson (1853) 16 Beav. 485 Per Romily, M.R.

though are to be exercised collectively as a board in order to bind the company, they are owed individually to the company since they all occupy fiduciary positions to the company.[5] These duties are broadly categorised into two, namely, the fiduciary duties and the duties of care and skill. While the former is a derivation of equity, the latter is a product of common law. Concerning these two sources, Dr. Osumbor has observed that:

> Although it is true that the streams of equity and common law now flow in the same channel, it is still necessary to keep these differences in mind as far as directors duties are concerned because of the varying standard which apply.[6]

The codification of directors duties especially under the CAMA has been attacked on the premise that it is impossible to codify all aspects of directors duties in a single code. Secondly, the criticism also hinges on the fact that codification of directors duties would introduce the element of rigidity into company law practice which would offend against the dynamics of human nature. These aside, a rigid code will have the tendency of discouraging honest and conscientious persons from aspiring to the office of company directors, thus ultimately denying corporate entities the benefit of capable hands.[7] But Professor Gower[8] seems to have a contrary opinion on this. He observes that the failure of the English Parliament to codify directors duties in the 1978 Companies Bill was more as a result of disagreement amongst

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5 See Gower (5th ed) op. cit. 155; Barnes, K.D. Cases and Materials on Nigerian Company Law (Ile-Ife, Nigeria: Obafemi Awolowo University Press Ltd., 1992) at 271.

6 Osumbor, O.A., "The Company Directors: Its Appointment, Powers and Duties" in Essays on Company Law, (Lagos: University of Lagos Press, 1992) p. 40.

7 See generally, Osumbor, op. cit. at 140-141, Olawoyin, op. cit. at 32.

8 See Gower (5th ed) op. cit. at 155 note 5.

members rather than any perceived disadvantage of a code. He submitted that:

> A comprehensive statutory re-statement of these duties would make it more likely that they are observed; a belief strengthened by the fact that the main reason for giving up the attempt was the impossibility of obtaining agreement of the legal profession on precisely what the duties are.

In Nigeria, the Law Reform Commission achieved commendable success in its codification drive but sadly though the finished product of the codification endeavour is replete with unpardonable defects. Both common law and equitable duties of directors, which have separate identities are not properly streamlined.[9] Another glaring error is found in Section 279(4) of the Act which provides that directors in the performance of their functions must now have the interest of the company employees at heart. This is an onerous task as it is not stated in the Act what these interests comprise. Apart from these, there are other defects bordering on poor draftsmanship and printing errors which copiously run through most of the provisions. But others which are more serious will be highlighted in the course of this work. The various duties of company directors will now be examined in some details.

4.2 FIDUCIARY DUTIES OF COMPANY DIRECTORS

In *Hospital Products Ltd v. United States Surgical Corporation*,[10] Mason, J. defined the term 'Fiduciary' as a person who agrees or undertakes to act for, or on behalf of, or in the interest of another person in the exercise of the

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9 See Ss. 279(3), 282 and 283.

10 (1984) 156 C.L.R. 41.

power or discretion which will affect the interest of that other person in a legal or practical sense.

Under common law, directors owe their fiduciary duties to the company and the company alone and not to individual shareholders or investors. The consequence is that individual shareholders or investors cannot complain once directors are in breach of their duties. The *locus classicus* for the above proposition is *Percival v. Wright*.[11] In the case, the plaintiff shareholders had written to the Secretary of the company asking whether he was aware of any person disposed to purchasing their shares. Three directors of the company bought the shares at a fixed price from the plaintiffs. The plaintiff later realised that at a time when the directors acquired the shares, negotiations were pending for the sale of the company's undertaking which the directors did not disclose and whose disclosure would have had the likelihood of having a substantial impact on the share price if successful. However, the negotiation was not successful. This notwithstanding, the plaintiff brought an action against the directors to set aside the sale of their shares to the directors on the premise that the directors ought to have disclosed the negotiation for the sale of the company's undertaking. The presiding judge, Swintein Eary held that directors do not occupy a fiduciary position towards the shareholders in their individual capacities and as such were not duty bound to disclose the pending negotiation to the shareholders.

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[11] (1902) 2 Ch. 421.

The above decision has not been spared by critics who view it as a dangerous proposition that is adversarial to the interests of investors who in the first instance placed such directors in the confidential position to safeguard their interest.[12]

However, a painstaking examination of the facts of the case would reveal that the decision could be justified on its peculiar facts. In the case, apart from the negotiation not being successful, there was no indication of a concrete offer which the directors would have been duty bound to disclose to the shareholders. Again, it was the shareholders that invited the directors to buy their shares and the eventual purchase price was determined by an independent valuer. It was such an attempt to put the case in its true perspective that led the English court in *Allen v. Hyatt*,[13] to observe that a distinction should be drawn between this situation and where agency relationship can be implied from the conduct of directors or by express appointment by the investors. Thus in the case the directors had obtained from the shareholders the option to purchase their shares through a necessary representation to be able to effect an amalgamation with another company. The option was exercised by the directors who later resold the shares at a profit to the amalgamated company. While holding the directors liable to the shareholders the court observed that:

> … no doubt the duty of the directors was primarily owed to the company itself. It might be that in circumstances such as those

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12 See Olawoyin, op. cit at 46; Gower (5th Ed) op. cit. at 518.

13 (1914) 30 T.L.R. 444

> of *Peraval v. Wright* they could deal at arms length with a shareholder but the facts in the present case were widely different from those in *Pecaval v. Wright* and their lordships thought that the directors must here be taken to have held themselves out to the individual shareholders as acting for them in the same footing as they were acting for the company itself and was as agents.

Another situation where the directors would be duty bound to the investors is where the investors had expressly asked for the advice of directors on issues relating to company security. The English court has however premised such duty in tort and by so doing the court observed that the directors have the duty to act honestly and with due care.[14] The directors will thus be bound to give honest advice by ensuring that all material facts within their disposal are disclosed without reservation.

Professor Olawoyin[15] has however faulted this assertion, noting that the directors may yet avoid liability if they are not put on any specific enquiry. In his opinion the directors will be under no duty to disclose even if it is apparent that certain material facts were known to them which affect the fairness of the transaction between them and the investors. This is another area of the law that needs urgent review and an amendment. It is submitted that once it is established that the directors were aware of certain material facts which are likely to put the investors at a disadvantage, the directors should be duty bound to disclose such circumstances to the shareholders.

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14 Prudential Assurance Co Ltd. v. Newman Industries Ltd. (No. 2) (1980) 2 All E.R. 841.

15 Olawoyin, op. cit. at p. 47-48.

In the New Zealand's case of *Coleman v. Myers*,[16] the judge observed that *Perceval v. Wright* could not be cited as a general proposition that directors do not owe to their shareholders fiduciary duties but conceded that on its peculiar facts the case was rightly decided. Particularly instructive is his lordships statement in the course of his judgement that:

> … while it may not be possible to lay down any general test as to when the fiduciary duty will arise for a company director or to prescribe the exact conduct which will always discharge it when it does, there are nevertheless some factors that will usually have an influence upon a decision one way of the other. They include … dependence upon information and advice, the existence of a relationship of confidence, the significance of some particular transaction for the parties and of course the extent of any positive action taken by or on behalf of the director or director to promote it.[17]

The American courts have also developed the special facts doctrine in an attempt to state the circumstances under which the directors would be presumed to owe a duty to the shareholders.[18] In *Strong v. Repide*,[19] the court came to the conclusion that where directors are aware of special facts in the course of their relationship with the shareholders such as the value of the company shares and which shares the directors have the intention of purchasing, they have a duty to disclose to the shareholders those special circumstances.

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16 (1977) 2 NZLR 225.

17 Even in other jurisdictions such as Canada and Australia, the decision in Coleman v. Myers has been preferred. See Dusik v. Newton (1985) 62 BCLR 17.

18 See Gower; Some Contracts Between British and American Corporation Law (1958) 9 Harv. Law Review 1369; The Principles of Modern Company Law (3rd ed.) at 554, Note 99.

19 (1909) 213 US 419 at 431.

Special facts have been identified to include peculiar knowledge of the directors regarding important transactions, prospective mergers, probable sale of the company's entire assets or business, agreements with third parties to buy large block of shares at high price and pending declaration of unusual dividends.[20]

In Nigeria, the Law Reform Commission after a painstaking consideration of the position in other jurisdictions distanced itself from the position in *Perceval v. Wright*, settling eventually for the American position.[21] In its reports it observed that:

> It is a mistaken appreciation of where actual ownership of companies lies. Companies are owed by and exist for the benefit of individuals and for the purpose of making profit. Insisting that duties must be owed only to an abstract entity appears unjust and a total disregard to the interests of the individuals who formed the company.

Section 279(1) of the CAMA however codifies the general position in *Perceval v. Wright* that a company director stands in a fiduciary position towards the company and shall observe utmost good faith towards the company in any transaction with it or on its behalf. The problem however is with Section 279(2) that is meant to codify the exceptions. This provision has brought more problems than anticipated. For instance the section provides that:

> A director of a company shall also owe fiduciary relationship with the company in the following circumstances –

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20 See Ballantine on Corporation (1946) at 213.

21 See Report on the Reform of Nigerian Company Law, Vol. 1 at 210-211.

(a) where a director is acting as agent of a particular shareholder;

(b) where even though he is not an agent of any shareholder, such a shareholder or other person is dealing with the company securities.

Apart from the poor syntax of Section 279(2), if examined along side the common law position as to whom a director owes his fiduciary duties, codified under Section 279(1), it is obvious that Section 279(2) is not necessary since a company director always owes fiduciary duties to the company. As already pointed out, the provision of Section 279(2) is meant to reverse the decision in *Perceval v. Wright* by placing directors in a fiduciary relationship with shareholders in relation to dealings in securities. But due to poor draftsmanship, it defines the duty as a duty owed to the company rather than the particular shareholders or persons dealing with the company's securities. It is submitted that in order to actualise the intention of the Law Reform Commission, Section 279(2)(b) should be re-drafted as an exception to the general rule that a director owes his duty to the company.

It would also appear that the intention of Section 279(2)(a) is to codify the principle in *Allen v. Hyath*,[22] but by providing that the duty is owed to the company the Commission missed the intended attempt to codify the principle. In view of the original intentions of the subsection, it is submitted that the words company in the opening paragraph should be substituted with shareholder. This will put to rest the controversy surrounding the draftsman

[22] Supra.

attempt or failure at the codification of the principle. Particularly instructive in this regard is the observation of Dr. Osumbor that:

> [It] makes very little sense, it is too elementary, if not pedestrian to state that directors owe their fiduciary duty (not relationship) to the company. In any event, why should a director owe any duty to the company when he is acting as an agent of a shareholder? Its duty for instance is owned to the shareholder as a principal, not the company. Furthermore, the words "a shareholder" in paragraph (b) ought to read a director, else it is completely meaningless …[23]

The fiduciary duties as codified in the CAMA are divided into four:

(a) Duty to act in good faith and in the interest of the company;

(b) Duty to exercise power for proper corporate purpose;

(c) Duty not to fetter managerial discretion;

(d) Duty to avoid conflict of interest.

4.2.1 Duty to Act in Good Faith

As corporate fiduciaries directors are required to discharge their responsibilities with utmost honesty and in the interest of the company. The common law principle was ably enunciated in *Re Smith & Fawcet Ltd*.[24] where his lordship, Green, M.R, held that the test is whether the directors acted bonafide in what they considered as in the best of the company and not what a court considers to be in the best interest of the company and not for an collateral purpose.

The duty to act in good faith by company directors is codified under Section 279(3) CAMA which states that:

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[23] See Osumbor, Essays in Company Law, op. cit. at 141.

[24] (1942) Ch. 304 at 306 C.A.

> A director shall act at all times in what he believes to be the best interest of the company as a whole so as to preserve its assets, further its business and promotes the purposes for which it was formed and in such manner as a faithful diligent careful and ordinarily skilful director would act in the circumstances.

The above section, it is submitted contains both subjective and objective standard. There is no doubt that probably by inadvertence the draftsman has expanded the scope of the rule beyond *Re Smith & Fawcet*. It submitted that this is a very serious error, which is buttressed by the fact that by interposing objective standard an essentially common law requirement into Section 279(3), the draftsman was confusing equitable duties with those of common law. In view of the fact that Section 282(1) already imposes a reasonable standard on company directors pertaining to their common law duty of care and skill, Section 279(3) should be amended to enable it retain its original equitable character.[25]

The question then is, what constitutes the interest of the company? It appears that the relevant company interest is that of the shareholders or investors collectively. This is so in equity, as the term "company" is defined by reference to shareholders and not to the company.[26] Thus, in *Greenhalgh v. Aderne Cinema Ltd*.[27] the court observed that:

> … the company as a whole does not mean the company as a commercial entity, distinct from its corporators. It means the corporators as a general body.

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25 This submission has the support of Prof. Okonkwo. See Okonkwo, Unpublished lecture notes titled "Position of Directors" (Presented to Law Students at University of Nigeria, Enugu Campus) at p. 3.

26 See Palmer's Company Law, op. cit. at 963.

27 (1951) Ch. 286 at 291, Per Evashea M.R.

The close affinity between investors interest and corporate interest now has statutory backing under Nigerian company law. Thus, Section 279(4) mandates company directors while in the performance of their functions to also have regard to the interest of the employees and members of the company.[28] What is not clear however is whether directors duties in this regard go beyond the interest of present members. Though the CAMA is mute on this, it could be implied from the words 'include' and "other persons dealing with the company's security" used Section 279(4). Though there is the latter addition of clause (b) to Section 279(4)(a), it would be appreciated, if a clear worded statement is made as to the categories of members protected by Section 279(4)(a) and (b). This will do away with the unnecessary interpretation problems that has arisen from the loose provision of Section 279.[29]

In an apparent attempt to create avenues for the actualization of the true intent of Section 279(4), the CAMA has churned out other relevant provisions for this purpose. First, Section 159(3) makes provision for employees shares scheme by which a company is required to make available money for acquiring fully paid shares in the company for the benefit of not only ordinary employees but also directors holding salaried employment in the company. Similarly, Section 384 takes cognizance of profit sharing schemes for

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28 S. 279(4) is identical in wording with S. 309(1) UK C.A. 1985.

29 See Gaiman v. National Association of Mental Health (1971) Ch. 317 at 330, where Megarry J. held that directors fiduciary responsibility includes the interest of both present and future members. Dixon J. in Mills v. Mills (1938) 60 C.L.R. 150 at 164 (Aust. H.C.) observed that directors are not required by law to live in an unreal region of detached altruism and to act in a vague mood of ideal abstraction from obvious facts when he acts as a director.

employees' subject however to the contract of service of such employees. Thus, where an employee's contact of service permits he will be entitled to share in the profits of the company by way of incentive, whether or not dividends has been declared or not. Most importantly, Section 494(1) enjoins the director to ensure that in the process of winding up a company, the payment of the wages and salaries of employees are given priority.

Under certain circumstances the interest of a company may also include the interest of the creditors of the company.[30] This is where the company becomes insolvent and the company's capital and the financial interest of members have become extinguished.[31] The duty does not however arise if the company remains a going concern. One other area that has elicited quite interesting and illuminating commentaries is that of nominee directors. To whom do they owe their duty to act in good faith? Is it the company which they serve as directors or the person that nominated them? Though such nominee directors would naturally own their allegiance to the person nominating them, such a disposition is however seriously frowned upon by law.[32]

Section 283(1) of the CAMA in unmistaken terms provides that as trustees of their company's money, properties, the directors shall exercise their powers honestly and in the interest of the company and all the shareholders and not in their own sectional interests. The above principle was ably

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30 Lonhro v Shell Petroleum Co Ltd. (1980) 1 WLR 627 at 634 per Diplock L.J.

31 See Adebayo v. Johnoson & Ors (1969) 1 ANLR 171. See also S. 509 CAMA.

32 IN Boulding v Association of Cinematograph Television & Allied Technicans (1963) 2 GB 606 at 626, Lord Denning, MR observed that the practice everywhere recognises the appointment of nominee directors provided the freedom to exercise their judgement in the company's best interest is not encumbered in anyway.

illustrated in *Kuwait Bank v. National Nominees Ltd*.[33] In the case, a bank held forty percent of the shares of a company. Subsequently, it appointed as directors of the company two of its bank employees. But at the same time the Bank continued to pay the two banks' employee for the time they spent in acting as directors. The court held that while the two nominee directors owe a duty to the bank - their employer while discharging their responsibilities as company directors, their primary loyalty or duty when acting as directors was to the company. The court then held further that the directors were bound to ignore the interest and wishes of their bank.

It is obvious that the position of nominee directors is a very difficult one. It was in recognition of this that Lord Denning in an apparent condemnation of the unrealistic position of the law observed that it is impossible to assume that company directors "live in an unreal region of detached altruism and to act in a vague mood of ideal abstraction from the facts.[34] Professor Olawoyin sees the nominee director as being in a dilemma. In his words: "if he puts the interest of the party he represents above those of the company, he may in the process be in breach of his duty towards the company, while if he considers primarily the interest of the company, he faces the risk of dismissal by the party he represents."[35] Considering the peculiar Nigerian corporate environment, especially the distress syndrome that has

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33 (1991) 1 AC. 187 PC

34 See Gower (5th ed.) op cit. at 556 borrowing the words of Latham C.J. in Mills v. Mills (1938) 60 CLR 150 (Austr. H.C.)

35 See Olawoyin, op. cit. at 51.

bedeviled it due to the self-serving nature of company directors, the position of the law should remain undisturbed, at least for now.

4.2.2 Duty to Act for Proper Corporate Purpose

This principle was enunciated as far back as 1854 in *Re Cameroon's Coal Brook Steam Coal, & Swansea & Laugher Railway Co. (Bannet's Case)*,[36] where Turner, L.J. stated in respect of company directors that "… powers given to them for one purpose cannot … be used by them for another different purpose …" Again in *Re Smith & Fancett Ltd*.[37] Green, L.J. emphasised that company directors must act "*bonafide* in what they consider … is in the best interest of the company and not for any collateral purpose."

Lord Green's statement has however been subjected to two varied interpretations by the courts of different jurisdictions. In the English case of *Hogg v. Cramphorn Ltd*.[38] Buckley J was of the view that the duty to act for a proper corporate purpose which is objective in nature is quite different from the duty to act *bonafide* in the company's interest which is subjective. In his opinion a company director would be in breach of his duty to his company where he exercised his powers for an improper purpose even though the act itself was *bonafide* and in the best interest of the company. But Berger J. in the Canadian case of *Tech Corporation Ltd. v. Miller*,[39] held that once directors have acted *bonafide* and in the company's best interest, the question whether they acted for an improper corporate purpose would not arise.

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36 Per Turner L.J. (1854) 5 G.M & G 284 at 298.
37 (1942) Ch. 304 at 304 (C.A)
38 (1967) Ch. 254 at 266-268.
39 (1972) 33 D.L.R. (3d) 288 British Columbia at 312-317.

Surprisingly, the above divergent decisions have received tacit judicial and academic recognitions. In *Olson v Phoenix Industrial Supply Co*.[40] the court approved Berger's approach. The court held that since the act of the directors is believed by them to be in the best interest of the company, they could not be held liable even though it was for an improper purpose. But a contrary decision was however reached in *Exco Corporation Ltd v Scotia Savings & Loan Co*,[41] where the court, apparently distancing itself from Berger J position held that where directors exercise their management powers for an improper corporate purpose, their act would be invalidated notwithstanding the fact that the directors acted *bonafide* and in the best interest of the company.

From the academic viewpoint, while some authors are of the opinion that the duty to act *bonafide* and the best of the company is quite separate so that directors may nevertheless be held liable where they act *bonafide* but for an improper corporate purpose,[42] others are of the opinion that the two should be synonymous in order to allow directors the freewill needed to take managerial decisions.[43]

It is submitted that considering the sensitive nature of the various competing corporate interests that would usually be at play in a company setting a different view may be canvassed. The interests that are usually in

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40 (1984) 9 DLR (4th) 451, Manitoba

41 (1987) 78 (2d) Nova Scotial

42 See Franzi, NCA. The subjective and objective elements of a Boards' power to issue shares (1976) 10 MULR 392; Gower, (5th ed) op cit at p. 536.

43 See Ziegel J.S. "Directors Powers and the Proper Purposes" (1974) J.B.S 85; Slusky, BV Canadian Rejection of the Hogg v Cramphorn "Improper Purposes" principle – a step forward? (1974) 37 MLR 457.

conflict are those of the investors, creditors, directors, the public, the employees, and the government. In order to ensure that a proper equilibrium is achieved amongst these competing interests, only an adjective standard would achieve the intended purpose. It is the courts responsibility to decide whether the proper balance has been maintained in a given situation.

A painstaking and exhaustive review of the proper purpose doctrine as well as the test to be applied was undertaken by the court in *Howard Smith Ltd v Ampol Petroleum Ltd,*[44] while approving the decision in *Tech Corporation case*. As for *Hogg v Cramphorm*, though the court approved of the decision, nevertheless it propounded a quite different formulation to be followed in handling future similar cases. Because of the importance of the Ampol Petroleum case, it would be necessary to reproduced in detail the court's pronouncement thus:

> When a dispute arises whether directors of a company made a particular decision for one purpose or for another or whether, there being more than one purpose, one or another purpose was the substantial or primary purpose, the court in their lordships opinion is entitled to look at the situation objectively in order to estimate how critical or pressing or substantial or per contra, insubstantial an alleged requirement may have been. If it finds that a particular requirement, though real was not urgent, or critical, at the relevant time, it may have reason to doubt, or discount the assertions of individuals that they acted solely in order to deal with it, particularly when the action they took was unusual or even extreme…
> To define in advance exact limits beyond which directors must not pass is in their lordships view, impossible.
> This clearly cannot be done by enumeration since the variety of situations cannot be anticipated. No more, in their lordships' view, can this be done by the use of a phrase – such as '*bonafide*

[44] (1974) AC 821

> in the interest of the company as a whole,' or for some corporate purpose. Such phrases, if they do anything more than restate the general principle applicable to fiduciary powers at best serve, negatively to exclude from the area of validity cases where the directors are acting sectionally or partially i.e. improperly favouring one section of the shareholders against another…
>
> In their lordships' opinion, it is necessary to start with a consideration of the power whose exercise is in question… Limits within which it may be exercised, it is then necessary for the court… to examine the substantial purpose for which it was exercised and to reach a conclusion whether that purpose was proper or not. In doing so, it will necessarily give credit to the *bonafide* opinion of the directors, if such is found to exists, and will respect their judgement as to matters of arrangement…

As is implicit in the above decision the court would always pay more attention to the actual purpose for the exercise of directors powers rather than being unduly swayed by the mere fact of the *bonafide* nature of the directors action. Of course the court in discharging their responsibilities would usually crutinise the circumstances of every case before it objectively to unearth the real purpose for granting the powers to the directors. Where however the purposes are more than one the court is required to find out the dominant purpose and where this coincide with the proper purpose, the court will be at liberty to validate the directors act including the particular transaction notwithstanding any adverse consequences to investors[45] or any beneficial result for a director.[46]

One area where the proper purpose doctrine has been applied frequently is in relation to the powers of directors to issue shares as well as adopting defensive measures when confronted by unwelcome take over bids.

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45 See S. 279 (5) CAMA

46 See Hivseche v Sims (1894) AC. 654; Richard Brady Franks Ltd v Price (1937) 58 CLR 112 (Austr. HC); Mills v Mills (1938) 60 CLR 10 (Austr. HC)

The previous attitude of the courts were that directors power to issue shares was given purposely to raise capital for the company.[47] But in *Ampol Petroleum's case* the court enlarged the scope for the application of the principle. Apart from doing away with self-interest of directors as a basis for invalidating an improper issuance of shares by company directors, it equally debunked the approach that the only right purpose for which shares can be issued is to raise capital. The correct approach in the view of lord Wilberforce is that directors power to issue shares cannot be so limited and that the primary concern should be to find out the main or substantial purpose for exercising the power.

It is submitted that the decision in the *Ampol Petroleum case* is a pragmatic one which is a welcomed development in all its ramification. Since it is hinged on the courts examining the facts of every case on its peculiar circumstances, it will more readily achieve a balanced conclusion or result.[48]

The common law proper purpose doctrine is now codified in Section 279(5) of the CAMA. Accordingly, once a director acts outside the powers conferred on him by the relevant company's articles and for purposes different from those envisaged he will be liable under the proper purpose doctrine. It will not be an acceptable defence for a director to plead that he acted bonafide and in the best interest of the company.

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47 See Punt v Simmons & Co Ltd (1903) 2 ch 506; See also Gower (3rd ed) op cit at 524; Morse op. cit at 394. See Tika Tore Press v Abina (1973) 1 ALL NLR 407

48 See Sasegbon "Nigerian Company and Allied Matters Law Practice" (Ikeja – Nigeria: DSC Printing Co. 1991) Vol. 2, p. 423.

One problem which tends to create confusion while interpreting the proper purpose doctrine is section 279 (3) of the CAMA. The section appears to run counter to section 279 (5) as it gives a different impression that directors have abundant leeway to maneuver when resisting hostile offers for take over bids. Section 279 (3) provides that:

> A director shall act at all times in what he believes to be the best interest of the company as a whole so as to preserve its assets, further its business and promote the purpose for which it was formed and in such manner as a faithful, diligent, careful and ordinary skillful director would act in the circumstances.

Considered alongside section 283 of the CAMA which provides that directors shall exercise their powers honestly and in the company's best interest and that of the shareholders, it is obvious that these provisions have made nonsense of the intended aim of section 279(1) by creating difficult huddles. Thus, once directors could show that a policy conflict exist between the need to safeguard the interest of the company and the need to take over the assets of the company, the directors would be at liberty to resist a take over bid. It is submitted that considering the peculiarity of the Nigerian situation where in fighting and sit tight syndrome of company directors is rampant, even where they lacked the requisite managerial acumen, Section 279 (3) should be further qualified to the effect that where directors act to prevent a takeover bid which they consider necessary and in the best interest of the company as a whole in order to preserve its assets, business and promote the purpose for which it was formed, they must show that they took their action pursuant to making reasonable and painstaking investigation, a requirement almost similar

to that formulated by the Delaware Supreme Court in *United States in Cheff v. Mathes*.[49]

It is noted however that where directors exercise their powers for an improper corporate purpose, that merely renders the transaction voidable. However, unlike under the common law, where such an action can be ratified,[50] Section 279(8) outrightly strips the shareholders of such powers. This, it is submitted, is a just provision considering the disadvantageous position which the minority investors occupy in the company. Section 279(8) thus ensures that the voting rights of the minority shareholders are not unduly manipulated for the self serving interest of the directors.

4.2.3 Duty Not to Fetter Discretion

The companies articles usually confer on the directors some considerable discretion in the running of the companies affairs. It will be wrongful on the part of a director to enter into an agreement to fetter his future discretion since the powers conferred on him by the articles are held on trust for the company.[51]

This duty is crucial especially in the case of a nominee director. This practice was rampant during the Federal Government indigenization's era when the Indigenization Act of 1972, allowed Government substantial holdings

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49 A 29 548 at 554 (1964)

50 See Hoog v Cramphorn Supra, where Bukley J. vividly illustrates the principle. In that case the shareholders ratified the directors issuance of shares for an improper corporate purpose by ordinary resolution.

51 See Clark v Workman (1920) 11r. R 107

in several key industries. And after the Indegenization Act,[52] the Nigerian management in those companies toed the line of Government appointors to the detriment of the companies, thus fettering their managerial discretion. This was clearly placing the interest of their appointors above that of the company they were managing or directing. Lord Denning, M.R. aptly emphasized the principle when he observed that:

> There is nothing wrong in it (i.e. in a director acting as a nominee of an appointor). It is done everyday. Nothing wrong, that is, so long as the director is left free to exercise his best judgement in the interest of the company which he serves. But if he is put upon terms that he is bound to act in the affairs of the company in accordance with the directors of the patron, it is beyond doubt unlawful.[53]

It is in the area of the exercise of the voting power of directors that the exercise of managerial discretion often come into play. The general principle is that directors cannot validly contract either with one another or with third parties to exercise their voting power in a particular manner at Board meetings.[54] According to Professor Gower,[55] the position remains the same even where improper motive or personal profit is not imputed on the part of the director.

However, it has been suggested that a director could while in the *bonafide* exercise of his discretion enter into contract on behalf of the company and validly agree to take such further action at Board meetings as are necessary to carry out the agreement reached in that contract. In *Thorby*

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52 See the Indigenization Act 1972.
53 See Boutling v. ACTAT (1963) 2 Q.B. 606 at 626
54 S. 279(6) of the CAMA.
55 See Gower, Principles of Modern Company Law (3rd ed.) op. cit. at 525.

v. Goldberge,[56] where this exception was admitted, Kitto J. pertinently observed that:

> There are many kinds of transactions in which the proper time for the exercise of the directors discretion is the time of the negotiation of a contract and not the time at which the contract is to be performed … If at the former time they are *bonafide* of opinion that it is in the interest of the company that the transaction should be entered into and carried into effect, I can see no reason in law why they should not bind themselves to do whatever under the transaction is to be done by the Board.

This decision and the exception recognised therein appear well founded. As long as the directors involved in the negotiation of such contracts do not exhibit any ulterior motive or self serving interest, there should be no reason why they should be prevented from carrying into execution the line of action earlier agreed upon by them at the initial stage of negotiation.

It appears that the duty not to fetter managerial discretion will not be binding upon company directors once the agreement to fetter discretion was entered into. In *Ringuet v. Bergeron*,[57] the Canadian court held that where directors and shareholders enter into an agreement to vote in a particular manner at a general meeting, such a meeting cannot be invalidated. The reason for this is not far-fetch since one of the parties likely to complain in the event of directors fettering their discretion is the shareholders. Thus having bound themselves in such an agreement, neither the shareholders, nor the directors are likely to complain. But Professor Gower has however warned the directors of the danger of carrying such a practice too far. On this the learned

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[56] (1964) 112 CLR 597 (Aust. H.C.)
[57] (1960) 24 DLR (2d) 449.

author has observed that such an agreement is likely to be challenged and possibly invalidated at a later date by the company where a new board, a later member or a liquidator initiates action on behalf of the company.[58] This will be the case where the directors are found to have secured such an agreement by any form of manipulation.

In *Savoy Hotel Ltd. Investigation*,[59] the directors skilfully used their controlling position to obtain an irrevocable covenant that the premises of Savoy Hotel should not be converted to an office.[60] The purpose of the covenant was to render ineffective a take overbid by a bidder who wanted to convert the Hotel into an office area. To actualise this, the directors alloted substantial shares to trustees to hold for the benefit of the employees which gave them voting powers. In this manner the directors ensured that the majority shareholders would not be able to challenged them at a subsequent date. Mr. Milner, Q.C., an investigator later appointed to investigate the affairs of Savoy Hotel discovered that the directors breached their duties to the company having fettered the discretion of the future Board members and shareholders on how the property of the company was to be used.

Delegation of duties by company directors also constitute an aspect of the duties which lie on company directors not to fetter their discretion. The position is that on those established circumstances where directors are not prohibited to delegate their duties to subordinate members of the company,

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58 See Gower (5rd ed.) op. cit. at 525-526.

59 See Savoy Hotel Ltd. Investigation and the Berkeley Hotel Investigation under S. 165(6) of the Companies Act (1948) (H.M.S.O. 1954), See also Pennington, op. cit. at 541.

60 Supra.

they must do so without abdicating their responsibilities because delegation does not imply abdication or denunciation of power and authority.

Under Nigerian Company Law, company directors are allowed to delegate their duties to a manager or a committee which they have appointed[61] as long as the Board maintains a firm control and supervision over them. Without the exercise of such control and supervision, that would amount to abdication of duty.[62]

No doubt, there is considerable wisdom in denying the directors the power to confer unlimited power delegation on committees and managers. Such uncircumscribed power delegation could be likened to an unruly horse which no one can tame. As similarly noted by Sasegbon,[63] an unlimited power delegation would be subject to abuses and manipulation.

It is submitted that considering the fact that directorial positions are sensitive and specialised positions where special training in certain areas is now a necessity in modern times, it would be suicidal to commit matters of management to persons who are devoid of the requisite skill necessary to keep the company going. Unrestrained delegation would also amount to denying shareholders the necessary protection which they need to guarantee their investment. Only a sound management team constituted by well tested, well informed and skilful directors can achieved that purpose.

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61 See Ss. 64 and 165 CAMA. See also Adebayo v. Johnson & Others (1969) 1 ANLR 171.

62 See Kyshe v. Alturas Gold Company (1885) 4 T.L.R. 331; Horn v. Henry Faulder and Co. Ltd. (1908) 99 L.T.S. 524.

63 See Sasegbon, op. cit. at 436.

4.3 DUTY TO AVOID CONFLICT OF INTEREST

Company directors are expected to exhibit a high standard of loyalty and transparency to their companies since they own fiduciary duties to the companies. Thus it has been the rule that company directors must not enter into transactions which are likely to result into a conflict between their loyalty to the company they manage and their own personal interest. The origin and basis of the rule is in agency which is well highlighted in the House of Lords decision in *Aberdeen Railway Co. v Blaike Brothers*,[64] in these terms:

> A corporate body can only act by agents, and it is, of course, the duty of those agents so to act as best to promote the interests of the corporation whose affairs they are conducting. Such agents have duties to discharge of a fiduciary nature towards their principal. And it is a rule of universal application that no one, having such duties to discharge, shall be allowed to enter into engagements in which he has, or can have, a personal interest conflicting or which may possibly conflict with the interest of those whom he is bound to protect…"[65]

Profit making on the part of a director is a criteria for determining a breach of this duty. Once a director puts himself in a conflict of interest and duty situation he would be in breach of his duty to the company. But in any case where a director uses his position to make profit that is unauthorised he would be in breach of this duty.[66] The relevant principles governing the rule that a director must not profit from his position as director nor engage in transactions that are likely to put his interest in conflict with the interest of the

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64 (1854) 1 Marg 461, per Lord Cranworth

65 See also Bray v Ford (1896) Ac 44 at 51 – 52; See also Sealy who has criticised the application of the rule in Aberdeen v. Blaike as not acknowledging the fact that where a director is involved in a transaction with his company, the company can appoint a disinterested quorum to act on behalf of the company

66 See Industrial Dev. Consultants v. Cooley (1972) 1 WLR 443 at 451, Per Roskill J, Regal (Hastings) Ltd. v. Gulliver (1967) 2 A.C. 134; (1942) 1 All E.R.

company are now codified under Section 280 of the CAMA. The section reads thus:

> (1) The personal interest of a director shall not conflict with any of his duties as a director under the Act.
>
> (2) A director shall not –
>
> (a) in the course of management of affairs of the company; or in the utilization of the companies property, make any secret or achieve other unnecessary benefit.

The circumstances under which the principles would apply will now be considered under three basic heads.

4.3.1 Directors Contract with the Company

The law does not specifically prevent a company director from entering into contracts with a company whose affairs he manages but that should not be so where there is likelihood of conflict between his personal interest and that of the company. The effect of the breach of this rule is that the contract is voidable at the option of the company and the director would be bound to forfeit any profit made to the company.

This principle is well illustrated in the leading case of *Aberdeen Railway Co. v. Blaike Brothers*,[67] where Lord Camworth L.C. succinctly observed that:

> A corporate body can only act by agents, and it is, of course, the duty of those agents so as to act as best to promote the interest of the corporation whose affairs they are conducting. Such an agent has duties to discharge of fiduciary character towards his principal. And it is a rule of universal application that no one, having such duties to discharge shall be allowed to enter into engagements in having a personal interest conflicting or what

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[67] Supra at p. 47-472; See also Transvaal Lands Co. v. New Belgium (Transvaal Land Dev. Co. (1914) 2 Ch. 488 C.A.

> possibly may conflict with the interest of those whom he is bound to protect. So strictly is this principle adhered to that no question is allowed to be raised as to the fairness or unfairness of a contract so entered into.

It appears that the reason why the courts have refused to consider the question of the fairness or otherwise of a particular transaction is as a result of the difficulty entails in discovering whether a director had infact obtained a benefit in such circumstances.[68] Thus once it is ascertained that a company director has entered into a transaction with his company in circumstances in which his personal interest conflicts with his duty to the company, the company will not be bound by such contract. This principle is reasonable and just. To do otherwise would mean the court putting itself into an extremely tight and helpless situation where many a company director would escape from justice where no specific advantage is traced to the director.[69]

In deciding the knotty question whether a director has put himself in a position where his personal interest conflict with that of the company, it seems there is no hard and fast rule laid down by the courts. Each case will have to be examined on its merits. This is brought out succinctly in the dissenting judgement of Lord Upjohn in *Boardman v. Philipps*,[70] where his lordship said that:

> The phrase "possibly may conflict" [in the dictum of Lord Cramworth] requires consideration. In my view, it means that the reasonable man looking at the relevant facts and circumstances of the particular case would think that there was a real sensible possibility of conflict, not that you could imagine some situation

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68 See Olawoyin, op. cit at p. 73.

69 See also Lagun Nitiate Co. v. Lagunas Syndicate (1899) 2 Ch. 392 at 443.

70 (1967) 2 A.C. 46 at 124.

> arising which might, in some conceivable possibility in events not contemplated as real sensible possibilities by any reasonable person result in a conflict.

Sealy's reaction to the above rule has been that the application of the rule in its true form and substance to directors as trustees is unfair. He says that a disinterested Board, is competent to act on the company's behalf in transactions where one of the directors has shown an adverse interest.[71] However, Professor Olawoyin's position and rightly it is noted is that, a director affected may have an overbearing and lingering influence on the Board so much so that even where he is not present in the Board his ghost will still prod other members to decide matters in his favour.[72] Such overbearing influence over other board members may arise from previous friendship and association.[73]

As stated before, the effect of the breach of this rule is that the contract is voidable at the option of the company and the directors would be bound to forfeit any profit made to the company. The position remains the same even if the directors disclose the particulars of such contracts to the Board of Directors. But this rule is no longer an inflexible one. With time, the courts attempted a modification of the rule by holding that if a director discloses his interest and the particulars of such contract to the general meeting and the latter affirms such transaction, even if by majority votes, the contract is valid

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71 See Sealy, "The Directors As Trustee (1967) CLJ 83 at 96.
72 Olawoyin, op. cit. at p. 69.
73 See Rothenburg v. Franklin Washington Trust Co; 12 A (2d) 667 at 672.

and enforceable. Thus in *Northwest Transport Ltd. v. Beatty*,[74] a director as well as a majority shareholder of a company sold a steamer named United States Umpire to the company and got the general meeting to approve it while exercising his right as a shareholder at the meeting. The plaintiff challenged the sale on the basis of breach of fiduciary duties. The court held that though as a general rule a director cannot contract with his company such rule may however be relaxed if the general meeting approves of it except where the approval was a product of improper or unfair means or is illegal or fraudulent or oppressive to the majority.

This principle which has been codified under Section 284 of the CAMA provides that a director shall not sell to his company, or purchase from his company a non-cash asset unless the transaction is first approved at the general meeting – if the value is not less than ₦21,000.00 but exceeds ₦100,000.00 or 20% of the company's asset determined by reference to the account of the company prepared or where no account has been prepared and laid before that time, the amount of the company's called up share capital.

Prior to the advent of CAMA, there existed a practice where businessmen used to insert a clause in the article called a waiver clause. This entitles the breach of the principle to be waived. Section 279(8) of the CAMA has however rendered inoperative such practices. The section provides that no provision whether contained in the article or company's resolution or in any

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[74] (1887) 12 App. Cas. 589.

contract shall relieve a director from his fiduciary duty or from any liability incurred once the duty is breached.

Another relevant provision touching on the fiduciary duties of directors is Section 277 which also requires directors to disclose their interest in any contract to the company at the earliest possible time. Specifically, the section provides that it shall be the duty of the director of a company who is in any way whether directly, or indirectly interested in a contract or proposed contacts with the company to declare the nature of his interest at a meeting of the directors of the company. Failure to comply with this provision makes a director guilty of a fine of ₦100.00.

The problem in interpreting the provision of Section 277 has been whether a director's mere disclosure of his interest to the Board of Directors would validate the transaction to the extent of doing away with the necessity of complying with Section 284 which requires the approval of the general meeting. In *Holy-Huchinson v. Brayhead Ltd.*[75] It was the courts decision that non-disclosure does not render the contract void but voidable.

4.3.2 Use of Corporate Property, Information or Opportunity

This duty preclude directors from using their offices to make secret profits by the use of corporate assets, information or opportunity arising from their position as directors. Secret profits in this case concerns all profits made by a director without the knowledge of his company in circumstances where he should have informed them and obtained the necessary consent. At the

[75] (1968) 1 Q.B. 549 CA.

beginning, the director could only be made liable where the company could establish ownership to the secret profits. The position has since changed so that a company is now entitled to secret profits or commission received by directors even in cases where the company could not have obtained them for itself.[76]

Section 280(2) codifies the principles by providing that a director shall not: (a) in the course of management of the affairs of the company; or (b) in the utilization of the companies properties, make any secret profit or achieve other unnecessary benefits. The section further provides that a director who makes any secret profit or unnecessary benefit shall be accountable to the company for them.

The applicable principles are well illustrated by the English case of *Regal (Hasting) Ltd. V. Gulliver*.[77] In that case a company which owned a cinema decided to acquire two additional cinema in the same location with the intention of disposing off the three as going concerns. The directors then formed a subsidiary to take a lease of the other two cinemas. Their owners however asked for a personal guarantee of the rent by the directors or that the paid up share capital of the subsidiary should not be less than £5,000.00. The company only raised £2,000.00 and therefore shares worth £3,000.00 were allotted to five other members including two directors of the holding company, brought in by the Chairman, as beneficial owner. Three weeks later,

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76 Olawoyin G, Status and Duties of Company directors, (University of Ife, Ile-Ife, Nigeria, 1977) at pp. 182-186.

77 (1942) All E.R. 375.

the value of the shares increased and the directors decided to sell all the shares of the two companies and made a profit of £2.16 per each share instead of selling the properties of the two companies. The new controllers of the company brought an action against the directors to recover profits made in the transaction. Though the court found as a fact that the directors did not act fraudulently or in bad faith, but instead had taken the required steps to facilitate the transaction for the company which unfortunately, the company was unable to finance from its resources. All the same, the House of Lords held that the directors were liable to account to the company. Lord Macmillan explained the rationale for the decision in this manner:

> … what the directors did was so related to the affairs of the company that it can properly be said to have been done in the course of their management and in utilization of their opportunities and special knowledge as directors; and (ii) that what they did resulted into a profit to themselves.[78]

It is not an excuse on the part of the directors to claim that they acted *bonafide* or without fraud or that the company was unable to finance the venture or that the company incurred no loss at all. The decision in the *Regal's case* has however been vehemently criticised. Professor Gower described it as "carrying equitable principles to inequitable conclusion".[79] But, he blamed the directors for not taking advantage of their controlling majority in the general meeting to ratify the transaction. It is submitted that instead of allowing the new purchasers to receive the secret profits, the solution proffered by

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78 Ibid at 153.

79 Gower, Principles of Modern Company Law, 5th Ed. (London: Stevens & sons, 1998) at p. 549. The absence of equity arises from the fact that the new purchasers were allowed to recover the profit.

Professor Olawoyin,[80] that such secret profits should be given to the original shareholders at the time the directors misdeeds took place is more preferable. This view can be fortified by a new legislation.[81]

It is clear from the House of Lord's decision in Regal and the subsequent commentary of Professor Gower that directors could by a majority resolution at the general meeting retain secret profits. It is also easy to comprehend why the same was not possible in *Cook v. Decks,*[82] even though both cases shared almost similar factual situations.

In the instant case, the directors got for themselves a contract which could have been taken by the company. The directors did this by passing a resolution at the general meeting and supported by their votes as holders of three forths of the issued shares. As a result of this the company lost the benefit of the contract. Though no fraud was discovered in the directors conduct, the court held that as trustees of the company property, their conduct amounted to a breach of trust towards the company which was incapable of ratification in their capacity as shareholders.

Gower's explanation for the courts different approach in *Cooks v. Deeks* is that there is a world of difference between:

(a) misappropriating the company's property, and

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80 See Olawoyin, "Status and Duties of Company Directors. Supra at pp. 182-186; See also Ferlman v. Ferlman (1955) 219 FED. 173.

81 See Ayua, "Nigerian Company", United Kingdom (Graham Burn, 1984 at p. 184, where he completely agreed with the ratio in Regal's case.

82 (1916) 1 A.C. 544.

(b) merely taking an incidental profit for which directors are liable to account.[83]

Gower's further contention is that while *Cooks v. Deeks* fall within the first situation, since it was the duty of the directors to acquire the contract on behalf of the company, and that allowing the directors conduct to be ratified would amount to allowing the company to give away part of its assets. In the case of Regal Hastings, he remarked that the directors cannot be said to have misappropriated any company's property and as such it was possible to ratify the directors conduct especially since the company lacked the financial muscle to finance the contract.

A case which appears to have laid to rest the academic controversy and strengthened Professor Gower's position on the question of ratification is that of *Daniel v. Daniel*.[84] In that case, a company sold land to the 2nd defendant (who together with the 1st defendant were majority shareholders and directors of the company) for the sum of £14,250 on the instructions of the first and second defendant as directors. The land was later sold by the 2nd defendant for £120,000. The plaintiff minority shareholders later brought an action against the defendant alleging that the land was sold at an undervalue to the 2nd defendants. The court held that a minority shareholders action was

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83 See Gower, Principles of Modern Company Law, Supra at pp. 617-619. See also K.W. Wedderburn, "Shareholders rights and the rule in Foss v. Herbottle (1957) C.L.J. 194; (1958) C.L.J. 93, 103-105; See Professor Beck, "The Sage of Peso Silver Mines" (1971) 49 Can. Bar. Rev. 80, 116-117, where he rejected the view that there is a demarcation between Regal and Cooks v. Deeks.

84 (1978) Ch. 406.

possible where the directors use their powers intentionally, fraudulently or negligently and in a manner which benefits them as the company's expense.[85]

What is discernable from the above decisions and the subsequent controversy is that in determining the criteria for ratification of directors conduct two situations are distinguishable:

(i) Where the property in question whether opportunity or information or real assets belongs to the directors. Here, in both law and equity, ratification is possible by the company.

(ii) Where the property could be owned by directors at law but under some situations where equity would presume ownership in favour of the company. Here, the directors conduct cannot be ratified as they are deemed to be acting as constructive trustees.

The position in Nigeria as far as secret profits by directors is concerned is a very strict one. In this regard, section 280(4) of the CAMA states that "the inability or unwillingness of the company to perform any functions or duties under its articles and memorandum shall not constitute a defence to any breach of duty". It is submitted that this current position of the law is unsatisfactory. It is further submitted that it is more inequitable and an obvious act of high handedness to deny a director the right to take up a contract in his name when his company might have either considered same not viable or is incapacitated to take it up. Where a director possesses the

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[85] See Bakinbinga, "Ratification: Reconciling, Cook v. Deeks and Regal (Hastings) Ltd. V. Gulliver" (1986) N.L.J. 127, where he stated that the decision in 'Daniels v. Daniels was a vindication of Prof. Gowers stand on the issue of ratification.

financial will to take up such a contract, he should be allowed, as long as it does not interfere with his directorial responsibility to the company. Continued insistence on Section 280(4) would achieve no fruitful result. The law should be modified to permit directors in appropriate cases[86(a)] to take up such contracts and possibly retain the profits. In *Industrial Dev. Consultants v. Cooley*,[86(b)] the defendant was Managing Director of the plaintiff's company. The defendant tried and failed to secure contracts for the company with another Gas Board due to the fact that the Board was not favourably disposed to the set up of the plaintiff's company. Subsequently, however, the Board approached the defendant on a private arrangement and proposed that he should act as an architect for the Board. The defendant was clearly told that it was a personal arrangement to him. The defendant on the strength of this information, resigned his appointment and accepted the offer. The court nonetheless held that the defendant was liable to account for all the profits he derived from the contract or alternatively liable for damages since he made use of the company's property, though he made the profit while away from his office.

The foregoing analysis deals with situations where directors made secret profits while still occupying their position as directors. Section 280(5) of the CAMA makes provision in respect of directors who make secret profits after ceasing to be directors of the company e.g. by resignation. The attitude of the law is that such a director could still be made accountable for secret profits

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86(a) See the Canadian case of Peso Silver Mines v. Cooper (1966) 15 DLC 2d.

86(b) (1972) 1 WLR 443; (1972) 2 All E.R. 162.

made by using company's corporate assets, information and opportunity while still holding office.[87(a)]

4.3.3 Competing with the Company

Prior to the promulgation of the CAMA, the law in this area remained unclear when determining whether or not a director is permitted to engage in any business or transaction that is capable of giving rise to a conflict of interest between his private interest and his duties to the company. The law then represented by *London and Mashonaland Exploration Co. v. New Mashonoland Corporation Co*.[87(b)] was that a director could not be restrained from acting as a director of a rival company, except prohibited by the company's regulations or contract of employment.

Professor Gower,[88] had problem accepting the decision in the case. In his considered opinion:

> … the duty of fidelity flowing from the relationship of master and servant may preclude a servant from engaging, even in his spare time, in work for a competitor and the servant duty of fidelity imposes lesser obligation than the full duty of good faith owed by a director or fiduciary agent. How can it be that a director can compete whereas a subordinate employee cannot? … Moreover, one who is a director of two rival concerns is walking a tight rope and at risk if he fails to deal fairly with both.

The support for Gower's observation can be found in the case of *Thomas Marshall Exploiters Ltd. V. Guile*,[89] where the managing director of a company who was under a service contract was prohibited from engaging in

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87(a) S. 280(5) CAMA. See Canadian Ecro Services v. O'Malley (1973) 40 DLR (3rd) 371

87(b) (1891) WN. 165 approved by Lord Blannesburgh in Bell v. Lever Brothers Ltd. (1932) AC 161 at 195 H.C.

88 See Gower, (5th ed.) op. Cit. At 599.

89 (1978) 2 WLR 116.

any other business without the company's consent or disclosure of confidential information. The managing director was found to have done both and converted the proceeds to himself. He was held to be in breach of his duties.

In Nigeria, the law is now firmly established under section 281 – which provides that multiple directorship shall not be a ground for derogation from the fiduciary duties of the directors. Consequently; it is a breach of the fiduciary duties of the director to engage in rivalry or competition with the company.

In summation, the implication of section 281 is that multiple directorship or competing business is allowed under Nigerian law except where it would lead to a breach of fiduciary obligation. Above all, a company director must keep his employer abreast of his multiple relationship with other rival companies.

4.4 DUTIES OF CARE, SKILL AND DILIGENCE

The duties of care, skill and diligence constitute the second most important aspect of the directors duties to the company. Before 1990, the Common Law Standard, an inflexible and less complex rule held sway. The reason was that most directors at the time were appointed for the purpose of attending Board meetings, but lacked the requisite knowledge of commercial life. Added to this, is that most appointments were motivated by the need to confer favour on the appointees, who were not bound to bring any special qualification to their office. Most of them were also completely ignorant of

their functions.[90] Considering the fact that there were, and still are different levels of company businesses in the commercial horizon, it must be practically difficult for the courts to foister upon company directors one uniform standard of the duties. As pertinently pointed out in *Recity Equitable Fire Insurance Co*:[91]

> It is indeed impossible to describe the duty of directors in general terms, whether by way of analogy or otherwise. The position of a director of a company carrying on a small retail business is very different from that of a director of a railway company. The duties of a bank director, and the duties of a director of one insurance company may differ from those of a director of another.

In this case, Romer, J. laid down three formulations as necessary yardstick for gauging the performance of directors. First, he said that:

> a director need not exhibit in the performance of his duties a greater skill than may reasonably be expected from a person of his knowledge and experience.

The above test bases a director's liability on the kind of knowledge and diligence expected of directors of his own standing or background. This was a subjective test which requires that an enlightened director would be judged by the standard of an enlightened person. The same goes for an illiterate director, which is the standard of an illiterate person.[92]

Secondly, he said:

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90 See Re Brazilian Rubber Plantation and Estate Ltd (1911) 1 Ch. 425, where Nouile, J. portrayed the olden days directors.

91 (1925) Ch. 407. This was quoted will approval in Huckerby v. Elliot (1970) All E.R. 189. See also Lord Justice Clerk Moncrack in Western bank v. Boards of Trustees (1872) 11 M. 96 at p. 112.

92 See Re Brazilian Rubber Plantations and Estate Ltd. op. cit; Logunas Nitrate Co. v. Lagunas Syndicate (1889) 2 Ch. 392 at 435.

> a director is not bound to give continuous attention to the affairs of his company. His duties are of an intermittent nature to be performed at periodic Board meetings, and at meetings of any committee upon which he happens to be placed. He is not however bound to attend all such meetings, though he ought to attend whenever in the circumstances he is reasonably able to do so.

It appears that this formulation refers to ordinary directors and not managing directors. It is rather lax, weak and unhelpful to the director and the commercial concerns which the directors were required to manage. In any case, the proposition shows the extent of attention which a director was required to give to the company's business. Indeed, this was an era where the law and the courts were excessively permissive of the directors shortcomings.

The third formulation is that:[93]

> In respect of all duties and having regard to the exigencies of business, and the articles of association, may be left to some other official, a director is, in the absence of any ground for suspicion justified in trusting that official to perform such duties honestly.

This formulation took cognizance of the ill-equipped nature and inexperience of directors in business matters and thus encouraged them to delegate their functions to other directors or members of the company that were professionally equipped and more competent. The only situation where a higher degree of care, skill and diligence was required of directors was where

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93 Supra at p. 428.

the person is a director of a specialised area e.g. a finance or legal director as the case may be.[94]

Before the CAMA 1990, the common law standard was subjected to scathing criticisms by learned authors. While Sealy[95] saw no reason why the extremely permissive attitude of the older generation of judges toward directors in their day should continue in modern times, Olawoyin was of the view that the common law standard should be discarded.[96] Apart from the Re Equitable Insurance case, further justification for the vehement criticisms of the old order can be found in *Re Cadiff Savings Bank, Marquis of Butt's Case*.[97] In this case the President of the Cadiff Savings Bank was succeeded by his son, Marquis of Bute, while still an infant. The Marquis succeeded in attending only one Board meeting in forty years. Subsequently, the bank went into liquidation and the liquidator argued that the Marquis should be held liable for his apparent neglect of duty and omission to manage the affairs of the company as a result of which the bank incurred loses. The court held that the Marquis was not liable in that a director's neglect or omission to attend Board meetings does not tantamount to neglect or omission to perform a duty at those meetings.[98] The court was also of the view that since there were many directors in the company, 50 in fact, the failure of one director to attend Board

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94 See Lister v. Romford Ice and Cold Storage Co. Ltd. (1957) A.C. 555; See also Adebayo v. Johnson & Others (1969) 1 ANLR 171 at 192; Dorchester Finance Co. Ltd. v. Stebbing (1989) B.C.L.R. 498.

95 See Sealy, "The Director as Trustee" (1967) C.L.J. 83 at 120; Keeton, 'The Directors as Trustee' (1952) 5 C.L.R. 13.

96 See Olawoyin, op. cit. at p. 219. See also Trebilock M.J. "The Liability of Company Directors for Negligence" (1969) 32 M.L.R. 499.

97 (1892) 2 Ch. 100.

98 At 109.

meetings should not be a reason for the other directors' misconduct, who were present at the meetings.

Meanwhile, the effect of the decision in *Re City Equitable Fire Insurance Co. Ltd*. in Nigeria is vividly illustrated in the case of *John Oyo Adebayo v. Chief M.A.K. Shonowo*,[99] where the Supreme Court by necessary implication ratified the principle of Romer, J. in *Re City Equitable Fire Insurance Co's case*. In *Adebayo v. Shonowo*, the complaint against the directors was for negligent breach of trust.

The facts of the case deal with the affairs of a bank which was set up in 1951 but which closed down its business in September 1961. This was followed by a voluntary winding up subject to the courts supervision and the appointment of some liquidators. The petition for winding up revealed a number of irregularities committed in the Bank as well as certain deficiencies in accounting. Large sums of money were also found to have been misappropriated. The court convinced of all the above, granted the petition for winding up in 1962. Meanwhile, the directors were alleged to have committed a breach of trust in their dealings. The substance of the allegation against them were:

(a) That huge losses of sums of money took place in the Bank which the directors failed to do anything to stop.

(b) That the directors woefully failed to comply with article 48 of the Articles of Association of the Bank requiring true account to be kept.

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[99] Supra at p. 176.

The Supreme Court per Onyeama, Ag. C.J. (as he then was) while absolving the directors of blame observed that:

> The responsibilities of directors must vary with the nature of the company as their special position as defined or regulated by the Articles of Association… The thing or matter complained of must be judged against the background of the realities of the case and a combination of circumstances may in one case fail to constitute a breach of trust… A director is not expected to fill all the positions in the company himself… he should be entitled to assume that qualified staff are performing the duties of their offices with competence …

The palpable weakness of the common law standard of duty of care, skill and diligence expected of directors is demonstrated by the *Re City Equitable and the Adebayo v. Shonowo's cases*. Being a subjective standard, a director's assessment was premised on his qualification, attributes and the skills he had before assuming the position of a board member. Thus, a director with deficient credentials had considerable liberty in running out of trouble. And sadly enough, the courts then sat tight and refused to intervene in the face of gross exhibition of negligence and lack of care by directors.[100]

The CAMA has now come in to remedy the anomaly inherent in the old common law standard which was unsatisfactory. Section 282 now sets out an objective standard for company directors in Nigeria. Subsection (1) provides that:

> Every director … shall exercise that degree of care, diligence and skill which a reasonably prudent director would exercise in comparable circumstances.

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[100] See Adebayo v. Shonowo (1969) 1 All NLR p. 176. See also Banes, Cases and Materials on Nigerian Company Law, op. cit. 286, where the author explains the reasons for the courts non-interventionist posture.

The key words in the section "reasonably prudent director" indicates that the test is an objective standard which admits of no discrimination unlike the common law standard.

In Subsection (2), it is further provided that failure to take reasonable care shall attract an action for negligence and breach of duty, while subsection (3) makes every director responsible individually for the Board of which he is a member. Another innovation embedded under subsection (4) is the application of the same standard of care for both executive and non-executive directors.

One area however where the CAMA has been mute is that pertaining to the delegation of functions by company directors. Under the common law standard, a director was justified in the absence of any ground for suspicion to trust an officer to discharge such duties delegated to the director under the relevant company articles. The CAMA has been silent in this area especially the extent to which a director can be held liable for misconduct arising from delegation. While Section 279 allows a director to delegate his powers under any provision of the Act, he is however warned to desist from delegation in a manner that may tantamounts to abdication of responsibility. Section 263(5) equally allows delegation of responsibilities to managing directors or committees of the Board. Beyond this, the CAMA has also not said much as to the nature and extent of the non-committee members liability for negligence occasioned by committee members. An additional provision indicating the circumstances under which non-committee members could be made liable for negligence of committee members would be preferable.

4.5 DUTIES OF A COMPANY DIRECTOR UNDER THE BANKS AND OTHER FINANCIAL INSTITUTIONS ACT (BOFIA) OF 1991 AND INSURANCE ACT 2003

The additional duties and responsibilities of directors of banks, insurance companies and other financial institutions will be examined. It is undeniable that financial institutions the world over constitute a major live wire in the economy of modern nations. A country whose financial institutions are unstable and groping for survival is surely an unhappy country, since viable financial institutions constitute an important thread that hold other sectors of the economy together. It is therefore the need to stabilize these institutions and ensure their efficiency that government at various points in time have come out with different legislations to regulate them specifically.

In this regard, the Banks and Other Financial Institutions Act of 1991 (BOFIA) has foisted on directors of those institutions additional stringent duties and responsibilities. These duties and responsibilities are specific and additional to those imposed on company directors generally. Some relevant aspects of these duties as contained in the provisions of the BOFIA will now be briefly examined.

The essence of the law in this area is to regulate the conduct of financial institutions in Nigeria. Another reason is to re-define, streamline and strengthen the Central Banks' authority and functions being the main supervisory and regulatory body for all financial institutions in Nigeria. However, there is no intention to delve into the procedure and the establishment of such institutions or the functions, powers and duties of the

Central Bank of Nigeria. The discussion here would dwell strictly on the additional duties and responsibilities of directors of these institutions.

One of he primary duties bestowed on the company directors of financial institutions is the duty to ensure compliance with the provisions of the BOFIA. Thus, for example, the director must ensure that no bank closes or opens any branch of a bank without notifying the Central Bank and obtaining the required consent. The same applies to any intended re-organization, mergers and acquisition. In all these, the prior consent of the Central Bank must be obtained.[101]

Section 8 of the Act also touches on directors of foreign registered companies. This provision frowns at any director of a foreign registered bank opening a representative office in Nigeria without the prior consent of the Central Bank of Nigeria.

Under the BOFIA, directors are also required to ensure that the general duties which lie on banks, and other miscellaneous matters are dutifully complied with. Such matters relate to a bank's duty to maintain reserve funds out of its net profit every year before the declaration of dividends;[102] restriction on dividends on its shares until all the banks preliminary expenses, organizational expenses shares selling commission, brokerage, amount of losses incurred and other capitalised expenses not represented by tangible

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101 See generally Sections 4, 5, 6 and 9 of BOFIA 1991, for details pertaining to matters which the directors are to ensure compliance.

102 Section 16. The appropriate conditions are that, where the amount of reserve is less than the paid up share capital, the amount to be transferred shall not be less than 30% of the net profit; however, where it is the same or in excess of the paid up share capital, the amount to be transferred must not be less than 15% of the net profit.

assets have been written off, etc;[103] duty to ensure that certain classes of persons such as bankrupts and ex-convicts for offences relating to fraud and dishonesty are not employed in the banks.[104] Other duties of the bank which the directors are mandated by the BOFIA to ensure compliance with are: duty to display at its offices, its lending and deposits, and render information on interest rates to the Central Bank;[105] duty to submit periodical returns to the Central Bank every month showing its assets and liabilities and its analysis of advances both at head office and branches,[106] duty to publish annual accounts in a daily newspaper printed and circulated in Nigeria,[107] and duty to ensure that the right calibre of persons are appointed as company auditors.[108]

The enumerated duties of the bank above which the director is required to ensure compliance are by no means exhaustive. The duty for ensuring compliance rests on the shoulder of the bank director. The position of the BOFIA is a very strict one. This strictness is further emphasised by the provisions of Sections 45 and 46 of the Act respectively.

Insurance companies are specialised companies since they are mainly concerned with indemnities and compensations in the event of losses. This notwithstanding, they constitute a vital segment in the financial system. They are also regulated by the laws and regulations governing other financial institutions. But because of the peculiarity of the insurance industry and the

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103 See generally, Section 17 for other details.

104 See Section 19 for details.

105 Section 23. Failure to comply makes the bank liable to a fine of ₦1000 for every day during which the offence continuous. Note however, that this provision is not applicable to profit sharing banks.

106 Section 25. Failure to comply with this provision is punishable on conviction to a fine of ₦5,000 for each day during which the offence continuous.

107 Section 27.

108 Section 29.

ever increasing need to ensure that insurance business is run on a sound basis, special laws and regulations have been fashioned out to meet these expectations. Thus, the chief responsibility of the director of an insurance company, like that of the bank is that of administration and the enforcement of the rules and regulations concerning the industry.

The director of an insurance company must act *intra vires* the company's constitution and make to third parties payments that are duly authorised. More importantly, he has the duty to account for secret profits made. Other specific duties have to do with the responsibility to ensure that the prescribed minimum paid up share capital is maintained.[109] Again, insurance directors under the Act have responsibility to ensure the separation of accounts and adequate reserve funds,[110] maintain at all material times a reasonable level of solvency,[111] and ensure that insurance accounts are audited only by professional auditors.[112]

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109 In the case of life insurance business, not less than 150 million Naira minimum share capital, while concerning non life insurance, not less than 200 million. And in relation to re-insurance business, not less than 350 million Naira in the case of Composite Insurance Business. See S. 9 Insurance Act 2003.

110 Sections 18 and 19 of Insurance Act 2003.

111 Sections 20-24 Insurance Act 2003.

112 Sections 25 Insurance Act 2003.

CHAPTER FIVE

TRENDS IN THE DEVELOPMENT OF MODERN CORPORATE GOVERNANCE AND MANAGEMENT PRINCIPLES

5.1 INTRODUCTION

The concept of effective corporate governance and management has no doubt aroused the interest of stakeholders, investors, creditors and governments all over the world owing to developments in financial market on a global scale.

The governance of corporation is now as important in the world economy as the governance of countries.[1] Developments at the global level have necessitated that corporations and their stakeholders imbibe the full complements of corporate accountability and efficiency. Similarly, globalisation of economics on the world scale has brought with it the need to develop international standards of best practices for the benefit of investors, and all the stakeholders, a development necessitated by corporate failures which affected America, Asia, Europe and Africa and creating in the process economic instability. In the case of Nigeria, the commercial and banking terrain has been groping and grasping for breath and survival since the 80s and 90s. Even in this new millennium, the ghost of financial distress can still be seen haunting the financial service sector.

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[1] See James Wolfesohn, "The World Bank", http://www.worldbank.org/html/fpd/private/sector/eg/aboutus.htm.

There is an inseparable link between corporate governance and management and investor confidence. No investor will consider investing in an enterprise devoid of transparency and accountability.

In this chapter, attempts is made to examine the meaning and the distinction between corporate governance and management in order to lay foundation for the subject matter since it constitutes the main theme of this thesis. The chapter also considers the need for effective corporate governance and management of corporations by stakeholders charged with such responsibility, especially as it relates to taking the overriding interest of all stakeholders and their corporations. This is done in accordance with current global commonwealth, Africa and Nigerian initiatives and developments in the area of corporate governance and management.

The chapter also attempts a synthesis of the various corporate governance codes of best practices applicable to various jurisdictions including Nigeria. The academic debate surrounding the convergence of the various corporate governance regimes is also replayed in this chapter. Finally, the chapter concludes by considering whether actual convergence is realistic for now or futuristic, considering the social, political, cultural and legal differences in every jurisdiction.

5.2 THE DEFINITION OF CORPORATE GOVERNANCE

The term "Corporate Governance" is the exercise of authority, which involves not only the right to direct but also to lead and to control within an

organization[2]. Corporate Governance as a subject matter has attracted a lot of attention of recent because of its undeniable importance to the economic well being of corporations and the society in general. It is a subject matter that has no generally accepted definition, as most scholars and stakeholders in the field tends to examine the concept from their own perspectives.

According to Wolfensohn, "Corporate Governance is about promoting corporate fairness, transparency and accountability".[3] The Organization for Economic Cooperation and Development (OECD) examines it thus:

> The system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as the Board members, shareholders and other stakeholders and spells out the rules and procedures for making decisions on corporate affairs. By this, it also provide the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance[4].

At the Nigerian scene, Sanusi views corporate governance from the perspective of building credibility, ensuring transparency and accountability as well as maintaining an effective channel of information disclosure that would foster good corporate governance performance, trust as well as sustaining confidence among the various interest groups that make up an organization[5].

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2 Edward W. Youkins, "Corporate Governance does not mean Corporate Government". Available at http://www.quebecoislibre.org/000513-10.htm

3 President of the World Bank

4 See the OECD (Organization for Economic Co-operation and Development_, Principles of Corporate Governance 1999, available at http://www.oecd.org/ab.utgeneralindex.html; The principles are presently undergoing review. The OECD is multilateral institution established in 1961 with a Secretariat in Paris, France.

5 Sanusi, S.O. "Enhancing Good Corporate Governance; A Strategy for Financial Sector Soundness". A Keynote Address Presented at the Dinner Nite of the Chattered Institute of Bankers Nigeria, November 8, 2002. Available at http://www.expisc.com/governance.htm

The definitions offered so far explain the concept of corporate governance, which is quite different from corporate management.

5.3 THE DEFINITION OF CORPORATE MANAGEMENT

The term 'management' is a concept that has many facets.[6] Here our main focus is management as a process in corporations. Just as governance is a process, management is also a process.

In defining the word management, it has been said that it is:

> … the process undertaken by one or more persons to co-ordinate the work activities of other persons, capital, materials, and technologies to achieve high quality results not attainable by anyone person alone.[7]

Co-ordination is thus an essential feature of the work schedule of those occupying management position and whose umbrella the various departmental heads and other employees operate. At the local scene, management is also defined elaborately as the process of "getting things done" or:

> … co-ordinating all resources of an organization through the process of planning, organizing, directing and controlling in other to attain organizational objectives … the guidance or direction of people towards organizational goals or objectives … the supervision, controlling and co-ordinating of activity to attain optimum results with organizational resources.[8]

The essential characteristic features that can be gleaned from these definitions are that those involved in the process of management as opposed to governance focus on corporate objectives, plan and set policies, organize staff,

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6 Other facets concerns management as a discipline, as a people and as a carrier.

7 See Ivancevich J.M;, Corenzi, P; Skinner, S.J; Crosby, P.B., Management: Quality and Competitiveness, 2nd ed. (USA: Irwin McGraw-Hill, 1997)

8 See Nwachukwu, C.C. Management Theory and Practice (Onitsa: Africana First Publishers Ltd., 1992).

communicate with subordinates, colleagues, direct and supervise by securing actual performance from subordinates and control organizational activities corporate management may be defined as the corporate management process involving certain responsibilities that those in executive positions such as directors and managers must carry out in the interest of the company to attain the set goals of a corporate entity.

It would seem however, that the definition of corporate governance viewed from those provided above encompasses the essential features of corporate management as the tendency and approach of most scholars is to blur any distinction between governance and management. This approach understandably is informed by the fact that some of the features of management as a process are imbedded in the definition of governance. Thus, the concept of governance according to latter day scholars is all encompassing. This approach, it is submitted, is unrealistic. Despite the affinity between the two interrelated concepts, it is obvious that a dividing line separates them.

5.4 THE DISTINCTION BETWEEN CORPORATE GOVERNANCE AND MANAGEMENT

While corporate governance has an external focus, corporate management has an internal focus. Corporate governance is strategy-oriented while corporate management is task-oriented. Again, corporate governance is

the responsibility of directors, while corporate management is the duty of the company executives.[9]

Trickler puts the definition in its real perspective when he said thus:

> Corporate Governance also entails giving overall direction to the enterprise, while overseeing and controlling the executive actions of management and with satisfying legitimate expectations for accountability and regulation of interest beyond the corporate boundaries. If management is about running business, governance is about seeing that it is run properly.[10]

Evidently, governance revolves around the intrinsic nature, purpose, integrity and identity of the institution; monitoring and overseeing strategic direction of an institution within a particular socio-economic context. It deals with the institution externalities. Management on the other hand is built around focusing on specific aims and objectives over a certain time frame by the judicious use of means directed towards their actualisation.

Two theories regulate the concept of corporate governance, namely, the stewardship theory and the agency theory. The former hinges the philosophy on the premise that a man, as a creature, is trustworthy, honest, and capable of acting bona fide (i.e. in good faith) in other people's interest; while the latter premises its philosophy on the platform that human beings cannot really be trusted to act in good faith.[11] A necessary consequence of the distinction between Corporate Governance and corporate management is that hierarchically, power resides at the top of the structural pyramid of the

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9 See Ohuabunwa, S. M., "Corporate Governance in Nigeria". Being text of a paper delivered by the Chairman/Chief Executive Nermeth International Pharmaceutical Plc. at the Annual Dinner/Merit Award Night of the Government Secondary School, Owerri, Imo State, 1999.

10 See Tricker, R. I. Corporate Governance (Gower Publishing Company, Hart, 1994) at p.6

11 See Kolade, C. "Board Performance Analysis". Distinguished Management Lectures 1997. Nigerian Institute of Management, Lagos, Weekend Concord Newspaper, Saturday, Nov. 1998, p.18

organization called the Board of Directors while at the base, the shareholders and employees have some modicum of relative powers of importance, one acting as pressure groups and a monitoring devise to management, the other acting as the transformers of corporate objectives into corporate realities. The management on the other hand, is the recipient of the decision-making apparatus of the company within the centralised structure.

Sometimes, however, the distinction between Corporate Governance and Corporate Management may overlap and intertwine where Board of Directors contain executive directors[12] who are both managers and directors. This apart, the ownership structure of a company may blur the distinction between Corporate Governance and Management. In private companies, ownership resides in few persons who are in most cases involved in the day to day running of the company affairs. The highest shareholder would usually perform the dual role of Company Chairman and Chief Executive. Thus, the same person ends up owing, governing and managing the company.

The various roles assigned to the Board of Directors and Management by law is a reflection of the distinction between Governance and Management. It is in this light that the Board of Directors, as of necessity, acts as arbitrator between competing interests; acts as crises manager; establish and define corporate polities and objectives; perform legal duties; promote the company; lend credibility to the organization; select chief executives; assist management to reach appropriate decisions through advice; protect and report to

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12 See Verr, B.B. "Distinction between Direction and Management". Being a paper presented at the National Workshop on Corporate Governance and the Rights and responsibilities of Shareholders in Nigeria, 28-29, November, 1994, p.1

shareholders, etc;[13] while management vested with formal authority over the organization, perform duties of a ceremonial nature,[14] leadership roles,[15] liaison roles,[16] the monitor role,[17] the disseminator and entrepreneurial role,[18] disturbance-handling role,[19] resource allocator and negotiation roles, etc.[20]

5.5 NEEDS FOR EFFECTIVE CORPORATE GOVERNANCE AND MANAGEMENT

Good corporate governance and management ensures that the Board of Directors and the Executive Directors of corporations act in the best interest of shareholders and the corporations which they direct. There is no doubt that globalization has greatly influenced many areas of human endeavour, especially the political, cultural and social aspects. More importantly, it has impacted on the governance of corporations leading to a more challenging demand on the Board and Directors.

Globalization of corporate entities entails that companies, wherever they exist, must act solely for the benefit of the people. There is no single model of

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13 For details of the functions of the Board of Directors, see infra.

14 The Managing Director has the responsibility to great touring dignitaries

15 The Managing Director is in charge of an organization, he has the right of hire and fire and that of training of his or her staff. Formal authority is vested in him. Effective leadership will however depend on the judicious use of such authority.

16 It is the responsibility of the Managing Director to make contact outside his organization to find relevant information that will benefit his organisation.

17 A director can scan his environment for relevant for relevant information, sometimes through other subordinate managers. Some of these information arrive by way of gossips, hearsay and speculation.

18 A managing director must be on the look out for good ideas and the development of relevant projects.

19 This role is evident during strike periods. The manner of reaction will depend on how effective the Managing Director is to the organization.

20 See Generally Verr, B. B. op. cit. at pp.7-11

effective corporate governance and management.[21] Irrespective of the model, it is based on the attitudes, practices and values of the changing society.

Essentially however, the need for effective corporate governance and management revolve round the belief in accountability of power and the exercise of it to promote human well being; the promotion and sustenance of democratic values in the sharing of corporate power, representation and participation.

The need also hinges on the efficient and effective utilization of corporate resources for the provision of good services; performance of corporate social responsibility; promotion of human rights and freedom and maintenance of essential order and security for the person and his/her property.

The essence of good corporate governance is that it paves the way for both local and foreign investment and the increase in profit. It is undeniable that capital is limited in supply and any nation or corporate entity that seeks to attract and retain capital must strive to create a favourable atmosphere for it. Investors also invest their capital on enterprises that are effectively managed and governed.

The results of ineffective corporate governance and management can be quite disastrous and enormous. It leads to company failure with the consequential loss of money, investments, life savings, sources of livelihood,

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[21] See Kwakwa, V. and Nzekwu, G. "International Best Practices on Corporate Governance" in Oladimesi Alo (ed) Issues in Corporate Governance (Lagos, Financial Institution, Trading Centre (TITC) 2003, p.18

jobs and lives. In the international arena, the case of Enron[22] provides a vivid example. Though not a financial institution, Enron, at the time of its collapse, was a gas pipeline energy company that was rated as the world's largest. The problem with Enron was that of bad management, misleading accounts, shoddy auditing and fraud on a high scale. Enron's problem started when Dyney, a rival company, refused to continue with the merger arrangement with Enron after discovering that Enron's debt was downgraded to junk status. The case reveals the ineffectiveness of the company's external auditor as an external backup corporate governance monitoring device. World Com is another sad example. The company fraudulently treated revenue expenditure of about $3.85 billion as capital investments, an amount that could have been treated as deductible expenditure at the time it was incurred. When eventually the expenditure was reclassified, the company sustained terrible losses that affected the stock price of the company, resulting in the company's bankruptcy. It is reported that ten thousand people in sixty-four countries lost their jobs as a result of this tragedy.[23]

Nigeria has a fair share of corporate failure, which cuts across both public and private corporations. In fact, it has been listed as the major reason for privatisation in Nigeria. Companies, both public and private, in Nigeria are beset with corruption and mismanagement. A review of the performance

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22 For an exhaustive analysis of the Enron's case see Redolfo Apreda "How Corporate Governance and Globalization can Run Afoul of the Law and Global Practices in Business: The Enron's Disgraceful Affair". Universal Del Cema 2003, working paper series, No.225, p.2

23 Adeola "Transparent and Accountable Corporate Governance in the Capital Market: Challenges for Market Operators and Shareholders" in Ndanusa, S. and Ezenwa, V. (ed). Nigerian Capital Market and the Globalization Challenge (Lagos, Macmillan Nigerian Publishers Ltd. 2003), p.2

chart of most companies in Nigeria would show that in 1998 alone, about ₦265 billion was granted to public enterprises in the form of transfers, subsidies, tax exemption and waivers, without a corresponding efficient management of the resources.[24] Experience has also shown that corporate failures were, in most cases, caused by specific incidents of huge off-book liabilities, procurement and award of contract without due process, conflict of interest of directors and managers, inflation of contracts and so on. A few examples that have been reported[25] are used as illustration hereunder.

(i) **African Petroleum Plc:**

This represents one of the most scandalous cases of corporate abuses in Nigeria, as it attracted even the attention of the National Assembly. Some of their abuses are as follow:

a. The former Managing Director, a government appointee, in conjunction with the Company Secretary, drafted and signed Board Resolutions authorizing borrowing by the Board without authority.

b. The company received a total short-term loan consisting of Commercial Papers (cp) and Banker's Acceptances (Bas) to the tune of ₦39,060,098,000,= (Thirty-nine billion, sixty-six million and nine-eight thousand Naira). This was received within a period of four years. Information for part of the amount

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24 See El-Rufai, N. "Importance of Corporate Governance". This Day Newspaper, vol. 9, No.3012, July 22, 2003 at p.24

25 Ibid. at p. 26.

(₦17,535,242,000) were not disclosed to Auditors. Again, the loans were never tied to specific project expenditures neither were vouchers made available to determine their nature or utilization of some of the funds. Nearly all the deals and other letters were negotiated and signed by the Finance Accounts Manager and not sanctioned by the Board.

c. After a detailed review of all available information from the company and from the Nigerian national Petroleum Corporation (NNPC), AP's indebtedness to NNPC was initially put at ₦8,258,279,951.00. Investigation also revealed an upfront payment of ₦70 million made to a company being 70% of a ₦100 million commission charged on a proposed sale of AP plaza for ₦1 billion, which was not consummated. The company failed to account for ₦4.8 billion being payment due from the lifting of petroleum products.

(ii) **Nigerian Securities and Minting Companies (NSPMC)**

In this case, the Company Secretary drafted and signed Board Resolutions, authorizing borrowing without the Board authorization. It was also discovered that there was procurement and award of contracts of about ₦3 billion without due process by the former Managing Director. When the Bureau for Privatization asked the Federal Government to fire him, he accused the government of breach of corporate governance rules. Since his removal, however, more

revelations of financial impropriety of the tune of ₦500 million for 2002 fiscal year alone have been discovered.

(iii) **The Nigerian Telecommunication Company (NITEL)**

NITEL is another public enterprise that was neck deep in the procurement and award of contracts without due process that also grounded it. This apart, there were conflicts of interest of Directors and Managers and other financial improprieties amounting to loss of billions of naira. For instance, the tender rules for NITEL made provision for the tender Secretariat to handover the opened tenders to the originating unit for evaluation. The government set up a commission of enquiry to investigate the affairs of NITEL. It was discovered by the commission that the responsibility for evaluating the project was that of the unit. The findings of the commission however revealed that this was far from being the practice, as the Managing Director and the Chairman single-handedly picked an evaluation team to evaluate big contracts without passing through the Tenders Board. Amongst others, it was also discovered that NITEL management gave inconsistent and contradictory reasons for rejecting some contracts.

There also existed substantial difference between job specification in the contracts signed after evaluation and job specification eventually adopted after the final work or design. Laziness and incompetence was also found to be the hallmark of the leadership of the planning and operations department of the organization.

As a Stated-Owned Enterprise (SOE), NITEL's operations are often regulated by the Federal Government through directives issued in circulars. In one of such circulars,[26] the government informed all State-Owned Enterprises of the suspension of all contracts, licenses, award approvals and appointments made or granted by the Federal Government between January 1st 1999 and May 23rd 1999. Such contract awards were to be reviewed by the Contract Review Panel set up by the government. One of the General Managers, however, adopted a different interpretation of the circular to exclude approvals obtained by the enterprise in 1998 for contracts awarded in 1999. The implication, according to him, being that the circular did not apply to some projects totalling the sum of ₦3,214,843,377. This misinterpretation deprived the government the opportunity to re-negotiate with the contractors, thus resulting in substantial loss to the company. The actions of the manager could have been motivated by personal interest. Furthermore, inflation of contracts could be as a result of the deep-seated connivance between the management of the enterprise and the contractors on one hand, and between the evaluation committee and contractors on the other hand.

It is as a result of the non-performance of NITEL due to a myriad of reasons indicated above that it was acquired by Multibillion Naira Transnational Corporation PLC (Transcorp). The buying over of NITEL

[26] Issued by the Secretary to the Government on May 31st 1999.

from the Federal Government by Transcorp following the privatization by the Bureau of public enterprises was to reposition the corporation as the number one investment conglomerate in Africa. Other objectives relates to striving to reduce the continents import bill of $150 billion which is spent in bringing in consumer products from Europe, Asia, and the United States. The ambition of Transcorp encompasses interest in agriculture, industry, oil and gas, tourism and commerce. Transcorp intends to create significant local capacity in Africa. To demonstrate its resolve. Transcorp is owned and managed entirely by Nigerians.[27]

The transfer of NITEL to a new management and Board appears to have marked the end of the liberalizaton of the telecommunication sector in the country. It is hoped that Transcorp will chart an entirely new course so as be able to fulfil its potential.

(iv) **Cadbury Nigeria PLC**

Recently, it came to public glare that Cadbury had been engaging in significant and deliberate overstatement of the financial position of the company over a number of years. No doubt, this disclosure raised serious concerns and implication about corporate governance and the effectiveness of the role of regulatory bodies with monitoring functions in corporate governance. The Cadbury case is particularly worrisome and remarkable considering its high profile status among operators in

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[27] See Fanawopo, S. "NITEL: Can Transcorp reposition the "family brand"? Daily Sun Newspaper, Wednesday, Nov. 22, 2006 page 29; Isa Godwin, "Workers drag Transcorp BPE to Court", Daily Sun, Nov. 14, 2006 at page 7.

the private sector of the economy and its international affiliation with Cadbury Schweppes, the world largest confectionery group. Having been listed in the stock market, no one in his wildest dreams would have doubted the authenticity of statement of accounts given to the public by the company over the years. The public especially, users of such financial statement would have thought that the Nigerian Stock Exchange as well as the Security and Exchange Commission had scrutinised them before placing them at the disposal of the public.

Interestingly, the Cadbury impropriety became public knowledge because owning to an investigation carried out by Price Waterhouse Coopers, an audit firm.

It is no gainsaying that the capacity and commitment of NSE and SEC to effectively live up to their responsibilities of ensuring that effective corporate governance issues are enforced to internationally accepted standards.

It is gladdening to note that the Institute of Chattered Accountants of Nigeria (ICAN) has swung into action and initiated steps to carry out an independent investigation into the alleged overstatement of accounts to get to the bottom of the matter since the Cadbury experience is capable of eroding investors confidence in the capital market apart from the negative effect upon the accountancy profession.[28]

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[28] See Asueliman, F. "Cadbury, Bunmi Oni and Corporate Governance", Financial Standard Newspaper, Monday, December 25, 2006.

(v) **Capital Hostels PLC (Abuja Sheraton)**

This also reveals a glaring case of deficient accounting system and documentation. For instance, fixed assets totalling ₦1.103 billion were acquired by the hotel with 50% of the fixed asset acquisition not routed through the Board for approval.

There was deficiency in the accounting for fixed assets. An investigation revealed, for instance, that the Hotel did not maintain an asset register and the accounting records for disposed items or assets were incomplete.

(vi) **NICON Hilton Hotel**

"*Owner's return*" averaging US $1 million a month totalling the sum of US $150 million for nearly 10 years, which was handed to NICON/NIRMSCO went into an inexplicable blockhole of NICON Insurance/NICON Hotels Ltd.; meanwhile, the hotel's constructed loan remained outstanding to the tune of US $250million. This was being paid by the real owner – the Federal Government of Nigeria through the Federal Ministry of Finance. It was discovered in the course of investigation that due to the absence of an informative Fixed Asset Register, fixed assets worth about ₦650 million could not be vouched for, while segregated assets worth about ₦1 billion could not be traced to all the company's audited accounts.

Despite huge bank balances of over ₦2 billion in Audited Accounts, bank accounts were not opened in NIRMSCO's name until the year 2002.

(vii) **Nigerdock Nigeria Plc:**

This entity was not also spared from the malady called inefficient management. Investigation revealed that there was very poor internal control, and again, Domiciliary Accounts kept by the company such as cashbooks, were devoid of opening or closing balances. Furthermore, there were glaring cash or destruction of some vital documents by the Managing Director on the eve of his exit (ala Enron and Anderson). Also revealed were multiple bank accounts operation, which created confusion and aided fraudulent practices. There were also established cases of sale of company's assets by the Managing Director without Board's approval.

Similarly, in the case of private companies, corporate abuses led to the collapse of such quoted companies like Unilever, Savannah Bank, Benue Cement, Allied Bank, to mention a few. To use Unilever as an example, it was revealed that the company under-provided for liabilities of billions of naira in its audited accounts.

5.6 GLOBAL INITIATIVES IN CORPORATE GOVERNANCE AND MANAGEMENT

Although the concept of corporate governance can be said to be initially an American phenomenon, it has spread around the world. Consequently, certain initiatives have been adopted at global level to ensure its enthronement in the corporate world. One of such initiative is the Global Corporate Governance Forum (G.C.C.F), which is directed towards assisting

countries to improve the standards of governance of their corporations, ensuring accountability, promoting fairness, transparency and responsibility.[29] This is possible owing to the combined initiative of the Organization for Economic Corporation and Development (O.E.C.D) and the World Bank Group. This international initiative made it possible for the leading bodies in Corporate governance to come together to dialogue, partner one another and deliver strategies for reform implementation. The forum achieves the above objectives through:

i. **Dialogue**: This came through Convening Several Conferences and round table meetings at National and Regional levels, debates by players, identification of key reform areas, development of action plan and spearheading of initiatives.

ii. **Technical Assistance**: This came through the provision of legal advice, particularly on legal, regulatory and best practice standards through exchanges and secondment of professionals and experienced individuals.

iii. **Capacity Building**: This is achieved through provision of materials, case studies, curriculum design, development training and education for the main players in governance.

iv. **Institution Building**: This is done through the establishment of centres for corporate governance.

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[29] http:/www.ecgi.org/codes/countrydocuments/commonwealth/cacgfinal.pdf. (hereinafter the "CACG Guidelines".

v. **Exchange of Information**: This is achieved through gathering and essential materials, contracts and case studies.

vi. **Task Force**: This comes in form of forming working groups or cases of specialist concern requiring innovation in thinking and practice.

It is important to note that nations and regions are availing themselves of these initiatives to enhance their corporate governance profile.

According to G.C.G.F survey:

> At a global level, the survey responses indicate that… companies in these emerging markets traditionally unworthy to pay for corporate governance related services, now understand the importance of changing their Board and disclosure practices in order to better attract international sources of capital…[30]

The result of the survey no doubt authenticates the assertion of the World Bank President, J. D. Wolfensohn that "the proper governance of companies will become as would the World Economy as the proper governance of countries.[31]

The International Corporate Governance Network has been established to promote and coordinate research and development in Corporate Governance.

5.6.1 Corporate Governance in the Commonwealth

The globalization of economies in the Commonwealth and their subsequent financial and investment markets gave rise, on one hand, to a convergence of originally separate initiatives in Corporate Governance and a

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30 The Inventory – A Survey of Worldwide Corporate Governance Activity: GCGF Publication, 2nd Edition, p. 36

31 Wolfensohn, J. in Financial Times, June 21st 1990.

new dimension of Corporate Governance defined to transcend the rules of national boundaries.

The requirement for standard that could represent the Commonwealth approach to corporate governance was formulated through the initiative of the Commonwealth Association for Corporate Governance (C.A.C.G) in April 1998 in response to the Edinburgh Declaration of the Common Wealth Heads of Government meetings in 1997. The objectives of the CACG was:

i. The promotion of good standards in corporate governance and business practice throughout the Commonwealth.

ii. Facilitating the development of appropriate institutions for the purpose of addressing, teaching and disseminating such standards.

The guidelines set out fifteen principles of corporate governance aimed primarily at the Boards of directors of all business enterprises namely, public, family or state-owned, and also to executive and other forms of enterprises such as Non-Governmental Organizations (N.G.O.s) and Agencies.

It is important to note that a number of Commonwealth countries now have national codes even long before the establishment of the CACG guidelines.

5.6.2 Corporate Governance in Africa

On the African continent, regional economic cooperation and integration have taken a firm hold. The essence of the activities of the various sub-regional bodies on the continent is the recognition of the need for governance

principles that would provide distinctively "African solution" to the numerous governance problems in Africa while still operating within the spectrum of global corporate governance principles. It is in this regard that New Partnership on African Development (NEPAD) has embarked on various initiatives directed towards ensuring sustainable development in Africa.

In the same vein, the African Capital Markets Forum (ACMF) plays a major role in ensuring good corporate practices in Africa. The forum is a non-governmental, non-profit making organisation whose activities are directed towards promoting capital market development in Africa.

ACMF pursues good Corporate Governance practices through the building and maintenance of a database on African Capital Markets, the promotion of research and training and provision of technical assistance to capital market institutions in Africa. The activities of the ACMF relate to the followings:

i. Participation and convening of international conferences and workshops seeking to enhance the performance of capital market institutions.

ii. Creating a conducive environment for capital market development.

iii. Provision of advisory services to African governments, institutions as well as international agencies on issues relating to capital markets development.[32]

It carries out the above objectives through the instrumentalities of the stock exchanges, securities regulatory agencies and market operators. The African Capital Development market Forum is a joint initiative of the ACMF and the United Nations Development Programme (UNDP) and the African Stock Exchanges Association (ASEA) in collaboration with New York Stock Exchange (NYSE).

In its attempt to create an all-embracing forum, the Pan African Consultative Forum (PACF) on Corporate Governance was launched in Johannesburg in July 2001 with support from World Bank group, the Global Corporate Governance Forum (GCGF), the Organization for Economic Cooperation and Development (O.E.C.D), the commonwealth secretariat and the African Development Bank (A.D.B) and other donors that share the same aspirations.

The objectives of the P.A.C.F, are:

i. To raise awareness of the significance of corporate governance.

ii. To reach consensus on the concepts and methods of Corporate Governance.

iii. To develop action plan across the continent.

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[32] ACMF – Background, Objectives Governing Council: http//www.ACMF@goggle.search.com.

iv. To contribute to and learn from the Global Policy Dialogue on Corporate Governance issues.[33]

At individual levels in Africa, some African countries have taken the initiative to organise workshops, seminars and trainings. Countries like Nigeria[34] and South Africa[35] have also taken the initiative to develop code of best practices.

5.7 MODELS OF CODES OF BEST PRACTICES

The OECD in its preamble to its "principles of Corporate Governance" states that "there is no single model of good Corporate Governance".[36] This cannot be farther from the truth.

Some models that have become guidelines for gauging corporate practice are the Cadbury Report of 1992, the Day Report of Canada 1994, the Greenbury Report of UK 1998, the Kings Reports 1 & 2 of South Africa (1999, 2002) and the Higgs Report of UK (2003). The Cadbury Report is a product of the committee chaired by Adrian Cadbury in May 1991 by the Financial Reporting Council, the London stock Exchange and the accountancy profession. The essence of the committee was to address the financial aspects of Corporate Governance owing to the low level of confidence in financial reporting as well as the questionable ability of auditors to provide the necessary safeguards for financial reports. This lack of confidence was necessitated by failures in major corporations in UK. The report reviews the

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33 2nd Pan African Consultative Forum on Corporate Governance: http//www.corp.gorn.inafrica@gogglesearch.com

34 Code of Best Practice, 2003

35 Kings Report 1992 & 2002

36 "OECD Principles of Corporate Governance" Preamble at www.oecd.org/daf/governance/principles.html

structure and responsibilities of Boards of directors, role of auditors and the rights and responsibilities of stakeholders.

The Greenbury Committee on Corporate Governance was set up in response to public and shareholders' concern for the remuneration of directors. The Greenbury report emphasised "accountability, responsibility, full disclosure, alignment of directors and shareholders interest and improved performance".[37]

In the case of the Kings Report on Corporate Governance for South Africa, the Kings committee on corporate governance was headed by a former supreme court judge, Mervyne King, S.C. The committee published its reports in 1994 to incorporate a code of best practice to promote the highest standard of corporate governance.[38] The ambit of the report, apart from incorporating the financial and regulatory aspects of corporate governance, also advocates an integrated approach to good corporate practice.

Due to perceived inadequacies in the 1994report, and the need for greater corporate accountability, transparency and shareholder confidence, the Kings committee released the Kings Report 2002, which embodies essentially the concept of "triple-bottom-line reporting" encompassing the economic, environmental and social aspects of corporate governance. The report emphasised the involvement of a wider spread of internal and external stakeholders consisting of workers, trade unions, consumers, suppliers,

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[37] Greenbury, R. "The Greenbury Report, Chairman's Preface at 7. www.ecgi.org/codes/country

[38] King Report 2002 – Sarbances Oyley www.ecgi/codes/country at 9.

communities and the media. The Report encourages stakeholders' institutional activism, business and the financial press and relies on disclosure as a regulatory mechanism. A major distinctive feature of the report is that the recommendations were regarded as binding instead of being voluntary. According to the report, the legal mechanism for the enforcement of the 2002 code remains the existing legal remedies of:

i. The South African Company Law of 1973 as amended;

ii. The Common Law; and

iii. The provision of the amended listing requirements of the South Africa Securities Exchange.

5.8 THE NIGERIAN CODE OF BEST PRACTICE ON CORPORATE GOVERNANCE AND MANAGEMENT

The need to align with global trend on corporate governance prompted Nigeria to identify with the nations with codes of best practices. This was made possible because of the collaborative efforts of the Securities and Exchange Commission (SEC) and the Corporate Affairs Commission (CAC) in inaugurating a seventeen (17)-member committee in June 15, 2000 to design a code capable of meeting the needs of the Nigerian corporate sector. The report is what is now known as the Code of Best Practices for Corporate Governance in Nigeria. The code was inaugurated in November 2003.

The code is a replication of the essential features of the following combinations, namely, the OECD principles, the recommendations of the

Cadbury, Dey, Greenbury, Kings 1 & 2, and the Higgs reports respectively.[39] The main trust of the code is the emphasis on the board of directors as leaders of corporate entities, the responsibilities of stakeholders such as shareholders and professional bodies as monitoring devices.[40] The code covers the responsibilities and composition of the Board of Directors of quoted companies and multiple stakeholders companies in Nigeria.[41] It states that the functions of the Board of Directors should cover policy and strategic matters.

Another highlight in the code is the provision that the composition of the Board of Directors, should reflect the diversity of experience without compromising compatibility, integrity, availability and independence. The separation of the position of the managing director of the company from that of the Chairman is also well emphasised in the code.[42] Also adequately covered is company proceedings generally, the frequency of meetings, executive and non-executive directors.[43]

The code does not leave out either, the all-important issue of the need to promote transparency in financial and non-financial reporting. The code thus requires the board to ensure *inter alia,* that internal controls are properly put in place; constitution of audit committee; proper preparation and presentation of annual reports and the compliance with the provision of the CAMA 1990.

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39 See El-Rufai N. "Importance of Corporate Governance". This Day, Vol. 9, No.30 of 12th July 2003 at p.24

40 See Ndanusa, S. and Mustapha, A. in their joint preface to the code

41 Section 1

42 Section 2

43 Section 3-7

Section 9 of the code has also directed the protection of both the statutory and general rights of shareholders. A new dimension in the recognition and articulation of the shareholder's rights is the codes provision that shareholders possessing more than 20 percent of the total issued capital of the company should ensure that they are represented at the Board unless they are in a competing business or have conflict of interest.

Apart from the role of the shareholders, the code equally emphasises the need and importance of audit committees in corporate governance. Consequently, the code mandates all companies to establish Audit Committees with the aim of raising standards of corporate governance. The composition, qualification and experience of members of that committee and its terms of reference are also dealt with.

The preface to the code also touches on the issue of enforcibility of the code. While the code urges companies to comply with the provisions of the code, it however states that:

> The Securities and Exchange Commissions and Corporate Affairs Commission will give due consideration to the compliance or otherwise of the provisions of this code in the treatment of the issues brought before them.

Apart from merely stating that due consideration will be given to the compliance of the provisions in the code, nowhere is it stated what the legal consequences for non-compliance would be. Would the provision of the CAMA or ISA be the basin for due consideration of compliance? We have not been told.

5.9 RULES OF CORPORATE GOVERNANCE AND THE CONVERGENCE DEBATE

Currently, there is a raging debate by academics, whether the corporate laws regimes of difference jurisdictions are converging due to the effects of globalization of economies of the world. In the United States particularly, some of the proponents of the view argue that convergence is not in substance but in form only. Other are however of the opinion that it is in function. Yet another view is that the convergence can be self-imposed by corporations through the instrumentality of contract.[44]

Convergence in form is said to occur where the appropriate corporate governance regulatory institution in one jurisdiction is transplanted in another jurisdiction by legislative action.[45] A major feature of formal convergence is that the basic structure of the existing governance institution of the recipient country is altered or restructured. This is not so in the case of functional convergence where the existing governance institutions are adequately elastic to meet the changed circumstances without necessarily changing the characteristics of the institution. In the case of contractual convergence, however, response may take the form of contract.

It is our submission however, that owing to differences in legal systems amongst nations of the world, which have serious foundational implications on

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44 See Gibson, J. Ronald, "Globalizing Corporate Governance: Convergence of Form or Function". Columbia Law School Centre for Law and Economic Studies. Working Paper 174, Feb. 2000. Available at http://papers.ssrn.com/paper:taf.abstract.ib=229517 pp.1-5, 26

45 See Khana, T.; Koganm, J. and Krishna P., "Globalization and Corporate Governance Convergence" A Cross Country Analysts, October 30, 2001, p.1

their corporate governance principles complete convergence may,[46] not be attainable now but in the nearest future. The various initiatives at the international, regional, sub-regional levels are a pointer to the above assertion. Because of social, political, cultural and legal differences in societal foundations, it is more likely that the various corporate governance standards would be subject to modifications depending on the local circumstance of the particular country.

[46] Anglo-Saxen Corporate Governance Regime relies heavily on stock market centred capital market; that of the Germans and the Japanese is built on bank-centred capital market, etc.

CHAPTER SIX

THE ROLES OF THE BOARD OF DIRECTORS, MANAGEMENT AND SHAREHOLDERS IN CORPORATE GOVERNANCE AND MANAGEMENT

6.1 INTRODUCTION

For quite some time now, the performance of corporate entities, especially the financial service industries in Nigeria, have left much to be desired. Because of poor performance, they have lost some of the confidence, which they hitherto enjoyed. Thus, so many companies have fallen by the wayside. The alarming rate of distress that have hit the financial service industries in particular has been a matter of serious concern not only to the nations monetary authorities but also to investors and the general public. Attempts made to unravel the root cause of this have indicated that the major reason for company failure has been mismanagement, and fraudulent practices by key players in the corporate terrain, as well as the inability to the inbuilt monitoring devices to perform their roles.

The management and governance of a company is a partnership between key stakeholders, such as the shareholders, Board of Directors, Management, External Auditors, Regulatory and Supervisory authorities. The interplay between the various stakeholders provide effective checks and balances required to make corporate entities survive,

The special focus of this chapter is the examination of the roles of the Board of Directors, Management and shareholders and their key officers, all fundamental indices for effective corporate governance and management in Nigeria.

6.2 THE BOARD OF DIRECTORS OF A COMPANY

The Board of Directors of a company is defined as " a committee made up of directors appointed by the shareholders of the company, charged with the responsibility of managing and directing the affairs of the company".[1] Another definition is that it "is a group of people elected or nominated by shareholders of a company to represent their respective interests in running the affairs of the enterprise".[2]

The directors make up the Board of Directors. Usually both Banks and other large companies share the same pattern of composition. Under the colonial period, directorship and shareholding were controlled by expatriates since they brought such businesses into the country. But during the indigenisation era, especially under the Enterprises Promotion Decree (1977-1979), the Federal Government for the first time took over the dominance and became the largest shareholder in most foreign companies and banks. The Federal Government initially appointed Chairmen of such Companies and Banks. Later it also appointed most members of the Board to take care of the interest of Nigerian shareholders. The above notwithstanding, the management of such foreign Companies and Banks were still under the firm grip of foreigners under various technical agreements. But with the divesting of its share in certain privatised

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1 Irukwu, The Company, the Shareholders, the Director and the Law (Enugu: Forth Dimension Publishing co. ltd. 1994) p. 89.

2 See Yahaya, M.I. "The Role and Functions of the Board" (Being a paper presented at the joint Bureau of Public Enterprise and Zonal Shareholders Association national Workshop on Corporate Governance and the Rights and responsibilities of shareholders in Nigeria, Abuja, 1992 p. 2.The writer is one time Managing Director/CEO Union Bank of Nigeria PLC.

industries the responsibility for appointment of directors to the Boards fell on the shareholders.

6.2.1 Duties of Board of Directors

The primary duties of the Board of Directors are:

(i) The duty to ensure that the company is operating within legal requirements and the provisions of the memorandum and articles of association.

(ii) The duty to ensure that adequate capital is available to enable the company fulfil the powers contained in the memorandum and articles of association.

(iii) The duty to ensure that all capital expenditures are approved first before management can embark on it.

(iv) The duty to maintain an efficient system to enable it govern effectively the company's affairs.

(v) The duty to oversee and approve all disposal of profits and the yardstick for such disposals.

(vi) The duty to appoint managing director or other chief executive officers.

(vii) The duty to ensure that the managing director develops good morale and create the feeling of security and job fulfilment amongst the employees in the company.[3]

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[3] Irukwu, J.O. Op. cit. at p. 91. See Davies, P.L. Gower and Davies: Principles of Modern Company Law, 7th ed. (London: Sweet and Maxwell, 2003) pp. 295-296.

Flowing from the primary duties are also other subsidiary duties. These entail the duty to: determine, assessed and decide the nature of businesses which a company will engage in within the spectrum of the objectives of the company; to select suitable managers or executive management team having regard to their capability, experience and expertise that would bring out the desired realization of the corporate objectives; the responsibility to monitor the activities of the management team who is in charge of the day to day running of the company's business; management team; setting a high team; set the standard of performance for the company's management moral tone for the company.[4] This also entails that the Board as the policy tink tank of the company must be able to influence positively the corporate image of the company and become a source of pride not only to the company as an entity but also to the companies employers, shareholders, and customers alike.

6.2.2 Functions of the Board of Directors

One central function of the Board of Directors is that of trusteeship. This is the specific responsibility to protect and manage responsibly the company's human and physical resources in the best interest of the company and the shareholders. As a trustee, the Boards responsibility lies to the shareholders, the society and other constituent group. The Boards function also includes planning effectively towards the attainment of the companies corporate policy objectives.

Aside from that of planning, the Board is responsible for the appointment of the management team. The Board determines what the company's

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4 Ibid at P.94

management team should be as well as the staff training policy. Usually, the chief executive is given a free hand to determine those that serve under him, while the Board sanctions or ratifies such appointment at a subsequent time.

The Boards functions also include taking crucial and major decisions that affect the affairs of the company. This is done after management must have fed it with all relevant information. Such decisions would usually border on pertinent issues like mergers, profit distribution, dividends and retention and so on.[5]

Ensuring corporate stability constitutes another function of he Board. Thus, the Board has the responsibility to examine and review the performance of the company against the background of market and economic forces both locally and internationally. Sometimes, the Board needs to exercise a firm control over management by reviewing periodically company financial statements, cash position, accrued revenues and expenses.

Another function of the Board is the compilation and presentation of the audited accounts and Directors Reports to the shareholders of the company at the Annual General Meeting. This is a serious and important statutory function for company directors.[6]

The enumerated duties and functions of the Board of Directors discussed above have clearly shown that the responsibilities are enormous and extensive. This raises the importance, therefore, for quality Board. The Board is the soul and body of the company. The success or otherwise of a company depends

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5 Yahaya, M.I. Op. cit. at pp.123-124.

6 A director who treats this particular function with levity may be held liable to creditors in the event of liquidation. In the banking sector, directors are made to comply with additional responsibilities. There are spelt-out in BOFID No. 25, 1991; CAMA 1990; the New Accounting Standard Rules etc. which imposes sanctions in the event of breach of duty.

largely on the quality of the Board it has in place. There is therefore the need to ensure that the right calibre of persons are appointed as Board members of corporate entities. These should be men of proven integrity, tested professionals in private or public service; men from specialized areas such as law, medicine, engineering, accountancy, finance and so on. With the appointment of this calibre of persons as non-executive directors, their esteemed role as an important corporate governance monitoring device would have been achieved.

6.3 THE PROBLEM WITH NIGERIAN BOARDS

The problems facing the Nigerian Board of Directors are basically of three kinds. These are:

(a) Externally induced problems;

(b) Internal Board problems;

(c) Personality induced problems.

Usually the external problems have to do with structural imbalances in the Nigerian economy and the economic system and inappropriate economic policies. In the case of Banks and other financial institutions, these may also involve unrelenting pressures from relatives and friends on Board members for favours. Such favours would usually border on request for minor contracts, loans and advances. And usually most congratulatory messages sent to directors on appointment are preparatory steps towards asking for favours. There is the obviously wrong impressing that company directors have unlimited power to interfere with the companies operational activities. And this subjects Board members to unwanted pressures. One way of tackling this problem is the

creation of awareness or enlightenment campaign. The public ought to be made to understand and appreciate the responsibilities of Bank directors and the legal environment in which they operate. With a clear understanding of the likely legal and non-legal sanctions which director are subject to, the public would likely appreciate the delicate position of a director.

Instability of tenure is another recognised externally induced problem facing most Board members. Quite often, one finds that company directors are relieved of their appointment following the dissolution of their Boards. This is quite correct in the case of Government Corporations and Government Controlled Banks or institutions. Instability of tenure does not give room for consistency in policy. According to professor Peter Umoh:[7]

> Instability of tenure tends to breed insecurity in Board members, some of whom are likely to quietly look for ways of helping themselves immediately on appointment. For the many directors with names and integrity to protect, sudden and unexpected removal from … Boards tend to cast a dark shadow over their integrity, leading to bouts of temporary depression and disillusionment.

The above clearly portrays the potential havoc that could be caused to the reputation of a company's business especially with regard to large corporations and the Banks and financial institutions. Tenure of Board members ought to be long enough to give room for effective formulation, implementation and monitoring of policies.

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[7] See Umoh, p. "The Problems of Corporate Government in the Nigerian Banking System," in Eguonu R. (ed). Board Room Management: A Book of Reading (Ikeja, Lagos: Strides Associates Ltd. 1994) p. 100. the author had the privileged of holding the following positions: Director of Research, Nigeria Deposit Insurance Corporation; professor of Finance and Former Head of Department, University of Port-Harcourt: Director, Fidelity Union Merchant Bank (1992-93); Director Agricultural Development Corporation, Calabar (1985-86) etc.

In Nigeria, the corporate environment is bedevilled with inappropriate Board/Management relationship. Appropriate relationship between the two can only be guaranteed where both the Board and the Management keep to their respective functions. Where the Board fails to resist the temptation of executing its own policies, there is bound to be friction and disharmony. Sometimes there is unnecessary rivalry between the Board Chairmen and their Managing Directors. Thus the Board Chairman may try to usurp the function of the managing Director. Both are supposed to cooperate with one another in the organizations best interest. The remedy to this problem lies in enlightening and educating the affected parties of the beauty of division of labour and the proper understanding of their respective responsibilities.

The idea of Executive Chairmanship practiced by some companies and Banks constitutes another problem facing corporate entities in Nigeria. This practice may not be in the best interest of such organization that engages in it. The problem is that it is unlikely for a Board Chairman to sit and pass judgement against himself or remove himself from office where there is abuse of office by such executive chairmen. The solution here lies on creation awareness on the part of the shareholders who are charged with the responsibilities of appointment. The Shareholders Association can take the lead to educate them of the dangers and adverse conditions inherent in the adoption of the Executive Chairmanship.

The quality of appointees to the Nigerian Board is yet another hydra headed problem. This is a problem that affects not only the public or large

corporations but also some Bank Boards. Board members are supposed to be people of unquestionable integrity, knowledge and experience in their professions. Apart from being persons committed to excellence and justice, they ought to be aware of the responsibilities and the obligations attached to their positions and the limits of the privileges and benefits derived there from. Unfortunately, they are not.[8] The remedy to its problem lies in ensuring that politics and favouritism are eliminated in the appointment of Board members. Secondly, Board appointments should not be an all comers affair. Board members must possess the right kind of academic qualification, enough to guarantee good quality reasoning, expertise in an area that is of strategic importance to the operation of the company. A Board filled with right quality of members no doubt will give birth to a good quality Board as well.

Multiple directorship and multiple Board membership, in spite of he earlier notion that it guarantees more exposure, experience and equips the director with useful information of the Board of another company, and thus enhances the director's ability for a thorough evaluation of alternatives,[9] time has proven that it can also create the feeling of arrogance and the wielding of excessive powers by directors. On the apparent disadvantage of this, Ebhodaghe[10] is of the view that:

> Such directors may not have enough time to devote adequate attention to the multiplicity of companies and may therefore operate below standard of expertise requires. Also, they may either

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8 Ogwuma, P.A. "Problems and Prospects of the Nigerian Banking Industry". Being a paper presented at the Financial Institutions Training Centre Seminar, Lagos, 1985.

9 See Eguon R. (ed). Board Room Management: A Book of Reading, (Ikeja, Lagos: Strides Associated Ltd. 1994) p.1

10 See Ebhodaghe, J. "Responsibilities and the Performance of a Bank". Being a paper presented at the Seminar on Bank Directors organized by the Department of Finance, Faculty of Business Admin., University of Lagos, November 22, 1989.

> unilaterally approve or influence the Board to grant credit facilities to these companies without disclosing their interest to other members. Such cases, when discovered, often lead to conflict.

Ownership arises, especially in the Banking sector, constitutes another reason for turning Nigerian Board rooms into warring grounds for shareholders attempting to control their Banks and sometimes, factionalizing the Boards. This ultimately affects the much-needed confidence in the banking sector.

There is also the rampant violation of legal provisions and rules regulating the operation of banks and other finance institutions. For instance, the provision of Section 18 of BOFIA states that no director, manager, or officer shall have any personal interest in any advance, loan, or credit facility, except where he declares his interest to the bank in question or grants such loan pursuant to the banks' rules and regulations. But, this has not been the case. Thus, many of the crises that rocked the Nigerian Board arose due to interest shown in such loans by Board members. On this issue, Eguonu[11] further observed elaborately that:

> Unfortunately, … declaration of interest in a company does not necessarily make the loan proposal from the company to the bank viable and profitable one. Some Board members insist on getting loans approved … in spite of management advice to the contrary. Such loans end up getting classified under the now in place prudential guidelines. Unfortunately, some of these loans go sour and the accounts get classified. In such situations, the Board members blame the chief executive for lack of credit judgement. Some Boards even suggest undue favouritism or downright malpractice. Contract award constitutes another problem area. Some banks and other Board members do not have contract sub-committees to recommend awards of contract for Board's approval. Chief executives who go ahead awarding contract without sufficient consultation with their Boards, run the risk of turbulent Board meetings at which their conduct are queried and in some cases, contract awards are revoked.

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[11] Eguonu, R. "Introduction to the Board Room" op.cit. p.2

The above clearly highlights that the self-serving interest of directors is a major problem militating against Nigeria Boards especially the banks of late.

6.3.1 Consequences of Board Room Crises on Corporate Governance

Though it is acknowledged that healthy and normal competitive conflict cannot be avoided at certain point in time in any organization, especially where it leads towards the achievement of the organizations corporate objectives, in the case of Nigeria, prolonged and unchecked crises at the Boards has shown clearly that it has the negative effect of causing short and long term damages to such organizations or companies and ultimately to the detriment of the affected factions, the shareholders, creditors and the customers respectively. For instance, this may lead to a myriad of consequences. And some of the long-term results could be: absenteeism of members at Board meetings; ineffective corporate governance; loss of tolerance, integrity and vision on the part of the Board; undesirable publicity; the employee' loss of confidence in the organization; confusion, chaos, misunderstanding and a feeling of depression, cheating and alienation in the minds of the losers in the aftermath of such crises; the dampening of job satisfaction and productivity of management and employees amongst others.

Meanwhile, the short-term consequences are; loss of investment and the prospect of financial gain in the company or organization; high labour turnover, a product of unstable and unfavourable work environment; loss of employment emanating from fall in the income of the organization; loss of deposits by

depositors, the collapse of the organization by banking system as the case may be.

6.3.2 The Chairman of the Board of Directors as a Stakeholder in Corporate Governance

The Chairman is the connecting link between the Board members and management, just as he is also the nexus between the organization and the general public. It is his duty to represent he Board in between meetings.

Section 263(4) of the CAMA governs proceedings of directors and the selection of the Chairman of the Board. The directors usually elect a chairman to represent them in their meetings. They also determine the specific tenure of his office. Commenting on the corporate expectation of the Chairman of the Board of Directors, Professor Nwankwo[12] has observed that the Chairman:

> … must be easily accessible to the Executive Directors … The Chairman is responsible for the work of the Board and he is accountable for its decision since he is expected to speak for the Board and to act for it between meetings. For him to perform these functions effectively, he should be involved in many decisions, which he may be called upon to speak in defence … He is the source of authority for the managers to run the operations. It is the Chairman who has the dual task of ensuring that the Board retains the confidence of the shareholders and management through dialogue rather than the Board passing a set of instructions to management to execute … The Chairman has the responsibility of monitoring the management and ensuring that progressive reports are submitted to the Board regularly.

In addition to the above, the Chairman, while exercising his powers must ensure that his appointment in the first place is valid and legal and that the meeting is conveyed in accordance with the relevant laws and regulations. It is

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[12] See Nwankwo, G. O. "Making the Nigerian Board Work" in Egouno R. (ed) Board Room Management: A Book of Reading (Ikeja, Lagos: Strides Associates Ltd. 1994) at p.95. The author was one time Chairman

also the Chairman's responsibility to decide on points of order whenever a member raises a point of order as to whether the proceeding being conducted complies with the relevant law or regulations of the organization.[13]

Unlike in the past when the Board Chairman was regarded as a mere figurehead,[14] the position now attracts a lot of prestige and importance, especially Chairmen of big corporations. The Chairman has a casting vote, which he uses in order to reach a decision or defer further discussion on a particular subject. However, he does not possess special powers above that of a director. While Section 263 deals with directors proceedings, Section 240 governs the powers and duties of company Chairman generally, which among other things include:

(a) Preserving order at meetings and taking such measures that are reasonably necessary;

(b) Ensuring that proceedings are conducted in a regular manner;

(c) Ensuring that the intention of any meeting is carried on while resolving any issue that arises before it;

(d) Ensuring that all questions that arise are promptly decided, and

(e) Acting in good faith in the best interest of the company.

Another power that can be gleaned from the provision of Section 239 is the power to adjourn a meeting. Considering the enormity of responsibilities of

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Union Bank of Nigeria PLC; one time Executive Director, Monetary and Banking Policies, Central Bank of Nigeria (1978-84).

13 Usually, such points of order border on: whether a particular motion is ultra vires the meeting; whether there is no quorum for a meeting; whether a particular line of discussion is unnecessary or whether an improper language has been used.

14 See Irukwu, J. O. Supra at p.24

the company Chairman and the sensitive and strategic importance of his position in the organization, it is submitted that persons seeking appointment to such positions must be persons of proven intelligence, knowledge, reasonable and must be persons with an impeccable tract record in effective management either in private or public capacity.

The Chairman must be in a position to exhibit certain qualities. He must be able to read and understand prevailing market forces and how they can be used advantageously to prop up the fortune of his organization. He must have a sound grasp of the legal environment under which is organization operates. He must be fair, impartial and not overbearing. He must be a good listener but a firm decision taker.

6.3.3 The Managing Director of a Company as a Stakeholder in Corporate Management

The managing director is the head of the executive management. His professional training, experience and background are important considerations in determining not only his appointment to office but also an indication of future happenings in his organization. He is a person appointed by the Board of Directors. He is usually armed with certain powers, which enables him to discharge specific managerial responsibilities delegated to him by the Board. He is also usually appointed under a service contract on full time basis and charged with the duty of effective management of his enterprise on daily basis.

In *Re Newspaper Proprietary Syndicate Ltd,*[15] the English court illustrated the status of a company's managing director. In the courts opinion, he is an:

> … ordinary director entrusted with some special powers. These special powers may be as broad or as strictly defined as the directors choose. The directors may … delegate to any managing director … such powers as they consider desirable to be exercised by him. Any such delegation may be made subject to any conditions the directors may impose, and either collaterally with or to the exclusion of their own powers and may be revoked or altered.

Implicit in the above is the fact that the appointment of a managing director connotes a delegation of powers of directors in accordance with the provision of the relevant articles or on the authority of the company,[16] apart from the earlier mentioned mode of appointment via service contract.

Under Nigerian law, the empowering provision is Section 262(5) of the CAMA, which allows the Board to appoint one of its members as managing director and to delegate any of their powers to him. In terms of remuneration, Section 268(1) provides that he shall receive such remuneration as the directors may determine. The special nature of the office of a managing director makes him a servant of the company.[17]

Like the company Chairman, the managing director is equally expected to be well equipped with all the relevant and necessary information bordering on the

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15 (1990) 2 Ch. 349

16 See also Boschoek Proprietary Co. Ltd. V. Fuke (1906) I CH. 148

17 See Anderson V. James Sutherland (Peterhead) (1941) SC 203; Re Newspaper Proprietary Syndicate, Supra in he Process of Winding up a Company, a managing director is given preferential treatment by paying all his remuneration. His salary ranks first in terms of priority of payment.

company's affairs than other directors. This is in view of his special proximity and connection with controlling machinery at his disposal.[18]

The managing director of a company would usually be required to perform certain functions while exercising managerial powers allocated to him. Such duties include: ensuring an effective link between the Board and interpreting Board's laid down policies; ensuring that such policies are carried out by various managers and company staff. On the overall position of the company affairs, the managing director has the added responsibility to ensure that the Board is always briefed fully; submit reports, statements and reviews aimed at keeping the Board adequately abreast of the current situation of the company's affairs.

Similarly, in ensuring the realization of the company's objectives, the managing director is expected to, with the tacit cooperation of the managers, design programme geared towards the realization of the objectives of the corporation he directs. Ensuring effective control and efficiency on the management of the corporation constitutes one of the most important and tasking responsibilities of a managing director. Since he cannot do everything all by himself, he can succeed if he fashions out an efficient structure of delegated responsibilities.[19] The strategic relevance of the managing director in a corporate set up cannot be overemphasised. His success or failure will always have a rub off effect on the company as a whole. It is in line with this that it is again emphasised that the issue of multiple directorship, like that of multiple Board

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[18] See Shonowo V. Adebayo (1969) (3) A.L.R. Comm 419 (1969) 1 All N.C.R. 175.

[19] Normally, the Managing Director is assisted by Senior Managers, Deputy General managers, Departmental Managers, Sectorial Heads, etc

membership must now be discouraged. It has not proved to be of any advantage to organizations. Instead, it breeds unnecessary arrogance, lack of dedication to duty and below par performance by directors.

6.4 THE CORPORATE INTER-RELATIONSHIP BETWEEN THE BOARD OF DIRECTORS AND THE MANAGEMENT OF A COMPANY

One of the greatest problems confronting corporate entities in Nigeria is the reconciliation of the different roles of both the Board members and the management team. This problem has led to company and bank failures in Nigeria. The problem revolves around the Chairman who is the Board's representative and the managing director as the management representative. As pointed out by Irukwu,[20] the problem working against efficient company administration:

> … centred around finding how best to achieve a sensible balance in the relationship between the company's board and its management…

Sometimes, the relationship between the Board and management is not necessarily that of competition, confrontation and antagonism. It is a relationship of two contrasting extremes. As have been pointed out, [21] the relationship "… is either adversarial or collaborative". The consequence of both of these two extreme relationships is that on one hand, an adversarial Board will always usurp or attempt to usurp management function; overtly and continuously antagonistic towards management powers to take decisions. Usually, the Chairman of Board of Directors of such corporations or companies enjoys a lot of connection or

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[20] Irukwu, J.O. Supra at p.100

political clout and visibility. This kind of Board represented by such Chairman ultimately strangulates management initiatives and morale. On the other hand, a collaborative Board unduly supports management even when it is obvious that certain decisions should be questioned. Thus, such complacent Boards either inhibit or kill management initiatives. Both the adversarial and the collaborative Board undermine effective Corporate Governance and management in corporate entities.

In public corporations, the relationship between the Board and the management is undermined by over-zealous ministers who intervene with the Boards and management and ultimately leaving the enterprise in a bad state. What the Nigerian Boards and management's need, therefore, is to effect a reasonable balance in their relationship to one another. Both the Chairman of the Board and management, as representatives of both the Board and management, should strive to keep within the sphere of their influence and operation. They should eschew greed and avarice. They should not forget the purpose of their appointments, which is to direct and manage their corporate entities and to protect the interest of shareholders, creditors, employees and the depositors in the case of banks.

Neither the Board nor the management can be absolved from blame on the sad state of corporate entities in Nigeria. Both play significant roles in the bad performances of their institutions. With particular reference to banks, the

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[21] Hayatudden M. "Transforming Company: Bridging the Gap Between Management Myth and Corporate Reality" being a paper at the National Workshop on Corporate Governance and the Rights and Responsibilities of Shareholders in Nigeria, 28 – 29 November, 1994.

Central Bank of Nigeria (CBN) and Nigerian Deposit Insurance Corporation (N.D.I.C.) collaborative study carried out in October 1995 revealed that most of the Banks "… attributed the distress condition in the industry to the following factors, which were ranked as follows: advances and bad loans (30.1%); fraudulent practices (16.4%); lack of adequate internal supervision (20.1%) and bad management (13.0%).[22]

As also shown by the findings, there were two sets of Banks namely, the distressed and the healthy banks.[23] The distressed ones attributed such distress, which were also ranked to undue interference by Board members (29.4%); bad credit policy (19.4%); economic depression (23.5%); and political crises (17.6%).[24] The healthy ones firmly attributed the virile condition to strict discipline (26.0%); adequate capital base (30%); high liquidity position (24.3%); minimum fraud and sound internal control (7.2%) and good management and competent staff (15.3%).[25]

Even in the international scene, a similar study carried out in the United States in 1988 by the United States Controller of Currency (the supervisor for National Banks)[26] heaped bank failure on the doorstep of management and the Board of directors. According to the report, 60% of the failed banks consist of directorate that were deficient of banking knowledge or were either uninformed or passive in the supervision of banks under them. Such deficiencies, according

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22 See Appendix 2 of the findings of the study titled "Distress in the Financial Service Industry:" A CBN/NDIC Collaborative Study, Page Publishers Ltd. Lagos (hereinafter called the Report).

23 See Appendix 1 of the Report

24 See Appendix 3 of the Report

25 See Appendix 4 of the Report

26 The study is titled "Bank Failure: AN Evaluation of Factors Contributing to the Failure of National Banks", Washington D.C. United State.

to the report, were as a result of the fact that the Board does not get adequate or timely information from management and the unwillingness to correct problems identified.

The essence of the above analysis is that in spite of macro or external economic factors, that threaten the existence of a bank or corporate entities; good and responsible management can halt or ameliorate such external factors even at the critical stage of deterioration and resurrect it from the point of imminent death. The root cause of business failure and collapse of corporate entities in Nigeria and elsewhere, therefore, is poor governance and management.

6.5 THE COMPANY GENERAL MEETINGS AS ORGANS OF CORPORATE GOVERNANCE AND MANAGEMENT

The company's general meeting of members represents the primary organs in the company. In fact, it constitutes the main avenue in which the company takes corporate decisions by resolutions properly perused. A company meeting is made up of the company's members. One of the basic rights of a member of a company is the right to attend any general meeting of the company and to speak and vote at such meetings with regard to any resolutions.[27] Though the word "meeting" impliedly connotes the presence of two persons and above at the gathering of members of a company, it is possible and within the ambit of law for one person to constitute the meeting of a company.[28]

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[27] See S.18 of CAMA

[28] See East V. Bennet Bros Ltd (1911) Ch. 163; SS. 223(2); 213(2) and 239(4) of the CAMA

The company meeting needs not be formal in every case.[29] It could be informal in nature. For instance, Section 234 of CAMA provides, in respect of a private company, that a written resolution signed by all company members who are entitled to attend and vote is effective and valid as if it was passed at the company's general meeting. Again, where a matter intravires the company, a decision on it need not be taken at a fully convened general meeting of the company. Once all the individual shareholders, not just a majority, assents expressly to it,[30] it is sufficient to bind the company even if it is a mere agreement or tacit acquiescence of the members ordinarily entitled to vote on the matter.[31]

There are three types of general meetings of companies. They are:

1. Statutory meetings
2. Annual general meetings, and
3. Extra-ordinary general meetings.

6.5.1 Statutory General Meetings

Section 211(1) provides that every public company shall, within a period of 6 months from the date of its incorporation, hold a general meeting of the members of the company.[32] The language of the provision indicates that the holding of a statutory meeting is mandatory. The essence of a statutory meeting

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29 The general rule that a company meeting must be formal for purposes of binding a company in its corporate capacity is stated in Re George Newman (1895) I Ch. 674 ay 686, where Lindley L.J. said that "… the company is entitled to the protection afforded it by a duly conveyed meeting and by a resolution properly considered and carried and truly recorded". See also Boulton, "The Law and Practice of meetings", 6th Edn. P.231.

30 See Okeowo V. Miglore (1979) 11 SC 138, 192; Re Express Engineering Works Ltd. (1920) 1 CH. 466; Re Oxford Motor Co. (1921) 1 All E.R. 646

31 See Re Bailye Hay & Co. Ltd. (1971) 1 WLR 1357; Re Gee & Co. Ltd. (1974) 2 WLR 515.

32 Under the 1968 Company Act, the minimum and maximum periods were one moth and three months respectively. See S. 122(1) of the 1968 Act.

is to avail members the opportunity of having the first progress report of the performance of the company from the company directors and promoters.[33] Usually, the maximum period stipulated under the CAMA is calculated from the first day of the company's incorporation. This is a radical departure from the 1968 Act where the maximum period of three months within which the meeting is held was calculated from the date in which the company is entitled to commence business.

A statutory meeting is held once in the existence of company to satisfy the provision of the Act – within the first six months. But sometimes, within that same maximum period, an extraordinary general meeting may be held. However, in *Gardener V. Iredale*,[34] the court held that with respect to statutory meeting, it must be clearly indicated that it is a statutory meeting and all other requirements pertaining to the convening of statutory meeting must be complied with.

The main purpose of a statutory meeting is to discuss matters relating to the floatation of the company or arising out of the statutory report. A statutory meeting has the added importance of availing the shareholders the privilege of subjecting directors to probing questions with respect to matters in the statutory report. Again, statutory meeting provides the shareholders the opportunity of meeting and knowing the directors and secretary of the company personally.

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33 See Orojo, J.C. Company Law and Practice, 3rd Ed. (Lagos: Mbayi & Associates Ltd. 1992) at p.274

34 (1912) 1 Ch. 700.

A statutory report must at least, 21 days before the date of the meeting be forwarded to every member of the company. It must also contain the following particulars,[35] namely:

(a) The total number of shares allotted and the amount paid thereon and distinguishing shares allotted as fully or partly paid up otherwise than in cash;

(b) The total amount of money received by the company in shares allotted;

(c) The names, addresses and descriptions of the principal officers of the company;

(d) Particulars of pre-incorporation contacts and proposed modifications thereon;

(e) Any underwritten contract that has not been carried out and the reason for it;

(f) The arrears, if any, due on calls from every director;

(g) The particulars of any commission or brokerage paid or to be paid in connection with the issue or sale of company securities to any director or manager; and

(h) Abstract of receipts and payments to the company, the balance in hand, and an account or estimate of the preliminary expenses of the company.[36]

Members present at statutory meeting are empowered under Section 211(8) to discuss any matter pertaining to the formation of the company and its commencement of business or emanating from the statutory report, and where a member wishes any resolution to be passed on any matter arising out of the statutory report, he is required to give 21 days notice from the date in which the

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[35] S.211(2) and (3) of CAMA
[36] S. 211(4) of the CAMA

statutory report was received, to the company of his intention to propose such resolution.[37]

Section 216 provides that the statutory meeting shall be held in Nigeria and the report must be certified by at least 2 directors. Failure to comply with the requirement for the holding of a statutory meeting or to prepare and send the statutory report to members or deliver a copy to the commission may be a ground for compulsory winding up a company.[38] This is apart from the general liability that lies on the company and any officer who defaults in complying with the requirements of Section 211 above.

6.5.2 Annual General Meeting

Section 213(1) regulates the holding of an Annual General Meeting. The meeting is held in every calendar year[39] and not more than 15 months after the last Annual general Meeting. Where a company holds its first Annual General Meeting within 18 months of its incorporation, it needs not hold it in that first year or in the following year.[40] But the Corporative Affairs Commission has the power to extent the time for holding such meetings by not more than 3 months. However, the time for the first Annual general meeting cannot be extended for whatever reason.[41]

Where there is default in holding an Annual General Meeting, the commission may on the application of any member call or direct the calling of the

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37 S. 211(9) of the CAMA
38 S. 408(b) of the CAMA.
39 S. 211(4) of CAMA
40 The period is calculated from 1st of January and ending on 31st of December and not 12 months from the date of registration of the company. See Gibson v. Barton (1875) CRW Q.B. 329
41 See the provision of S. 213(1) of CAMA

meeting and give such directions as it deems fit including direction that the members of the company present in person or by proxy shall be deemed to constitute a meeting and that it may take decisions capable of binding on the members.[42] The limit of the commission's power to call a meeting is not intended to enable the commission to make any general change in the articles of the company. They are simply powers to enable the commission make temporary and ad hoc changes necessary for the purpose of the meeting.[43]

The Annual General Meeting is a general meeting for all intents and purposes. Thus, any matter or thing that can ordinarily be done in the general meeting can also be undertaken at the Annual General Meeting. Such matters generally include:

(a) Declaration of dividends;

(b) Appointment of directors and auditors;

(c) Consideration of directors' and auditors' report;

(d) Presentation of financial statements.

The importance of an Annual General Meeting stems from the fact that it personifies the forum where the ultimate control of a company lies. Professor Gower[44] said this much when he observed as follows:

> The Annual General Meeting is an important protection to members, for it is the one occasion when they can be sure of having an opportunity of meeting the directors and of questioning them on the accounts, on their report; and on the company's position and prospects. It is at this meeting that normally a proportion of the

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42 See S. 213(1)(b) of CAMA. Under the 1968 Company Act, the Registrar of Companies lacked the capacity to extend time within which AGM may be held.

43 S. 213(2) of CAMA

44 See Danjuma, M. The Role of the Company Secretary in Corporate Management, (Ibadan: Heinemann Educational Books, Nig. PLC, 1991) at p.148

> directors will retire and come up for re-election and at which the members will be able to try to exercise their only real power over the board – that of dismissal. Moreover, it affords members an opportunity of moving resolutions on their own account.

The Annual General Meeting of the company does constitutes another avenue where the members could also exercise their right. It thus personify an important forum of immeasurable value to members.

6.5.3 Extraordinary General Meetings

An extraordinary General Meeting is a meeting designed to take urgent matters that had arisen and which cannot wait till the next Annual general Meeting. Thus, matters discussed at an Extraordinary General Meeting are regarded as special matters.[45] The meeting may be convened at the members instance, who are holders of not less than one-tenth of the paid up capital of the company, carrying voting rights at general meetings in the case of a company with share capital. While in the case of company with no share capital, by members representing not less than one-tenth of the total voting rights of all members having a right to vote at the general meeting.

Section 215(3) however requires that the requisitions must specify the objects of the meeting and signed by all requisitionists, which must be deposited at the registered office of the company.

The court may *suo moto* or upon application of a person entitled to vote at such meetings, order a meeting to be called and held. This is where it is impracticable for any reason to call or conduct a meeting of the company. Both

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[45] Gower, Principles of Modern Company Law, 5th Ed. (London: Stevens & Sons, 1998) at p.528

directors and ordinary members are entitled to apply to court for the holding of such meetings.[46]

6.5.4 The Proxy Machinery

Section 230(1) confers on any member of a company who is entitled to vote but unable to attend the meeting of the company, the right to appoint a proxy and vote on his behalf. A proxy may or may not be a member of the company. Appointment of proxies do not apply to companies without share capital except where the articles so provides.

It is mandatory for notices calling for a meeting to include or provide for the right of members to appoint a proxy to attend and vote instead of the member in question. Every officer responsible for such an omission is liable to a fine of ₦250.00.[47]

Usually the form of the instrument appointing the proxy is regulated by the articles. The proxy may either be general or special in nature. A general proxy gives a person the right to vote as he deems fit, while a special proxy right to vote is depended on the wishes of the appointor.

The instrument appointing a proxy must be in writing under the hand of the appointor or his attorney. A proxy may be a member of a company or a total stranger. The instrument and Power of Attorney is deposited at the head office of the company or other specified place in Nigeria not less than 48, has elapsed before the commencement of the meeting at which the proxy is to vote.[48]

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46 S. 215(8) of the CAMA

47 S. 230(2) of the CAMA. See also S. 218(4), which provides for a penalty of ₦500 for a similar default

48 See S. 230(7) of the CAMA

Once a vote is carried out, pursuant to the terms of a proxy, the vote is valid notwithstanding the previous death or insanity of the principal or the revocation of the proxy or authority as long as the company had not received prior information in writing regarding such death, insanity or revocation.[49]

Where both the appointer of a proxy and the proxy attend a meeting and vote on a particular resolution, only the vote cast by the appointor shall be counted.[50] But the voting right of the proxy is not extinguished, especially with regards to other resolutions on which the appointor or principal does not participate.

The proxy machinery represents, in corporate life, an important internal corporate governance monitoring devise. Effective use of the proxy instrument by shareholders would no doubt, contain effectively the continued divergence between the interest of the shareholders and those of management. Instead, in Nigeria, shareholders' voting have always been fraught with the problem of lack of collective action and free riding. The problem of collective action persist because many shareholders who are entitled to vote are erroneously of the view that their single votes are not likely to sway a particular decision on any issue on their side so they give up. It is instructive to note that effective use of the proxy instrument would ameliorate this problem. It is submitted that the solution here lies in every shareholder studying the affairs of a company first and anticipating what way the contest will be decided. Once this is done, even where the shareholder cannot personally attend, he can appoint a special proxy to do his

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[49] See S. 230(5) of the CAMA

bidding at the meeting. On the issue of free riding or apathy on the part of shareholders, the problem has been complacency on the part of shareholders who always believe that whether or not they take active participation in changing management policy or not, they would share in the benefits that results from the efforts of other shareholder. One can imagine the result of the side effect of this kind of corporate behaviour on effective corporate governance and management in Nigeria. The solution here lies in every shareholder contributing his quota in changing management policy where it is necessary. This is one way of ensuring that management, especially in public companies ceases from continuing as "self-perpetuating oligarchy".

The failure of shareholder in this regard has been a major benefit to the management and thus enable them to perpetuate found. In reality Nigerian directors cognisant of the proxy instrument as an effective and decisive tool of corporate control have never hesitated from nominating themselves as proxies given the slightest opportunity. Thus cashing in on the fact that Nigerian shareholders are mostly dispersed and with small shareholdings,[51] company directors apart from controlling the administration of corporate entities, have taken effective control of the general meeting despite the fact that all put together, their shareholding is in the minority.[52]

6.6 THE CORPORATE RELATIONSHIP BETWEEN THE BOARD OF DIRECTORS AND THE COMPANY GENERAL MEETINGS

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50 See Cousins v. International Brick Company Ltd. (1931) 2 Ch. 90 CA
51 Supra at p.29.
52 See Orojo, Supra, p.29.

The point has previously been made that both the directors and the member in general meeting are key players in the corporate set up, and that both possess collective responsibility in corporate governance and management. Above all, both represent two important organs of a company. While the powers of the Board of Directors is primary, that of the shareholders is residual or concurrent or supervisory as it is often called. In spite of their different backgrounds, their aims and aspirations are effective corporate governance and management of their corporate set up.

In theory, shareholders owe the company, while the Board of Directors constitute an important aspect of the company entrusted with governing responsibilities. The supervisory power of the Board is exercised through the platform of the general and extraordinary meetings.

One point that should however be taken note of is that both are important internal corporate governance monitoring devises. But while the Board exercises its monitoring responsibility through the Board, the shareholders do theirs through the platform of the general meetings.

One practical advantage of the general meeting as a primary organ of the company is that it "makes for corporate democracy and facilitates checks and balances".[53] Additionally, it gives the company shareholders, an essential avenue to air their views and ventilate their grievances on matters pertaining to and concerning the affairs of the company, especially those bordering on company management. It has been held that the ultimate control of the company rests

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[53] See Danjuma, N. The Role of the Company Secretary in Corporate Management, Supra at p. 133.

squarely on the shoulder of the members in the general meeting.[54] To this extent, the CAMA especially the Articles of Association has given the members two kinds of powers namely primary and residual. Section 296(3) CAMA, deals with the primary powers reserved to the members to do among other things, alter constitutive documents of a company via the resolution of the general meetings; alter, increase or reduce capital in the general meeting; appointment and removal of directors and auditors in the general meeting. The residual powers on the other hand, pertains to matters such as: the exercise of all the powers in vested in the Board of Directors where the board cannot or will not exercise them or ever ratify or confirm any action taken by the Board.[55]

An agency relationship exists between the members in general meeting and the Board of Directors. Perhaps, the necessity for delegation of functions by the company general meeting arose out of the need for practical business convenience. Theoretically, members of a general meeting occupy a supreme controlling position. Thus while the general meeting can remove the board, the general meeting is itself irremovable. Theoretically, there exist the sovereignty of the members in the general meeting. But the reality of the case shows a contrary situation. The problem of the Nigerian shareholders, as explained earlier on, borders on desecration of the companies Annual General Meetings by the Directors, the fragmented nature of members shareholdings; disinterestedness of shareholders attendance of meetings, lack of collective action, free riding and the block voting by minority shareholders. Thus, the Annual General Meeting has lost

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[54] See Yalaju Amaye v.A.R.E.C. Ltd. (1990) 4NWLR (pt.145) 422.

its esteemed place as a platform for shareholders monitoring and supervisory function. Instead, it has become a platform for the directors disenfranchisement of the shareholders. In fact the Annual General meetings has turned to social events of little practical importance. As explained by Dr. Ahmed Abdullahi,[56] not only are shareholders:

> … denied any meaningful say in the affairs of their company … most reports read out by directors or chairmen at Nigeria AGMs tend to be formal, colourless and of little value as they contain no useful information for the benefit of the shareholders. The Directors know this and the shareholders also know.

In view of the above and with a view of ensuring that both Nigerian shareholders, and the Board of Directors perform efficiently their monitoring role in corporate entities in Nigeria, they must converge and chart deliberately a genuine course for the growth, governance and management of the Nigerian corporate entities. Unless these responsibilities are effectively discharged, the contribution of Nigerian companies to national and societal growth will remain a mirage.[57]

6.7 THE COMPANY SHAREHOLDERS

The governance and management of a company requires the fashioning out of aims and objectives and the appropriate strategies for their realization. It is in this view that both the directors and shareholders as strategic stakeholders in the corporate terrain are assigned the responsibilities of management and that of providing necessary checks on the activities of directors. The Nigerian

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55 S. 63(5); and 265 of The CAMA

56 Abdulahi, A. The Company in a Changing Environment, Supra at p.46.

57 Companies Perform Several responsibilities, consisting of profit and non-profit making activities.

shareholders especially in public companies, has the primary duty of monitoring the activities of management.

In private and state owned companies, it has been observed that the owners[58] of such companies in most cases display strong and highhanded influence and control over management policies and decisions since in most cases shareholdings are highly concentrated in a few persons or government. This has made nonsense of the monitoring or watching role of the Nigerian shareholders. In fact, hardly can a distinction be drawn between owners of the company and the company since the same person own, govern and manage the company.

In public companies, however, ownership is highly diffused and not concentrated especially in companies that have large and fragmented shareholdings. This in turn has created its own problem, which is the reduction of shareholders activism in corporate governance in Nigeria.

6.8 THE RIGHTS AND RESPONSIBILITIES OF SHAREHOLDERS

The word "right" means an interest which the law acknowledges and protects. But of necessity, rights cannot be discussed in isolation since correlatively, it also involves the duty or obligation to perform.[59] These rights and obligations are only summarily dealt with here, since most of them are indirectly treated elsewhere. The rights which a shareholder has are rights within and

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58 Usually the majority equity holders is both the Chairman and Chief Executive officer of the Company.

59 See Atoki, A. "The Rights and Responsibilities of Shareholders", Being a paper presented at the National Workshop on Corporate Governance and the Rights and Responsibilities of Shareholders in Nigeria, 28-29 November, 1994, p.3

against the company. It is a personal claim and not a proprietary claim.[60] Shareholding gives a person the right of membership of the company. Before a shareholder can be entitled to the exercise of his rights, and the enjoyment of the consequential advantages accruing from such rights, he must be a member of the company.

A person can become a shareholder in a company once shares are allotted to him; by agreeing to take qualifying shares; by transfer; by transmission; by operation of law or by conversion of debentures into shares.

Shareholders rights emanate from three important sources, namely; the Company's Act 1990; the Common Law and Equity and Case Law. As the chief source of shareholders rights, the CAMA, apparently motivated by the overriding need to build a protective wall around shareholders, prospective investors and the company creditors, provides that every company must now disclose certain fundamental information with regards to certain issues.

Specifically, Section 42 of the CAMA mandates a company, once requested by a shareholder, to provide him an up to date version of the Memorandum and Association on the payment on a prescribed fee. Secondly, it also debars a company from requesting a shareholder to subscribe for more shares than the one he previously held on becoming a member or increase his liability to contribute to the share capital of the company or pay more by any other means

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[60] A Proprietary right can only be demanded by the Board of Directors of the Company since only them hold the right to manage the affairs of their company. The shareholders cannot therefore demand for this right. See generally Atoki, A. "The Rights and responsibilities of Shareholders" Ibid. at p.4

to the company where a company's memorandum and articles of association has been altered after becoming a member of a company.[61]

A third instance is where a company's articles contain pre-emptive rights in favour of existing shareholders. In such a situation, a company is estopped from issuing new or unissued shares unless same are offered first to the company's existing shareholders in such proportion determined by the shareholding.[62]

Another instance is governed by Section 79 of the CAMA. The Section provides that a subscriber to the memorandum of Association of a company is deemed to be a member of the company'[63] while any person whose name is entered in a company's register of members and have a minimum of one unit of share in the company is deemed to be a member of the company.[64] One basic right of the shareholder is the right to attend the general meeting of the company. Thus, once a member has paid for all calls and or other sums payable by him on the shares which he holds in a company, he is entitled to attend, speak and vote at any general meeting of the company.[65]

Persons entitled to receive notice of meeting for purposes of such general meetings is regulated by Section 219(1) of CAMA, which states that every member who is in his capacity as the actual owner of such share, legal representative, receiver or trustee in bankruptcy of a member is entitled to receive the notice convening the meeting. Persons in the above categories are

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61 See S. 49 of CAMA

62 See Part II, Table A Schedule 1 CAMA 1990. Presently, most public companies exclude pre-emptive clauses from their Articles.

63 S. 79(2) of CAMA

64 S. 79(3) of CAMA

65 This means the Statutory Meeting, the Annual General Meeting and the Extraordinary General Meeting. And does not include creditors meetings or meetings of the Board of Directors.

entitled to appoint proxy in their stead.[66] And a consequent right to the right of attendance of general meetings by shareholders, is the right to obtain courts injunction to restrain the holding of a general meeting, and if already held, set it aside by courts declaration.[67]

A shareholder may signify his intention to vote either by the show of hands or by poll.[68] The demand for poll will normally be resorted to immediately after the conclusion of voting by show of hands an indication that there is dissatisfaction with voting by show of hands.[69]

Section 225(1), however prevents a shareholder from demanding for poll at the general meeting on matters bordering on the election of the Chairman of the meeting or the adjournment of the meeting; and election of members of the audit committees.[70]

The shareholder has the additional right to requisition for a general meeting where the directors fail to hold it. The condition precedent however, is that such a shareholder must hold not less than five percent of the total voting rights in the company.[71]

Section 385 gives a further right of payment of dividends to shareholders. This section provide that a shareholder has the right to be paid dividends in proportion to the nominal amount of shares he holds in the company. Dividends

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66 See S. 230 of the CAMA

67 See Onwuka v. Taymani (1968) ALR 313; see also S. 224 of the CAMA

68 A poll is a more matured way of counting members' votes usually dtetrmined by their shareholdings. Usually, a unit share carries one vote only.

69 See Anthony v. Seger (1789) 1 HAG. CON. 9.

70 S. 359 of CAMA

71 See S. 235(2) of the CAMA

represent a return on a shareholder's investment in a company and payable out of the distributable profits of a company.

A company may decline to pay dividends on reasonable and compelling grounds of inability to discharge debt obligations.[72] But where a company's failure to declare and pay dividends is motivated by the selfish need to avoid taxation, the Federal Board of Inland Revenue may direct that any such undistributed profit of such company be deemed paid or distributed[73] and thus will be assessed to tax accordingly.[74] Outside this, however, it appears the right to decide whether or not profits should be distributed and what is to be distributed lies within the exclusive preserve of the directors. And again, while shareholders can seek to reduce the amount of dividends recommended by directors, they cannot increase it.

A shareholder's right to sue the company to enforce payment of dividend is dependent upon the Board of Directors' "interim" or "final" declaration for approval by the company in general meeting. Once the declaration requirement is satisfied, the shareholder acquires from then on the right to specialty debt due from the company and recoverable within a period of twelve years.

Right to inspect Statutory Books of the company[75] constitute another important right of the shareholder. Statutory books are kept at the registered office of the company for purposes of accessibility. While a shareholder is entitled

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72 S. 381 of the CAMA

73 S. 17(1) of the Companies Income Tax Act (hereinafter called C.I.T.A. 1990)

74 S. 17(2) of the CITA

75 Ss. 87, 192, 194, 242, 215(6) and 332(1) of CAMA, which deals with Company Statutory Books such as Register of Members, Register of Charges, Register of Debentures, Minute Book, Register of Directors and Secretaries and Accounting Records respectively.

to inspect the register of members at no monetary cost, a non-member can only do so upon obtaining prior permission of the company and the payment of a nominal inspection fee of a specified amount.

With specific reference to accounting records however, it appears a shareholder cannot inspect the accounting records of a company in view of the provision of Section 337(1) of CAMA, which makes such inspections the preserve of the officers of the company.[76]

The shareholders are also vested with the right of appointing key officers of the company who are charged with the responsibility of directing and managing the affairs of the company. Though the first directors of the company may be appointed by the subscribers to the Memorandum of Association or by naming them in the Articles of Association,[77] the shareholder's right of appointment of such key officers relate to the appointment of subsequent directors. This is done by an ordinary resolution of the members at the general meeting.[78] It is also the shareholder's right to approve or not to approve the Board of Directors appointment of directors in the event of casual vacancies, either due to death, resignation, retirement or removal of such previous directors. Such shareholders' approval is exercised at the Annual General Meeting. Section 249 of CAMA provides that in the event of the shareholders refusing to approve the Board's appointment of such directors, the appointee shall immediately cease to hold office. The shareholders' right is not narrowed down to appointment

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[76] The definition contained under S. 650(1) of the CAMA does not equate shareholders to officers of the company.

[77] S. 247 of the CAMA

[78] S. 248 of CAMA. Usually such appoints are made at the Annual General Meeting of the Company.

alone. It also extends to the removal of directors by ordinary resolution passed at any time, despite any agreement between the director and the company or any provision in the articles to the contrary.[79]

Under Section 350, every company is mandated to appoint an auditor or auditors, whose responsibility shall be to examine the financial statement and certify whether accounting records have been properly kept. This apart, the auditor's responsibility also includes the determination of whether the company's balance sheet and its profit and loss account tallies with what is reflected in the accounting records. It is the shareholders' right to appoint Company Auditors. This right is exercisable at the company's Annual General Meeting.

In public companies, the CAMA confers on the shareholders the power to appoint another shareholder as a member of the Audit Committee at the company's Annual General Meeting provided the shareholders give a minimum period of 21 days notice in writing to the Secretary of the company before the date fixed for the general meeting. The primary purpose of the Audit Committee is to examine the auditor's report and make recommendation to members at the Annual General Meeting. The whole essence is to propel the shareholders towards genuine and effective supervisory role in corporate governance. The committee normally consists of equal numbers of directors and representatives of the shareholders.

An equally important right, which the shareholder has is the right to material information pertaining to the affairs of the company.[80] The position is

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[79] Ss. 357, 379, 383 of the CAMA

that financial statements, which form the basis of shareholders information are to be laid before the shareholders at least twenty-one (21) days before the date slated for the Annual General Meeting. In the case of shareholders of public companies, the medium of shareholders information may be the holding of an extraordinary general meeting where urgent matters necessitating urgent attention had arisen.[81]

The right to seek relief against illegal and oppressive conduct is conferred on the shareholder under the CAMA.[82] Normally, the exercise of the right is preceded by the allegation that the activities of a company are being conducted in a manner unfairly prejudicial and oppressive against the interest of the minority shareholders. The affected member(s) is at liberty to apply to court to obtain relief. There is truth in the saying that one cannot take a benefit under a deed without subscribing to the obligations thereunder. Therefore, shareholders also owe certain obligations and responsibilities to the company. But while the shareholders rights are mainly a derivation of statute, the same cannot be said about their accompanying obligations and responsibilities. These are not specified by the CAMA. Nevertheless, some of these responsibilities and obligations could be gleaned from the general principles of company law.

A shareholder has the responsibility to pay for the number of shares, which he has agreed to take in a company once he has subscribed to the memorandum of association or become a member subsequently. The essence of this obligation

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80 Iwuchukwu c. Nwizu (1999) 7 NWLR

81 See S. 334(1) of the CAMA. Financial Statements include company audited profits and loss account, the balance sheet, and the Report of the Directors.

82 See Ss. 310 and 311 of the CAMA

is that, once there is a call upon the winding up of a company, he will be duty bound to pay for any unpaid call or unpaid portion of shares held by him.[83] Once a call is made and the member fails to honour it, such member may forfeit the shares upon which the call was made as well as being financially liable for all monies payable to the company by him in respect of such shares. According to Section 41(2) of CAMA, such monies payable by the member are in the nature of a specialty debt payable by the member to the company within a period of twelve years. As an addendum to the above, shareholders' obligation and responsibilities entail displaying objective vigilance over management exercise of its executive powers and to curb any excesses that may result from the exercise of such power vested on them.[84] Finally, they have the corporate obligation to project the image and business activities of the company.[85]

6.8.1 The Role of Shareholders Associations

In 1992, the technical Committee on Privatization and Commercialization incorporated seven zonal Shareholders' Associations, all as autonomous and independent entities and operating under a common generic name, Shareholders Association of Nigeria. The birth of the Zonal Associations had its root in the Privatization and Commercialization Decree 1988[86] which was promulgated in order to promote the ownership of shares by Nigerians in productive investments that were before then owned by the Federal Government. On a specific note, Section 4 required the Technical Committee on Privatization and

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83 This is true where the company is a Limited Liability Company. See also S. 21(1)(b) of the CAMA
84 S. 63 of the CAMA
85 See Atoki, "The Rights and Responsibilities of Shareholders" Supra at p.44
86 Decree No. 25 of 1988

Commercialization to fashion out the modality for ensuring even spread in shares ownership, and the equitable and meaningful participation by Nigerians and foreigners alike. This was however a daunting task for the Technical Committee for Privatization and Commercialization. In order to avoid mistakes of the indigenisation exercise of the past,[87] in which participation in share ownership was one sided, they ran into fresh problems, namely, the foreign shareholding formed the block shareholders (forty percent) while the remaining sixty percent was held by thousands or millions of Nigerians that were scattered throughout Nigeria. How to organise the scattered shareholders to exercise their rights as shareholders to nominate their representatives on the Board of Directors of such affected entities became a problem. Even though Nigerian Shareholders Solidarity Association headed by Chief Akintunde Asalu made an earlier debut into the corporate scene, it remained a largely Lagos-based association and made little or no effort to involve shareholders outside the Lagos axis for democratic participation in Corporate Governance.[88] This was in spite of their laudable motto,[89] aims and objectives, which *inter alia* include promotion of the interest and welfare of shareholder in publicly quoted and unquoted companies in Nigeria; ensuring orderly behaviour at company meetings; the arrangement of seminars and or lectures for the enlightenment of shareholders; organising shareholders

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87 The Nigerian Enterprises Promotion Decrees1972 and 1977 were promulgated to minimise foreign domination of Nigerian economy and to ensure Nigerians participate actively in the ownership and management of the economic activities in the country. These activities were classified into Schedules I, II and III. The objectives of the Decrees were not realised. The foreigners used their block vote consisting 60% or less to dictate who can be a director of both quoted and unquoted companies. Nigerian shareholders became voiceless and powerless.

88 See Zayyad, "Directors and Shareholders: Partners in progress". Being a paper presented at the National Workshop on "Corporate Governance and the Rights and Responsibilities of Shareholders in Nigeria", 28th – 29th November, 1994 at p.10. Dr. Zayyad was one time Chairman, Bureau of Public Enterprises, Abuja.

for companies general meetings; ensuring that shareholders keep simple records of their shareholdings and dividend payments; the eradication of corruption, nepotism, victimisation, immorality and other associated social vices; working in concert with government and the Nigerian Stock Exchange on matters of interest to shareholders and the Nigerian economy and working assiduously for shareholders representatives election to the board of public quoted and unquoted companies in Nigeria.

Nonetheless, its contribution, even though geographically limited, is undeniable. For the Association prides itself with compelling the management of the Aviation Development Company PLC in 1994 to send its Annual Reports and Accounts to its new shareholders when it threatened it with court action after refusing to release same earlier;[90] compelled the management of Owena Bank PLC in 1993, who had earlier moved the Annual General Meeting of the bank to Port Harcourt, to cancel the meeting on the premise that most of the shareholders who were mainly in Lagos could not attend.[91]

As hinted earlier, the formation of the Shareholders Association of Nigeria and its organization on zonal basis[92] was to create an appropriate and a much more elastic association that will make shareholders in quoted companies to participate effectively in the decision making process in Nigerian companies. It is the responsibility of the Technical Committee to organize and link them with the

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89 Their motto is "United We Stand, Divided We Fall".

90 See Fagunjade, B. This day, the Sunday Newspaper, September 7, 1997, p.38

91 Ibid. at p.38

92 The seven zones are Lagos (serving shareholder in Lagos State alone); Ibadan (serving Oyo, Ogun, Ondo, Osun, and Kwara States); Jos (serving Plateau, Bauchi, Adamawa, Taraba); Kaduna (serving Kaduna, Kogi, Niger, and Abuja); Onitsha (serving Anambra, Enugu, Benue, Edo, Delta); Port Harcourt (serving Rivers,

Stock Exchange and the Securities and Exchange Commission for the requisite professional guidance and regulation of their activities with the aim of ensuring that it become instrumental in the development of the capital market as well as enhancing their position generally.

The constitution of the Shareholders Association of Nigeria has the following aims and objectives, which were similar to the defunct Shareholders Solidarity Association, namely; to undertake the education and enlightenment of the average Nigerian shareholder on their rights and responsibilities; to promote solidarity between individual shareholders and encourage their interest in their respective company affairs; to facilitate representative participation in corporate decision making at the company meeting; encourage their regular attendance at company meetings; to nominate their representative to serve on the Board of Directors of publicly quoted companies; and to facilitate easy access to individuals and script share certificates, which in most times, are not claimed due to ignorance.

Shareholders activism in corporate governance in Nigeria is not a new-fangled idea. The concept had gained prominence in other capitalist countries, notably Britain, France [93] and the United States.[94] In France for instance, shareholders operating under the umbrella association of 'ROBINHOODS' adopted militant or radical postures to compel management to respond positively to their demand. Sometimes, the proxy machinery came in handy. By this, shareholders

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Akwa Ibom, Imo, Abia, Cross River) and Kano (serving Jigawa, Sokoto, Kebbi, Borno, Yobe and Katsina States).

93 See Policy, "The Decision Makers Magazine", Vol. 3, No. 4, January 20th – 1st February, 1998, p.16

94 See Hadden, "Company Law and Capitalism" (2nd Ed. London, 1977) p.327.

solicits for proxy votes at company meetings with the aim of effecting changes either in the company mandate or in the structure of management.[95] Similar efforts have been made in United States too,[96] where a group of shareholders, acting as pressure groups appropriately converted company general meetings into avenues for examining corporate conduct and in some occasions resort to actual revolt against corporations.[97] Similar efforts have been reported in Britain under the Investors and Shareholders Association Limited (ISA).[98]

Before drawing curtain on the role of the Shareholders Association of Nigeria, one needs to point out that, the association, unlike its predecessor – the Shareholders Solidarity Association; eschew confrontational postures as a means of compelling management to respond to its needs. Ironically, this has been said to be the major shortcoming of the organization. This has led to the accusation that:

> … it is more of a paper tiger and seemingly an elongation of the activities of the Technical Committee on Privatisation and Commercialisation now Bureau of Public Enterprises. More like Jacob's hand but Esau's voice.[99]

Notwithstanding, the above assertion, the Nigerian Shareholders Association has remained not only as an important pressure group but also a relevant corporate governance-monitoring device within the corporate set up.

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95 See Policy, op. cit. p.6

96 See Hadden, T. op. cit. p.327

97 See Hadden, T. Ibid. at p.327. In 1996 shareholders successfully led a revolt against corporations such as Westing Inc., Kodak Inc. and Sear Roe Buck Inc.

98 See Agom, "Shareholder Activism in Corporate Governance". Journal of Finance and Investment Law, vol. 4, No. 4, October 2000 p.267.

99 See Agom, Ibid. at p.270

Our preceding discussion has revealed that Corporate Governance and Management of corporate entities is a partnership between the three key players, notably, the shareholders, Board of Directors and Management. Each of these corporate arms has a unique responsibility to play in the process. Thus, the success or failure of a company will depend largely on the understanding and acceptance to play these important roles in good faith and to the best of the company. It is the failure to effectively perform the assigned responsibilities by each of the key players that initiates the process of corporate collapse.

The importance of corporate governance and management cannot be overemphasised. A country's economy will always be measured by the prosperity of its companies. And again, any company desirous of attracting investment and reasonable capital from both foreigners and domestic scene must attain a high level of corporate governance and management.

We have seen that the ineffectiveness of the inbuilt monitoring devices and the poor level of governance contribute to the problem of ineffective corporate governance and management. It is as a result of this that the realisation of the interest and expectation of the shareholders, is being championed by the Shareholders Association of Nigeria. Despite complaints about their modus operandi, they have achieved some success in prodding management to react in appropriate circumstances to managerial issues bordering on the interest and welfare of shareholders, though more is still being expected from the organization considering the current deplorable state of most Nigerian shareholders.

Finally, the Nigerian Boards and the Management, apart from being realistic, must brace up and ensure that corporate decisions are taken with the interest and expectation of all stakeholders in the company in mind.

CHAPTER SEVEN

THE CORPORATE MAJORITY AND MINORITY RIGHTS

7.1 INTRODUCTION

In the previous chapter, some of the matters examined were the duties owed by company directors, their role in the effective management and governance of their companies as well as the civil and criminal liabilities they are likely to be subjected to in the event of breach of duties. In this chapter, what is discussed is the enforcement of these duties which the company directors owe to the company as an entity and as well the company shareholder. But unlike the company, which stands in a clearly advantageous position when it come to enforcing these duties owed to it by simply commencing an action in its own name, in the case of the company shareholders, the situation is different since they must establish that they are seeking to enforce a personal right otherwise they must comply with the procedural huddle which requires the proof of *locus standi* to maintain a suit or seek relief as required in the rule of *Foss v. Harbottle*[1], also known as the majority rule.

Our focus therefore will consist in examining the rule in the case, the exception to it and how currently it fits into company law as well as the problems surrounding its application in Nigeria.

[1] (1843) 2 Hare 461

7.2 THE RULE OF *FOSS V. HARBOTTLE*

The essence of the rule is that where a wrong is done to a company, the proper plaintiff is the company and not the individual members for as long as the company is in existence, it is bound by the decision of the majority in general meeting who may ratify or confirm the very act of which these individuals are complaining against. As pertinently observed by Geoffrey Morse:[2]

> The rule is that as one would expect the proper plaintiff in an action to redress an alleged wrong to a company on the part of any one, whether director, member or outsider, to recover money or damages alleged to be due to it, is *prima facie* the company and where the alleged wrong is any irregularity which might be made binding on the company by a simple majority of members, no individual member can bring an action on it.

In plain language, the company is the proper plaintiff in an action to enforce a duty that is owed to the company by the directors or controlling members and where the breach of duty can be pardoned by an ordinary resolution of the members in general meeting, no individual member or minority member can sue.

For a clearer understanding of the rule in *Foss v. Harbottle*,[3] it is important to present the facts of the case. In brief, two shareholders of Victoria Park Company brought an action on behalf of themselves and the other shareholders in the company apart from the defendants alleging that the defendants who were five directors of the company had carried out various

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2 Chalseworth's Company Law, 11th Ed. P.435.

3 (1843) 2 Hare 461.

fraudulent and illegal transactions as a result of which the property of the company was misappropriated. The courts held that the plaintiffs were estopped from bringing an action against the defendants. The majority rule, which was propounded more than a century ago has been subject of controversy. For instance, it is stated that:

> The rule in *Foss v. Harbottle* is the deepest mystery of company law but is of great practical importance; a lawyer must be able to determine whether his client's claim will or will not be heard by the court and if the client's claim concerns the affairs of a company of which he is a member, then the lawyer must determine whether it is an exception to the rule. Unfortunately, there is disagreement over defining the rule itself, let alone its exceptions and the topic has been and will continue to be the subject of a vast amount of academic and judicial comment.[4]

The other aspect of the rule was propounded in *MacDougall v. Gardener*,[5] where some members of the company demanded for a poll at the company general meeting to enable them remove the company chairman. While denying them of the right to do so, the court held that even though the conduct of the chairman was wrong, it was a wrong done to the company for which only the company could sue or ratify. Melish L.J. said *inter alia*:

> If the thing complained of is a thing in substance, the majority of the company are entitled to do, or if something has been done irregularly, which the majority of the company are entitled to do regularly, or if something has been done illegally, which the majority of the company are entitled to do legally, there can be no use in having litigation about it, the ultimate end of which is only that a meeting has to be called, and then ultimately the majority gets its wishes.

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4 Mayson et al at 449. See also Olawoyin, op. cit. at 259; Gower, op. cit. 584.

5 (1875) 1 Ch.D. 13 (C.A) at 23

No doubt, the rule in *Foss v. Harbottle* is an embodiment of the incidence of the separate corporate personality of a company. The rule also applies to trade unions who in law have separate legal personality.[6] The rule demonstrates the futility in litigating on an irregularity that can effectively be ratified by the general meeting.

The rule in *Foss v. Harbottle* has been applied by Nigerian courts in many cases, few of which will be examined here. First in *ACB v. Haston Nig. Ltd.*,[7] the respondent a private liability company operated a current account with the Appeliants Bank at Calabar. The respondent's contention was that its account was fraudulently debited with a total sum of ₦212,700.00 by means of certain forged cheques owing to the Appeliants' negligence. The respondent further contended that as a result of the Appeliants' negligence and the consequential loss of ₦212,700.00, which it suffered in it trade, business and injury as to its credit, he has been unable to pay its creditors.

At the trial, one of the issues that came up for determination was whether the respondent's solicitor at the high court could be said to have failed to sign the respondent's amended statement of claim. The trial judge entered judgement for the respondent. The Appellant appealed to the Court of Appeal. In allowing the appeal the Appellate, court held that where a party's right to initiate an action is contested, the onus falls on a plaintiff in the action to prove his competence to commence the action. The court stated that by virtue of Section 244(1) of the CAMA, the management of a company is the

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6 See Cotter v. National Union of Seaman (1929) 2 Ch. 58. C.A.

7 (1997) 8 NWLR (Pt. 515) 110, C.A.

collective duty of the Board of Directors of the Company. No person can institute an action in the name of the company unless the company is authorised by the resolution of the Board of Directors or the resolution of the shareholders. That an action commenced on behalf of a company without such a resolution is null and void. Similarly, in *C.B.N. v. Kotoye*,[8] the respondent challenged the Central Bank of Nigeria's directive that a new Board be constituted for the company and that the annual general meeting be postponed. The court held that it was only the company that could complain since the wrongs alleged were wrongs committed against the company and not against the respondent as a member. The rule not only applies to limited liability companies but also to trade unions, incorporated associations,[9] and religious bodies as well.[10]

The rule has however been criticised as being unfair on two fronts. Wedderburm,[11] while commenting on the two problems associated with the application of the rule noted that the rule has not stated in clear terms what conducts of the directors are ratifiable and which are not. This has given rise to conflicting decisions. While in *Hogg v. Cramhorn Ltd.*,[12] the court held that where an act of a director is in good faith and in the best interest of the company but for and improper corporate purpose, it could still be ratified. And yet in *Provident International Corporation v. International Leasing*

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8 (1994) 3 NWLR (Pt. 330) 66, Per Kaglo J.C.A. at 75. See also Ejekam v. Devlom Ind. Ltd. (1998) 1 NWLR (Pt. 54) 419; Yalaju v. Anaaye v. AREC (1996) 2 NWLR (Pt. 145) 422.

9 Edwards v. Halliwell (1950) 2 All E.R. 1064.

10 Alhaji Immam Abubakar & Ors. v. Abdu Smith & Ors. (1973) 1 All N.L.R. (Pt. 1) 730; See also Mbene v. Ofili (1968) N.L.R. 293, Alhaji Agbaja & Ors. v. Chief Salami Agboluaja & Ors. (Unreported) S.C. 236/1967/20-2-70.

11 Unreformed Company Law (1969) 32 M.L.R. 563 at 564

12 (1960) Ch. 254. See also Bamford v. Bamford (1969) 2 W.L.R. 1107.

Corporation,[13] the court was of the opinion that the view that where company directors exercise powers conferred on them malafide but in the best interest of the company, it could not be ratified by the general meeting as wrong. Again, in *Ngurli Ltd. V. McCann*,[14] the court held that the ratification is ineffective once it is tantamount to fraud of the minority.

The lack of unanimity by the courts in fashioning out what acts are ratifiable and which are not is highly lamented. Ratification cannot be determined by merely looking at an act. One expects a better approach by the courts in this regard. The second problem pointed out by Wedderburn is that the rule makes the incorrect assumption that ratification, to be effective depends not on the circumstances of those ratifying a particular act but on the nature of the act itself. Thus, the motive behind the ratification of a particular act is being relegated to the background. In spite of the problems identified above, the rule has been justified on a number of grounds.

7.3 JUSTIFICATION FOR THE RULE IN *FOSS V. HARBOTTLE*

One of the reasons for the justification of the rule is the courts belief that a company should be run like a democracy and that the majority will/should be allowed to determine whether or not the company should sue. In *Cole v. R.C. Irving & Co*.,[15] a case which involved a petition for compulsory winding up of a company, Kazeem, J. (as he then was) stated that a transaction that was neither *ultra vires*, nor fraudulently and irregularly

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13 (1969) 89 W.N. (Pt. 1) (N.S.W.) 370, Per Helsham, J.
14 (1953) 90 C.L.R. 525.
15 (1971) 1 UILR 314

entered in to by a company cannot be the subject matter of a court's interference if it could be regularised by an ordinary resolution of the company general meeting. Professor Wedderburn[16] also puts it straight when he asserted that:

> Whatever the ordinary majority of the members could ratify was outside the purview of the court. Internal affairs were not for the courts to decide.

Thus, the court's attitude has been that businessmen should have absolute control over their own affairs and that any decision falling within the spectrum of the internal management of the company should be the exclusive preserve of the company itself.

The rule has also been justified on the ground that it eliminates multiplicity of suits. Where every member of the company is allowed to sue the company for every wrong done to the company, the courts will certainly be harassed by a floodgate of unending litigations. Mellish, L.J. alluded to this point elaborately in *MacDougall v. Gardener*,[17] when he said:

> Looking to the nature of these companies, looking at the way in which their articles are formed and that they are not always lawyers who attend these meetings, nothing can be more likely than that there should be something more or less irregular done at them – some directors may have been irregularly appointed, some directors as irregularly turned out, or something or other may have been done which ought not to have been done according to the proper construction of the articles. None of that gives a right to every member of the company to file a bill to have the question decided, then if there happen to be one cantankerous member, or one member who loves litigation, every of this kind will be litigated. Whereas if the bill must be filed in

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16 See Wedderburn, "Shareholder's Rights and the Rule in Foss v. Harbottle", C.L.J. (1958) at p.93.

17 (1875) 1 Ch.D. 13 at 15

> the name of the company, then, unless there is a majority who really wish litigation, the litigation will not go on. Therefore, holding that such suits must be brought in the name of the company does certainly greatly tend to stop litigation.[18]

Another ground in support of the retention of the rule is that the company, being a distinct legal person, the right of action of any wrong committed against the company should be vested in the company itself. Obviously, this reason is based on the distinct legal personality of a company, which is different from that of its members, a principle founded on the now notorious case of Salomon v. Salomon and Co. Ltd. Perhaps more serious reason for the continued justification for the rule is the unwillingness of the courts to make themselves an object of mockery since there is the likelihood of the company turning round to convene a meeting to ratify an action that had been decided in the favour of a single shareholder previously. This possibility was confirmed by the Nigerian Supreme Court in *Tika-Tore Press Ltd. V. Abina*,[19] where the Supreme Court held that the company has a distinct legal personality and where there is an alleged improper exercise of allotment of shares by the Board of Directors, only the company could complain or sue and secondly, that however wrong the director's action might be, the company shareholders can still ratify such wrongdoings in the general meeting.

The committee on the Reform of Nigerian Company Law apparently convinced of the merits of the rule recommended its codification. Thus, Section 299 of CAMA, which presently embodies the rule, states that where an

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[18] See also wedderburn, op. cit, at p. 93

[19] (1973) 4 S.C. 63.

irregularity has been committed in the course of a company's affairs or any wrong has been done to the company, only the company can sue to remedy that wrong and only the company can ratify the irregular conduct.

7.4 EXCEPTIONS TO THE RULE IN *FOSS V. HARBOTTLE*

By reason of the hardship and injustice that arise by the strict application of the rule on minority shareholders, various exception were recognised under which the rule may be excluded in its application. It was in *Edwards v. Halliwell*[20] that Jefkins L.J. first made the judicial pronouncement on the exceptions. His lordship stated four main circumstances under which the exceptions may be applied. They are:

(a) Where the act is *ultra vires*,

(b) Where the act can only be ratified by special majority,

(c) Where there is an infringement on an individual's right,

(d) Where the act complained of amounts to fraud on the majority.

A fifth exception was added by his lordship, when while stating that the rule in *Foss v. Harbottle* is not an inflexible rule, observed that the court would always relax it in the "interest of justice". While the English courts[21] were divided in the acceptability of this omnibus exception as a fifth exception; the Nigerian Supreme Court had no difficulty accepting it as such. Thus, in *Edokpolor & Co. Ltd. v. Sem-Edo Wire Ind.*,[22] the court stated that:

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20 (1950) 2 All E.R. 1064 at 1067.

21 See Heyting v. Dypont (1964) 1 W.L.R. 843 CA at 854, where Herman L.J. emphatically stated that it could amount to an additional exception; see also Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No. 2) (1982) Ch. 204 at 221

22 (1984) N.S.C.C. 553; (1984) 7 S.C. 19 at 142, Per Nnamani, J.S.C. (of blessed memory)

> This is a fifth exception requiring that an individual minority shareholder can sue where the interest of justice demand that he should be allowed to sue.

The Supreme Court's acceptance of the new fifth exception has attracted criticisms from Professor Akanki, who in his assessment of the apex Court's decision observes that:

> It has not been easy for the minority to seek redress under it (i.e. the fifth exception). Invocation of this exception is reserved for the occasion whenever and if ever it arises, when there is no juristic basis for protecting the minority against majority rule. This is why the statement … "interest of justice" … should be treated as orbiter dicta …[23]

However, Barns[24] own assessment of the same Supreme Court's decision is that:

> It firmly demonstrates that the courts are willing to decide delicate areas of company law, with or without persuasive reliance on leading English authorities. Edokpolor also follows a meaningful pattern of Supreme Court cases where it has pointedly refused to permit the rules of technicalities to triumph over the claims of justice.

It is submitted that the major problem likely to be associated with the phrase "interest of justice" is that it is a fluid and wide phrase whose ambit may not easily be determined. It could turn out to be an unruly horse. In any case, since there is no likelihood that the fifth exception will come into play until the minority shareholder is able to prove that there has been an infringement of his individual right, a situation already covered in the original

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[23] See Akanki, "Protection of Minorities in Companies" in Akanki (ed), Essays on Company Law, op. cit. at 278. See also the author's earlier commentary regarding the same rule in Akanki, "Controlling the Vagaries of Democracy in Companies" (1988) 15 N.J.C.L. 111, where he said the Supreme Court should not be taken as laying down a new exception.

[24] See Barnes K.D. Cases and Material on Nigerian Company Law, (Ile Ife, Nigeria: Obafemi Awolowo University Press Ltd. 1992) p.378.

exception, we do not think that the fifth exception has added any new substantial basis for minority shareholder action, despite its current codification under Nigerian law.[25]

Section 300 of the CAMA codifies the exceptions to the rule. It provides thus:

> Without prejudice to the rights of member under Sections 303-308 and Sections 310 to 312 of this Act or any other provisions of this Act, the court on the application of any member, may by injunction or declaration restrain the company from the following:
>
> (a) entering into any transaction which is illegal or *ultra vires*;
>
> (b) purporting to do by ordinary resolution any act which by its constitution or the Act requires to be done by special resolution;
>
> (c) any act or omission affecting individual rights as a member;
>
> (d) committing fraud on either the company or the minority shareholders where the directors fail to take appropriate action to redress the wrong done;
>
> (e) where a company meeting cannot be called in time to be of practical use in redressing a wrong to the company or to the minority shareholders; and
>
> (f) where the directors are likely to derive a benefit or have profited or benefited from their breach of duty.

The various actions, which a member of a company can institute on behalf of the company, are discussed hereunder.

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[25] See Ephraim F. Falough v. Haniel Williams & Ors. (1978) 4 FRCR 32, where the court ruled that where a plaintiff is unable to bring his action within any of the exceptions, the rule in Foss v. Harbottle will apply with full force. Per Belgore J. (as he then was).

7.5 TYPES OF MINORITY ACTION

There are a number of avenues opened to a minority shareholder to challenge a corporate wrong. We will now examine them and the conditions for their availability.

7.5.1 Derivative Action

A derivative action confers on a company the main right of action. The member acquires his own right of action indirectly from the company. Derivative action has been justified on the basis that it is a way of ensuring that certain wrongs which would have gone unredressed because the directors who perpetrated the wrong are in control of the company, are redressed by a member of the company.[26]

The right of derivative action is codified in Section 303 of the CAMA. The section states that:

(1) Subject to the provisions of subsection (2) of this section, an applicant may apply to the court for leave to bring an action in the name or on behalf of a company, or to intervene in an action to which the company is a party, for the purpose of prosecuting, defending or discontinuing the action on behalf of the company.

The conditions which an applicant is required to fulfil before the leave indicated in subsection (2) can be granted for purposes of commencing an action are that:

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[26] (1975) Q.B. 373 at 390, Per Lord Denning M. R. in Wallersteiner v. Moir (No. 2) (1975) Q.B. 373 at 390.

(a) the wrongdoers are the directors who are in control and will not take necessary action;

(b) the applicant has given reasonable notice to the directors of the company of his intention to apply to the court under subsection (1) of this section of the directors of the company do not diligently prosecute or defend or discontinue the action;

(c) the applicant is acting in good faith;

(d) it appears to be in the best interest of the company that the action be brought, prosecuted or discontinued.

As evidenced in condition (c) and (d) above, a member who wishes to rely on Section 303 must show that he has acted in good faith and in the best interest of the company. He must not have been tainted in any way with regards to a transaction which he seeks to sidetrack. This is because a derivative action is anchored principally on the principles of equity.[27] This principle was exemplified in the case of *Nurcombe v. Nurcomber*.[28] The facts of the case are both the plaintiff and the defendant were husband and wife who invested in a company known as C.H.N. Investment Co. Ltd. While the plaintiff had 34 shares in the investment company, the husband had 66 shares. The couple subsequently got divorced but still retained their respective shares in the company. Mr Nurcombe later entered into an arrangement on behalf of the company for an important property development deal. Mr Nurcombe ended up diverting the contract to another company that

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[27] See Omisade v. Akande (1987) 2 NWLR (Pt. 55) 158 Per Bello C.J.N

[28] (1951) 1 W.L.R. 370 (CA), (1985) 1 All E.R. 65.

he had some interest. Meanwhile, the wife, Mrs Nurcombe initiated a matrimonial proceeding against Mr Nurcombe. The court had to assess Mr Nurcombe's wealth. In doing so, the court took cognisance of the diverted contract which he had derived benefit from and ordered him to pay a lump sum to Mrs Nurcombe. After receiving two-thirds of the sum, she initiated a derivative action to recover for C.H.N. Investment Co. Ltd., the contractual benefit that was diverted by Mr Nurcombe. The court promptly dismissed the action. His lordship Lawton, L.J. has this to say:

> The court is entitled to look at the conduct of a plaintiff in a minority shareholders action in order to satisfy itself that he is a proper person to bring the action on behalf of the company and that the company itself will benefit. A particular plaintiff may not be a proper person because his conduct is tainted in some way which under the rules of the equity may bar relief. He may not have come with 'clean hands' or he may have been guilty of delay.

Then his lordship launched a moral attack on the plaintiff's conduct when he said:

> The plaintiff took her chance of persuading Rees J. [in the matrimonial proceeding] that she should benefit from the ill-gotten gains which the first defendant had made. She succeeded and by the time this action started she had received two-thirds of the fruits of her victory. When she received these fruits she knew how the first defendant had got them and at whose expense, she is in effect saying: 'Although I have shared with the first defendant his ill-gotten gains, I want the court to order that he should pay over to CHS his share of them plus my share so that I can have a chance of getting some more because of my status as a shareholder.' In my judgement, the court should not countenance such conduct.

What has been discovered so far from the analysis of the rule in *Foss v. Harbottle* and the exception to it as well as the statutory derivation action

entrenched under Section 303 of the CAMA is that a shareholder that sues in respect of a corporate right can do so under either any of the statutory exceptions to *Foss v. Harbottle* or the statutory derivation action provision under Section 303(2). This indicates that two types of derivative actions now exist under the CAMA. These are the *ultra vires* or "fraud on the minority" derivative suit contained under sections 39(2) and 300(d), and the section303 derivative suit. A prospective applicant wishing to avail himself of a derivative suit may have to weigh the two options before reaching a decision. A painstaking perusal of the two options would indicate that while an action under section 303(2) would require the leave of court before the derivative suit can be brought, litigating shareholders can tactfully and wisely sidetrack this requirement by simply bringing the action under any of the relevant statutory exceptions to the rule in *Foss v. Harbottle* stated under Section 300, where the wrongdoer control requirements is not even need.

It is submitted that after codifying the rule in *Foss v. Harbottle* and the exceptions to it, it was no longer necessary to introduce into our company law statute a statutory derivative action. It was an unnecessary and unhelpful duplication. The writer does not see how the two forms of action can exist side by side. In Canada for instance, after introducing the statutory derivative action, it did not find it necessary to codify the rule in *Foss v. Harbottle* and the exceptions to it. Thus, in *Shield Development Company v. Snyder*,[29] where the plaintiff sought to initiate a common law derivative action to vindicate the

[29] (1976) 3 W.W.R. 44.

breach of a corporate right and by so doing attempted to avoid the leave of court, the presiding justice, McKay, J. pertinently observed that:

> The legislation (the statutory derivative action provision) does not expressly prohibit the bringing of a common law derivative action, but in my view, such an action is prohibited by necessary implication. I am unable to see how the two remedies can exist side by side without confusion to an intolerable degree.

We humbly submit, in the light of this apparent error or oversight, on the part of our Company Law reformers, that Section 303 be deleted from the CAMA. It serves no useful purpose for the minority shareholders who my find it difficult to obtain leave of court. According to Section 650, the persons who can apply for relief pursuant to Section 303 of the CAMA are: a registered holder or a beneficial owner and a former registered holder or beneficial owner, of a security of a company.[30] Both the present and past shareholders or investors can conveniently commence a derivative action on behalf of the company.[31]

The requirement of 'fraud' and 'control' on the part of the wrongdoers remains a Herculean task or burden which a shareholder litigant must have to discharge even after fulfilling the conditions under Section 303(2). No doubt, the word fraud is an elusive concept, which is difficult to establish. So also is 'control whose exact ambit is not easily ascertained.

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30 The word security is defined under S. 650 to include shares, debenture, stock, bonds, notes (excluding promissory notes) and units under Unit Trust Scheme.

31 Such persons are: a director or an officer or a former director or officer of a company, the Corporate Affairs Commission, a creditor, or any other person allowed by court. See S. 309CAMA.

(a) **Fraud**

In *Yalaju Amaye v. A.R.E.C. Ltd*. the Nigerian Supreme Court critically examined the word 'fraud' an gave it an elaborate definition. According to his lordship,[32]

> … any act which may amount to an infraction of fair dealing, or abuse of confidence, or unconscionable conduct, or abuse of power as between a trustee and his shareholders in the management of a company, is fraud …

Again, in *Estimanco (Kilner House) Ltd. v. Greater London Council*,[33] McGarry V.G. in his carefully reasoned judgement held that:

> … the exception usually known as 'fraud' on the minority is wide enough … and if it is not, it would now be made wide … and I feel little doubt that the council has used its voting power not in order to promote the best interest of the company but in order to bring advantage to itself and disadvantage to the minority … it seems to be that the sum total represents a fraud on the minority in the sense in which fraud is used in that phrase or alternatively represents such an abuse of power as to have the same effect.

In that case, the majority, while in breach of the company's article used their superior voting power to pass a resolution, which mandated the directors to halt an action which had already been commenced on the company's name against the defendants. Apparently dissatisfied, a minority shareholder applied to court to be substituted for the plaintiff to enable it continue the action in the company's name. The court felt obliged to grant the application.

Also in *Prudential Assurance Company Ltd. Industries v. Newman Industries Ltd.*,[34] the minority shareholder instituted a derivative action to have

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32 Per Nwaemeka Agu J.S.C. at 466.
33 (1982) 1 All E.R. 92.
34 (1974) L.R. 9, CH. App. 350

an agreement entered into on behalf of the company set aside and damages for breach of fiduciary duty due to incomplete and misleading information. In its judgement, the presiding judge, Vinellot J. observed *inter alia*:

> The fraud lies in their use of their voting power not in the character of the act or transaction giving rise to the cause of action. On the other hand, if the persons against whom an action might be brought do not control the company, there is no obvious limit to the power of the majority to resolve in general meeting to condone the injury of the company or not to pursue the action whatever may have been the act or transaction giving rise to the course of action and whether fraudulent or not.

It appears that the courts, in considering the meaning of 'fraud' have often been swayed by the desire to do justice in appropriate cases. For instance, in the general rule of *Foss v. Harbottle*,[35] it self Wigram said that:

> … if a case should arise of injury to a corporation by some of its members for which no adequate remedy remained except that of a suit by individual corporations in their private character … I cannot but think … the claims of justice would be found superior to any difficulties arising out of technical rules respecting the mode in which corporations are required to sue.

And in *Edwards v. Halliwell*,[36] Jenkins J. in a similar vein said:

> … of the exception that it should be showed that the rule is not an inflexible rule and that it will be relaxed where necessary in the interest of justice.

Professor Schumittoff,[37] has also observed that the wide and elastic scope which 'fraud' has assumed in company law parlance makes it intertwined with the interest of justice exception so much so that it is no longer of any practical relevance to continue to demarcate the two in conceptual terms.

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35 Supra.

36 (1950) 2 All E.R. 1064.

37 See also Onisade v. Akande, Supra. See Mayson et al. op. cit. at 463.

Professor Akanki[38] apparently aligning himself with the above view observed that in the case of Nigeria, Section 300(f) of the CAMA is merely an elongation of the fraud requirement entrenched in Section 300(d), while Section 300(e) merely codifies the so-called interest of justice requirement – the fifth exception in the rule in *Foss v. Harbottle***.**

What can be garnered from the preceding well thought out analysis is that the inclusion of a fifth exception in the interest of justice, is a surplusage which should be deleted from our company law. Otherwise, the circumstances under which it could come into application should be clearly stated in the form of an amendment.[39]

(b) **Control**

No less problematic is the issue of 'control' by wrongdoers. In *Prudential Assurance Co. Ltd. v. Newman Ind. Ltd***.** (No. 2), Vinelott J. made it clear that the term 'control' has acquired a new connotation well beyond 'voting control' and that it also includes those who did not actually possess voting control but who by their position in the company establishment or set up have the capability of manipulating their position to ensure that the minority are prevented to bring a claim against the majority.[40]

It is not always easy on the face of it to demarcate the issue of wrongdoers in control and perpetrating fraud on the minority. They both

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38 See Akanki, 'Essays on Company Law', op. cit. at 227.

39 Barns K. D. Cases and Materials on Nigerian Company Law, Supra at p. 381. See also Osunbor, 'A Critical Appraisal of the Interest of Justice', as an exception to the rule in Foss v. Harbottle (1987), 361 CL 91.

40 See also Orojo (3rd Ed.) op. cit. at p. 356.

appear to be tied to the same apron strings. In the Prudential's case,[41] for example, Vinelott J. observed that:

> If the control is being exercised so as to deprive the company of the power to sue for money due to it by way of damages or compensation this would seem to be a fraud on the minority.[42]

It does appear that where control is exercised by directors to frustrate the company from initiating proceedings against wrongdoer directors that would be sufficient to constitute fraud on the minorities. As stated before, fraud includes an abuse of power which enriches the tortfeasor and amounts to a breach of fiduciary duty.

Another enormous condition which a minority shareholder may likely face in his attempt to initiate an action on behalf of the company is the requirement that the wrong in question must be incapable of ratification at the general meeting. Though it appears simplistic that a fraudulent act is incapable of ratification, the difficulty however lies in the fact that as the recent English case of *Smith v. Croft (No. 2)*,[43] would appear to indicate a fraudulent act may be capable of ratification by the majority who are in control of the company. In that case, Knox J. asserted forcefully and regrettably that:

> The ultimate question has to be … is the plaintiff being improperly prevented from bringing these proceedings on behalf of the company? If it is an … independent organ [i.e. the majority shareholders] that is preventing the plaintiff from prosecuting the action, he is not improperly but properly prevented and so the answer to the question is 'NO'.

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41 Supra at 850.
42 See Orojo, op. cit. at p. 356.
43 (1988) Ch. 185.

This case appears to follow a characteristic pattern of recent English decisions, which has no sympathy to the minority shareholders. First, it was in Prudential Assurance case,[44] where the Court of Appeal in trampling upon Vinelott's test that a minority shareholders action may lie against a company in the interest of justice, said without mincing words that: "We are not convinced that this is a practical test."[45]

Professor Gower in his analysis of the decision in *Smith v. Croft***,** said that Knox J's decision was a loud pronouncement of the fact that despite the establishment of "fraud" and "wrongdoer control" a derivative action may still not be available to an aggrieved minority shareholder once an independent organ of a company has ruled against it. It is submitted that an independent organ may be the company Board of Directors, which may exercise its power without reference to the general meeting of the company. If this view is accepted, it then means that in Nigeria, the statutory derivative action is a barren means of redressing corporate wrong. But happily there are other avenues for redressing corporate wrongs. In the light of the foregoing, it is firmly recommended that the Nigerian courts should not waver in their determination in providing succour to minority shareholder when the need arises. This they can do by standing firmly by the decision in *Edwards v. Halliwell***,** which says that a fraudulent act is incapable of ratification even by a special majority.

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44 (1882) 2 W.L.R. 31 at p. 47. See also Megarry J. in Estimanco (Kilner) Ltd. v. Greater London Council (1982) 1 W.L.R. 2.

45 See Gower, Principles of Modern Company Law (5th Ed.) op. cit. 659.

One however welcomes the provision of Section 308, which allows a minority shareholder to be paid an interim cost before an action is concluded. This certainly will ensure that not so rich shareholders will not be debarred from instituting genuine actions aimed at redressing corporate wrongs.[46]

A derivative action once instituted, can neither be stayed or stopped by the company except the leave of court is obtained.[47] It can only be commenced against a company that is solvent. Thus, once a company is in liquidation, only the liquidator can decide whether to sue or not, since the company's power reside with the liquidator from that point.

7.5.2 Personal Action

A member as well as shareholder of a company can commence a personal action against a company for purposes of seeking for an infringement against his membership right. A member instituting a personal action can do so in his own name. The member is the plaintiff while the company is the defendant in the suit. A member's right to commence proceedings against the company is presently codified under Section 300(c) of the CAMA.

The purpose of a member's right of personal action is well stated in *Pender v. Lushington*.[48] In the words of Jessel M.R.:

> This is an action by Mr Pender for himself. He is a member of the company and whether he votes with the majority or the minority, he is entitled to have his votes recorded … an individual

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46 S. 308 appears to have codified the decision in Wallersteiner v. Moir (No. 2) (1975) Q.B. 373, where the court recognized that since a derivative action is in the companies interest, it is equitable to indemnify the company for expenses incurred from the company's fund, whether the action is successful or not.

47 S. 306 of the CAMA.

48 (1877) 6 Ch. 70 at 80- 81.

> right in respect of which he has a right to sue. This has nothing to do with the question … raised in *Foss v. Harbottle* and that line of cases. He has a right to say, whether I vote in the majority or minority, you shall record my vote as that is a right of property belonging to my interest in this company, and if you refuse to record my vote I will institute legal proceedings against you to compel you.

The facts of the case were that a shareholder in a company split his shares among nominees. At a meeting of the company, a resolution was proposed by him and this would have been carried with the assistance of the votes of the nominees. But the chairman declared that the motion was lost. The plaintiff then brought an action on behalf of himself, the other shareholders and the company seeking for an injunction to restrain the directors from giving effect to the Chairman's ruling. The court held that the plaintiff was entitled to succeed not just as a plaintiff in a representative action but also as an individual plaintiff since he is a member of the company who is entitled to have his votes recorded. Once he is prevented from exercising this right, he is at liberty to sue. Also in *CBN v. Katoye*,[49] where the main issue at stake was whether having regard to the nature and circumstances of the case the respondent has the necessary *locus standi* to maintain his claim, the court held that an individual member of a company who has suffered an injury is entitled to the provision of Section 6(6) of the 1979 Constitution to seek redress despite the rule in *Foss v. Harbottle*.

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[49] (1994) 2 NWLR (Pt. 580) 22. See also Muzango v. Mozingine (1996) E.A. 390; National Stores Workers Union v. Udo & Others (1971) 2 NCLR 412.

The facts of the case were that the respondent, a shareholder of the company filed a suit at the Federal High Court challenging the directive of the Minister of Finance, which mandated the Central Bank to issue a directive to the third defendant bank asking it to reduce the shareholding of the plaintiff and allocate same to other Nigerians. The plaintiff challenged this directive and the reallocation of his shares which he said affected his interest personally. In its lucid judgement, the court stated thus:

> The rule *[Foss v. Harbottle]* is not total and is subject to certain exceptions. One of such exception which may appear to be relevant here is that it would not apply to an action brought to protect the invasion of a personal right of an individual member. In such a situation, the wrong ceases to be wrong to the company … and so it goes beyond the authority of the company … or the majority of its members to seek redress in the court.[50]

Again, in *Edokpolor & Co. Ltd. v. Sem-Edo Wire Ind. Ltd.*[51] the court further re-emphasised the exception that where the personal right of a plaintiff is infringed, the aggrieved plaintiff can commence a personal right of action. In that case the appellant complained that the 1st respondent allotted it 40% of the companies shares. While the shares were still in the appellants name, the 1st respondent purportedly allotted out of it 4% to the 2nd respondent and another 3½% to the 3rd respondent respectively. The contention of the respondents was that since the shares was the property of the company, the appellant lacked the stands to complain as regards the manner of allotment.

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50 See also Pennington, op. cit. p. 587; Okoye v. Santilli (1990) 2 NWLR (Pt. 131) 172.

51 Supra.

The Supreme Court held that the appellant was right in challenging the allotment.

Explaining the true essence of personal action, Professor Henn[52] observed that:

> … the direct or individual shareholder action involves the enforcement by a shareholder of a cause of action belonging to such shareholder on the basis of his membership contract against the corporation and possibly others, being brought by the shareholder either individually or on behalf of himself and all other shareholders similarly situated.

Unlike a derivative action where the company is only a nominal defendant since the benefit of the proceedings sees to the company, in a personal action, the company is a real defendant while successful outcome of the proceedings will be to the benefit of the plaintiff shareholder.

7.5.3 Representative Action

This form of action arises where shareholders or a group of shareholders would allege that their personal rights have been violated. Professor Pennington[53] states the essence of a representative action thus:

> The plaintiff in such an action does not sue in his own right alone, but on behalf of himself and all his fellow members other than these, if any, against whom relief is sought.

Basically, this form of action is appropriate where the persons challenging a particular corporate act share a common interest or a common grievance, since in the end, the result is that the relief sought would in its very nature be one that would benefit all those whom the plaintiff is

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52 See Henn H. Law of Corporation, 2nd Ed. (1970) p.775.

53 Pennington, op. cit. p.589.

representative.[54] In a representative action, the essence of joining the company as a defendant is to ensure that he is bound by the judgement.

In a situation where a representative action is brought not only against the company but against other persons as well in order to enforce a personal right, the company will be joined as a co-defendant. This will put the company in a position where it could be bound by the judgement as well as enforcing any order against the substantive defendants.[55] Representative action is provided for under Section 301(2) of the CAMA. Essentially, it provides that a member may institute a representative action on behalf of himself as well as other persons in order to enforce a right peculiar and due to them.

Prominently, some of the acts which a member is likely to challenge through the instrumentality of a representative action are embedded under Section 300(a) and (b) respectively. Under Section 300(a) a member or members may restrain the company from engaging in an *ultra vires* or illegal act by obtaining an injunction or a declaration. This provision constitutes an adequate safeguard for prospective investors at least by reassuring them that errant directors would not be allowed to fiddle with investors' funds and go free.[56]

It is interesting to note that the potential of Section 300(a) is not likely to be affected by the abolition of the *ultra vires* doctrine in Nigeria. While

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54 See Otuagor Ogamioba and Others v. Chief D.O. Oghene & Others (1961) All N.L.R. 441.

55 Pennington, op. cit. at 588.

56 See Yalaju Amaye v. AREC Ltd. Supra. See Gower (5th Ed.) op. cit. at 664.

commenting on the provision of Section 35(2) of the English Companies Act of 1989 (similar to S. 300(a) of the CAMA), Professor Gower noted that:

> Despite the abolition of the strict *ultra vires* rule by the 1989 Act, this seems to be unaffected as the new Section 33(2) expressly entitles a member to bring proceedings to restrain an act which but for Section 35(1) would be *ultra vires*.

But the point must be made that the potential of Section 300(a) is narrowed down to cases where the directorial act is only at its executory stage. The Section would not apply where the act has already been engaged in, executed or completed. Section 300(a) is essentially a prohibitive relief, and nothing more.[57]

Secondly, under Section 300(b) of the CAMA, a member is also in a position to restrain the company by injunction or declaration when the company purports to do by ordinary resolution of an act which can only be done by special resolution having regard to the company's memorandum and articles of association. This provision constitutes an important protective provision for the preservation of companies' constitution in particular and the provisions of the CAMA in general.

Apparently restating the fact that vigilant and well meaning members or shareholders of the company should not be allowed to labour in vain, Section 301(3) of the CAMA empowers the court to award costs to members or

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[57] See S. 39(4) of the CAMA; where also the act has already been engaged in Ss. 300 and 303(1), (2) would be more helpful for the litigating shareholder or member. But the obstacle of proving 'fraud' or control must be surmounted.

shareholders who dutifully restrain or attempt to restrain personal wrong meted out on individual members of the company.[58]

7.6 THE REMEDY OF PROTECTION AGAINST UNFAIRLY PREJUDICIAL AND OPPRESSIVE CONDUCT

This remedy constitutes another avenue for challenging management conduct on the ground that the affairs of the company are being conducted in an illegal or oppressive manner. In the early days, it was believed that the only remedy available was the winding up of a company on just and equitable ground.[59] This misconception arose because the courts were of the view that joint stock companies shared the same attributes with businesses ran under the umbrella of partnership and whose existence derived from the consensus of the members.[60] But since a company differs significantly from partnership, the remedy of winding up became highly inadequate and unattractive to prospective investors who had eyes on company management, but who felt that the existing legal regime lacked the required mechanism for the protection of investors.

In Nigeria, what was contemplated as a viable solution or remedy was provided under Section 201[61] of the 1968 Companies Act by which special provisions were made for alternative remedy to wind up the company. The relief provided members with the remedy of relief against oppression once a complaint wais lodged to the effect that the affairs of the company were being

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58 See also Wallersteiner v. Moir (1975) Q.B. 373, where the House of Lords laid down this all-important equitable principle.

59 Gower (5th Ed.) op. cit. 662.

60 Thus, where the basic element of trust or harmony is destroyed, the alternative option was to wind up the business.

61 This is the same with S. 210 of the UK Company Act 1948.

conducted in a manner oppressive to some parts of the members including the member lodging the complaint.

The provision was found inadequate in a number of respects. First, its scope was severely limited in that only a member qua member could present the petition under Section 201.[62] Secondly, the provision was inextricably linked with liquidation in that an order cannot be made unless the facts would justify the making of a winding up order on the ground that it was just and equitable that the company be wound up. Thirdly, the oppression must be continuous and not an isolated act. The result was that there were inconsequential numbers of successful petitions.[63]

In view of these shortcomings, the CAMA, by virtue of Sections 310-313 came in to widen considerably the scope of the relief and persons who may now petition. For purpose of clarity, the other differences between the 1968 Act and the CAMA 1990 are that:

(1) the addition of unfairly prejudicial conduct to oppression;

(2) the relief for conduct that is unfairly discriminatory;

(3) the expansion of the category of persons who may petition;

(4) the removal of the link with winding up;

(5) the possibility of relief for threatened acts.[64]

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62 See for instance, Ebrahimi v. Westbourne Galleries (1973) AC 360; Re Jeremyn Street Turkish Bath Ltd. (1976) 3 All E.R. 57; Ogunade v. Mobil Films (WA) Ltd. (1976) 2 FRCR 10.

63 Two known successful suits under the corresponding English provision of S. 210 of the 1948 Act are: Re H. R. Harmer Ltd. (1958) 3 All E.R. 689 and Scottish Co-operative Wholesale Society v. Meyer (1959) A.C. See also Gower, op. cit. at 665.

64 See also Barns, Cases and Materials on Company Law, op. cit. at 392. But the author appear to have made a slip when he said the unfairly prejudicial conduct as a new requirement under S.

Section 311(1) of the CAMA provides the basis for the remedy of unfairly prejudicial and oppressive conduct. It says:

> An application for relief on the ground that the affairs of the company are being conducted in an illegal or oppressive manner may be made to the court by petition.

While under subsection 2(a), it is provided that a member of the company may apply to court for relief on the following grounds:

(1) that the affairs of the company are being conducted in a manner that is oppressive or unfairly prejudicial to, or unfairly discriminatory against a member or the member as a whole; or

(2) that an act or omission or a proposed act or omission, by or on behalf of the company or a resolution or a proposed resolution or a class of members, was or would be oppressive or unfairly discriminatory against, a member or members or was or would be in a manner which is in disregard of the interest of a member or members as a whole.

This provision which is quite wide and accommodates new avenues for minority shareholders relief is bisected by a death of Nigerian cases, but a combined English authorities as well as opinion of learned writers have come in handy to do justice to this aspect of the subject matter especially the special emphasise placed on key words which offer insight into the actual scope of the new provisions.

331(1) substituted the former relief of oppression under the 1968 Act. It was an addition and not substitution.

7.6.1 Oppression or Unfair Prejudice

Under the 1968 Companies Act while attempting to define the term in *Ogunade v. Mobil Films (W.A) Ltd*.,[65] Karibi-Whyte J. (as he then was) said:

> The oppression or fraudulent conduct of the majority must be harsh, burdensome and wrongful … and must represent a consistent pattern of conduct intentionally directed at the oppressed minority over a period of time … Thus negligence in conducting the affairs of the company, or lack of business ability or inefficiency will not be sufficient.

Apparently, his lordship definition was an affirmation of the earlier definition provided in *Scottish Co-operative Wholesale Society v. Meyer*,[66] where the court equated the word oppressive with burdensome, harsh and wrongful.

It does appear from these definitions that an oppressive act must contain the vital ingredient of premeditation to cause economic lose or injury to the plaintiff. Thus in *Re Five Minutes Car Wash Service Ltd*.[67] the court held that an unwise, inefficient and careless mismanagement resulting to loss which the majority had acquiesced did not tantamount to oppression because it was not unfair or unscrupulous or lacking in probity.

While assessing the efficacy of Section 201 of the 1948 English Companies Act (equivalent to S. 311 of the 1990 Act), professor Gower observed that the section has been:

> … an invaluable weapon in the shareholders armoury and the paucity of decided cases is merely due to the fact that the

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65 (1976) 2 FRCR 101.
66 (1959) A.C. 324.
67 (1996) All E.R. 242.

> threatened invocation of this section has often caused oppression to cease.[68]

But it is equally true that because of the extremely strict approach in the construction of the provision, it ceased to provide the requisite succour to members and investors desirous of challenging management decisions.[69] But following the reform of the Nigerian Company Law, leading to the addition of the term "unfairly prejudicial" to oppression to the CAMA 1990, the word appears to have now acquired an elastic connotation. For instance, in *Re Company*,[70] Harman J. observed that:

> The words "in a manner which is unfairly prejudicial" … connote that there must be harm or prejudice and that such harm must be unfair harm.

Implicit in his lordship observation is the fact that the managerial conduct in question must be unfair harm. Thus where the harm, examined from corporate perspective appears as fair, or fair dealing, that would not be unfairly prejudicial. Even from a quasi partnership viewpoint, Professor Gower,[71] notes that not every prejudicial act or omission will be regarded as unfair prejudice. But the obvious shortcoming in the foregoing judicial and academic definitions was noticed by Hoffman J. in Re A Company No 11869 of 1985,[72] when he cautioned that the meaning of "unfair" prejudice should not

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68 See final of the Commission of Enquiry report into the Working and Administration of the Company Law of Ghana (1961) p. 161.

69 See Akanki, op. cit. at 285-286.

70 (1987) B.L.C. 141.

71 See Gower (5th ed) op. cit. at 666.

72 See Diligenti v. R.W.M.D. Operations Kelocona Ltd. (1976) 1 B.C.L.C. 36 at 46, where his Lordship Fulton J. examined the meaning from the perspective of "unjust and inequitable conduct".

be ascribed a narrow meaning but be widened depending on the circumstances of each case. According to his lordship:

> Unfairness is a familiar concept employed in ordinary speech often by way of contrast to infringement of legal right. It was intended to confer a very wide jurisdiction upon the court and I think it would be wrong to restrict that jurisdiction by adding any gloss to the ordinary meaning of the word.[73]

Not too long ago, Nourse J. in *Re R A Noble & Sons (Clothing) Ltd*.[74] narrowed the ambit of a similar provision under the English Act, when he pointed out that:

(1) all cases successful under Section 210 of 1948 Act would fall within section 459 and Section 459 could include cases which would have not succeeded under Section210;

(2) it would be sufficient for a member to show that the value of his shareholding had been seriously diminished or at least seriously jeopardised by a course of conduct by those who had de facto control of the company;

(3) the test of unfairness is objective – there is no need to show any conscious knowledge on the part of the controller that it was unfair, or any other evidence of bad faith. It would be a question of whether a reasonable bystander would regard it as unfairly prejudicial.

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73 See also Re A Company No 007623 of 1984 (1986) B.C.L.C. 362, where Hoffman J. ascribed a restricted meaning to the term "unfairness" by declining to apply the test where there was a remedy for the petitioner in the articles. This was however set aside by the Court of Appeal in the later case of Verdi v. Abby Leisure Ltd. (1990) B.C.L.R. 342 CA.

74 (1983) B.C.L.R. 273

It is thus clear that the introduction of the additional term "unfairly prejudicial" to oppression is designed to whittle down or eliminate the limitation inherent in term oppression. Thus, its spectrum is wider than oppression. It would appear that negligent mismanagement causing economic loss to a member or an investor in a company may be sufficient to ground a cause of action under Section 311(2) (a) of the CAMA 1990. [75] We urge the Nigerian courts, when confronted with the question whether a directorial conduct is unfairly prejudicial, to give it a flexible interpretation in order to do justice in appropriate cases. Indeed, such a judicial posture would no doubt accord with the spirit of the CAMA itself.

7.6.2 The Remedy of Protection Against Unfair Discrimination

Unfair discrimination provides another ground upon which a member can challenge management action in company law. Thus a member may allege that the affairs of a company are being conducted in a manner which is "unfairly discriminatory" to his interest. There has however been diversity of opinions as to the exact import of the phrase. According to Shapira:[76]

> Discrimination is specifically mentioned, so it is clear that unfair prejudice need not necessarily involve an element of discrimination.

But Akanki,[77] while agreeing with the above view has noted that:

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75 Pavilides v. Jensons (1956) ch.565, where negligent mismanagement failed to ground a cause of action derivatively. But this may no longer be the case in view of recent development. See also Ogunade v. Mobil Films, Supra, where mismanagement failed under 1968 Act but would possibly have succeeded Under the CAMA1990.

76 See G, Shapira, "Minority shareholders Protection – Recent Development" (1983) 10 N.Z.U.L.R. 134.

77 See Akanki, Essays on Company Law, op. cit. p.292.

> This is not to suggest that each phrase has to be treated in isolation as one may amplify the other.

But if the opinion expressed by the New Zealand Court of Appeal in *Thomas v. N.W. Thomas Ltd.*[78] is anything to go by, it would seem that both expressions are coterminous and as Akanki suggested, it may amplify the other. The court, while considering a similar provision in New Zealand observed that:

> These expressions overlap, each in a sense helps to explain the other, and read together, they reflect the underlying concern of the subsection that conduct which is unjustly detrimental to any member of the company, whatever form it takes and whether it adversely affects all member alike or discriminates against some only is a legitimate foundation for complaint.[79]

What can possibly be gleaned from the above analysis is that unfair prejudice has a wider outlook than unfair discrimination. But what was intended to be achieved by the expression 'unfair discrimination' is not easy to decipher since in our humble opinion unfair prejudice will certainly encompass "… every conduct that is oppressive, unfairly discriminatory…"[80] to minority members of a company. In *Greenhalgh v. Arderne Cinema Ltd.*[81] a discriminatory act was defined as an act which while conferring on the majority shareholders an advantage also denies the minority shareholders that same advantage. No doubt, this definition only bears the testimony that a discriminatory act is part and parcel of a conduct that is unfairly prejudicial.

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78 (1984) 1 N.Z.L.R. (Pt. 5) 686.

79 See also Professor Okonkwo, Supra at p. 24, who appears to also suggest that the terms have the same connotation.

80 See Okonkwo, Supra at p. 24.

81 (1951) 1 Ch. 286 at 291.

We therefore submit that the expression should be deleted from the CAMA. The futility and impracticality of such a provision was ably demonstrated by the refusal of the English Parliament to see the attraction of including the same phrase in a similar provision contained under the English Act.[82]

7.7 THE REMEDY OF PROTECTION AGAINST DISREGARD OF INTERESTS

Before, it was believed that to be able to establish unfair prejudice, a member must establish that his right under the relevant articles of association has been infringed. The obvious explanation for such reasoning was that the interest of a member was thought to be inextricably linked with his membership right expressed in the memorandum and articles of association in addition to other's regulated and protected by the CAMA. But in *Ebrahimi v. Westbourne Galleries Ltd*,[83] Lord Wilberforce recognised that a member of a company has other rights apart from those contained in the articles. These he said are based on wider equitable considerations encompassing expectations and obligations generally.

The implication of this decision in company law is ably demonstrated in the later case of *Re A Company No. 00477 of 1986*[84] where the court held that a member of a company who had invested his capital in the business of a company on the premises that he would participate in the company management has a genuine expectation that he would continue to be a director of the company so that where he is improperly removed, by the Board

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82 See S. 459 UK CA 1985.
83 (1973) B.C.L.R. 342 CA.
84 (1986) B.C.L.R. 376.

of Directors, that act of removal would be regarded as unfairly prejudicial to him.[85]

A member of a company would not have his cause of action foreclosed despite the fact that the interest disregarded by the management whether legal or equitable is *bonafide* and in the best interest of the company. Commenting on the positive strength of the expression "disregard of interest" Akanki notes that:

> The new provision appears to be well designed … by allowing the minority to challenge company controllers not only on grounds of oppression, unfair prejudice or discrimination, but also on the ground that their conduct amounts to disregard of members' interest. This ground of relief is very unusual and may produce far-reaching consequences. In the past, the majority could get away if the conduct complained of was "*bonafide* and in the interest of the company as a whole", even if it adversely affected the interest of the minority. But by this new provision, it seems the effect of such actions on the minority can no longer be ignored.

Thus, under the new position under the CAMA, a wide range of corporate and directorial abuses hitherto disallowed[86] would now seem actionable by minority shareholders. A case in point which personifies the old order is *Re Five Minute Cash, Wash Service Ltd*[87] where the majority shareholders refused to act in the face of unprofessional, reckless, careless, and inefficient conduct of the company Chairman and Managing Director causing untold financial losses. Sadly enough, the court, obviously influenced

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85 See also Re A Company (1986) B.C.L.R. 382, where the court allowed a petition where the director's statement contained inaccurate statements recommending acceptance of a bid from another company owed by them.

86 See Re Carrington v. Yalla PLC (1983) 1 B.C.L.R. 98; Re Blue Arrow PLC (1987) B.C.L.R. 585.

87 (1966) 1 W.L.R. 745.

by the twin doctrines of non-interference in the internal affairs of company, as well as the requirement that the conduct complained of must affect only the interest of some part of the members including the plaintiff (mismanagement, being a conduct that affects all the members of the company) refused to intervene.

As earlier noted, decisions such as those analysed above, would now seem unlikely. But in spite of the salutary and commending posture adopted by the CAMA in its departure from the English attitude, the question is, what is the potential of the new CAMA provision on "disregard of interest" of the minorities? The response to this is that apart from the fact that it might unleash on the company a deluge of vexatious actions by minority shareholders, it does not create any new and substantial avenue for minority shareholders to challenge managerial abuses by majority shareholders. It seems indisputable that any grievance capable of being brought under the expression disregard of interest is equally capable of being regulated under the expression "unfairly prejudicial". Like we submitted in respect of "unfair discrimination" the phrase disregard of interest should be struck off from the CAMA to make the provision more apt.

7.8 PERSONS WHO CAN SUE

Section 310(1) of the CAMA provides that an application to the court in form of a petition may be made by:

(a) a member;

(b) a director or officer or former director or officer of the company;

(c) a creditor;

(d) the commission; or

(e) any other person who, in the discretion of the court, is the proper person to make the application under Section 311.

Any member of a company can petition provided his interest is affected. A member of a company includes the personal representative of a deceased member and any person to whom the shares have been transferred or transmitted by operation of law.

The elastic definition of the term member under the CAMA has appreciably removed the obstacle, which the requirement of *locus standi* would have engendered. Thus, a personal representative of a deceased person may not now be required to register with the company, the same applies to all those persons whose shares have been transmitted by operation of law. The rights of such persons to initiate proceedings cannot be foreclosed by the directors by refusing to include their names in the register of members. This is in view of the fact that Section 310(a) has now conferred expressly membership rights on such persons.

However, in the case of transfer of shares, a transferee must ascertain the fact that proper instrument of transfer is executed and delivered to him or to the company by the transferor in respect of the shares. Merely relying on an agreement to transfer would serve no useful purpose.[88] In *Re Quickdome*,[89]

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88 Mayson et al, op. cit. at 468.

89 (1888) 4 BBC 296.

a shareholder failed in his petition on the ground that the instrument of transfer did not contain any name. But where the issue of membership is resolved, a petitioner who sues on that platform will succeed despite the fact that the number of shares in his name is inconsequential. In *Re Garrage Associate Ltd*,[90] a member who had only one share to his name was allowed to petition the company for improper allotment of 790 shares out of total of 800 shares.

Section 310(1)(b) also permits a member with dual capacity to sue in appropriate cases. These are members who are also directors of the company. Generally, any person qualified under the CAMA may commence action not only for past or prejudicial conduct but for a proposed conduct as well. Thus, in *Re Kenyon Swanber Ltd*.[91] the court held that a member could initiate action in respect of a proposed act which if executed will be injurious to him. In *Re Whyte Petitioner*,[92] the court held that the fact that immediate threat for the proposed act was withdrawn before the matter was heard by the court is no defence. What is important is that the threat was in existence at the time the petition was filed.

7.9 COURTS POWER TO MAKE ORDERS

The nature of the orders which the court can make are well spelt out under Section 312 of the CAMA. While Section 312(1) gives the court

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90 (1884) 1 W.L.R. 35.
91 (1887) B.C.I.C. 514.
92 (1884) S.L.T. 330.

considerable discretion to make any order it considers appropriate, subsection (2) tabulates the variety of orders which the court can make.

Whereas under the 1968 Act, a member had to prove that his complaint would justify a winding up order[93] before the court could grant the remedy of winding up, this is no longer a requirement under the CAMA 1990.[94] Thus, the CAMA has now made a winding up a separate remedy under Section 312(2) (a).

Apart from a winding up order, the court can also make an order pursuant to para (b) for regulating the conduct of the affairs of the company in future. Under paragraph (c) and (d), the court is further empowered to make appropriate orders for purposes of ordering the purchase of the shares of the members by other members or by the company. In *S.C.W.S. v. Meyer*,[95] the court held that the shares of an aggrieved shareholder should be bought over by the controlling wrongdoers at a price which the court determined. Similarly, in *Re Harmer*,[96] the court effectively ordered that a wrongdoer director be removed but that the director in question be retained as the company's expert adviser at fixed salary. Obviously, the above two cases are clear demonstration of the judicious exercise of the wide discretion which the court had under the old Act.

The court also has power under paragraph (e) to direct the company to institute, prosecute, defend or discontinue proceedings that are pending in the

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93 Ibrahim v. Westbourne Galleries, Supra.
94 S. 312(2) (a).
95 (1959) A.C. 324.
96 Supra.

company's name or on its behalf. This provision is a welcome relief for the company members and investors alike. Indeed, the provision contains the most effective remedy for the minority shareholders. It is the best antidote to the action inhibiting rule of *Foss v. Harbottle*. Thus, under the provision, a minority shareholder can apply to court to sue the wrongdoer majority who are reluctant to do so. The provision now relegates to the background the provision of Section 303 of the CAMA. In *Re A Company No. 005287 of 1985*,[97] a husband and wife and their four daughters initially held the shares of a private family. In 1982, they jointly transferred to the husband sufficient shares belonging to one of their daughters 'H'. 'H' according to the other three daughters mismanaged the company in breach of his fiduciary duties contrary to their agreement. The three challenged the allotment under Section 459 of the 1985 English Companies Act. In the petition, they claimed *inter alia* an account and purchase of their shares at a price to be fixed by the court. It was however found out that at the time the petition was being filed in court, 'H' had disposed off her shares to a Gibratarian company and the assets and undertaking of the family company had been sold and the records of the sale could not be traced. At the trial, it was canvassed on "H" behalf that the only remedy capable of being granted against her was in the realm of a derivative action. The court[98] after painstaking evaluation of the submissions of the parties, held that Section 461(1)[99] (in pari material with S. 312(1) of the

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97 (1982) 1 W.R.L. 281, cited with approval by Gower (5th ed.) op. cit. at 669.

98 Per Hoffman J.

99 UK CA 1985.

CAMA) gives the court considerable discretion to grant such order as is proper for it to make in terms of relief pertaining to the matters complained of by the aggrieved party. The court therefore allowed the petition to proceed against both "H" and the Gribratarian company as a co-defendant.

As said earlier, Section 312(1)(e) is a major gain to minority shareholders. But as a complementary provision, it is suggested that like a derivatives action there should be provision in the CAMA to reimburse minority litigants who put upon themselves the burden of challenging corporate wrongs, especially if considered from the angle that the company is the most prominent beneficiary of this type of action.

The court under paragraph (f) has power to vary or set aside a transaction or contracts in which the company is a party and compensate a company or other party to the contract or transaction.

We think the subsection remains a better deal for minority shareholders unlike Section 39(4), (5) which regulates executory contracts only. But the problem with Section 312(1)(f) will have to be that of interpretation. If the courts are pragmatic to widen the scope of the provision to embarrass *ultra vires* transactions, it would have commendably remedied the obvious imperfection in Section 39(4) (5) and empowered itself to set aside such transactions.

Paragraph (G) also empowers the court to direct the Corporate Affairs Commission to investigate the affairs of the company, pursuant to an application brought before the court by either a member or the commission itself. The

purpose of investigating the conduct of the directors is to bare open any irregular dealings of such directors that are prejudicial to investors' interest.

Section 312(2)(h) provides for the appointment of a receiver or a manager of the company by the court, while subsection (i) and (j) confer on the court the power to grant the orders of prohibitive and mandatory injunctions respectively. The essence of these equitable remedies is to ask the wrongdoer majority to either carry out some specific acts or refrain from doing certain acts considered prejudicial to minority members interest.

In view of the many avenues opened to minority shareholders to challenge management for corporate abuses, it is undeniable that these avenues may have the unpleasant effect of encouraging frivolous and vexations suits on companies. To forestall such abuses, it would be necessary if procedural rules are put in place with the sole aim of guiding the courts and prospective litigants. This was the protective mechanism adopted in the United Kingdom[100] in the case of the remedy of unfair prejudice.

7.10 WINDING UP

Winding up connotes a process that leads to the extinction of the existence of a company. Here, it is intended only to discuss windings up to the extent that it confers a remedy on a member despite the action limiting rule in *Foss v. Harbottle***.**

Apart from Section 312(2)(a) which confers on the court the power of winding up a company, Section 408(e) also states that a court may wind up a company if it considers it just and equitable to do so. In *Ebrahimi v. West*

[100] See Companies (Unfair Prejudice Application) Proceeding Rules 1986.

Bourne Gallaries Ltd,[101] Lord Wilberforce lamenting the impracticability of stating exhaustively the circumstances that would deem it just and equitable to wind up a company said:

> "It would be impossible and wholly undesirable to define the circumstances in which these considerations may arise."

Notwithstanding, his lordship's lamentation, he proffered some guides as follows:

> The superimposition of equitable consideration requires something more than typically may include one or probably more of the following elements:
>
> (i) an association formed or continued on the basis of personal relationship involving mutual confidence;
> (ii) an agreement or undertaking that all or some (for there may be sleeping partners) of the shareholders shall participate in the conduct of the business;
> (iii) restriction upon the transfer of the members' interest in the company so that if confidence is lost or one member is removed from management, he cannot take out his shares and go elsewhere.

Similarly, in the *Scottish case of Bird v. Lees*,[102] the Lord President in stating the circumstances that amounts to just and equitable ground said:

> I have no intention of attempting a definition of the circumstances which amount to a 'just and equitable cause'. But I think, it may be this: a shareholder puts his money into a company on certain conditions. The first of them is that the business in which he invests shall be limited to certain definite objects; the second is that it shall be carried on by certain persons elected in a specified way. And the third is that the business shall be conducted in accordance with certain principles of commercial administration defined in the statute which provides some guarantee of commercial probity and efficiency. If shareholders find that these condition or some of them are

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101 Supra at p. 379; (1930) 1 All E.R. 99 at p.103.
102 (1924) S.C. 83.

> deliberately and consistently violated and set aside by the action of a member and official of the company who wield an overwhelming voting power and if the result of that is that, for vindication of their rights as shareholder, they are deprived of what the Companies Act would provide them with, then there does arise, in my opinion, a situation in which it may be just and equitable for the court to wind up the company.

Apparently, his lordship well considered circumstances cover a wide spectrum of situations. In any case, the common denominator in the preceding observations is that the phrase 'just and equitable ground' is a concept founded firmly on equitable considerations. Thus, it was held that a petitioner wishing to rely on it must do so with cleans hands.[103] And in determining this, the plaintiff's conduct will be a primary consideration.[104]

A winding up order is usually granted by the courts as a last resort since its effect is to proclaim the death of a company. Thus, where there is an alternative remedy, the court will not be disposed to grant it. In *Cole v. R.C. Irving and Company Ltd*, the plaintiff petitioned for a winding up of the company on the basis that it was just and equitable to do so. The grouse of the petitioner were that:

(1) he was prevented from participating in the company's business;

(2) that the affairs of the company had reached a deadlock situation;

(3) that the appointments of directors and officers of the company were irregularly carried out;

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[103] Ebrahimi v. West Bourne Gallaries Ltd., op. cit. at p. 360, Per Lord Cross of Chelsea.

[104] See Morgan v. 45 Avenue Pty Ltd. (1986) 10 A,C.L.R. 692, Per Young J. at 708.

(4) that transfer of shares had been made fraudulently in contravention of the company's articles of association;

(5) that the company was in substance a partnership and that it should be wound up.

The court, in refusing to grant the winding up order, held that where a petitioner acts unreasonable in seeking the order, and an alternative remedy appears available to him, the court will not be disposed to grant it. Kazeem, J. (as he then was) observed in the course of his judgement that:

> … the question of the petitioner's exclusion form all participation in the business of the company, there is evidence before me that he resigned as an employee of the company in 1961 and that he thereafter established an agency business of his own similar to the one being carried on by the company. Nevertheless, he was still employed on a part time basis by the company either as an auctioneer or on other similar duties for which he was adequately remunerated. He is also recorded in the minute book as being present at some of the meetings of the company where vital decisions were taken, and although he has denied being present at such meetings because there is no attendance register kept by the company, he was no doubt aware that no such register was kept by the company since its inception in 1948, and he did nothing. Even as a director, the petitioner has signed some statement of accounts and executed documents on behalf of the company. But when in 1968 he became aggrieved because he was asked if he was willing to sell his remaining four shares, he was no longer prepared to participate in the affairs of the company … In the light of the evidence before me, I am strongly of the opinion that the petitioner has acted unreasonably in seeking to wind up the company instead of putsuing the remedy prescribed under Section 201[105] of the Companies Decree …

It is thus clear that a petition based on Section 408(c) must disclose sufficient facts which the court would be expected to base its decision on an

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[105] Under the 1965 Companies Act, this empowered the court to aid a petitioner who alleges that the affairs of the company are conducted in a manner oppressive to him.

order for winding up.[106] A case in point here in *Re Law-Solavin*,[107] where the court found for the petitioner for having complied fully with the above. In that case, the Chairman of the Board of Directors of the company petitioned for the winding up on the plank that the company's management had reached a deadlock. The company only had two directors. The Chairman who was the petitioner and the respondent who occupied the position of managing director. The petitioner in his affidavit stated that there had been a dispute between him and the managing director and that a subsequent meeting which convened to iron it out ended in a deadlock as a result of which the companies business could not be run any longer. The petitioner however said that he was still interested in the company business but certainly not with the petitioner any longer since they could "never agree again". The court, upon examining the facts critically, held that there was a deadlock which necessitated an order that the company be wound up on just and equitable ground.[108]

Apart from deadlock, another important requirement is that the petitioner must have suffered from injury of exclusion from management. The right to participate in management is a special underlying obligation of members of the company that they shall be entitled to participate in management, which if not honoured will entitle a member to petition for winding up. In fact, there is no denying the fact that entitlement to

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106 See Farmat Produce v. E.D.C. Co. (1971) 1 All N.L.R. 247 at 252, Per Madarinkan JSC.

107 (1971) 1 U.I.L.R. 421.

108 See also Re Yenidje Tobacco Co. Ltd. (1916) 2 Ch. 426.

management participation constitutes one of the major principles of corporate governance and management which is aimed at ensuring probity and efficiency. But except in private companies where the court held that the denial of a member to participate in management tantamounts to a breach of an underlying obligation which will entitle a petitioner to a winding up order in public companies, it would seem that a winding up order would not be granted except such exclusion constitutes a major reason for breakdown in mutual confidence.[109] Apparently, acknowledging the fact that an underlying obligation is easier to find in private companies than public companies, the CAMA has by virtue of Section 310-312 provided such members easier remedies. The remedy based on unfairly prejudicial conduct is quite apt in this regard.[110]

Alternatively, the provision of Section 262(6) of the CAMA which provides for compensation or damages payable for persons or members wrongly removed from participation in company management could be an easier route for any member who wishes to challenge his exclusion from management to take.

In Ebrahimi's case, Lord Wilberforce stated that a court may grant a winding up order where there is restriction in transfer of shares. It would seem that the circumstances in which this condition may apply is when a petitioner relies on the approval of the directors or shareholders to carry out

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109 See in Re R.A. Noble (1983) B.C.L.R. 273, where Nor\urse J. granted a "winding up order" where the exclusion from management was adjudged a substantial cause of the breakdown in mutual confidence.

110 See Chalseworth's Company Law, Supra at 453, for the underlying consideration in winding up based in exclusion from management and remedy based on unfairly prejudicial conduct.

the transfer but is unable to do so because he is already excluded from management. In this kind of scenario, it seems the courts sympathy would readily be in the petitioners favour when determining whether it is just and equitable to have the company wind up.

For a clearer understanding of Section 262(b) of the CAMA, it would be pertinent to refer to an earlier Nigerian case of *Re Stevedoring (Nig.) Ltd*.[111] where Crage, Ag. J. (as he then was) had occasion to consider extensively, the issue of exclusion of shareholders from management and its effect on the winding up of a company. In the case, the petitioner was one of the six directors who were supposed to hold office for life pursuant to the provision of the Companies Articles of Association. But owing to the fact that the petitioner had on previous occasions criticized and accused his co-directors of wrongdoings, the wrongdoer directors convened an extra-ordinary general meeting of the Board of Directors, and altered the Articles of Association, which enabled them to effect the removal of the petitioner.

In his quite explicit judgement, his lordship while analysing the second circumstance presented by the Lord President in *Bird v. Lees*[112] for winding up a company on just and equitable ground said:

> I take the second circumstance referred to …that the business of the company 'shall be carried on by certain persons elected in a specified way'. It is clear to me that the manner in which the removal of the petitioner was secured from the directorate of the company left much to be desired. I have no doubt that the special resolution of the Extraordinary General Meeting of the

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111 (1962) L.L.R. 164 1t 169.

112(a) Supra.

> Board of Directors … altering the Articles of Association … was null and void since it was proposed and seconded by Mr Odutola … already found disqualified … by becoming a partner in Standard Stevedors Company by virtue of the special resolution of 7th December 1959 … Both Mr Odutola and Dr. Doherty were disqualified by Article 20(F), and so it was improper for the former to attend the meeting … and move the alteration of the Articles of Association … I think the circumstance of this case come clearly within the instance mentioned … when it would be just and equitable for the court to wind up the company … 'that the petitioner was excluded from all participation in the business' as the petitioner clearly has made in this case.

This Nigerian case which came earlier than the Ebrahimi's case could easily have been the leading authority on the issue in the opinion of a learned author "… had it not got into our heads that to succeed under the Section, you must prove loss of substratum or deadlock".[112(b)]

In Ebrahimi's case, Lord Wilberforce stated that a court may grant a winding up order where there is restriction in transfer of shares. It would seem that the circumstances in which this condition may apply is when a petitioner relied on the approval of the directors or shareholder to carry out the transfer and is unable to do so because he is excluded from management. In this kind of scenario, it seems the court sympathy would be for the petitioner when determining whether it is just and equitable to have the company wound up.[113]

For a clearer understanding of all the underlying issues in that case, it would be pertinent here to state the facts of the Ebrahimi's case. In that case, the plaintiff Ebrahimi had for many years carried on the business of Persian

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[112(b)] See Akanki, Supra at 280.

[113] See Mayson et al, op. cit. p. 478.

Carpet with one Naser as partners. Both Ebrahimi and Naser subsequently converted the business into a limited liability company, with each of them holder 500 shares. Later, Naser's son was brought into the business and given 200 shares; and 100 shares of the company's dividends were paid to the directors (who were also members) in the form of remuneration. Trade blossomed and after sometime, a dispute arose whereby the Nasers used their majority vote to remove Ebrahimi as a director. This therefore means he was excluded from management and also from sharing in the company's dividends as dividends were not declared.

Ebrahimi therefore brought a winding up petition as well as relief against oppression. The trial court refused to grant the relief against oppression especially on the premise that Ebrahimi did not sue as a qua member. But the court found that the company was similar to a partnership where an underlying obligation of good faith, trust and confidence could be said to have been seriously abused. He therefore granted the relief for winding up. The Court of Appeal reversed the holding of the trial court on the ground that though partnership analogy could be enforced, the conduct complained of were in breach of the company's article. On further appeal, the House of Lords reversed the judgement of the Court of Appeal and reaffirmed the decision of the trial court. In the process, Lord Wilberforce had occasion to formulate the rules as follows:

(1) That the essence of winding up relief is subject to the exercise of corporate right to an equitable consideration and this will apply whether the company's constitution is breached or not.

(2) That although a director removed in accordance with the articles cannot complain against his removal, but the just and equitable consideration nevertheless comes to his assistance once he can establish some "underlying obligation" of his fellow members in good faith or confidence that he should be entitled to management and if such obligation is broken, the association must be dissolved.

(3) That it is no longer necessary that a company should possess all the attributes of a partnership before this application can be successful. It would suffice, if the petitioner can prove any one of the following: (a) that the association is based on mutual confidence or on a personal relationship, or (b) that there is an arrangement that everyone shall participate in management, or (c) there is restriction on transfer of interest in the company.

It would therefore seem appropriate to asset that mere restriction on transfer of the share of member is not a reason per se for granting a winding up order but where it is accentuated by breakdown in mutual confidence leading to the inability of the petitioner to obtain the requisite consent of the directors, the court would readily be inclined to grant the order.

Again, it would also seem that where the articles expressly allow the shares of a private company to be transferred, the court would not restrain

itself from a winding up order on just and equitable ground if the majority in control constitute an obstacle in the way of members who are desirous of taking advantage of such a statutory right. But it is however unlikely or improbable if such a right will be available to members of public companies considering the avalanche of remedies available to them under Section 312 of the CAMA.

Another circumstance pointed out by Lord President in the *Bird v. Lees* case was that where a shareholder invest in a business he does so on the understanding that the business of the company shall be limited to the object of the company. Thus where the company veers outside such agreed objects leading to the "failure of substratum" the court would have no alternative than to wind up a company on just and equitable ground. A case in point here is that of *Re German Date Coffee Ltd.*[114] where a company that was to operate under a German patent under the articles operated under a Swedish patent in contravention of the articles. Obviously, such a company has failed to carry out its objects. The court wound up the company on just and equitable ground.

It would be necessary to point out however that an application filed in pursuance of an order of winding up a company on just and equitable ground

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[114] (1882) 20 Ch.D. 169. See also Re Blarot Aircraft Co. (1916) 32 T.L.R. 253; Re Crown Bank (1890) 44 Ch.D. 634; Re Haven Goldmining Co. (1882) 20 Ch.D. 151.

would only be granted if it is brought by way of petition and the petitioner must not only be a member but a contributory as well.[115]

Finally, where the court makes an order that the company be wound up, then the relevant provisions of the CAMA relating to the winding up of companies will apply with such adaptation as are necessary, as if the order had been given upon an application filed in the court by the company. And under Section 313, it is an offence punishable by fine or imprisonment for any person to contravene or fail to comply with any order made by the court relating to winding up.

In this chapter, attempts have been made to examine the concept of majority rule, otherwise known as the rule in *Foss v. Harbottle* as well as the protection afforded the minorities in companies. We have noted that the majority rule emphasises the judicial policy that the courts are traditionally reluctant to meddle in intra-corporate squabbles, since it is the preserve of the company, i.e. the majority shareholders to decide whether or not to take legal action against perceived wrongdoer directors. This we noted is no mean obstacle that lies on the way of minority shareholders to enforce directorial breach of duties. Certainly this action-inhibiting rule was based on the fact that membership of a company not only carry individual tight but also

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115 See also S. 410 which requires that the petitioner must in addition have held such shares as original allotee or hold same within 6 months during the eighteen months preceding the application or must have been entitled the same by transmission. The former requirement that the company must be solvent has now been done away under S. 410(4) of the CAMA. A contributory not only include a present member but also a past member of the company. S. 8 CAMA defines him as every person liable to contribute to the assets of a company in the event of its being wound up.

corporate rights i.e. rights that can be enjoyed and exercised not by a single individual or personal right but a number of individual members action.

We have also seen that because the rule virtually left corporate wrong unredressed, exceptions were created to the rule in order to whittle down its effect and afford minority shareholders avenues to challenge corporate wrongs perpetrated by the majority.

Though the rule is still part of the Nigerian law having now been codified, the generous protection it gives selfish and unfair exercise of the company majority powers have been removed. But in the process of codifying some of the remedies, it is evident that something went wrong somewhere. A case in point is the adoption of the Canadian statutory derivation action in the same breath codifying the majority rule imbedded in *Foss v. Harbottle*, an unnecessary duplication.

CHAPTER EIGHT

CORPORATE ACCOUNTS AND AUDIT

8.1 INTRODUCTION

An effective system and policy of corporate financial reporting is the cornerstone of corporate governance and management. Considering the separation of ownership from management, the company directors are required to give account on their stewardship through the instrumentality of the annual report and financial statements sent to the shareholders. The audit on the other hand is supposed to give an external and objective check in the manner in which financial statements have been prepared in order to provide the necessary checks and balances.

When a company raised funds from the public, the company assumes an obligation of public trust and a commensurate level of accountability to the public. Again, where a company wants to have access to the capital market the company must be prepared to accept and fulfil the fundamental obligations of full and fair disclosure. The whole essence of corporate financial reporting therefore is corporate accountability and effective corporate governance and management. But in order to free such corporate financial statements from bias and material error, the law has made it necessary to subject such statements to the scrutiny of company external auditors, an important corporate governance monitoring device. But it is glaring that over the years external auditors have come under considerable criticisms for not being able to report many irregularities that led to the failure of many

corporate entities especially the banks. Many have wondered why auditors failed woefully to provide the needed monitors despite various statutory provisions in the CAMA, BOFIA and NDIC respectively which guarantee them of their independence.

In this chapter, attempt will be made to critically examine the relevant provisions in the laws applicable to company financial statements, a number of issues within the existing scope of auditors responsibilities, especially against the background whether they exhibit substantially the philosophy of disclosure which they were all designed to achieve.

8.2 COMPANY FINANCIAL STATEMENTS

The financial statement of a company is the reflection of the state of health of that company. This is because, it portrays the yearly state of affairs. While emphasizing the practical importance of financial statements. Dr. Orojo observes that:

> They are vital and, indeed of crucial importance not only to members of the company but also to third parties dealing with it, while the financial statements enable a member to know, for instance, whether his investment are growing or depreciating and whether to sell or retain his shares in the company. It provides a potential investor with information which would either persuade him to invest or dissuade him from investing in a particular company.[1]

The regulation of corporate financial statements was first made compulsory under the 1968 Companies Act[2] In the same vein the CAMA 1990 is patterned in several essential aspects after the English Companies Act of 1985. What the

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1 Orojo: Company Law and Practice in Nigeria, Supra.

2 Which was pari material with Companies Act 1948 (United Kingdom)

CAMA has done however is to considerably widened the scope of the provisions dealing with financial statements. Thus more that half of the provisions on company account in the CAMA are new,[3] while others were transferred from the 1968 Act.

Section 334(2) provides a clue as to what amounts to financial statements. The section provides thus:

> Subject to subsection (3) of this section, the financial statements required under subsection (1) shall include –
>
> (a) Statement of the accounting policies;
> (b) The balance sheet as at the last day of the year;
> (c) A profit and loss account or, in the case of a company not trading for profit, an income and expenditure account for the year;
> (d) Notes on the accounts;
> (e) The auditors report;
> (f) The directors report;
> (g) A statement of the source and application of fund;
> (h) A value added statements for the year;
> (i) A five year financial summary, and
> (j) In the case of a holding company, the group financial statement.
>
> This list does not exhaust all the possible items that can be classified under the heading. They are examples of a larger group of items.

It is the duty of the directors to prepare financial statements of a company in every accounting year though a private company is not obliged to include in its list the same matters required of public companies under subsection (a), (g), (h) and (i) of section 334(3).

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[3] See Ss. 331-356 of the CAMA. See Ss. 334, 339, 340, 341, 343, 347, 349, 354, 355 and 356 – These were re-enacted from the 1968 Act.

Section 333(1) mandates every company to keep "accounting records"[4] and it is this record that affords the director the source material from which to prepare the companies financial statement. The phrase "accounting record" is quite an elaborate one which envisages any record inscribed on a sheet of paper or a note on the accounts, to be kept at the registered office of the company or any other place which the director deems proper, as long as such place can be accessible to the officers of the company[5] for purposes of inspection. Section 332(2) is emphatic about the life span of accounting record. It provides that it must be kept for a minimum period of 6 years. It is an offence not to keep accounting records in the manner provided by the CAMA.[6]

An accounting record must be capable of showing and explaining the transactions of a company. Thus it should be able to disclose the financial position of a company at any point in time with reasonable accuracy; enable the directors of the company to ensure that financial statements prepared pursuant to part XI of the CAMA tallies with the requirements of the CAMA in forms of the form and content of the financial statement of the company.[7]

In specific term, the records must disclose daily entries of sum of monies received and spent by the company and the matters necessitating the receipt and expenditure in addition to a record of the assets and liabilities of

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4 Under the 1968 Act, it was known as “books of Account”.

5 E.g. directors, managers, or secretary of the company.

6 S. 333(3) says such a person shall be liable to imprisonment for a term not exceeding 6 months or to a fine or both.

7 S. 331(2) of the CAMA.

the company.[8] For instance, where the line of business of the company concerns buying and selling of goods the accounting records would take this pattern.

(a) Statement of stocks held by the company at the end of each financial year of the company;

(b) All statement of stock takings from which any statement of stock as is mentioned in para (a) has been or is to be prepared; and

(c) Except where the goods are sold by way of retail trade, statement of all goods sold and purchased showing the goods and the buyers and sellers in sufficient detail to enable all these to be identified.[9]

The above analysis underlines the fact that the mandatory requirement of companies to keep accounting record is to emphases the corporate obligation of disclosure and thus provide investors with background information capable of influencing investment decisions. But in the opinion of Professor Gower,[10] this view is debatable. He argues in this respect that:

> Unfortunately, accounts in general and those of companies in particular are of little immediate help except to the well instructed, who are least in need of protection. To the average investor or creditor - "the man on the Clapham Omnibus" - they are cryptograms which he is incapable of solving. He looks to the skilled professional assistance to interpret them for him.

Professor Gower's opinion notwithstanding, it is submitted that whatever shortcomings noticeable in accounting records they still present to outsiders a

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8 S. 331(3) of the CAMA

9 S. 331(4) of the CAMA

10 See Gower, L.C.B. Gowers Principles of Modern Company Laws (4th ed.) (London: Stevens & Sons, 1992) p. 507.

fair view of the financial standing of a corporation and that it is incumbent on the less informed or enlightened to avail themselves with professional assistance where they are unable to interpret such records.

The balance sheet is also required to present a true and fair view of a company's state of affairs as at the end of the financial year.[11] It is also required that the statement of the source and application of funds will supply information on how the company has generated and expended its funds in the particular financial year. Again, the wealth which the company generated during the year and its distribution amongst the various competing interest groups must be reflected in the value added statement. Such interest groups being employees, the government, creditors, proprietors and the company.[12] The five year financial summary is also required pursuant to Section 335(5) to provide a report covering five or more years from which a comparison can be drawn of vital financial information.

Under schedule 2 item 36 of the CAMA the company must state in clear terms its accounting policies for formulating both the balance sheet and the profit and loss account respectively in addition to such policies concerning the depreciation and diminution in value of assets. The profits and loss account is a true account in every sense of the word.[13] They represent the figures for a period in which a company engages in business activity. It is a document

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11 S. 335(2) of the CAMA

12 S. 335(4) of the CAMA

13 See Gower, L.C.B. (4th Ed.) op. cit. p. 510.

designed to mirror the profit or loss of business concern. According to Professor Gower, the profits and loss accounts:

> ... is not necessary very informative but the study of a series of accounts over a number of years can be most revealing since the trend of profits is the best indication of the prospects of the company and on the continuation of the business as a going concern to the valuation of its assets depends.[13(b)]

The layman undoubtedly finds it easier to study these trends from this account than from the balance sheet in its traditional form and confusing layout. The primary principle is that the profit and loss account shall give a true and fair view of the profit or loss of the company for the financial year.[14]

The profit and loss account thus constitutes an important corporate performance chart which every prospective investor is expected to avail himself before determining whether to invest in any particular company or not. But how does this differ from balance sheet? Professor Gower again provides the difference. He notes that:

> ... the balance sheet - is not an account in the strict sense. It is merely a statement of the company's asset and liabilities as at the end of the financial year. Unlike the profit and loss account which deals with a course of events during a period of time, in practice, it is its interpretation that the layman finds particularly difficult. He is especially likely to be baffled when the balance sheet is in the old-fashioned two-sided format with assets on one side and liabilities on the other and in which a perfect equilibrium between the two appears to have been achieved. It might be thought ... that a member or a creditor could from a study of the balance sheet ascertain the company's net worth. That, however, is not wholly true ... The balance sheet is still essentially a historical document and not one which purports to show the net worth of the company's

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13(b) See Gower, L.C.B. Ibid at p. 510.

14 Annually the details which are reflected in the balance sheet include investment income from listed and unlisted investments merits receivable interest on loans, the amount clerical for depreciation corporation and other tax, increases of and withdrawals from services, hiring of plants or machinery, and for remuneration etc.

> business at the time present. What it should show with much accuracy are the total and types of the company's liabilities and how its funds are spread between various types of assets ...[14(b)]

Despite the striking differences pointed out between profit and loss account and balance sheet, both however share one important statutory object, which is that they must give "a true and fair view" of the state of affairs of the company as at the end of its financial year".[15] This is a golden rule and the object of statutory provision which require disclosure of company account and audit with specific reference to the balance sheet. It is clear from Professor Gower's observation that it is unlikely that a member or a creditor will ascertain a company's financial worth or viability by merely perusing the balance sheet. Added to this is the possibility that both may not represent the actual state of financial affairs of a going concern either because of deliberate manipulation or mistake of some sort.

The "notes on the account" as observed earlier form part and parcel of financial statements. It relates to supplementary information that must be provided in a separate note. This becomes relevant if such information is not already contained in any other account or the balance sheet of the company. The other circumstances that would warrant the necessity for this is where compliance with any requirement in relation to the balance sheet or profit and loss account will not result to the actualization of the presentation of a true and fair view of the accounts. The option opened to such a company is for the director to depart from complying with such requirement in preparing the

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14(b) See Gower, L.C.B. op. cit. at p. 512.

15 See schedule 2 item 36.

balance sheet or profit and loss account in order to actualise the essential statutory requirement of providing such a true and fair view,[16] where the company adopts this option, it must provide notes of the particulars of the departure and the bases for the departure.[17]

The director's report which also form part of financial statement is regulated by section 342 of the CAMA. In each financial year directors are mandated to prepare a director's report to be attached to the balance sheet. The report reflects a fair view of the development of the business of the company and its subsidiaries in a particular financial year as well as the position of the company at the end of the year. The report must also state such amount (if any) that the directors must have recommended to be paid as dividend and the amount (if any) proposed to be carried to reserve.[18] A director's report is also an invaluable component of the company financial statement. Thus it is required to contain important financial statements such as asset values, interest of directors; charitable gifts, acquisition of its own shares by the company, employment of persons that are disabled, health, safely and welfare at work of employees of the company, employee's involvement and training.[19]

Section 336(1) also regulates the filing of group financial statement of holding[20] companies. This statutory requirement is important where a

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16 S. 335(7) and (8) of the CAMA

17 S. 335(9) of the CAMA; Part III Schedule 2 of the Act, such supplementary information consist of information on supplementary debentures; on fixed assets; on investments; capital and provisions; on provision for taxation, details on indebtedness; on guarantee and other financial commitments and miscellaneous matters.

18 S. 342(1) of the CAMA

19 See generally Schedule 5 part I, II and III of the CAMA; See also Gower, op. cit. at 516.

20 Under S. 338(5) a company is said to be a holding company of another. If the other is its subsidiary.

company also has subsidiaries. At the end of each financial year such companies are required while preparing individual accounts for that year to also prepare group financial statements, being accounts or statements which regulate the state of affairs and the profit or loss of the company and its subsidiaries.[21] But section 336(2) provides that section 336(1) will not apply where the company at the end of the financial year is the wholly owned subsidiary of another body corporate incorporated in Nigeria. Implicit in section 336(1) therefore is the fact that a subsidiary company cannot prepare group financial statement representing its account and that of the holding company. Group financial statement also need not necessarily encompass the account of a subsidiary where the directors consider it impracticable or would be of no value to the members, considering the insignificant amount involves; or it would involve expenses or dealings out of proportion to its value to members of the company; or the result would be misleading, or harmful to the business of the company or any of its subsidiaries; or the business of the holding company and that of the subsidiary are so different that they cannot reasonably be treated as a single undertaking.[22]

By and large, the group financial statement which may be wholly or partly incorporated in the individual balance sheet and profit and loss account of the holding company must mirror the actual relationship between the holding company and its subsidiaries.

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[21] A company is said to be a subsidiary company of another if that other company is a member of it or holds more the composition of its Board of Directors; See S. 338(1) (a) & (b) of the CAMA.

[22] S. 336(3) of the CAMA

Section 337 regulates the form and content of group financial statements. It states that the group financial statement of a holding company must be prepared pursuant to the requirements of schedule 2 as far as aplicable and must together with any notes on them give a true and fair view of the state of affairs and profit or loss of the company and the subsidiaries concerned.[23]

Section 337(4) also permits in respect of group financial statements that where the information contained therein are not sufficient so as to give a true and fair view of the affairs of the company any necessary additional information must be provided by way of notes to the group financial statements. In a similar view, where compliance with sections 336 and 337 would prevent the company, owning to some special circumstances from presenting a true and fair view of the affairs of the company, the directors must depart from those requirements so as to give such a view.[24]

The group financial statement of a holding company in any financial year is required to contain details of relevant informations pertaining to loans granted to directors or other connected persons as well as officers of the company including managers and secretaries.[25] These are important disclosures which enables the company take stock of loans already given out and puts it in a position as regards what to be done with respect to future

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23 S. 337(2) of the CAMA

24 S. 337(5) of the CAMA

25 Section 340 governs loans granted to directors and connected persons. S. 341 deals with loan in favour to officers of the company excluding directors. See also generally Schedule 4 part I as well as Schedule 4 part II of the CAMA.

request. While a public company is mandated to file a statement of the source and application of funds a private company is not obliged to do so. This pertains to information regarding the generation and utilization of funds by the company during a particular financial year.

In the same vein, every public company is required to file a value added statement in every financial year. This statement is required to report the wealth created by the company during the year and how it was shared out among the various groups both within and outside the company. These are the company itself, the creditors, the proprietors, the government and the employees.

The five-year financial summary is another important document required to be filed by companies especially public companies. Information contained therein should provide a report and a comparison over a time frame of five years or more of important financial information. Apart from the above, companies are required to prepare and file Statement of Accounting Policies.[26] But it must be emphasised that private companies are not obliged under Section 334(3) to prepare and file a statement for the year as well as a five year financial summary, but may do so if they so wish.

It is of utmost importance that financial statements are prepared with reference to an accounting period. Thus section 334(5) provides that the accounting period of each subsidiary company should coincide with the

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[26] This relates to policies for formulating both the balance sheet and the profit or loss account as well as policies pertaining to the depreciation and diminution in the value of assets.

accounting period of the holding company unless the directors have strong reasons to think differently. In taxation, an accounting period presently starts from 1st January to 31st of December of each year.[27] In any case the directors must determine to what date in each year financial statements shall be made up. Usually the directors are required to determine this at their first meeting after the incorporation of the company. They are also required to give notice of the date to the commission within a period of 14 days of the determination.[28]

The four major "statement" of accounts i.e. the balance sheet, profit and loss account, the directors report and the auditors report are required to be annexed together and duly signed by two directors on behalf of the Board of Directors pursuant to Section 343 of the CAMA. The section punishes the company and every of its officer who lay before the company in the general meeting or deliver to the Corporate Affairs Commission any of the above-mentioned documents without the signatures of the directors. The penalty is ₦300.00 for being in default.

While a newly incorporated company has up to eighteen months after[29] its incorporation to lay before the company in general meeting all the financial statements tabulated under section 334(2), older ones are mandated to do theirs every year. But whether the company is old or new, the financial

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27 Before an accounting period used to commence from 1st of March to 1st of February.

28 S. 334(4) of the CAMA.

29 S. 345(2) entitles every shareholder to impact the auditors report which must in any case be read before the coming in general meeting.

statement must be prepared at least nine months before the date of the meeting.

Company directors are also under a duty to deliver to the commission the annual return of the company together with the balance sheet, the profit and loss account and the supplementary notes on the financial statements that had already been laid before the general meeting.[30] It is an offence to fail to carry out this responsibility by both small and big companies. Thus both immediate past directors and present directors may be liable under Section 345(1) except as indicated under subsection (2). The director in question is not to be blamed having been diligent on his part in ensuring full compliance and yet to no avail. The CAMA provides for a penalty of ₦500.00 in the case of a big company and ₦50.00 in the case of small companies.

Avenues however exist for compelling the performance of the directors' responsibility under Section 346 of the CAMA. Thus Section 347 provides that:

(1) If -

(a) in respect of a year, any of the requirements of subsections (1) and (3) of section 345 of the Act has not been complied with by a company before the end of the period allowed for laying and delivering financial statements; and
(b) the directors of the company fail to make good the default within 14 days after the service of a notice on them requiring compliance, the court may on the application by any member or creditor of the company or by the commission make an order directing the directors or any of them to make good the default within such time as may be specified in the order.

(2) The Court Order may provide that all costs of and incidents to the application shall be borne by the directors.

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30 S. 345(3) of the CAMA

(3) Nothing in this section shall affect the provisions of Section 346 of this Act.

Analysing the equitable nature of the above provision Professor Anifalage observes that the admirable provision in section 347 which seeks result as opposed to strict legality is an authority to either a shareholder or a creditor or even to the commission to seek and obtain a judicial order to compel the discharge of the directors duties under section 345.[31] Indeed one cannot but agree with the learned writer that the provision is a welcome development and a potent instrument in the hands of investors to prod into action directors who are diligent in the discharge of their corporate responsibilities. The substantive civil sanction in section 345 against the directors is an added deterrent mechanism for the directors.

Apart from default or non-compliance by directors to lay and deliver financial statements, the CAMA equally frowns at a situation where a company director would lay or deliver defective financial statements. Thus Section 348 of the CAMA provides that it is an offence for a director not to take reasonable precaution to ascertain that statements are not inaccurate or defective. The CAMA stipulates a fine of ₦250.00 in the case of group financial statement and ₦100.00 in the case of individual financial statement. It is also a defence under subsection 3 for a director to establish that he took all reasonable steps to secure compliance but to no avail.

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[31] See Anifalage, J.O. "Current Principles and Policies on Company Accounts, Annual Returns and Audit in Nigeria" in Akanki (ed.) Essays on Company Law, (Lagos: University of Lagos Press, 1992) p. 206.

Certain persons are entitled to be given to them a copy of the company's financial statement. These are shareholders and creditors. These persons are entitled to receive it at least 21 days before the date of the general meeting. The period could be less than 21 days if the persons entitled to receive the notice decide to waive it. But nonetheless, the company and every officer in default are liable to pay a fine of ₦250.00.[32] Section 349(2) however appears to be a deliberate mechanism to shield persons entitled to receive such notices from possible corrupt abuse by company directors. Thus the provisions states in unmistaken terms that both shareholders and creditors need not pay any money to obtain or demand a copy of the financial statement of the company even if such a person is not entitled to receive it as a matter of right under Section 344 of the CAMA. Failure to comply, is punishable with a fine.

According to the CAMA a financial statement that is published[33] by a company could be full or abridged. Section 354 regulates the publication of full financial statement and states that where a company does so, it must also publish the auditors report with them and where necessary, its group financial statement.[34]

In the case of an abridged financial statement, the company publishing it must indicate (1) that the statements are not full financial statement; (2) whether full individual or full group financial statement according to the

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32 S. 349(1) of the CAMA

33 A company is said to have published its financial statement when the statement is laid before the company in general meeting and delivered to the Commission.

34 See S. 354(2), (3), (4) and (5) respectively.

abridge statement deal solely with the company's own affairs or with the subsidiaries and have been delivered to the commission or in the case of an unlimited company exempted under Section 345(4) from the requirement to deliver financial statement; whether the company's auditors have made a report on the company's financial statement for any year with which the abridged financial statements purport to deal; and whether any report so made was unqualified;[35]

Where abridged statements are published by the company, the auditors report should not be published with it.[36] Unlike the big companies which the CAMA has required elaborate financial statements, it has however adopted a liberal disposition towards the small companies. Justifying the special statutory privilege accorded small companies by the law, Anifalage[37] has this to say:

> …it has been recognized in the Decree (New Act) that not only would it be unreasonable to set the same standard and require the same type of information for the say the United African Company Limited and a registered company exclusively formed and managed by a man and immediate family; it would also be needlessly burdensome financially for such a small company to face such an ordeal considering the definition of a small company under the CAMA. We think the statutory advantage conferred on small companies is not without basis.

Section 351 provides that a company qualifies as a small company … if the … following conditions are satisfied:

(a) it is a private company having a share capital;

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35 This means a report without qualification to the effect that in the opinion of the auditor, the company financial statements had been properly prepared.

36 S. 355(4) of the CAMA

37 See Anifalage, J.O., op. cit. at p. 207.

(b) the amount of its turnover for that year is not more than N2 million or such amount as may be fixed by the commission;

(c) its net assets value is not more than M1 million or such amount as may be fixed by the commission;

(d) none of its members is an alien;

(e) none of its members is a Government nominee or a Government Corporation or agency or its nominee, and

(f) the directors between them hold not less than 51 percent of its equity share capital.

The statutory privilege translated in concrete terms means that a small company can simply file modified financial statement which consist of both abbreviated versions of the full statements which are shorter in form, less cumbersome, probably less complex but cheaper to produce.[38]

But it would appear that without adequate publicity or a conscious corporate policy of engaging persons knowledgeable in company law especially the different aspects of company accounts, it is unlikely that the benefits of modified financial statements will be taken advantage of by small companies.[39]

8.3 ACCOUNTING STANDARDS

The Nigerian Accounting Standard Board present from time to time certain standards that must be followed by the accountancy profession in the preparation and use of company financial statements. These accounting standards are expected to harmonise with the relevant provisions of the CAMA

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38 See Anifalage. Ibid at p. 207.

39 See Geoffrey More Chalsworth's Company Law (13th ed.) Stevens & Sons Ltd, London, 1987 p. 455, where the author observed that more than lack of the large body of small companies in England has not taken advantage of the filing modified financial statements. See also Schedule 7 part (I); Sections 352 and 353 of the CAMA which deals with modified financial statements.

dealing with financial statement as well as international Accounting Standards. The Accounting Standards cover several aspects of Accounting.[40]

The statements of accounting standards which are issued from time to time by the Boards is statutorily recognised under Section 335(1) of the CAMA. The Board is constituted by the Minister of Finance and is made up of representatives from the Federal Ministry of Finance and economic development, Central Bank of Nigeria; the Nigerian Association of Chamber and Commerce, Industries, Mines and Agriculture, the Nigerian Accounting Teachers Association, Nigerian Institute of Bankers, Employers Association, Nigerian Stock Exchange and the Institute of Chattered Accountants of Nigeria.

8.4 COMPANY AUDIT AND AUDITOR

We have discussed the importance of keeping accounting records. We noted that its importance cannot be overemphasised where they are kept according to the provisions of the law, fraud, misrepresentation, mismanagement associated with company's finances will certainly be curtailed.[41] This will in turn invite public confidence in the companies whose account has been properly prepared and kept. But since accounting records are subject to two possible evils, human errors and deliberate abuses, the law has therefore assigned an independent auditor to inquire into and investigate such facts that are presented in order to assist the audit. The importance of auditing cannot also be overemphasised. This is because it assists in detection

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40 Examples are: Disclosure of Accounting Policies (SAS 1), Information to be disclosed in Financial Statements (SAS 2), Accounting for Property Plant and Equipment (SAS 3), Accounting on Stocks (SAS 4), Accounting on Construction Contracts (SAS 5), Accounting on Extraordinary items and prior year adjustments (SAS 6).

41 See Gower, L.B., Principles of Modern Company Law, 5th Ed. Supra at 507.

of errors and fraud and provides assistance in putting in place adequate accounting system.

Blacks Law Dictionary[42] defines the Company's Audit as: "The systematic inspection of accounting records involving analysis, tests and confirmations …" Also in *R v. Carson*,[43] it was defined as the examination of the accounts of a company by auditors with a view to ascertaining and stating the true financial position of the company. The responsibility for the Company Audit therefore falls on the company external auditor.

8.5.1 Appointment of Company First Auditors

Section 351(1) of the CAMA provides that every company must appoint an auditor or auditors at each annual general meeting whose responsibility shall be to audit the financial statements of the company.

The first auditors may be appointed by the directors at any time before the company commences business. Auditors appointed in this manner shall occupy the office until the next Annual General Meeting.[44] However, at the Annual General Meeting, such auditors may be removed by the company and in their place may be appointed any other person nominated for appointed by any member of the company. The nomination notice of such substitute must have been given to the company's members not less than 14 days before the Annual General Meeting.[45] If the directors fail to exercise their powers of

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42 5th Ed. West Publishing Co. St. Paul Minn. 1979, 120. See also The American Heritage Dictionary of the English Language, New College Ed. Houghton, Mifflin Company, Boston 1982 at p. 46, where it is defined as an examination of records of accounts to check their accuracy.

43 (1908) 1 K.B. 407 Per Farewell, L.J.

44 S. 357(5) of the CAMA.

45 S. 357(5) (a) of the CAMA.

appointment of first auditors, the company may convene a general meeting to appoint the first directors by ordinary resolution. Where the company appoint the first auditors, the directors having failed to do so, the director's power to appoint auditors ceases.[46]

8.5.2 Appointment of Subsequent Auditors

Every company is required at its annual general meeting to appoint an auditor or auditors to audit the company's financial statement. An auditor or auditors so appointed shall hold office from the conclusion of that annual general meeting until the conclusion of the next annual general meeting.

A retiring auditor must be automatically re-appointed at any annual general meeting without any resolution being passed except:

(a) he is not qualified for re-appointment;

(b) at the meeting, a resolution has been passed appointing some other person instead of him or providing expressly that he shall not be re-appointed;

(c) he has notified the company in writing that he is unwilling to be re-appointed.[47]

There is however a limitation on the automatic re-appointment of a retiring auditor. This is where a notice of an intended resolution to appoint some person or persons in place of a retiring auditor and by virtue of the death, incapacity or disqualification of that person or of all these persons, or

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46 S. 357(5) of the CAMA.

47 S. 357(2) of the CAMA.

as the case may be; the resolution cannot be proceeded with, the retiring auditor shall not be automatically re-appointed by virtue of this.[48]

An auditor may be appointed to fill casual vacancy that may arise in certain situations. This is where no auditors are appointed or re-appointed at an annual general meeting. In such a situation, the surviving or continuing auditor or auditors (if any) may be appointed act in the office as an auditor.[49] However, the directors has the power to appoint a person to fill the casual vacancy. The person so appointed will hold office until the next annual general meeting. In such a situation, the members lacked the power to remove such an auditor.

Where in the coming year, the annual general meeting fails to appoint an auditor, no casual vacancy would be deemed to exist any longer. In that event the Corporate Affairs Commission has power to appoint and that power is exclusive.

Section 357(4) of the CAMA however states that where the directors so appoint an auditor due to the failure of the members to do so in annual general meeting, the company must give appropriate notice of the fact to the Corporate Affairs Commission within seven days. Failure to comply with this statutory notification will make the company and any officer in default to be liable to a daily default fine of ₦100.00.

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48 S. 357(1) (c) of the CAMA.

49 S. 357(6) of the CAMA.

Under Section 29 of BOFIA 1991, it is provided that every bank shall appoint annually a person approved by the bank referred to as "approved auditor" whose duties shall be to make to the shareholders a report upon the annual balance sheet and profit and loss account of the bank and such other informations as may be prescribed from time to time by the ban.[50]

8.5.3 Qualification and Disqualification for Appointment as Auditors

Before a person can be appointed as company auditor, he must be a member of a body of Chattered Accountants in Nigeria established from time to time by an Act or Decree.[51] This means that Chattered Accountants under the Institute of the Chattered Accountants Act, Chattered Institute of Public Accountants as well as Association of National Accountants of Nigeria are all qualified to be so appointed. But it appears that for purposes of any investigation of audit pursuant to the relevant provisions of the CAMA, only the provisions of the Institute of Chattered Accountants of Nigeria Act 1965 shall have effect.

The following persons are however not eligible for appointment under the CAMA, as company auditors:

(a) An officer or servant of a company.

(b) A person who is a partner of an officer of the company.

(c) A person in the employment of an officer or servant of a body corporate.

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50 S. 29(4) of BOFIA 1991.

51 See ICAN Act, Cap. 185, Law of the Federation of Nigeria, 1990 and ANAN Decree 76 of 1993. See also CAMA as amended.

(d) A body corporate.[52] However, there is no general prohibition of a firm if all the partners of the said firm are qualified for appointment as auditors.

(e) A person who is disqualified for appointment as an auditor of any other body corporate which is that company's subsidiary or holding company or auditor of the company.

A person who knows he is disqualified for appointment must not vie for the position of company auditor. In the same vein, an incumbent auditor who is aware that he has been disqualified from being appointed must vacate office and notify the company in writing that he is vacating his office as auditor.[53] Section 362(1) prescribes a fine of ₦500, and where the breach is continuous, a daily default fine of ₦50 is prescribed.[54]

Section 359 of the CAMA which governs the appointment of auditors generally equally applies to the appointment of approved auditors of banks. But on a specific note, Section 29(2) BOFIA states that the approved auditor shall be an auditor who is:

(i) a member of one professional body recognised in Nigeria;

(ii) approved by the bank;

(iii) resident in Nigeria, and

(iv) carrying on in Nigeria professional practice as an accountant and auditor.

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52 S. 358(2) (d) of the CAMA.
53 S. 358(5) of the CAMA.
54 S. 358(6) of the CAMA.

The effect of the combined provisions of the CAMA and BOFIA is that a person outside the purview of the provisions cannot be appointed as an approved auditor. It is also glaring that the provisions of the CAMA are more detailed comparably. The provisions in the BOFIA are highly inadequate and very economical. It is no surprising that all manners of persons were appointed to the office of approved auditors of banks and who found it difficult to perform thereby contributing to distress in the industry.

An auditor may resign from his office by depositing a notice in writing to that effect at the company's registered office and such notice automatically has the effect of bringing the tenure of the office of such auditor to an end on the date the notice as deposited or on such later date as may be specified in the letter.[55]

A company auditor is subject to removal. A company can do this by ordinary resolution before the expiration of his terms of office irrespective of any agreement to the contrary existing between such auditor and the company.[56] The company must however give notice of the ordinary resolution to the Corporate Affairs Commission within 14 days failing which the company and the officer in default will be penalised. The penalty is a daily default fine of ₦100. This is however without prejudice to his right to compensation of damages payable to him pertaining to the termination of his appointment.[57]

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55 S. 365(1) of the CAMA.
56 S. 362(1) of the CAMA.
57 S. 362(2) of the CAMA.

The BOFIA does not specifically provide for auditor's resignation but instead states certain circumstances where an approved auditor of a bank may cease to continue to function as an auditor. For instance, Section 29(3) provides that where a person appointed as an auditor subsequently:

(i) acquires an interest; or

(ii) becomes a director, officer or agent of that bank;

(iii) becomes indebted to a partner in a firm which a director of a bank is interested as a partner or director, he shall cease to be such auditor.[58]

In terms of removal, Section 29(1) is not emphatic but merely states that in the event of removal, reasonable steps should be taken to justify it and that it should not be carried out without the prior approval of the bank. Under the CAMA, it is however explicitly provided that a removed auditor has certain rights which he can exercise consequent upon his removal. For instance, he has the right to:

(i) attend any general meeting at which it is proposed to fill the vacancy created by his removal;[59]

(ii) to receive all notices of and other communications concerning any such meeting which any member of the company is entitled to receive;[60]

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58 S. 29(3) BOFIA.

59 S. 363(2) (a) & (b) of the CAMA.

60 S. 363(2) of the CAMA.

(iii) the right of audience at any such meetings which he attends on any part of the business of meetings which concerns him as a former auditor of the company.[61]

It is important to point out that the elaborate statutory provisions governing personality of the auditor is the recognition of the detrimental influences which might diminish the auditor's actual or apparent independence.[62] The idea of independence can be found in the statements and rulings issued from time to time by the various professional accounting bodies.[63]

It is of primary importance to the accountancy profession that the confidence of the general public be maintained. Thus it would be wrong ethically and a sabotage of an auditor's independence if an auditor makes a statutory audit of the same company he has prepared the books of accounts. According to Wolziner:

> The legal provisions and regulatory requirements are aimed at removing the auditor from any conflict of interest arising between management as the preparer of financial statement. It is argued here that however desirable such independence may be, if it does not ensure that the product of the auditing function is financial information which is in itself free from the influence of corporate managers, then the objective of credible and reliable financial disclosure cannot be attained.[64]

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61 S. 363(2) of the CAMA.

62 See Bakibinga, "The Audit Function," (1989) Gravitas Review of Business and Property Law, pp. 18-19.

63 An example is the Institute of Chattered Accountants of Nigeria (ICAN); and Association of National Accountants of Nigeria (ANAN). These are the bodies responsible for accountancy practice in Nigeria. They have codes for the guidance of their members. Similar codes are also drawn up by similar bodies in America, England and Australia.

64 Wolziner P.W. "Independence in Auditing: An incomplete notion". ABACUS Journal of Accounting and Business Studies, Vol. 14 (June, 1978) p.40.

It is thus not further from the truth that the legislative objective of the statutory provisions regulating the conduct of the company auditor is the removal of dependence between him and management with the aim of enhancing the credibility and status of audit report.[65] Certain happenings within the auditing profession also contribute in no small measure to eroding whatever semblance of independence that the auditor has. First, the auditors renumeration is normally fixed by those that appoint him, whether by the members, Board of Directors or the Corporate Affairs Commission.[66] Where the appointment of an auditor is not made by the directors, this may be fixed by the company in general meeting in the manner determined by the company at the general meeting. The quantum of auditors renumeration, which would usually consist of fees and expenses depends on the auditors professional experience since they carry out their assignment at the pleasure of the company, notwithstanding any agreement to the contrary. Again, auditors may not want to lose their clients.

8.5.4 The Legal Status of Company Auditors

The company auditor has come to be identified with a dual personality in company law. That of an officer of a company as well as an agent of the company. In *R v. Stracter*,[67] the court was of the view that an auditor

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65 See Ikhahale, M. "How Independent is the Company Independent Auditors?" (1987) 1 ULR Vol. 2 p. 22.

66 S. 361 of the CAMA. See 362 of the CAMA, an auditor can despite anything to the contrary in his service contract be removed by an ordinary resolution. Though the commission must be informed of his removal within 14 days and any contractual remedy he may have is prescribed under S. 362 as well.

67 (1960) 2 Q.B. 252 C.A.

appointed pursuant to the U.K. Companies Act, 1948[68] is an officer of the company who could be sanctioned in respect of all those offences for which officers of the company are prohibited.[69]

Under the CAMA, Section 650(1) which defines who an officer is does not include company auditors. But it does not expressly exclude it either. But an auditor appointed on an ad hoc basis to carry out a private audit may not be regarded as an officer of the company.[70]

An auditor of a company may also be regarded as an agent of the members of the company to discharge certain specific duties as provided by the CAMA and articles for purpose of the company audit.[71] They are therefore not general agents of the members.

8.6 THE AUDITORS' REPORT

The auditors' report is regulated by section 359 of the CAMA. The report is usually attached to any circulated or published copies of the accounts. This is a detailed report to the company's members on the accounts examined by them and on every balance sheet and profit and loss account and on all group financial statements copies of which are to be laid before the company in a general meeting when the auditor hold office as auditor.[72]

The auditors report must be read in the general meeting and must state certain matters.[73] (1) The auditors would be required to state whether they

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68 i.e. S. 159 the same with S. 357 of the CAMA.
69 In the CAMA, the relevant provisions are SS.357, 502, 504, 507, 508.
70 See Shonowo v. Adebaya (1969) NCLR 82.
71 Ibid.
72 See 359(1) of the CAMA
73 See Schedule 6 to the CAMA.

have obtained all the informations and explanations necessary for the purpose of the audit; (II) whether proper books of account have been kept and whether proper and adequate returns have been received from the branches which they could not visit; (III) whether the companies balance sheet and profit and loss account covered by the report tallies with the books of accounts and returns (IV) whether in their opinion and to the best of the information and explanations offered them the financial statement provides the information required by the CAMA in the manner required especially in respect to:

(a) whether the balance sheet gives a true and fair view of the state of the company's affairs as at the end of its financial year and

(b) whether the profit and loss account gives a true and fair view of the profit and loss for its financial year or as the case may be, a true and fair view thereof subject to the non-disclosure of any matter (to be indicated in the report) which by virtue of Part (I) of Schedule 2 of the CAMA are not required to be disclosed.

(c) Whether in the case of a holding company submitting group financial statements, the group financial statement have been properly prepared pursuant to the provisions of the CAMA as to give a true and fair view of the state of affairs and profit or loss of the company, or as the case may be, so as to give a true and fair view thereof subject to the non-disclosure of any matters (to be indicated in the report) which by virtue of Part (I) of Schedule 2 are not required to be disclosed.

To ensure that the auditor is not unduly inhibited from discharging his functions creditably and efficiently, he is allowed to have access at all times to company books of accounts and vouchers of the company and any necessary information or explanation which they must require from any officer of the company.[74]

The auditors report must be delivered to the secretary of the company who would normally bring it beofre the general meeting. Before its repeal section 359(2) was an innovation in the CAMA which required that the auditors report be countersigned by a legal practitioner. Critics who vehemently opposed the innovation argued that legal practitioners are not versed in accounts and therefore incompetent to dabble into matters relating to it; that by virtue of the technical matters which the law stringently prescribed should be stated by company auditors in pursuance of Schedule 6 to the CAMA only an accountant is qualified to deal with such technical matters. The critics further asserted that while the law makes provision for liability in negligence in the case of company auditors,[75] in the course of discharging their auditing functions, the legal practitioner is not made to pass through a similar fate for countersigning an auditors report.[76]

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74 S. 360(3) of the CAMA.

75 S. 368(1) of the CAMA

76 See Lamitanra, R. "Company and Allied Matters Decree 1990 – a critique (IV) published in the Business Times of Monday 16/2/90 at p. 7; See also Lamkanra, R. "The Audit Report and The Legal Practitioner" Business Times of Monday, 14/5/90 at p. 22; See also The Guardian, Monday, 19/2/90 at p. 20.

But according to Professor Anifalaje, the provision of section 359(2) which directed that a legal practitioner should "countersign" the auditors report:

> Was not denigrating of the profession but has asked "another reasonable head" to join forces with the auditor in preparing his report.[77]
> The lawyer is not merely a signatory without more. He is implicitly required to be familiar with the entire Decree and be aware of its relevance to the task of the auditor and to advice the auditor on the requirements of the law…
> The absence of a provision in the Decree to impose civil liability on the legal practitioner for any negligence comparable to the civil liability of the auditor is not a handicap: The directors can still sue the legal practitioner on behalf of the company because a breach of a statutory duly amounting to negligence is always actionable at common law…
> One hopes no mistake would be made in amending the Decree…[78]

We align ourselves with the profound wisdom of the author and also add that the critics argument was baseless if it is considered that the CAMA allows accountants and chattered secretaries to sign incorporation documents (except Form C01) which are substantially legal documents. Besides, in the event of dispute in relation to any of the CAMA provisions such disputes can truly be resolved by judges and lawyer alike.[79] It is sad that an amendment was later effected to section 359(2) which makes the countersigning of an auditor's report unnecessary.[80] We submit that considering the considerable criticism which company auditors have come under before and after the amendment of

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77 See Anifalaje, J.O. "Supra p. 205.
78 Ibid at pp. 213 – 214.
79 See S. 6 of 1999 Constitution.
80 See Decree 46 of 1991.

section 359(2) for providing unreliable and outrightly deceptive reports,[81] it would be pertinent in the circumstance to reenact the above provision. It should be noted that a lawyers' duty to countersign a document is not merely a ministerial act or duty. In all intents and purposes, it connotes that the lawyer in question has attested to the veracity or authenticity of the report.[82] If the true picture of the happenings within the auditing profession and the antics of management of companies had been taken into cognizance, perhaps the provision would not have been repealed. For instance as far back as 1974 studies[83] in Australia had shown that financial report of most companies were often doctored by management to reflect management pre-determined conclusion to elicit the favour and support of shareholders. The attitude of the law in most common wealth countries do not help matter. This is because the law does not specify a particular accounting style for any particular business concern with the result that management can always teleguide those preparing its accounts to select the particular accounting standard, rules or principles favourable to its desired intentions. Out of sheer timidity, complacency or inducement, auditors have not been known to complain about this. But this attitude has been at the detriment of the investors and the potential investors alike. This situation is not different in Nigeria. The Australian studies which investigated a number of companies, some of which would be shown here revealed as follows:

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81 For instance, See Olakunri, O. "The National War Against Fraud – A Challenge to the Accountancy Profession" Being a paper presented at the 26th Annual Accountants Conference on the ICAN, Sheratons Towers, 1996 p. 8.

82 See Anifalaje, Supra at p. 212.

83 See Chambers, R.J. "Securities and Obscurities – A case for Reform of the Company Law Accounts, Gower Press (Melburne 1973) p. 13.

(a) Thiess – Peabody – Mutsin, increased an account by as much as & 11, 272,090 and a provision for depreciation by & 5,266,170 by changing the valuation of a drag-line from a machine rental basis to a hire purchase basis.[84]

(b) Amatil Ltd, increase its reported net profit for the six months ended 29th April, 1977 by 85.2% i.e. (from & 6, 971, 000 to & 12, 910, 000). The increase was made possible by the adoption of tax-effect accounting system.[85]

(c) Ardmona Fruit Products Co-op Ltd. reduce its losses for the financial year 1976 by more than & 1,00,000,000 by changing its stock valuation method. It was the change in accounting practice that enabled the increase in the closing stock figure in the balance sheet and reduced the operating loss reported by & 1, 055, 153. The actual loss reported was & 469, 651.[86]

Also in the United States, A.J. Brilosff 83(e) carried out a similar finding whose report revealed that:

(a) For the year 1974, Hoover Ball and Bearing Company reduced reported net profit by 25%. This was achieved by changing the accounting valuation of inventories from Fifo (First in First out) to Lifo (Last in First out). Net profit was reduced from & 14, 88

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84 See also Australian Financial Review 13th Sept. 1974.

85 See Australian Financial Review, 28 July 1977.

86 See Australian Financial Review, 16th March 1976.

million (or & 3.68 per share) to & 1.73 million (or & 2.75 per share).[87]

(b) Eastman Kodak estimated that 1974 earnings would be reduced by & 41 million (& 0.25 per share) by virtue of adopting Lifo for all its domestic inventories.[88]

Inspite of the insistence of accounting conventions that companies should maintain consistency in styles adopted by them, company, auditors are still at the mercy of management who may decide to engage in unrestrained and indiscriminate juggling with figures owing to the absence of a unified system of accounting.

8.7 THE DUTIES OF COMPANY AUDITORS

In the process of fashioning out a report which must be laid before the company in a general meeting during their tenure, the auditors must, among other things comply with certain duties. Perhaps, the appropriate starting point would be the all important case of *Re London and General Bank (No.2)*,[89] where the court concisely summarised the duties of an auditor. In the case, Lope L.J. eloquently stated that the duties of an auditor is to:

> … ascertain and state the true financial position of the company at the time of the audit … But he does not discharge his duty by doing this without inquiry and without taking any trouble to see that the books themselves show the company's true position. He must take reasonable care to ascertain that they do so … An auditor, however, is not bound to do more than exercise reasonable care and skill in making inquiries and investigations. He is not an insurer; he does not guarantee that the books do

87 See Briloff, A.J., "Unaccountable Accounting" Harper and Row, New York, 1972.
88 Ibid.
89 (1895) 2 ch. 673.

> correctly show the true position of the company's affairs; he does not even guarantee that his balance sheet is accurate according to the books of the company. if he did he would be responsible for error on his part even if he were himself deceived without any want of reasonable care on his part say by fraudulent concealment of a book from him… he must be honest i.e. he must not certify what he does not believe to be true and he must take reasonable care and skill before he believes that what he certifies is true.[90]

Though his Lordship's dictum would appear to indicate that an auditor needs to rely on the honesty and accuracy of others especially on the certificate of stock balance given him by reasonable official of the company, this position has changed as clearly shown by later developments in judicial circles. For instance in *Formento Sterling Area Limited v. Selsdon Fountain Pen Co. Limited,*[90(a)] Lord Denning observed that:

> An auditor is not confined to the mechanics of checking vouchers and making arithmetical computations. He is not to be written off as a professional "adder and substracter". His vital task is to take care to see that errors are not made, be they errors of computation, or errors of omission or commission, or down right untruths. To perform this task properly he must come to it with an enquiry mind – not suspicious of dishonesty, I agree but suspect that someone may have made a mistake somewhere and that a check must be made to ensure that there has been none.

Lord Denning dictum is an apparent denunciation of Lope, L.J's statement in *Re-Kingston Cotton Mills*. Thus, an auditor would now be expected to attend stock accounts and test stock records for reliability and authenticity.

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90 (1958) 1 L.R. 61; See also Re-Kingston Cotton Mills (No.2) 2 ch. 279, CA 288 – 289; Leads Estates Building & Investment Co. v. Shephard (1887) 36 ch. D 787; Formento (Sterling) Area Ltd v. Selsdon Fountain Pen Co. Ltd. (1958) W.L.R. 61; Re-Thomas Gerald & Sons Ltd. (1968) ch. 465.

90(a) (1958) WLR 61

The specific duties of the company auditor are codified under Nigerian Company Law. These will now be examined as follows:

(1) The duty to make a report on the accounts examined by them on all balance sheet, profit and loss accounts and on all group financial statements copies of which are to be laid before the company in a general meeting during the tenure of the auditor.[91] Such report must state, in a matter of fact whether:

(a) the accounts have been prepared pursuant to the provision of the CAMA 1990 and with International Audit Guidelines. The report must also state whether the financial statements are in agreement with the generally accepted principles of SAS, IAS among others and whether the provisions of the income policy guide lines have been complied with by the company

(b) the accounts give a true and fair view of the company's transactions in accordance with paragraph 3 of the Schedule 6 to the CAMA

(c) the auditors report contains all the informations and explanations necessary to carry out their audit responsibilities

(d) the company's balance sheet and (if not consolidated) its profit and loss account agree with the accounting records and returns.[92]

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91 S. 359(1) of the CAMA

92 S. 360(1) of the CAMA.

(2) Auditors are under a duty to consider whether information contained in directors report for the year in relation to which the accounts are prepared is consistent with the accounts and where such information is inconsistent with the account, the auditors are bound professionally to state it in their report.[93]

(3) In every public company, auditors are duty bound to make a report to an audit committee which every public company must put in place.[94]

(4) Where financial statements do not indicate both the chairman's and director's emoluments, pensions and compensation for loss of office, particulars concerning number of employees enumerated at higher rates and particulars of loans and transactions in favour of directors and officer, the auditor as a point of duty must include a statement stipulating the required particulars in their report.[95]

(5) The auditor owes a duty of care to the company.

Apart from the above duties ably set out in case law and statute, it was previously observed that various accounting bodies for public accounting and auditing all over the world have drawn up detailed code for the guidance of its members. The contents are similar to one another. The codes which take the form of statements and rulings are known as auditing statements and guidelines respectively. Auditing standards are basic principles and practices which members of the accountancy bodies are expected to follow in the

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93 S. 360(5) of the CAMA.
94 S. 359(4) of the CAMA.
95 S. 360(4) of the CAMA.

conduct of an audit. Compliance with these principles is mandatory, as failure attracts disciplinary action. The auditing standards also provide basic standards of care required of an auditor whenever an audit is to be carried out. Courts do regard auditing standard as authoritative statements when considering the adequacy of the auditors report.

Unlike auditing standards which are mandatory, auditing guidelines are merely persuasive as they are guidelines on auditing standards. An auditor is allowed to depart from auditing guidelines provided he explains sufficiently the reason for such a departure.

In providing for the auditors duties, paragraph 10 of the statement of auditing standards issued by the Institute of Chattered Accountants of Nigeria (ICAN) in November 1990 states that:

> It is not part of an auditor's duty to search for fraud unless he is required to do so by a specific term of his engagement. The responsibility for prevention and detection of fraud and irregularities is that of management who may obtain reasonable assurance that the responsibility has been discharged by establishing an adequate system of internal control.

And laying down the auditing standard and guidelines, the court in *Maddison v. Miner*[96] was of the view that in cases of professional negligence involving members of the auditing profession, the standard of care is the standard of knowledge, skill and care which is expected of a reasonable member of the auditing profession.

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96 (1991) C.W.D. 40.

Under the Common Law, the standard of care expected of the company auditor is not an extremely high one either. The reason is not farfetched. In the first place, the company auditor in the performance in his functions occupies a secondary and accessory position to the company director.[97] Secondly, professionals are entitled to errors of judgement unless the error is of such a kind that no reasonably well informed and competent member of the profession would have made it. Thus allowance is given to the effect that two auditors in the exercise of their skill and judgement could while working on the same sets of facts arrive at different results without being negligent. And as Lord Hailsham Ian pertinently pointed out in *Re (an infant)*[98] "Not every mistake in the exercise of judgement is unreasonable".

One could therefore discern the apparent limitation in the attitude of the common law standard, and that of the auditing standard in fashioning out a standard of care which the auditor is expected to comply with. Given these limitations, the audit expectation gap will certainly continue to grow. However, even within the existing scope of auditor's responsibilities, there are a number of issues which if critically analysed and addressed the distress in Nigerian corporate environment particularly the financial service sector would have been known early enough and be averted or considerably reduced. For instance, it is noted that:

> The prudential guidelines on asset classification provisions and income recognition introduced…. Sought to standardized the policy on reviewing the quality of banks assets…. The guidelines

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97 See Bingham L.J. in Caparo Industries Plc v. Dickman & 6 Others (1959) 1 All E.R. at 804.

98 (1971) A.C. 682 at 700.

> provided for both objective and subjective criteria for asset classification, provisioning and income recognition on non-performing assets. The guidelines are further reinforced by the Statement of accounting Standard (SAS) 10. It is sad to observe that many auditors of banks failed to comply with the provisions of the prudential guidelines and SAS 10. This act of omission either by design or default has allowed management of banks to hide losses and declare spurious profits through which they have paid taxes and dividend.[99]

Evidently, it could be seen that one of the primary causes of the poor performance of the company auditors is that of deliberate refusal to discharge their responsibilities either because they compromised their integrity or allowed their personal interest to prevail over that of their clients, or in some cases because they are patently inefficient.[100]

It has been found out that even management letters issued by auditors do not address the major risk areas faced by the banks. Few reports gave details on credit risk, liquidity risk, interest rate risk, solvency risk, operational or transaction risk, regulatory compliance risk and reputational risk. Again, many auditors failed to ensure compliance with their recommendations. Instead the recommendations are repeated at subsequent yearly audits. And despite obvious cases of irregularities, most auditors were unwilling to qualify the accounts they audit.[101]

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99 See Ahmad, M.K. "Distress in Banks: A General Overview of the Role of Directors and Auditors". NIDC Quarterly Vol. 8 No. ½, 1998, p. 58.

100 See Manu, Bulanna, "An Opening Address at a Training Programme on Bank Closing Procedures for Firms of Chattered Accountants" organized by the Nigerian Deposit Insurance Corp. (NDIC), NDIC Training Centre, Lagos, 16th September 1997.

101 See Ahmad, M.K. op. cit. at pp. 73 – 74.

Another dimension to the self inflicted malady of the auditor which led to the financial deterioration of banks and eventual corporate distress is explained thus:

> Ordinarily auditors are expected to seek the support of the regulatory authorities in cases of difficulties faced in the audit of banks. Regulatory authorities are required to intervene and protect auditors in order to ensure safe and sound banking practices. Unfortunately, auditors appeared to have shied away from close contact and consultation with the Regulatory Authorities even at the risk of contravening the provisions of banking laws… auditors are statutorily required to report any adverse development in banks to CBN and NDIC... NDIC had to issue a standard report to assist auditors to comply with the provisions of Section 38 of NDIC Decree. The depth and quality of the reports became stereotyped and could not provide any useful information on the conditions of the banks. Therefore, the financial condition of banks continued to deteriorate…[102]

It could be seen that the unsatisfactory performance of the company auditor which has brought his estimation in the eyes of the public very low is not actuated by the mere reason of the expectation gap between what his real functions are and what the public expect from him, but by attitudinal problems bordering on sheer incompetence, conflict of interest, lack of audit focus, and criminal abdication of auditing responsibilities.

8.8 THE AUDIT COMMITTEE

The Corporate Audit Committee came into being as an answer to the abuse of the due process of corporate accountability. It has been reported that the activator of the idea and the eventual birth of it is the McKesson and Robins case of 1940 in which a fraudulent misstatement of about US $19

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[102] See Ahmad, M.K., Ibid at 74.

million, most of them in inventory and accounts receivable was discovered in the company's financial statement. Accordingly, it was felt that investors would be better protected if an oversee function is exercised by a body properly and effectively interfacing corporate management, the investor community and the financial reporting process of the company.[103] The role contemplated in the McKesson and Robins case eventually gave birth to the Corporate Audit Committee.

Also according to Orojo:

> In the United States they (Audit Committee) were established only in the seventies and by the end of that decade, the overwhelming number of public companies had audit committees. Indeed, it soon became one of the requirements of the New York Stock Exchange for listing of securities on the exchange. In Canada, audit committee first became mandatory under the Ontario Business Corporation Act 1970 and later under the Canada Business Corporation Act 1975. In the United Kingdom Audit Committee became common about the same time although it had not yet become mandatory.

Despite the check put in place by the few companies that voluntarily established it, it seemed the incidence of fraud and fraudulent reporting did not abate as would be expected.

Thus in October 1987, a Commission known as the Treadway Commission[104] on fraudulent financial reporting was constituted by the SEC of the United States and sponsored by the various financial institutions and the American Institute of Certified Public Accountants (A.I.C.P.A.). It objectives consist *inter alia*, to determine what causes fraudulent reporting, and what

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103 See Ikhazoboh, E.O. "The Corporate Audit Committee: Financial Risk Dimension" in Eguonu (ed) Board Room Management: A Book of Reading (Ikeja, Lagos: Slides Associates Ltd, 1994) p. 222.

104 It was named after its Chairman, James C. Treadway.

environmental factors are involved; define auditors role in preventing, detecting and reporting fraud; identify corporate structures and attitudes that contribute to the problems.[105]

In Nigeria, before 1990 only few companies voluntarily established either ad hoc or permanent audit committees. Section 359(3) however makes its establishment mandatory in Nigeria. As regards its structure, Section 359(4) states that:

> The Audit Committee shall consist of an equal number of directors and representatives of shareholders of the company (subject to a maximum number of six members) and shall examine the auditors' report and make recommendations thereon to the annual general meeting, as it may think fit.

The members are however not entitled to renumeration and are subject to re-election annually. And concerning the selection process, any member of the Committee may nominate a shareholder as a member of the committee by giving notice in writing of such nomination to the secretary of the company at least 21 days before the annual general meeting.[106] The CAMA showing a favourable disposition towards the small shareholders states that a poil shall not be demanded for the election of members of the Audit Committee.[107]

In terms of qualification, the CAMA is mute except that of directorship or shareholding membership. We think this is an untidy development. An important committee such as this ought to be constituted by members with proven tract records of verse knowledge in business, industry, financial

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105 Stated in Ikhazoboh, E.O. "The Corporate Audit Committee: Financial Risk Dimension" in Eguonu (ed) op. cit. at p. 222.

106 S.359(4) of the CAMA.

107 S. 225(3). of the CAMA

reporting as well as the regulatory framework of accounting and finance. We recommend that a clearly worded provision be inserted in the CAMA, as well as the BOFIA detailing qualification of Audit Committee.

The CAMA confers considerable authority on the Audit Committee. The Committee is not supposed to discharge the primary assignment of the Board or the auditors, though it has power to investigate any activity of the company that might be of interest to it. As have been noted the Committee has a wide scope of activities which are set out in the CAMA.[108] The general duty of the Audit Committee is to examine the auditors report and make recommendations thereon to the Annual General Meeting as it may think fit.[109] However, the specific objectives and functions of the Committee relates to:

(a) ascertaining whether the accounting and reporting policies of the company are in accordance with legal requirements and agreed ethical practices;

(b) reviewing the scope and planning of audit requirements;

(c) reviewing the findings on management matters in conjunction with the external auditor and departmental responses thereon;

(d) keeping under review the effectiveness of the company's system of accounting and internal control;

(e) making recommendations to the board in regards to the appointment, removal and renumeration of the external auditors of the company; and

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108 S. 359(6) of the CAMA.

109 S. 359(4) of the CAMA.

(f) authorize the internal auditor to carry out investigations into any activity of the company which may be of interest or concern to the communities.

Unlike the United Kingdom where no statutory function are fostered on the audit committee, the Nigerian company law, due to the peculiarly of the Nigerian situation prefer to thread a different pattern.

It must be noted that the existence of an audit committee does not diminish management primary responsibility for the financial statement and for operating the business, nor the external auditor's responsibility for independently attesting to the fair presentation of the financial statement in conformity with the CAMA and International Auditing Standards.

The chief purpose and advantage of the audit committee is to serve as a focal point for effective communication between non-committee directors, the external auditors, internal auditors and the management of the company; serve as the agent of the board of directors in ensuring the independence of the company's external auditors, the integrity of the management and the adequacy of disclosures to the company shareholders.[110]

It needs also to be stated that the corporate audit committee can also be a cause of conflict and misunderstanding between the committee, management and auditor. This is where the committee does not have well defined objectives and encroaches on management functions. Another situation is where the auditors discussion with the audit committee on matters

[110] See Ikhazoboh, E.O. Supra at p. 225.

bordering on accounting policies, internal control and financial reporting matters may show adversely on the performance of management and exposing it to criticism in the process. But it is submitted that even at that such problems can be avoided if the committee can adopt formal procedures such as: the Board of Management first approving a statement of the audit committee's purpose and specific responsibilities; representatives of management being present for discussion on items contained in the agenda which affect management; maintaining minutes for all committee meetings and distributing copies to members of the board, the chief executive officer, auditor and possibly other senior members of management of matters intended to be discussed.

8.9 THE LIABILITIES OF COMPANY AUDITORS

The need for the company auditors to be extra careful in the preparation of their audit report and financial statement is not unconnected with the value attached to an audit report by users of financial statements. The expectation is not without basis if it is considered that people invest their hard earned money in companies which they take no part in their management. Consequently, the attitude of the law is that in those established circumstances where the company auditor fails to discharge his auditing responsibilities arising from negligence resulting into misfeasance or the commission of a criminal act, the law must take its full course.

8.9.1 Liability in Negligence

Under the Common Law, the standard of care required of a company auditor is not an extremely high one. For instance, in *Maddison v. Miner,*[111] the court was of the view that the standard of care in cases involving professional negligence is the standard of knowledge, skill and care expected of a reasonable member of the auditing profession. This attitude can be explained by the fact that, on one hand, the auditor in the performance of his functions occupies a secondary and accessory position to the company director.[112] On the other hand, professionals are entitled to errors of judgement unless the error is of such a kind that no reasonably well informed and competent member of the profession in question could have made it. Thus in *Whitehouse v. Jordan,*[113] Fraswer J. stated the true position that:

> … an error of judgement may or may not be negligent; it depends on the nature of the error. If it is one that would not have been made by a reasonable, competent professional man professing to have the standard and type of skill that the defendant held himself out as having and acting with ordinary care, then it is negligent.

His lordships dictum should not be understood to mean that under the law the auditors implied duly to exercise reasonable degree of care and skill as a professional has been whittled down in any way. Thus an auditor will be liable in tort to his client for negligence. There are however conditions that must be

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111 (1991) GWD 402-459.

112 See Bingham, L.J. in Caparo Industries Plc v. Dickson & 6 Others (1990) 1 All E.R. 789 at 804.

113 (1981) 1 All E.R. 267.

met before the auditor can be found wanting for negligence. First, the plaintiff must establish that the auditor owed him a duty of care and skill. [114]

The second requirement is that the plaintiff must prove that the auditors breach of duty arose directly from his failure to exercise the standard of care contemplated by law. Thus where an auditor professes to be a financial expert or analyst as well, the standard expected of him will be that of an auditor and financial expert or analyst rather than simply that of an accountant who is practicing as an auditor. Thirdly, the plaintiff must prove that he incurred damage that flows directly and naturally from the auditors breach of duty.[115] The conditions must be established otherwise, a prospective plaintiff may be unable to recover damages.

The circumstances under which an auditor could be found liable are many. For instance, in *AGC Advances Ltd v. R. Lower Lippman Figdor & Frank,*[116] a company auditor failed to reconcile the figure in the accounts with the stock sheet total an did not qualify the audit stock. This therefore led to an over valuation which was adjudged significant. The court in that case held that the appropriate standard of care was the standard adopted by the Australian Society of Accountants and the Institute of Chartered Accountants. In that case, the auditors failed both standard as they did not attempt to reconcile the figure in the accounts. Similarly, in *Recity Equitable Fire Insurance Co,*[117]

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114 See Hedley Bryne & Co. v. Heller and Partners (1964) A.C. 465. But this case was not solely narrowed down to the auditing and accounting profession.

115 See the Wagon mound No. 2 (1967) AC 617. See also Caparo Industries Plc v. Dickman & Others. Supra where the court stated that the three basic elements which are requested to impose a duty on a company are (a) foreseability of damages (b) proximity of relationship (c) reasonable of imposing a duty. All these must be proved by a plaintiff.

116 (1991) 4 S.C.S.R. 337.

117 (1925) Ch. 467.

Romer, J. observed that an auditor who fails to make a personal inspection of securities that are in the custody of a person or a company with whom it is supposed to be would be liable for negligence. The Court of Appeal in the same case observed that the auditor has the overall responsibility to be careful of whom he trusts, whether it is the enterprise management or third parties who are separate from the enterprises management. An auditor would be adjudged to have breached his basic standard of care where he fails to detect fraudulent errors which are material and could have been reasonably detected by normal audit procedures.

It would seem that the 1896 case of *Re-Kingston Cotton Mills Co. (No. 2),*[118] represent the era when the standard of reasonable care and skill was less exacting. In the case, auditors had relied on directors' certificates which turned out to be deliberately false. Curiously, the Court of Appeal held that it was not the duty of company auditors to take stock, and that being the case, they incurred no liability if they rely on directors certificate of closing stocks since a director was a person whom the law adjudged as being competent and reputable. In fact the current United Kingdom auditing standard and guidelines prescribes a much more exacting standard than that the Re-Kingston Cottons era. In the United Kingdom auditing guidelines permit auditor's attendance at stokctakings.[119] It states that if an auditor wishes to rely on management stocktaking in cases where stock are of primary importance to an enterprise financial statements, the auditor should endeavour to attend the stocktaking

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118 Supra.

119 This is stated in para. 8 of the U.K. Auditing Standard and Guidelines.

by way of providing audit evidence. In consonance with this reasoning therefore, it appears the auditors in Re-Kingston Cottons Mills would have been expected to perform more audit testing to be in a safe position to either rebut or confirm the certificate of closing stock prepared by the enterprise's management.

It was not therefore surprising that *Re-Thomas Gerrard & Son Ltd.*[120] had to be decided differently even though it shared the same factual situations with *Re-Kingston Cotton Mills.* In the instance case, the managing director had falsified the accounting book of the company. The court was of the opinion that rather than relying on the directors' certificate, the auditor should have in accordance with the auditing guidelines on evidence of U.K. have subjected the certificate to serious testing before deciding whether the profit or loss account was materially correct. Acknowledging that a lot of changes has taken place with regards to the publics expectation of the modern day company auditor between 1896 and 1968, Penny Curt, J. had no difficulty in holding the auditor negligent. A notable aspect of his lordships judgement is as follows:

> If the directors do not allow auditors time to conduct… investigations as are necessary in order to make those statements (i.e. the audit reports), the auditor must… either refuse to make a report at all or make an appropriately qualified report. They cannot be justified in making a report containing a statement the truth of which they had not had an opportunity of ascertaining.[121]

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120 Supra.

121 Ibid at p. 477.

Implicit in the above remark therefore is that the auditors could only have escaped liability in negligence if they had for instance checked the statements of the suppliers which would have enabled them to discountenanced the purchase figures falsely stated in the profit and loss accounts.

It would therefore appear that the most apt explanation which one can offer in the light of the foregoing cases is that two propositions have emerged and the first is that the courts no longer rely solely on the Common Law standard of care in order to determine questions of liabilities of company auditors. It would also seem that in order to establish the legal standards expected from an auditor the court would have recourse to current prescribed standards and guidelines practiced by the auditing profession. Secondly, that professional standards of care are not static, they evolve with time. And in assessing the auditors conduct in line with the legal standard of care, innovations and technical developments within the auditing industry may be considered.

At this juncture, it would be important to examine the actual scope of the auditors' liability for negligence. First, in relation to shareholders of the company. It is now firmly established in line with the corporate personality principle that the interest of the body of shareholders of a company is inseparable from the interest of the company itself in the management of the affairs of the company and consequently, it is the company itself i.e. the body of the shareholders that the auditors owes a duty of care and not individual shareholders. In fact, the auditors client is the company, thus implying that no

individual shareholder is entitled to legal protection from the auditor. So it would seem that the case of *Hedley Bryne & Co. v. Hellers and Partners*,[122] where the House of Lords held that professionals including accountants and auditors owes a duty of care to third parties for any financial injury suffered in reliance of auditors negligent professional opinion, if they fail to exercise reasonable care is no longer good law. The judgement in the *Caparo Industries case* changed all that. An attempt to canvas the argument that a shareholder is entitled to rely on the auditors report as an investor of the company and therefore sue for damages in the event of negligence was roundly rejected by the House Lords in the *Caparo Industries case*. Because of the importance of the case, since it represents the current legal position on the scope of auditors liability for negligent statements, it will not be out of place to give a concise but lucid account of the facts of the case. The issue in the case emanates from the take over in 1984 of *Fidelity PLC by Caparo Industries PLC* which were both listed companies. The action was brought against two directors of Fidelity PLC and the auditors who audited the accounts of the company for March 31st 1984. *Caparo Industries PLC* in taking over *Fidelity PLC* relied on the accounts that was audited by the auditors of an internationally reputable Chartered Accounting firm called *Fouche Ross*. The successful take over highly depended on the audited accounts of Fidelity Plc which showed a pre tax profit of £1.3m instead of at least 400,000 pounds. The plaintiff's contention was that if he had known of the true facts, he would

122 Supra.

not have made a bid for Fidelity Plc. Caparo further alleged that in carrying out their auditing functions, the auditors owed a duty of care to investors in the form of existing shareholders and to potential investors including Caparo Industries. In considering the issue of duty of care, the court held that the auditors owed no duty of care to Caparo Industries either as an existing shareholder or as a potential investor. In the Appeal Court, it was the unanimous view of the court that there was no duty of care between an auditor and potential investors in a company, but held that an auditor owed a duty to Fidelity existing shareholders. On further appeal however, the House of Lords emphatically adopted the judgement of the court of first instance by holding that there was no duty of care on the part of an auditor either to existing shareholders or potential investors. Thus, if an individual shareholder while either selling or retaining share in the company relied on accounts that had been negligently prepared by a company external auditor, no liability will arise on the part of the company auditor. It is submitted that this was quite an unfortunate decision, as it displays copious insensitivity to the plight of existing and potential investors in companies. One would have thought that the court would have drawn a distinction between ordinary negligence and gross negligence for purposes of determining the liability of auditors as is obtainable in homicide cases in criminal law.

It is therefore submitted that considering the unsatisfactory performance of the company external auditor a provision should be inserted in the CAMA to make him liable for gross negligence where his conduct shows

insensitivity and complete disregard to the shareholders, investors, creditors and potential investors. There is consensus in this regard. For instance, the continued limitation of auditor's duty of care to a single body of shareholders has been vehemently opposed by a notable scholar.[123] He explains his dissatisfaction in these terms.

> … This limitation of duty to shareholders as a single body can produce anomalous results in purely economic terms. Contrast the founder shareholder who holds on to shares and paid little or no regard to the financial management of the enterprise with the shareholder who buys shares at a price inflated as a result of audit negligence and who sells the share after its discovery (and subsequent drop in share price) but before any action is instituted. If it was subsequently decided that the auditors were negligent and that the company should be compensated, would that founder shareholder not be enriched by the companies successful suit against the auditors at the expense of the (remediless) shareholder who sold? It can hardly be argued that the founder shareholder relied on the audit reports and it is difficult to see what economic loss the auditor's negligence has caused him …

The spirit and rationale of the principle in *Caparo Industries* later influenced the court's decision in *El-Nakib investments (Jersey) Ltd. v. Longsoft*.[124] When Mervyn Davies J. held that the defendants directors did not owe a duty of care to the plaintiffs who purchased shares by relying on a prospectus issued and distributed by the defendant company to the shareholders in connection with an invitation to take up one share in a subsidiary for every five shares in the parent company. Though the defendants were directors, it is doubtful if a different conclusion would have been reached

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123 See Suzanie Chua, "The Auditors Liability in Negligence in respect of the Audit Report" (1995) Journal of Business Law, p. 1.

124 (1990) 2 W.L.R. 1390.

by the courts if they were auditors. These decisions though unfortunate are in tune with the position of the law which does not impose on an auditor a duty of care to a member of the public who is a potential investor. Cardozo C.J. restated this position when he said that the law does not impose on the auditor "Liability in an indeterminate amount for an indeterminate time, to an indeterminate class" in the American case of *Ultramares Corporation v. Youche.*[125] However, it would seem that in very extreme situations the potential investor may be able to impose a legal duty on a negligent auditor. Such extreme cases are the ability of the plaintiff to prove that the defendant offering the advice was fully aware of the plaintiff and of the transaction which the plaintiff contemplated.[126] Although the potential investor may be able to establish forseability on the part of the defendant auditor, he may run foul of the second arm of the test formulated in the Caparo Industries case which states that apart from forseability, the plaintiff must as well prove proximity between him and the auditor. So, both foreseability and proximity are separate considerations. Again, where a defendant makes a strong representation verbally or documentarily with the clear intention that the potential investor should rely on the piece of information contained in it, and the potential investor did rely on it, a duty of care will arise on the part of the auditor (it could as well be a director or financial adviser). This was the situation in *Morgan Crucibles v. Hill Samuel and Others*.[127] In the case, the defendants

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125 (1931) 255 N.Y. Rep. 170 at 174.

126 See Caparo Industries Plc. v. Dickman, Supra.

127 (1991) 1 All E.R. 148 at 159.

who were directors and financial advisors of the target company, in a takeover bid made representations in a series of documents meant for use by shareholders of the target company and it happened that one of the documents contained "continuing representations" on the part of the defendant that the plaintiff should use and rely on them in deciding whether to takeover the target company. The plaintiff made use of the piece of information contained in the document to his detriment. At the Court of Appeal, Slade L.J. overruled the Hoffman J. decision in the Lower Court that there did not exist sufficient proximity between the defendants and the plaintiff to give rise to a duty of care. His lordship inferred that where there is continuing representations which shows that the potential investor should rely on it and was indeed relied on, a duty of care would arise. It is to be noted that the potency of this case springs from the fact that it comes after the decision in the Caparo Industries case.

It has also been established that before a third party can succeed in an action for negligence against an auditor, it must be proved that the auditor contemplated not only the particular and identified recipient of the information but also the known purpose for which the auditors would foresee that the information would be depended on. The principle applies equally in relation to creditors. As in others, sufficient proximity between an auditor and creditors is the basis of liability on the part of an auditor.[128] Where this is the case, there would be no justification for denying the plaintiff a fruitful cause of action.

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[128] See Al-Sauli Banque and Others v. Clark Pixly (A Firm) (1990) in L.R. 344.

In *AGC (Advance) Ltd. v. R. Lowelippman Figdor and Frank (An Austrian case),*[129] the plaintiff finance company before granting credit facilities to a company (L) requested for the statement of accounts of the company from the auditor. The auditor in doing so failed to reconcile the figures in the accounts with the stock total nor did he qualify the audit report. The result was that there was an over valuation in the financial strength of the company. Vinellet J. held and rightly, it is submitted that a duty of care arose.

Under Nigerian law Section 368 of the CAMA has codified the common law principles governing the liability of a company auditor arising from negligence as a result of breach of duty of care. Section 368 states that a company auditor shall in the performance of his duties exercise all such care, diligence and skill as is reasonably necessary in each particular circumstance and where a company suffers loss or damage due to the failure of its auditor to carry out his fiduciary duty, the auditor is liable for negligence against him. But where the auditor for whatever reason fails to do so any member of the company may commence an action for negligence against the auditor.

Evident in the CAMA provision is the fact that it is merely an adoption of the common law principle that the auditor is only liable to company, that is the general body of the shareholders and not to individual shareholders, existing and potential investors, nor creditors. It is submitted that considering the peculiar Nigerian situation, Section 368 should be amended to make auditors liable in tort.

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129 (1991) 1 SCSR 337 Supra.

8.9.2 Liability for Misfeasance and Crimes

The company auditor is also liable for misfeasance under Section 508 of the CAMA. The section governs the prosecution of delinquent officers and members of the company generally. Liability arises in the course of winding up if it appears that such officers are guilty of misfeasance.

Section 508 in parts provides that:

(1) If it appears to the court in the course of a winding up by, or subject to the supervision of the court that any past or present officer or any member of the company has been guilty of an offence in relation to the company for which he is criminally liable, the court may, either on the application of any person interested in the winding up or of its own motion direct the liquidator to refer the matter to the Attorney-General of the Federation.

(2) If it appears to the liquidator in the course of a voluntary winding up that any past or present officer, or any member of the company has been guilty of any offence in relation to the company for which he is criminally liable, he shall forthwith report the matter to the Attorney-General of the Federation and shall furnish him such information and give to him such access to any facilities for inspecting and taking copies of any documents, being information or documents in the possession or under the control of the liquidator and relating to the matter in question, as he may require.

As the provision clearly shows the institution of criminal proceedings is the preserve of the Attorney-General. He also has the right to decline prosecution under the section. The Attorney-General is empowered to solicit the assistance of the liquidator, officers and agents for purpose of prosecution.[130] It is an offence for such officers to decline or refuse to provide assistance.[131] But it would appear that the company auditor may obtain relief where he had acted honestly and reasonably. The section embodies the power of the court to grant relief in certain situations where an officer of a company or a person employed as an auditor by a company is guilty of negligence, fraud or any other breach of duty, or trust but found to have acted honestly and reasonably. The relief may be partial or complete depending on the court's discretion.

The CAMA also criminalizes the conduct of the auditor in relation to falsification of books of account under Section 435 of the Criminal Code. The section provides thus:

Any person who –

(1) being a director or officer of a corporation or company, receives or possess himself as such of any of the property of the corporation or company otherwise than in payment of a just debt or demand, and with intent to defraud, omits either to make a full and true entry thereof in the books and accounts of the corporation or company, or to cause or direct such an entry to make therein; or

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130 S. 508(5) of the CAMA.

131 S. 508(6) of the CAMA.

(2) being a director, officer, or member of a corporation or company, does any of the following acts with intent to defraud –

(a) destroys, alters, mutilates or falsifies, any book, document valuable security, or account, which belongs to the corporation or company, or any entry in any such book, document, or account, or is privy to any such act; or

(b) makes or is privy to making any false entry in any such book, document or account; or

(c) omits or is privy to omitting any material particular from any such book, document or account;

is guilty of a felony, and is liable to imprisonment for seven years.

Similarly, the Penal Code[132] provides for the same offence along the same line except that the punishment is "imprisonment for a term which may extent to seven years or with fine or with both". Under the above provisions,[133] the ingredients of the offence must be proved beyond reasonable doubt.

It is submitted that an auditor is within the scope or contemplation of Section 435 of the Criminal Code and Section 371 of the Penal Code respectively since he is an officer of the company.[134] The basis for liability on the part of the auditor would be where he deliberately "swell up accounts to exaggerate the profits" of the company.[135] It would amount to falsification

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132 S. 371 of the Penal Code.

133 i.e. S. 435 Criminal Code and S. 371 of the Penal Code.

134 S. 357 of the CAMA; Shonowo v. Adebayo, Supra, Ss. 502, 504, 507, 508 of the CAMA.

135 See Ofori-Amankwah, E.H., Criminal Law in the Northern States of Nigeria (Zaria: Gaskiya Corp. Ltd.

where an auditor deliberately swells up accounts to cover loses incurred by a company. Any form of suppression of accounts or documents by an auditor would also be punishable. It would also seem that it is not material whether the falsification is made with the intention to acquire personal gain or not. What is important is that the falsification is detrimental to the collective interest of the shareholders of the company.

The obvious shortcoming noticed in both the Criminal Code and the Penal Code provisions is the requirement to establish "intent to defraud". We hereby maintain that fraud is not easily established. It is therefore submitted that it would be more preferable to reduce the *mens rea* to "knowingly and recklessly" falsifying the company's document instead of with "intent to defraud". The words "intent to defraud: should be deleted from the provisions of Sections 435 and 371 of the Criminal Code and Penal Code respectively. Otherwise it remains a potent obstacle capable of hindering successful prosecution of errant auditors.

As we have consistently maintained, the role of the company auditor in every economy cannot be overemphasized. This uncontrolled falsification and distortion of corporate reports will continue to result into accommodation of hidden losses or profits and ultimately leads to corporate collapse and bankruptcy. In a developing economy such as Nigeria where Nigerians are still struggling to imbibe the investing habit corporate collapse engendered by falsification or inaccuracies in audit report will certainly inhibit both local and foreign investment in Nigeria.

We have seen that despite the attitude of the existing legal regime in ascribing to the auditor some measure of independence in the discharge of his functions, the auditor has been unable to live up to his potential as well as the expectation of the public. One possible explanation for this is that apart from cases of collusion, the auditor is still at the mercy of management. To guarantee the auditors complete independence, apart the various duties imposed on them, they need fresh statutory and judicial empowerment in view of the magnitude of corporate distress and failure of late. It is in this respect that we consider the decision in the *Caparo Industry PLC v. Dictman & Co;* an unfortunate development. We urge that Nigerian courts should as a matter of policy refuse to be persuaded by the ratio in that case taking into cognizance the peculiar Nigerian circumstances of late specially the distress syndrome.