

Promoter's Liability under the Common Law and the Companies and Allied Matters Act 2004

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ABSTRACT

A company as an artificial entity can only be brought into existence by a natural person, “that is a human being”. That human being is referred to under the Company Law as a promoter. Before or during the incorporation of a company, the promoter would have incurred certain expenses or other forms of liabilities. This article examines to what extent the promoter or the company that is not yet incorporated would held liable under the Common Law and the Companies and Allied Matters Act, the two laws that govern company administration in Nigeria.

Keywords: Company, Formation Promoter, Liability, Common Law Statute

INTRODUCTION

A company incorporated under the provision of the Companies and Allied Matters Act comes into existence as soon as the certificate of incorporation is issued. The date stated in the certificate is the date of birth of the company. However, the promoter would have incurred some liabilities. Who then should be held responsible? The problem is compounded by the dual application of Common Law and the Companies and Allied Matters Act over companies in Nigeria. This article seeks to examine the two laws with a view to reconciling the conflicts if any.

Company as a Corporation

The Oxford Advance Dictionary¹ defines a company as;

A business organization that makes money by producing or selling goods or services.

A company as used in this article, is an association formed under the Companies and Allied Matters Act to carry on commercial transactions or engage in philanthropic activities such as sports, education and so many others.

A company is a corporation and a corporation is defined in *Trenco Nigeria Company Ltd v. African Real Estate by Aniagolu*,² J.S.C as follows;

My Lord, a corporation is an abstraction, it has no mind of its own, it active and directing will must be consequently be sought in the person of somebody who for some purposes may be called an agent, but who is really the direction mind and will of the corporation, the very ego and centre of the personality.

¹ Oxford Advance Dictionary p. 276

² (1978) All NLR

On the other hand, the Black's Law Dictionary defined a corporation as, an artificial person or legal entity created by and under the authority of the law of a state. A corporation is an association of persons created by statutes as a legal entity.

Although a company in law is regarded as a person, it is in reality an artificial person acting through natural person.

As an artificial person a company can only be created artificially just as its existence could only be brought to an end through an artificial means by instrumentality of the law

Establishment of Companies

A company is an artificial entity that can only be brought into existence by the act of a natural person. That natural person is referred to as a "Promoter". Who then is a promoter? In *Garba v. Graba int. Nig. Ltd.*³ a promoter was defined as a person who undertakes to form a company with reference to a given object and set it going and who takes necessary steps to accomplish that purpose.

The Companies and Allied Matters Act⁴ defined a promoter as;

Any person who undertakes to take part forming a company with reference to a given project and to set it going and who takes the necessary steps to accomplish that purpose, or who, with regards to a proposed or newly formed company, undertakes a part in raising capital for it, shall prima facie be deemed as promoter of the company.

Qualification of a Promoter

As stated above, the person who initiates the idea and who takes steps to actualize such idea is known as a promoter.

The Company Allied Matters Act however provides that there are certain professional who are permitted by law to do business of incorporation with the Corporate Affairs Commission on behalf of the promoter. While carrying on such duties, such professionals are not to be regarded as promoters. It thus means that such professionals are not to be held liable as promoters during such promotion exercise. The professionals are.

A legal practitioner within the meaning of Legal Practitioner Act.⁵ It means any person with a first degree in law and a B.L certificate. That is a person that has attended the Nigerian Law School successfully with a B.L certificate.

In *Re-Great Wheal Polyglot Ltd*⁶ the court held that, a solicitor who prepares a document for a client who pays him his professional fees is not a promoter. However, where the professional does anything more than just rendering professional services in registering the company, he is deemed to be a promoter.

The second person is an accountant that is chartered.⁷

The third is a Chartered Secretary from the Institute of Chartered Secretaries and Administrators⁸ of Nigeria.

³ (2002) 1 NWLR (pt 748) 372

⁴ Section 31 Companies and Allied Matters Act Cap. C20 LFN 2004

⁵ See Legal Practitioners Act LFN 2004

⁶ (1883) U CH, 42

⁷ The Institution of chartered Accountants of Nigeria Act and that of Association of National Accountant of Nigeria act

⁸ See the Institution of Chartered Secretaries and Administrators of Nigeria Act

Duties of a Professional

Under the common law or under the Companies Allied Matters Act, a promoter stands in fiduciary relationship. He is expected to act in good faith, and if he fails to do so, the promoter is liable.

In *Erlanger v New Sambrero Phosphate Co.*⁹ the court held that a promoter "stands undoubtedly in a fiduciary position".¹⁰ They have in their hands the creation and molding of the company. they have the power of defining how, and when, and in what shape, and under what superiors, it shall start into existence and beginning to act as a trading corporation.

Arising from the foregoing a promoter who acquired any property or information in circumstances in which it was his duty as fiduciary to acquire it on behalf of the company, shall account to the company for such property and for any profit which he may have made from the use of such property.¹¹

A promoter could be held for breach of fiduciary duty when acting as an agent of the company. Thus in *Mahesan v. Malaya Governement Officers Cooperative Housing Society*,¹² "an agent of a Housing Society dishonestly agreed with "M" that "M" should purchase some land of a low price and sell it to the Housing Society at a profit and that the agent should neither tell nor reveal the price which "M" paid. The court held that, the Housing Society should recover from the agent both bribe and damages for loss sustained as a result of the agent's fraudulent breach of duty.¹³

Generally, the liability of a promoter would arise from the breach of the following duties.

- Duty to account for money/properties received in the course of promotion activities.
- Duty not to make secret profit
- Duty not to exploit confidential information¹⁴
- Duty to disclose conflict of interest
- Duty of skill and care¹⁵

Where a promoter mis-represent information to a would be shareholder, such a promoter shall be held liable. This could be a situation where he sold different categories of shares to a would-be buyer at the same price. It could also arise from mis-representation of object or business of the company.

An aggrieved person can seek for the following remedies.

Recovery of Secrete Profit

In *Gluckstein v. Barnes*¹⁶, four would be directors acting as promoters of a company made secret profits by selling properties bought by them without disclosing their interest, to the company. The court held that they must refund the profit.

Recession

The shareholder could rescind the contract. However, recession is a remedy of limited application.¹⁷

⁹ (1978) 3 APP cas 1218, at 1236

¹⁰ See Emiola A. Nigeria Company Law (1st ed. Ogomosho, Emiola Publishing Co. 2001) p. 79

¹¹ See Bhadmus F.H. Corporate Law Practice (Enugu, Chenglo Publishing Co. Ltd 2009) p. 111

¹² (1978) AC 57, 64

¹³ See *Fonsseca v. Passman*

¹⁴ See Section 289 CAMA 2004

¹⁵ *Bernard Ojelfor v. First Bank Plc* (2006) 1 CLRN

¹⁶ (1900) Ac 240 See Tom D.F. Company Law in Nigeria, (1st ed. Benin City, Union Publishers 2009) p. 37

¹⁷ See Gower on Company Law p. 330

Account

The aggrieved person would demand for account by the promoter.

Promoter's Liability under the Common Law and Companies and Allied Matters Act

A promoter's liability under the common law is slightly different from the liability under the Companies and Allied Matters Act. Under both laws, a promoter owes a fiduciary duty and the remedies are the same which is damages, account, recession, or recovery of secret profit.

There is however, a sharp difference where the breach relates to pre-incorporation contract.

Pre-Incorporation Contract

A pre-incorporation contract is a contract entered into by a promoter on behalf of a company that has not been incorporated. Most time the promoter would have engaged the services of a solicitor to prepare the necessary documents such as Memorandum of Association or Article of Association. At the same time things like stationeries would have been bought. Travelling expenses are also included. How then can a company that is not yet incorporated be made to pay such expenses?

Promoters Liability under the Common Law

Under the common law, any pre-incorporation contract or expenses incurred before the company as was incorporated is to be borne by the promoter.

The common law position is based on the fact that, a company that is not yet in existence cannot incur or be made to bear expenses incurred before the company was incorporated.

In *Dr. Emmanuel Urhobo v. J.S. Tarka and Anor*,¹⁸ the defendant was held personally liable for pre-incorporation contract.

However, in *Newborne v. Sensolid (Great British Ltd)*¹⁹ the court held that to be able to enjoy the benefit of a pre-incorporation agreement, the Company ought to have entered into a fresh agreement upon the same terms of the previous one after incorporation.

This judicial pronouncement is an exception to the general rule that a promoter is liable for pre-incorporation contract under the common law.

Liability of a Promoter under the Companies and Allied Matters Act

Under the Companies and Allied Matter Act, a promoter is liable for pre-incorporation contracts. The Companies and Allied Matters Act²⁰ provides as follows:

Section 72²¹ (1) Any contract or other transaction purporting to be entered into by the company or by any person on behalf of the company prior to its formation may be ratified by the company after its formation and thereupon the company shall become bound by and entitled to the benefit the of as if it has been in existence at the date of such contract or other transaction and had been a party thereto.

(2) Prior to ratification by the company, the person who purported to act in the name of or on behalf of the company shall, in the absence of express agreement to the contrary, be personally bound by the contract or other transaction and entitled to the benefit thereof.

CONCLUSION

From the discussion so far, it has been established that a promoter is a human agent whose effort brings into existence a company. A promoter owes a fiduciary duty the company and would be shareholder. The

¹⁸ (1976) 1 FNR 208

¹⁹ (1954) 1 QB. 45

²⁰ See Section 72 CAMA 2004

²¹ See Section 72 CAMA Cap C 20 LFN 2004

fiduciary duties include duty to account, not to make secret profit, to desist from conflict of interest and to exercise utmost care and skill.

The provisions under Section 72 make the promoter liable for pre-incorporation contract.

However, where the company ratifies pre-incorporation contract, the company will be liable and not the promoter.

Remedies for Breach of Fiduciary Duty

The remedies include recession, account, damages and recovery of secret profit.

With respect to pre-incorporation contract, a promoter is entirely liable under the common law.

However, on incorporation, a company can enter into a fresh contract in respect of the same contract thus making the company liable.

Under the Companies and Allied Matters Act, the promoter is also liable for pre-incorporation contract. If the company ratifies the contract, the company will be liable.

From the discussion so far, there seems not to be any difference between promoter's liability under the common law and the Companies and Allied Matters Act.

To this extent it is suggested that the provisions of the common law with respect to promoter's liability should be dispensed with since in any circumstance statutory revisions take precedence over the common law in Nigeria.

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