COURSE GUIDE

CLL801
CORPORATE LAW, MANAGEMENT AND FINANCE (ADVANCED CORPORATION LAW) I

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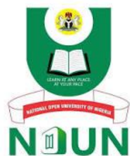

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INTRODUCTION

A registered company is one of the means of doing business. Once registered, the company obtains the status of a legal person. It can enter into contracts; own properties and it can sue and be sued in its own name. As a business entity with artificial personality, its operations and activities are executed on its behalf by the appointed management personnel, who are supervised by a board. The board supervises the management to ensure that they carry out their duties effectively in compliance with the relevant regulations.

There is a web of interests in a corporation. The role of the management board is to promote the economic success of the corporation to ensure that the interests attached to the corporation are ultimately satisfied. This is usually a challenge, since the interests rank differently. For example, shareholders claim to be the predominant beneficiaries of the economic success of a company because they are the equity investors. Creditors make similar claims as debt capital investors. Other stakeholders include employees, customers, suppliers, the community and government.

The extent to which corporate entities can finance their investment opportunities and the role of the management board largely determines the economic success of the corporation. Hence, the modern corporation is now required to observe some relevant governance regulations which is distinct from the traditional rules that govern the incorporation of a company and the ways in which the corporation is to be administered. These governance rules are mainly concerned with corporate accountability, financial and non-financial reporting. This is aimed at ensuring that management boards are not merely complying with the rules of establishing and running a company, but that they are also being made responsible for showing how their policies are promoting corporate value in a responsible way. It ultimately depicts the role of corporate managements as agents of accountability.

WORKING THROUGH THIS COURSE

To complete this course, you are advised to read the study units, recommended books, relevant cases and other materials provided by NOUN. Each unit contains a Self-Assessment Exercise, and at points in the course you are required to submit assignments for assessment purposes. At the end of the course there is a final examination. The course should take you about 13 weeks to complete. You will find all the components of the course listed below. You need to make out time

COURSE MATERIALS

The major components of the course are.

a) Course guide.
b) Study Units.
c) Textbooks
d) Assignment file/Seminar Paper
e) Presentation schedule.

MODULES AND STUDY UNITS

There are six (6) modules. They are made up of twenty-four (24) units of study.

Module 1 Nature of Corporate Entities

Unit 1 The Separate Legal Personality Doctrine and its Limitations
Unit 2 Basic Objectives and Policies Underlying Company Legislation
Unit 3 Challenges of Incorporation

Module 2 The Company Constitution (comparative – UK / Nigeria)

Unit 1 Company Constitution I
Articles and Memorandum of Association
Unit 2 Company Constitution II
Resolutions and Shareholder Agreement
Unit 3 Limitations of Shareholder Democracy

Module 3 Management Powers and Responsibilities (Comparative)

Unit 1 Directors' Duties
Unit 2 Scope of Directors' Duties
Unit 3 Remedies / Liabilities for Breach of Directors' Duties
Unit 4 Ratification of Breach / Relief by the Court

Module 4 Dividends and Minority Shareholder Protection

Unit 1 Register of Members
Unit 2 Dividend
Unit 3 Shareholder Residual Management Role
Unit 4 Majority Rule & Minority Protection

Module 5 Corporate Governance

Unit 1 Meaning and Theories of Corporate Governance
Unit 2 Structure of Corporate Management
Unit 3 Approaches to Corporate Governance Regulation
Unit 4 Board Effectiveness
Unit 5 Corporate Scandals and Failures

Module 6 Mergers, Acquisitions and the Market for Corporate Control

Unit 1 Types of Acquisitions and Theories of Mergers and Acquisitions
Unit 2 Mechanisms for Corporate Acquisition
Unit 3 The Regulatory Framework for Corporate Acquisitions in Nigeria
Unit 4 Takeover Hypothesis
Unit 5 Managerial Defences

All these Units are demanding. They also deal with basic principles and values, which merit your attention and thought. Tackle them in separate study periods. You may require several hours for each.

We suggest that the Modules be studied one after the other, since they are linked by a common theme. You will gain more from them if you have first carried out work on the law of contract. You will then have a clearer picture into which to paint these topics. Subsequent units are written on the assumption that you have completed previous Units.

Each study unit consists of one week's work and includes specific Learning Outcomes, directions for study, reading materials and Self-Assessment Exercises *(SAE).* Together, these exercises will assist you in achieving the stated Learning Outcomes of the individual units and of the course.

REFERENCES – FURTHER READING

Certain books have been recommended in the course. You should read them where so directed before attempting the exercise.

ASSESSMENT

There are two aspects of the assessment of this course, the Tutor Marked Assignments and a written examination. In doing these assignments you are expected to apply knowledge acquired during the course. The assignments must be submitted to your tutor for formal assessment in accordance with the deadlines stated in the presentation schedule and the Assignment file. The work that you submit to your tutor for assessment will count for 30% of your total score.

SELF-ASSESSMENT EXERCISES

There is a self-assessment exercise at the end for every unit. You are required to attempt all the assignments. You will be assessed on all of them, but the best three performances will be used for assessment. The assignments carry 10% each. Extensions will not be granted after the due date unless under exceptional circumstances.

FINAL EXAMINATION AND GRADING

The duration of the final examination for this course is three hours and will carry 70% of the total course grade. The examination will consist of questions, which reflect the kinds of self-assessment exercises and the tutor marked problems you have previously encountered. All aspects of the course will be assessed. You should use the time between completing the last unit and taking the examination to revise the entire course. You may find it useful to review yourself assessment exercises and tutor marked assignments before the examination.

COURSE SCORE DISTRIBUTION

The following table lays out how the actual course marking is broken down.

Assessment	**Marks**
Assignments 1-4 (the best three of all the assignments submitted)	Four assignments. Best three marks of the four counts at 30% of course marks.
Final examination	70% of overall course score
Total	100% of course score.

COURSE OVERVIEW AND PRESENTATION SCHEDULE

Module / Unit	Title of Work	Weeks Activity	Assessment (End of Unit)
Course Guide			
MODULE 1	NATURE OF CORPORATE ENTITIES		
Unit 1	The Separate Legal Personality Doctrine	1	Assignment 1
Unit 2	Basic Objects and Policies Underlying Company Legislation	2	Assignment 2
Unit 3	Challenges of Incorporation	3	Assignment 3
MODULE 2	THE COMPANY CONSTITUTION IN THE UK AND NIGERIA		
Unit 1	Company Constitution I	4	Assignment 4
Unit 2	Company Constitution II	4	Assignment 6
Unit 3	Limitations of Shareholder Democracy	5	Assignment 7
MODULE 3	MANAGERIAL POWERS AND RESPONSIBILITIES	6	Assignment 8
Unit 1	Directors' Duties	6	Assignment 9
Unit 2	Scope of Directors' Duties		
Unit 3	Remedies/Liabilities for Breach of Directors' Duties		
Unit 4	Ratification of Breach/Relief by the Court		
MODULE 4	DIVIDENDS AND MINORITY SHAREHOLD PROTECTION		
Unit 1	Register of Members		
Unit 2	Dividend	8	Assignment 12
Unit 3	Shareholder Residual Management Role		
Unit 4	Majority Rule and Minority Protection		
MODULE 5	CORPORATE GOVERNANCE		

Unit 1	Meaning and Theories of Corporate Governance	9	Assignment 15
Unit 2	Structure of Corporate Management	10	Assignment 16
Unit 3	Approaches to Corporate Governance Regulation		
Unit 4	Board Effectiveness		
Unit 5	Corporate Scandals and Failures	10	Assignment 17
MODULE 6	MERGERS, ACQUISITIONS AND THE MARKET FOR CORPORATE CONTROL		
Unit 1	Types of Acquisitions and Theories of Mergers and Acquisitions	9	Assignment 15
Unit 2	Mechanisms for Corporate Acquisition	10	Assignment 16
Unit 3	The Regulatory Framework for Corporate Acquisition in Nigeria	10	Assignment 17
Unit 4	Takeover Hypothesis		
Unit 5	Managerial Defences		

HOW TO GET THE MOST FROM THIS COURSE

In distance learning, the study units replace the lecturer. The advantage is that you can read and work through the study materials at your pace, and at a time and place that suits you best. Think of it as reading the lecture instead of listening to a lecturer. Just as a lecturer might give you in-class exercise, you study units provide exercises for you to do at appropriate times.

Each of the study units follows the same format. The first item is an introduction to the subject matter of the unit and how a particular unit is integrated with other units and the course as a whole. Next is a set of learning objectives. These objectives let you know what you should be able to do by the time you have completed the unit. You should use these objectives to guide your study. When you have finished the unit, you should go back and check whether you have achieved the objectives. If you make a habit of doing this, you will significantly improve your chances of passing the course.

Self-Assessment Exercises are interspersed throughout the units. Working through these tests will help you to achieve the objectives of the unit and prepare you for the assignments and the examination. You should do each Self-Assessment Exercise as you come to it in the study unit. Examples are given in the study units. Work through these when you have come to them.

TUTORS AND TUTORIALS

There are 15 hours of tutorials provided in support of this course. You will be notified of the dates, times and location of the tutorials, together with the name and phone number of your tutor, as soon as you are allocated a tutorial group. Your tutor will mark and comment on your assignments. Keep a close watch on your progress and on any difficulties you might encounter. Your tutor may help and provide assistance to you during the course. You must send your Tutor Marked Assignments to your tutor well before the due date. They will be marked by your tutor and returned to you as soon as possible.

Please do not hesitate to contact your tutor by telephone or e-mail if:

- You do not understand any part of the study units or the assigned readings.
- You have difficulty with the self-assessment exercises.
- You have a question or a problem with an assignment, with your tutor's comments on an assignment or with the grading of an assignment.

You should try your best to attend the tutorials. This is the only chance to have face to face contact with your tutor and ask questions which are answered instantly. You can raise any problem encountered in the course of your study. To gain the maximum benefit from course tutorials, prepare a question list before attending them. You will gain a lot from participating actively.

MAIN COURSE

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MODULE 1 NATURE OF CORPORATE ENTITIES

Unit 1 The Separate Legal Personality Doctrine and its Limitations
Unit 2 Basic Objectives and Policies Underlying Company Legislation
Unit 3 Challenges of Incorporation

Unit 1 The Separate Legal Personality Doctrine and Its Limitations

Unit Structure

1.1 Introduction
1.2 Intended Learning Outcomes
1.3 Characteristics of a Company
  1.3.1 Perpetual Succession
  1.3.2 Company Sue and be Sued in Its Corporate Name
  1.3.3 Company can Acquire Assets in Its Name
  1.3.4 Company can Execute Contracts
1.4 Limitation of the Separate Legal Personality Doctrine
  1.4.1 Lifting the Veil under Statute
  1.4.2 Piercing the Veil under Common Law
1.5 Tortious and Criminal Liability of the Company (Roles of Attribution)
  1.5.1 Tort
  1.5.2 Criminal Liability
1.6 Summary
1.7 References/Further Readings/Web Resources
1.8 Possible Answers to Self-Assessment Exercise(s)

1.1 Introduction

When a company is registered, it becomes a body corporate and assumes a separate identity, distinct from that of its shareholders and its officers. *The Companies and Allied Matters Act 2020* (CAMA)s 42, provides:

> *As from the date of incorporation mentioned in the certificate of incorporation, the subscriber of the memorandum together with such other persons as may, from time to time, become members of the company, shall be a body corporate by the name contained in the memorandum, capable forthwith of exercising all the powers and functions of an incorporated company including the power to hold land, and having perpetual succession and a common seal, but with such liability on*

> *the part of the members to contribute to the assets of the company in the event of its being wound up as is mentioned in this Act.*

The registered entity becomes capable of acquiring properties in its own rights by becoming an artificial person. It is able to do most things that a natural person of contractual capacity could do. It enters into contracts; it conducts business and incurs debts in its own name. This principle of corporate personality which was developed in *Salomon v Salomon & Co Ltd* (1897) AC 22 is the foundation upon which company regulation is built. Is there any limit to the capacity of the company to act or to do things a natural person could do?

There are certain benefits and challenges of incorporation. Individuals who intend to establish a company because of its benefits must also consider the challenges, especially the requirement to comply with the relevant regulations. It is also important to consider the types of companies to be registered and whether the company would be a group of companies. In the same way that a company deals with third parties (outside the company) in its own name, it also enters into contracts with its shareholders, the company officers and employees in its own capacity. Does it accord with common sense to suppose that the contractual relationship between the company and its shareholders or directors or officers could be at arm's length?

1.2 Learning Outcomes

By the end of this unit, you will be able to:

- discuss the characteristics of an incorporated company;
- analyse the limitations of the separate legal personality doctrine;
- evaluate tortious and criminal liability of the company and rules of attribution.

1.3 Characteristics of an Incorporated Company

1.3.1 Perpetual Succession

The company may live on in perpetuity. The death or bankruptcy of a member of a company does not affect the life or continuous existence of the company. The company outlives the shareholders as members. Can you think of situations capable of constituting any limitation to the supposition or notion that companies are capable of indefinite duration or interminable existence?

1.3.2 Company can Sue and be Sued in Its own Name

A company can take legal action in its own name against any person or against another company. Legal actions can also be taken against the company using the company's name. Also, the company can enter into contracts in its own name and the benefits and obligations arising from the contracts belong directly to the company and not to the members or officers of the company.

1.3.3 Company Can Acquire Assets in Its Name

The company can acquire properties in its own name, for example, in *Macaura v Northern Assurance Co [1925] AC 619* Macaura (M) ran a sole business as a timber merchant. He had also insured the properties of the business against fire in his own name. He later incorporated a company in which he had a majority shareholding and transferred the business to it. He did not transfer the insurance policy to the new company, the insurance policy remained in his name. The properties of the company were destroyed by fire and M sought to recover from the insurance company. It was held that M could not recover the losses from the insurance company since the property covered by the policy belonged to the company and the insurance policy was taken in his own name.

1.3.4 Company can Contract with Employees directly, including Its Members

In *Lee v Lees Air Farming Ltd [1961] AC* 12, the majority shareholder of the company who was also a director, was held to be an employee of the company for the purposes of a life insurance contract after he died while working for the company. Similarly, in *Secretary of State v Peter Bottrill [1999] BCC 177*, it was held that a sole shareholder/director of a company may be regarded as an employee of the company for the purposes of recovering a redundancy payment under an employment contract.

1.4 Limitations of the Separate Legal Personality Doctrine

The separate legal personality doctrine generally applies to every company upon registration in default. However, there are circumstances where the doctrine may be inapplicable. The objective of the inapplicability of the doctrine is mainly to identify relevant persons for purposes of potential liability for acts done in contravention of established regulations. This could either be breach of statutory provisions or common law rules. In certain exceptional circumstances, the doctrine may be made inapplicable to simply identify individuals

liable in certain ways to the company. These circumstances are briefly examined below.

There are two main ways of piercing the veil of incorporation, statutory piercing and piercing under common law rules. It can be forcefully argued that statutory piercing and common piercing are two tended towards the end and therefore are not mutually exclusive. Do you agree with this thinking? What are your thoughts?

1.4.1 Lifting the Veil under Statute

Statutory piercing occurs when the veil of incorporation is made to be inapplicable in compliance with a relevant statuary provision. This is mainly aimed at protecting the overall interests of the company where it is necessary to do so.

1) Wrongful Trading

When a director engages in wrongful trading, the director and any other officers involved in the activities of the company may be held liable to contribute to the liabilities of the company if the company becomes insolvent. Wrongful trading occurs when in the course of insolvency, a director or relevant officer of a company continue to carry on the business of the company in a reckless manner, i.e., when s/he knows or ought to have known that there is no reasonable prospect that the company would avoid insolvent liquidation. While directors are not prevented from trading and carrying on the business of the company at difficult times, they are responsible for ensuring that the liability of the company does not increase unjustifiably as a result of the negligence or recklessness of the directors. *See CAMA s 673*

2) Fraudulent Trading

If in the course of winding up a company, directors carry on the business of the company with the intention to defraud creditors, every officers of the company who was involved in the trading would be liable to contribute to the liabilities of the company. *See CAMA s 672*. To establish fraud, it must be shown that the directors have acted dishonestly. For example, it was held in *Re William C Leitch Bros Ltd* [1932] 2Ch 71 that fraud would likely be established where directors incur credit without any justifiable reason for believing that the creditors would ever be paid. Further, third parties who were involved in the fraud and benefited from the transaction(s), knowingly, may also be liable to contribute to the assets of the company – see *Re BCCI, Banque Arabe v Morris* [2001] 1 BCLC, 263.

3) Breach of other relevant provisions of CAMA

In certain circumstances, failure to comply with the provisions of the *Companies and Allied Matters Act 2020,* may lead to a disregard of the corporate veil. Non-compliance could either require the delinquent directors or officers to contribute to the assets of the company or to pay a fine or imprisoned. For example, directors and officers of a company would be liable for the debt incurred by a company, if they carry on business without the required number of members. Section 118 provides that,

> *If a public company or a company limited by guarantee 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 with only one or no member shall be liable jointly and severally with the company for the debts of the company contracted during that period.*

Also, the promotors, directors and/or officers would be liable to contribute to the assets of the company if they misapplied or retained company funds. What other section(s) of CAMA 2020 made provisions for liability of promoters? Section 674(1) provides that,

> *If, in the course of winding up a company, it appears that any person who has taken part in the formation or promotion of the company, or any past or present director, manager or liquidator, or any officer of the company, has misapplied or retained or become liable or accountable for any money or property of the company, or been guilty of any misfeasance or breach of duty in relation to the company which would involve civil liability at the suit of the company, the Court may, on the application of the official receiver, liquidator, creditor or contributory, examine into the conduct of the promoter, director, liquidator or officer, and compel him to repay or restore the money or property or any part thereof respectively with interest at such rates as the Court deems just, or to contribute such sum to the assets of the company by way of compensation in respect of the misapplication, retainer, misfeasance or breach of trust as the Court deems just*

Other relevant provisions of the Act do not require contributions to be made to the company, rather, the delinquent officers would be identified

and prevented from hiding under the corporate veil. They may be convicted and fined or imprisoned. This include, failure to cooperate with liquidators, for example, withholding company properties from the control of the liquidator, falsification of the books and account of the company. See CAMA ss 668-671.

4) Other Statutory Provisions

The corporate veil may also be disregarded where there is reasonable ground to do so. The veil may be lifted to aid a statutory body in its investigative powers. For example, The Economic and Financial Crimes Commission EFCC, is empowered under the *EFCC Act 2004,* s 7, to carry out investigation on the activities of a corporate entity where there is reasonable grounds to believe that financial crime has been committed. The Act also empowers the commission to enforce the provisions of other relevant Acts. *Section 7 (1).* Can you at this point attempt to identify the differences, if any, between enforcing the provisions of other relevant enactments as against piercing the corporate veil while discharging this duty of enforcement?

The Commission has power to –

a) cause investigations to be conducted as to whether any person, corporate body or organisation has committed any offence under this Act or other law relating to economic and financial crimes

b) cause investigations to be conducted into the properties of any person if it appears to the commission that the person's lifestyle and extent of the properties are not justified by his source of income;

Section 7 (2)

The Commission is charged with the responsibility of enforcing the provisions of –

a) the Money Laundering Act 2004; 2003 No.7 1995 N0. 13

b) the Advance Fee Fraud and Other Fraud Related Offences Act 1995;

c) the Failed Banks (Recovery of Debts) and Financial Malpractices in Banks Act 1994, as amended;

d) The Banks and other Financial Institutions Act 1991, as amended; and

e) Miscellaneous Offences Act

f) Any other law or regulations relating to economic and financial crimes, including the Criminal code or penal code

g) Common Law Piercing

1.4.2 Piercing under Common Law

The corporate veil may also be pierced by reference to certain common law rules. These rules were developed by the court over the years to aid in the identification of particular circumstances when it may be justifiable to invoke the principle and disregard the corporate veil to identify the persons behind the veil.

1) Fraud/Evasion

The corporate veil may be lifted where the company has been set up to defraud third parties, to evade liabilities or where the company was particularly set up as a sham or façade. In *Trustor AB v Smallbone* (No. 2) [2001] 2 BCLC 436, a company was used as a façade to commit fraud. S as MD of the claimant company transferred the equivalent of £39 Million from the claimant's account into the account of Introcom Ltd., a company owned by him. It was held that S was personally, along with Introcom, liable to refund the money to the claimant.

Further, the corporate form can be disregarded, if it is used to evade an existing and binding legal or contractual obligation. In *Gilford Motor Co v Horne* [1933] Ch. 935, the employee Horne, undertook in his contract not to solicit the customers of the claimants, his employer if he left their employment. He left his employers and formed a company with his wife and the company went about soliciting the customers of the claimants. Held: That the claimants were entitled to enforce the agreement against H and his company; that the company was a sham used by Horne. Also, in *Jones v Lipman* [1962] 1 All ER 442, the defendant Lipman, L entered into a contract to sell land to the claimant Jones J. L however sold the land to another person. To avoid specific performance of the contract with J, L formed a new company and transferred the land to it. It was held that L and his company were bound to perform the contract with J. The company which he purported to transfer the land to, was a sham, merely used to cover his contractual obligation to J.

2) Emergency

The corporate veil may be lifted in the interests of national security or any emergency situation. In *Daimler Co. v Continental Tyre Co Ltd* [1916] 2 AC 307, the claimant company was owed some money by the defendant company during WW1. The UK was at war with Germany at that time. Both companies were registered in the UK. It happened that the members of CTC Ltd. Were German nationals. The claimants sought

a court order to enforce the payment of the debt. It was held that the court could not sanction the payment of the debt since the owners of the claimant company were enemy nationals at a time the nation was at war. The character of individual shareholders cannot of itself affect the character of the company; but the enemy character of individual shareholders and their conduct may be material on the question whether the company's agents or the persons *de facto* in control of its affairs are in fact adhering to, taking instructions from, or acting under the control of enemies. A company incorporated in the United Kingdom but carrying on business in an enemy country is to be regarded as an enemy.

3) Agency

In certain exceptional circumstances, the relationship between a subsidiary company and its parent company may be considered as an agency relationship. In *Smith, Stone & Knight v Birmingham Corporation* [1939] 4 All ER 116 it was held that the parent company was entitled to compensation in respect of a business carried on by its subsidiary on the basis that the subsidiary was in reality carrying on the business on behalf of the parent company. An implied agency existed between the parent and subsidiary companies so that the parent was considered to own the business carried on by the subsidiary and could claim compensation for disturbance caused to the subsidiary's business by the local council. Does the holding that an implied agency existed between the parent and subsidiary amount o lifting the veil?

This decision appeared to negate the separate legal personality principle. Particularly, the *Salomon v Salomon's* principle regard a subsidiary company as a separate entity from its parent company. In determining whether a subsidiary company should be considered as an implied agent of the parent, Atkinson J formulated six relevant criteria, namely:

a) Were the profits treated as profits of the parent?
b) Were the persons conducting the business appointed by the parent?
c) Was the parent the head and brain of the trading venture?
d) Did the parent govern the venture, decide what should be done and what capital should be embarked on the venture?
e) Did the parent make the profits by its skill and direction?
f) Was the parent in effectual and constant control?'

Hence the agency principle would only apply in exceptional circumstances.

4) Sham group of companies/single economic group

In light of the separate legal personality of companies, a company can own shares in another company. In a group of companies, a parent company owns controlling shares in another company called the subsidiary and the parent company usually determines the composition of the board of directors of the subsidiary. Generally, companies in a group have their own separate legal personalities. In some circumstances, the companies may be treated as a single economic entity, where the group structure was a sham or mere façade or used to commit a fraud. In *Woolfson v Strathclyde Council* (1979) 38 P & CR 521, it was held that the corporate veil would not be lifted except in cases where the relationship between a group of companies was a façade. In your opinion, do you believe that company group structure is capable of evading or whittling the potency or practical application of the principle of separate legal personality?

Similarly, in *Adams v. Cape Plc* (1990) BCLC 479, the English parent of an American subsidiary company was sued for asbestos contamination in America. The English company had a subsidiary that operated in the United States. The issue was whether the presence of the subsidiary company in the United State was sufficient to make the English parent company in the United Kingdom liable for the acts of the subsidiary company. The court held that the presence of the subsidiary in the US does not automatically make the parent company present in the United States. The court held that:

'…Save in cases which turn on the wording of particular statutes or contracts, the court is not free to disregard the principle of Salomon v. Salomon merely because it considers that justice so requires. Our law, for better or worse, recognises the creation of subsidiary companies, which though in one sense the creatures of their parent companies, will nevertheless under the general law fall to be treated as separate legal entities with all the rights and liabilities which would normally attach to separate legal entities…' (p 513).

In *Ord v Belhaven Pubs* [1998] 2 BCLC 447, it was held that the court will not allow a plaintiff with a claim against one company in a group to substitute the holding company or other group subsidiaries as defendants to that claim merely because the group may be a single economic entity. A company is in law entitled to organise the group's affairs in the manner that it does, and to expect the court to apply the principle of Salomon in the ordinary way. Thus, companies in a group are to be treated by law as separate legal entities, except in cases where the companies are a sham or façade. From the foregoing, can you identify specific cases where sham or façade would be founded justifying the lifting of the veil in group structure?

5) Interest of Justice

In certain exceptional circumstances, the corporate vail may be pierced if it can be shown that the corporate form was abused or used to evade the consequences of non-performance performance of an existing obligation. In *Re A Company* [1985] BCLC 333, a chain of companies was used by the defendant to put assets out of the reach of the plaintiffs after the plaintiff had commenced proceedings against the defendant for deceit and breach of fiduciary duty. It was held that the veil in the chains of companies would be pierced to enable the plaintiffs pursue the assets. Similarly, in *Trustor AB v Smallbone* [2001] 2 BCLC 436, £39m was missing from the claimant company, with £20m traced to another company I Ltd. I Ltd was a 'front' for S the former Managing Director of the claimant company. The court held that I Ltd was a device used by S for the receipt of the claimant's money. What is 'interest of justice' would be determined by the court in the circumstance. Each case would be its own example.

6) Shareholders/members as contributory s 117 CAMA

Since a company is a separate legal entity, the liability of the members of the company is limited to the amount of money that they agreed to contribute to the company when acquiring the shares. Members can be allotted shares with a promise to pay the company the cost of the shares in future. If the company undergoes insolvent liquidation, any members who has not paid the full price of the shares allotted to them would be required to make the payments to contribute to the assets of the company, see CAMA s. 117. Any sole director/shareholder may also be required to make contributions to the company in similar circumstances.

7) Disqualified director

Where a director continues to act after being disqualified, the director would be jointly and severally liable with the company for any liabilities incurred during the period that s/he acted as a director whilst being disqualified. If a director is held personally liable for his actions as a director on account of being disqualified from acting, does that constitute lifting the corporate veil? Would your answer be the same if all the directors were held liable personally because the entire board was disqualified?

1.5 Tortious and Criminal Liability of the Company (Rules of Attribution)

1.5.1 Tort

As a separate legal entity, a company can sue and be sued in its name in respect of any tortious act. A company would be vicariously liable for the acts of its agents, as long as they act within the scope of their authorities and in the course of their employment. Both the agent/employee and the principal/company are joint tortfeasors and liable jointly and severally, see *Lloyd v Grace, Smith & Co* [1912] AC 716 at 737.

The personal liability of the agent or director acting on behalf of the company may be considered in those circumstances where the agent acted in a way that may suggest that he should be personally held liable. *In Standard Chartered Bank v Pakistan National Shipping Corp (No 2)* [2003]1 BCLC 244, HL, the managing director of a shipping company presented false shipping documents that led to the company receiving $1.1m from a bank. The bank sued the company and the director for deceit. The House of Lord held that the company was liable, and the director was also personally liable for his actions. The court held that by virtue of the law of agency, his representation and the knowledge with which he made it would also be attributable to the company. However, this did not detract from the fact that they were his representations and his knowledge. He was being sued for his own tort, and all the element of the tort were proved against him.

However, in *Williams v Natural Life Health Foods Ltd* [1998] 1 BCLC 689 HL, a one-man company gave negligent advice. The company held itself out as an expert in providing advice on running health food shops. The expertise was derived from the sole director in running his own shop. The plaintiffs relied on financial projections negligently provided by the company in opening their health shop. The health shop collapsed, leading to significant losses. The court held that even though the functions of a one-man's company would be centred on the individual, it does not make him personally liable for the tort of the company. The one-man or director would only be personally liable for loss suffered by third parties if it can be shown that the director assumed personal responsibility for the advice and the plaintiff relied on that assumption of responsibility.

The difference between *Williams* and *Standard Chartered Bank* is that where the elements of a tort claim can be established against an individual director, e.g. where he makes fraudulent misrepresentation, his position as director would not prevent him from personal liability.

1.5.2 Criminal Liability

As an artificial person, a company can be held liable for breach of criminal law just like any other natural person. However, there are some offences that are incapable of being committed by a company. These include offences where imprisonment may be the appropriate punishment, such as murder and other special kind of offences such as bigamy. Common criminal liabilities of companies include; filing false tax returns, conspiracy to defraud or intent to deceive. Criminal liability against a company can be derived from the company's vicarious liability for the acts of its agents who could be its board members, or senior managers. In *Meridian Global Funds Management Asia Ltd v Securities Commission* [1995] 2 BCLC 116, two employees of the company used company funds to purchase a 49% stake in a New Zealand company. The purchase was not disclosed by the company as required by the New Zealand Securities Amendment Act 1988. The company argued that in the absence of the knowledge of the directing mind and will (i.e. the board,) of the acquisition of the shares, there was no breach. The Privy Council held that it was appropriate to attribute the knowledge of the senior employee (the chief investment officer) to the company, otherwise the policy of the Act would be defeated. *Meridian* knew that it was a substantial shareholder in another company when that was known to the employee who had authority to acquire the shares and was therefore in breach of the disclosure requirement.

The rules of attribution are important in the determination of whether the act of a person can be validly attributed to the company to make the company liable. The primary rules of attribution are to be found in the company's constitution which will determine how the affairs of the company are to be run. Other general rules of attribution include agency; vicarious liability would determine whether the acts of others should be regarded as the act of the company.

Self-Assessment Exercises

1. Identify at least five instances in which corporate veil can be disregarded.
2. When a company is formed, registered, and incorporated it becomes____.
3. The case of *Lloyd v Grace, Smith & Co* [1912] AC 716 at 737 is an authority for proposing that _____________________
4. Not being a natural human being, can a company be amenable to criminal liability?

1.6 Summary

The separate legal personality doctrine of a company is a fundamental principle in corporate law. This principle has been protected since its development in *Salomon v Salomon.* Attempts at undermining the principles has led the development of rules that aim at disregarding the corporate form with the objective of protecting the principle. While the corporate form is protected, a disregard of the corporate form mainly leads to the imposition of liability for the purpose of shielding the corporation from liability. Despite the long list of circumstances where the corporate form may be disregarded, the separate personality doctrine remains the rule, rather than the exception.

1.7 References/Further Readings/Web Resources

Sofowora, M.O. (1992). Modern Nigerian Company Law.

Orojo, O. (1984). Company Law and Practice in Nigeria. Sweet and Maxwell, London

Gower and Davies. (2016). Principles of Modern Company Law (10th edn). Sweet and Maxwell London.

Sealy and Worthington's Cases and Materials in Company Law (10th edn Oxford University Press 2013).

1.8 Possible Answers to Self-Assessment Exercises

a) The instances justifying the lifting or disregarding of corporate veil are:

(i) Common law cases
- Fraud/Evasion
- Emergency
- Sham group of companies/single economic group
- Interest of justice

(ii) Statutory instances
- Wrongful trading
- Fraudulent trading
- Breach of relevant provision of CAMA
- Breach of other statutory provision, see section 7, EFCC Act

b) A body corporate and assumes a separate identity, distinct from that of its shareholders and its officers, section 42 CAMA 2020.

c) A company would be vicariously liable for the acts of its agents, as long as they act within the scope of their authorities and in the course of their employment.

d) Yes, a company can be held liable for breach of criminal law just like any other natural person. The criminal liability against a company can be derived from the company's vicarious liability for the acts of its agents who could be its board members, or senior managers. See *Meridian Global Funds Management Asia Ltd v Securities Commission* [1995] 2 BCLC 116

Unit 2 Basic Objectives and Policies underlying Company Legislation

Unit Structure

2.1 Introduction
2.2 Learning Outcomes
2.3 Objectives and Policies underlying Company Legislation
 2.3.1 Certainty
 2.3.2 Enabling or Regulatory Function
2.4 Summary
2.5 References/Further Readings/Web Resources
2.6 Possible Answers to Self-Assessment Exercise(s)

2.1 Introduction

The objectives of corporate regulation are not outlined in statutes that regulate corporate entities, neither are they outlined in any single decision of the court. Nevertheless, the policies underlying corporate regulations can be inferred from the approach to corporate regulation. The objective is either for an enabling purpose or a regulatory agenda or both.

2.2 Learning Outcomes

By the end of this unit, you will be able to:

- discuss the importance of corporate regulation and outline the policies that influences its development.

2.3 Objectives and Policies underlying Company Legislation

2.3.1 Certainty

The most profound objective of corporate regulation is to promote certainty in relation to the rights and liabilities of the various corporate constituents. This includes the relationship between the company and third parties. Challenges that undermine certainty in corporate affairs are directly related to the separate personality doctrine of corporate entities. For example, the questions of whether the company should be liable to third parties or whether liability should personally rest on the board, or any particular officer(s) of the company has been dealt with by the rules of attribution examined in *Meridian Global Funds Management Asia Ltd v Securities Commission* [1995] 2 BCLC 116 above. Other rules relate to circumstances where the corporate veil may be disregarded to

ultimately protect the separate legal personality doctrine.

2.3.2 Enabling or Regulatory Function

A view about the primary objective of company regulation is that it provides an enabling environment for corporate participants to determine how the corporation should be run. This view is supported by the concept of freedom of contract and the nexus of contract theory. It tends to promote a corporation free from government intervention and subject to market forces. However, several challenges limit the application of this approach. The uncertainty and challenging nature of the separate legal personality doctrine has led to government intervention through legislative instruments to regulate and enforce the relationships among the corporate constituents. For example, company constitution determines how the affairs of a company should be conducted and members of the company are free to determine its contents. However, the effects of the company constitutions are determined by regulation. For example, it has been held that the company constitution is a statutory contract that binds the company and its shareholders – see *Companies and Allied Matters Act, 2020* s 46(1); the *UK Companies Act 2006*, s 33.

Second, the freedom of contract is limited to the contents of the company constitution. In terms of the approach to regulation, the interest of shareholders is promoted over other interests in a company. For example, the shareholder value approach influences the development of company law regulation. In the United Kingdom, the Company Law Steering Group attempted to expand the scope of this approach by requiring that directors consider the interests of other stakeholders when they promote the interests of shareholders. This approach which is known as the 'enlightened shareholder value approach' does not actually 'enable' the corporate constituents to determine how corporations should be run, since directors are required to promote the success of the company for the benefit of the members, while merely considering the interest of other stakeholders.

The UK *Companies Act 2006*, s 172

Duty to promote the success of the company:

(a) A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to;

a) the likely consequences of any decision in the long term,

b) the interests of the company's employees,
c) the need to foster the company's business relationships with suppliers, customers and others,
d) the impact of the company's operations on the community and the environment,
e) the desirability of the company maintaining a reputation for high standards of business conduct, and
f) the need to act fairly as between members of the company.

This type of government intervention limits the ‘enabling’ characteristics of company law and enhances its ‘regulatory’ role towards other social considerations.

Self-Assessment Exercises

1. Identify the objectives of company law regulation?
2. Do you think that these objectives are justifiable?

2.4 Summary

A corporate entity is one of the mechanisms for doing business, and it should be free to determine how its affairs are to be conducted, including its relationship with third parties. However, to ensure that the rights of third parties are protected and uncertainties in the relationships among corporate constituents are anticipated, regulations may be necessary. The importance of regulation is to ensure that a balance between the different conflicting interests is struck. It is also aimed at addressing unfairness and lack of accountability and incidence of abuse of the corporate form. Hence, there might not be any need for regulation in the absence of these challenges.

2.5 References/Further Readings/Web Resources

Sealy and Worthington’s Cases and Materials in Company Law (10th edn Oxford University Press 2013).

2.6 Possible Answers to Self-Assessment Exercises

(a) Principally the objectives of company law regulation are for certainty of outcome in respect of the rights and liabilities of the corporate actors; and to provide an enabling environment for the participants to determine how to run the corporate system.

(b) The objectives have largely been met. For instance, in a private company limited by shares, the participants know that shares are not freely transferable but subject to pre-emption rights as provided by the Articles. Similarly, the institutional mechanism through the Corporate Affairs Commissions provides the environment that promotes the conduct of company matters.

Unit 3 Challenges of Incorporation

Unit Structure

3.1 Introduction
3.2 Learning Outcomes
3.3 Challenges of Incorporation
3.3.1 Abuse of Corporate Form
3.3.2 Agency Conflicts of Interests
3.4 Summary
3.5 References/Further Readings/Web Resources
3.6 Possible Answers to Self-Assessment Exercise(s)

3.1 Introduction

The registration of a corporate entity as a business venture has several advantages over other forms of businesses, such as sole proprietorship, partnership, or limited partnership. Among the advantages are; members are not personally liable for the debt of the company and the company can transact in its own name, among other things. Despite these and other benefits, there are certain challenges of incorporation that can undermine the advantages and objectives of a business entity. Two main challenges of; abuse of the corporate form and agency conflict of interests are briefly examined in this unit.

3.2 Learning Outcomes

By the end of this unit, you will be able to:

- explain the challenges of incorporation.

3.3 Challenges of Incorporation

3.3.1 Abuse of the Corporate Form

The separate legal personality doctrine is capable of being abused, when companies are registered to promote ulterior motives or used as a shield to avoid liabilities. Often, when the corporate form is abused, the individual responsible for the abuse would either be personally held liable or be required to contribute to the liability of the company to third parties. Some examples of the abuse of corporate form were examined in unit 1 above. They will not be examined in this unit. See Unit 1 above. Is there any difference between abuse of corporate form and piercing the corporate veil?

3.3.2 Agency Conflicts of Interests

The relationship between company management (directors and executive managers) and shareholders in the administration of the business of a company has been described as an agency relationship. Directors are contractually employed to use their professional expertise to manage the business of companies. Shareholders invest their capital in companies by acquiring shares. They are referred to as the 'residual owners' of companies. They may not have the requisite expertise or capacity to manage the business, hence management board is appointed to manage the business as agents of the principals – shareholders. While ownership resides with the shareholders, the control of the firm is located in the management board. Hence, there is a separation of 'ownership 'and 'control.'

As principals, shareholders expect management to promote shareholder interests and maximise profit. However, since the contract of employment may not predict all possible outcomes, managers are left with a wide range of discretion in making certain decisions. Some managers may be influenced by the desire to promote their own personal interests, leading to a conflict of the interests of these managers with the interests of their shareholders.

'...The directors of such [joint stock] companies, however, being the managers rather of other people's money than of their own, it cannot well be expected, that they should watch over it with the same anxious vigilance with which the partners in a private co-partnery frequently watch over their own. Like the stewards of a rich man, they are apt to consider attention to small matters as not for their master's honour, and very easily give themselves a dispensation from having it. Negligence and profusion, therefore, must always prevail, more or less, in the management of the affairs of such a company...' - **Adam Smith. The wealth of Nations, 1776, Cannan Edition (Modern Library, New York, 1937) p. 700.**

The problems inevitably lead to agency costs, which 'are the costs incurred by shareholders in a bid to ensure that shareholders' interests align with the interests of the managers. These include 'monitoring costs' incurred from monitoring the activities of the agents; 'bonding costs' incurred to guarantee that the agent will not take certain actions which would harm the principal or to ensure that the principal will be compensated if agent takes such action; and 'residual loss' which occurs anyway, despite the monitoring and bonding costs incurred by the principal and agents. It is loss incurred from divergent principal and

agent interests despite the use of monitoring and bonding costs. Why do you think negligence, an example of corporate governance failure, prevail in the management of the affairs of a company?

Note that abuse of the corporate form does not refer to all the circumstances that can lead to lifting of the corporate veil. There are cases where the veil may be lifted even though the separate legal personality doctrine had not been abused. For example. The corporate veil may be disregarded and lifted in emergency situations. This was examined above in Unit 1 in circumstances where the veil may be lifted under common law. See *Daimler Co. v Continental Tyre Co Ltd* [1916] 2 AC 307.

Self-Assessment Exercises

1. Explain the challenges to the corporate personality doctrine.
2. What effective measures can be used to address the problem?
3. Lifting the corporate veil is applied only in cases of abuse of corporate form. Do you agree?

3.4 Summary

The challenges of incorporation are a threat to the aims and objectives of the separate legal personality doctrine developed in *Salomon's* case. The abuse of the corporate form has been addressed by statute and common law. These measures are aimed at preserving the corporate personality doctrine. Further, they seek to deter future abuses by identifying the individuals responsible and holding them accountable. In relation to agency conflicts, the problem caused by separation of 'ownership and control' between company shareholders and management boards has not been completely addressed. Attempts have been made to resolve this problem through corporate governance regulation and regulation at the level of the market for corporate control – takeovers and mergers. Increased level of accountability is being demanded from the management board to ensure that the interests of board are largely aligned with the interests of shareholders. However, shareholders do not seem to be adequately informed about their companies. Information asymmetry limits the capacity of shareholders to effectively challenge the board. Further, shareholders' over-reliance on government regulations to make the board accountable is a dominant moral hazard that limits the participation of shareholders in the activities of their companies. For shareholder activism to be effective, shareholders must play active roles in their companies. They must take active interests and learn about the activities of their companies so that they would be able

to challenge the board.

3.4 References/Further Reading/Web Sources

Eugene F. Fama and Michael C. Jensen, "Separation of Ownership and Control," *The Journal of Law and Economics* 26, no. 2 (Jun., 1983):301- See link - https://doi.org/10.1086/467037

Michael C Jensen and William H Meckling, 'Theory of the Firm: Managerial Behaviour, Agency Cost and Ownership Structure' (1976) 3 *Journal of Financial Economics* 305. See link - https://doi.org/10.1016/0304-405X(76)90026-X

3.5 Possible Answers to Self-Assessment Exercises

1. The main challenges facing the corporate form are abuse of the corporate form and the presence of conflict of interest.

2. The measures to stem abuse of the corporate form will be to institute a strong regime of corporate governance, which, thankfully CAMA 2020 has a made interesting provisions. Another measure is through the market control.

3. I disagree because abuse of the corporate form does not refer to all the circumstances that can lead to lifting of the corporate veil. There are cases where the veil may be lifted even though the separate legal personality doctrine had not been abused

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MODULE 2 THE COMPANY CONSTITUTION IN THE UK AND NIGERIA

Unit 1 Company Constitution I:
Articles and Memorandum of Association
Unit 2 Company Constitution II:
Resolutions and Shareholder Agreement
Unit 3 Limitations of Shareholder Democracy

Unit 1 Company Constitution I

Unit Structure

1.1 Introduction
1.2 Learning Outcomes
1.3 Articles of Association
  1.3.1 Effects of Articles of Association and Memorandum of Association
  1.3.2 Enforcement of Articles
  1.3.3 Outsider Rights
1.4 Summary
1.5 References/Further Readings/Web Resources
1.6 Possible Answers to Self-Assessment Exercise(s)

1.1 Introduction

Company constitution governs the affairs of a company. It contains rules that determines how the internal affairs of a company should be run and it determines the relationship between or among the members and the company and its officers. In view of the separate legal personality doctrine that a company is an artificial person, the company constitution is vital to the smooth operation of its affairs. It is the highest decision-making authority in a company. The different components of a company's constitution are examined below.

1.2 Learning Outcomes

By the end of this unit, you will be able to:

- define what constitutes company constitution;
- explain the effects of company constitution;
- explain the differences in the scope of company constitution in the United Kingdom and Nigeria.

1.3 Articles and Memorandum

In Nigeria, company constitution consists of the memorandum of association and the articles of association of a company. It also includes any resolution passed by members at meetings or any agreement of the members of the company. What are the similarities and dissimilarities between company's constitutional documents in Nigeria and the UK?

The memorandum of association typically contains the name of the company, the business which the company seeks to carry on and any restrictions on the powers of the company. The articles of association contain regulations on how the affairs of the company should be organised and managed. See CAMA s 27(1), s 32, and s 262(3). The articles of association is the most important document of a company.

The articles will normally contain provisions for the appointment, removal, conduct and remuneration of directors, secretaries, solicitors, auditors, the regulation of the conduct of different meetings, voting rights and procedure, rules on dividends, the preparation of company accounts, membership of the company and other incidental matters. In the United Kingdom, a company constitution consists of its articles of association, and any special or unanimous resolution passed by the members and any agreement of the members. See UK *Companies Act 2006,* sections 17 & 29.

In the UK, the memorandum of association is no longer a part of a company's constitution. The things previously required to be included in the memo, such as the name, registered address, type of company, and objects are no longer required to be included in the memorandum under the UK *Companies Act 2006*. While the articles of association contain rules for the regulation and management of companies in the UK, the memorandum is only relevant for identifying the names of the first subscribers and the shares allotted to them. This implies that in the UK, the memorandum of association is merely a historical document. The bundle of rights available to members of a company are more often articulated in the Articles. Can you provide examples of such rights?

1.3.1 Effects of Articles of Association and Memorandum of Association

In Nigeria, the articles and memorandum have the effect of a contract between the company and its members and between each member.
CAMA 2020, s 46(1) provides:

Subject to the provisions of this Act, the memorandum and articles, when registered, shall have the effect of a deed between the company

and its members and officers and between the members and officers themselves whereby they agree to observe and perform the provisions of the memorandum and articles, as altered in so far as they relate to the company, its members, or officers.

In the United Kingdom, the memorandum is omitted from the company constitution. The company constitution is regarded as a contract that binds the members to each other and binds the members to the company.
UK Companies Act 2006, s 33 provides

(a)The provisions of a company's constitution bind the company and its members to the same extent as if there were covenants on the part of the company and of each member to observe those provisions."

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1.3.2 Enforcement of Articles

- A contract between the company and the members
- A contract between/among the individual members *inter se*

In *Wood v Odessa Waterworks* (1889) 42 Ch D 636, it was held that "the articles of association constitute a contract not merely between the shareholders and the company, but between each individual shareholder and every other. The provisions of the articles may be enforced by a member against the company, or by the company against the members. It can also be enforced by the members against fellow members.

1) Company can enforce against members

See *Hickman v Kent and Romney Sheep Breeders Association* (1915 1 Ch 881 where a company's articles contained provision that any disputes between the company and its members should first be submitted to arbitration. The claimant sued the company for an injunction to prevent his expulsion. It was held that the action was in breach of the claimant's obligation under article 49 requiring him to submit his grievance to arbitration.

2) Members of a company can enforce against the company

Companies have obligation to its members. This includes, right of members to receive dividend when declared, right to attend meeting, right to vote at company meetings, right to receive share certificate, right to a return of capital upon winding up of the company, among others.

In *Wood v. Odesa Waterworks Co. (*1889) 42 Ch. D 639*,* the articles provided that the directors may, with the sanction of the ordinary meeting,

declare a dividend to be paid to the members in proportion to their shares. The General meeting approved a resolution to pay dividends by way of debentures/bonds/future payment. This effectively prevented members from receiving dividend by cash. An action was brought by dissenting shareholders to stop the company from implementing the resolution. It was held that the articles constitute a contract not merely between the shareholders and the company but between each individual shareholder and every other. Accordingly, the provisions of the articles on the distribution of the profits have not been followed; an injunction was granted against the company. See also *Pender v Lushington (1870) 6 Ch D 70,* where a company chairman refused to count the votes of a shareholder. It was held that the chairman had no right to disallow the votes in breach of the company's articles. Compare and contrast the holding in Pender v Lushington and the extant provisions of CAMA 2020 in section 248 on the right of the chairman to demand a poll.

3) Members can enforce provisions of articles against fellow members

A member of a company may also sue a fellow member to enforce the provisions of the articles. In *Wood v Odesa Waterworks* (supra) the court made it clear that the articles constituted a contract also between each individual shareholder and every other shareholder. Also, in *Rayfield v Hands* (1960) Ch 1, [1958] 2 All ER 194, the articles of the company provided that any member who wished to transfer their shares should notify the directors who would take the shares among them at a fair price. The plaintiff wanted to transfer his shares, he informed the company and the other directors. The directors refused to take the shares and denied any obligation to do so. The court held that the directors are obliged to take the shares in accordance with the contractual provision of the articles. Does CAMA 2020 recognise the concept of outsider rights with reference to the Articles?

1.3.3 Outsider Rights

Members of a company cannot enforce outsider rights against the company. Outsider rights are those rights which do not correspond to the general rights of membership available to all shareholders of the same class. For example, a member cannot enforce a right as a director, solicitor, except in certain circumstances. It was observed in *Hickman v Kent and Romney Sheep breeders Association Ltd. (1915) 1 Ch 881*, that,

Firstly, that no articles can constitute a contract between the company and a third person; secondly, that no right purporting to be given by an article to a person, whether a member or not, in a capacity other than that of a member, as for instance a solicitor, promoter, director, can be enforced

against the company; and thirdly, that articles regulating the rights and obligations of the members generally as such do create rights and obligations between them and the company respectively. (p. 900)
Accordingly, in *Eley v Positive Government Security Life Assurance*

(1876) 1 Ex D 88*,* the articles of association of the company provided that the claimant who was also a member of the company, should be appointed as the company solicitor for life. The court held that the claimant could not enforce that provision.

See also *Browne v. La Trinidad* (1877) 37 Ch D 1. where a company's articles contained a provision that in consideration of the sale by plaintiff of his property to the company, he would become a member of the company and would be appointed a director for at least four years. The plaintiff was removed as a director before the stated four years. He never became a member of the company. It was held that even if he had become a member, he could not enforce the provision since it was an outsider right. Note that outsider rights may be enforceable in certain exceptional circumstances. These include:

- if it is supported by an independent contract or
- if its enforcement necessarily or would lead to the enforcement of a membership right.

*In Quin & Axtens v Salmon (*1909) AC 442 – a company's articles provided that any of the two managing directors could veto a decision of the Board of Directors in certain circumstances. The claimant, pursuant to that provision, vetoed a decision of the Board. The veto was ignored. The claimant sued as a member of the company to compel compliance with the articles. It was held that the company, in seeking to disregard the veto, was in effect attempting to bypass its own rules on decision-making; and that this was an irregular attempt to alter the company's articles.

Self-Assessment Exercises

1. What constitutes company constitution in the United Kingdom and Nigeria?
2. Explain the effects of company constitution from the point of Articles of Association?

1.4 Summary

The effect of company constitution on the relationship between the

company and its members and between the members of the company clearly indicate that the constitution is the most important document of a company. While the company constitution has similar effects in Nigeria and the United Kingdom, the scope of company constitution in both jurisdictions differs. In the UK, it does not include the memorandum of association. The memo is now a document of historical value. It merely identifies the names of the first subscribers that were allotted shares in a company. In Nigeria, the memo and articles remain the relevant company constitution and can be enforced by a company and its members. Other aspects of company constitution, namely, the resolutions of members and agreement are examined briefly in the next unit. The limitations of the powers of shareholders to amend the provisions of the company constitution are also examined.

1.5 References/Further Readings/Web Resources

M.O. Sofowora. (1992). Modern Nigerian Company Law. Alpha, Lagos

Olakunle Orojo. (1984). Company Law and Practice in Nigeria. Sweet and Maxwell, London.

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Drury, R. R. (1986). "The Relative Nature of a Shareholder's Right to Enforce the Company Contract." *The Cambridge Law Journal*, vol. 45, no. 2, pp. 219–246. *JSTOR*. See link - www.jstor.org/stable/4506877

1.6 Possible Answers to Self-Assessment Exercise(s)

(a) The company's constitutional documents in Nigeria and the UK are the Articles of Association and Resolutions. To the exclusion of the UK, the Memorandum of Association remains a part of the constitutional documents of a company Nigeria**.**

(b) The effect of the company's constitution from the point of Articles of Association is that it is a contract under deed between the company and its members and officers and between the members and officers themselves whereby they agree to observe and perform the provisions of the memorandum and articles, as altered in so far as they relate to the company, its members, or officers.

Unit 2 Company Constitution II

Unit Structure

2.1 Introduction
2.2 Learning Outcomes
2.3 Shareholder Resolutions (Shareholder Democracy)
 2.3.1 Ordinary Resolutions
 2.3.2 Special Resolutions
 2.3.3 Written Resolutions
 2.3.4 Unanimous Resolutions
 2.3.5 Registration of Resolutions
2.4 Shareholder Agreement
2.5 Summary
2.6 References/Further Readings/Web Resources
2.7 Possible Answers to Self-Assessment Exercise(s)

2.1 Introduction

Resolutions of members of a company at meetings and shareholder agreement also form part of company constitution. They are supplements to the main regulations that govern the affairs of a company in the articles, hence they are also considered as company constitution. While resolutions are made at shareholder meetings, shareholder agreement is used to define or expand the scope of members' rights and liabilities and to make rules relating to other incidental matters affecting the company. The effect of resolutions on members' rights and liabilities depends on the particular type of resolution that is passed at meetings. Meanwhile, shareholder agreement has certain characteristics that makes the scope and effects of its application different from articles of association which is considered to be the tradition company constitution. How many types of resolutions can be found under CAMA 2020?

2.2 Learning Outcomes

By the end of this unit, you will be able to:

- explain the effects of shareholder resolutions;
- discuss the effects and scope of application of shareholder agreement.

2.3 Shareholder Resolutions (Shareholder Democracy)

Decisions in companies are made by way of a democratic process and confirmed by resolutions. Resolutions are agreement reached by all the members of a company or majority of members that are present in a

meeting after a vote had been held. There are four types of resolutions recognised by the UK *Companies Act 2006* and the *Companies and Allied Matters Act 2020*. They include; ordinary resolution, special resolution and written resolution. It also includes unanimous resolution, which was earlier established under Common Law. Ordinary and special resolutions can be passed at general meetings. Written resolutions and unanimous resolutions do not require a general meeting.

2.3.1 Ordinary Resolutions

CAMA 2020, s 258 (1)
UK Companies Act 2006, s.282

This is a decision by a simple majority of at least 51% of members present and voting at a general meeting. The necessary majority is counted from the shareholders who actually attend the meeting and cast their votes. For example, if a company has hundred members and only fifty attend a general meeting, the simple majority shall be twenty-six. Provided that all members entitled to vote at a meeting were duly invited to attend the meeting, they would be bound by the decisions of those who attend the meeting. Where the articles of association of a company does not stipulate a larger majority in making decisions, decisions at a general meeting should be adopted by ordinary resolution. See CAMA s 258(6).

2.3.2 Special Resolutions

CAMA 2020 s. 258(2)
UK Companies Act 2006, s. 283

This requires at least 75% vote of the members that are present and voting at a general meeting. Usually, decisions of serious matters are done by way of special resolution. If a matter is to be proposed as a special resolution, the notice of meeting must state the text of the proposed resolution and the intention to propose it as a special resolution. This is necessary to allow members to study the proposal and be able to decide which way to cast their votes.

Matters requiring special resolutions include; alteration of articles of association, voluntary winding up and reduction of share capital among others. All resolutions of a public company must be passed either by ordinary or special resolution. Private companies are not required to hold annual general meetings, hence they do not have to use ordinary resolution or special resolution to make decisions. Differentiate between special resolutions and unanimous resolutions.

2.3.3 Written Resolutions

CAMA 2020, s 259
UK Companies Act 2006 s. 288

A private company may make decisions by way of a written resolution. This is a resolution signed by the members without the need for a general meeting. A public company cannot pass a written resolution.

Written resolutions are designed to make decision-making easier for private companies. Members of a company or the board may propose a resolution as a written resolution. A class of shareholders may also use written resolutions. The proposal of the resolution must contain a text of the resolution and the method of assenting to the proposal and must be circulated to all eligible members along with any supporting statement.

However, directors and auditors of a company cannot be removed by written resolution before the end of their tenure because of the requirement for representation by the director or auditor. Directors and auditors can only be removed by ordinary resolution for which a special notice is given. CAMA 2020, ss 288, 409(1), 411(1)(d).

2.3.4 Unanimous Resolutions

Where all the members of a company entitled to attend a meeting reach an agreement on a matter, that agreement is binding as if it was reached at a general meeting. The agreement will not be invalidated simply because it was not reached at a formal meeting. The objective of this principle is that since the essence of a meeting is for members to assemble and take a decision, if they are able to agree on a decision without holding a formal meeting, there is no reason why that decision should not be respected. This is sometimes referred to as *'the duomatic principle'*

In *Re Duomatic Ltd.* (1969) the court held that a payment approved unanimously by all the shareholders of a company without a general meeting as required by the company's articles was valid as if it was approved by the general meeting. The court remarked as follows:

…Where it can be shown that all shareholders who have a right to attend and vote at a general meeting of a company assent to some matter which a general meeting of the company could carry into effect, that assent is binding as a resolution in general meeting would be…

2.3.5 Registration of Resolutions

When a company passes a resolution, the effect of the resolution may be to change the contents of a document already filed at the Corporate Affairs Commission CAC. The old document may give a misleading information about the company to creditors, investors, and other customers and third parties. Thus, it is necessary to keep the CAC informed of important changes to companies' affairs or documents. Accordingly, CAMA requires companies to ensure that they register resolutions that have been passed. This must be done within 15 days of passing the resolutions. See *CAMA 2020,* s 262.

2.4 Shareholder Agreement

Shareholder agreement is a contract entered into by the shareholders either at the time of formation of the company or any time after the company has been formed. It supplements the provision of articles. The terms in a shareholder agreement must be agreed by all the members of the company. It can be used to contract with new members of a company. For example, a family-owned company in need of capital may invite an outsider to join the company as an additional shareholder through an agreement.

Some features of shareholder agreement include the following:

1) Normal contractual rules apply – its terms cannot be altered by a majority vote. Alteration requires the consent of all the members of the company.
2) Majority shareholders can benefit from provisions on prices of shares and good/bad leavers provisions.
3) Contractual obligations are enforceable as of right, not discretionary remedies that apply to limit the capacity of minority to challenge major shareholders.
4) They are not constrained by the rules governing the enforcement of articles e.g., that articles can only be enforced by individual members – *qua* members.
5) It is not a public document available for inspection like articles. It offers privacy in dealing with sensitive matters of managements …dividend, remuneration…etc.
6) It would not bind future shareholders since they were not parties to the contract that created the shareholders' agreement except the new shareholders agree to be bound and sign a deed of adherence.

One of the challenges of shareholder agreement is that it is difficult to amend since the approval of all members is required. Thus, member(s) not convinced of any new term may veto the amendment. This implies

that shareholder agreement is one of the ways of protecting minority shareholders from amendments that would have merely require majority votes to be effective.

Self-Assessment Exercises

1. What are company resolutions?
2. Briefly define "the Duomatic Principle."
3. Explain the advantages and challenges of shareholder agreement.

2.5 Summary

The supplementary role of shareholder resolution and shareholder agreement does not imply that they are less important than the provisions of articles of association. Since resolutions can amend provisions of articles, they are as important as the previsions of company articles. Also, since shareholder agreement apply as of rights, that is they are considered to be contractually enforceable by members, they are equally as important as provisions of articles of association.

2.6 References/Further Readings/Web Resources

M.O. Sofowora, Modern Nigerian Company Law (Alpha 1992)

Olakunle Orojo, Company Law and Practice in Nigeria (London Sweet and Maxwell, 1984)

Gower and Davies: Principles of Modern Company Law 10th edn (any relatively recent edition) (London, Sweet and Maxwell 2016)

2.7 Possible Answers to Self-Assessment Exercises

(a) Company resolutions are agreements reached by all the members of a company or majority of members that are present in a meeting after a vote had been held

(b) The Duomatic Principle allows shareholders of a company to informally approve the company's actions without the need to hold a general meeting, as long as the approval is unanimous.

(c) One of the advantages of shareholder agreement is that normal contractual rules apply, and its terms cannot be altered by a majority vote. On the other hand, the challenge of shareholder agreement is that it is difficult to amend since the approval of all members is required.

Unit 3 Limitations of Shareholder Democracy (Alteration of Articles)

Unit Structure

3.1 Introduction
3.2 Learning Outcomes
3.3 Conditions for Effective Amendment of Articles
 3.3.1 Amendment that is Inconsistent with CAMA
 3.3.2 Alteration cannot Increase the Liability of Members
 3.3.3 Alteration must be made for Company's Interest
3.4 Summary
3.5 References/Further Readings/Web Resources
3.6 Possible Answers to Self-Assessment Exercise(s)

(a) Introduction

The articles of association is the most important document of a company, it can be amended by members in general meeting. This implies that shareholder meeting is the highest decision-making organ of a company. Shareholders take part in company decision-making process by attending and voting at meetings. This quasi-management role enables every shareholder, including minority shareholders to have a voice on how the affairs of the company should be run. Although the decisions are made through simple majority, (50%+1 present) absolute majority (at least 75% majority) or unanimous decision (consent of all shareholders), however, there are certain limitations to the extent to which majority decisions can be valid. These restrictions are briefly explained below.

(b) Learning Outcomes

By the end of this unit, you will be able to

- outline and explain the limitation on the powers of majority decision of shareholders to alter/amend the articles of association.

(c) Conditions for Effective Amendment of Articles

3.3.1 Amendment that is Inconsistent with CAMA

Shareholders cannot amend the provisions of the articles of association in such a way that the articles would be inconsistent with the provisions of CAMA or any other legislation. This does not merely prevent shareholders from voting to amend the provisions of the articles of their company to make certain regulations to be different from the Act.

Members can amend articles to require a higher standard to be complied with in respect of certain matters that are regulated by the Act. However, such amendment must not undermine the purpose of the particular provision(s) of the Act as to render the provision of the article grossly inconsistent with the provisions of the Act.

3.3.2 Alteration cannot Increase Liability of Members

The rights of members of a company to amend the provisions of its articles of association is restricted if the amendment would increase the shares or the liability of members. Usually in a corporate entity set up to do business, members of the company agree to contribute (pay for their shares) to the capital of the company in exchange for the shares that are allotted to them. The amount of money that members agree to contribute to the company cannot be increased by amending the provisions of the articles to reflect the increase, except the members affected by the increase agree to such increase in writing.
CAMA, 2020, s 54
UK Companies Act 2006 s. 25

3.3.3 Alteration must be made for Company's Interest

Despite the widely practised shareholder democracy where decisions are made by majority votes, the validity of the process leading to the alteration of the articles is not dependent on majority votes. Amendments are only considered valid if they are made to promote the interests of the company. This is usually expressed as amendment done in good faith in the interests of the company or of the members as a whole. For example, in *Allen v. Gold Reefs of West Africa Ltd* [1900] 1 Ch 656, the company had altered its articles so as to give itself a lien on paid up shares in respect of the failure of the shareholder to pay calls on other shares which had not been fully paid up. The effect of the amendment was to alter the contractual rights of the shareholders. It was held that the amendment to the articles was within the power of the company.

'… the power of companies to alter their article…..must, like all other powers… be exercised, not only in the manner required by law, but also bona fide for the benefit of the company as a whole…'(Lindley J.).

In Sidebottom v. Kershaw, Leese & Co. Ltd [1920] 1 Ch. 154, the defendant company altered its articles to enable its directors to buy out the shares of any member who carried on a business in competition with the company. The plaintiffs carried on such business and the directors compulsorily purchased their shares. It was held that it was primarily in the interest of the company that the alteration should be made.

Note that where the alteration was oppressive or suspicious, or extravagant such that no reasonable person would consider it to be in the best interest of the company, the court may set it aside, especially where the interests of minorities are concerned. In *Browne v. British Abrasive Wheel Co. Ltd.*, [1919] 2 Ch. 290, the company was in great need of capital. The majority of shareholders with 98% of shares were willing to provide the capital if they could buy the remaining 2% of the company's shares held by the minority shareholders. The provisions of the articles of the company were altered to enable holders of 98% of the shares to compulsorily buy out the holders of the remaining 2%. The alteration was held to be invalid because it discriminated against the minority for the benefit of the majority. It was therefore not in the interest of the company as a whole. This implies that where alteration is not in conflict with the provision of the Act, it is important that such alteration does not undermine the interests of any particular member(s) of the company. Alterations must not be used by majority members to promote their own personal interests.

Self-Assessment Exercise

1. Outline the limitations to the alteration of company articles.
2. In a situation similar to Browne v British Abrasive Wheel Co Ltd, what do you think would be attitude of the court?

(d) Summary

The role of the court in enforcing changes made to company articles is very clear. While the court would not decide what is best for the company, it would determine by reference to an objective test whether the amendment was done for the overall interest of the company and whether any members' interests would be unfairly undermined by it.

(e) Reference/Further Reading/Web Resource

Rixon, F. G. (1986). "Competing Interests and Conflicting Principles: An Examination of the Power of Alteration of Articles of Association." *The Modern Law Review*, vol. 49, no. 4, pp. 446–475. *JSTOR*, See link www.jstor.org/stable/1095943

3.6 Possible Answers to Self-Assessment Exercise

(a) The limitations to alteration of the Articles include where (i) it is inconsistent with CAMA; (ii) it increases the liability of members or (iii) it is not made in the interest of the company as a whole.

(b) In such a case the Court would view the alteration as oppressive or suspicious or extravagant that no reasonable person would consider the alteration to be in the interest of the company. The alteration would be set aside.

MODULE 3 MANAGEMENT POWERS AND RESPONSIBILITIES

Unit 1 Directors' Duties
Unit 2 Scope of Directors' Duties
Unit 3 Remedies / Liabilities for Breach of Directors' Duties
Unit 4 Ratification of Breach / Relief by the Court

Unit 1 Directors' Duties

Unit Structure

1.1 Introduction
1.2 Learning Outcomes
1.3 Fiduciary Duties of Directors
1.4 The Common Law Duty of Care
    1.4.1 The Standard of Skill and Care Required
    1.4.2 Objective and Subjective Standards
1.5 Summary
1.6 References/Further Readings/Web Resources
1.7 Possible Answers to Self-Assessment Exercise(s)

(a) Introduction

An incorporated company is an artificial person, it can enter into contracts on its own behalf, and it can sue and be sued in its own name. However, as an artificial person, (unlike a natural person), a company cannot act on its own, it needs people to act on its behalf, hence, directors are appointed to manage the business of companies. Directors' duties are provided to ensure that there is clarity of purpose in the role of directors and to make directors understand the limits of their role in companies. It may also be relevant to shareholders and other stakeholders to challenge directors whenever there is a proposed or actual breach of directors' duties. To whom do you think the director's duties are owed?

(b) Learning Outcome

By the end of this unit, you will be able to:

- explain the fiduciary and common law duties of directors.

(c) Fiduciary Duties of Directors

Fiduciary duties are outlined in CAMA 2020, ss 305 and 306 as follows, s. 305 CAMA

1) A director of a company 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.
2) A director owes fiduciary relationship with the company where -
(a) a director is acting as agent of a particular shareholder;
(b) though he is not an agent of any shareholder, such a shareholder or other person is dealing with the company's securities.
3) A director shall act at all times in what he believes to be the best interests of the company as a whole so as to preserve its assets, further its business, and promote 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 and, in doing so, shall have regard to the impact of the company's operations on the environment in the community where it carries on business operations.

4) The matters to which the director of a company is to have regard in the performance of his functions include the interests of the company's employees in general, as well as the interests of its members.
5) A director shall exercise his powers for the purpose for which he is specified and shall not do so for a collateral purpose, and the power, if exercised for the right purpose, does not constitute a breach of duty, if it, incidentally, affects a member adversely.
6) A director shall not fetter his discretion to vote in a particular way.
7) Where a director is allowed to delegate his powers under any provision of this Act, such a director shall not delegate the power in such a way and manner as may amount to an abdication of duty.

s. 306
1) The personal interest of a director shall not conflict with any of his duties as a director under this Act.
2) A director shall not-
(a) in the course of management of affairs of the company; or
(b) in the utilisation of the company's property, make any secret profit or achieve other unnecessary benefits.
3) A director shall be accountable to the company for any secret profit made by him or any unnecessary benefit derived by him contrary to the provisions of subsection (2).
4) 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 of a director under this Act.

5) *The duty not to misuse corporate information shall not cease by a director or an officer having resigned from the company, and he shall still be accountable and can be restrained by an injunction from misusing the information received by virtue of his previous position.*
6) *Where a director discloses his interests before the transaction and before the secret profits are made before the general meeting, which may or may not authorise any resulting profits, he may escape liability, but he shall not escape liability if he discloses only after he has made the secret profits, and in this case, he shall account for the profits.*

Directors' fiduciary position is based on their role as agents for the company, hence they are expected to exhibit loyalty to the company in line with the following;

1) no profit rule
2) no conflict rule
3) no rule against self-dealing

A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. The ultimate obligation of a fiduciary is the obligation of loyalty. What are the indicia of the fiduciary obligation of a director?

A fiduciary must exhibit the following characteristics

- They must act in good faith at all times
- They must not make any secret profit
- They must not place themselves in a position where their duties and their interests may conflict, so that they would not be in a position to obtain profit.
- A fiduciary should not act for his own benefit or the benefit of a third person without the informed consent of his principal (the person on whose behalf he is acting).
- A fiduciary must generally act honestly.
- They must act within the scope of their powers/authority.

In the United Kingdom, fiduciary duties are outlined in the Companies Act 2006, ss 171-173, 175-177. They have the same effects as the fiduciary duties that are applicable in Nigeria and outlined in CAMA 2020, s 305 and 306.

Directors are expected to be loyal to their companies; they must not obtain any benefit or receive any favours as a result of their position as directors, except such benefits were made known to and approved by the

company. This is meant to ensure that a director's independence is not compromised and that they are not influenced in their capacity to make informed decision in the best interests of the company.
See the following cases: *Bristol and West Building Society v Mothew* [1998] Ch 1 and *Bairstow v Queen's Moat Houses Plc* [2001] EWHC Civ 712.

(d) The Common Law Duty of Care

The common law duty of care was developed by the court to ensure that persons that are appointed by the company as directors are held accountable where they fail to exhibit their expertise. Directors are required to exercise reasonable care, skill and diligence in the performance of their duties.

CAMA 2020 legislated the common law duty of care and by section 308 provides that:

1) Every director of a company shall exercise the powers and discharge the duties of his office honestly, in good faith and in the best interests of the company, and shall exercise that degree of care, diligence and skill which a reasonably prudent director would exercise in comparable circumstances.
2) Failure to take reasonable care in accordance with the provisions of this section is a ground for an action for negligence and breach of duty.
3) Each director is individually responsible for the actions of the board in which he participated, and the absence from the board's deliberations, unless justified, shall not relieve a director of such responsibility.
4) The same standard of care in relation to the director's duties to the company shall be required for both executive and non-executive directors:

Provided that additional liability and benefit may arise under the master and servant law in the case of an executive director if there is an express or implied contract to that effect.
Similarly, see *Companies Act 2006*, s 174

1.4.1 The Standard of Care and Skill Required

The measure of directors' care and skill was first established in *Re Equitable Fire Insurance Ltd.* [1925] Ch 407

The case resulted from the insolvency of an insurance company due to the illegal activities of its managing director, Bevan (described by

Romer J as "a daring and unprincipled scoundrel"). Subsequently, the company liquidator sought an order to require the other directors of the company to contribute to the company's assets on the basis of their having committed misfeasance. That the other directors did not give sufficient attention to the affairs of the company and that they would have prevented the main culprit, Bevan from engaging in the illegal activities. The directors were exculpated due to a clause in the company's articles of association which provided that they could only be liable for the company's losses if such losses arose due to their "wilful neglect or default". The court held that a director might only exercise such knowledge as may be expected of a person of his knowledge and experience; that he is not bound to give continuous attention to the affairs of the company; and that he may delegate his duties to other directors and officers of the company. The court clearly did not apply a high standard; hence the other directors were not held liable for not dedicating sufficient time to the affairs of the company. However, the standard of care applied by the court in this case has now been reviewed and there is now a higher standard. The effect of the revised standard is that the same directors in *Re Equitable* would have been held liable if this case was decided today.

1.4.2 Objective and Subjective Standards

The standard of care has been made stricter. The test of directors' competence and skill is now both objective and subjective. Do the dual (objective and subjective) tests obtain under CAMA 2020?

1) Objective Test
CAMA s 308(1)

Every director of a company shall exercise the powers and discharge the duties of his office honestly, in good faith and in the best interests of the company, and shall exercise that degree of care, diligence and skill which a reasonably prudent director would exercise in comparable circumstances.

UK Companies Act s 174
With the care, skill, and diligence that would be exercised by a reasonably diligent person with the knowledge and skill, and experience of any person in the same position

2) Subjective Test

Additional subjective test applies in the United Kingdom.
See s 174(2)(b)

The general knowledge, skill, and experienced possessed by that particular director.

While the objective test applies in both Nigeria and the United Kingdom, both the objective and subjective tests apply in the UK. This dual test is the same test used to determine whether a director is guilty of wrongful trading under *the UK Insolvency Act 1986*, s 214(4). Thus, subjective test would also apply as a persuasive authority in Nigeria.

In light of the higher standards – objective and subjective tests, the courts now hold directors to a higher standard of care. In *Re D'Jan of London Ltd* [1993] BCC 646 A director who failed to read an insurance proposal before signing it was held liable to the company at common law in negligence. D, a director of the company, signed an insurance proposal filled in by another without reading it. The proposal gave inaccurate information and enabled insurers to repudiate the policy. The liquidator brought an action against D in negligence. It was held, that a director's duty of care to the company at common law is the same as that set out in s.214 of the Insolvency Act 1986 . By failing to read the proposal, D had been negligent. Would you support the view that directors of companies need not devote their full time to the company?

The decision in *Re City Equitable Fire Insurance* [supra] case that a director need not devote his/her full time to the affairs of the company now applies only to non-executive directors who are employed on a part-time basis. Executive directors who have full time service contracts are required to devote their full time to the service of the company. Even non-executive directors should attend board meetings whenever they can, because continuous absenteeism from board meetings for a considerable period of time without permission may be a ground for breach of duty. Non-executive directors would be judged by reference to the same standards as executive directors. See CAMA s 308(4).

Self-Assessment Exercises

1. Enumerate the characteristic elements of fiduciary duties.
2. With the use of a decided case, what is defining difference between executive directors and non-executive directors from point of duty of skill and care?

1.5 Summary

Director's fiduciary duties and the duty of care and skill are the framework from which every duty of director is based. Directors must be loyal to their companies; they must ensure that they do not put

themselves in a position whereby their personal interests' conflicts with the interests of their company. Furthermore, a director must ensure that s/he has the required competence and capacity to act as director before accepting to act as director. Where necessary, they must obtain requisite training and support to be able to effectively discharge their duties to the best interests of the company.

1.6 References/Further Readings/Web Resources

M.O. Sofowora, Modern Nigerian Company Law (Alpha 1992)

Olakunle Orojo, Company Law and Practice in Nigeria (London Sweet and Maxwell, 1984)

Gower and Davies: Principles of Modern Company Law 10th edn (any relatively recent edition) (London, Sweet and Maxwell 2016).

1.7 Possible Answers to Self-Assessment Exercises

(a) The characteristic elements of fiduciary duties of a director include to act in good faith at all times; not to make any secret profit; must not place themselves in a position where their duties and their interests may conflict, so that they would not be in a position to obtain profit; and A fiduciary should not act for his own benefit or the benefit of a third person without the informed consent of his principal (the person on whose behalf he is acting).

(b) The defining difference is that non-executive directors are not required to devote their full time to the affairs of the company. However, executive directors normally with full time service contract must devote their full time to the company: *Re City Equitable Fire Insurance*

Unit 2 Scope of Directors' Duties

Unit Structure

2.1 Introduction
2.2 Learning Outcomes
2.3 Discovering the Extent of Directors' Duties
    2.3.1 To Whom are Directors' Duties Owed?
    2.3.2 By Whom are Directors' Duties Owed?
    2.3.3 Classification of the Duties
2.4 Summary
2.5 References/Further Readings/Web Resources
2.6 Possible Answers to Self-Assessment Exercise(s)

2.1 Introduction

A clarification of the scope of directors' duties is important for various reasons. First, it provides clarity to directors of what is expected of them in the discharge of their duties as directors. Second, it ensures that shareholders and other stakeholders are aware of this expectation so that they can challenge directors prior to or when there has been a breach of duty. Lastly and importantly, it provides certainty to the court in resolving questions of breach of duty.

2.2 Learning Outcomes

By the end of this unit, you will be able to:

- explain the scope of directors' duties.

2.3 Discovering the Extent of Directors' Duties

(a) To Whom are Directors' Duties Owed?

The directors' duties are owed to 'the company' and not to the shareholders or any other stakeholder in the company – see CAMA s 309(2) which provides that director, when acting within his authority and the powers of the company, would be regarded as agent of the company. See also 305(1) and (9); *Companies Act 2006,* s.170(1) (*Percival v Wright* [1902] 2 Ch. 421: directors are not trustees for individual shareholders). These provisions do not imply that directors can ignore shareholder interests. Shareholders as residual owners/ claimant would benefit from the economic prosperity of the company as long as directors promote the value of the company. In exceptional circumstances, directors' duties can be owed to shareholders, e.g. when

a takeover offer is being considered by the directors – *Heron International Ltd v Grade* [1983] BCLC244, 265.

(b) By Whom are Directors' Duties Owed?

Directors' duties are owed by any person who occupies the position of director. This includes, persons that have been duly appointed as directors, those not duly appointed, but carry out the duties of directors CAMA 2020, ss 269, 270, 286 and it also includes former directors of a company.

1) Persons who cease to be directors remain subject to certain duties, namely; the duty as regards the exploitation of any property, information or opportunity of which he became aware at a time when he was a director. CAMA s 306(5), CA, s 175. A person who benefits from any transaction as a result of the information that he obtains when he was a director could be liable to account to the company, even though s/he is no longer a director.

2) In addition, in CA s 176 (duty not to accept benefits from third parties) as regards things done or omitted by him before he ceased to be a director. Where a person resigns or is removed from the position of director such person can be liable afterwards, if he failed to act or acted contrary to provision of s 176. The benefit that was received at the time that he is no longer a director was as a result of his acts or omissions at the time he was a director.

The general duties shall be interpreted and applied in the same way as common law rules or equitable principles, and regard shall be had to the corresponding common law rules and equitable principles in interpreting and applying the general duties.

Statutory duties 'extract and express the essence of the rules and principles which they have replaced…That did not consign the replaced rules and principles to legal history' *Premier Waste Management Ltd v Towers* [2011] EWCA Civ 923

(c) Classification of the Duties

Directors' duties are mainly classified into fiduciary duties and common law duties of care. These were examined in Unit 1 above. Directors must supervise delegated functions/Non-Executive Director Liability. See CAMA s 305(7). Can you discover any difference between duties of directors and the fiduciary obligations of directors?

1) Even though directors, especially non-executive may still, in appropriate circumstances, delegate their duties to other directors, they now have a responsibility to supervise and monitor the discharge of those duties and keep themselves informed of their companies' businesses. In *Equitable Life Assurance Society v. Bowley* [2003] EWHC 2263 (Comm) it was held that a non-executive director was not entitled to delegate his responsibilities if it meant an unquestioning dependence on others to do his job. In *Re Barings Plc* (No 5) [2000] 1 BCLC 523, it was held that the exercise of the power of delegation does not absolve a director from the duty to supervise the discharge of the delegated functions. It was also held that directors collectively have a continuing duty to acquire and maintain a sufficient knowledge and understanding of the company's business to enable them to properly discharge their duties.

2) Further, in *Dorchester Finance Co. v. Stebbing* [1989] BCLC 498 two non-executive directors of a finance company were in the habit of signing blank cheques for the use of their co-director. One of the directors was a chartered accountant while the other had extensive experience in accounting. The result of the directors' actions was that the company lost a lot of money due to the misuse of the cheques by their co-director to give irregular loans to friends and family members. It was held that the company was entitled to sue the two non-executive directors for negligence.

3) *Note also* that for listed companies, it is now required that their directors and senior management must collectively have appropriate expertise and experience to manage their businesses.

Self-Assessment Exercise

1. Are the duties of directors amenable to delegation?
2. If yes, are there any control to the right to delegate but if no, what options are available to directors?
3. Identify those by whom the director's duties are to be specifically performed.

2.4 Summary

No doubt, the scope of directors' duties is extensive. The fiduciary duty and common law duty of care constitute the main aspects of directors' duties. Enforcement of the duties is primarily related to the extent to which the fiduciary duty and the common law duty of care have been complied with. Also, it is important for persons acting as directors by

whatever name called to ensure that they are properly informed of the scope of their role towards the company. Where there is a doubt, advice should be sought and obtained, and the company should be required to clarify the role and the extent of liability in the event of a conflict. The principles on the scope of directors' duties are not intended to make directors' duties cumbersome; it is simply intended to protect the interests of the company and its stakeholders and to particularly promote the integrity of the position of directors, whether the person occupying the role has been duly appointed or not.

2.5 References/Further Readings/Web Resources

M.O. Sofowora, Modern Nigerian Company Law (Alpha 1992)

Olakunle Orojo, Company Law and Practice in Nigeria (London Sweet and Maxwell, 1984)

Gower and Davies: Principles of Modern Company Law 10th edn (any relatively recent edition) (London, Sweet and Maxwell 2016)

2.6 Possible Answers to Self-Assessment Exercise

(a) Yes, directors can delegate their responsibilities in appropriate cases: *Equitable Life Assurance Society v. Bowley* [2003] and *Re Barings Plc* (No 5) [2000].

(b) There are controls to the extent of delegation. One, a non-executive director was not entitled to delegate his responsibilities if it meant an unquestioning dependence on others to do his job: Equitable Life Ass Society v Bowley. Two, the exercise of the power of delegation does not absolve a director from the duty to supervise the discharge of the delegated functions. In sum, a director that delegates cannot abdicate as ultimate responsibility rests on him.

(c) Directors' duties are owed by any person who occupies the position of director. This includes persons that have been duly appointed as directors, those not duly appointed, but carry out the duties of directors CAMA 2020, ss 269, 270, 286 and it also includes former directors of a company.

Unit 3 Remedies/Liability for Breach of Directors' Duties

Unit Structure

3.1 Introduction
3.2 Learning Outcomes
3.3 Breach of Fiduciary Duties
3.4 Breach of Duty of Care
3.5 Summary
3.6 References/Further Readings/Web Resources
3.7 Possible Answers to Self-Assessment Exercise(s)

3.1 Introduction

To ensure that directors' duties are complied with, a breach of directors' duties can lead to various forms of remedies for the company against the erring director(s). These liabilities do not aim at putting directors under pressure, rather, they are part of the process towards incentivising anyone who occupies the position of a director and enforcing compliance with the Act. The remedies also ensure that the interest of the company is protected. Do you support the long held view that the Court should grant relief to a director who fell in breach and thereby defaulted in his duties?

3.2 Learning Outcomes

By the end of this unit, you will be able to:

- identify the main remedies available to the company for breach of directors' duties.

3.3 Breach of Fiduciary Duties

CAMA 2020, ss 306(3), 313, CA 2006 s 178

Every duty of directors in CAMA or the Companies Act are fiduciary duties, except the common law duty of care. Do you agree that fiduciary duties or obligations arise and are similar in all situations of fiduciary relationship and it does not matter whether one is a director, solicitor, an agent or stands in any other form of fiduciary relationship? As explained above, directors as fiduciaries are expected to exhibit loyalty to their companies. They must not make secret profit or receive any benefit from third parties as a result of their positions as directors without the permission of the company. The company can bring a claim against the erring director if it can show that it has suffered some loss. If the

director has made some profits, the director can be required to account to the company for the profit made. Generally, when there is a breach of fiduciary duty, the contract is voidable at the instance of the company against any party who has notice of the breach of duty. See *Hely-Hutchinson & Co Ltd v Brayhead* [1968] 1QB 549.

Any profit received by the director pursuant to the breach can be recovered by the company. In *Aberdeen Railway Co v Blaikie Bros*, (1854) 1 Macq 461 HL, the company entered into a contract with a firm for the supply of some goods. The chairman of the company was also a partner in the firm supplying the articles. It was held that there had been a breach of duty. The court stated that no one having fiduciary duties to discharge shall be allowed to enter into engagements in which he has, or can have, a personal interest conflicting, or which possibly may conflict with the interest of those whom he is bound to protect. Also, in *Transvaal Lands Co. v New Belgium (Transvaal) Land and Development Co.* (1914), company A and company B entered into a contract. One of the directors of company A held shares in company B on trust for someone else. It was held that the contract was invalid because of the conflict of interest as director and trustee.

Where there is a breach of fiduciary duty, the company can:

- Apply for an injunction to stop the director from carrying out or continuing with the breach;
- Seek for a restoration of the company's property;
- Apply for the rescinding of a contract in which the director had an undisclosed interest.

Where the contract or act of director is to be approved by the company, the vote of the relevant director would not count. How can the meeting at which the act of the director is to be approved be conducted without undue influence from the concerned director?

3.4 Breach of Duty of Care CAMA 2020 s 308(2)

The duty of care requires directors to show attention to the affairs of the company and act competently in the discharge of their duties. A breach of the duty of care is an indication of failure to exhibit competence and lack of reasonable conduct in the discharge of duty by the erring director. Such directors would be held to have been negligent. The company can institute an action for damages against the erring director(s). The measure of damages to be awarded by the court would be dependent on the particular circumstances of the case and the nature and effect of the breach on the company. For example, in In *Equitable Life Assurance Society v. Bowley* (2003), it was held that a non-

executive director was not entitled to delegate his responsibilities if it meant an unquestioning dependence on others to do his job.

Delegating without a corresponding supervision was a failure to exhibit reasonable care towards the affairs of the company. In *Re Barings Plc* (2000), it was held that the exercise of the power of delegation does not absolve a director from the duty to supervise the discharge of the delegated functions. It was also held that directors collectively have a continuing duty to acquire and maintain a sufficient knowledge and understanding of the company's business to enable them to properly discharge their duties.

Self-Assessment Exercise

1. Identify at least one consequence for breach of director's fiduciary duties.
2. What is the measure of damage in a case involving breach of a director's duty of skill and care?
3. How can directors mitigate their exposure to risk or liability associated with failure to discharge their duty of skill and care?

3.5 Summary

Liability for breach of directors' duties is a remedy for loss suffered by the company for negligent act of directors or for benefits diverted from the company. The benefits or opportunities could either have been diverted from the company or the directors may have compromised their independence and become incapable of acting for the company in such a way that would have enhanced the company's interests. The remedies are not meant to persecute directors for erroneous conduct or breach that occurred when directors have acted reasonable. In circumstances where directors are shown to have acted reasonable, they may be excused from liability.

3.6 References/Further Reading/Web Source

Gower and Davies. (2016). Principles of Modern Company Law, 10th edn. Sweet and Maxwell, London.

M.O. Sofowora. (1992). Modern Nigerian Company Law. Alpha, Lagos.

Sealy and Worthington's Cases and Materials in Company Law, (10th edn. Oxford University Press, Oxford UK, 2013.

3.7 Possible Answers to Self-Assessment Exercise

(a) One of the consequences of breach of the fiduciary duty avoidance of a situation of conflict or against making of secret profit or the duty of account is that any secret profit made by the defaulting director would be disgorged: *Aberdeen Railway Co v Blaikie Bros*, (1854) and *Transvaal*

Lands Co. v New Belgium (Transvaal) Land and Development Co. (1914)

(b) In a case where it is shown that a director has fallen in breach of his duty of skill and care to the company, the measure of damages to be awarded by the court would be dependent on the particular circumstances of the case and the nature and effect of the breach on the company.

(c) To mitigate their risk of exposure to liability due to non-performance, it has been held that directors collectively have a continuing duty to acquire and maintain a sufficient knowledge and understanding of the company's business to enable them to properly discharge their duties: Re Barings Plc.

Unit 4 Ratification/Relief from Liability

Unit Structure

4.1 Introduction
4.2 Learning Outcomes
4.3 Authorisation/Ratification of Directors' Conduct
4.4 Relief by Court
4.5 Summary
4.6 References/Further Readings/Web Resources
4.7 Possible Answers to Self-Assessment Exercises

4.1 Introduction

The scope of liability for breach of directors' fiduciary duty and duty of care and skill may serve as an incentive for directors to carry out their duties diligently and in good faith. Also, the high standard that is required to be upheld by directors in the discharge of their duties may increase the risk of a breach of duty. Consequently, vacant positions may become less attractive to applicants. However, breach of directors' duty may occur even where directors act reasonably. In such circumstance, liability for breach of duty may be unfair. Hence, it may be reasonable for directors to escape liability in certain exceptional circumstances. Are there any limits to the power of the company to ratify a wrong which if not ratified would amount to breach of duty?

4.2 Learning Outcomes

By the end of this unit, you will be able to:

- explain the circumstances where directors may escape liability when there is a breach of duty.

4.3 Authorisation/Ratification of Directors' Conduct

CAMA ss 305(8), 341; CA ss.180(4) s.239, 225

The acts of directors which would be considered a breach of duty may be authorised by the company, as long as such authorisation is permitted by law. Also, if the director(s) acted reasonably, the act may be approved or authorised by the company.

- are there any rules of law enabling company to authorise what would otherwise be a breach of duty by director?
- has the director acted in accordance with any provisions of company's constitution dealing with conflicts of interests?

In Nigeria, directors' duties appear to be absolute, whereby a breach of duty may not be ratified by members of the company. Compare and contrast the provisions of section 305(8) and section 341 CAMA 2020.

CAMA, s 305(8) provides:
"No provision, whether contained in the articles or resolutions of a Company, or in any contract shall relieve any director from the duty to act in accordance with this section or relieve him from any liability incurred as a result of any breach of the duties conferred upon him ..."

This appears to indicate that members lack the capacity to ratify a breach of duty for the purpose of absolving any director from the liability arising from the breach. However, s 341, suggests that members may be able to ratify a wrongful conduct.

s. 341 provides:

Subject to the provisions of this Act, where an irregularity is made in the course of a company's affairs or any wrong is done to the company, only the company can sue to remedy that wrong and only the company can ratify the irregular conduct.

Can you attempt reconciling, if possible, section 305(8) providing against relief of a director from "breach of duties" and section 341 permitting the ratification of "an irregular conduct" in the course of a company's affairs or a wrong done to the company?

In the United Kingdom, a company can ratify conduct by a director amounting to negligence, default, breach of duty or breach of trust in relation to the company. The ratification can be done through a resolution passed by the members of the company.

In passing the resolution, the company shall disregard the votes of the relevant director(s) and any person connected with the director(s). Directors must also make full and frank disclosure. See *Bamford v Bamford* [1970] Ch. 212. Articles of a company provided that all unissued shares were to be at the disposal of the directors. In order to prevent a takeover bid, the directors allotted shares to a particular person. There was no question of fraud. The members by resolution in general meeting later ratified the issue. On a preliminary point of law, held, that assuming the directors made the issue with an improper motive, the issue was capable of being effectively ratified by an ordinary resolution of the members in a general meeting. It was further held that where directors act *intra vires* the company but *ultra vires* their own

powers in that they issue shares with an improper motive, such act may be validated by the members of the company in general meeting, provided that a full and frank disclosure is made to them.

4.4 Relief by the Court

CAMA s 738(1); CA s.1157
Are there circumstances where the court may grant relief to director and exclude such directors from liability even where a breach of duty occurred?

In Nigeria, a director or officer of a company may be granted relief from liability by the court for negligence, default, breach of trust and breach of duty, and consequently excluded from liability, if it can be shown that they acted honestly and reasonably.

CAMA s 738(1)

If in any proceeding for negligence, default or breach of duty or trust against an officer of a company or a person employed by a company as auditor, it appears to the Court hearing the case that the officer or person is or may be liable but that he has acted honestly and reasonably and that, having regard to all the circumstances of the case, including those connected with his appointment he ought fairly to be excused, the Court may relieve him, either wholly or partly, from liability on such terms as it may deem fit.

Similar principle applies in the United Kingdom. CA s 1157

1) If in proceedings for negligence, default, breach of duty or breach of trust against—

(a) an officer of a company, or
(b) a person employed by a company as auditor (whether he is or is not an officer of the company), it appears to the court hearing the case that the officer or person is or may be liable but that he acted honestly and reasonably, and that having regard to all the circumstances of the case (including those connected with his appointment) he ought fairly to be excused, the court may relieve him, either wholly or in part, from his liability on such terms as it thinks fit.

In the UK and Nigeria, while the court may relieve erring directors of liability for breach of duty, the relevant director(s) are required to show that they acted honestly and reasonably in the circumstance. See

Premier Waste Management Ltd v Towers [2011] EWCA Civ 923. The court would likely be guided by the level of breach, the scope of loss or damage suffered by the company and the acts or omission of the director in relation to the breach.

Self-Assessment Exercise

1. How can the shareholders or board ensure that the resolution to ratify an act of a director is not tainted?
2. What is the effect of directors acting intra vires the powers of the company but ultra vires their powers as directors?

4.5 Summary

Ratification/relief granted to directors for breach of duty is aimed at ensuring that particular conducts of directors that are aimed at promoting the objective of corporate entities are encouraged, even though a breach of duty may erroneously occur. This would ensure that directors remain free to discharge their duties without fear of fault which may undermine their capacity to engage in risky investment decisions that can enhance the economic value of companies. Although the possibility of relief/ratification may be argued to encourage misconduct, however, since the court would consider the merit of each application by reference to the particular conduct of the director, it is doubtful whether a deliberate misconduct would lead to a relief from liability or succeed in obtaining shareholder ratification.

4.6 Reference/Further Reading

Sealy and Worthington's Cases and Materials in Company Law (10th edn Oxford University Press 2013)

4.7 Possible Answers to Self-Assessment Exercise

(a) In passing the resolution, the company shall disregard the votes of the relevant director(s) and any person connected with the director(s). Directors must also make full and frank disclosure: Bamford v Bamford.

(b) The effect where directors act *intra vires* the company but *ultra vires* their own powers is that such act may be validated or ratified by the members of the company in general meeting, provided that a full and frank disclosure is made to them: Bamford v Bamford.

MODULE 4 DIVIDENDS AND MINORITY SHAREHOLDER PROTECTION

Unit 1 Register of Members
Unit 2 Dividend
Unit 3 Shareholder Residual Management Role
Unit 4 Majority Rule and Minority Protection

Unit 1 Membership of a Company

Unit Structure

1.1 Introduction
1.2 Learning Outcomes
1.3 Membership of a Company
 1.3.1 Register of Members
 1.3.2 Inspections and Investigations
1.4 Summary
1.5 References/Further Readings/Web Resources
1.6 Possible Answers to Self-Assessment Exercise(s)

1.1 Introduction

As soon as a company is incorporated, shareholders become the primary source of capital through the shares that are allotted to them. Their ownership of the shares makes the shareholders to be the residual owners of the corporate entities in which they have invested. Afterwards, the names of the shareholders are included in the register of members as a confirmation of their membership of the company. Subsequently, any person who becomes a shareholder of the company can have their names included in the register of members to ensure that the company keeps them informed about its activities, to confirm their membership and more importantly, that the registered members enjoy the benefits of membership of the company. What are the rights attached to membership of a company limited by shares? This unit identifies the importance of registration and the benefits that attaches to shareholders that are included in the register of members.

1.2 Learning Outcomes

By the end of this unit, you will be able to:

- explain how a person can become a member of a company;
- explain the effects of register of members;
- explain the relevance of inspection and investigation.

1.3 Membership of a Company

There are different ways that a person can become a shareholder of a company. These include the following:

1) By subscribing to the memorandum and articles of association of the company - A subscriber to a company's memorandum is a person who agrees to become a member of the company and to have their name entered into the register of members of the company CAMA s 105(1); UK CA 2006 s.112(1*).*

2) By making a successful application for the company's shares – From time to time, public companies allot or issue their shares to potential shareholders. A public company can allot its shares to the public, by observing the rules applicable to trading through the stock market. A private company cannot offer its shares to the public. CAMA s 22(5) CA 2006 s. 755.

3) By transmission_– Shares can be acquired by operation of law, e.g. on the death, mental incapacity or bankruptcy of the owner of the shares. The shares are transmitted in accordance with the applicable laws. CAMA, s 178, 179. The executor or administrator of a deceased person is deemed to be entitled to the shares as far as the company is concerned, because they have legal title to the shares. *CA, 774*. See *Roberts v Letter 'T' Estates Ltd* [1961] AC 795.

4) Share transfer – sale or gift- Shareholders can transfer their shares by selling some or all of their shares. In public companies, this is usually done through stockbrokers. In private companies, the sale has to be by private arrangement. The transfer can be made by way of a gift. CAMA s 175(4) CA, s 772.

5) Employee Share Scheme - Shares may be allotted to *bona fide* employees or former employees of a company, or to their spouses, widow or widower, children or stepchildren. The scheme is aimed at providing incentive to the employees for their services or as a reward for their commitment and productivity.

(a) Register of Members

Every company must keep a register of its members. The register is to be kept in the registered office of the company or at any other place where the company is registered. The register of members contains the

names, addresses, the type and number of shares owned by the members. It also includes the amount that has been paid for the shared held by the members, i.e. whether the members have paid the entire cost of the shares or whether there are outstanding payments to be made by the member. It also includes, the date of commencement of membership. When a member ceases to be a shareholder, membership ceases, this is also recorded in the register of members – the register is amended periodically.

The inclusion of the name of a person in the register of members does not automatically make them a member of the company if they had not agreed to be members of the company, their names can be removed from the register. However, if the name of a person who had not previously agreed to be a member of a company is included in the register, and they act as members of the company by attending meetings, sending proxies to act on their behalf or attempting to sell shares, such a person would be deemed to have accepted the allotment. The articles of association usually provide rules for membership; these rules must be complied with in the admission of new members, see *POW Services Ltd v Clare* [1995] 2 BCLC 435; except the articles are amended.

Joint holders of shares shall be treated as a single member with a single address to be entered against their names and address – different names, single address Anything to be agreed or specified by the holder must be agreed or specified by all the joint holders. Anything authorised or required to be sent or supplied to the holder may be sent or supplied either to each of the joint holders, or to the holder whose name appears first in the register of members. CAMA ss 109-116, 244(4); CA s 113(5). Can you think of the circumstances under which the rectification of register of members can be allowed?

Where a company fails to include a person's name in the register of members where the company was supposed to include such name, the company would be liable to pay damages for any loss. CAMA s 180(3) CA s. 125(2); *Re Ottos Kopje Diamond Mines* [1893] 1 Ch 618 CA.

(b) Inspections and Investigations

CAMA ss 357-362.
UK CA s 116 (3)(4) s 119 (1)(2) ss 1035 -1039

The register of members is one of the important documents of a company. Since it contains the names of the registered shareholders in a company, it is expected to generate much interests from various company stakeholders and regulatory authorities. Thus, the register of members may be inspected for purposes of investigations by individuals

or regulatory authorities. In Nigeria, the Corporate Affairs Commission may appoint one or more persons – inspectors – to investigate the affairs of a company as part of its regulatory and supervisory role; where there is a suspicion of irregularity or where there has been a petition or pursuant to an order of the court. The directors and officers are obliged to co-operate with the inspectors and tender any documents and provide any information requested by the inspectors. Do you think that the investigatory powers of the Commission compare favourably to other jurisdictions like the UK?

In the UK, there is a similar opportunity to inspect company documents, especially the register of members. The register is open for inspection and any person either seeking to inspect the register or obtain a copy of any part of the register must make a request. The request must include the following.

a) Identify the names and address of the individual making the request or the name and address of the individual responsible for making a request on behalf of an organisation.
b) State the purpose of the inspection.
c) State whether the information is to be disclosed t any other person. If so, the details of that other person must be provided, including the purpose for which the register would be used by that person.

The objective of an inspection is to ultimately promote the objectives of the separate legal personality doctrine and the benefits that attaches to it. For example, inspection may be required to challenge a wrongful act of a company officer or directors who may be personally benefiting from their positions. It is an offence for those who obtain information from the company register to provide misleading information or use the information obtained for an improper purpose. They must not also share information with unauthorised persons, knowing that the persons would use the information for an improper purpose.

The announcement of an inspection or investigation of the affairs of a company can affect the public image of the company, thus, power to appoint inspectors is not often used. This power is exercised in the UK by the Secretary of State (for Business Innovation and Skills) where it is considered that there is fraud or an improper conduct. Inspectors may be officers appointed from the office / department of the Secretary of State. Other private inspectors may be appointed for more serious cases.

Investigations that reveal irregularities in a company can led to prosecution, disqualification of directors or the winding up of the company. To what effective uses can the inspector's report be put?

Self-Assessment Exercises

1. List the different ways of becoming the member of a company.
2. Mr. Boots discovered that his name is in the register of members of Fashions and Perfumes Nigeria Limited. Meanwhile he did not apply to be a member. What is the effect of this?

1.4 Summary

The members of a company are the primary source of capital for their companies; hence the register of members is one of the important documents of a company. It is not merely a document that evidences ownership of shares, it contains the address and contact details of the members, to ensure that they can be contacted to attend meetings to decide how the affairs of the company would be run. Hence, it is important that the register is regularly updated, and it should be rectified if any names or detail are entered incorrectly. An updated and accurate register is important for the company administrators to ensure that they can contact the members whenever there is a need to hold meetings. It is also important for regulatory authorities for the purposes of inspection and investigation.

1.5 References/Further Readings/Web Resources

Sealy and Worthington's Cases and Materials in Company Law (10th edn. Oxford University Press, London.

M.O. Sofowora. (1992). Modern Nigerian Company Law. Alpha, Lagos

1.6 Possible Answers to Self-Assessment Exercise(s)

(a) The various ways of becoming member of a company include by share transmission, transfer of shares, subscribing the memorandum and articles of association and through employee share ownership scheme.

(b) The law is that inclusion of the name of a person in the register of members does not automatically make her a member of the company if she had not agreed to be a member of the company. The name can be removed from the register. However, if the name of a person who had not previously agreed to be a member of a company is included in the register, and she acts as a member by attending meetings, sending proxies to act on her behalf or attempting to sell the shares allotted to her, such a person would be deemed to have accepted the allotment. Except it is shown that Mr. Boots took the foregoing steps which automatically validates the entry of his name in the register, his name can be safely removed without any trouble.

Unit 2 Dividend

Unit Structure

2.1 Introduction
2.2 Learning Outcomes
2.3 Dividend
    2.3.1 Distributable Profit
    2.3.2 Rules on Dividend Payment
2.4 Summary
2.5 References/Further Readings/Web Resources
2.6 Possible Answers to Self-Assessment Exercise(s)

2.1 Introduction

Dividend is one of the benefits of membership. A shareholder receives dividends periodically when declared by the board of directors. There are certain rules governing the payment of dividends and the rights of members to receive dividends. Dividends are not received as of right, except declared by the board. The board must ensure that dividend is paid lawfully. Apart from dividend, identify the other benefits of membership of a company.

2.2 Learning Outcomes

By the end of the unit, you will be able to:

- explain the rules relating to the payment of dividends.

2.3 Dividend

(a) Distributable Profit

CAMA ss 426-428, 433

UK CA ss 830-852

Dividend is the payment made out of the profits of the company to the shareholders. Shareholders with ordinary shares have rights to vote in a meeting, to share in surplus assets, and a right to return of capital. There is no automatic right to dividend unless the board of directors declares dividend. The shareholders are not generally entitled to receive dividends even though the company makes profit, except in certain circumstances relating to preferential shareholders. Define distributable profits as a basis for payment of dividend.

Dividends may only be paid out of distributable profits. Distributable profits include profits arising from the use of the company's assets, including a wasting asset, revenue reserves and realized profit on a fixed asset sold and where more than one asset is sold, the net realized profit on all the assets sold. Distributable profits refer to surplus profits that a company has received and accumulated over a period of time which is more that its accumulated losses or liabilities. This means that if the company pays dividend to its shareholders, it would still be able to meets its debt obligations when demanded by its creditors. The directors and officers of a company must ensure that the company would be able to pay its liabilities as they become due before, they declare that the company has a distributable profit.

Dividends are payable to ordinary shareholders after the preference shareholders have been paid. Preferential shareholders own shares with preferential rights. The preferential rights usually relate to the payment of dividends. This means the shareholders of that class have a right to be paid dividend before other shareholders and the rate of dividend is stated in the articles or in the terms of issue as a percentage of the nominal value of the shares, e.g. 5% or 8%. Preference shareholders have a right to their dividend at the stated rate. Just like ordinary shareholders, preference shareholders are only entitled to dividend if the directors have declared a dividend. If dividend is not paid in any year, preferential shareholders would be able to carry their dividends over to the next year because, the right to dividend for preferential shareholders is deemed to be 'cumulative' unless otherwise stated. This implies that, if dividend is not paid in any year, they are carried forward to the following year. The right to cumulative payment may be lost if a company goes into insolvent liquidation, unless the cumulative payment is preserved or had been safeguarded.

Employees would be entitled to a share in the profits of the company if it is provided under their contract of service. They can claim the share whether or not dividends have been declared provided the company made profit. While payment to shareholders is called dividend, what is the nature of payment made to staff out of the profits of a company?

(b) Rules on Dividend Payment

The articles of association usually specify how dividends should be declared; usually directors are given the power to declare dividends. Shareholders are entitled to declared dividend only on their paid-up shares. In *Precision Dippings Ltd v Precision Dippings Marketing Ltd* [1986] Ch 447, CA, it was held that the statutory procedure prescribed for the declaration of dividend which includes an auditor's report among

other things, was mandatory and that a departure from it could not be rectified by a subsequent resolution by the shareholders.

The company's paid up capital is not available to be used to pay dividend because, it is kept as a guarantee to creditors that the debt from the company would be paid. Dividend can only be paid out of the distributable profits of the company. Where dividend is paid out of capital, it may be recovered from any shareholders who knew that the dividend they received was paid from the company's capital. Any director or officer of the company or any person who knowingly pay dividends out of capital would be jointly and severally liable to indemnify the company to the value of the dividend that was paid out – see *Re Exchange Banking Co, Flitcroft's case* (1882) 21 Ch D 519 CA

Dividends are usually approved by the members in general meeting. The general meeting may reduce the amount of dividend recommended by the board, but the amount may not be increased since the scope of distributable profit was considered before the recommended amount. Any increase may extend the dividend beyond distributable profits.

Also, dividends may be declared and paid out only where there are reasonable grounds for believing that the company would be able to pay its outstanding liabilities to creditors when due, if the dividend is paid.

While there is no right to receive dividends, it was held in *Re Sam Weller & Sons Ltd* [1990] Ch 682 that non-payment of dividend may be a ground for ordering the winding up of a company on just and equitable grounds. It can also be a ground for relief from unfairly prejudicial conduct. This order may be made if there had been a restrictive dividend policy and a shareholder is denied a return on their investment which they were reasonably entitled to expect.

Self-Assessment Exercise

1. What is the consequence of paying dividend when the same is not made out of or from distributable profits of the company?
2. What is the position of law as regards absence of right to receive dividend?

2.4 Summary

One of the main reasons for acquiring shares in a corporate entity is to receive dividends periodically. There are several conflicting interests in corporate entities, especially public companies or large private

companies. This could lead to conflicts among the various interests. Hence, several rules and regulations apply in relation to the distribution of company profits. These include statutory provisions and the provision of articles of association. Further, these regulations are necessary to ensure that the corporate personality is not used as a medium to promote fraud by undermining the interests of some shareholders, creditors or other stakeholders.

2.5 References/Further Readings/Web Resources

M.O. Sofowora. (1992). Modern Nigerian Company Law. Alpha, Lagos

Olakunle Orojo. (1984). Company Law and Practice in Nigeria. Sweet and Maxwell, London.

Gower and Davies. (2016). Principles of Modern Company Law 10th edn. Sweet and Maxwell, London.

2.6 Possible Answers to Self-Assessment Exercise

(a) It means that such a dividend must have been paid out of capital. The effect is it may be recovered from any shareholders who knew that the dividend they received was paid from the company's capital. Any director or officer of the company or any person who knowingly pay dividends out of capital would be jointly and severally liable to indemnify the company to the value of the dividend that was paid out: *Flitcroft's case* (1882)

(b) While there is no right to receive dividends, it was held in *Re Sam Weller & Sons Ltd* [1990] Ch 682 that non-payment of dividend may be a ground for ordering the winding up of a company on just and equitable grounds. It can also be a ground for relief from unfairly prejudicial conduct. This order may be made if there had been a restrictive dividend policy and a shareholder is denied a return on their investment which they were reasonably entitled to expect

Unit 3 Shareholder Residual Management Role

Unit Structure

3.1 Introduction
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3.1 Introduction

As the residual owners of corporate entities, shareholders perform residual management functions. Although, these roles are described as 'residual', they are nevertheless 'core' roles because as we will see from the main section, these roles substantially affect the corporate existence and the business of companies. The roles are described as residual management roles because the main management roles are usually carried out by the management team of the company. Hence any other management roles in a company is considered to be residual rather than a major one. At this point, can you identify the specific instances where CAMA 2020 made provisions permitting the activation of the members' residual or interventionist managerial powers?

3.2 Learning Outcomes

At the end of the unit, you should be able to explain the residual management roles of company shareholders.

3.3 Residual Management Roles

Generally, corporate managerial powers are reserved in the board of directors, that may delegate that power to committee of its own or to the managing director. Notwithstanding, CAMA recognises that there are circumstances where the members in general meeting can step in and carry out residual managerial roles. The instances include where the board of directors are disqualified or unable to act because of a

deadlock, to ratify or confirm any actions taken by the board of directors, etc. See section 87(5) CAMA 2020.

The residual management roles of shareholders are exercised through their voting rights. To exercise their voting rights, shareholders pass resolutions at meetings. The meetings are usually annual general meetings AGMs or extra –ordinary general meetings EGMs. See, *CAMA ss 237, 239; CA s 301-354*. The rule requiring companies to hold meetings is flexible with private companies. Private companies can pass written resolutions (ordinary or special) without the need to hold a meeting. Except a resolution is to be passed to remove a director or auditor from office since a special notice is required to remove a director or auditor from office. CAMA ss 288, 409; CA ss, 168 and 510.

Shareholders' individual voting rights are to be exercised for individual shareholder interests; they do not have fiduciary duties to the company. See *Estmanco v GLC* [1982] 1 WLR 2. Shareholders residual management roles include the following:

(a) Shareholder Power to Ratify Director's Breach of Duty

CAMA ss 341, 87(5)(c); CA ss 239

Shareholders can ratify a conduct of a director amounting to negligence, default, breach of duty or breach of trust. In ratifying the breach, the vote of the relevant director or any person connected with him/her who sits on the board will not count towards the required majority needed for ratification. The objective of this power is to ensure that that directors who breach their duties while honestly acting to promote the success of the company, can be excused from liability. It ensures that directors would not be deterred from taking risks and that persons who have the capacity to manage the business of companies would not be discouraged from taking up roles of directors. The circumstances of each particular case would be considered to ascertain whether the act of the director was reasonable to warrant the ratification.

(b) Shareholders' Power to Act as a Board

In light of the legal requirement for companies to have directors - at least 2 directors for public companies and 1 director for private companies, at all times a company must have directors who make up the board. Also, certain documents require at least one director's signature to be valid. Hence, shareholders may constitute themselves or a part of them into a board. In *Baron v Potter* [1914] 1 Ch 895, directors of a company were deadlocked; there were two factions of directors, both of

whom refused to turn up to board meetings called by the other side in order to prevent a quorum. General meeting of shareholders purported to appoint an extra director to break the deadlock. One group of directors challenged this decision on grounds that only directors had power to appoint directors. It was held that it is a **default common law rule** that annual general meeting has power to appoint directors where the board is incapable of acting due to deadlock, thus appointment was valid. It is unlikely for company shareholders to constitute themselves into a board of directors. Since vacant positions or sudden retirement or emergencies would be addressed by holding EGM – extra-ordinary general meetings.

(c) Shareholder Power to Alter Articles of Association

A company has the power to alter the provisions of its articles at any time and it cannot be deprived of the power to do so. The procedure for alteration depends on whether the provision to be altered is a general provision of the article or an entrenched provision. For general provisions, a special resolution is usually required. For entrenched provisions, a unanimous consent of the members would be required. See notes in Module 2 Unit 3 above.

(d) Power to Authorise Certain Transactions between the Company and Directors

Usually, the board of directors of a company are empowered to authorise transactions on behalf of the company, however, shareholder approval is required for certain types of contracts between directors and the company. These include the following:

1) Directors service contracts longer than 5 years CAMA, s 317 - UK more than 2 years – CA *s 188*
2) Substantial property transactions CAMA s 310; CA ss 190-191 (except the company is being wound up or is in administration)
3) Loans, quasi loans, security for loans and guarantee to directors CAMA s 296; CA, ss 197-19

(e) Power to Appoint and Remove Directors and Auditors from Office

Irrespective of any contractual agreement that directors and auditors have with a company, they can be removed at any time by the shareholders in general meeting. As the highest decision-making organ of a company, the decision to remove directors or auditors which may be exercised by resolution overrides any agreement that the auditors or directors had with the company. However, the affected directors or

auditors can bring a claim against the company for breach of contract and claim damages. See CAMA 288, 409; CA ss 168-169, 510.

Self-Assessment Exercise

1. Identify the species of company contracts that may require the approval of members in general meeting.
2. Is a shareholder bound to exercise his/her private voting rights for the benefit of the company?

3.4 Summary

Shareholders have a substantial role in promoting the success of the business of companies. Even though the management team is saddled with the responsibility of managing the business of a company, the extent to which their roles can enhance corporate growth is partly dependent on the extent to which the shareholders can be actively involved. To be actively involved in their roles, shareholders must ensure that they obtain information about the company and be regularly acquainted about the activities of the company from time to time. This would ensure that they are sufficiently equipped towards challenging the roles of management.

3.5 References/Further Readings/Web Resources

M.O. Sofowora, Modern Nigerian Company Law (Alpha 1992)

Olakunle Orojo, Company Law and Practice in Nigeria (London Sweet and Maxwell, 1984)

Gower and Davies: Principles of Modern Company Law 10th edn (any relatively recent edition) (London, Sweet and Maxwell 2016)

Sealy and Worthington's Cases and Materials in Company Law (10th edn Oxford University Press 2013)

3.6 Possible Answers to Self-Assessment Exercise

(a) They include directors service contracts longer than 5 years CAMA, s 317; substantial property transactions CAMA s 310 (except the company is being wound up or is in administration); and loans, quasi loans, security for loans and guarantee to directors CAMA s 296.

(b) The shareholder is not bound to exercise her private voting rights for the company but for her individual shareholder interests. This is for the simple reason that she does not owe fiduciary duties to the company: *Estmanco v GLC* [1982]

Unit 4 Majority Rule and Minority Shareholder Protection – I

Unit Structure

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4.9 Possible Answers to Self-Assessment Exercise(s)

4.1 Introduction

The decisions of shareholders are usually made at meetings by voting and passing the relevant resolutions. In light of the voting mechanism, certain conflict may arise between or among the shareholders of a company. It is important to ensure that the conflicts are effectively managed to ensure that the corporate personality objectives of corporate entities are not undermined or used to achieve the objectives of a few individuals at the expense of other shareholders. In light of this, certain rules apply in relation to the use of shareholder powers and the ways that they are exercised in relation to the interest of other shareholders in a company.

4.2 Intended Learning Outcomes

By the end of this unit, you will be able to explain the following:

- the proper plaintiff rule and its exceptions
- derivative action procedure

- unfairly prejudicial conduct
- winding up a company on just and equitable grounds

4.3 The Proper Plaintiff Rule and Its Exceptions

In view of the doctrine of separate legal personality, if a company suffers any detriment, loss or is harmed in any way, it may sue for damages. As a distinctive legal person, it is different from its shareholders. Thus, it is only a company that can sue to remedy any wrong that had been done to it, not its shareholders. In *Foss v Harbottle* (1843) 2 Hare 461, two members brought proceedings against the directors of a company, on behalf of themselves and all other members except those who were the defendants. The directors bought their own land for the company, and it was alleged that the company had overpaid for the land. The members wanted the directors to repay the company the loss from the transaction. The court held that there was nothing to prevent the company from buying the land – action failed. The decision to sue must be taken by the company – by passing ordinary resolution - not individual shareholders. The rule in *Foss v Harbottle* has been upheld in *Prudential Assurance Co Ltd v Newman Industries Ltd (No2)* [1982], CH 204 CA, and *Edwards v Halliwell* [1950] 2 ALL ER 1064.

The rule in *Foss v Harbottle* prevents every member from bringing proceedings against acts of directors – it prevents multiple actions against a single defendant(s) in relation to a single wrong. What is the role of good faith as a factor for commencing statutory derivative action?

4.3.1 The Exceptions to the Proper Plaintiff Rule

1) Fraud on the Minority

Where an act amounts to fraud, and the act has been done by those who are in control of the company, the aggrieved minority may bring a minority shareholder action on behalf of themselves and all other shareholders. They are allowed to bring the action because the wrongdoers will not support the action if the rule that the company must bring the action is not relaxed.

2) Diversion of Business from Company to Director

Cook v Deeks [1916] 1AC 554 – the directors who were also the majority shareholders in the company diverted a contract which the company was pursuing to themselves. They purport to ratify the contract by passing ordinary resolution in the general meeting. An individual

shareholder sued the directors to recover the benefit of the contract. It was held that the majority shareholders could not ratify the contract, the Privy Council allowed the action to proceed.

3) The Sale of Company Assets to Majority Shareholder at Undervalue

Daniels v Daniels [1978] 2WLR 73 – in a minority shareholders' action against directors alleging that they had cause the company to sell a piece of land to one of the directors at undervalue, it was held that minority shareholders could sue where there was fraud… and where the action of the majority and the directors though without fraud confers some benefit on those directors and the majority shareholders. per Templeman J.

4) Disablement of Company

This arises where majority shareholders preventing company from pursing aims that it was established to pursue. *Estmanco v GLC [1982] 1 WLR 2* – the local council formed the company to regulate the management of a block of 60 flats being sold off to owner- occupiers with each of the occupiers acquiring one of the 60 shares in the company when the sale went through. The council covenanted with the company to use its best endeavours to sell all the flats. When 12 of the flats had been sold, control of the council changed, a new housing policy was introduced, and the remaining flats were used to house disadvantaged families. The council had voting control in the company. One of the original occupiers of the flat, also a shareholder in the company successfully obtained the leave of court to bring derivative action against the council. Note that <u>negligence</u> is not covered by the exception in *Foss v Harbottle*. - Where the wrongdoers do not benefit directly or indirectly, fraud on the minority cannot be pleaded.

5) Action to Prevent Illegal Act

Acts of the company officers are attributed to the company. If an illegal act was committed, it is considered to have been committed by the company hence a shareholder can restrain the company from proceeding with an illegal act. The majority shareholders could not ratify an act that was illegal. However, see *Smith v Croft*, <u>where it was held that the views of other independent shareholders were relevant as to whether a minority can sue on behalf of the company</u> *Smith v Croft (No 2)* [1988] CH 114 - sums of money were paid out to assist in the acquisition of the shares of the company. The act of directors who were the majority shareholders was considered to be *ultra vires* and illegal, and the company was entitled to relief. However, the court held that since the independent shareholders – different from the plaintiff and defendant did

not wish the company to proceed with the action, the plaintiff could not sue on behalf of the company.

6) Failure to Follow Procedure

The rule in *Foss v Harbottle* would not apply and a member may successfully challenge a decision where an act of the company fail to follow the required procedure. For example, where special resolution of shareholders is required for a decision to be made, failure to follow this produce can lead to a successful challenge by a minority shareholder.

4.4 Derivative Action

CAMA 2020 ss 346-352
s 346

1) Subject to the provisions of subsection (2), an applicant may apply to the Court for leave to bring an action in the name or on behalf of a company or a company's subsidiary, or to intervene in an action to which the company or the company's subsidiary is a party, for the purpose of prosecuting, defending or discontinuing the action on behalf of the company or the company's subsidiary.

2) No action may be brought, and no intervention may be made under subsection (1), unless the court is satisfied that-

(a) a cause of action has arisen from an actual or proposed act or omission involving negligence, default, breach of duty or trust by a director or a former director of the company;

(b) the applicant has given reasonable notice to the directors of the company of his intention to apply to the Court under subsection (1);

(c) the directors of the company do not bring, diligently prosecute, defend or discontinue the action;

(d) the notice contains a factual basis for the claim and the actual or potential damage caused to the company;

(e) the applicant is acting in good faith; and

(f) it appears to be in the best interest of the company that the action be brought, prosecuted, defended or discontinued.

3) An action under this section may be against the director or any other person (or both).

4) In any action referred to in this section the plaintiff shall have the right to obtain any relevant documents from the defendant and the witnesses at trial and may in pursuance of that right request categories of documents from such person without identifying specific documents.

UK CA *2006* s 260-269
S 260 (3)
A derivative action is an action that is brought by a shareholder on behalf of the company in respect of an actual or proposed act or omission relating to negligence, default, breach of duty or breach of trust – it replaces the common law action which required fraud to be proved.

a) The action is brought by a shareholder
b) The action is brought on behalf of the company because the cause of action is vested in the company
c) The relief is sought on behalf of the company not the shareholder who brought the action.

Derivative action does not require the proof of fraud - a shareholder can bring an action against a director for breaching any of the directors' duties. The cause of action may be against the director or another person (or both). It is immaterial whether the cause of action arose before or after the person seeking to bring or continue the derivative claim became a member of the company. Is shareholder approval or possibility of ratification of an alleged wrong capable of moving the Court to refuse an application for derivative action?

4.4.1 Procedure

Actions or applications brought shall not be stayed or dismissed by reason only that it is shown that an alleged breach of a right or a duty owed to the company has been or may be approved by the shareholders of the company. However, in making an order, the court would consider the extent to which shareholder approval would be likely obtained in respect of the matters complained of.

Similarly, in the UK, the member who wishes to bring a derivative claim must first obtain the permission of the court. The court may either give permission to continue the action or refuse permission and dismiss the action.

In the UK, in deciding whether to grant permission to continue the derivative claim, the court is guided by the following rules:

1) Circumstances where the court must refuse the application before hearing evidence
2) Circumstances where the court must refuse the application after hearing evidence

3) Where the court is not bound to refuse permission, the court must consider certain factors before deciding whether it would refuse or grant permission.

Before hearing the application –when the court must dismiss

If it appears to the court that both the application and the evidence filed by the applicant in support of it do not disclose a *prima facie* case for giving permission (or leave), the court

- must dismiss the application, and
- may make any consequential order it considers appropriate.

If the application is not dismissed, the court may give direction for evidence to be provided so as to hear the application.

On hearing the application:

- The court may give permission or leave to continue the claim or
- refuse permission (or leave) and dismiss the claim, or
- adjourn the proceedings on the application and give such directions as it thinks fit.

4.4.2 Orders the Court may Make

Pursuant to an application for permission to institute a derivative claim in Nigeria, the court may, at any time, make any one or more of the following orders as it deems fit in the circumstance:

1) authorising the applicant or any other person to control the conduct of the action;
2) giving directions for the conduct of the action;
3) directing that any amount adjudged payable by a defendant in the action shall be paid, in whole or in part, directly to former and present security holders of the company instead of to the company;
4) requiring the company to pay reasonable legal fees incurred by the applicant in connection with the proceedings.

4.4.3 Effect of Derivative Action

The effect of the derivative action procedure is that the court is enjoined to consider a range of matters before a derivative action can be brought on behalf of a company. These include the views of persons acting in the position of directors – under UK CA s 172 and whether the acts complained of would be ratified or authorised by the company. In Nigeria, this is apparently expressed as 'the applicant has given

reasonable notice to the directors of the company of his intention to apply to the court'- see CAMA s 346 (2)(b).

4.4.4 Cases Where Permission was Granted or Refused:

1) In ***Franbar Holdings v Patel*** **[2008] EWHC 1534** the shareholder bringing the claim (Franbar) had a 25% stake in the company; the remainder of the shares were held by Casualty Plus. Franbar alleged that the directors of the company that had been appointed by Casualty Plus had diverted business opportunities away from the company to Casualty Plus, had wrongly suspended one of Franbar's nominated directors and had failed to provide adequate financial information. Held - the court considered the importance that a person acting in accordance with a director's duty to promote the success of the company would attach to continuing the claim – would an objective hypothetical director think it would promote the success of the company to pursue the complaint raised by the shareholder? - the court found that such a person would not attach much importance to continuing the claim, this was because of, amongst other things, the claim's chances of success, the costs involved and the likelihood of recovery of any damages actually awarded.

2) In ***Iesini and others v Westrip Holdings,*** [2009] EWHC 2526 claimants asserted that defendants in breach of their duty deprived the company of its assets. Court considered the derivative procedure laid down under Section 260, 263 in conveying that the case was one for the application of Section 263(3)(b), as it was inferred that some directors would not seek to continue the claim. Moreover, it was found that the board took advise on technical matters from eminent counsels before acting. Hence, the permission to continue the claim was refused.

3) In ***Kiani v Cooper***, [2010] EWHC 577 claimant's assertion on the first defendant that - in claiming personally as a creditor of the company, insisting on winding up the company, paying another company from company's bank account, he acted in breach of his duties involving negligence, default and breach of trust. Hence, made out a strong case for breach of fiduciary duty by the defendant. While giving the permission to continue derivative action in company's name in accordance with the procedure followed for a derivative claim under the CA 2006, it was found that the claimant acted in good faith (Section 263(3)(a)), and

having regard to all the factors it was inferred that a director would wish to continue the claim down to disclosure stage.

4) In ***Stainer v Lee***, [2010] EWHC 1539 the Applicant contends that the two directors are in breach of their duties by reason of the circumstances surrounding the lending of very substantial sums of money by the Company to Eldington, a company of which Mr Lee is the sole shareholder and director. Mr Lee, directly and through Eldington, now owns some 87% of the issued shares of the Company. The complaints concern the terms on which those loans were made and, as regards part of the monies, the fact that the loans were made at all. As regards the lending that is subject to the latter complaint, on the basis that the knowledge of Mr Lee is attributable to Eldington, it is alleged that Eldington holds that money as constructive trustee for the Company and so should repay it to the Company - the court identified certain factors, which would influence directors' action in a manner conforming to Section 172 i.e. size and strength of the claim; cost, disruption and impact of the proceedings on the company; funding abilities of the company etc. The circumstances of the case suggested that availability of unfair prejudice proceedings could not be a valid reason to refuse permission. Moreover, having regard to the director acting in accordance with section 172 (under Section 263(3)(b)), permission to continue the claim could be given (subjected to some control) even if the likely level of recovery is not so large, as it may qualify for summary judgment or it may be in the company's potential interest i.e., when the amount of potential recovery is large. The case is an example towards a progress and for believing that derivative claims may be more effective after the CA 2006 was implemented.

4.5 Unfairly Prejudicial Conduct

CAMA 2020 ss 353-356; UK Companies Act 2006, ss 994-996

A member of a company can file a petition in court for relief from conduct which is or which has the potential to be oppressive or unfairly prejudicial to the interests of the members as a whole or to the petitioner. Can you spot any causal link between statutory derivative action and unfair prejudice provision under CAMA 2020?

4.5.1 Scope of Unfairly Prejudicial Conduct

a) The conduct complained of must be both unfair and prejudicial. In Nigeria, the conduct includes oppressive conducts.

b) The conduct could be an actual or proposed act or omission

c) The conduct affects members generally or of some part of its members (including at least the petitioner)

1) The conduct complained of must be both unfair and prejudicial and not merely unfair – *Re Saul D Harrison & Sons Plc,* [1995] 1 BCLC 14.

Saul D Harrison & Sons plc ran a business that was established in 1891 by the petitioner's great grandfather. It made industrial cleaning and wiping cloths, made from waste textiles. It operated from West Ham and after 1989 from Hackney. The petitioner had "class C" shares, which gave her rights to dividends and capital distribution in a liquidation. But she had no entitlement to vote, and the company had been running at a loss. She alleged that the directors (who were her cousins) had unfairly kept running the business just so they could pay themselves cushy salaries. Instead, she said, they should have closed down the business and distributed the assets to the shareholders.

HELD: On the facts, there was no unfairly prejudicial conduct. The board of directors were bound to manage the company in accordance with their fiduciary obligations, the articles of association and the Companies Act. The unfair prejudice action does not protect certain legitimate expectations, akin to those which may affect one's conscience in equity. From being disappointed. But here, there was no legitimate expectation for more than the duties discharged and so no obligations had been breached.

2) The conduct complained of must be both unfair and prejudicial and Not merely prejudicial *Grace v Biagioli* [2005] EWCA Civ 1222
The claimant was a member and director of a company. He was removed from office because he was attempting to set up a rival company. The conduct complained of was prejudicial but, given the obvious conflict of interest that the claimant's actions had created, it was NOT UNFAIR

Re R.A. Noble and Sons [1983] BCLC 273: The company was a quasi-partnership formed on the basis that the petitioner would provide capital and that the respondent would manage the company. The petitioner alleged that he had been excluded from the management of the company. The respondent contended that this had not been done deliberately. It was held that it would depend on whether a reasonable bystander would consider the conduct to have unfairly prejudiced the petitioner's interests. Here, it was prejudicial but not unfair.
From the foregoing, you should note as follows:

a) The test for unfair prejudice is objective, not subjective.

b) No need to show bad faith or intention to cause harm

c) Conduct must cause harm to relevant interest of the member

d) Conduct must be unfair

4.5.2 Cases of Unfairly Prejudicial Conduct

Examples of conducts that have been held to be or capable of being unfairly prejudicial include:

1) Exclusion from management in a company formed as a quasi-partnership - it is not necessary for the members to have equal shares in the venture – in *Quinlan v Essex Hinge Co Ltd* [1996] 2 BCLC 417, a junior partner successfully petitioned following his exclusion from management by a dominant senior partner.

See also *Ebrahimi v Westbourne Galleries Ltd* [1973] AC 360. Mr Ebrahimi and Mr Nazar were partners. They decided to incorporate the business as it was highly successful; they were buying and selling expensive rugs. Their store was originally in Nottingham, and then moved to London at 220 Westbourne Grove. Mr Ebrahimi and Mr Nazar were the sole shareholders in the company and took a director's salary rather than dividends for tax reasons. A few years later, when Mr Nazar's son came of age, he was appointed to the board of directors and Mr Ebrahimi and Mr Nazar both transferred shares to him. After a falling out between the directors Mr Nazar and son called a company meeting, at which they passed an ordinary resolution to have Mr Ebrahimi removed as a director. Mr Ebrahimi, clearly unhappy at this, applied to the court for a remedy to have the company wound up.

The House of Lords held that as a company is a separate legal person, the court would not normally entertain such an application. However, they believed that as the company was so similar in its operation as it was when it was a partnership, they created what is now known as a quasi-partnership. Mr Ebrahimi had a legitimate expectation that his management function would continue and that the articles would not be used against him in this way. Based on the personal relationship between the parties it would be inequitable to allow Mr Nazar and his son to use their rights against Mr Ebrahimi so as to force him out of the company and so it was just and equitable to wind it up. The company was wound up and Mr Ebrahimi received his capital interest

2) Taking excessive remuneration – *Re Cumana Ltd* [1986] BCLC 430

3) Diversion of corporate assets or business opportunity - *Re London School of Electronics Ltd* [1986] CH 211

4) Not paying dividends *Re Sam Weller & sons Ltd* [1989] 3 WLR

Re Sam Weller & Sons Ltd [1990] Ch 682 (Ch). A company making a healthy profit had paid the same relatively low dividends to its members for 37 years. The court held that the company's persistent failure to pay higher dividends amounted to unfairly prejudicial conduct. They continued to draw directors' remuneration and accumulate cash reserves.

5) Stacking with board with directors having interests adverse to the company – *Whyte petitioners* [1984] 1BCC 99

6) Misuse of fiduciary powers – *Scottish Cooperative Wholesale Society Ltd v Meyer*[1959] AC 324

7) A proposal to sell the company's business at a substantial undervalue to connected persons- *Re Posgate and Denby (Agencies) Ltd* [1987] BCLC 8 (also fraud on a minority). Note that - Petitioner's conduct is not relevant when an unfairly prejudicial petition is brought – he does not have to come with clean hands. See *London School of Electronics Ltd* [1986] Ch 211

8) Except the petitioner brought the relevant conduct upon himself – the court may decide that the prejudiced act complained of is not unfair, it may also determine the relevant remedy to be made by the court.

9) A restrictive approach to the rule relating to exclusion from management *O'Neill v Phillips* [1999] 2 ALL ER HL: The company carried on the business of stripping out asbestos from buildings, and Phillips was its sole shareholder and director. In 1983 he appointed O'Neill (who had been employed as a manual worker) to the board of directors and gave him a 25% shareholding in the company. In 1985 they discussed informally Phillip's hope that one day O'Neill would take over the sole management of the company, and he was accordingly allowed a 50% share of the profits of the business. Shortly afterwards, Phillips retired from the management of the company, leaving O'Neill as de facto managing director. By 1991, however, the business was struggling, and Phillips became critical of O'Neill's management. He resumed control of the company and repudiated the profit-sharing agreement. O'Neill filed a petition, arguing that Phillips' conduct amounted to unfair prejudice.

<u>The House of Lords held that, although O'Neill had been prejudiced, it could not be said that Phillips' conduct had been unfair in the circumstances.</u> The fact that the 1985 discussion had never been

formalised was fatal to his petition, as without any firm agreement that O'Neill would manage the company, he had no basis for the argument that he have the right to do so. As for the profit-sharing agreement, all the evidence established that this only was to subsist so long as O'Neill was de facto managing director, and following Phillips' resumption of control, the agreement was no longer in force. Lord Hoffman described O'Neill's petition as amounting to a request to grant a "no-fault divorce", which the section could not provide.

4.5.3 Remedies by the Court

The most common remedy is for the majority to purchase the shares of the petitioner at fair market value, using either of the following bases:

1) Usually at full value - *Re Bird Precision Bellows* [1984] Ch 658
2) Date of valuation may be the date of the hearing - *Re A Company*
3) An independent valuer may be required to determine the value of the shares if parties do not agree on a price. – *Re OC (Transport) Services Ltd* [1984] OCLC 25

4.6 Just and Equitable Grounds to Wind Up a Company

CAMA s 571(f), 573 – UK Insolvency Act 1986 s 122(1) (g)
A company may be wound up by the court if the court is of opinion that it is just and equitable that the company should be wound up. An aggrieved contributory can petition the court for the company to be wound up. A contributory is a person who is liable to contribute to the assets of the company on winding up, this usually include any shareholder, particularly those that have not fully paid for the shares allotted to them. The use of the term contributory does not limit the categories of shareholders that can petition the court, it extends to any aggrieved shareholder. The court is usually reluctant to wind up a viable and prosperous company – this remedy is a drastic one that can only apply in special circumstances, as opposed to the unfairly prejudicial conduct remedy.

4.6.1 The Scope of Application

The court is unlikely to order the winding up of a company where unfair prejudice has not been shown, even though unfair prejudice is not actually the main reason for a claim to wind up a company on just and equitable grounds. The approach was taken in *Re R.A Noble (Clothing) Ltd* [1983] BCLC 273 A narrower view was taken in a later decision in *Re Guidezone* [2000] 2 B.C.L.C. 321 K, a minority shareholder in a family-owned company, GL, petitioned for a forced share buyout of his

interest in the company pursuant to the UK earlier Companies Act 1985 s.459(1) and s.461, together with a winding up order under the Insolvency Act 1986 s.122(1). K maintained that the company had been run in a manner that was unfairly prejudicial to his interests, that the remaining shareholders had refused to agree to the sale of a hotel which comprised the company's principal asset, thus preventing him from realising the value of his investment. K further maintained that the hotel had originally been purchased on the basis that he would have the final say on matters related to it, and that in consequence his legitimate expectation that the hotel would be sold at his request had been frustrated. Jonathan Parker J dismissing the petition, that there had been no unfairness in the way in which the affairs of the company had been run and there had been no agreement between the family members at any stage that K would have the final say on matters concerning the hotel. Given that there was no unfairness, it followed that there was no right to request winding up under s.122(1). With the introduction of the unfair prejudice remedy, the role of the winding up remedy is likely restricted.

4.6.2 Reasons to Apply to the Court for a Winding Up Order

1) Dishonesty by directors

Loch v John Blackwood Ltd (1924) AC 783: The directors representing the majority had refused to call meetings, submit accounts or recommend a dividend. The minority had lost confidence in the management and suspected that the majority were trying to force them to sell their shares at undervalue. HELD: the company should be wound up as there was a justifiable lack of confidence in the management.

NOTE– Mismanagement should be more than mere inefficiency or negligence to successfully petition for winding up.

In *Re Five Minutes Car Wash Service Ltd* [1966] All ER 242: A petition by a former director and minority shareholder complained of disagreements on policy on the board before he ceased to be a director, and unwise and inefficient management by the chairman and managing director C, who had a little under half the issued shares, and that two associated companies holding just under half the issued shares had done nothing to prevent this. On the respondents taking the preliminary point that the petition was demurrable as not alleging any unfairness, harshness or lack of probity by C, the court held, that the petition was demurrable and should be dismissed with costs.

To establish a case of oppression, those who are alleged to have acted oppressively must be shown to have acted at least unfairly towards those who claim to have been oppressed. It is not enough to prove that they have been unwise, inefficient and careless in the performance of their duties. Per Buckley, J.: A mere omission might perhaps amount to oppressive conduct, but it would be necessary to allege and establish that it was designed to achieve some unfair advantage over those claiming to be oppressed before mere omission could be held to be oppressive.

2) Deadlock Within the Company

In *Re Yenidje Tobacco Co Ltd* [1919]2 Ch 426, the company had 2 shareholders, each of them held an equal number of shares and they were the directors. They could not agree on how the company should be run. There was no provision in the articles for breaking the deadlock – A petition for winding up on just and equitable ground was granted.

3) Purpose of the Company Can No Longer Be Achieved

In *Re German Date Coffee Co [*1882] 20 Ch D 169 - A company which had been solely formed to obtain a German patent could not obtain the patent after the application for patent was refused – the company was wound up on just and equitable grounds.
Note that if the company has other purposes which it can still pursue, a winding up petition will not be granted – see *Re Kitson & Co Ltd* [1946] 1 All ER 435

4) Breakdown of Trust and Confidence in Quasi Partnership

Re Yenidje Tobacco Co Ltd [1916] 2 Ch 426 Two men were the sole shareholders and directors of a company, with equal rights of management and voting power. After some time they became very hostile to each other and disagreed about appointment of staff and other matters. All communications between them were made through the secretary. Despite this, the company made substantial profits. Held: Mutual confidence had been lost and the company should be wound up

5) When one member exercises his / her membership rights in an unjust and inequitable way - *Ebrahimi v Westbourne Galleries Ltd* [1973] AC 360 HL

6) Extended Application of Unfair Prejudice

While unfair prejudice petition provides a remedy that is different from the winding up remedy, act of the majority shareholder(s) refusing an application to wind up a company to force members to continue to work together might be sufficient to warrant a winding up, especially where the remedy to purchase the shares of the petitioner will not practicably meet the justice of the matter. – *Amin v Amin [2010]* EWHC 528 (Ch)

4.6.3 Restrictions

A winding up order is an equitable remedy; this means that it is at the court's discretion whether to grant an application or not. The court is not bound to make a winding up order, and the petitioner must have 'clean hands', they must not have caused the problems that requires a winding up.

Also, since a winding up order brings the life of a company to an end it has to be carefully considered. Where there are other alternative remedies, such as the purchase of minority shares, the court may not grant an application for winding up.

SELF-ASSESSMENT EXERCISES

Explain the legal principles relating to the following.

a) The proper plaintiff rule and its exceptions
b) Derivative action procedure obtainable in the UK jurisdiction
c) Unfairly prejudicial conduct
d) Winding up a company on just and equitable grounds

4.7 Summary

The challenges relating to majority shareholder rule and minority shareholder remedies are particularly caused either by conflict of interests affecting directors or conflict of interests relating to majority or co-shareholders. The remedies are aimed at ensuring a fair resolution of the conflicts as best as possible with a view towards preserving the corporate existence of the corporate entity where possible. Ultimately, it can be observed from the analyses above that where the court is satisfied that the interests of a shareholder has been undermined, a suitable remedy is provided to ensure that the interests of the innocent shareholder is protected.

4.8 References/Further Readings/Web Resources

M.O. Sofowora. (1992). Modern Nigerian Company Law. Alpha, Lagos

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CA Riley. (2014). 'Derivative Claims and Ratification: Time to Ditch Some Baggage' *Legal Studies*, 34/4, 582. Link - https://onlinelibrary.wiley.com/doi/epdf/10.1111/lest.12028

4.9 Possible Answers to Self-Assessment Exercise

(a) The proper plaintiff rule draws from the personification of the company. Thus, if a wrong is done to the company, only the company has the right to remedy the wrong, no other person. However, the law recognises that the existence of certain circumstances is capable of disabling the company from remedying the wrong done to it. Hence, the exceptions, which include diversion of business from the company, actions to prevent illegal act, etc.

(b) The procedure in the UK is: (i) circumstances where the court must refuse the application before hearing evidence; (ii) circumstances where the court must refuse the application after hearing evidence; and (iii) where the court is not bound to refuse permission, the court must consider certain factors before deciding whether it would refuse or grant permission.

(c) Unfairly prejudice is a relief provided in the CAMA for cases where a member feels that the activities and affairs of the company are conducted in a manner that is unfairly prejudicial and discriminatory with reference to the interest of the member.

(d) Winding up on just and equitable grounds lies within the equitable jurisdiction of the court. The court will make such an order upon the application of a relevant person or applicant and in cases warranting such an order to be made.

MODULE 5 CORPORATE GOVERNANCE

Unit 1 Meaning and Theories of Corporate Governance
Unit 2 Structure of Corporate Management
Unit 3 Approaches to Corporate Governance Regulation
Unit 4 Board Effectiveness
Unit 5 Corporate Scandals and Failures

Unit 1 Meaning and Theories of Corporate Governance

Unit Structure

1.1 Introduction
1.2 Intended Learning Outcomes
1.3 Meaning of Corporate Governance
1.4 Theories of Corporate Governance
1.4.1 The Agency Theory
1.4.2 Stakeholder Theory
1.4.3 Stewardship Theory
1.5 Summary
1.6 References/Further Reading/Web Sources
1.7 Possible Answers to Self-Assessment Exercise(s)

1.1 Introduction

Company law is mainly concerned with the rules relating to the formation of corporate entities, the way that the activities of the company is run and the functions of the organs of a company. Corporate governance is also concerned with the regulation of corporate entities; however, it is particularly concerned with the ways that the activities of a company and the functions of the organs are controlled. The focus of corporate governance regulation is the accountability of the directing minds and the extent to which they can be made to give stewardship of their roles and policies. Are there any institutional mechanisms for promotion of corporate governance in Nigeria?

1.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- define and explain the meaning of corporate governance; and
- explain some of the theories of corporate governance.

1.3 Meaning of Corporate Governance

Broadly, corporate governance is concerned with the measures that are developed to ensure that company managers and directors do not abuse their corporate powers. The ultimate objective of corporate governance is to promote accountability in the administration of the affairs of a company. Corporate governance has been defined as 'the system by which companies are directed and controlled' – (*The Cadbury Code of Corporate Governance 1992*). Is there any Nigerian Code with comparable or even preferred definition of corporate governance?

This definition is explained further:

'The board of directors are responsible for the governance of their companies. The shareholders' role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company's strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship. The board's action is subject to laws, regulations and the shareholders in general meeting'.

Corporate governance is therefore about what the board of a company does and how it sets the values of the company. It is to be distinguished from the day to day operational management of the company by full-time corporate executives.

1.4 Theories of Corporate Governance

One of the dominant arguments in corporate governance is whether a company should be administered for the interests of shareholders or for every stakeholder in a company, such as creditors, employees, suppliers, customers, the community, etc. These arguments form the bases of the theoretical frameworks of agency theory and stakeholder theory.

(a) The Agency Theory

The agency theory suggests that the relationship between the managers in a company and the shareholders is an agency relationship – the shareholders are the principals (they invest their money in the company) and the managers are the agents. The managers as agents of the shareholders are expected to promote the interests of the shareholder. However, this expectation is not often met because the managers as

agents tend to have different goals from those of the shareholders because of conflicts of interests. Hence the shareholders as principals suffer agency loss, leading to less return on investments, low level of profits and low corporate productivity. These losses arise because shareholders do not manage the company, they rely on the managers (who may not always be reliable) to run the company. It was observed by Adam Smith in as follows:

'...The directors of such companies, however, being the managers rather of other people's money than of their own, it cannot well be expected that they should watch over it with the same anxious vigilance with which the partners in a private co-partnery frequently watch over their own. Like the stewards of a rich man, they are apt to consider attention to small matters as not for their master's honour, and very easily give themselves a dispensation from having it. Negligence and profusion, therefore, must always prevail, more or less, in the management of the affairs of such a company...' Adams Smith *An Enquiry into the Causes and Wealth of Nations* (W. Strahan and T. Cadell, London 1776).

From the analysis of Adam Smith, it can be observed that agency problem has been a major challenge to corporate entities. In light of this agency problem, shareholders incur certain costs in an attempt to address the problem, these include: first, financial reward to managers in the form of executive compensation to encourage managers to promote shareholder interests and second, appointing directors to supervise and monitor the performance of the managers. These mechanisms are aimed towards ensuring that the managers enhance the economic value of companies by making the company profitable for the ultimate benefit of the shareholders as principals.

(b) Stakeholder Theory

Arguments in favour of the stakeholder theory suggest that a wider group of stakeholders are interested in the success of a company, not just the shareholders. These stakeholders include company employees, creditors, customers, suppliers and the community. They have a stake in the company because they can be affected by either the success or failure of the company. Some of these stakeholders have demonstrated several years of commitment to the company and they have provided the support that has helped their companies to expand and become successful. In light of these, the stakeholder theory suggest that managements should run companies for the interest of the wider stakeholder interests, without focusing on the interests of shareholders.

(c) Stewardship theory

The stewardship theory suggests that managers are stewards of the company and their shareholders. It argues that unlike the agency theory, managers and executive members of the management team as stewards, have common goals as shareholders. They do not have conflicting interests as suggested by the agency theory and that the managers are genuinely interested in promoting the interests of the company. It is argued that management are accountable and are predominantly concerned with promoting the value of the company. In light of this view, it further suggests that the board of directors should not act as monitors of managements, they should not be controlling, rather, they should co-operate with the managements to collectively promote the value of the company.

Self-Assessment Exercises

1) Explain the meaning and objectives of corporate governance.

2) Enumerate the main theories of governance and explain one of them

1.5 Summary

Since corporate governance is concerned with the ways that companies are directed and controlled, it implies that the objective of corporate governance regulation is to promote accountability in corporate entities. It is aimed at ensuring that those who are responsible for managing the business of a company act responsibly and are accountable to the shareholders and arguably other stakeholders of the company.

1.6 References/Further Readings/Web Resources

Christine Mallin. (2018). *Corporate Governance* 6th Edn. OUP, London

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1.7 Possible Answers to Self-Assessment Exercises

(a) Corporate governance is concerned with the measures that are developed to ensure that company managers and directors do not abuse their corporate powers. The ultimate objective of corporate governance is to promote accountability in the administration of the affairs of a

company. Corporate governance has been defined as 'the system by which companies are directed and controlled'

(b) The main theories of corporate governance are agency theory, stewardship theory, and stakeholder theory.

- The stewardship theory suggests that managers are stewards of the company and their shareholders. It argues that unlike the agency theory, managers and executive members of the management team as stewards, have common goals as shareholders.

- Stakeholder theory holds that group of stakeholders are interested in the success of a company, not just the shareholders. They include company employees, creditors, customers, suppliers and the community. They have a stake in the company because they are be affected by either the success or failure of the company.

- The agency theory supposes that the relationship between the managers in a company and the shareholders is an agency relationship – the shareholders are the principals (they invest their money in the company) and the managers are the agents. Most prominently, it holds that the agents will devote their time in festering their own nests against the overriding interest of the shareholders.

Unit 2 Structure of Corporate Management

Unit Structure

2.1 Introduction
2.2 Intended Learning Outcomes
2.3 Executive Management
2.4 Board of Directors
2.4.1 Structure of the Board
2.5 Summary
2.6 References/Further Readings/Web Resources
2.7 Possible Answers to Self-Assessment Exercise(s)

2.1 Introduction

The day-to-day business of a corporate entity is run by executive management team. They set out policies for the growth and productivity of the corporation. To ensure that the management team achieve corporate objectives, a board of directors is appointed to supervise the management team. This unit will briefly examine the role of the supervisory board and management team and the structure of the board. To what extend can it be successfully promoted that the executive management team is a creation of the company's legislation?

2.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- explain the difference between the roles of executive management team and the supervisory board;
- explain the main board structures.

2.3 Executive Management

Persons that are appointed to manage the day-to-day operation of a company form part of the executive management team of the company. They are responsible for setting the company's strategic plans and they develop the investment objectives of the company. They have different designations, for example, finance officer/head of finance or director of finance, director/head of personnel, director/head of administration, etc. by whatever name called. They may form part of the main board of directors of the company. They are usually appointed based on their expertise and/or experience in the relevant areas or department of the company.

The management team of a company is led by a Chief Executive Officer (CEO) or managing director. S/he has overall responsibility and every other heads of department report to him/her and authority and responsibility are delegated downwards to line managers and employees' levels.

This executive management team is appointed by the board of directors of the company. they manage the company's business operations as a whole, which includes planning of different development processes.

2.4 The Board of Directors

The board of directors is appointed to act on behalf of the shareholders of a company to supervise the management team in their day-to-day activities. The board is accountable to the shareholders and each year the company will hold an annual general meeting (AGM) at which the directors usually report to the shareholders on the performance of the company. For example, the board inform the shareholders about the current position of the company, its future plans, strategies, challenges and recommendations on how to move the company forward. Even though the board is accountable to members in general meeting, do you think that the shareholders have sufficient statutory or constitutional muscle to restrain directors' dominance in modern companies?

The objective of the board is to ensure that the economic success of the company is promoted, by directing the company's affairs, whilst meeting the appropriate interests of its shareholders and other stakeholders. In addition to business and financial issues, boards of directors must deal with challenges and issues relating to accountability of the board and the management team, corporate social responsibility and matters relating to corporate ethics. Importantly, the board must ensure that the company complies with the existing regulations.

The board of directors of a company is led the chairman, he/she sets the agenda of the board and provide leadership that can lead and position the board towards effectively supervising the management team of the company. The board is composed of directors appointed by the board (usually confirmed by shareholders in general meeting) including some top executive officers of the company who also acts as directors and other non-executive directors. Board meetings are held periodically to ensure that directors discharge their responsibilities towards the company. The meetings are held in furtherance of the monitoring and supervisory roles of the board. Individual directors can also report on their particular areas of responsibility at the meetings. What is the procedure for appointing chairman of the board?

Board meetings are led by the chairman; s/he ensures that the meeting is conducted in such a way that the business for which it was convened is properly attended to, and that all those entitled to attend the meeting are present and are able to express their views, and that the decisions taken by the board reflects as much as possible the views of the board as a whole.

Individual directors have specific powers that have been given to them by the board. However, the board remains responsible for its actions as a whole. The role of the board includes, appointing directors, appointing the executive management team, setting the agenda of the company, delegate functions to management, exercise accountability to shareholders, among others. The central role of the board includes the following.

1) The board provides entrepreneurial leadership for the company.
2) The board should set the company's strategic aims.
3) Ensure that the necessary financial and human resources are in place for the company to meet its objectives.
4) Review the performance of the company managers.
5) The board should set the company's values and standards and ensure that its obligations to its shareholders and others are understood and met.

2.4.1 The Structure of the Board

There are two main types of board structures, namely unitary board and dual board. Can you hypothesise on the advantages and disadvantages of the unitary and two-tier board structures?

1) Unitary Board

A unitary board is a board that is made up of a single governing body. It can either be composed of a single type of directors or a combination of different types of directors. It can have various structures, these includes; a board with only executive directors; a board with a majority of executive directors; a board with a majority of non-executive directors and a board with only non-executive directors.

A unitary board that is made up of non-executive directors and the executive management team of the company hold meetings as a single board. This type of unitary board system operates in several countries, including Nigeria, the UK and the United States.

Executive directors/management team, as explained above is responsible for the day to day management of the affairs of the company. Non-executive directors are not responsible for the day to day operation of the company. Their responsibilities include supervision of the executives to ensure that the executive directors are actually promoting the set objectives of the company. They are appointed to generally ensure that the executive team do not promote their personal interest, they ensure that the executive team are accountable to the company and its shareholders.

A unitary board that is composed of both executives and non-executives is led by the chair as a whole. While the chair leads other non-executive directors to supervise and monitor the activities of the executive management team, the executive management team is led by the CEO or managing director.

2) A Dual Board Structure / Two Tier Boards

A dual board consists of two separate boards, the two boards meet separately. These include the management board and the supervisory board. The management board (operating) board which is responsible for the day to day running of the company's business consist of executives only and are led by the chief executive / CEO.

The supervisory (corporate) board consists of non-executive directors, led by the chairman / chairperson. The supervisory board is responsible for the strategic oversight of the company; they supervise the management board. Membership of the supervisory board may include shareholders representatives and employees' representatives. The dual board structure applies in Germany.

Since directors are appointed to provide leadership role for the company, they are responsible for ensuring that their companies comply with the relevant corporate governance requirements. Hence, the supervisory board must ensure that the management team and the entire corporate activities are in compliance with existing regulations.

Self-Assessment Exercises

1) What do you consider to be the central role of the board?
2) Explain the ways that unitary and dual board structures are composed.

2.5 Summary

The role of the board of directors of a company and the management team is pivotal to the success of a corporate entity. While the management and supervisory boards have different functions, their ultimate objective is to promote the success of the company for the interests of the shareholders and other stakeholders. Irrespective of the ways that boards are composed or the type of board structure that the company adopts, the board renders account to the company.

2.6 References/Further Readings/Web Resources

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2.7 Possible Answers to Self-Assessment Exercises

(a) I consider the central role of the board to include the following:

- The board provides entrepreneurial leadership for the company.
- The board should set the company's strategic aims.
- Ensure that the necessary financial and human resources are in place for the company to meet its objectives.
- Review the performance of the company managers.
- The board should set the company's values and standards and ensure that its obligations to its shareholders and others are understood and met.

(b) A unitary board is composed of both executives and non-executives and is usually led by the chair as a whole. While the chair leads other non-executive directors to supervise and monitor the activities of the executive management team, the executive management team is led by the CEO or managing director. On the other hand, the two-tier or dual board consists of two separate boards, the two boards meet separately. These include the management board and the supervisory board. The management board (operating) board which is responsible for the day to day running of the company's business consist of executives only and are led by the chief executive / CEO

Unit 3 Approaches to Corporate Governance Regulation

Unit Structure

3.1 Introduction
3.2 Intended Learning Outcomes
3.3 Approaches to Corporate Governance
  3.3.1 Voluntary Approach (Principles)
  3.3.2 Rule-Based Approach
3.4 Summary
3.5 References/Further Readings/Web Resources
3.6 Possible Answers to Self-Assessment Exercise(s)

3.1 Introduction

Corporate governance regulation provides an important complementary regulatory function to the traditional company law regime. The successful implementation of corporate governance regulation largely depends on the suitability of the approach in the particular society where it is expected to be applied. Hence, different approaches have been adopted in different countries, depending on the extent to which the particular approach is suitable. Some of the main approaches will be examined briefly.

3.2 Intended Learning Outcomes

By the end of the unit, you will be able to:

- explain the main approaches to corporate governance regulation; and
- explain the justification for each approach.

3.3 Approaches to Corporate Governance

There are two main approaches to corporate governance regulation, (among other approaches that would not be examined here). These include the voluntary or principles-based approach and the mandatory or rule-based approach. At this point, you will ask what type of approach to corporate governance regulation is obtainable in Nigeria?

3.3.1 Voluntary Approach (Principles)

The principles-based approach to corporate governance regulation does not require a compulsory application of the relevant corporate governance principles. It applies on the basis that the stakeholders in corporate entities having been widely consulted and partly involved in

the development of the principles, they would be encouraged to comply with the provisions of the relevant principles. For example, in the UK, the application of corporate governance code is not mandatory. Its application is based on the 'comply or explain' approach – a company with premium listing should comply with the provisions of the code. Where it does not comply with the code, the board should explain to the shareholders and other stakeholders the reasons for non-compliance with the provision of the code. The 'comply or explain' approach is explained in the *UK Corporate Governance Code 2018* as follows:

At the heart of this Code is an updated set of Principles that emphasise the value of good corporate governance to long-term sustainable success. By applying the Principles, following the more detailed Provisions and using the associated guidance, companies can demonstrate throughout their reporting how the governance of the company contributes to its long-term sustainable success and achieves wider objectives.

Achieving this depends crucially on the way boards and companies apply the spirit of the Principles. The Code does not set out a rigid set of rules; instead it offers flexibility through the application of Principles and through 'comply or explain' Provisions and supporting guidance. It is the responsibility of boards to use this flexibility wisely and of investors and their advisors to assess differing company approaches thoughtfully

The effective application of the Principles should be supported by high-quality reporting on the Provisions. These operate on a 'comply or explain' basis and companies should avoid a 'tick-box approach'. An alternative to complying with a Provision may be justified in particular circumstances based on a range of factors, including the size, complexity, history and ownership structure of a company. Explanations should set out the background, provide a clear rationale for the action the company is taking, and explain the impact that the action has had. Where a departure from a Provision is intended to be limited in time, the explanation should indicate when the company expects to conform to the Provision. Explanations are a positive opportunity to communicate, not an onerous obligation.

The underlying aim of the 'comply or explain' approach is self-regulation not strict adherence to the rule of law. This implies that the application and adherence to the code is voluntary. Companies can comply with certain principles and when they do not comply with any principle, they should explain reasons for non-complying. Compliance

can be influenced by activist shareholders and other stakeholders. Compliance can also be influenced by the need to avoid reputational damage. The first code of corporate governance in the UK was published in 1992 – *The Cadbury Code of Corporate Governance*. The most recent code is *The UK Corporate Governance Code 2018* – it became applicable in January 2019. Is it possible implement an approach that is hybrid, involving voluntary as well as mandatory approach at the same time?

3.3.2 Rule-Based or Mandatory Approach

Mandatory approach to corporate governance refers to the use of rules and the strict enforcement of the rules to ensure compliance. In the United States, there is a mandatory application of corporate governance rules. The strict application was partly influenced by the corporate governance failures that undermined investors' confidence in corporate accountability. The *Sarbanes-Oxley Act 2002* introduced reforms to improve financial disclosures from companies and to prevent accounting fraud. The Act was in response to accounting malpractice in the early 2000s in corporations, such as *Enron Corporation, Tyco International plc* and *WorldCom*.

One of the prominent provisions of the Act is the requirement for certification under section 302 of the Act - the Chief Executive Officer and Chief Financial Officer of a public company are to certify the accuracy of the company's annual or quarterly report, as applicable, and the company's disclosure controls and procedures and internal control over financial reporting. False or misleading certification may lead to personal liability of the CEO and CFO. Hence, the CEO and CFO are motivated to take appropriate steps towards ensuring that misleading information is not published and that the internal control mechanisms of the company are effective. This is ultimately aimed at promoting corporate accountability,

In Nigeria, the current corporate governance code is '*The Nigerian Code of Corporate Governance 2018*'. The code was revised and published by the Financial Reporting Council of Nigeria in 2019. It became applicable in January 2019. The rule-based approach to corporate governance applies in Nigeria - '*apply and explain*' approach. Companies are required to apply the principles of the corporate governance code and further explain how they have applied the principles in relation to their companies.

In the introduction section of the code, the philosophy of the code was explained as follows:

…Where so required, companies should adopt the "Apply and Explain" approach in reporting on compliance with this Code. The 'Apply and Explain' approach which assumes application of all principles and requires entities to explain how the principles are applied. This requires companies to demonstrate how the specific activities they have undertaken best achieve the outcomes intended by the corporate governance principles specified in the Code. This will help to prevent a 'box ticking' exercise as companies deliberately consider how they have (or have not) achieved the intended outcomes. Although the Code recommends practices to enable companies apply the principles, it recognises that these practices can be tailored to meet industry or company needs. The Code is thus scalable to suit the type, size and growth phase of each company while still achieving the outcomes envisaged by the principles.

This implies that the corporate governance code applies mandatorily in Nigeria. This is apparently because of the lackadaisical attitude of corporate entities in complying with previous versions of the code. While this is commendable, the main challenge would be in the enforcement of the principles of the code. The wider challenges in the Nigerian society, such as ineffective institutions and corruption among others may undermined the effective implementation of the code. However, the revised code is a step further, towards enhancing board effectiveness in Nigeria, to enhance market discipline and to instil investors' confidence in the market.

Self-Assessment Exercises

a) Explain the Principles and Mandatory approaches to corporate governance regulation.

b) Contrast the corporate governance approach that is applicable in Nigeria and the UK.

3.4 Summary

Corporate accountability is the objective of corporate governance. The extent to which this can be achieved is largely dependent on the approach to corporate governance regulation. This is further dependent on the peculiar society where the code or rules are to be implemented. In Nigeria, the Financial Reporting Council adopted a mandatory approach

since companies would not likely be inclined to voluntarily apply the code without a mandatory application. This is likely as a result of the challenges of the wider Nigerian society that may undermine a voluntary approach. This includes corruption and other institutional deficiencies.

3.5 References/Further Readings/Web Resources

Christine Mallin. (2018). *Corporate Governance* 6th Edn. OUP, London

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3.6 Possible Answers to Self-Assessment Exercises

(a) The principles-based approach to corporate governance regulation does not require a compulsory application of the relevant corporate governance principles. Conversely the mandatory approach to corporate governance refers to the use of rules and the strict enforcement of the rules to ensure compliance. This approach obtains in the US.

(b) The rule-based approach to corporate governance applies in Nigeria - '*apply and explain'* approach. Companies are required to apply the principles of the corporate governance code and further explain how they have applied the principles in relation to their companies. On the other hand, the approach adopted in the UK is voluntary. Its application is based on the 'comply or explain' approach – a company with premium listing should comply with the provisions of the code. Where it does not comply with the code, the board should explain to the shareholders and other stakeholders the reasons for non-compliance with the provision of the code.

Unit 4 Board Effectiveness

Unit Structure

4.1 Introduction
4.2 Intended Learning Outcomes
4.3 Board Effectiveness
    4.3.1 Composition of the Board with Non-Executive Directors (NEDs Independent Directors)
    4.3.2 Separating the Roles of CEO and Chair of the Board
    4.3.3 Executive Pay and Performance
    4.3.4 Board Committees
    4.3.5 Board Diversity
    4.3.6 Re-election of Directors
4.4 Summary
4.5 References/Further Readings/Web Resources
4.6 Possible Answers to Self-Assessment Exercise(s)

4.1 Introduction

The role of the board of directors is vital towards the successful implementation of good corporate governance practices in corporate entities. From the analyses in Units 1-3 above, it can be observed that the board of directors is responsible for the implementation of corporate governance regulation in corporate entities. For example, in countries where voluntary application of corporate governance principles apply, such as the UK, the board determines whether their company would implement any particular principle. The board is responsible for explaining why they have refused to apply any principle of the corporate governance code. Also, in other countries where mandatory application is required, the board or at least the CEO and CFO –as applicable in the US- are required to confirm that certain mandatory rules have been complied with. This implies that a successful implementation of corporate governance regulations whether voluntary or mandatory is dependent on the extent to which a company has an effective board.

4.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- explain what is meant by effective boards; and
- explain the characteristics/factors of an effective board.

4.3 Board Effectiveness

An effective board of directors is a board that has sound leadership and is composed of a well-balanced board, with appropriate levels of experience, skills, expertise and independent judgment in decision-making. The criteria for an effective board have been suggested to include; recognising the distinction between the supervisory role of boards and managerial role of managements; effective support mechanism to support the board; for example, board committees, effective statutory and regulatory provisions and codes of best practice and effective regulators. An effective board ensures that the value-creation objective of the entity is achieved within the scope of corporate regulation. *The Nigerian Code of Corporate Governance 2018*, Part A principle 1 provides,

A successful Company is headed by an effective Board which is responsible for providing entrepreneurial and strategic leadership as well as promoting ethical culture and responsible corporate citizenship. As a link between stakeholders and the Company, the Board is to exercise oversight and control to ensure that management acts in the best interest of the shareholders and other stakeholders while sustaining the prosperity of the Company.

It is impracticable to identify a comprehensive list or criteria that certainly determines an effective board. A generally acceptable standard for determining an effective board may be elusive in view of the various interests that a corporate entity may seek to promote. However, from the analysis of the role of the board of directors, certain factors may be likely capable of promoting board effectiveness. These include the following.

(a) Composition of the Board with Non-Executive Directors (NEDs Independent Directors)

The composition of the board refers to the mix between executive and non-executive independent directors. For the first time, CAMA 2020 made provisions respecting independent directors in section 275. Do you think the statutory can be efficient in promoting board effectiveness? It is a corporate governance requirement that boards should be composed of executive and non-executive directors. *The Nigerian Code of Corporate Governance 2018* Principle 2 – 2.3 require boards to be composed of the appropriate mix of executive and independent non-executive directors.

2.3 *The Board should consider the following factors in determining the requisite number of its members:*

(a) appropriate mix of knowledge, skills and experience, including the business, commercial and industry experience needed to govern the Company;

(b) appropriate mix of Executive, Non-Executive and Independent Non-Executive members such that majority of the Board are Non-Executive Directors. It is desirable that most of the Non-Executive Directors are independent;

Similarly, the *UK Corporate Governance Code 2018* Section 3 (17) requires the board of directors of listed public companies to be composed of a balanced mix of executives and non-executive directors.

17. The board should establish a nomination committee to lead the process for appointments, ensure plans are in place for orderly succession to both the board and senior management positions, and oversee the development of a diverse pipeline for succession. A majority of members of the committee should be independent non-executive directors. The chair of the board should not chair the committee when it is dealing with the appointment of their successor.

The requirement for non-executive directors to be members of boards is to promote independence and objectivity in the board. It strengthens the board in its supervisory role, and it ensures that the board is capable of challenging the executive management to be accountable.

4.3.2 Separating the Roles of CEO and Chair of the Board

It has been suggested that one of the ways of making boards effective is to ensure that no individual holds both positions of CEO and Chair of the board. In Nigeria (principles 2 – 2.7) and the UK (2 G), the corporate governance requires that the roles of Chair of the board and CEO should be separated, means that one individual should not hold both positions; the roles should be occupied by different individuals. This is to ensure that no one has dominant control over the decisions of the board. Also, it is meant to ensure that a balance is created between the roles of chair who leads the supervisory board and the CEO who leads the day-to-day executive management team of the company. In addition to the provision of the code, it is also required by CAMA 2020, s 265(6) that the chairman of a public company should not act as the chief executive officer of such company.

4.3.3 Executive Pay and Performance

One of the major debates in corporate governance is the level of pay (salaries and compensations) provided to company executives. In certain

instances, company executives receive large amounts of salaries and benefits despite the poor performance of their company. This has led to questions about whether the executives are being rewarded for failure, and it has led to suggestions that executive pay should be linked to corporate performance. This is aimed at ensuring that the level of executive pay should be determined by the extent to which their company is profitable. A more profitable company would lead to higher salaries for executives. However, it has also been suggested that executives should be paid the salaries that they deserve to ensure that companies are able to attract the best and most competent executives.

4.3.4 Board Committees

One of the ways of promoting good corporate governance practices through an effective board is to ensure that committees of the board are composed of the right balance, skills and competence to support the role of the board. Apart from public companies or public interest entities in the context of Financial Reporting Council of Nigeria Act 2011, do you think it is necessary to have board committees in private companies other than small companies in Nigeria? It has been recommended that the committees of the board should be composed as follows:

1) Audit Committee – CAMA, s 404.

Audit committee of the board is responsible for internal controls, approval of financial statements and other significant documents prior to agreement by the full board. It liaises with external auditors and reports to the shareholders. The committee may carry out investigations and deal with matters reported by whistle blowers on fraud. Corporate Governance codes and rules recommend that audit committees should be made up of independent non-executive directors, with at least one individual having expertise in financial management.

2) Remuneration Committee.

The remuneration committees set the remuneration of executive directors, and sometimes other senior executives. The committee is responsible for the formulation of written remuneration policy that should have the aim of attracting and retaining appropriate talent, and for deciding the forms that remuneration should take. It is recommended that remuneration committees should be made up of independent non-executive directors - executives should not fix their own salaries.

3) Nomination Committee

The nomination committee is responsible for the development and maintenance of a formal, rigorous and transparent procedure for making recommendations on appointments and re-appointment of directors to the board of the Company. It also reviews the succession plans for the executive directors and the non-executive directors. It has been recommended that the majority of the members of the nomination committee should be independent non-executive directors.

4.3.5 Board diversity

Essential to the effective functioning of any board is dialogue which is both constructive and challenging. The problems arising from "groupthink" have been exposed in particular as a result of the financial crisis. One of the ways in which constructive debate can be encouraged is through having sufficient diversity on the board. This is not limited to gender and race. Diverse board composition in these respects is not on its own a guarantee. Diversity is as much about differences of approach and experience, and it is very important in ensuring effective engagement with key stakeholders and in order to deliver the business strategy.

The *Nigerian Corporate Governance Code 2018* principle 2- 2.2 provides that

'The Board should assume responsibility for its composition by setting the direction and approving the processes for it to attain the appropriate balance of knowledge, skills, experience, ***diversity*** *and independence to objectively and effectively discharge its governance role and responsibilities'.*

Boards should consider the balance of skills, experience, independence and knowledge of the company on the board, in its evaluation. Its diversity, including gender, how the board works together as a unit, and other factors relevant to its effectiveness should be regularly reviewed.

4.3.6 Re-election of Directors

Directors are usually subject to re-election; they do not hold the positions in permanent capacity. This reminds directors that they can be removed from their positions if they do not promote the value of the company.

Self-Assessment Exercises

1) Briefly discuss some of the factors that can make for board effectiveness.

4.4 Summary

The board of directors of a company is the decision-making organ of the company, having been appointed to manage the business/activities of the company. To ensure that the role of the board is discharged in such a way that meets the objectives of the company, it is important that the board is effective. Some important elements/factors that can promote and strengthen board effectiveness have been examined above. These factors should be periodically reviewed to ensure that boards continue to meet the requirement of an effective board. Other general attributes of an effective board have been suggested to include the following; '6 Cs': commitment, culture, collaboration, competence, creativity and contribution.

4.5 References/Further Readings/Web Resources

Bob Tricker. (2019). *Corporate Governance*: *Principles, Policies and Practices* 4th Edn. OUP, London.

Christine Mallin.)2018). *Corporate Governance* 6th Edn. OUP, London

Francis Okanigbuan J. (2019). **'Institutions and Board Effectiveness: Any link'? The United Kingdom, United States and Nigeria in Perspective** in Ngwu FN, Osuji O, Ogbechie C, Williamson D. eds *Enhancing Board Effectiveness: Institutional, Regulatory and Functional Perspectives for Developing and Emerging Markets.* Routledge, New York

Kose John and Lemma W Senbet. (1998). 'Corporate Governance and Board Effectiveness. 22 *Journal of Banking & Finance,* 371.

4.6 Possible Answers to Self-Assessment Exercise(s)

(a) An effective board of directors is a board that has sound leadership and is composed of a well-balanced board, with appropriate levels of experience, skills, expertise and independent judgment in decision-making. The criteria for an effective board include recognising the distinction between the supervisory role of boards and managerial role of managements; effective support mechanism to support the board; ensures that the value-creation objective of the entity is achieved within the scope of corporate regulation.

Unit 5 Corporate Scandals and Failures

Unit Structure

5.1 Introduction
5.2 Intended Learning Outcomes
5.3 Corporate Scandals and Failures
 5.3.1 Corporate Scandals and Failures in Nigeria
 5.3.2 Corporate Failures Elsewhere
5.4 Summary
5.5 References/Further Readings/Web Resources
5.6 Possible Answers to Self-Assessment Exercise(s)

5.1 Introduction

Corporate failures and scandals are products of the challenges of effective corporate governance administration. Corporate failures and scandals occur globally, these failures have demonstrated the extent of the inefficiency of corporate governance regulation, leading to reviews of the rules of codes of corporate governance at different times in different countries. The failures and scandals have been addressed by strengthening different areas of corporate governance regulation to avoid a re-occurrence of the problems. In this unit, some corporate failures across the world will be highlighted to demonstrate the ways that corporate governance regulations have been influenced by the failures and scandals. Can you distinguish between corporate scandal and company in the vicinity of insolvency?

5.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- identify some of the challenges of corporate governance and the mechanisms that were developed to address the problems.

5.3 Corporate Scandals and Failures

5.3.1 Corporate Scandals and Failures in Nigeria

Several corporate failures and scandals have occurred across the world. This indicates that the problem of ineffective board is not restricted to any particular country. Also, the continuous re-occurrence of corporate scandals and failures is an indication that corporate governance regulation must be reviewed regularly to deal with new and re-occurring

issues. Do agree that strong corporate governance regime would have mitigated the opportunities for corporate scandals witnessed in Nigeria? In Nigeria, the challenges of ineffective boards are mainly caused by CEO dominance, ineffective non-executive directors, corruption, lack of effective shareholder activism, among others. These have led to several corporate failures and scandals, such as, Lever brothers (Unilever), Cadbury plc, Oceanic Bank, Intercontinental Bank, etc. For example, in 2006, it was discovered that overstatements which were between *thirteen* to *fifteen* billion naira were made in the financial accounts of *Cadbury Nigeria Plc*, spanning over a period of three years. The CEO and finance director were indicted for fraud.

Also, in 2009, the Chief Executives of some commercial banks were persecuted for their involvement in corrupt practices relating to financial scandals in their banks: *Bank PHB, Oceanic Bank, Union Bank, Finbank, Afribank, Intercontinental Bank and Spring Bank).*

Attempts towards strengthening board effectiveness in Nigeria was partly influenced by these corporate governance challenges. The review was meant to ultimately ensure that companies abide by corporate governance regulation to promote market discipline and the enhance investor confidence in Nigeria. The current code; the *Nigerian Code of Corporate Governance 2018*, which became effective in January 2019 seeks to promote this objective. The 2018 code among other things, seeks to achieve the following as part of its aims and objectives: See Introduction (B)

...The Nigerian Code of Corporate Governance 2018 seeks to institutionalise corporate governance best practices in Nigerian companies. The Code is also to promote public awareness of essential corporate values and ethical practices that will enhance the integrity of the business environment. By institutionalising high corporate governance standards, the Code will rebuild public trust and confidence in the Nigerian economy, thus facilitating increased trade and investment. Companies with effective boards and competent management that act with integrity and that are engaged with shareholders and other stakeholders are better placed to achieve their business goals and contribute positively to society. In such well managed organisations, the interests of the Board and management are aligned with those of the shareholders and other stakeholders...

While the review of the code is commendable, the extent to which the code can effectively prevent corporate failures and scandals in Nigeria remains to be seen. The effectiveness of the code will be determined by

the extent to which its principles can be applied and enforced, including its capacity to prevent corporate scandals and failures.

5.3.2 Corporate Failures Elsewhere

1) United Kingdom

The historical development of corporate governance regulation in the United Kingdom indicates that financial reporting and corporate accountability scandals, - especially the *BCCI and Maxwell Corporation* scandals - prompted the inauguration of the Committee on the Financial Aspects of Corporate Governance by the Financial Reporting Council. Further to this, corporate governance institutional framework has been developed with considerable focus on the effectiveness of the role of boards of directors. The UK Corporate Governance Code functions on the basis of 'comply or explain'. The non-compliance with the provision of the codes is to be explained to the shareholders of the company who can decide to use the mechanism of shareholder democracy to address any concerns that they may have. The successful implementation of this compliance mechanism is based on the considerations of the informal and formal institutions in the UK which includes shareholder enlightenment, shareholder democracy and access to justice. However, scandals and corporate failures have not been completely eradicated, as indicated in the *Carillion* failure below.

(a) Barings Bank

British merchant bank based in London and the world's second oldest merchant bank (after Berenberg Bank). The bank collapsed in 1995 after suffering losses of £827 million ($1.3 billion) resulting from poor speculative investments, primarily in futures contracts, conducted by its oversee employee, Nick Leeson, working at its office in Singapore. Mr Leeson was the floor manager for Barings' trading on the Singapore International Monetary Exchange. He was also the unit's head of settlement operations. In the latter role, he was in charge of ensuring accurate accounting for the unit. These positions would normally have been held by two different employees, but he held both roles. This meant that Mr Leeson, as trading floor manager would settle his own trades. He was not accountable to anybody since he took both roles. There were no accounting safeguards. In effect, Mr Leeson was able to operate with no supervision from London—an arrangement that made it easier for him to hide his losses. Interestingly, when the bank collapsed, several observers, including Mr Leeson himself, placed much of the blame on the bank's own deficient accounting system / internal control

and risk management practices. A number of people had raised concerns over Leeson's activities, but they were ignored.

(b) Carillion Plc January 2018

Carillion Plc, a facilities management and construction services company. The collapse of Carillion was caused by governance issues, particularly accounting irregularities. Board minutes from May 2017 show that the finance director of Carillion’s construction arm raised questions about accounting practices. Being dissatisfied with the responses that she received from the groups’ chief executive and then finance director she initiated whistle-blowing procedures with the human resource (HR) department. The company ran into trouble after losing money on big contracts and running up huge debts. Some argue that it overreached itself, taking on too many risky contracts that proved unprofitable. It also faced payment delays in the Middle East that hit its accounts: clearly no internal control and lack of effective accounting procedures. It employs over 40,000 workers across the world and about 19,000 in the UK.

2) United States of America and others

In the United States, statutory rules that challenge the role of company boards towards greater accountability have been established to promote board effectiveness as a response to corporate scandals, e.g. the ENRON scandal. The *Sarbanes Oxley Act 2002* was enacted in response to the scandal. *The Sarbanes-Oxley Act* provides a direct and stringent regulatory measure that prescribes personal liability for corporate scandal. This regulation has not totally eradicated corporate failures or scandals in the Unites States. It implies that further review and a periodic re-evaluation of the role of the board of directors and top managements of corporate entities is required.

(a) <u>Enron Corporation Scandal 2001</u>

Within a short period of time, this energy giant went from being one of the biggest companies in the world to being bankrupt. What set the scandal apart from the relatively common instances of accounting fraud were the failures of accounting firm Arthur Andersen LLP, which neglected to report Enron’s crimes and led to the firm’s own dissolution. The auditors were paid large sums of money for non-audit work, they were ‘loyal’ to the directors for their non-audit duties where they received large sums conflicted with their main auditing role. Hence, they could not report the fraud of the directors. The accounting fraud allowed the business to pretend that it was running at $100 billion in revenues through the use of loopholes, poor financial reporting and more to conceal its massive debt.

(b) WorldCom Scandal 2002. Telecommunications company

The company inflated its assets by $11 billion, leading to 30,000 lost jobs and $180 billion in losses for investors. The CEO Bernie Ebber underreported line costs by capitalizing rather than expensing and inflated revenues using fake accounting entries. The company's internal auditing department uncovered $3.8 billion of fraud. Consequently, the CFO was fired, controller resigned, and the company filed for bankruptcy. Ebbers sentenced to 25 years for fraud, conspiracy and filing false documents with regulators. Within few weeks of the WorldCom scandal, the US Congress passed the Sarbanes-Oxley Act which introduced the most sweeping set of new business regulations since the 1930s.

(c) Parmalat -- Italy

Parmalat, a dairy company that is a household name in Italy discovered that it had a €14bn was hidden away from the company's accounting records -a black hole in its books-. The scandal in Parmalat was simply how a small company piled up €14bn of debt without anyone noticing. It was founded in the 1960s by Mr Calisto Tanzi and his family. It had operations worldwide, with revenues of €7.5bn before it collapsed. Mr Tanzi lived the life of a rich man, he had a company jet. Mr Tanzi and some of his fellow executives had enmeshed Parmalat in a bewildering array of borrowings, false accounting, and misleading reports to investors and regulators. These were created to hide accumulating losses that were the result of a series of expensive acquisitions after Parmalat went on a buying spree in the 1990s following a flirtation with bankruptcy and a restructuring of its operations. Many of the acquisitions were financed by bond issues underwritten by the leading investment banks. Within a few years it came crashing down. Mr Tanzi was detained before Christmas 2003 after leading Italian and international investigators on a wild goose chase for seven days. Several former executives of Parmalat have been convicted for their roles in the fraud and were given short prison sentences.

Self-Assessment Exercises

1. Identify and explain at least one corporate scandals that has occurred in Nigeria.
2. What factor(s) caused these corporate scandals?

5.4 Summary

The few examples of corporate scandals and failures outlined above, is an indication that good corporate governance is determined by effective boards. Since corporate governance is mainly about the extent to which companies are accountable, an effective board is a necessary aspect of corporate governance regulation. From the examples above, we can observe that top corporate executrices were the main players in the scandals. The weakness and lack of independence of some members of their company boards contributed to the successful fraudulent conducts of these corporate executives. This implies that every member of the board of a company must be proactive, committed and be ready to question the activities of other members of the board where there is a reason to do so while also providing a supportive role.

5.5 References/Further Readings/Web Resources

Christine Mallin. (2018). *Corporate Governance* 6th Edn. OUP, London.

Ben Oghojafor, Olusoji George and Oluwakemi Owoyemi. (2012). Corporate Governance and National Culture are Siamese Twins: The Case of Cadbury (Nigeria) Plc. 3 *International Journal of Business and Social Science* 269. Link - http://www.ijbssnet.com/journals/Vol_3_No_15_August_2012/30.pdf

5.6 Possible Answers to Self-Assessment Exercises

(a) The cases of several corporate failures and scandals in Nigeria include Lever brothers (Unilever), Cadbury plc, Oceanic Bank, Intercontinental Bank, etc. In 2006 it was discovered that overstatements which were between *thirteen* to *fifteen* billion naira were made in the financial accounts of *Cadbury Nigeria Plc*, spanning over a period of three years. The CEO and finance director were indicted for fraud. Also, in 2009, the Chief Executives of some commercial banks were persecuted for their involvement in corrupt practices relating to financial scandals in their banks: *Bank PHB, Oceanic Bank, Union Bank, Finbank, Afribank, Intercontinental Bank and Spring Bank).*

(b) Some of the causes of corporate scandals and collapses include the challenges of ineffective boards are mainly caused by CEO dominance, ineffective non-executive directors, corruption, lack of effective shareholder activism, outright managerial fraud and opportunism.

MODULE 6 MERGERS, ACQUISITIONS AND THE MARKET FOR CORPORATE CONTROL

Unit 1 Types of Acquisitions and Theories of Mergers and Acquisitions
Unit 2 Mechanisms for Corporate Acquisition
Unit 3 The Regulatory Framework for Corporate Acquisitions in Nigeria
Unit 4 Takeover Hypothesis
Unit 5 Managerial Defences

Unit 1 Types of Acquisitions and Theories of Mergers and Acquisitions

Unit Structure

1.1 Introduction
1.2 Intended Learning Outcomes
1.3 Types of Acquisitions/Takeovers
  1.3.1 Friendly Takeover
  1.3.2 Hostile Takeover
  1.3.3 Reverse Takeover
  1.3.4 Backflip Takeover
  1.3.5 Buyouts (MBOs or LBOs)
1.4 Theoretical Perspectives of Mergers and Acquisitions
  1.4.1 Value-Creation Hypothesis
  1.4.2 Value-Redistribution Hypothesis
  1.4.3 Value-Destroying Hypothesis
1.5 Summary
1.6 References/Further Readings/Web Resources
1.7 Possible Answers to Self-Assessment Exercise(s)

(a) Introduction

Mergers and acquisitions have apparently become an inevitable phase in the lives of companies. A company may either acquire another company or be acquired by another. In other instance, companies may merge their operations. Although, some companies do not experience any form of merger or corporate acquisition in their lifetime, they may be threatened by corporate acquisitions activities, especially when there is an increase in mergers and acquisitions activities in a relevant industry. There is limited controversy when companies merge, since mergers occur after friendly negotiations between the affected companies. Whereas in takeovers/acquisitions, the controversies often arise from disagreements, leading to hostilities between the managements of the affected

companies. Thus, the module would focus on acquisitions/takeovers, its theories, regulatory framework and other related matters. This unit briefly outlines the types of acquisition and its theoretical perspectives. Note that in this module, 'takeovers' or 'acquisitions' would be used interchangeably.

(b) Intended Learning Outcomes

By the end of this unit, you will be able to:

- explain the different types of acquisitions; and
- explain the main theoretical perspectives of corporate acquisitions.

(c) Types of Acquisitions/Takeovers

Investors seeking to acquire a company can achieve their objective through friendly takeover, hostile takeover, reverse takeover or a backflip takeover. Do you see any discernible difference between takeover and mergers and acquisition?

1.3.1 Friendly Takeovers

Friendly takeover may also be referred to as '*a negotiated takeover*'. It involves series of negotiations between the acquiring investors(s) and the target board. The shareholders of the target company receive cash and/or shares in the acquiring company as part of the process leading to the successful completion of the takeover. As its name suggests, its entire process is aimed at creating synergies between the acquirer and the target company.

1.3.2 Hostile Takeovers

Hostile takeovers are attempts by acquiring companies towards gaining control of corporate powers through different methods. These include direct negotiations with shareholders in the target company and the purchase of shares in the target company discreetly. A hostile takeover may also commence because of failed negotiations of a friendly takeover attempt. In view of the nature of this type of takeover, it has been suggested that hostile takeovers are the most effective ways of getting rid of non-performing managers without bribing them.

Considering the direct negotiations between the shareholders of a target company and the outside investors, a hostile takeover has the characteristics of promoting private benefit to the negotiating parties,

rather than conferring any form of social value. Hostile takeovers can be privately beneficial even though they are not socially desirable. They can lead to a renegotiation of contracts of labour and employee dismissal, contrary to the theory of a corporation as a nexus of contracts

While friendly takeovers are mainly non-controversial, hostile takeovers represent a control contest amongst the incumbent managers in the target company, the shareholders and the outside investors. The nature of this type of takeover suggests that it is mostly activated through the mechanisms of the direct purchase of the shares of the shareholders in target companies by the outside investors who are keen on taking over control of the company. This is usually done through tender offers wherein an offer is made by the outside investor to the shareholders of the target company to tender (offer their shares to be bought at a specific price, within a given period of time) their shares for sale, usually at a price higher than the market value of the shares

1.3.3 Reverse Takeover

A reverse takeover is the type of corporate takeover where the shareholder(s) of a private firm purchase a large majority of the shares of a public company. One of the main objectives of this type of takeover is to achieve public company status for the acquirer private company, without the usual process of re-registration from private to public company.

1.3.4 Backflip Takeover

A backflip takeover occurs where an acquiring company becomes the subsidiary of the acquired company. This type of takeover occurs where the acquired company has a well-known market brand, but it became a takeover target because of its challenging financial status. The combined company often retains the name of the acquired company because of its brand, customer base, and other goodwill advantage.

1.3.5 Buyouts (MBO or LBO)

A buyout is the acquisition of a controlling interest in a company. If the stake is bought by the firm’s management, it is known as a management buyout MBO. Where loan is used to fund the buyout, it is called a leveraged buyout LBO. The assets of the acquiring company and the acquired company can be used as collateral for the loan.

1) Management Buyout - MBO

It is a type of buyout where the management board of the company acquires the controlling shares of the company. Usually, the management would obtain financial support from a private investment group. The providers of finance offer the financial assistance to the management on the basis that the management understand the business and can project the future prosperity of the company. However, it may also be difficult for the management to convince investors to fund the acquisition, especially if there are concerns that the managements were partly responsible for the financial challenges of the company.

2) Leveraged Buyout - LBO

This a type of buyout where investors obtain loan to acquire the company and use the assets of the company as a collateral to secure the loan. There are different types of LBO.

(a) The Repackaging Plan

A private company acquires a public company using leveraged loans and the company becomes a private company. The acquired company is made a private company so that the investors can take time to repackage the company and avoid public attention. Then the company is offered for sale, by issuing IPO – initial public offer- new shares are issued to the public, the shares are sold, and the company becomes a public company again with a better brand, having being repackaged.

(b) The Split UP

When a company is acquired through leveraged buyout, the different sections or different operations of the company can be sold if the investors realise that it would be more profitable to unbundle the company and sell the separate business sections rather than selling the entire company as a single entity.

(c) Saviour Plan

This method is not commonly used – It applies where management and employees acquire the company using leveraged loans. It is similar to MBO but employees are also involved. Thus, it can be referred to as employee owned.

(d) Theoretical Perspectives of Mergers and Acquisitions

1.4.1 Value-Creation Hypothesis

Takeovers can be used to create value, by replacing low productive management personnel with a different set of management that can enhance the economic value of the firm. Corporate acquisition enables the efficient combining of assets which are worth more together than they are worth apart. This is the *value-creation hypothesis* of takeovers. This hypothesis also emphasises that the value of firms can be enhanced by fusing the operations and assets of different companies into a single entity. A combination of the operations of two companies can save costs through economies of scale, whereby a combined firm can produce more resources in less time, using a more formidable input. This can arise from maximizing the utilisation of plant, machinery and property. E.g. Two companies with two under-utilised call centres could use only one call centre to run their operations. This would lead to cost saving, from rent, labour, running costs and equipment.

1.4.2 Value-Redistribution Hypothesis

Takeovers can also be used as a tool towards redirecting and redistributing resources from one corporate constituent to another, without necessarily adding value. This is referred to as the *value-redistribution hypothesis* of takeovers.

When investors purchase shares at a premium and they gain control of corporate powers, they can renegotiate the existing contracts with the management and employees. The management of the acquired company may be dismissed; a large number of employees may also be disengaged. Large premiums paid to shareholders of target companies may represent losses to shareholders of acquiring companies. These loses can be mitigated by a reduction of employees post-takeovers. For example, the interests of employees are often traded to mitigate the general expenditure of a corporation after engaging in costly acquisition. This does not add wealth to corporate entities or acquiring shareholders, it merely reduces further corporate expenditure. E.g. If two companies combine their operations and run their production from a single plant, there may be the need to dismiss some employees. When American company *Kraft Foods* acquired UK based *Cadbury* in 2010, the plant in Somerdale was closed, employees were dismissed. Although dismissed employees may be employed elsewhere and their dismissal may be needed to align the company operation, it is arguable whether takeovers should be or can be concluded without the need to dismiss employees.

1.4.3 Value Destroying

Empirical evidence suggests that takeovers can destroy value, largely because of the high cost of the exercise. The high cost of acquisition is

beneficial to the shareholders in target companies and the shareholders in acquiring companies must retain their shares in the company and wait for gains to materialise. The high premium paid by the acquiring company is suggested by several research studies to be responsible for the losses after acquisitions. While gains to target shareholders are clear and instant, gains to acquiring shareholders are not clear and sometimes shown to be little or negative. Some research result show that acquisitions can lead to gains for acquiring shareholders, none has shown that the gains to acquiring shareholders and target shareholders are equally shared – target shareholders are mainly reported to make substantive gains when compared with acquiring shareholders. Although research into the level of value added to acquiring company shareholders and target company shareholders provide mix results, the results are in favour of gains to target shareholders. Since target shareholders often take the wealth out of the company – they transfer their shares to the acquirer- it is arguable that they benefit from acquisitions without question, while gains to acquiring shareholders are unclear.

Self-Assessment Exercises

1) Identify the main types of corporate takeovers

2) Briefly explain one of the main theoretical perspectives of takeovers.

(e) Summary

Corporate acquisitions affect the interests of the various corporate constituents, especially the interests of shareholders and employees. The objective that the main investors seek to achieve apparently determine the type of takeover that would be adopted. Also, the acquisition objectives can determine the particular theoretical perspective that would apply after an acquisition has been completed. Irrespective of the type of takeover/acquisition that is adopted, the major objective of a takeover should be to promote synergies between the acquired/target company and acquiring company, this synergistic objective will be explained in Unit 4 below.

(f) References/Further Readings/Web Resources

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1.7 Possible Answers to Self-Assessment Exercises

(a) The main types of takeovers are friendly takeover, hostile takeover, reverse takeover, backflip takeover, and buyout – which may be management by objectives or leveraged buyout.

(b) One of the main theoretical perspectives is value redistribution thesis, which occurs when takeover is used as a tool towards redirecting and redistributing resources from one corporate constituent to another, without necessarily adding value. When investors purchase shares at a premium and they gain control of corporate powers, they can renegotiate the existing contracts with the management and employees. The management of the acquired company may be dismissed; a large number of employees may also be disengaged. Large premiums paid to shareholders of target companies may represent losses to shareholders of acquiring companies. These loses can be mitigated by a reduction of employees' post-takeovers. For example, the interests of employees are often traded to mitigate the general expenditure of a corporation after engaging in costly acquisition. This does not add wealth to corporate entities or acquiring shareholders, it merely reduces further corporate expenditure.

Unit 2 Mechanism for Corporate Acquisition

Unit Structure

2.1 Introduction
2.2 Intended Learning Outcomes
2.3 Direct Purchase of Shares
    2.3.1 Open Market Purchase
    2.3.2 Tender Offers
2.4 Proxy Contests
2.5 Scheme of Arrangement
2.6 Summary
2.7 References/Further Readings/Web Resources
2.8 Possible Answers to Self-Assessment Exercise(s)

2.1 Introduction

The mechanisms that are used to acquire a company can also be referred to as tactics or devices. Any of these mechanisms can be used by prospective acquirer to obtain control of a target company. The choice of the particular mechanism that is adopted would be dependent on prevailing factors such as costs of the acquisition process and the prospect of success of the acquisition, among other factors. Is acquisition one and the same thing as scheme of arrangement or compromise under CAMA 2020?

2.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- explain the main mechanisms/devices that can be used to acquire a company, including direct purchase of shares, proxy contest and scheme of arrangement.

2.3 Direct Purchase of Shares

Direct purchase of shares is the most obvious and direct method through which the controlling powers of a company may be acquired by outside investors. This method which enables investors to directly acquire the controlling powers of the company may be attempted through one or more of the following ways, namely:

1) The direct purchase of shares from an individual or individuals who have a controlling block of shares.

2) The gradual acquisition of a controlling number of shares through anonymous open market transactions. – Open Market purchases
3) A tender offer to purchase shares at a specific price above the usual market price.
4) An offer of marketable securities in exchange for the required number of shares.

2.3.1 Open Market Purchases

The acquisition of shares by a prospective acquirer in the open market is one of the ways of gaining control over a company. In practice, it applies by identifying the shareholders of the target company, approaching the shareholders, directly or indirectly and acquiring their shares, usually at market prices.

1) Advantages of Open Market Purchase

(a) Acquiring shares in the open market is initially less expensive, since the shares are usually acquired at the applicable market price.
(b) This method of acquisitions may be easier with less dispersed shareholding.
(c) Open market purchase is a quicker way of obtaining ownership of shares. This only applies after the shareholders in a particular company have been identified and they are willing to sell their shares.

2) Challenges of Open Market Purchase

(a) There could be legal restrictions. For example, in the United States, - Delaware, 15% holders are restricted from engaging in a takeover for 3 years under the Delaware General Corporations Law.
(b) A company with dispersed shareholding will be difficult to be acquired by open market bid. The potential acquirer would face challenges in locating majority of the shareholders, except a few majorities of the shareholders hold the requisite majority of shares. Nevertheless, they may be unwilling to sell their shares at market price if they know that the reason for the share purchase is to acquire the company.
(c) Further, as soon as information is released in the market that an investor is acquiring shares of a certain company, the prices of the outstanding shares would rise to a point where the acquirer may not be able to acquire the company. The rise will increase

steadily in each transaction. This is the main reason that tender offer is preferred.

2.3.2 Tender Offer

A tender offer is a formal proposal made directly to the shareholders of a company to buy their shares with cash or share exchange (or other securities) or both cash and shares. A tender offer occurs, when a prospective buyer offers or invites the shareholders of a target company to offer for sale or tender their shares at a stated price, usually above the market price. Tender offers may either be made by 'cash tender offer' or 'a public exchange offer'.

Cash tender offer involves the use of cash by outside investors to purchase certain number of shares directly from the shareholders of the target company through the bidding process, usually at a premium above the market value. Where a tender offer is made by share exchange, the outside investors usually offer company securities to the shareholders of the target company in exchange for certain number of shares. It may also include a combination of cash and shares. A tender offer may include an agreement to keep an offer for sale open within a specific period of time. The nature of the offer may also contain the condition that certain percentage of the total shares should be offered for sale. The conditions may also include the right of the investor to withdraw the offer if the required number of shares are not tendered.

1) Top Up Option

A "top-up" option is a stock option granted by the board of directors of a target corporation to a bidder which has agreed to commence a tender offer, in most cases for all the outstanding shares of the target corporation. The "top-up" option, when exercised, enables the bidder to purchase that number of newly issued shares of the target corporation's capital stock which, when added to the number of shares of capital stock owned by the bidder immediately following the tender offer, constitutes at least 90% of the outstanding shares of capital stock on a fully diluted basis. As a result, when a bidder holds a "top-up" option, the bidder will be able to complete a short form merger even though the bidder, after closing the tender offer, may not hold 90% of target's capital stock. By design, a "top-up" option may be exercised only after the tender offer closes and generally is exercisable for the same consideration per share that the bidder offered in the offer. In most cases, a "top-up" option will provide that it may be exercised only if the bidder's tender offer succeeds in acquiring some threshold amount of the target's capital stock

2) Advantages of Tender Offers

(a) It is a quicker means of concluding an acquisition.
(b) It is easier, since a single offer is made to the required number of shareholders, especially when there is dispersed shareholding.
(c) Offeror can withdraw from the bid if the conditions are not met, e.g. That certain percentage of shares should be tendered.
(d) Relatively cheaper, since it prevents the upward spiral of prices if individual shareholders are contacted in open market purchases.

3) Challenges of Tender Offers

(a) It is regulated and several disclosures must be made.
(b) It may be expensive, since control is bought not merely shares.
(c) Competition can also increase the prices.
(d) Management may device defensive measures for several reasons (to prevent their dismissal, or to protect their shareholding or to increase the bid price or for other reasons. Although these measures may be limited for example in the UK and regulated in the US.
(e) Free riding by minority shareholders – squeeze out or top ups may defeat free riding.

2.4 Proxy Contests

Proxy contests occur when there is active competition between two or more groups, usually the incumbent managers and a group of dissident shareholders. The aim is to either solicit proxies to elect their candidates or to vote in favour of desired policies or against such policies. Typically, proxy contests occur between the management of the company and some dissident shareholders whereby company shareholders either vote for the slate of directors proposed by management or for a rival slate proposed by the dissidents who seek to replace them. Proxy contests may occur for the purpose of gaining control of the management of the company, by seeking a majority position of the board. It could alternatively occur for the purpose of proposal contests, in which dissidents seek to vote to defeat a management-sponsored proposal or to initiate their own proposal. Where the dissident shareholders are successful with the election of new directors, a new management team is appointed, but where they fail to replace the directors, the management team retain their positions. Shareholders may increase their support for outside investors in proxy contests, where they believe that the current managers are not sufficiently promoting their interests. Companies which have a low rate of dividend payment, relative to other companies in the same industry are more likely to become targets of a proxy contest.

1) Advantages

(a) It is cheaper than other traditional means of acquiring control over a company. It merely requires an outside investor to successfully convince the shareholder with majority voting shares to support the proxy war.
(b) There is less regulatory hurdle, unlike tender offers.

2) Challenges

(a) The chances of succeeding in a proxy contest for a takeover is not as high as open market bid or tender offer.
(b) The outside investor must obtain the support of the shareholders with the majority voting rights. In a company with dispersed shareholding, it would be difficult to contact the majority shareholders.
(c) The cost of obtaining information about the shareholders may also undermine the exercise.
(d) Managements may use certain measures to gain support of shareholders, such as increased dividend payments, short term improvement in the operating performance of the firm.

2.5 Scheme of Arrangement

CAMA 2020 ss 434-439; UK Companies Act 2006, ss 895, 899
Scheme of arrangement can also be used to take over the control of a company. It does not have the character of corporate acquisitions as a mechanism of the market for corporate control because it can include arrangements with creditors who did not intend to obtain control of the company.

In relation to takeovers, scheme of arrangement is used to restructure a company's capital. An arrangement or compromise can be proposed between a company and its members for the purpose of a takeover, sanctioned by the court. A scheme is an offer to acquire control over the shares of the company (App 7 Takeover Code). A scheme must be approved by most shareholders - 75% of the voting class of the shares that are subject to the scheme of the target company and the High Court. (the acquirer cannot vote if they already have some shares in the company). The arrangement is binding on the company and its participating shareholders. Can you attempt to compare the takeover options with business rescue provisions of CAMA, otherwise known as administration?

1) Advantages

It creates certainty- once shareholders vote in support of the scheme, it becomes binding on the company and the participating shareholders.

2) Challenges

The use of scheme of arrangement to acquire a company requires the support of the board of the target company. It cannot be used in hostile acquisitions.

Self-Assessment Exercises

1. Outline briefly the various mechanisms that can be used to acquire a company
2. What are the benefits and challenges of at least one of these methods?

2.6 Summary

Although, several interests are affected in a corporate acquisition, such as shareholders, employees, creditors, directors, and managers; only shareholders and directors/managers appear to have control over the exercise. This can be observed from the above devices used to obtain control over a company, except scheme of arrangement which included creditors input, however, it is not a major acquisition device. It can also be observed that the device used to acquire a company is largely dependent on the benefit to be derived by the main participants. In recent times, tender offer remains the most prominent device used to takeovers a company considering the relative certainty. Despite the high costs of acquiring a company through tender offers, it remains relatively cheap compared to open market purchase which is the next popular mechanism for corporate acquisition.

2.7 References/Further Readings/Web Resources

Francis Okanigbuan Jnr. (2020). *Corporate Takeover Law and Management Discipline.* Routledge, Oxon.

David Kershaw. (2016). *Principles of Takeover Regulation.*OUP, London

Fischel D R. (1978). 'Efficient Capital Market Theory, the Market for Corporate Control and the Regulation of Cash Tender Offers'. 57 *Texas Law Review* 1 Link-- -

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2.8 Possible Answers to Self-Assessment Exercises

(a) The various mechanisms include direct purchase of shares (which can be executed either through open market purchases or via tender offers); proxy context and scheme of arrangement or compromise.

(b) The benefits of a scheme of arrangement or compromise is that it creates certainty- once shareholders vote in support of the scheme, it becomes binding on the company and the participating shareholders. On the downside its use to acquire a company requires the support of the board of the target company. It cannot be used in hostile acquisitions.

Unit 3 The Regulatory Framework for Corporate Acquisitions in Nigeria

3.1 Introduction
3.2 Intended Learning Outcomes
3.3 Tender Offers
3.3.1 Target Company
3.3.2 Acquiring Company
3.3.3 Open Market Purchase
3.3.4 Scheme of Arrangement
3.4 Summary
3.5 References/Further Reading/Web Sources
3.6 Possible Answers to Self-Assessment Exercise(s)

3.1 Introduction

Takeovers and mergers are regulated in Nigeria to protect the interests of investors and to provide fairness in market competition. These objectives are mainly promoted by the following regulations; *The Investments and Securities Act 2007* (ISA 2007) administered by the Securities and Exchange Commission SEC and the *Federal Competition and Consumer Protection Act, 2018* – (FCCPA 2018), administered by the Federal Competition and Consumer Protection Commission. Other applicable regulations include, *Companies and Allied Matters Act, 2020* (CAMA 2020); the *Central Bank of Nigeria Act 2007* (CBN Act 2007) and *Banks and Other Financial Institutions Act 2020* (BOFIA 2020). When banks and financial institutions are involved in transactions leading to takeovers and mergers, the affected institutions may be required to comply with the CBN Act and BOFIA in addition to the main regulation under the ISA 2007 and the FCCPA, 2018.

3.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- identify the main regulatory framework that applies in relation to corporate acquisitions in Nigeria.

3.3 Tender Offers

The major mechanism used to take over a company is tender offers. Tender offers were examined in Unit 2 above. The applicable rules that govern the use of tender offers are provided in the *Investments and Securities Act 2007* ISA -2007. These rules apply in relation to the target company and the acquiring company. See the ISA 2007, part 12, section

117 – 151. *The Federal Competition and Consumer Protection Act 2018* also applies. The Federal Competition and Consumer Protection Commission must be satisfied that the mergers or acquisition if approved, would not lessen competition, and promote monopoly. See the FCCPA 2018, Part 12, section 92 - 103.

3.3.1 Target Company

One of the objectives of the ISA is to protect investors when mergers and takeovers are made. The extent to which this objective can be achieved is dependent on the relevant provisions of the ISA that are capable of activating investor protection and the maintenance of a fair and transparent market.

The ISA 2007, s 140(1) provides –

Where ... a bid under a takeover bid is dispatched to each of the directors of an offeree company, the directors shall send a directors' circular to each shareholder of the offeree company and to the Commission at least seven days before the date on which the takeover bid...is to take effect.

This implies that the directors of the target / offeree company should notify the shareholders in the company that an offeror has made an offer to acquire their shares for the purpose of taking over the company. The shareholders should be informed not more than 10 days after the directors receive the takeover bid from the offeror and at least 7 days before the takeover bid takes effect.

Shareholders are not required to accept a bid or make any decision until they receive the director's circular about the bid. The circular usually contains the directors' advice to the shareholders whether they should accept or reject the offer.

Section 140 (2) of the Act provides…

Unless the directors of an offeree (target) company send a director's circular as required by subsection (1) of this section within ten days of the date of a takeover bid, the directors shall forthwith notify the shareholders and the commission that the directors' circular shall be sent to them and may recommend that no shares be tendered pursuant to the takeover bid until the directors' circular is sent.

The shareholders are free to make their independent decision whether to accept or reject the bid. They are not bound by the advice of the directors.

3.3.2 Acquiring Company

The ISA 2007 creates important role for the board of directors of a company that seeks to engage in acquisition. An acquisition must be approved by the board of the offeror / acquiring company. Under s 137(1) –

A corporation shall not make a take-over bid either alone or with any other person unless the making of the takeover bid has been approved by a resolution of the board of the directors of the corporation.

Also, the *Securities and Exchange Commission, Rules and Regulations* SEC Rules and Regulations which is applicable to takeovers pursuant to the ISA 2007, s 313 recognises and confirms the role of the board of directors of the acquiring company in approving a takeover bid. Rule 445(2) provides –

Where a takeover bid is made by a corporate body, a resolution of the directors approving the bid shall accompany the bid. The resolution shall be signed by at least one director and the company secretary.

The role of the board of directors of acquiring companies during takeovers may be considered to have been recognised by the regulatory mechanisms because of their managerial authority.

Under the ISA 2007, s 136 (1) (a) and the SEC Rules and Regulation 2013, rule 446 (a), the following must be included in a takeover bid –

A bid being an invitation under a takeover shall be incorporated in a document that:

(i) states the full names and addresses of the offeror;
(ii) the addresses should be a street address and post office box (if any) where the offeror is a corporate body, the name of the current head office address and a statement of the date at which the approval of the directors of the company was given.

The requirement for board approval may have been included in the ISA in furtherance of the role of the board in managing the business of a company. Hence, corporate acquisitions are being considered here as a usual investment decision that should be taken by the board of directors.

3.3.3 Open Market Purchase

Open market purchase was examined in Unit 2 above. Open market purchase is regulated by the applicable capital market rules that relates to the issuance of shares and the acquisition of shares in the capital market. See the ISA 2007 generally.

3.3.4 Scheme of Arrangement

This is also briefly explained in Unit 2 above as one of the uncommon ways that a company may be acquired. The rules that apply in relation to scheme of arrangement are outlined in CAMA 2020, ss 434-439.

Self-Assessment Exercises

1. Outline the applicable regulations for mergers and acquisitions in Nigeria.
2. What is the objective of the FCCPA 2018 in relation to mergers and acquisition?

3.4 Summary

The important role of the board of directors and the entire management team of a company has been further strengthened by the regulatory framework for corporate acquisitions in Nigeria. This is evident in the requirement for board approval before a takeover bid is made in the ISA 2007. It would be expected that shareholders should be actively involved in the acquisition process, since their interests would be affected by the acquisition, particularly in acquiring companies, since the costs of acquisitions could undermine the economic interests of the shareholders. Shareholder activism would be required to ensure that shareholders have inputs in the role of the board when corporate acquisitions are made. Further, the role of the FCCPA 2018 in relation to mergers and acquisitions was highlighted. Its objective in promoting competitive market economy in Nigeria is important towards avoiding monopolies and ultimately protecting the interests of consumers and smaller competitive entities.

3.5 Reference/Further Reading/Web Resource

Fabian Ajogwu. (2011). *Mergers and Acquisitions in Nigeria: Law and Practice*. Centre for Commercial Law Development Lagos.

3.6 Possible Answers to Self-Assessment Exercises

(a) The following instruments regulate the Nigerian environment of mergers and acquisitions, namely *Investments and Securities Act 2007* (ISA 2007) administered by the Securities and Exchange Commission SEC and the *Federal Competition and Consumer Protection Act, 2018* – (FCCPA 2018), administered by the Federal Competition and Consumer Protection Commission. Other applicable regulations include, *Companies and Allied Matters Act, 2020* (CAMA 2020); the *Central Bank of Nigeria Act 2007* (CBN Act 2007) and *Banks and Other Financial Institutions Act 2020* (BOFIA 2020).

(b) The objective of the FCCPA 2018 is to ensure that any proposed mergers or acquisition if approved, would not lessen competition, and promote monopoly.

Unit 4 Takeover Hypothesis

Unit Structure

4.1 Introduction
4.2 Intended Learning Outcomes
4.3 Takeover Hypothesis
  4.3.1 Synergies
  4.3.2 Hubris Hypothesis
  4.3.3 Disciplinary Role of Takeover
4.4 Summary
4.5 References/Further Readings/Web Resources
4.6 Possible Answers to Self-Assessment Exercise(s)

4.1 Introduction

Corporate acquisitions have certain underlying effects. These are the ultimate results or outcomes of acquisitions. They include; synergy, disciplinary effects and hubris. The ultimate objective of mergers and acquisition is to promote a synergy of the companies involved. However, as shown in several empirical research outputs, corporate acquisition can also have disciplinary effect and it can lead to loss – hubris.

4.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- identify the takeover hypothesis and explain the implications of these hypotheses.

4.3 Takeover Hypothesis

(a) Synergies

The synergy hypothesis suggests that acquisitions are motivated by the desire to create wealth through a combination of the resources of the acquiring and target companies. This occurs in such a way that the value of the combined entity is greater than the sum of the separate entities' values. This includes; operating, managerial and financial synergies. The hypothesis identifies takeovers as an avenue for corporate expansion, and value creation.

Generally, corporate takeovers have been vastly motivated by the synergy hypothesis. The disciplinary effect is merely an outcome which is not anticipated by the acquirers. While the synergy hypothesis seeks to promote corporate wealth through a combination of the resources of the target and acquiring companies, the disciplinary hypothesis ultimately applies to correct managerial failures by dismissing poorly performing managers. However, irrespective of their different motives, the objectives of these hypotheses have the capacity to enhance the value of the shareholders of the acquiring and target companies.

(b) Hubris Hypothesis

When acquiring companies record a loss after an acquisition has been concluded, it may be referred to as the hubris hypothesis of takeover. It implies that the average increase in the target firm's market value should be more than offset by the average decrease in the value of the bidding firm, in such a way that the combined gain to the target and bidding firms is non-positive. It is mainly caused by costly acquisitions which arguably lead to the transfer of wealth from the acquiring company to the shareholders in the target company.

Loss of wealth by shareholders in takeovers may not necessarily affect the interests of managers; rather, acquisitions may lead to increase in remuneration by reason of increase in the size of the company.

Corporate managers whose takeover exercises are defeated by hubris may have negligently rather than deliberately paid higher takeover premiums. It has been suggested that managers of larger companies are much more likely to be involved in empire-building exercise towards achieving higher levels of remuneration. The acquisition ambitions of managers of larger companies appear to suggest that their acquisition-related activities are aimed at expanding the size of their companies without significantly increasing shareholder wealth. This may partly be caused by the view that the economic interests of the shareholders and managers of smaller firms are better aligned, since managers of smaller firms have a higher level of firm ownership than managers of larger firms.

The hubris hypothesis suggests that managers are zero maximising agents for their firms. This could make such firms which have been combined with little or zero gains to be takeover targets, with managerial discipline not necessarily a possible motive but an underlying effect. While the motives of the managements that engage in acquisitions leading to hubris may not be clearly determined, the effects of hubris is that, shareholders record losses or insignificant gains.

Although managements may pursue acquisitions without value creation, nevertheless, takeovers and mergers remain important investment-decisions through which the economic value of companies can be enhanced. The value-creation objective of takeovers can be promoted where managements are made to shun the practice of engaging in needless takeover transaction costs that can potentially undermine corporate value.

(c) Disciplinary Role of Takeover

The disciplinary hypothesis of takeover suggest that the value of the target company is likely to be enhanced where there is a threat of takeover by a raider who actually knows that the present economic value of the company can be improved if the company has a better management team than it presently has.

Takeovers can be influenced by the inefficiency of the management team of the acquired company. This includes poor managerial decisions that lead to value-decreasing acquisition which subsequently reduces the value of the company to the level of a target company. Hence such managers are not expected to be retained after the company is acquired.

It appears that managers of larger firms are more likely to be disciplined by the market for corporate control; - apparently, they are easily spotted by the market because of their size-. They are more inclined to indulge in value-destroying, empire building acquisitions than managers of smaller companies apparently because of prestige and their access to capital.

There is no consensus that the disciplinary hypothesis is responsible for managerial turnover, however, the effect of the takeover activities on target companies especially its disciplinary role cannot be denied. Whether the dismissal of managers of target companies is caused by poor performance prior to the takeover or by the initial rejection of bids by the managers to enhance the bid premiums, a takeover has a disciplinary character. The disciplinary nature of the exercise may extend to unsuccessful takeovers, since such threats could serve as incentives to managers to develop corporate policies towards enhancing shareholder value. This could be aimed at preventing the company from becoming or remaining a takeover target.

Self-Assessment Exercises

1. What is the main objective for engaging in takeovers and mergers?
2. What other result(s) can occur from takeovers and mergers apart from the main objective?

4.4 Summary

From the above analysis, it can be observed that an acquisition is particularly aimed at promoting synergies. It seeks to promote the economic value of the combined companies, for the benefit of the shareholders and other stakeholders. Disciplinary objective is also promoted. Since managers are aware that they can potentially be dismissed, they have the incentive to ensure that the economic value, including the market value of the shares of their companies is enhanced so that their company would not be an easy target of a takeover. However, other undesirable result could occur after a takeover has been concluded. The combined company could record a loss, caused by managerial hubris. As explained above, there is no evidence to suggest that hubris is a deliberate act. However, managers need to take cautious decisions when they engage in corporate acquisitions to ensure that they do not act carelessly or negligently in making acquisition that would lead to losses for their companies and shareholders.

4.5 References/Further Readings/Web Resources

Francis Okanigbuan Jnr. (2020). *Corporate Takeover Law and Management Discipline.* Routledge, Oxon.

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4.6 Possible Answers to Self-Assessment Exercises

(a) The overriding objective of mergers and acquisition is to promote a synergy of the companies involved.

(b) However, as shown in several empirical research outputs, corporate acquisition can also have disciplinary effect and it can lead to loss – hubris.

Unit 5 Managerial Defences

Unit Structure

5.1 Introduction
5.2 Intended Learning Outcomes
5.3 Takeover Defences
 5.3.1 Pre-Bid Takeover Defences
 5.3.2 Post-Bid defences
5.4 Summary
5.5 References/Further Readings/Web Resources
5.6 Possible Answers to Self-Assessment Exercise(s)

5.1 Introduction

The management board of a company involved in a takeover, perform active roles in negotiations. In a target company, the main role of the board is to ensure that the acquisition ultimately promotes the interests of the main stakeholders in the company, particularly shareholders. When an acquirer is interested in acquiring a company, the board of the target company may be contacted. The board may agree to the takeover or merger proposal or reject the proposal and request for further negotiations. There are circumstances where the target board may reject the acquisitions proposal. They may further set up certain mechanisms to defend the bid with the objective of either preventing the success of the takeover attempt or obtaining a higher bid price for their shareholders. Some of the mechanisms by which a target board can defend takeover attempts are briefly explained below.

5.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- explain the meaning of takeover defence and outline some of the common mechanisms that can be used by management of target companies to defend a takeover bid.

5.3 Takeover Defences

Takeover defences can be broadly classified as pre-bid defences and post-bid defences. Pre-bid defences are actions taken by managements before an actual takeover bid is made. Such actions are meant to prevent the successful acquisition of the company, they include but are not limited to; *poison pills, staggered boards provision, fair price*

amendment, super majority provisions, and *golden parachutes.* Some of these defences may be referred to as shark repellents.

5.3.1 Pre-Bid Takeover Defences

1) Poison Pills

Poison pills are strategies that are intended to make hostile takeover expensive and undesirable. They include the issuance of stock warrants or rights which allow shareholders (excluding acquiring shareholders) of a target company to buy shares (including those of the acquirer and the target) at a substantial discount from the market price. This right becomes exercisable when an acquirer buys more than a certain percentage of shares in the targets company preparatory to a takeover bid. These warrants or rights also allow target's shareholders to purchase shares of the newly formed company at a discount, if the acquisition is successful. When the option is exercised before the acquisition, it is referred to as a *flip-in*, where it is exercised after the acquisition, allowing the target shareholders to acquire shares at a discount, mainly the acquirers stock, it is referred to as a *flip-over*.

2) Staggered Boards

It is a device that may be incorporated in a company's constitution, which ensures that the majority of members of the board of directors are not available for election during any election period. The board of directors may be classified into three groups, and only one of the three groups are elected annually. This makes it difficult for a hostile bidder to gain immediate control of the target company, since only one third of the board is elected at a time

3) Super Majority

This requires that the acquirer obtain certain percentage of shares before the merger or acquisition may be successful.

4) Fair Price

This defence is used when the super majority tactics is relaxed, and the acquirer is required to pay all the shareholders of the company the same price per share.

5) Golden Parachutes

It is a device which is included in contractual arrangements between managements and their companies. It entitles the management to large forms of compensation in the event of loss of office, which may be caused be a takeover. The compensation to be paid could be so large that it may discourage an acquirer from taking over a company, especially where it would lead to the dismissal of the management that would lead to the payments being made.

5.3.2 Post-Bid defences

1) White Knight and White Squire

In *white knight* defence strategy, the target company invites another friendly company to make a bid towards acquiring the company, to prevent the hostile acquirer from acquiring the company. White squire is a modified form of the white knight defence. Instead of taking over the control of the company, the friendly company is invited to acquire a large percentage of shares in the target company called 'a corner' which is used to vote against the takeover bid of the hostile acquirer.

2) Crown Jewel

A target company sells its important assets to another company to become less attractive to the acquirer. Sometimes the assets are sold to a white knight for a possible repurchase on an agreed price after the acquirer withdraws its bid.

3) Greenmail & Standstill agreement

A defence tactics in which the target company repurchases certain number of shares from its Shareholders, usually one or more shareholders who are threatening to take over the company if the company does not pay for the shares at a premium, above the market price. This prevents the hostile bidder from acquiring a major percentage of the companies' stocks. It is effectively paying to prevent a company from being acquired. It is usually followed with a *standstill agreement* in which the shareholders agree not to re-buy any shares in the company for a given period of time. It can also be concluded without a repurchase and the shareholders agree not to buy any more shares. The shareholder(s) may be given some seats on the board to vote with management.

4) Pac-Man defence.

The target company makes a counter move and starts acquiring shares in the company that has placed the bid.

Self-Assessment Exercises

1) What is takeover defence?
2) Explain at least three pre-bid defences
3) Explain *White Knight* as a form of defence strategy after the fact.

5.4 Summary

Generally, takeover defences are undesirable as a result of the costs of the mechanisms and its hostile characteristics. It may lead to an increase in target shareholder value through increased bid premium by the acquirer as a challenge to the defences. Although takeover defences may enhance the bargaining powers of the shareholders, through enhanced bid price, it is also important to consider the sensitivity of such defences on the overall value of the company. Some defences may not necessarily enhance takeover premiums; they may serve as mediums through which inefficient managers entrench themselves in managerial positions. Thus, takeover defences may either be driven by conflict of interests between the managers and shareholders or a genuine attempt by managements to promote shareholder's interests and the overall corporate value.

5.5 References/Further Readingd/Web Resources

Francis Okanigbuan Jnr. (2020). *Corporate Takeover Law and Management Discipline*. Routledge, Oxon.

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5.6 Possible Answers to Self-Assessment Exercises

(a) Takeover defences are actions meant to prevent the successful acquisition of the company. They can be broadly classified as pre-bid defences and post-bid defences. Pre-bid defences are actions taken by managements before an actual takeover bid is made. They include but are not limited to *poison pills, staggered boards provision, fair price amendment, super majority provisions,* and *golden parachutes*

(b) Generally, pre-bid defences include poison pills, staggered boards, super majority, fair price and golden parachute. Golden parachute is a device which is included in contractual arrangements between managements and their companies. It entitles the management to large forms of compensation in the event of loss of office, which may be caused be a takeover. Conversely, poison pills are strategies that are intended to make hostile takeover expensive and undesirable. They include the issuance of stock warrants or rights which allow shareholders (excluding acquiring shareholders) of a target company to buy shares (including those of the acquirer and the target) at a substantial discount from the market price.

(c) In *White Knight* defence strategy, the target company invites another friendly company to make a bid towards acquiring the company, to prevent the hostile acquirer from acquiring the company.