STUDY MANUAL

CORPORATE LAW (PEB 4)

ASSOCIATION OF NATIONAL ACCOUNTANTS OF NIGERIA (ANAN)

TABLE OF CONTENTS

MODULE 1

MODULE 2

MODULE 3

MODULE 4

MODULE 5

MODULE 6

MODULE 7

MODULE 8

MODULE 1

1.00 TYPES OF BUSINESS ORGANISATIONS AND ACCOUNTING PROCEDURES

1.01 Learning Outcomes

On successful completion of this module, students should be able to:

i. Appraise the nature, function and accounts of a Sole Trader;

ii. Prepare and analyse the accounts of a Partnership business;

iii. Evaluate the steps in dissolution of a Partnership.

1.02 Sole Trader

A business is classified as a Sole Trader when it is fully owned by one man. He employs other people to work for him as labourers, technicians, accountants, etc. but he is fully in control of all the decisions that relate to the operations of the business. He can raise capital from his own savings, borrowing from bank or money lenders or friends and relatives. The direction of growth or facilitation of the business depends solely on his ingenuity and self-control. All profits or losses accrue to him. He is the complete risk bearer and liable to the debts of the business, even to his personal property. That is to say that, if this business is owing somebody the sum of ₦5,000, that creditor could come to his personal house and carry his Television Set or any other property he thinks will compensate for the ₦5,000 debt.

In the same way, when the business is making profit, he can decide how much he will take for his private use or how much he wants to plough back into the business. In most cases, the life of the business ends with the death of the sole trader. Such one man-business is commonly seen in farming, trading, technical works such as mechanics. welding, carpentry, shoe-making and a host of other businesses.

1.03 Peculiarities of accounts of Sole Traders

The business of the sole trader is usually not recognised by law as a separate entity. Although the Final Accounts need to be prepared to keep the Entrepreneur informed of the progress of the business, the company or business is not subject to a separate tax different from the owner. The tax paid by the business is the same as the tax paid by the owner. The Final Accounts prepared is simply to show the basis of Personal tax assessment for the owner. The owner simply draws an amount for Tax payment from the business and pays the tax in his name. Since the Tax is on his personal name, the money taken from the business for payment of tax is usually treated as drawing.

The Accounting treatment is simple because of the nature of the Capital structure. Since the business is solely funded by the sole-trader, he decides what to do with his profits and how to off-set his losses. There is no need for the Appropriation of profit or loss. Although for good financial management, Entity concept need to be applicable in keeping his records, but this is not a statutory requirement. The Earnings statement and the Balance Sheet is for the sole trader or some few interest groups like the trade creditors, and banks or other financial institutions that assist the sole-trader to finance his business. Apart from the treatment of Taxation and Profit and Loss Appropriation, the financial statements of the sole trader are similar in structure to those of partnership and limited liability companies. The major fact to note is that even where the one-man business is registered with a Business name with Corporate Affairs Commission, it is not a legal entity and the sole trader is free to transact business and control his funds without any legal restrictions.

1.04 Partnership Business

When two or more persons come together with a view of doing business, it is referred to as Partnership. There are many legal aspects to partnership business. The important thing to know at this point is that the partnership business is registered as such. The law made it mandatory that in Nigeria the maximum number of people who can come together to form partnership must not exceed 20 persons. The law however allows for less number in cases of professional firms such as Architects, Lawyers, Accountants etc. Where the court has an evidence that the number of persons involved in the partnership is more than the stipulated number according to the law, such partnership can be declared an illegal association by the law court and can be forced into liquidation, closed or converted to limited liability company as may be pronounced by the court. Thus, in Akinlose Vs A.I.T. Co. Ltd., (1061) WNLR 213, a group of people formed the Ondo and District Timber Group for timber trade. Evidence was led to show that the group was a partnership of over 100 members and that it was not registered under section 3(2) of the companies' ordinance then in force. Madarikan, J. in his judgment declared the association illegal. Where an association is illegal, the court will refuse to give effect to its transactions. The English Partnership Act of 1890 was adopted and applicable to Nigeria. Although few modifications were made by some Regions and States of Nigeria, the 1890 Partnership is by and large applicable.

Since partnership involve more than one person, there is the need to have agreement on how profits and losses should be shared, the amount of capital to be contributed by each partner, how new partner can be admitted, the time the partnership will operate and a host of other details. The agreement is called the Deed of Partnership.

1.05 Qualities of Partnership Business

Partnership is an improved form of running a business when compared with the Sole Trader. The advantages of partnership as a form of business organisation are many. They include:

1. Two or more persons can contribute different types of capital to enable the business take-off and grow. For example, while Mr. Ola has a store which can be used for a supermarket, Mr. Tunde may have a pick-up van while Mr. Duro has a cash of ₦150,000. The three of them can team up to start-off a supermarket business with the small sum. All these forms of contributions are all capital.

2. It is clear to us that different persons have different talents. This means that Messrs Ola, Tunde and Duro can now form a Board of Directors each taking up a defined responsibility that he knows best for the interest of the partnership. With this type of division of labour, the business will grow within a period of few years.

3. Very often, there are cases where the older persons have more money and experience to run a business but they require younger ones who are professionals to join them to form a partnership. Although the younger one may contribute lesser money, they are Accountants, Engineers, Market specialists etc. and they do the running around to make the partnership grow to the benefit of both the older and younger partners.

4. Since more than one person is involved in the partnership business, it is possible for them to rest in form of annual leave without fear of the business collapsing since other partners on the ground also have stake in the business. This is also an advantage over the sole trader who will work all round the year at the expense of his health for fear of the business collapsing.

1.06 Peculiarity of Partnership Accounting

The Income Statement usually has Realisation Accounts and Profit and Loss Appropriation Accounts. These sections are designed to comply with the Deed of Partnership. The Balance Sheet has two sections which are classified as Current Accounts and Capital Accounts for each partner. All these differentiate the Accounts from that of the sole trader.

It is important to note that partnership Business is not a legal entity but unlike the sole trader the contents of the Deed of Partnership can be enforced-in the court of law.

1.07 Deed of Partnership

This is an agreement agreed upon by both parties on how the partnership will be conducted. The conditions may be verbally agreed where there is mutual trust especially where the partners are close friends or are blood relations. It is however advisable that such agreement should be in writing preferably drawn by a lawyer and signed by all parties involved. The agreement or deed of partnership handles all relevant issues that may arise in the future. Each issue will be fully discussed and agreed upon before the agreement is finally signed. The type of issues generally included in the Deed of partnership are many but only few of them are mentioned below *(Okoye, 2000)*.

1. How much capital each partner should contribute to the business.
2. If any interest will be paid on the capital introduced, and if so, what will be the rate of interest.
3. How profit and loss will be shared by the partners.
4. Whether any of the partners will be entitled to salary because of his special skill e.g. an Accountant, Engineer, Medical Doctor, Architect etc.
5. The responsibilities of each partner in the day to day running of the business.
6. If commission will be paid to any partner for example if one attracts or wins a business or contract for the partnership etc.
7. Whether partners are entitled to drawing and if so, what will be the monthly or quarterly limit within the financial year.
8. Whether interest should be charged on drawings and where applicable the fixed interest must be defined.
9. How new partners should be admitted into the business if the need arises.
10. A clause that no additional capital shall be introduced, nor any existing capital withdrawn by the other partners, without the consent of the others.
11. The procedure to be adopted in case of the death or retirement of a partner.
12. The duration of the partnership says 10 years.

Partnership Law

In cases where the partners to the Partnership business made the initial mistake of not having a Deed of Partnership either expressed in writing or implied, the partnership law will apply the following provisions.

1. All partners should contribute equally to the capital.
2. Profits and losses are to be shared equally.
3. Any loan made to the business by a partner is to carry interest at the rate of 5 % per annum.
4. No partner is entitled to salary.

5. No partner is entitled to interest on capital.
6. No new partner may be introduced without the consent of all partners.

Number of Partnership Membership

The number of persons that can come together to form a partnership is limited by law:

1. The minimum number of persons is two; and
2. The maximum number of persons is twenty

However, there are special cases e.g. in the Banking Industry where the maximum number of persons used to be ten. The laws were in accordance with the Act of 1890. It is important to note that Nigerian Companies Act of 1968 and other subsequent amendments have lifted the maximum limit of twenty persons in respect of professional partnership such as solicitors, stock brokers, accountants etc. The Ministry of Trade and Industry on application can exempt any other partnership business from the maximum limit of twenty.

It should be noted that most partnership businesses do not take advantage of the liberated condition of lifting maximum limit since the advent of limited liability company status.

1.08 Types of Partners

Partners to partnership business can be classified into two groups: viz General partners and Limited partners.

General Partner

The General Partner is a partner who is fully involved in the conduct of the business of the organisation. He gets the full benefits from the partnership business if things are going well i.e. If the company is making profit. In the same token, he is fully liable to Debts and losses of the business even to the extent of his personal property. For example, the court can order that his personal house, motor vehicle etc. be sold to pay the creditors to the partnership business.

The General Partner(s) can be classified as **active** or **dormant**. **Active partners** participate in the day to day running of the business while the ***Dormant*** or ***Sleeping*** partners do not participate in the day to day running of the business. However, every General Partner whether active or dormant is liable to the full extent of his personal property in respect of the liabilities of the partnership business (*Okoye, 2000*).

Limited Partner

A Limited Partner is one who contributes an agreed amount of capital but will not participate in the management of the business. In the case of liquidation of the partnership business by the order of the court or voluntary liquidation, he is liable to the debts of the partnership only to the extent of the capital he has paid or promised to pay. He is not liable to the extent of his personal property. The law stipulates that where there are limited partners there must be at least one General Partner who will be fully liable for the debts of the partnership business.

Admission of New Partner

In the Deed of Partnership, the conditions for admission of a new partner are usually well spelt out. The rule is that the consent of all the General Partners is sort. All other issues are also agreed upon for example, the amount of capital the new partner should contribute, how profit and loss should be shared under the new dispensation and so on.

1.09 Accounting Procedure

When a new partner is introduced, the old partnership will cease to exist. For example, if Chuks and Ike partnership decided to admit Mr. Okeh into the business, it means that Chuks and Ike Partnership will cease to exist and what now exist is Chuks, Ike and Okeh partnership. To reflect this logic in accounting, the manoeuvre is to adjust the Books of Accounts as if the company is closing for Chuks and Ike Partnership business and the Books are then reopened to reflect the new business structure of Chuks, Ike and Okeh partnership. The procedure of Book-Keeping is to:

(a) Distribute any reserves made by the previous partners among the old partners in their profit-sharing ratios.
(b) Distribute all capital gains made to the old partners in their profit-sharing ratios before the admission of a new partner.
(c) Distribute any goodwill which can be valued to the old partners before admitting a new partner.

1.10 The Need for Goodwill

Goodwill can be defined as an intangible asset based on the assumption that the business unit has built up a good name that will make the customers or clients to continue to patronize its goods or services for a long time. Although it is a function of common sense to recognise the existence of goodwill, it is extremely difficult to set up a standard formula that will satisfy different goodwills as perceived by different ways of calculating goodwill to suit specific conditions of various businesses. For example, many people define goodwill as the price paid over and above the Book value of the business.

The fallacy of such definition is that the price paid over and above the book value may be simply caused by inflationary trend, scarcity of the product, Government polices which may be to the advantage of the business at that point in time and so many other factors.

In partnership accounts, the Goodwill is the property of the old partners. It is usually estimated using a suitable base to share the value allocated to the Goodwill before the new partner is admitted. Alternatively, the new partner may be required to pay a specified amount to cover the value of the goodwill. In each case the goodwill will be shared between the old partners in their profit-sharing ratio and transferred to their capital accounts.

1.11 Dissolution of Partnership

It is a common saying that everything with a beginning must have an end. It is in recognition of this that the duration of the partnership is usually stated in the Deed of Partnership. Many factors can lead to the dissolution of partnership.

Reasons for Dissolution

1. Expiration of the time fixed in the Deed of Partnership for the existence of the Partnership.
2. Where a Court of law ordered the dissolution of the partnership following litigation from one of the partners, creditors or any other interest groups.
3. The bankruptcy of one of the partners may lead to liquidation.
4. The death or retirement of a partner.
5. Where one partner gives notice to the other on his intention to dissolve the partnership.
6. Where the partners agree on the need to dissolve the Partnership.
7. The business is consistently running at a loss.
8. Where the partnership is converted to a limited liability company to replace the existing partnership. In such cases the partners take shares in the new Company equivalent to their capital in the Partnership business.

For whatever reason, the dissolution of the Partnership is synonymous with liquidation. The principles of liquidation apply in the dissolution of partnership. On the dissolution of partnership, the entire assets of the company are sold.

Legal Framework for Dissolution

The legal procedure is that all amounts realised from the sale of the assets of the Partnership will be used to offset the liabilities of the partnership in the following sequence:

1. Outside creditors: In Partnership dissolution the amount realised from the asset will be used to discharge the creditors. Where this is not enough, the personal property of individual ordinary partners will be sold to offset the debt.
2. If there is any balance after settling the outside creditors, the loan made by the partners to the business will be redeemed.
3. If there is any balance after that, then the partners’ capital will be paid.

4. Any balance remaining in form of profit will be distributed to the partners in their profit-sharing ratios.

Accounting Framework for Dissolution

In dissolving partnership business, accurate book-keeping is maintained, and the following accounting entries will be necessary to be adhered to:

1. Transfer all balances in the current account of each Partner to his capital account. With this step, Current Account ceases to exist.
2. Keep a separate account for all the loan made by the partners to the business.
3. Open Realisation Account:

   Dr. Realisation Account with the Book value of the assets (except cash).

   Cr. The individual asset accounts. With this entry, the Asset Account is closed.
4. When any Asset is sold

   Dr. Bank or Cash with the value of sales.

   Cr. Realisation Account with the sales value.
5. If any partner can take over any Asset:

   Dr. The Partners Capital Account

   Cr. Realisation Account with the agreed value
6. Costs or expenses incurred in the dissolution process:

   Dr. Realisation Account

   Cr. Bank or Cash.
7. Where a partner incurred cost or expenses to assist in the dissolution:

   Dr. Realisation Account

   Cr. Partners Capital Account.
8. Where creditors are paid off:

   Dr. Creditors Accounts.

   Cr. Realisation Account (Bank or Cash).

9. Where a Discount is received from creditors:

   Dr. Creditors Accounts

   Cr. Realisation Account.

10. When any loan is repaid to a partner:

    Dr. Partners loan Account

    Cr. Realisation Account (Bank or Cash)

The balance in the realisation account is finally transferred to the partners Capital accounts in their profit-sharing ratios. With this final operation, the sum of the amounts in the capital accounts of individual partners will be equal to the amount in the Bank. The dissolution is finally closed by transferring the amount in the Bank to the individual capital account.

Dr. Capital Account

Cr. Bank Account.

When a partner's Capital Account is at deficit, he will be required to pay-in cash to offset it. This by implication means that he must borrow money or sell his personal property to off-set the deficit. Where the partner is declared insolvent i.e., he cannot off-set the deficit after selling all his personal property, the other ordinary partners are liable by law to off-set the deficit caused by the insolvent partner (see Ruling in Garner V. Murray by Mr. 1 Joyce in November 1903). The issue of Book-keeping and Accounting aspects are outside the scope of this work. Emphasis here is on the legal aspects of the business Organisations.

1.12 Review Questions

1. "Small-scale sole trader businesses can be the engine for growth and development in Nigeria". Evaluate the pros and cons of this statement.
2. In what ways could partnership business play key roles in economic growth and development in Nigeria?
3. Carefully deconstruct the procedure for:
   a. Setting up a Partnership
   b. Dissolution of Partnership
   c. Conversion from Partnership to Limited Liability status

MODULE 2

2.00 INCORPORATED COMPANIES

Incorporated Companies are those companies that are registered as limited Liability Companies. The companies are registered as Corporate Bodies legally recognised as corporate individuals which can sue or be sued. Since we are one of the colonies of Britain, the Nigerian Company Law is still rooted strongly on the British Parliament Act of 1855. Although there has been subsequent amendment in Nigeria Companies Acts in 1948 and 1967, it was only the Companies and Allied Matters Decree (CAMD) of 1990 now (CAMA) that made a substantial deviation from that of the British Parliament of 1855 probably because of the introduction of Structural Adjustment Programme (SAP) in the mid-eighties. The main difference therefore between the sole trader and partnership business and that of Incorporated companies is that Incorporated Bodies are recognised by law while the sole trader and the partnership are not. This legal recognition has created different Accounting treatments for incorporated companies, which are generally referred to as Limited Liability Companies.

2.01 Learning Outcomes

On successful completion of this module, students should be able to:

i. Assess the procedure for listing of member bodies by the Corporate Affairs Commission;
ii. Appraise the registration process of a company, including the legal issues;
iii. Classify and clearly distinguish between the following: Statutory Books, Accounting Procedures, Shares and Stocks and Underwriting Account.

2.02 Corporate Affairs Commission (CAC)

The Corporate Affairs Commission otherwise referred to as the commission came into existence through Act Number I of 1990. The commission is a body corporate, with perpetual succession and a common seal, and can acquire property to carry out its function. The Commission's function is the regulation and supervision of the formation, incorporation, registration, management and liquidation of companies in Nigeria. To carry out the above functions, the commission is required to establish offices in all states of the federation. The commission can investigate the activities of any company where it is discovered that the interest of the public or the company shareholders is at stake.

Member-Bodies of the Corporate Affairs Commission (CAC)

a. According to Section 2 of CAMA 2004, the Commission is headed by a Chairman appointed by the President and Commander-in-Chief of the armed forces. The Chairman of the commission must be a professional person with powers amid wealth of experience in corporate, industrial, commercial or economic issues, who can bring these qualities to bear on the work of the Commission. Other members include:

    1. A representative of the Nigeria business community appointed by of the Minister on the recommendation of NACCIMA (Nigerian Association of Chamber of Commerce, Industries, Mines and Agriculture).
    2. A representative of the legal profession appointed by the minister on recommendation of NBA (Nigerian Bar Association).
    3. A representative of the Accountancy profession appointed by the minister on recommendation of Institute of Chartered Accountants of Nigeria.
    4. A representative of MAN (Manufacturers Association of Nigeria) appointed by the minister on the recommendation of the Association.
    5. A representative SEC (Securities and Exchange Commission) appointed by minister on the recommendation of the Association.
    6. One representative of Security and Exchange Commission not below the grade of Director or its equivalent.
    7. One representative of each of the following ministries (1) Commerce (2) Justice and (3) Industry.
    8. The Registrar General of the Commission.

2.03 Registration of Companies

The documents required for the registration of a company with **Corporate Affairs Commission** include:

1. Memorandum and Article of Association
2. Addresses of the registered office and that of the headquarters if situated in different environment. Such addresses will not include post office box or private mail bag.
3. A statement in prescribed form containing the lists and particulars of potential directors.
4. Any other document considered necessary for the registration of companies.

The memorandum of association defines the power and objectives of the companies.

The **Memorandum of Association** defines the power and objectives of the company. Form and content of the **Memorandum of Association** are as provided in Schedule Table B, C, D of CAMA 1990. According to section 27 of the same act, the **Memorandum of Association** of a company will state:

i. The name of the company with the words limited, limited by guarantee,unlimited depending on the type of company.

ii. The domicile or the place where the registered office of the company is situated.

iii. The objects of the business which emphasizes the nature of the business which the Organisation or the company is authorized to embark upon.

iv. Restrictions, if any, on the powers of the company.

v. Declaration that the company is a public or private company.

vi. A declaration on the limitation of liability, i.e. whether limited by shares or guarantee or unlimited.

vii. The authorized share capital of the company with which the company is to be registered and the division of the shares.

viii. A declaration that the subscribers of the memorandum must take up not less than 25% of the authorized share capital of the company (S.567 CAMA 1990).

ix. The memorandum of association must be duly signed by the prescribe minimum number of people, i.e. 2 persons in the case of private companies and seven persons in the case of public company.

The article of association as prescribed in section 33 of the 1990 Act contains regulations for the internal workings of the Organisation. It spelt out the rights of members of the companies and the duties and powers of the Directors. The forms and content of the articles of association of the different types of companies are provided in schedule 1, Table A, Part I, II, III and VI of the 1990 company act. The content of the **Article of Association** will include:

i. The regulation for the issue of capital, variation in the right of members, a lien on shares and payment of underwriting commission.
ii. The different types of call on shares.
iii. Transfer and transmission of shares.
iv. The appointment and powers of the managing director.
v. Accounts and audit.
vi. Members right interes.t
vii. Notices of meeting to members.
viii. Borrowing powers of the company.
ix. Dividend declaration and rate of dividend.
x. Powers, duties of the board of directors.

After due consideration, the Corporate Affairs Commission will issue a certificate of incorporation which will be a prima facie evidence that the company has complied adequately with the requirement prescribed by the commission. The certificate of incorporation accords the company a corporate status and can, therefore, exercise all relevant powers.

2.04 Legal Issues on Incorporated Companies

Section 21 of CAMA (caps 59) LFN 1990 prescribed three types of companies and these are: companies limited by **shares**, companies limited by **guarantee** and **unlimited** companies. A company is said to be limited by shares when the liability of its members is limited by the memorandum to such amounts, if any, unpaid on the shares respectively held by them. In such Organisation, the business entity convention is highly pronounced. There is legal distinction between the business and those who have economic interest, to the extent that in the event of a corporate debt, the personal belongings of the owners cannot be realized. Rather, they will be indebted to the amount they had agreed to pay to the company for share allotted them. In the case where a member has paid fully for his shares, such member is discharged of further liability. In Nigeria, a lot of companies are limited by shares, for example First Bank of Nigeria plc, Okomu Oil, Nestle, Coca-cola, Nigeria Breweries, etc. The name of a company limited by shares usually ends with Ltd (Limited) for a private company and Plc for a public company (*Ilaboya, 2008*).

A company is said to be limited by **guarantee** when the liability of its members is limited by the memorandum of association to which such member undertakes to contribute toward the assets of the company in the event of liquidation. Mainly, non-profit making Organisations and government parastatals are limited by **guarantee**. The Corporate Affairs Commission, Financial Reporting Council of Nigeria and so on, are examples of Organisations limited by guarantee. Such companies are formed for and promoting commerce, art, science, religion, sports, culture, education, research, charity and other similar objects. The name of a company limited by guarantee will end with the words limited by guarantee (Ltd/Gte). If a company is not limited by shares or **guarantee**, it is said to be unlimited and the name of the company must end with the word “unlimited” (CAMA 2004: Cap I Sec. 21).

2.05 Statutory Books

As the name implies, Statutory books are books which are required by law to be kept by the company. These books include:

1. **Register of Members**

This is a book containing the names of shareholders of the company and those of signatories to the Memorandum of Association. According to section 83 of CAMA 1990, every company is statutorily required to keep a register of members which will contain the following particulars:

a. Name, address, the classes of shares in case of a company limited by shares and the amount paid or considered as paid on shares allotted.
b. The date of registration as a member of the company.
c. Date on which a member is delisted from the register.

All entries in the register of members concerning the listing of a new member and delisting of an existing one, must be concluded within 28days. The register of members is open for inspection within business hours in the business or registered office of the company or any other place convenient for the company provided such place or places are duly notified to the commission.

d. **Annual Returns**

   In accordance with the provision of Section 370 of CAMA 1990, all companies in Nigeria are required to make and deliver to the Commission within 42 days after the annual general meetings a copy of the annual returns duly signed by Directors and the Company Secretary.

The annual returns will contain

i. Register of members and debenture holders.
ii. The company's shares and debentures.
iii. The company's indebtedness.
iv. The names of past and present Directors.
v. The name of the Company Secretary.

The following documents are required to be attached to the annual returns as provided in Section 375 of CAMA 1990:

a. Signed copy of the Balance Sheet and Profit and Loss Account;
b. Report of the Auditors;
c. Reports of the Directors.

e. **Minute Books:**

in accordance with Section 241(1) of CAMA 1990, every company must cause minutes of all proceedings and resolution of general meetings, directors' meetings and managers' meeting to be documented in a book designated minute books and kept in the registered office of the company and made available for inspection by members during the business hour for no cost. It is however possible, upon payment of a specified amount of money for a member to request a copy of the minutes. Such copy duly signed by the Company Secretary must be delivered to the member within seven days of such request. Though the minute book is open for inspection; this does not include minutes of directors' meeting. The reason for this exclusion may be because such minute will contain issues of strategic importance which when made available to competitors can have adverse effect on the company.

f. **Register of Directors Holding**

The register of directors holding contains information on each director's shareholding capacity in terms of number, description and value including debentures of the company or any other company. The register will be kept in the registered office or head office of the company and open to members for inspection during business hours, such register of directors holding will be required to be produced during any annual general meeting and can be inspected by any member who is in attendance in the meeting. The register need not include shares in any body corporate which is the wholly owned subsidiary of another body corporate. And for this purpose, body corporate will be deemed to be the wholly-owned subsidiary of another if it has no members but that others wholly-owned subsidiary and its or their nominees; see Section 275(1) CAMA 1990.

g. **Register of Charges**

In accordance with section 191(1) CAMA 990, every limited company is required to keep a register of charges in the registered offices of the company. Such register shall enter charge attaching the assets of the company and those which are not attached to specific property known as **floating charges particulars**. The floating particulars of the charges will include short description of the asset charged, the value of the charge and the names of beneficiaries. As usual, the register of charges will be open for inspection by the members of the company and the company's creditors for no cost.

h. **Register of Debenture Holders**

Under Section 193 of CAMA 1990, any company which has issued debentures is required to maintain a register of the debenture holders in their registered offices with respect to names and addresses of the debenture holders, principal amount of the debenture held by them, the amount or highest amount of premium payable on redemption of the debentures, the issue price of the debenture and the amount paid, the date in which each holder was listed or delisted from the register. The register of debenture holders will be opened for inspection to shareholder, registered holders for no cost and to any other person on payment of ₦1 or such less sum as may be prescribed by the company. Any such person as mentioned above can request for a copy of the register of debenture holder or any part thereof on the payment of ₦0.50 for every 100 words required to be copied.

2.06 Company Share Capital

A share is defined as the smallest indivisible unit of capital. The Company and Allied Matters Act 1990 was silent on the definition of shares. To Beckett, "a share has been defined as the interest of a shareholder in the company measured by a sum of money for the purpose of liability in a limited company in the first place, and of interest in the second, but also consisting of a series of mutual covenants entered into by all the stakeholder's interest".

Simply put, a share is the smallest indivisible unit of capital which represents transferable ownership interest in a limited liability company.

The share capital of a company can be divided into two broad categories, i.e. the ordinary share capital and preference share capital.

a. The Ordinary Share Capital: This class of capital bestows on the holders a non-guaranteed ownership in the company. They are the risk bearers and are last in line with claims on the company assets in the event of liquidation. Hence, they are commonly referred to as Residual owners. This class of shares attracts some basic right and such rights will be dependent on the terms of issue and on the company's Article of Association (Section 114 of CAMA 1990):

i. The right to vote on issues that come before the shareholders' deliberation when it is resolved, that decision will be by simple majority. The right on a poll of a general meeting of the company is one vote in respect of each share. One frequent situation in which shareholders exercise this right is election of corporate directors. The procedure of exercising this right as contained in Section 224(1) CAMA 1990 will be by a show of hand. The right to vote can be transferred to another person whether a member or not to vote instead. This is called a proxy appointment (Section 230(1) CAMA 1990).

ii. Right to distributed profit inform of dividend. When the company declare dividend, each shareholder is entitled by right to the dividend based on his percentage of ownership.

iii. Right to share in the distribution of the company's asset if the company is liquidated. This right can only be exercised after all fixed interest obligations, i.e. debenture and preference shares have been settled. The percentage of share ownership will also determine what will accrue to individual shareholders.

Iv. Right to maintain one percentage share ownership of shares in case of additional issue. This right is called Preemptive right and is seldom exercised due to its administrative inconvenience. Unless specifically excluded, the preemptive right is usually built into the contract between the shareholders and the company which is usually established when the person made an offer through application for shares and the company accepted by allotting shares.

Ordinary shares, loosely referred to as equities, can be divided into two categories: Deferred ordinary stock and preferred ordinary stocks. Suffice to mention that this distinction is not a loud one hence it is seldom applied. Preferred ordinary shares attract a preferential, fixed rate of dividend while the deferred ordinary shares are entitled to the surplus or a given percentage of it after settling the claims of all prior right holders. Sometimes the deferred ordinary shareholder will be entitled to nothing when there is no surplus.

b. The Preference Share Capital: This is a class of share with a claim on the company's property which supersedes the claim of the ordinary shareholder but subordinates to debenture holders claim. Preference shares are sometimes described as a "**hybrid**" security because it behaves like the ordinary share and debt capital. Like ordinary share capital, preference shares attract dividend and like debt capital, the dividend accruable to preference share capital is fixed. Preference shares attract some rights and privileges, such as:

i. The right to receive fixed amount of dividend which is calculated as a percentage of the nominal value of the share or a predefined amount per share. If dividend is declared by the Board of Directors, the preference shareholders are entitled to receive their fixed dividend rate before the surplus can be distributed to the ordinary shareholders (preferred ordinary share first, then the deferred, if the equity is classified).

ii. Right to receive a distribution of the company property upon liquidation before the ordinary shares.

iii. Right of conversion, which entitles the preference shareholders opportunity to convert to ordinary shares.

In addition to the rights mentioned above, the preference shareholders have a redemption privilege contained in Sections 122, 158 of CAMA 1990 which allow preference shareholders to return their shares at the instance of the company predetermine redemption price. The shares can only be redeemed when they can pay. The shares are redeemable from distributable profits or from proceed of shares issued specifically for that purpose.

Preference shares can be participating or non-participating, cumulative or non-cumulative and redeemable or non-redeemable. Preference shares are said to be participating when the shareholders are entitled to additional dividend beyond fixed amount accruable to the preference shares. The cumulative feature entitles preference shareholders opportunity to cumulate or accrued dividends which could not be paid in one accounting period. Such accrued dividend must be settled in subsequent years before any dividend can be paid. The redemption privilege is as explained earlier.

2.07 Accounting Procedure

The accounting procedure of incorporated Companies are more complex when compared with the Sole Trader and Partnership businesses. The complexity in limited liability companies is because of the capital structure. Their capital structure has a lot of accounting implications.

Some forms of capital include:

i. **Authorised share capital** sometimes called the **nominal capital**, as stated in the Memorandum.

ii. **Issued capital** - representing the part of the authorised capital that has been issued for sale.

iii. **Called up capital** i.e. where a capital has been issued but partly paid for, the balance of the capital can be called up for payment at any time. In Nigeria as at now, most Issued Capital are paid for as a result "**called up capital**" is not common.

iv. **Reserve capital** i.e. that part of uncalled capital which has been issued and partly paid for. Although this type of capital is rare, so it is usually called-up when the company is under financial pressure or it is winding-up.

Shareholders

The fundamental way of becoming a shareholder of a limited liability company is to be a signatory to the Memorandum and Articles since these signatories must from inception have subscribed to some shares. There are other methods of becoming shareholders to a company.

i. To supply some required assets to the existing business in exchange for fully paid shares.

ii. By receipt of shares of the company for shares in another company in a take-over or merger.

Iii. By buying the shares in response to invitation through a prospectus.

iii. By buying the shares from an existing shareholder through the Stock Exchange. This method is only applicable to companies that are quoted in the Stock Exchange often referred to as Public Limited Companies (PLC).

iv. The already existing members could also increase their shares in the firm through Bonus Shares which is a form of sharing some classes of Reserve e.g. from Share Premium Reserve Accounts.

Peculiarities of Accounting for Incorporated Companies

The complex nature of the capital structure of Incorporated companies has a lot to do with the accounting disclosures. There is the need to account for different classes of dividend, maintain accurate record of Premium Share Reserve or its transfer to Bonus or script shares and Interest of various classes of loans or Debentures. Some of the Debenture holdings are cumulative while others are not. In the same way while some of the Debentures are convertible to ordinary shares others are not. The intricacies of these disclosures make the Accounts more complex compared to the Accounts of the Sole Trader or Partnership business. Where Incorporated companies are quoted, they are required to comply with the Stock Exchange directives. For example, they are required to publish the Accounts twice yearly i.e. half-yearly. The published half-year's Account is referred to as **Interim Report**. The information required for the Interim Report disclosure include:

i. Turnover for the period.
ii. Profit after Tax.
iii. Tax to be paid for the period.
iv. Dividend declared if any.
v. Earnings per share.
vi. Comparative figures for the corresponding previous period.
vii. Any other relevant information that will be of relevance to different classes of
viii. interest groups.

Some highly organised companies may publish their Accounts quarterly while the last quarter or half year report serve as a preliminary report for the year. Since ownership structure is wide, it is a statutory requirement that both the limited liability companies and public limited liability companies must publish their Accounts in two or more widely circulated daily newspapers.

2.08 Shares and Stock

Under Section 150 of CAMA 1990, the shares of a company can be converted into stock and vice-versa. A stock is the agglomeration of shares into a divisible unit of capital. The essence of converting shares into stock is based on administrative convenience because it seems to reduce the rigorous clerical work associated with recording of share transactions. The coming into being of the Central Securities Clearing System in the Nigerian stock exchange market has become a seemingly permanent solution to this problem. Though the concept of stock and shares can be used interchangeably, there exist a lot of differences which we need to understand.

		Shares	**Stock**
1.	Meaning	Indivisible unit of capital	Agglomeration of shares into one divisible unit quoted in bundles.
2.	Quotation	Quoted singly	Quoted in bundles

3.	Initial issue	Can be issued by the company (IPO) and need not be fully paid	Stock cannot be issued by the company. Must be issued as shares before it can be consolidated into stock and such shares must be fully paid
4.	Divisibility	Shares are indivisible	Stock can be divided into aliquot parts.
5.	Fractions	No fractional shares	Stocks have fractions
6.	Transferability	Transferable (Section 1 51 CAMA 1990)	Transferable
7.	Distinguishing number	Must be distinguished by appropriate number (Section 145 CAMA 1990)	Stock needs not have numbers.
8.	Transmission	Can be transmitted from the owner to his estate in the case of death (S. 155 (1) CAMA 1990)	Stock can be transmitted to the estate of the owner in case of death.

Source: Ilaboya 2008

Nominal Value of the Share

The concept of nominal value also referred to as par value dates to history of share ownership. Nominal value is the price at which a share is quoted in a stock exchange market. Before now, it was thought to represent the amount of capital distributable as dividend to shareholders. It was relied upon for public confidence even the creditors relied on the concept of nominal value as a form of protection. Though, events such as distress and corporate failure in Nigeria and the global corporate setting have revealed that the issue of per value as means of protecting investors was a mirage.

The only importance that can be attached to the concept of nominal value is that it allows accountants to properly record all details relating to issue of share. For example, per value will be important in recording the amount of premiums shares issued. The dividend accruing to a preference shareholder is a function of nominal value. Par values can be designated in naira amount which varies from company to company. In most cases it is either ₦1 or 50k, although this is not a standard practice. Per or nominal value is also important to determine the number of ordinary shares in calculating financial indices such as earning per share, dividend per share, etc. However, modern corporate Organisations are beginning to de-emphasize the concept of nominal value.

Hence in the United States of America, through the 1996 Model Business Corporation Act, it is possible to issue shares without par value. Shares without par value were before now issued to founders or promoters in consideration for their selfless services which cannot be quantified financially. Shares of no par value are designated in units only and can be sold at the prevailing market price, i.e. price determined by the interaction of the forces of demand and supply *(Ilaboya, 2008)*.

Procedure for Issue of Shares:

Issue of a prospectus to the public: A prospectus is a document prepared by reporting accountant at the instance of the underwriter which is to serve as means of advertising the company to members of the public.

Minimum Subscription

This is the minimum capital that can be raised by the issue of shares. According to Section 567 of CAMA 1990, no allotment will be made of any securities (shares) of a company offered to the public for subscription unless the amount stated in the prospectus as the minimum amount which in the opinion of the directors is required to be raised by the issue of share capital has been subscribed and the sum payable on application for the said amount has been duly received by the company.

The minimum subscription will include 25% of the authorized share capital of the company. For instance, if the authorized share capital of ABC Plc is ₦2,000,000 (Two million naira), it means the minimum subscription it can receive to allow the issue is ₦500,000 (Five hundred thousand naira), or such amounts as prescribed by the directors in the prospectus. And the amount payable on application will not be less than 50% of the nominal value of the shares. If on the expiration of 40 days after the first issue of the prospectus, the amount of minimum subscriptions has not been received, all application moneys are to be returned to the applicants. Thereafter (after 48days) such money will be repaid with interest at the going rate.

The minimum subscription as prescribed in schedule 15 Part 1 of CAMA 1990 will be used to meet the following costs.

a. Acquisition of property
b. Preliminary expenses and Commission on shares
c. Repayment of loans acquired by the company.
d. To provide for working capital for the Organisation.

Accounting for Issue of Shares

There are three methods for issuing shares to the public viz; issues of share for cash, issues of shares on account and issue of shares for non-cash consideration. When shares are issued for cash, it means the shares taken up are paid immediately. Such payment is completed on application. When shares are issued for cash, the proceeds from the issue are debited to cash or bank account and credited to share capital account. If the issued price is higher than the nominal value which is usually the case, the total sales proceeds are debited to cash or bank account and the nominal value is credited to a share capital account while the excess of the issue price over nominal value is credited to a share premium account.

Issue of Shares at a Premium

Shares are said to be issued at premium when they are issued at a price above the nominal value of the shares (Section 120 of CAMA 1990). When shares are issued at premium, the sum equal to the value of the premium (share price nominal price number of shares issued) will be transferred to an account designated the *share premium account*". And the account will form part of the share capital account and will not be reduced in any manner (Section 106 of CAMA 1990) except as provided for in section 120(3) of CAMA 1990.

Issue of Shares at a Discount

Shares are said to be issued at discounts when they are issued at a price below the nominal value. This process can be considered as a form of capital reduction and should be de-emphasized unless in extreme cases when it is considered the only option. Section l 21(1) of CAMAI 990 outlined certain conditions that must be met before shares can be issued at a discount:

a. Such shares must be a class of shares already issued.
b. Such issues must be authorized by a resolution passed in the general meeting of the company.
c. Such resolution must be sanctioned by the court.
d. The resolution must state the maximum rate of discount at which the shares are to be issued.
e. The shares must be issued within the month after the date on which the court sanction was received or within such extended period as the court may allow.

In most cases, only unpopular companies in dire need of additional capital can issue shares at a discount (*Ilaboya, 2008*).

Issues of Shares at PAR

Although very uncommon practice, shares are issued at par when the issue price is equal to the nominal value of the shares. The Companies and Allied Matters Act 1990 is silent on this approach to issue of shares. The purchase price of shares issued on account can be paid on installment basis. Upon receipt of the application money, the amount is debited to cash or bank account and credited to ordinary shares application account.

When applications are rejected either due to over subscriptions or otherwise, the amount of application rejected are debited to application account and credited to the cash or bank account using the application money. Surplus money retained and transferred or carried over to allotment is debited to ordinary share application account and credited to ordinary share allotment account using application money.

The balance in the ordinary share application account represents the application money received from the shares issued and this is debited to ordinary share application account and credited to ordinary shares capital account. On allotment, the ordinary share allotment account is debited, and the ordinary share capital account is credited with (the allotment money less premium) the amount of premium on allotment also debited to ordinary shares allotment account and credited to a share premium account.

It is however not in all cases that the premium value will be attached to the allotment money. It can equally be paid with the application money although the usual practice is to attach the premium value to the allotment money. On the receipt of the allotment money, the value after adjusting for the amount carried forward from application, is debited to cash account and credited to ordinary share application account.

Issue of Shares for Non-Cash Consideration

It is sometimes possible to issue shares not for cash but for non-cash consideration. This approach can be adopted to reward the selfless services of promoters who muted the idea of establishing the business. In addition, it is possible to issue shares in exchange for landed property and other assets which the business cannot afford to purchase due to lack of cash flow but which it requires to carry out its daily operations. Although the shares are not exchanged for cash, the value to be placed on the shares must be determined by the forces of demand and supply and the nearest approximation to this is the fair market value which can be determined with reference to either the value of the shares or the purchase price of the asset in an open market such fair market price can be established as:

i. Professional valuation of the asset to be exchanged.

ii. The prices of shares of similar company or the same company if the issue is to an initial public offer.

iii. The market price of the shares in issue. For example, if XYZ Nigeria PLC issues 500,000 ordinary shares with a nominal value of ₦1 in exchange for a landed property situated in Victoria Garden city, and the current price of XYZ Nigeria PLC shares in the Nigerian stock exchange market is ₦5 per share. Then the cost of the landed property will automatically approximate the market price of the total shares in issue. The journal entry to record the above transaction will appear as follows:

Journal Entry

	Debit ₦	Credit ₦
Landed property	2,500,000	
To ordinary share capital		500,000
share premium		2,000,000
Being the value of shares exchanged for a landed property at the market price of ₦ 5 per share		

Although issue of shares for non-cash consideration is a feasible option, it is hardly practicable in Nigeria hence it is conspicuously absent in the Act regulating corporate activities in Nigeria (CAMA 1990). It is however seldom seen in practice in Nigeria.

Script Issue

Script issue also referred to as bonus capitalization are shares issued to existing shareholders for no cost. They are normally issued from reserves hence the process is usually referred to as Capitalization of reserves. The reserves utilized for purpose of capitalization is the revenue reserve. On a general note, the only effect of bonus capitalization is to rearrange the equity structure of the Organisation. It does not affect the net worth of the Organisation. But should the future of the business improve, the interest of individual shareholders in form of dividend, may likely improve. Against the above back ground, one can succinctly say that the economic interest of bonus capitalization is not in the immediate but in the future.

Right Issue

These are shares issued to existing shareholders at a price below the current market price of the share. It is adopted when the company needs additional capital and does not want the public to subscribe so as not to dilute control. Though a form of capital reduction, it does not put the shareholders at a disadvantage position since the issue price is not below the nominal value of the shares. Rights issues are normally prorated. The distinguishing features between right issue and script issue is that while the latter are issued from reserve i.e. not paid for, the former is usually paid for by shareholders though at a price below the current value of the shares. Both types of issue are similar to the extent that they are to existing shareholders of the company.

2.09 Small Companies

The term “small company” has been captioned differently and defined severally by different writers. To some, small company is the same as small scale enterprise as well as small scale industry. The Nigeria Industrial Policy described small scale industries as those industries with total investment between ₦100, 000 - ₦2, 000, 000 exclusive of land but including working-capital. The Nigerian Industrial Development Bank defined small scale enterprises as enterprises with project cost (investment and working capital) not exceeding ₦ 30,000,000.

According to the Nigerian Economic Reconstruction Fund, they are those enterprises with fixed assets other than land but inclusive of cost of investment, not exceeding ten million naira. The Central Bank of Nigeria Credit and Monetary Guideline Number 25 defined small-scale enterprises as those with capital investment not exceeding five million naira including land and working capital. The Center for Industrial Research and Development, Obafemi Awolowo University ile-Ife, defined small scale enterprises as those with total investment capital not exceeding two hundred and fifty thousand naira and employing not more than fifty full time workers. The above perception of the concept; small scale businesses also differ from one economy to another.

In the United States of America, they are businesses that are independently owned, operated and whose annual receipts do not exceed five million dollars in some cases and eight million dollars in others. The Asian countries of China, Hong Kong and Korea defined small scale industries as establishments whose annual turnover on the average does not exceed three million American dollars. This version was however adopted in the United Kingdom. The United Nations Industrial Development Organisation had a different view when it captured the concept as one carried on by the group of small manufacturing enterprises which produce variety of consumer and simple goods as well as components and parts required by large industries. (*Ilaboya, 2008*).

The law regulating corporate activities in Nigeria- Companies and Allied Matters Act (Cap 59) LFN 1990 Section 351, described a small company in terms of the following conditions:

- Must be a private company with share capital
- Must have turnover of not more than ₦2,000,000
- Must have net assets of not more ₦l,000,000
- Non-alien members
- Must be without members who are government, government corporation or agency
- The directors between them must hold not less than 51% of the equity share capital of the company.

Privileges of Small Companies

Small companies enjoy certain privileges as prescribed by Schedule 7 Part I CAMA 1990.

1. Small companies are required to deliver a copy of a modified balance sheet instead of the full balance sheet as contained in Section 334(2b) of CAMA 19 and such balance sheet must be signed as required by Section 343 of CAM 1990.
2. Small company need not deliver a copy of the profit and loss account.
3. Small company need not deliver a copy of the director's report as required under Section 345 of C 1990.
4. Small companies need not supply information relating to number of employees remunerated at a higher rate.
5. Small companies need not disclose information on director's emolument.
6. Small companies need not disclose notes on the account except as related accounting policies, share capital, particulars of allotment and basis of translating foreign currency into Naira.

2.10 Conversion of Business to Limited Liability Company

Separate entity concept is a convention and not binding in law until the Company is granted incorporation. Conversion of a Business to a Limited Liability Company constitutes a significant manner of granting an incorporation status to hitherto unincorporated business. It makes it a distinct5 and separate entity and such company begins to acquire rights, duties and obligations from the relevant statute. Such a change is significant irrespective of whether the owner(s) changes or not. The limitations of shareholders' liabilities have been thought of as a disadvantage to the creditors. But it is to be considered as a protection for the absentee shareholders who are not involved with the daily management of the business since the ownership is divested from control. The creditor is however protected based on the formal relationship which exists in terms of publication of account, (Section 334 of CAMA 1990), inability to arbitrarily reduce capital of the company (Section 105 of CAMA 1990), prohibition of a company from acquiring its own shares (Section 160 of CAMA 1990) and the prohibition of any form of drawings.

Advantages of Conversion to a Limited Liability Company

1. Access to more funds.
2. Facilitates succession without liquidation.
3. Assets realization without divestment of control.
4. Perpetuity
5. Detailed reporting of business activities.
6. Gives room for diversification.

Forms of Conversion

Conversion of business to limited liability company can assume any of the following forms:

- Form a public company to take over the business of the existing firm and the existing shareholders are compensated in form of share exchange.
- Promoters purchase existing business and sell it to a public company which will be formed for the purpose of the acquisition and the new company issue shares to the public to raise capital.
- Convert the business to a private company and the existing owners will allot shares to themselves to retain the control of the company.
- Convert into a company and sell part of the shares to public and retain others.

The implication of any of the alternatives above is that the business needs to be revalued at the point of transfer since the existing assets are not stated with current values, goodwill is not reflected in the current balance sheet and also to “wash” the balance sheet of fictitious assets such as preliminary and formation expenses, discount on shares and debentures, losses carried forward and advertisement cost which are borderline cases.

2.11 Underwriting Account

This is a contract of guarantee that shares issued to the public will be taken up, failing which the underwriter takes up the shares. Shares issued to the public is usually based on uncertainty because it is not easy to determine the number of shares the public can take up.

Based on this uncertainty, companies issuing shares must take up the service of an underwriter who gives a reasonable guarantee to take up any share not fully subscribed by the public. In a situation where the shares are fully subscribed, there is no obligation to take up the reminder. The major reason why management uses underwriters may include:

i. To raise the minimum subscription which S5.67, schedule 15 paragraph 2 of CAMA 1990 specified as 25% of the authorized share capital or as specified by the company directors in the prospectus.
ii. Since the initial public offer is fraught with uncertainties, the guarantee by underwriter helps to avoid under-capitalization which may result from poor subscriptions since the underwriters guarantee to take up the balance unsubscribed.
iii. To meet the threshold capital requirement of the Organisation which will guarantee the success of the Organisation.

There are two basic types of underwriting contracts. These are the *firm commitment* and *best efforts*, under the firm commitment*,* the underwriter underwrites the securities. He purchases the securities for less than the offering price and accepts the risk of selling all the securities. This is merely a purchase-sale arrangement. If it thus happens that one underwriter cannot do this contract alone, he arranges for a group of underwriters called **Syndicate** to share in the risk and ensure full subscriptions. In a **Syndicate** arrangement, the coordinator is called the **principal manager or lead underwriter** who assumes the risk flowing from the syndication. Underwriter has the primary objective of ensuring that the shares are taken up by their clients. The interest of the underwriter in a firm commitment arrangement is spread or discounted which is the difference between the underwriter buying price and offering price of the shares. But in addition to the spread, the underwriter can equally be entitled to a non-cash consideration or compensation in form of share warrants.

The *best effort* arrangement is completely different from the firm commitment contract. This is because in the former, the underwriter does not purchase the shares in a best effort arrangement, he merely acts as an agent who is rewarded based on shares sold to the public.

He has a legal duty to ensure that the securities are sold at the offering price and any balance unsold is withdrawn. In the firm commitment arrangement, the lead underwriter is entitled to a commission for taking the extra effort to organize the syndicate. In most cases, it is usually 1% of the total number of shares underwritten and not on the total issued.

2.12 Review Questions

1. Differentiate between an incorporated company and a partnership. What advantages and disadvantages attend each type of organization.
2. Why are statutory books so called and briefly describe each of its constituents?
3. Compare the different forms of business capital. Which one would you recommend to a Nigerian entrepreneur and why?
4. How and why may a business be converted to a limited liability company

MODULE 3

3.00 LAW RELATING TO BANKING

3.01 LEARNING OUTCOMES

On successful completion of this module, students should be able to:

i. Assess and analyse the conditions for establishing Banking Businesses in Nigeria;

ii. Discuss and appraise the roles of CBN, NDIC and EFCC in the banking business in Nigeria;

iii. Categorise Nigerian Banking statutes and analyse associated common law principles of Banking;

iv. Distinguish between the different kinds of Negotiable Instruments;

v. Deconstruct features of cheques.

3.02 The Banker

Most definitions have used the words "bank" and "banker" interchangeably, thereby making the definition of the terms difficult. The draft of the British Bankers Act 1856 attempted a definition of this concept thus: "A banker includes any person or persons or corporation or joint stock or other company acting as a banker or bankers".

H.L. Hart in his famous book, The Law of Banking; Fourth Edition 1931 defines a banker or bank as:

> *… a person or company carrying on the business of receiving moneys and collecting drafts, for customers, subject to the obligation of honouring cheques drawn upon them from time to time by customers to the extent of the amount available on their current accounts.*

S.2 of the Bills of Exchange Act 1882 narrowed the definition of "banker" to: "A body of persons whether incorporated or not who carries on the business of banking." This is the definition adopted by Nigerian Bills of Exchange Act Cap 35, Laws of the Federation of Nigeria 1990.

The Banks and Other Financial Institutions Act defines a bank as:

> *"a duly incorporated company in Nigeria holding a valid banking license to receive deposit on current account, savings account or other similar account, paying or collecting cheques drawn by or paid in by customers, provision of financial or such other business as the governor may by order publish in the gazette designate as banking business".*

This means that a human being cannot be correctly called a banker in Nigeria. This was confirmed in ***Akule and 10 Ors v. R (1963).*** In that important case, the appellant was the branch manager of the Bank of West Africa Ltd, Kano. He was in the habit of fraudulently passing cheques to the credit of his co-accomplice. He was charged for criminal breach of trust as a banker under s.31 of the Penal Code of Northern Nigeria. The question was whether he was a banker under the Banking Act 1958. The Supreme Court held that he was not a banker but only an employee of the bank and that the banker was the company carrying on banking business.

3.03 Duties of Banks to Customers

The duties of banks to their customers include:

a. Duty of care and skill in the management of the customer's account. It includes correct payment of interest on deposits and correct deduction of interest on loan facilities. See *UBN Plc v. Ajabule (2011) 18 NWLR pt 1287 p152.*
b. Duty of confidentiality, not to disclose the details of customer's account to third parties without approval of the customer. See *UBA Plc v. Davies (2011) 11 NWLR pt 1259 p.591.* This case arose on banker/customer relationship between the Appellant and the Respondent which resulted in publication of the indebtedness of the customer by the Appellant Bank without proper notice of the indebtedness to the customer to liquidate same. The court held that the defense of qualified privilege was not available to the appellant Bank.
c. Duty not to cause injurious falsehood in giving incorrect recommendations for the customer. See *UBA Plc v. Davies (2011) 11 NWLR pt 1259 p.591.*

d. Duty of honouring customer's cheques and other lawful instructions. If the bank fails to honour a cheque when the customer has enough credit in the relevant account to cover the value of the cheque, it is a breach of the bank's duty that attract special and general damages. The customer does not need to prove that his reputation was injured to secure substantial damages. See *UBN Plc v. Ajabule (2011) 18 NWLR pt 1278 p.152.*

e. Duty to prevent fraud on the customer's account. However, S.60 of the Bill of Exchange Act provides that a banker who pays on a cheque fraudulently obtained, in good faith and in the ordinary course of business, incurs no liability. In *Bank of England v. Vigliano Bros. (1891*), it was held that a banker is not an authority on signatures and that commerce will be greatly hampered if a banker is held to be. This was also the view of the Nigerian court in *Irosogie v. Standard Bank (1977).* Also see *London Joint Stock Bank v. MacMillan & Arthur (1918).*

3.04 Conditions for Establishing a Banking Business in Nigeria

The following conditions are pre-requisites for establishing a banking business in Nigeria:

1. A company is incorporated under the Companies and Allied Matters Act as public liability company with share capital of at least N25 billion.

2. The top hierarchy of staff especially the managing director is appointed subject to the approval of the Central Bank of Nigeria

3. An application is made to the Central Bank of Nigeria for a banking license. The application is supported with the required mandatory deposit, list of proposed management staff, application fee, copies of the incorporation documents and other documents.

4. Central Bank processes the application including visits to the proposed head office of the bank to ensure the installation of appropriate facilities including IT and other infrastructure.

5. A banking license is issued, and the bank is authorized to commence business.

3.05 Regulation of Banking Business in Nigeria

The banking industry is tightly regulated in Nigeria. The following institutions eventually are the main regulators of the Nigerian banking sector namely: CBN, NDIC and EFCC.

1. Central Bank of Nigeria (CBN)

This is the institution that exercises close control of the Nigerian financial system through its Monetary and Fiscal Polices and directives, enforced by direct supervision of commercial banking. S.42 of the CBN Act provides that the Central Bank has powers to control other banks in the system. S.40 stipulates that the CBN is the bankers' bank, and S.27 stipulates that the bank has the powers to discount and re-discount treasury bills and treasure certificates. The bank also has the power to withdraw the license of a commercial or merchant bank that contravenes the regulations, by the provisions of Banks and Other Financial Institutions Act. So, held the Supreme Court in *NDIC v CBN (2002)*. This suit was instituted by the Republic Bank Limited against the actions of the Central Bank of Nigeria that withdrew its banking license issued by it in June 1988. The Nigerian Deposit Insurance Corporation was appointed as provisional liquidator. The Republic Bank Limited went to court to seek a declaration that the revocation of the license was illegal, null and void as same was not based on a good reason as provided under section 23 of the Banks and other Financial Institution Decree 1991. The court held that the revocation was properly done under the condition envisaged by section 12 of the BOFIA of 1991.

To be able to exercise its statutory powers, the CBN periodically and very frequently, carries out commercial bank audit, through scrutiny of mandatory reports sent to it by the banks as well as physical visits to those banks by officials of the Supervision Department.

2. Nigerian Deposit Insurance Corporation (NDIC)

The NDIC is the agency of the Federal Government that is responsible for insuring commercial bank depositors' funds so that if a bank should fail, innocent depositors will be paid something. At the inception of the institution in the early 1990s, the maximum a depositor could get was ₦50,000 regardless of how much above this amount the depositor had in the failed bank. This has now been increased to ₦100,000.

The NDIC tries to prevent bank failure by carrying out periodic inspection of commercial banks to ensure that bank officials play the game according to the rules. The NDIC has powers to:

a. Take deposits as insurance premiums from commercial banks to grant insurance cover over the bank's customers' funds.
b. Inspect books of commercial banks to ensure compliance with the law;
c. Sanction a bank manager for acts that are inimical to proper bank performance;
d. Initiate the process of withdrawing a banking license and eventual winding up of a bank before its assets become hopelessly depleted. The court confirmed this power in the case of *NDIC v. CBN (2002)* supra.

3. Economic and Financial Crimes Commission (EFCC)

This law enforcement agency was set up when it became clear that the magnitude of financial crimes in Nigeria is beyond what can be safely left in the hands of the Nigeria Police alone to battle with. The Commission has powers to:

a. Investigate any case of financial crime and to prosecute suspects, independent of the Office of the Attorney-General of the Federation.

b. Investigate and prosecute money laundering activities and obtaining money by deceit (s.419 of the Criminal Code).
c. Investigate and prosecute suspects accused of stealing money from Organisations and government as well as from individuals.

As part of the efforts to curb these financial crimes, the Act stipulates that –

i. Any single deposit of ₦500,000 by any individual or ₦5 million by any corporate Organisation must be reported to the EFCC by the bank into which the deposit is made;
ii. No transaction involving the sale of land or landed property should be paid for by cash.

3.06 Some Banking Statutes in Nigeria

1. Banking Act, Cap B1, LFN 2004

S.1 of this Act empowers the Minister of Finance to approve the licensing of an incorporated company to operate as a bank in Nigeria. This means that in Nigeria, there cannot be a bank that is not an incorporated company. The Act also provides that all banks shall set aside at least 25% of their profits as reserves when the existing reserves are less than the paid-up capital. Where the existing reserves are more than the paid-up capital, then 12 ½ % of the profits must be retained as reserves.

S.10 of the Act also provides that no bank shall pay dividends if losses or preliminary expenses are not yet completely written off or if bad and doubtful debts are not fully provided for. This is the import of the Prudential Guidelines issued by the Bank. S.14 of the Act provides that banks should not grant loans, guarantee or enter into commitment to any one person up to 33 1/3 % of their paid-up capital and reserves. Finally, the Act provides that all banks must make monthly reports (called returns) to the CBN not later than 28 days into the ensuing month. Where there are significant discrepancies between the Returns and the findings of CBN supervisory teams when they visit banks, the banks will be penalised and the offending bank managers may be relieved of their positions.

2. Central Bank Act Cap C5 LFN 2004

This law empowers the Central Bank (CBN) to control the banking industry in Nigeria. Targeted at the regular banks, the law empowers the CBN to check bank books to ensure compliance with the CBN and other Acts as well as CBN's own prudential guidelines. Erring banks can be sanctioned by the CBN. Sanctions can include recommendation to the Minister to:

a. Withdraw a banking license; Licensing of companies as bankers is the responsibility of CBN;
b. Remove some offending managers or directors;
c. Pay fines.

The CBN can also suspend an erring bank from:

i. The clearing system;
ii. Deals in foreign exchange market
iii. Acting as issuing house for new offers

Under the Act, the CBN must approve the appointment of a bank's chief executive officer as a person sufficiently skilled in bank management (usually a person who must have attained the rank of executive director in a bank).

3. Banks and Other Financial Institutions Act (BOFIA) Cap B1 LFN 2004

The Act gives CBN as well as NDIC powers to further control the regular banks, especially in the areas of frauds, money laundering, and other financial crimes. Under this law, activities of finance houses, micro-finance banks, discount houses, bureaux de change, and other quasi-banks are brought under CBN and NDIC control.

The main provisions of the BOFIA are:

1. Licensing of companies as bankers is the responsibility of CBN;
2. A banking license may be withdrawn (revoked) for contravening S.12 of the Act due to:

a. Failure of the bank to operate the type of business for which the license was issued. For example, if the license was issued for merchant banking, the bank cannot go into retail commercial banking unless an amendment to its status has been approved by the CBN.

b. The winding up or liquidation of the banking institution. It must be noted that once the NDIC concludes that a bank cannot survive as a going concern by looking at the banks books, it would have initiated a winding up process before the bank collapses.

c. Failure to comply with the conditions of the license, such as making periodic returns to the CBN and NDIC, payment of NDIC insurance premiums or to maintain capital and reserves as well as mandatory liquidity cover for transactions.

d. Allowing the assets to be depleted (i.e. Less than its liabilities).

e. Failure to comply with other obligations imposed by BOFIA or CBN. This saving clause is designed to take care of situations where new regulations are made after the Act and the License.

f. Failure to display lending and deposit rates, and financial summary for the immediate past reporting period in all banking halls.

4. Bank Employees Etc. (Declaration of Assets) Act Cap B9 LFN 2004

a. S.1 of the Act provides that 14 days after employment, all bank employees must disclose/declare their assets.

b. S.4 provides that 7 days after the anniversary of an employment, a bank employee must declare any increase or decrease in his assets, and that this to be an annual compulsory event.

c. The yearly declaration must continue 2 years after an employee has left the bank in question.
d. S.8 stipulates that failure to declare or improper and or incomplete declaration attracts a jail term of 10 years on conviction together with forfeiture of the assets of such employee to the Federal Government.
e. S.9 of the Act prohibits the use of smoke-screens or agents to hide assets. Such agents on discovery will on conviction face Seven (7) years imprisonment.

5. Failed Banks (Recovery of Debts) and Financial Malpractices in Banks Act No.18, 1994

This law empowers the CBN and NDIC to, in cases of failed banks, institute criminal proceedings in the name of the Federal Government against anybody particularly bank officials, with leave of court.

This law has therefore contradicted the provisions in the Constitution that only the Attorney-General of the Federation can institute criminal proceedings against any person on behalf of the Federal Government. However, it was used to prosecute the case of *Controller General of Nigerian Prison Services vs. Adekanye & 25 Ors (No.1) (2002).* The respondents were held in prison custody for alleged offences under the failed Banks (Recovery of Debts) and Financial Malpractices on Banks Decree. They filed a habeas corpus proceeding against the appellant (NPS) in the Lagos State High Court. The appellant however raised an objection that the High Court does not have jurisdiction to entertain the case. The court dismissed the preliminary objection and held that whoever asserts that a provision has not been complied with has the onus to prove same.

6. Banking (Freezing of Accounts) Act Cap B7 LFN 2004

The Act empowers the President to freeze the bank account of any person who is suspected of having committed fraud or bribery or any act amounting to corruption, etc. Once an account is frozen under the provisions of the Act, the bank will be committing a criminal offence if it allows any transactions out of it.

7. **Economic and Financial Crimes Commission Act Cap E1 2004 (EFCC Act)**

S.6 (2) of this Act empowers the Economic and Financial Crimes Commission to administer the provisions of the following Acts:

(a) Money Laundering Act 1995

(b) Advance Fee Fraud and Other Fraud Related Offences Act 1995

(c) Failed Banks (Recovery of Debts) and Financial Malpractices in Banks Act 1994

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

(e) Miscellaneous Offences Act, and

(f) Any other law or regulations relating to economic and financial crime.

This means that in future, its scope of activities can widen as other laws in this area come into being. Section 13 of the Act provides that any person who, being an officer of a bank or other financial institution:

a. Fails to comply with the provision of the Act, or
b. Fails to secure the authenticity of any statement submitted pursuant to the provisions of this Act, commits an offence and may be convicted and sentenced to a term of imprisonment of 5 years or a fine of ₦50, 000 or both. The important directives under the Act which banks are expected to comply with are:
    1. S.31 (2) requires banks to pay over to the Commission any money which is the subject of a final order sequel to a conviction for fraud or some other crime. Failure to do so will attract a prison term for the offending bank official for a period of up to 3 years without the option of a fine.
    2. S.33(1) empowers the Commission to cause a bank to freeze any person's bank account, and to call for scrutiny, bank books, documents or any other information as may be required by the Commission.
    3. Under S.33(1) the Commission can demand from the bank the identity of any person who, in one transaction, deposits a cash amount of ₦500,000 and above or a company which deposits ₦5 million and above.

3.07 Common Law Principles of Banking

Apart from the provisions of the various statutes outlined above, our courts still employ some common law provisions in deciding matters relating to the business of banking in Nigeria. The more important of them are as follows:

1. **Garnishee Proceedings.** Where a judgment debtor is himself a creditor to another person (the garnishee), a garnishee proceeding is embarked upon to force the ultimate debtor to pay over to the judgment creditor. The judgment creditor normally applies for an order of court *nisi* that the judgment debtor pay him by the instrumentality of attaching the debt due from the judgment debtor. If it is money in a bank account, the bank is served with the order not to allow the debtor take any money out of the account (garnishee order). When the order is made *absolute*, the bank is ordered to pay the money to the court. This was what happened in *Sokoto State Government v. Kamdax Nigeria Ltd (2004).* The respondent (Kamdax Nig. Ltd) sued the Appellant at the High Court of Lagos claiming the sum of N792, 250 being the balance of outstanding payments on a contract for the supply and installation of Gas chlorinators and interest thereon. The trial court entered judgment for the Respondent and granted order nisi for the 3rd Appellant (Standard Trust Bank) to pay the sum as owed the judgment debtor. The Appellant appealed the decision to the appeal court which dismissed the appeal.

2. **Guarantee.** When a person guarantees another person for a loan from a bank, the bank can proceed to recover the money from the guarantor without first suing the person guaranteed and regardless of whether the person guaranteed has defaulted. So, held the court in *Auto Import Export v. Adebayo (2005) 19 N.W.L.R (Pt. 959) 44.* It was also held that a guarantor is technically a debtor because where the principal debtor fails to pay debt, the guarantor will be called upon to pay the indebtedness so guaranteed. The guarantor can, however, be absolved from liability if he can show that the principal debtor has paid the indebtedness.

A guarantee once issued, is legally a standing one, so that if the original amount borrowed is repaid, the guarantee does not expire unless it is specifically tied to that particular loan by careful phrasing of the guarantee instrument. It was held in ***F.I.B Plc v. Pegasus Trading Office (2004) 4 N.W.L.R (Pt 863) 369 S.C***, that if the borrower should take money again from the bank and fails to pay, the guarantor will be liable for such subsequent debt. See also *Dragetanos Const. (Nig) Ltd. v. F.M.V. Ltd (2011) 16 NWLR pt 1273 p.308.* The appellant was contracted by PTF to construct certain roads in some parts of Niger State. The appellants sub contracted the contract to the 1st Respondent. In lieu of the N10,000,000 (Ten Million Naira) paid by the Appellant to the 1st Respondent as mobilization fees, the 1st Respondents were made to secure a loan of N5,000,000 (Five Million Naira) from the 2nd Respondent. The 1st Respondent in the course of execution of the contract had some problems with the Appellant. They sued the appellants and claimed both general and special damages. The trial court granted the special damages sought but declined to grant the general damages. The Appellant appealed to the court of appeal and the court allowed the appeal on the ground that the Respondent did not sufficiently prove their case and that the findings of the trial court were perverse.

3. **Indemnity**. Indemnity aims to protect business owners and employees when they are found to be at fault for a specific event such as misjudgment. It is a sum paid by party A to party B by way of compensation for a particular loss suffered by B. The indemnitor (A) may or may not be responsible for the loss suffered by the indemnitee (B). Thus, a guarantor may (and will always) require the customer he is guaranteeing to enter into an indemnity with himself for any loss he may incur because of guaranteeing the customer. Forms of indemnity include cash payments, repairs, replacement, and reinstatement. An indemnity should also be differentiated from a guarantee.

This distinction between indemnity and guarantee was discussed as early in the eighteenth century in ***Birkmya v Darnell (1704) 1 Salk 27.*** In that case, concerned with a guarantee of payment for goods rather than payment of rent, the presiding judge explained that a guarantee effectively says, "Let him have the goods; if he does not pay you, I will." See also: *Mountstephan v Lakeman (1871) LR 7 QB 196*

Bank Drafts

These are crossed cheques issued by banks, guaranteed to be backed by prior payments deducted from the account of the customer that requests for it. They are therefore bankers' cheques drawn on the bank's resources. So, held the court in *F.A.T.B. Ltd. v. Partnership Inv. Co. Ltd. (2003) 18 NWLR pt 851 p. 35.* The Respondent sued the Appellant at the High court of Lagos state claiming the sum of N7,000,000 (Seven Million Naira) for refusal of the Appellants to honour a bank draft it issued. The trial court and the court of appeal granted judgment in favour of the Respondent because there is a presumption in law that once a person signs a promissory note, he is bound by it. On appeal to the Supreme Court, the court upturned the decision of the courts below on the ground that for a party to benefit from a promissory note, he must pay some value for it and that the Respondent's case is tainted by fraud and they did not pay any value for the note. See also *UBA Plc. V. G.S. Ind. (Nig) Ltd. (2011) 8 NWLR pt 1250 p.590.* The Respondent sued the appellant at the trial court for negligence over a value of a draft of the Allied Bank it lodged with the Respondent for transmission to the Allied Bank for clearing on the 4/4/96. The Appellant negligently did not transmit the draft to the bank and the Allied Bank were sent out of the clearing house on the 10/4/96, occasioning loss to the Respondent. In this suit, the Respondent claimed both pre and post judgment interests on the value of the note. The trial court granted all the reliefs sought by the Respondent. Dissatisfied, the Appellant appealed to Court of Appeal and after being denied by the appellate court, later to the Supreme Court. Both courts affirmed the decisions of the lower courts. Dismissing the Appeal, the Supreme Court held that the Appellants were liable to the Respondent in negligence for keeping the note for that long and when it was rejected they did not return same to the Respondent.

Letters of Credit

Letters of credit are international credit arrangements whereby a local bank in Nigeria guarantees a foreign bank to pay a supplier of goods for which the customer in Nigeria has paid or entered an irrevocable contract with his local bank, that he will pay the bank for goods to be supplied to him by a foreign supplier. Once the foreign supplier ships the goods, he uses the shipping documents as evidence of delivery to collect proceeds from his local bank. The local bank sends the shipping documents to the Nigerian bank as evidence of payment to the foreign supplier. The local bank then pays the foreign correspondent bank (through the Central Bank of Nigeria).

3.08 Negotiable Instruments

In Nigeria, the first main enactment to control negotiable instruments was the Bill of Exchange Act, 1917. This was replaced by the 1958 Act which has metamorphosed into the Bill of Exchange Act, Laws of the Federation 2004. Also relevant is the Dishonoured Cheques Decree 1977 which is special for cheques (now the Dishonoured Cheques Act, 2004).

Negotiability is the quality of legal transfer of title in a document from one holder to another (that other thereby becoming a holder in due course). The mere delivery of the instrument entails the concept of negotiability. When an instrument is transferred (delivered) by one person to another, that other person acquires an unfettered right to claim in his own name, and to enforce the contract or promise. He becomes a holder in due course, and acquires a status which is basically one of a bona-fide purchaser acquiring an over-riding title. The holder in due course needs not to have given value himself. For example, if he acquires the bill by gift or finds it lying on the ground, the law will bestow good title to anyone to whom it is negotiated, provided that other person has no notice of his defect of title. That other person is said to have acquired a good title "free of equities", meaning that no defect of title of the previous holder affects his rights. So held the Court of Appeal in England long ago in the case of *Webb, Hale & Co. v. Alexander Wate Co. Ltd (1905).*

Negotiability requires four important features to be present at the same time as follows:

a. Title passes on mere delivery of the instrument by one person to another. This means that if one person gives another person a bill, that other person becomes automatically entitled to the property in the bill. In other words, he becomes the owner.

b. A holder for value takes delivery and therefore title, free of defects in the title of the transferor. This means that even if the transferor stole the instrument, as long as the transferee does not have notice of such a defect in title of the transferor, he (the transferee) has a perfect title to the instrument.

c. The holder can sue in his own name. This is because, in law, he is the absolute owner of the instrument.

d. No notice is required to be given to the payer regarding transferability of the instrument. The ultimate transferee (there can be many transferees each endorsing the instrument to the next) can present the instrument for payment and the payer cannot refuse on the ground that he was not informed that the document has changed hands.

Holder in Due Course

This term with regards to Negotiable Instruments means that the –

1. possessor is the holder of the instrument
2. holder obtained it for valuable consideration
3. holder obtained it before its maturity date
4. holder has no notice of its previous dishonour
5. holder obtained it in good faith without notice of any defect in title of (any of the previous) previous holder(s)
6. instrument is complete and regular in the face (i.e. no visible sign of alteration or defacement since the last endorsement).

Kinds of Negotiable Instruments

All negotiable instruments have three essential features of being an instrument: (a) written, (b) being a contract and (c) being negotiable, which make them a special type of contract which can be assigned by one person to another person who was not a party to the contract at the inception (*ab initio*). The assignee is though not privy to it in the beginning but is later subrogated in the process of negotiation.

Negotiability sets negotiable instruments apart from other contracts. It means that mere delivery is enough to vest title in a holder even if he has not furnished any consideration as long as some person has already done so.

The following are species of negotiable instruments:

1. Bills of Exchange (of which cheques are of special importance).
2. Promissory Notes
3. Travelers' Cheques
4. Treasury Bills
5. Bearer Bonds
6. Bearer Debentures
7. Dividend Warrants.

Bills of Exchange

A bill of exchange is defined at S.3 of the Bill of Exchange Act 2004 as:

> *"an unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed, to pay on demand or at a fixed or determinable future time, a sum certain in money, to or to the order of a specified person or to bearer".*

The bill will therefore, be valid only if –

a. it is an unconditional order (without any conditions precedent or subsequent);
b. it is in writing;

c. payment is on demand or at a determinable future date or time;

d. there are three parties (drawer, drawee and payee);

e. payment is by money (a sum certain); and

f. Payment is to an existing person.

Types of Bills of Exchange

Foreign and Inland Bills (s.4 of the Act). Foreign bills are bills drawn on an overseas person or institution (e.g. a bank) while inland bills are payable within the country. A Bill of Lading, Letter of Credit and Airway Bill are examples of foreign bills.

1. Sight Bills (also called Demand Bills). These are payable on demand, like a cheque.
2. Time Bill – a bill payable at a specifically stated time.
3. Accommodation Bill – is a bill drawn on a person who has resources to pay in future but not the present and who accepts it now for negotiability and discounting.

Parties to a bill of exchange - Parties that may be liable under a negotiable instrument are:

1. The drawer (the originator who wrote the Bill) S.55 (1)
2. The drawee / acceptor (the person who will pay) Ss.53 and 54.
3. Payee / Endorser (beneficiary who takes or assigns value to another person) S.31
4. Quasi endorser (guarantor) S.55 (2)
5. Transferor or bearer who transfers.

No. 0011	Jos, Plateau State
	1st July, 2014
₦5, 000:00k	

Two months after sight of this first of exchange (second and 3rd parts of this exchange are not being paid), pay to Mr. Okoro Adekunle or order, the sum of Five Thousand Naira only for value received.

The drawer is primarily responsible and liable if the instrument is dishonoured. However, if the instrument is accepted by the drawee, then the drawer becomes a guarantor so that if the acceptor should fail to pay, the payee will call on the drawer to pay.

The payee can acquire liability if he endorses the instrument to another person who becomes the holder or holder in due course as the case may be. Similarly, a quasi-endorser who guarantees honour will become liable to a holder if the acceptor fails to pay in which case he replaces the original drawer for convenience.

An acceptor can accept unconditionally or conditionally. In case of unconditional acceptance, he is liable to pay. In a conditional acceptance, the acceptor can validly refuse to pay if the condition is not fulfilled. Similarly, if after acceptance there has been a fraudulent endorsement, he can refuse to pay but if such endorsement had been made before his acceptance, he must pay mandatorily.

Dishonour: Dishonour can be either refusal to accept or refusal to pay on the instrument. S.47 provides for two types of dishonour, both of which produce the same result. If the payer insists on qualified acceptance and the holder refuses to take a qualified or conditional acceptance, it may amount to a constructive dishonour, entitling the holder to take legal action against all endorsers.

If a bill is dishonoured, every endorser and ultimately the drawer must be notified before the expiration of its tenor or else it is regarded as having been discharged.

Discharge

The instrument is discharged if the party liable to pay is released and relieved of the obligation to pay. Discharge may happen in the following instances:

1. When the instrument is paid in due course. S.59.
2. When the acceptor becomes the holder in his own right on or after maturity. S.61.
3. When the holder waives or renounces his rights against the acceptor, Ss. 62 and 63.
4. When the bill is intentionally cancelled by the holder.

A party may be discharged and yet the bill itself is not discharged:

a. When a bill is dishonoured and the drawer and endorsers are not put on notice, they will be discharged and yet the acceptor is still liable.

b. Where a holder accepts conditional acceptance without notice to the endorsers and drawer, these are discharged but the acceptor is not.

c. Where the holder fails to present the bill for acceptance or payment as the case may be, this releases the endorsers and drawer but not the bill.

d. Where it is materially altered. S.64 (1) provides that where an instrument is materially altered, it is void except against parties who have made, authorized or assented to the alteration, and subsequent endorsers who follow them.

3.09 Cheques

A cheque is a bill of exchange drawn on a banker payable on demand. This is the definition adopted by S.73 of the Bill of Exchange Act. Most of the provisions relating to a Bill also apply to cheques. Note must however be taken of two distinct qualities of a cheque –

1. It is almost always drawn on a bank.
2. A cheque is always payable on demand.

Due to the foregoing, the definition of a Bill of Exchange is amended by S.73(1) for the cheque, as “an unconditional order in writing addressed by one person to a banker, signed by the person giving it, requiring the banker to pay on demand, a sum certain in money to or to the order of a specified person or bearer”.

Negotiability of Cheques

Negotiability of cheques is better discussed with the aid of an example. If Mr. A draws a cheque payable to Mr. B or bearer, anybody who happens to come in possession of the cheque other than Mr. B is called a bearer if he is simply holding it, or an endorsee if Mr. B writes at the back of the cheque that the bank should pay such a person and he (Mr. B) signs his name.

If that person presents the cheque to the cashier of the paying bank (the banker), he can be paid, and such payment will be quite legitimate and legal provided the banker paid in good faith and without notice of any fraud or theft. In *Clerk v. Pigot (1699*), a rogue presented a cheque and was paid. The true owner of the cheque sued the bank and the court in England held that the bank incurred no liability because it paid the cheque in good faith and without notice of the theft of the cheque. Similarly, if the payee (the person whose name is written on the face of the cheque) endorses it to another person (at the back of the cheque), that other person becomes the new payee. Cheques can be endorsed in this way indefinitely until one endorsee presents it for payment. Therein lies the beauty of negotiability as an aid to commerce.

But to prevent *Clerk v. Pigot* situations, cheques are usually protected against thefts by "crossing" which incidentally destroys free negotiability.

Other qualities of a cheque that differentiate it from other Bills of Exchange include the following:

1. Cheques take no days of grace unlike bills which have 3 days of grace. S.14 (1) Bill of Exchange Act.

2. There are statutory protections for bankers who pay out on cheques or who collect on a cheque for their customers, e.g. no liability for paying to wrong person if done in good faith without notice of any defect in that person's title. No such protection exists in respect of bills.

3. A bill must be presented for payment when due otherwise the drawer is discharged under S.45. The drawer of a cheque is never discharged in this way.

4. A bill necessarily has to be presented for acceptance. Cheques are payable on demand. No acceptance stages are necessary.

Features of Cheques

1. **Crossings. S.78.**

   a. *General Crossing* -- Two parallel lines drawn across the face of the cheque with or without the words "& Co." written in between them. Under S.78 (1), when a cheque is crossed in this way:

   i. it is payable only through a bank account
   ii. thereby allows time to detect fraud before payment
   iii. and affords more time to countermand (stop) the cheque if necessary, e.g. when a fraud is detected early.

   b. *Special Crossing* - Two parallel lines drawn across the face of the cheque with the name of a banker. Under S. 78(3), when a cheque is crossed in this way:

   i. it is payable only through a bank account in the named bank
   ii. thereby allows time to detect fraud before payment
   iii. and affords more time to countermand (stop) the cheque if necessary, e.g. when a fraud is detected early.

   c. *Non-Negotiable* - Two parallel lines drawn across the face of the cheque with the words "Non-Negotiable" written in between them. This destroys negotiability. In case of fraud, the transferee cannot receive value or if he does, it can be recovered from him by the payer. The subsequent transferee takes with full equities, i.e. with defects of the transfers' title. In other words, the principle of negotiability does not apply.

   d. *Payee A/C Only* - When these words appear between two parallel lines on the face of a cheque, they mean that the cheque is not transferable and must be paid to the payee's bank account.

e. *Limits of Payment* - Sometimes a drawer will use cheques pre-printed with a maximum value at the top. This limits how much a rogue can take if the blank cheque should fall into wrong hands. If for example, the cheques are printed with "Maximum Value - One Million Naira" at the top, a rogue who forges the signature of the drawer cannot write more than ₦1 million on the face of the cheque and expects the bank to pay it. If he does so, it will, or should surely raise suspicion, and the banker will be put to enquire from the drawer if indeed the drawer issued the cheque.

f. *Safest Crossing* - Combines the above. When a cheque is crossed in this way, it is almost impossible for an unauthorized person to obtain value from it. No banker can honour such a cheque from a rogue without incurring responsibility for reimbursing the true owner. This was why in *Trade Bank Plc v. Benilux Nigeria Ltd (2003)*, the court held that if a collecting bank pays to a wrong person (not entitled to the proceeds), it is guilty of a tort of conversion. In that case, the court wondered aloud how a bank could pay to a wrong account, a cheque clearly marked "A/C Payee Only" and "Not Negotiable". That was exactly what happened 14 years earlier in *BBC Brown Boveri v. Wema Bank (1989).*

2. Protection of Bankers

S.60 of the Act provides that a banker who pays on a cheque fraudulently obtained, in good faith and in the ordinary course of business, incurs no liability. In *Bank of England v. Vigliano Bros. (1891*), it was held that a banker is not an authority on signatures and that commerce will be greatly hampered if a banker is held to be. This was also the view of the Nigerian court in *Irosogie v. Standard Bank (1977). See* also the case of *London Joint Stock Bank v. MacMillan & Arthur (1918).*

A collecting bank is similarly protected under S.2.

Parties to a Cheque:

There are usually three parties to a cheque, as follows:

The Drawer:

This is the account holder in a bank, who issues the cheque. He is the one giving authority to the banker to pay the person named on the face of the cheque or to bearer or to the order of that person. He is the one primarily liable for the payment, if the banker fails to pay the holder.

The Payee:

This is the person named on the face of the cheque. It also refers to the bearer where no payee is named on the cheque, e.g. when the drawer merely writes "cash." If the payee endorses the cheque at the back to another person, that person becomes the endorsee (i.e. the new payee). A typical endorsement is "please pay X" with the signature of the primary payee at the end. Mr. X can also endorse the cheque to Mr. Y in a similar way. This can continue indefinitely until an endorsee presents the cheque for payment.

The Drawee:

This is the banker who is authorised to pay the monetary sum stated on the cheque. He must obey the drawer's instructions and is under a duty to pay the payee or holder unless there is a problem. However, he can legally refuse to pay if he suspects fraud.

a. the cheque has been countermanded by the drawer i.e. the drawer had "stopped" the cheque.

b. the drawer has no sufficient funds (called "effects" in the banking parlance) to support the value on the cheque. In that event the banker will refer the cheque to the drawer, usually by writing DAR (drawer's attention required).

c. the cheque is "stale." In banking custom, a cheque is stale if presented after 6 months from the date on it.

Collecting Bank

A cheque may be paid in a different bank other than the bank on which it is drawn (called the drawee bank). The payee or his endorsee may have account in that different bank. That bank will collect the value on the cheque from the drawee bank in a process called "clearing". The payee's bank (where the cheque is lodged for collection) in that case becomes the collecting bank. A collecting bank as a rule collects into a bank account and not for cash. This is because the law places upon that bank the onerous responsibility of ensuring that the money is collected for and paid only to the person entitled to be paid. The practice whereby the collecting bank must pay into an account and not to pay cash to the presenter of the cheque, reduces fraud and therefore, the liability of the collecting bank.

The Use of Cheques

In the developed countries, credit cards and the direct debit system is threatening the use of cheques. The account owner simply issues a letter or memo, usually through the internet, to the bank to authorise direct debits, or the issuance of credit cards or another bank facility. However, even there, the use of cheques is still important. There are ample legal provisions to safeguard parties to commercial transactions, who are given cheques to settle obligations such as the price of goods and services provided by them. One such provision is the Dishonoured (Offences) Act, 2004.

Dishonoured (Bounced) Cheques

The Dishonoured Cheques (Offences) Decree 1977 (now The Dishonoured Cheques (Offences) Act, 2004) provides that "any person who obtains or induces the delivery of anything capable of being stolen either to himself or to any other person by means of a cheque, that when presented for payment not later than three months after the date of the cheque, is dishonoured on the grounds that no funds or insufficient funds were standing to the credit of the drawer, shall be guilty of an offence punishable by an imprisonment for a term of two years without the option of a fine and if a company, a fine of not less than ₦5,000.

This Act is currently under review by the National Assembly to make its provisions stiffer and for special courts to be established to try such cases. The most likely effect of this will be that:

(a) people will respect cheques, which will enhance civilisation.
(b) use of cheques will move the nation towards the use of more sophisticated devices such as debit cards, credit cards and direct debit system.
(c) respect for cheques will lead to less cash holding and carrying.
(d) use of cheques will reduce corruption.
(e) use of cheques will reduce tax evasion.
(f) it is hoped that less of cash holding will reduce robbery cases.

Promissory Notes

Promissory Notes are simply notes that acknowledge debt coupled with an unconditional promise to pay the debt, which is certain in money, to a named person. This is the definition in *William v. Rider (1962).* The date of maturity of the promise is not a requirement of a valid promissory note but the date on which it is written is. This is because the debt acknowledged will be statute barred if after 5 years, the creditor has not recovered the debt or secured another Promissory Note. The Statute of Frauds stipulated a period of 6 years, but most States in Nigeria have limitation laws lowering this to 5 years. Therefore, if a creditor sleeps over his rights for 5 years, he can as well forget the debt. He is said to have been caught up by laches.

A Promissory Note looks like this:

<u>Promissory Note</u>
I promise to pay Bayo Usama or order, ₦5, 000.00
Kunle Okonkwo, Date …………………………

Or this:

Promissory Note
I acknowledge myself to be indebted to Abubakar Abiola in the sum of ₦1, 000.00k to be paid on demand for value received.
Audu Umana, Date……………………….

Qualities of a Promissory Note

1. The promise to pay must be unconditional.
2. The consideration for payment must be a sum certain in money, or ascertainable in money terms.
3. The payee must be certain.
4. The date of execution must be on the face of the Note. This is important because of the provisions of the Statute of Limitation that bars the payment of debts older than 5 years unless the debt is acknowledged in writing dated less than 5 years.

Travelers' Cheques

Travelers' cheques are like conventional bank drafts but drawn on foreign banks and payable on demand to holders. If a foreign bank pays on stolen traveler's cheques in good faith, and in the ordinary course of business, the drawer (the bank who issued them) is bound to accept its liability under the cheques. The best-known traveler's cheques are Thomas Cooke and VISA. Travelers' cheques are the most convenient form of carrying money from one country to another for travel expenditure, apart from credit cards. Hotels accept them as money and so do most airlines, airports, especially international airport duty free-shops, and other appointed shops and supermarkets.

Benefits of Travelers' Cheques include the following:

(1) They obviate the holding of cash and therefore, no need for buying foreign currencies, which may turn out to be fake.

(2) If they are lost or stolen and the holder discovers the loss early, they can be cancelled if the financial system is notified immediately.
(3) They are light and easier to carry than currencies, especially the high denominations.
(4) Their use is neater and suggests gentleman-like conduct, compared to the rather crude perception which raw cash engenders.

Drawbacks of Travelers' Cheque

The main drawback is the strong possibility of theft (especially in hotel rooms) and the attendant possibility of their being cashed or used by the thief before the theft is discovered and reported.

3.10 Review Questions

1. Examine the different roles of the CBN, NDIC, and the EFCC in the economic development of Nigeria.
2. "Banks have become critical and key aid to economic businesses in Nigeria". Expatiate.
3. Appraise the efficiency or otherwise of the bank payment system in Nigeria.
4. Assess the importance of THREE Banking statutes and THREE common law principles of banks in Nigeria.

MODULE 4

4.00 INSURANCE LAW

4.01 Learning Outcomes

On successful completion of this module, students should be able to:

i. Evaluate the Nature of Insurance business in Nigeria and analyse its basic principles;

ii. Examine Insurance premiums and associated terms.

4.02 Nature of Insurance Business

Insurance is essentially a law-based business. It is a very important industry within the financial system of any nation. Its existence ensures that a person's undertakings in either business or personal chattels are protected against the vagaries of life and that no one should be reduced by mishaps to begin again in life. To this end, a pool of funds is created by persons who take insurance policies so that anyone of them who suffers mishap is indemnified to the extent of what is lost. The first Insurance law in Nigeria was brought to us by the Englishmen when in 1945, the Third-Party Motor Insurance Act was promulgated. Today, the practice of insurance is governed by the Insurance Act, 2003. Contracts of insurance are aleatory. This means that it must be either some uncertainty whether the event will ever happen at all, or if the event is one which must happen at some time or another (such as death), there must be some uncertainty as to the time at which it will happen. We want to be sure or prepared against events of which we are uncertain. However, a person is only allowed to insure what concerns him, i.e. that he stands to suffer should the event happen. No busy-body can benefit from an insurance contract, because it is not a wagering contract.

4.03 Definition of Insurance

The definition of insurance is not precise, and it depends on the disciplinary leaning from which the industry is being looked upon. A sociologist would define insurance as a device by society aimed at providing financial compensation to the victims of the many social misfortunes that befall humanity. An economist may see insurance as wealth maximizing arrangement whereby losses that may diminish the creation of wealth are ameliorated by the provision of a cushion from a pool of funds acting as bail-out aimed at sustaining the ability of a firm or an individual to continue to contribute to wealth creation and sustenance. A finance analyst may see insurance as a hedging strategy to ensure that future survival and profitability is not snuffed by an intervening misfortune. Professor E.R.H. Ivamy in his book, "General Principles of Insurance Law" defines insurance as follows:

> *A contract of insurance in the widest sense of the term may be defined as a contract whereby one person called the insurer undertakes in return for the agreed consideration called the premium, to pay to another person called the assured, a sum of money, or its equivalent, on the happening of a specified event.*

From legal viewpoint, insurance is defined as a "contract whereby a person called the insurer or assurer, agrees in consideration of money paid to him, called the premium, by another person, called the insured or assured, to indemnify the latter against loss resulting to him on the happening of certain events." This is the Black's Law Dictionary definition.

In ***Prudential*** **Insurance** ***Company v. I.R.C. (1904)***, Channel J. gave the following judicial definition:

> *A contract of insurance can be described as a contract whereby the party called the "insurer" promises in return for a money consideration called the "premium" to pay to the other party called the "insured" or the "assured" a sum of money or to provide him with some corresponding benefit, upon the occurrence of one or more specified events.*

From the above latter definition, the following must be noted in relation to the nature of contracts of insurance:

1. Insurance is a contract. Therefore, the general principles of the law of contract are also applicable to contracts of insurance.
2. As stated in the introduction, contracts of insurance are aleatory. This means that the event insured against must involve some amount of uncertainty. There must be either some uncertainty whether the event will ever happen at all, or if the event is one which must happen at some time or another, there must be some uncertainty as to the time at which it will happen.
3. The proposer (the person applying to take out the insurance contract) must have insurable interest in the property or life to be insured. That is, he must stand to suffer a financial loss should the event insured against, happen. This is what differentiates the contract of insurance from a wagering contract. Note that a parent has no insurable interest in the life of a child, but a wife may have an insurable interest in the life of her husband. This is because it is the legal presumption that a husband provides his wife with financial upkeep and consortium.
4. Contracts of insurance are generally contracting of indemnity. All contracts of insurance, apart from life and personal accident insurance, are contracts of indemnity. Indemnity means the assured is to be placed in the same position (by the insurer) as he was before the happening of the event he insured against. This means that the insured cannot (or is not supposed to) recover more than the amount of the loss.

This also means that if the insured double-insures a property with two or more insurers and there is a damage or injury to be claimed, all the insurers will contribute to make good the loss. In ***American Surety Co. of NY v. Wrightson (1910),*** the court confirmed that the insured is not allowed to make a profit by claiming separately from all the insurers.

The general rule is that the measure of indemnity with respect of the loss of any property is not determined by its cost but by its value at the date of loss and at the place of the loss. If the value has increased during the currency of the policy, the assured is entitled to the indemnity at the rate of the increased value.

If the policy is unvalued and the property is damaged, the cost of repairs provides the basis of indemnity. Where it is valued, the measure of the indemnity will be the percentage of the loss in relation to the total value of the insurance cover. Where the policy is valued and there is total loss, the calculated value of the damage is paid after calculating the "average". We will see the definition of "average" at the end of this chapter under "Definition of Terms". If the subject matter of the insurance, e.g. a car, is not destroyed, the assured can claim for the value of the damage done to it. If the subject matter is destroyed and the insurers pay, they are entitled to whatever remains. This is the principle of "salvage".

4.04 Principles Forming Basis of Insurance

The basic principles underlying the business of insurance are: (1) utmost good faith, (2) insurable interest, (3) proximate cause, and (4) indemnity. We will discuss these in turn as follows:

Utmost Good Faith

A contract of insurance is a contract of utmost good faith (uberrima fidei). This means that each of the parties to the contract must display utmost good faith in his dealings with the other parties during the whole period of the transaction, particularly at the outset of the contract. It is with regards to declarations of fundamental and relevant information, or what in insurance is termed, disclosure of all relevant facts. In an ordinary commercial contract, the law allows each party to make the best bargain that he/she can, and if a party does not make any false or fraudulent statements, there is no need to draw the attention of the other party to anything which might influence his judgment against entering into the contract.

This is because the rule which applies in ordinary commercial contracts (as opposed to insurance contracts) is *caveat emptor* which means "let the buyer beware". In insurance contracts however, the knowledge as regard the nature of the risk, life or property proposed for insurance is usually exclusively possessed by one side. The proposer is familiar and knows all about his risk he brings for insurance.

On the other hand, the insurer knows nothing about the risk and has to rely entirely on the proposer to supply him with the necessary information which will enable him asses the risk. He may well refuse the risk as an “uninsurable risk”. He may accept the risk and decide to charge a higher premium if thinks that the risk is greater than normal. The law therefore requires the proposer to disclose all material facts. In the leading case of ***Rivaz v. Gerussi (1880)***, a material fact was defined as:

> *A fact which would affect the judgment of a prudent and rational underwriter in considering whether he would enter into a contact at all or enter into it at one rate or another.*

Throughout history, many people took insurance policies for less than proper motives for avoiding risk. A lot of people think that it would be smart to make money from insurance by defrauding the companies. Although it is possible that many people have profited this way, most cases that go to court and which the courts have decided in favour of the insurance companies are of this nature. One of such cases was ***Carter v. Boehm (1766),*** in which the principle of utmost good faith was expounded upon in the following words of the learned judge:

> *……The special facts upon which the contingent chance is to be computed lie most commonly in the knowledge of the insured only; the underwriter trusts to his representations, and proceeds upon confidence that he does not keep back any circumstance in his knowledge to mislead the underwriter into a belief that the circumstance does not exist. The keeping back of such a circumstance is a fraud, and therefore the policy is void. Although the suppression should happen through mistake, without any fraudulent intention, yet still the underwriter is deceived, and the policy is void; because the risk run is different from the risk understood and intended to be run at the time of the agreement. Good faith forbids either party,*

by concealing what he privately knows, to draw the other into a bargain from his ignorance of that fact and his believing the contrary.

However, the duty to disclose imposed by the law is confined to facts known to the party on whom the duty falls.

Material Fact (Material Hazard). This is a fact that must be disclosed by the proposer to an insurance contract. What is a material fact in the words of Mackinnon LJ, in the case of ***Zurich General Accident and Liability Insurance Co Ltd v. Morrison,*** *"…*? that which would influence the mind of a prudent insurer in deciding whether to accept the risk or fix the premium and if this be proved, it is not necessary to further prove that the mind of the insurer was affected". Examples of material facts which must be disclosed at the time of taking out the policy include:

a. All facts suggesting that the subject matter of insurance is exposed to more than ordinary danger from the peril insured against, by reason of condition, nature, use, surrounding and other circumstances.
b. All facts suggesting that the proposed assured was actuated by some special motive, e.g. over-valuation, making the risk speculative.
c. All facts suggesting that the liability of the insurer might be greater than would be normally expected. e.g. second-hand machinery insured on reinstatement/replacement basis.
d. All facts that will reduce moral hazards.

Moral Hazards. Moral hazard is an insurance term that deals with the risk associated history of the proposer. The proposer must disclose any historical event, whether favourable or unfavourable, that bears or has any relationship with the type of risk being proposed for insurance. Moral hazard was described in *Locker Woolf Ltd v. Western Australian Assurance Co. Ltd. (1936),* thus:

It is elementary that one of the matters to be considered by the insurer in entering into contractual relationship with a proposed assured is the question of the moral integrity of the proposer – what has been called the moral hazard.

Examples of disclosures which bear on the moral integrity of the proposer and which can reduce the moral hazard are:

1. That the insured suffered loss in the past from the same peril.
2. Facts or circumstances which from previous experience of the assured are relevant to the subject matter, e.g. fire in an adjoining building which had been put out recently.
3. In motor insurance contracts, the fact of a previous conviction of the assured in respect of motoring offences.
4. In an "all risk policy" on jewellery, the fact that the husband of the insured was convicted of receiving stolen goods and for theft.
5. All facts within the knowledge of the proposed insured regarding the subject matter are material.

It must be noted that what are required to be disclosed are facts, not opinions and the facts must be only those within the specific knowledge of the insured. In ***Akpata v. African Alliance Insurance Co Ltd (1967)**),* the wife of the deceased insured, sued the insurance company who had refused to pay the claim on the life policy taken out by her late husband. The insurance company argued that the deceased who died ten months after taking out the policy, withheld a material fact, to wit: that he suffered from stomach disease and that he was in fact, suffering from that ailment at the time he took out the policy.

In short, the insurance company's position was that he should have disclosed this and that, that failure amounted to misrepresentation which ought to vitiate the contract. Indeed, the deceased suffered stomach pains but did not know what it was nor, could the doctor detect any particular disease. The court held that the claim must succeed because the deceased did not hide any known stomach disease of which he was aware.

Insurable Interest

Every person who takes out an insurance policy must have an insurable interest in the subject matter of the insurance. The insured must stand to lose personally if the peril insured against should happen to the subject matter.

If the insured has no insurable interest in the subject matter, the insurance contract is invalid. This is what distinguishes a genuine insurance transaction from a gambling or wagering transaction. An insurable interest is therefore, the benefit or interest (usually financial) of the insured in the event or thing insured.

In ***Lucena v. Crafurd (1906***), the court was presented with the need to define insurable interest, in order to determine whether the insured was entitled to claim under the policy which was the subject of dispute. The court defined insurable interest in the following manner:

> *A man is interested in a thing to whom advantage may arise or prejudice happen from the circumstances which may attend it. Interest does not necessarily imply a right to the whole or a part of a thing, nor necessarily and exclusively that which may be the subject of privation, but having some relation to, or concern in the subject of the insurance, which relation or concern by the happening of the perils insured against may be so affected as to produce a damage, detriment, or prejudice to the person insuring; and where a man is so circumstanced with respect to matters exposed to certain risks or dangers, as to have a moral certainty of advantage or benefit, but for those risks or dangers, he may be said to be interested in the safety of the thing.*

The court held further that:

> *To be interested in the preservation of a thing, is to be so circumstanced with respect to it as to have benefit from its existence, prejudiced from its destruction. The property of a thing and the interest devisable from it may be very different; of the first, the price is generally the measure, but*

by interest in a thing, every benefit or advantage arising out of or depending on such thing may be considered as being comprehended.

In ***Macaura v. Northern Assurance Co***. *(1925)*, it was held that a man who had incorporated a company, in which he held virtually all the shares and transferred his lumbering and sawmill trade to the company, had no longer any insurable interest in the business which was the subject matter of the insurance contract. The fact that he owned virtually all the shares in the company and that the few other shares were owned by members of his nuclear family, did not change the position of the law – insurable interest must be direct and personal.

However, it must be noted that a person has insurable interest in the circumstances that can be said to be exceptions:

a. A person has an insurable interest in the life of the spouse.

b. A trustee of a property as the legal 'owner' of the property has insurable interest in the property.

c. A beneficiary of a trust property similarly has insurable interest in the trust property.

d. A creditor has insurable interest in the debtor.

e. A mortgagee has insurable interest in the mortgaged property. The mortgagor also has insurable interest in the mortgaged property because of the reversionary interest he has in it.

f. Both the bailor and bailee of a bailed property have insurable interest in the bailed property.

g. Insurance companies have insurable interests in relation to the properties and other contingencies insured with them. They are therefore entitled to effect reinsurances to protect themselves against heavy losses resulting from claims in respect of perils suffered by those holding their policies.

Proximate Cause

Every event that occurs is the result of some cause. The event must have been preceded by something which happened. Therefore, where there is a loss or damage, that loss or damage must have been brought about by the operation of some peril or perils. Since it is not all perils that are insured, it is always necessary to ascertain the actual peril that caused the loss. The reason is that if a loss is occasioned by an uninsured peril, there no basis for a claim, as the event would be outside the insurance contract covered by the policy. When a peril happens, the insurer checks for the presence of ***novus actus interveniens*** (or any intervening circumstance or event that directly caused or catalyzed the happening of the event), which could be the intervening act or event which was the proximate cause of the injury complained about. If the proximate cause is not the insured peril, then the insurer is not liable.

For example, if a person is wounded during a fight from which ordinarily a person would have recovered, and he dies because the hospital refused to attend to him, the hospital's omission caused the death. See **Smith v. Leech Brain (1961)**, where burns sustained by a worker activated a malignant cancer. In that case, it was held that the malignant cancer was not the proximate cause of death and therefore the burns were actionable. But in Bannett v. Chelsea & Kinsington Hospital Management Committee (1969), it was held that the negligent omission of doctors on call could not have been the cause of death because the deceased would have died anyway from lethal dose of rat poison he ingested.

A classical definition of proximate cause was given in the leading case of ***Pawsey v. Scottish Union & National Insurance Company (1908)*** as follows:

> *Proximate cause means the active efficient cause that sets in motion a train of events which brings about a result, without the intervention of any force started or working actively from a new or independent source.*

Lord Summer has stated in ***Becker Gray & Company v. London Assurance Corporation (1918)*** that:

> *…. cause and effect are the same for the underwriters as for other people. Proximate cause is not a device to avoid the trouble of discovering the real cause or the 'common-sense cause', and though it has been and always should be rigorously applied in insurance cases, it helps the one side no oftener than it helps the other. I believe it to be nothing more nor less than the real meaning of the parties to a contract of insurance...*

In ***Leyland Shipping Co. v. Norwich Union Fire Insurance Society (1917)*****,** it was held that proximate cause is not based on time lapse but on proximate efficiency so that a blow to the head a year ago could result in a mental illness as a proximate cause this year, notwithstanding that the victim is known to take mild alcohol.

Types of Peril

Perils are the contingencies or the undesired events that happen to people and their undertakings. The risk of the happening of these contingencies and events is what insurance contracts are entered into to cover. There are basically three types of perils recognised by the insurance industry. They are: (a) the insured perils; (b) the excepted perils, and (c) the uninsured perils. The insured perils are those perils which are specifically covered in the contract, for example, death arising from an automobile accident is covered as an insured peril in a personal accident policy.

The excepted perils are those perils which are specifically excluded from the insurance contract and they are always listed out in the policy. A peril may be excluded from the cover granted either because that peril is not insurable in which case the insurer would never accept it or because it would require an additional premium to obtain the cover. In the latter case, if the policy-holder requires the extra cover, he would have to pay the appropriate additional premium and the peril will be deleted from the policy exceptions.

The uninsured perils are those which are not specifically mentioned in the policy, but which are obviously outside the scope of the cover granted. For example, fire is an uninsured peril in a burglary policy because damage caused by fire is logically outside the scope of cover in the burglary policy. But consider the case of fire insurance policy in which it is stated that the policy covers fire, combustion, conflagration and burning. If a heater causes a non-combustible substance to melt and cause smoke which in turn contaminate products or work-in-progress in a factory, it would not be covered because of the absence of fire or combustion. In insurance law, there can be smoke without fire!

Indemnity

When an insurance policy is said to be a contract of indemnity it means that in the event of a claim, the amount to be recovered is determined by the extent of the value of policyholder's actual pecuniary loss. It is an essential rule of insurance that all insurance policies, except those of life and personal accident, are contracts of indemnity. Today in Nigeria, all types of accident insurance are contracts of indemnity except personal accident policy which covers only injuries and death. In the event of a loss, the insured should be placed in exactly the same position that he occupied immediately before the loss as far as money can achieve. The insured is not allowed to recover more than his actual financial loss. If he chooses to insure the same asset with more than one insurance company and there is a loss, all the insurance companies contribute and not pay separately the full value of each insurance contract.

Agreed Value Basis

However, the principle of indemnity can be modified in certain circumstances, e.g. in the fleet vehicle policies of large corporations, vehicles can be insured on **Agreed Value** basis. This means that average and market value of the insured property do not apply.

4.05 Premiums

A premium is the cost of purchasing insurance cover, i.e. the consideration for the insurance contract, paid by the insured to the insurer in return for the promise of the insurer that he would reinstate or indemnify the insured whenever the stated event happens. The Insurance Act 2003 provides that if the insured fails to pay the premium as and when due, then there is no cover and if loss occurs; the insurance company is not liable. The favourite term used by the insurance companies is 'No premium no cover'. However, S.50 of the Act provides that if premium is paid to a broker, then it is deemed to have been received by the insurance company and S.41 stipulates that the broker has up to 30 days to pay over such premium to the insurer or face liability to the insurance company and face sanction from the National Insurance Commission. In this respect, a broker may be authorized by the insurer to issue a cover note to the insured along with the receipt of payment of premium to indicate cover.

4.06 Payment of Claims

S.7 of The Insurance Act provides that claims must be paid 90 days after acceptance of liability. If the insurance company fails to pay within this period, the insured can claim the payment from the Insurance Commission who will in turn, obtain payment plus a fine of ₦0.5m from the insurance company concerned. The weak point here is that the Section comes into operation after the claim has been accepted as a liability.

Insurance companies can avoid this by delaying acceptance of liability without risking lawsuit, e.g. by requiring the insured to meet certain frivolous conditions or demanding for a series of frivolous documents one at a time, ostensibly to enable it to decide whether to accept liability or not while the real reason may be to delay or frustrate a claim.

4.07 Classes of Insurance

S.2 of the Insurance Act 2003 lists two main classes of Insurance Contracts:

1. Life, and
2. General Insurance Business.

Under the Life Insurance Business, we have three categories:

1. Individual life insurance
2. Group life insurance
3. Health insurance business.

Under the General Insurance Business, we have 8 categories, thus:

1. Fire
2. General accident
3. Motor vehicle
4. Marine and aviation
5. Oil and gas
6. Engineering
7. Bonds credit guarantee and suretyship
8. Miscellaneous insurance business. This includes such diverse covers as property insurance, agricultural insurance, and terrorism insurance.

Compulsory Insurance

The following insurance covers are among the compulsory insurance decreed by the Federal Government of Nigeria:

1. **Workmen Compensation Act (WCA)** which provides that employers of labour in the private sector must insure their employees against industrial injuries or death. The values to be paid on each type of injury or death are stated in the Act. It must be noted that WC insurance does not cover senior employees.
2. **Builders' Liability Insurance.** This covers building engineers against such things as collapsed buildings, where they may be sued for damages and death of workers.
3. **Occupiers' Liability (Public Building) Insurance.** Those who rent out commercial buildings must insure such them against fire, collapse, etc.

4. **Third Party Motor Insurance Act 1945.** This Act makes it compulsory for any person operating a motor vehicle on Nigerian roads to take out an insurance policy at least on third party basis, so that if he causes an accident in which an innocent road user is injured in person or in goods, the insurance company will indemnify the unfortunate but innocent road user. Under S.68 of the Act, the amount covered is now a minimum of ₦1 million for property damage and no limit for personal injury or death. See the unreported case of ***Pump Services (Nig) Ltd & Anor v. A.R.A. Onisiwo & Anor, Suite No. MIK.357/63*** Lagos High Court, where a motorist killed an employee who was fixing 'cat eyes' on Ikorodu Road, Lagos. The logic behind Third Party Insurance scheme is that the motorist that causes an accident may not have money to pay compensation.

5. **Bank Depositors' Insurance.** This is a peculiar compulsory insurance cover. Banking companies are to insure their depositors' deposits with the Nigerian Deposit Insurance Corporation. The premiums are paid by the banking companies and not the depositors, but the depositors are the beneficiaries. Additionally, the cover is a maximum of ₦100,000; therefore, a depositor whose bank account is larger than ₦100,000 can only receive a claim of ₦100,000 from the NDIC if the banking company should fail.

4.08 Definition of Some Insurance Terms

Average: When a policy is made subject to average, and the insured under-insures, he becomes his own insurer for the difference between the sum insured and the full value of the property at the time of the loss. For example, if a car worth ₦1m is insured for ₦0.5m, and it is subsequently involved in an accident and ₦100,000 is required to repair it, the insurance company will pay only half of ₦100,000, because as the car is insured for half its value, the insurance company can only bear half the risk and therefore, by extension, half the repair cost. Average is based on the believe that under-insurance is unfair to the insurer in as much as he does not receive the correct premium for the risk and should not be made to pay for risk he did not assume.

Broker: An insurance broker is an expert who acts between the insurer and the insured. He seeks business for the insurer, and *advises the insured* as to many technical matters, such as capacity and reputation of insurance companies, important warranties and how best to comply with them, rates of premium, etc. The broker, though an agent of the insured, is paid by the insurer (takes a percentage of the premium paid by the insured). Dealing through a broker is encouraged because it does not cost the proposer anything.

Contribution: Where an insured decides to insure the same asset with many insurers, and there is a claim, each insurer will contribute a quota towards the total claim sum. Also, where the insurance contract is based on co-insurance, the claim will be met by contribution from the various insurance companies based on their percentage holding of the risk. For contribution to apply, the following conditions must be met:

a. There must be two or more policies in force at the material time;
b. Each of these policies must insure the same subject matter and the same interest of the same insured;
c. The policies must cover the same peril that caused the loss; and
d. All the insurances concerned must be contracts of indemnity. The court made this age-old statement of truism in the case of ***North British & Mercantile Insurance Company v. Liverpool, London & Globe Insurance Company (1877).***

Co-insurance: Many heavy insurance contracts are entered based on co-insurance whereby the leading insurance company or the broker, offers the risk(s) to various insurance companies to take a share of the risk(s). An insurance company may decide to take 15% in which case it will receive 15% of the premium and in the case of a loss, will contribute 15% of the claim amount.

Insurer: The insurer is the party who agrees in return for a premium, to pay money to another party known as the insured, or assured, on the happening of a stated event. As a rule, there are usually two parties to an insurance contract – the insurer and the insured.

Loss Adjuster: A Loss Adjuster is an insurance expert employed by the insurer. He verifies claims by visiting the site of damage/injury to inspect the damage and recommend to the insurer as to the value of the property at the time of damage, compliance with warranties, and breach of any condition, etc.

Policy: The insurance policy is the document which evidences the terms, warranties, and extensions of the insurance contract between the parties. In short, it is the contract document.

Policy Excess: Policy excess is the amount of claim above which the insurance company will pay in a claim. The insured is to bear this part of the claim. The insurance contract, especially motor vehicle insurance policies, usually contains a Policy Excess Clause. For example, the clause may state that if there is a claim, the insured shall bear the first ₦10,000 or 10% of the claim amount. This means that if there is an accident and the repair cost is ₦50,000 whichever is higher, the insurance company will pay ₦40,000 and the insured is to pay ₦10,000 towards the repairs. The purpose is to discourage small or frivolous claims.

Proposer: When a person approaches an insurer (insurance company) for an insurance cover or when an insurance agent is discussing or negotiating with a prospective insured, the prospective insured or the person who needs the insurance cover is called the proposer. The initial forms filled by the proposer are called the Proposal Form and it contains the offer from the prospective insured or the proposer. When the premium is paid and accepted by the insurance company, the insurance company is said to have accepted the contract or the risk, and the proposer becomes the insured.

Re-insurance: Insurance companies also insure their exposure of risks with re-insurance companies. All insurance companies in Nigeria re-insure with the Nigerian Re, who in turn re-insures with West African Re, who in turn re-insures with Lloyds of London, the largest re-insurance company in the world. The original insurance company that deals with the insured is called the 'direct insurer' or the 'ceding company'.

Re-insurance follows the fundamental purpose of insurance – the spreading of risks. The re-insurer takes part of the risks for part of the premium.

Superintendence: In marine insurance contracts, the policy is subject to superintendence. This means that an insurance expert, called the superintendent acting somewhat like a loss adjuster but up-front, checks the goods either at the port of shipment or at the port of discharge and advises the insurer as to actual state of the goods which may affect the premium. The superintendent acts before a claim, in case of a claim.

Subrogation: This means that once the insurer has indemnified the insured, he is placed in the legal position of the insured with respect to the subject matter of insurance. The insurer is said to have been subrogated to the rights of the insured. The insurance contract must be that of an

indemnity for subrogation to apply. Therefore, if the loss is caused by a third party, the insurer can claim from the third party to reduce his own outlay. See ***Yorkshire Insurance Co. Ltd v. Nisbet Shipping Co Ltd.***

Tariff and Non-Tariff Premiums: Certain types of assets attract tariff premium, meaning that the premium to be paid is set by the industry at a percentage of the value of the asset. This forecloses negotiation of the premium by both parties. An example of tariff premium insurance is the third-party motor vehicle insurance where the Nigerian Insurance Association stipulates ₦5000 flat. All insurance companies in Nigeria charge the same premiums for tariff risks.

Third Party: There are two parties to an insurance contract – the insurer and the insured. All others are strangers to the contract and are referred to as third parties because they are not parties to the insurance contract. For instance, the pedestrian who is knocked down by the insured in a motor accident is a third party.

Under the Common Law provisions, a third party cannot claim under the policy, but the Insurance Act 2003 provides (at S. 69(1)(b)) that a third party can claim from the insurance company if the third party notifies the insurance company 7 days after commencement of legal proceedings against the insured. Additionally, where the insured becomes insolvent, a third party creditor can be subrogated to the debtor's position so that the creditor can obtain the proceeds of a judgment against the insurance company.

Warranties: Warranties are clauses which insurers insert in policy documents by which the right of the assured to recover is made subject to the existence and maintenance of a given fact or state of things defined in the clause. So, held the Court in *Dawsons v. Bonini Ltd (1922) KC 41.* For example, in a fire policy, the insured may be required to maintain a hydrant with a functioning hose; in a motor policy, an insured may be required to park the car in a lock-up garage, after having fixed a pedal lock.

4.09 Review Questions

1. "Insurance business is not popular among Nigerian business men". Examine the impediments and the process to strengthening Insurance business in Nigeria;
2. Identify the parties to Insurance contract and carefully deconstruct their role in making Insurance business effective;
3. Carefully elucidate on the following: (a) Insurable Interest; (b) Proximate Cause; (c) Utmost Good Faith; (d) Indemnity.
4. Distinguish among Insurance, Gambling and Wagering?

MODULE 5

5.00 BANKRUPTCY LAW

5.01 Learning Outcomes

On successful completion of this module, students should be able to:

i. Evaluate the Nature of Bankruptcy Law in Nigeria and analyse its basic principles;

ii. Examine the issues associated with bankruptcy in Nigeria.

The law of bankruptcy has a British origin. The first was the Bankruptcy Act 1883. This was followed by other Acts in 1890 and in 1914, each repealing the previous, culminating in the Bankruptcy (Amendment) Act, 1926. In Nigeria, the main enactment governing bankruptcy is the Bankruptcy Act, CAP B3, Laws of the Federation of Nigeria (LFN 2004). The aim of the Bankruptcy Law is to extricate a person who has become hopelessly but not fraudulently involved in financial difficulty. In such a hopeless situation, his estate is distributed equitably among his creditors on pro-rata basis and thereafter, he is released from further obligations in respect of the past debts, so that he can start life again. The law is then used to cleanse him up so that he can start life all over again. In other words, once a bankrupt is discharged, he is "born again" commercially and socially. The provisions are not meant to help the debtor to cover up crimes, fraud or sharp practices or to enrich him. It is just to rehabilitate him so that he can reconstruct himself financially.

5.02 Acts of Bankruptcy

The Act provides in S.1 that a person (i.e. a debtor) commits an act of bankruptcy if he offends any of the provisions of that Section, i.e.:

a. a creditor has obtained a final judgment or a final court order against the debtor for any amount and the execution thereon has not been stayed and has a bankruptcy notice served on him and does not, within 14 days after such service of the bankruptcy notice, satisfy the requirements of the notice nor satisfy the court that he has a counter-claim, set-off or cross demand which is equal to or is higher in value than the judgment debt.

b. In an execution of a judgment debt, his goods have been seized for 21 days and he has not paid the debt to claim it. The goods can be recovered if the debtor pays the debt. Note that if the bailiff has sold the goods in the meantime, the goods can be recovered from the purchaser.

c. The debtor himself files in the court, a declaration that he cannot pay his debts. The debtor can also file a bankruptcy petition against himself. In doing so, he avoids many lengthy litigations from various creditors.

The kernel of these three acts of bankruptcy is that the debtor is unable to pay his debts, on the condition that:

a. The inability to pay debts must be genuine and not fraudulent.

b. The debts must not also be ones incurred fraudulently.

If any of the above is the case, the debtor commits an offence punishable under S.27 of the Act and will most certainly be sent to prison.

5.03 Conditions for Presenting Bankruptcy Petition by a Creditor or Creditors

S.4 of the Bankruptcy Act provides that when a debtor has committed an act of bankruptcy, a creditor or a group of creditors may present a petition to court, praying the court to issue a Receiving Order (RO) against the debtor. Such an order, when issued, transforms the debtor (with full personal constitutional rights) into a potential bankrupt (whose rights are greatly curtailed).

S.4 lists the conditions for a valid petition as follows:

1. The debt must be at least ₦2,000. A lesser sum cannot be a condition for a petition for bankruptcy. It will amount to a *de minimis* action which the court will interpret as frivolous.
2. The debt must have become due and has been demanded but unpaid for more than three weeks. There must be evidence that a proper demand has been made for a validly due debt. The debtor must have received the demand (best done in writing and acknowledged

either by the debtor himself or the transporter (post office, courier, etc.) who must have obtained a delivery receipt of some kind).

3. It cannot be a claim subject to negotiation or arbitration.
4. The petition must be presented within 3 months of the last act of bankruptcy. In the case of a demand, the petition must be within three months calculated from the date the receipt of the demand by the debtor reached three weeks.
5. The debtor is domiciled in Nigeria, which means -
   a. The debtor is ordinarily resident in Nigeria (whether he is a Nigerian or not), or
   b. within a year before the petition, was resident in Nigeria, or
   c. has a dwelling house or place of business in Nigeria, or
   d. has carried on business in Nigeria personally or via an agent or manager, or
   e. has been a partner with a person having business in Nigeria.

5.04 Partners

Partners in a firm can be declared bankrupt. This may be due to the act of one partner who has dragged other partners into the financial mud.

The applicability of the law on bankruptcy to partnerships is as follows -

a. Any partner can commit an act of bankruptcy with reference to the partnership business and bind other partners in bankruptcy.
b. The name of the firm can be used in the petition to bind all partners.
c. The petition will succeed even if any or all the partners are not citizens of Nigeria and or are not resident in Nigeria.

5.05 Receiving Order

When a debtor commits an act of bankruptcy and a petition is validly filed in the court, the court will make a Receiving Order and then appoint an Official Receiver (usually the court registrar). The Receiving Order empowers the Official Receiver to take over the estate (all the assets) of the debtor, primarily to protect it from abuse by the debtor, such as paying preferred creditors.

Once the Receiving Order (RO) is made, the debtor is required by law to cooperate with the Official Receiver and the trustee (if any). To this end, he is required under S.16 (1):

a. to swear to a verifying affidavit, and
b. prepares a Statement of Affairs, listing all his assets and liabilities and
c. submitting same to the Official Receiver (and where applicable) also to the trustee. The affidavit will support his Statement of Affairs.

5.06 Proof of Debts

At the first meeting of the creditors, each creditor shall present his/her proof of debt. The proof of debt is the evidence that the creditor is entitled to his claim that the debtor is owing him the stated amount. It is a statement accompanied by evidence of transaction; the fact that the stated amount is outstanding.

5.07 Compromise, Composition or Scheme of Arrangement

After the RO is made, the first meeting of the creditors is called. The Statement of Affairs is tendered and discussed at the meeting. This gives the debtor the opportunity to make representations in the form of compromise, composition or scheme of arrangement.

a. At the first meeting of the creditors, the debtor may propose and present a scheme for payment of his debts if he has a strong belief that substantial amount of money can be realized from such forced sale as opposed to public auction. The reason for such an effort is to avoid an embarrassing public hearing. This is variously called a Compromise, Composition or Scheme of Arrangement.

b. The Compromise, Composition or Scheme of Arrangement has dual advantage. It obviates the public hearing which may be embarrassing to the debtor. It may also prove advantageous to the creditors who may get more fraction of their claims from the unfortunate situation if the debtor sells his property himself than they can get if the properties are sold by public auction.

c. In it, the debtor states that he can substantially pay his debts and that the creditors should agree to this and allow him to sell his properties himself instead of a public auction following an Adjudication Order. At auctions, the properties would be sold to the highest bidder which may be quite lower than what the debtor could have got if he sold the properties himself.

The creditors have the liberty to accept or reject such a scheme. If the scheme is rejected, the next stage is public examination. The Scheme is normally embodied in a Deed and it assigns all assets of the debtor to the trustee or to the Official Receiver, for the benefit of the creditors.

5.08 Public Examination (Hearing)

After the RO is made, a public examination is conducted. S.17 of the Act provides that there shall be a public examination of the debtor in the course of the bankruptcy procedure. The hearing follows normal court hearing procedures. The hearing gives the bankrupt the opportunity of being heard. It is therefore mandatory for fair hearing purposes, even if the bankrupt wishes to avoid this public exposure. He can mitigate the effects, though, through a compromise, composition or a scheme of arrangement. Public hearing can be made quite simple and short if the debtor has made a successful (acceptable) offer for Debtors' Composition or a Scheme of Arrangement. These are schemes showing details of how the debtor is to pay the debts. The purpose of this is to avoid the adverse publicity that goes with full-blown public examination of the debtor. Once the Scheme is approved, there will not be any full public examination. Any one creditor who disagrees to the Scheme frustrates it and a full public examination must be held. However, a creditor that agrees is bound and cannot later disagree.

5.09 Trustee in Bankruptcy

The creditor(s) may, in addition to the Official Receiver, apply to court, to appoint a trustee to sell off the debtor's property and to distribute the proceeds (usually on pro-rata basis) to the creditors. Such a trustee then reports to the Official Receiver on the progress he makes. He also reports to the creditors as a whole (usually at a creditors meeting) or where the creditors are many, to a Committee of Inspection, which is a small group of creditors who oversees the trustee on behalf of the totality of the creditors.

5.10 Adjudication Order (or Final Order)

After the hearing and the court is of the opinion that a good case has been made against the debtor, the Receiving Order is vacated, and an Adjudication Order is made in its place. It is a final order which turns the debtor into a BANKCRUPT. It enables the Official Receiver and or the trustee to sell off the properties of the Bankrupt to pay off his creditors, usually on a *pro rata* basis.

5.11 Committee of Inspection

Where the creditors are many, they may set up a committee from amongst themselves to interface with the official receiver or the trustees in bankruptcy. The committee, called the committee of inspection ensures the judicious disposition of the bankrupt's assets and equitable distribution of the proceeds to all the creditors in the correct order.

5.12 Payment to Creditors

The Official Receiver or the trustee uses the statement of Affairs to identify the assets which are then sold off by auction. Any onerous assets will be declared to the Court, as unsaleable and avoided. An onerous asset is an asset that is in fact, a liability, such as a villa in the bankrupt's village. In paying the creditors, the following priority debts must be paid first in the order listed:

1. All debts due to the State (i.e. to any government) 6 months to the date of the Receiving Order (the RO). This includes taxes outstanding, ground rents, etc.
2. Wages, salaries and commissions due to employees 4 months to the date of the RO. These debts must be liquidated sums of money. That means that it must not be sums subject to negotiation or arbitration.

3. Any charge on distrained goods held by a landlord or any other person. It includes rents outstanding.

After satisfying the above in that order, and there is still a remainder, it is subjected to a 1% interest charge and paid to other non-priority creditors. In the unlikely event that there is still any further remainder (called financial surplus), it goes to the bankrupt's escrow account pending his discharge.

5.13 Maintenance

While the sale of the estate of the bankrupt is going on, the bankrupt may be paid a maintenance allowance. S.60 allows this but stipulates that it can be paid only if the creditors through the Committee of Inspection approve it. The purpose of the allowance is merely to keep the bankrupt alive (he is considered almost civilly dead during the pendency of the bankruptcy).

5.14 Disqualifications and Disabilities of a Bankrupt

Ss.26, 27 and 126 provide that until a bankrupt is discharged:

1. All mails and messages to him will be redirected to the Official Receiver for scrutiny.
2. The bankrupt is under continuous investigation (e.g. to see if he has hidden any assets). This extends to his spouse and any debtor of his.
3. He is disqualified from being elected into or holding any elected office or being appointed into boards of directors of any corporation.
4. He is disqualified from being appointed a Justice of the Peace (JP), or a trustee, and cannot practice any profession regulated by law.
5. He may be imprisoned as provide by S.27 if it is proved that:
   5.1 He over-traded knowingly, leading to the current insolvency.
   5.2 he omitted to keep proper books of account.
   5.3 his assets cannot pay up to 50% of his debts.
   5.4 he failed to account for any loss or deficiency of assets.

5.5 he has been a bankrupt previously.

5.6 he made unjustifiable expenditure to the detriment of his business.

5.7 he has been guilty of fraud or fraudulent breach of trust

5.8 he has frustrated a creditor's action in court by vexatious and frivolous defenses.

5.9 He made unjustifiable preferential payments in anticipation of bankruptcy proceedings.

5.15 Discharge Order

When all the assets have been disposed of and all the creditors have been paid their due *pro rata* from all the proceeds of the realization of the assets, then the bankrupt is ripe for discharge to start a new life. When the conditions for discharge are met, the court makes a Discharge Order. A bankrupt may be discharged by the court on an application by the bankrupt himself or on a similar application by the Official Receiver, stating *inter alia*, that there is nothing more to be gained by the creditors or any person else for that matter, by further keeping the bankrupt in his present legal state.

After the Discharge Order, the bankrupt becomes a normal person again.
A bankrupt will however, not be discharged –

a. If a State debt is unpaid. This may happen when all the proceeds of the sale of the bankrupt's property are not enough to pay state debts.

b. If his debts were incurred by fraud even if discharged generally as a bankrupt, he cannot obtain a discharge certificate until the court exercises its discretion that the bankrupt has either suffered enough or that as far as possible, the fraud has been addressed to the advantage of the creditors.

It must be noted that a discharge can be qualified, e.g. if it is suspected that the bankrupt had hidden some assets, but they cannot be discovered. This hangs the discharge for an indefinite period until the court exercises its discretion that it has taken enough time to discover hidden assets to no avail. A discharge is evidenced by the issuance of a Discharge Certificate by the

Court. Such a Certificate is conclusive against any prior debt (except state debt as sated above). The Certificate is a new legal birth certificate.

Vacation of Trustee

When the estate of the bankrupt has been sold and all possible proceeds have been realized and distributed to the creditors, the trustee will apply to court for his release from office. The application is in practice, accompanied by final Statement or Report of his activities. A Releasing Order is then issued by the court, which is conclusive, except for fraud, which may necessitate investigation of the trustee's activities even after his release.

5.16 Treatment of Trust Property of a Bankrupt

Whether a trust property is outside the class of properties of the bankrupt for purposes of receivership, depends on the type of trust. A property which is the subject of public trust cannot be sold by the official receiver but a property that is the subject of private trust can be sold by the official receiver. There are two main types of trust. A private and a public trust. A private trust is for the benefit of an individual or a group or class of individuals, e.g. one set up by a parent for the benefit of the children. A public trust is one created for the benefit of the public or at least a section of it as beneficiaries. This class of trust is also known as charitable trust. A private trust is usually not exempt from tax or from distribution as part of the estate of the settlor if he becomes bankrupt. Public trust on the other hand is tax exempt and also escapes distribution as part of the estate of a bankrupt settlor.

5.17 Definition of Bankruptcy Terminologies

1. **Bankrupt** – this is the former debtor in respect of who an Adjudication Order has been made by the court, after a hearing. The adjudication order causes the debtor to metamorphose into a bankrupt.
2. **Dividend** - this is the periodic distribution of payments to creditors as assets are realized by the trustee or the official receiver.

3. **Financial surplus** – this is the money paid to the bankrupt after all the creditors have been paid in full.
4. **Onerous property** – is a property that is difficult or impossible to sell or a property with encumbrances (charges or restrictive covenants). Trustees usually disclaim (refuse) to deal with such properties. Example is a large country house in the village of the debtor.
5. **Vacation of trustee** – when the trustee has concluded the assignment, he applies to court for his release. The application is usually accompanied with a final Statement of Affairs or Report. The Releasing Order made by the court is conclusive and no one will afterwards call the trustee for any explanation or action with regard to that particular bankruptcy or winding up activities except if it is discovered that he committed fraud in the course of that work.
6. **Executor** – is the person who is named in the will of a deceased testator, to distribute the property to the beneficiaries. He is like a liquidator of a company.
7. **Receiver** – this is the person appointed to manage the estate of an insolvent company or person. His primary objective is to get out the debt of the creditor from the asset. If he can do this without closing the company down or declaring the individual bankrupt, it is preferable to do so.
8. **Trustee** – is the person appointed by the creditors in bankruptcy or winding up, to act as receiver. A trustee can also be a person named in the will of the testate person, appointed to manage the asset for the benefit of the beneficiaries.
9. **Discharge** – when a bankrupt's properties have been fully dealt with, the bankrupt will apply to the court for a discharge order, to set him free. The order releases the bankrupt, that is, he ceases to be bankrupt. All former debts not satisfied expire (or abate) and he becomes "born-again".
10. **Official Receiver** – is the official (usually a court official) who oversees the bankruptcy or winding up process and reports to court. His duties are provided by s.74 of the Act, viz:
    (a) to investigate the conduct of the bankrupt and report to court to determine whether to discharge him, to refuse his discharge or to qualify the discharge;
    (b) to conduct public examination and

(c) to help to prosecute a fraudulent bankrupt.

It is also the duty of the Official Receiver to identify the assets and liabilities of the bankrupt. He supervises the sale of the assets of the bankrupt and the distribution of the proceeds to the creditors.

5.18 Review Question

1. "Bankruptcy is a subject on the borderline of Law and Economics". Discuss.
2. Examine the roles of the following in Bankruptcy proceedings:
   a. Receiving order
   b. Trustee in Bankruptcy
   c. Discharge order
   d. Adjudication Order
3. List and explain ten terminologies that facilitate your understanding of bankruptcy law.

MODULE 6

6.00 LAW OF AGENCY

Agency can be defined as a relationship between one person called Principal and another called the Agent whereby the Agent is vested with the authority to alter relationships of the Principal with third parties. An Agent is thus a person employed to act on behalf of another. The Oxford Advanced Learner's Dictionary defines Agency as an arrangement whereby an individual or Business or Organisation provides a service on behalf of another Individual, or Business or Organisation.

6.01 Learning Outcomes

On successful completion of this module, students should be able to:

i. Discuss the nature of Agency;
ii. Classify and analyse the different types of agents;
iii. Deconstruct the duties of the agent to his principal.

6.02 Nature and Consequences of Agency

The law which governs agency relationships in Nigeria is the received English Law, particularly the Common Law and equity. The received English Law were the laws existing in England in 1900AD which were merely adopted by Nigeria. The true nature of the law of agency is that, it applies only when acts of the Agent produces legal consequences. Thus, the law of agency does not apply to social or non-legal situations. For example, when a village Head sends a person to represent him at a village ceremony, the law of agency has no application to the relationship. Another nature of agency is that, where it subsists, it does so irrespective of what the parties concerned choose to call or label it. Consent of the parties is a vital nature and consequence of Law of agency. More recently, several writers have tended to focus attention on the consensual aspect of agency as a determining factor. This view has received Judicial attention in the ***Garmac Grain Co. Ins. V H.M.F. Faure and Fairclough Ltd (1967) I Lyds Rep 495.***

In that case, Lord Pearson said, "The relationship of Principal and Agent can only be established by the consent of Principal and the Agent". However, his Lordship went on to say that "they will be held to have consented if they have agreed to what amounts in law to such a relationship even if they do not recognise it themselves and even if they have professed to disclaim it". He further emphasized that "the consent must have been given by each of them either expressly or by necessary implication from their words and conduct". It should be noted however that under certain circumstances, the law imposes agency relationship upon parties irrespective of their consent. It would seem to be incontrovertible to state that the consequences of agency can arise by estoppel and necessity without the need to show consent between the Principal and his agent.

Consent need not be in writing but may arise by legal imposition deriving from equity, quasi-contract or even tort. In fact, there may be situations in which agency relationship may arise from unilateral act. Another nature and consequence of agency is the authority of the Agent. If the Agent acts were authorized, the consequences are that the Principal is bound by the acts to third parties. The Principal will be bound even if the Agent acted with his "actual" (or real) authority or his "apparent" (or ostensible") authority. The "actual" or "real" authority refers to authority of the Agent to do what the Principal has agreed that the Agent should do. It includes the powers to carry out whatever the Principal has expressly or impliedly engaged the Agent to accomplish. A good example of express authority is the POWER OF ATTORNEY. Implied authority may be conferred by custom or usage of community, trade, business or profession where the Agent operates or by conduct of the Principal. In the case of ***Freeman and Lockyer V Burkhurst Park Properties Ltd; (1964) I ALL ER*** 630 at P 644. Diplock L.J. described the actual or real authority as a legal relationship between Principal and Agent created by a consensual agreement to which they alone are parties. He further stated that such authority may be express when given by express words or implied when it is inferred from the conduct of the parties. The "apparent" or "ostensible" authority refers to authority which in fact does not but merely appears to exist.

Thus, the basic difference between actual authority and apparent authority is that in the former the expression of authority is made directly to the Agent whereas in the latter, the expression is made to third party by the Principal making the third party believe that the Agent he deals with has authority. In summary, once the Agent has brought his Principal into contractual relations with another, he drops out, and his Principal can sue or be sued.

6.03 Types of Agent

Due to development in commercial activities and need for specialization, Agents have been broadly classified into various types namely: - General Agents, Special Agent, Commission Agents, Mercantile Agents and Del Credere Agents.

1. **General Agent**

   A general Agent is one who is authorized to act for and on behalf of his Principal in all his affairs in connection with a particular kind of business, trade or profession or to represent him in the ordinary course of his own trade, business or profession as an Agent. For example, a Director of a Limited Property Company is a general Agent of the company for the purpose of the company business. Similarly, a Solicitor, Factor, Broker, or Auctioneer who is employed to perform in the ordinary course of his business is a general agent of his employer in relation to that employment.

2. **Special Agent**

   A special Agent is one who is authorized to act for his Principal for some special occasion or purpose or to handle a particular transaction or to do a specific act which is not within the ordinary course of his business or trade or profession. For example, a Dealer in goods taken on hire purchases does not become a general Agent of owners. He is a special Agent for the purpose of executing the documents, paying initial deposit and taking delivery of goods.

3. **Commission Agent**

A Commission Agent is a Commercial Agent to whom goods have been consigned for a Foreign Principal. He holds dual personality as Agent of his Principal but does not bind his Principal contractually to third parties.

Instead, he stands in position of Principal to such third parties. In the case ***of Ireland V Livingstone (1872) 5L RAC 395,*** Lord Blackburn stated that a person who supplies goods to a Commission Agent sells them to him and not his Foreign Principal and the Commission Agent has no authority to pledge the credit of his principal for them. Donaldson J in the case of ***Teheren Europe Co. Ltd v S.T. Belton (Tractors) Ltd (1968) P.216*** stated that a Commission Agent in relation to third parties is a Principal but in relation to his Principal, Agent.

4. **Mercantile Agents**

This is an Agent having in the ordinary course of his business, authority to sell goods or to consign goods for purpose of sale or to buy goods or to raise money on the security of goods. There are three classes of Mercantile Agents namely: Factors, Brokers and Del Credere Agent.

i. A Factor is a mercantile Agent entrusted with possession of goods for sale only.

ii. A Broker is a mercantile Agent who in ordinary course of his business is employed to make contracts with third parties for purchase of goods or property or for sale of his principal's goods or property of which he is not entrusted with possession or document of title thereto. He is a mere Negotiator.

5. **Del- Credere Agent**

A Del credere Agent is a mercantile Agent who in consideration of extra remuneration called del credere commission, guarantees to his Principal that third parties with whom he enters into contracts on behalf of Principal shall duly pay any sums becoming due under the contracts. He guarantees the solvency of third parties and thus liable when third party fails to pay.

6. **Government Agent**

Over the years, Governments in many countries saw the need to set up agency Organisations to discharge certain specialized functions on its behalf. Nigeria was not left out as the following Agencies were set up by Nigerian Government to discharge certain specialized function: -

- Nigerian Television Authority
- National Orientation Agency
- News Agency of Nigeria
- National Emergency Management Agency
- Nigeria Intelligence Agency
- National Drug Law Enforcement Agency, etc.

7. **Agent Provocateur**

Though not a commercial Agent but an arrangement by the Police to let in one of their officers to join the detainee in cell for purpose of obtaining certain evidences or information. Such officer is an Agent and his Principal is the Police Authority. Other sub-classification of Agents that may come under any of the above broad types are:

i. Advertising Agents
ii. Employment Agents
iii. News Agents
iv. Collaborations Agents
v. Communicative Agents
vi. Estate Agents.

6.04 Formation of Agency Relationship

Agency can be created by word of mouth or conduct or by writing. Agency can be created by Agreement, Estoppel, Ratification and Necessity.

1. **Agency by Agreement**

The Law requires creation of some Agency relationship in writing via agreements. Where the Agent is empowered to execute a deed on behalf of his Principal, its creation must be by deed and Power of Attorney is a good example of Agency by Agreement.

See the case of ***AG Western State of Nigeria V Ogundana (1970) NCLR at P135***, where Agbaje J. held that agency must be by agreement if Agent was empowered to execute a deed.

2. **Agency by Estoppel**

Where a principal intentionally causes a third party to believe that another is his Agent, and the third party so relies in dealing with the supposed Agent, the Principal will be estopped from denying the existence of agency relationship. ***In Reccah V Standard Co. of Nigeria (1922) NLR 48***. W was employed as Agent to Defendant for purchase of produce to the knowledge of Defendant representative. Subsequently the Representative instructed W not to purchase produce for Defendant.

Despite instruction W induced the plaintiff to enter into contract to sell produce to him. Plaintiff had dealt with W as Agent of Defendant. Plaintiff then claimed contract price of produce and action succeeded. There are essential elements that must be present to successfully set up a plea of agency by estoppel.

Essential Elements of Estoppel

a. **Representation**: -

   A party must show some statement or conduct by the Principal amounting to a representation that the supposed Agent has the authority he has been represented to have.

b. **Reliance on Representation**: -

   The party who raises issue of estoppel must show not only that representation was made but that he acted upon it.

c. **Alteration of position: -**

Even when where a representation has been proved to have been made by the principal and acted upon by third party, the latter must further prove that he altered his position thereby and to his detriment.

3. **Agency by Ratification**

An agency by ratification may be created when the alleged Principal accepts or otherwise affirms the act or conduct of one purporting to act on his behalf even though there was no agreement authorizing the act. To constitute a valid ratification, certain conditions must be satisfied.

a. **Act must be on behalf of Principal**

The act of ratification can only be validly executed by the alleged principal on whose behalf the act was performed. It follows that such act must have been done on behalf of the alleged principal. In Folashade V Alhaji Duroshola (1961) I ALL NLR 87, it was held that there could be no ratification unless A purported to act as an Agent and to act for B.

b. **Existence of Competent Principal**

The alleged Principal in order to effect a valid ratification must be in existence at the time the act was supposedly done on his behalf. In Caligara V Giovanni Sarfori & Co. (1961) 3 ALL NLR 534, it was held that a company cannot ratify a contract purported to have been entered into on it behalf by the promoters prior to its incorporation.

c. **Legal quality of the Act**

An act which the principal could not have authorized in the first place because it was illegal cannot be made effective by ratification. In Urhobo V J.S. Tarka (1976) II CCHCJ 2629, it was held that if a pre-incorporation contract is purported to be made by the company which does not exist, the contract is a nullity.

d. **Ratification must be on time**

For ratification to be valid, it must be within time agreed by the parties. In Folashade V Alhaji Duroshola (Supra), it was held that ratification must be within a reasonable time after which the act cannot be ratified to the detriment of a third party.

e. **Ratification must not be partial or conditional**

Ratification, in order to be valid and effective must be absolute and unconditional.

f. **Awareness of Material Facts**

Ratification may be deemed as supplying the necessary consent for the principal-Agent relationship.

Thus, to find such consensus, there must be some evidence that the principal knew or ought to know of the material facts in question and elected to affirm it. ***In Marsh V Joseph (1897) I chD 213,*** it was held that, to constitute a binding ratification, it must be proved that the principal had full knowledge of the nature and circumstances of the acts.

The Effect of Ratification

Ratification has a retroactive effect. Once the Agent's act has been ratified, it is treated as though it had been authorized from the beginning. All rights and liabilities are said to "relate back" to the date of original act. However, it should be noted that ratification will not have effect if to do so will prejudice an innocent third party.

4. **Agency by Necessity**

In cases of emergency or necessity the law may compel a person to act on behalf of another in a particular way to avert some irreparable loss, injury or damage irrespective of any prior agency or agreement between them. The person who has acted in such circumstances becomes an Agent of necessity. ***The case of Hutchinson V Madam O. Olagide (1970) NNLR 31,*** it was held that a wife whose husband cruelty forced her to leave him was entitled to pledge his credit for necessaries.

6.05 Agency and Other Relationship Distinguished

The best way to understand the typical features of Agency relationship is to compare an Agent with other functionaries such as Trustee, Servant, Bailee, Independent Contractor.

1. **Agent and Trustee**

In some circumstances an Agent may be treated as a trustee of his principal E.g. For money received on behalf of principal.

Equally a Trustee may be treated as an Agent of the cestui que trust (A person for whom another is a Trustee). E.g for sale of trust property.

Despite this convergence, both are different in many ways: -

a. The relationship between Agent and Principal is consensual except for few cases, but a trust except for minor cases is created without consent of Trustees or cestui que trust.
b. Where an Agent is appointed, it is done by the Principal, but the Trustee is never appointed by the cestui que trust.
c. Whereas the Agent is the representative of the principal in dealing with third parties, the trustee is not in any way the representative of cestui qui trust.
d. Action between principal and Agent may be barred by time but no such limitation is imposed between cestui qui trust and the Trustee.

2. **Agent and Servant**

A servant merely works for his master but an Agent acts for and in place of his principal to effect legal relations with third parties. An Agent has representative character and derivative authority which gives him some degree of discretion in executing the terms of his agency, but a servant does not have such opportunity.

3. **Agent and Independent Contractor**

The Independent Contractor contracts with employer only as to the results to be achieved not to the means whereby the work is done. Thus, he employs his own means and skill as he is independent of control and supervision of employer. The main distinguishing element between Agent and Independent Contractor is that the doctrine of respondent superior (let the principal answer) which exists in agency does not apply to independent contractor.

4. **Agent and Bailee**

Where a personal property is delivered by the owner (Bailor) to another person (Bailee) under an agreement that the property be returned to the Bailor or transferred to a third party or dealt with in any other way indicated by the Bailor, a bailment is said to have taken place. The Bailee here is not an Agent but a situation may arise in which a person can be both an Agent as well as a Bailee of the same person. Thus, as Insurance Agent who has been provided with an Official Company Car, may be a Bailee in respect of the car but an Agent for Insurance Purposes. Another distinguishing feature is that the Agent is the representative of his principal, but the Bailee is not the representative of the Bailor. Another difference is that the Agent can contract on behalf of his Principal and can make him liable in tort, but a Bailee cannot make a Bailor liable in tort.

6.06 Principal and Agent Relationships

The relationship of Principal and Agent is consensual (by agreement), fiducial and confidential. From this relationship flows rights, duties and liabilities which may be express or implied between the parties. Sometimes the principal may engage an Agent who belongs to a particular trade, business or profession and may instruct him to operate at a particular place or locality. In such cases the usage or customs of such community, trade, business or profession may be expressly or via operation of law incorporated into the dealing by Agent. From such usage or customs, certain right and obligation may be annexed to their relationship provided these are reasonable and lawful.

Agent's Duty to the Principal

The Agent owes defined duties to the Principal which arise out of their agency relationship and these exist whether the principal is disclosed or not.

1. **Duty to Perform**

   The primary duty of an Agent is to execute his agency in accordance with terms. ***Thus, in the case of Otto Hamman V. Isenbanjo and Another (1962)2 ALL NLR 139,*** Adeferasin Ag. J. observed that "It is the duty of an Agent to carry out the business he had undertaken. This was his obligation unless he had in his contract expressly excluded responsibility."

   If the Agent fails to perform his duties he is liable for breach of agency agreement but if he performs his duties carelessly, he is liable for negligence. However, his duty to perform is not absolute but if he could not do so, he must promptly inform his principal.

2. **Duty of Obedience or Loyalty**

The Agent must execute the Agency according to instructions of the principal. Thus, in ***Esso West African Inc. V. Alli (1968) NMLR 414,*** the Court held that it is duty of an Agent to carry out instructions of the principal. The Agent's duty of obedience or loyalty is not absolute:

a. If no instructions, he can use his discretion in the interest of principal without liability.
b. If the principal's instructions are ambiguous, the Agent may act fairly and honestly without liability.
c. If the Agent is a professional, the principal's instructions will be subject to any custom or usage, trade, business or profession to which the Agent belongs.
d. The duty of obedience or loyalty does not prevent the Agent from stopping the dishonest deals of the principal.

3. **Duty of Care and Skill**

When executing the agency, an Agent must do so with reasonable care, skill and diligence. ***In Omotayo V Ojikutu (1961) ALL NLR 901,*** both Appellant and Respondent were general traders and members of same syndicate in Lagos. Appellant visited London where he acted as Agent for Respondent for purchase of Trucks. Respondent suffered loss and sued to recover from Appellant. It was held that -

a) A principal who appoints an Agent knowing his skill and experience is not entitled to expect a higher measure of skill than what the Agent has to offer.
b) An Agent does not guarantee the successful outcome of transactions.

4. **Duty of Personal Performance**

Due to the confidential nature of Principal – Agent relationship, the Agent is expected to perform the agency personally. The maxim **"delegatus non postest delegare"** applies to the relationship. However, the Agent may sub-delegate his functions in any of the following circumstances: -

a. Express authority of principal.
b. Function requires particular skill.

c. Where an emergency has arisen requiring immediate actions to protect the principal's interest.

d. Where nature of agency requires delegation.

e. Where the custom or usage of the trade, business or profession of the Agent where he operates allows it.

f. Where authority of delegate is derived from status.

5. **Duty to Act in Good Faith**

The duty arises out of the fiduciary nature of the Principal-Agent relationship. The Agent must not allow his personal interest to conflict with his duty as Agent. The rule is that unless the Principal consents, the Agent is accountable to the Principal for any benefit from the agency. ***Thus, in the case of Oke V Etawaries (1971) INCLR 85,*** a High Court of Benin held that an Agent must not allow his personal interest conflict with his principal's interest.

6. **Duty to Account**

It is the duty of the Agent to keep and render, appropriate account of his stewardship to his principal. ***See the unreported case of Akibola V Neburagho decided 1977***.

Plaintiff was the proprietress of Nursery school in Warri. She proceeded overseas for further studies and put Defendant to manage the school. Defendant refused to render account and it was held that the plaintiff was entitled to the account for which Defendant must render.

Principal's Duties to the Agent

The Principal has implied duties in law to his Agent.

1. **Duty to Remunerate**

It is the duty of the principal to remunerate the Agent for services rendered. Such remuneration may take the form of agreed commission or wages or other benefits agreed by parties. The duty to remunerate is however not absolute thus amount payable, the conditions for payment are according to agreement. Even when remuneration arises expressly, it must be earned. Thus, in the ***case of Brit Bank for***

Foreign Trade Ltd V Novinex Ltd (1949) I KB 623, it was held that remuneration is only said to have been earned when the Agent has done all that qualified him for remuneration.

2. **Duty to Reimburse and Indemnify**

   In every agency, there is implied duty on the principal to indemnify the Agent for losses, damages, or liabilities sustained by the Agent in the discharge of his duties. The principal is also under obligation to reimburse him of all reasonable expenses except:

   a) Where Agent acted without express or implied authority except transaction is ratified by Principal.
   b) Where Agent incurred losses, expenses or liabilities due to negligence.
   c) Where Agent acted in an unlawful transaction.
   d) Where Agent acted in breach of his duties
   e) Where Agent acted in respect of any transaction rendered null and void by Law.

Remedies Available to Principal

The following remedies are available to the principal in case of breach of agency by the Agent.

1. **Dismissal**: - The principal may dismiss Agent without notice.
2. **Rescission and Damages**: - Principal may rescind any contract made and hold Agent accountable for damages.
3. **Action for Account**: - Principal may act to compel the Agent to render account of all dealings and money had on his behalf.
4. **Action for Conversion**: - Principal may sue Agent for conversion where Agent had received property and misappropriated the same.

Remedies Available to Agent

Where the principal commits breach of agreement, the Agent has the following remedies; -

1. **Action for Damages**

   The Agent may sue principal to enforce right to re-imbursement and indemnity.

2. **Right of set-off**

Where principal sues the Agent, the Agent has right to set-off or counter-claim of amounts due to him.

3. **Right of Lien**

The Agent has right to hold on to the properties of the principal in his possession until he is paid.

4. **Right of stoppage in Transit**

The Agent has remedy to stop his principal goods in transit until he is paid.

5. **Other Remedies**

The Agent may demand an accounting by principal where there is reciprocal indebtedness by the parties.

6.07 Authority and Power of Company Officers Under the Law of Agency

The law of agency is an area of commercial law dealing with a set of contractual and non-contractual fiduciary relationships that involve a person (called the Agent) that is authorized to act on behalf of another (called the principal) to create legal relations with third parties. A corporation is a fictitious legal person and can only act through Agents. The corporate officers are all those Executives and senior Employees with decision making authority to bind the corporation with third parties just like the Agent and his principal. Corporate officers are generally regarded as Agents of corporation but an individual Director or even the whole Board is not regarded as Agents of the corporation because when the Board acts collectively it functions as principal in agency law terms. An Agent may have either actual, apparent or inherent authority to enter into contracts on behalf of his corporate principal. Likewise, the corporation may be estopped from denying the authority of its employees.

For example, if the Board instructed the Chief Executive Officer (CEO) not to hire an Assistant, the CEO lacks actual power but if it is the custom that the CEO can hire an Assistant then he has inherent power which when used binds the corporation. The CEO is regarded as general agents of the corporation vested with managerial powers. Contracts executed by him on behalf of

Corporation arising from ordinary course of business are binding on the corporation. As for the subordinates, they have little or no implied or apparent authority to bind the corporation except authority as expressly conferred on them by the Board resolution.

The corporate Secretary has actual authority to keep corporation books only except other authorities as conferred by Board resolution. ***In the case of Musulin V Woodtek Inc (1971) 491,*** it was held that unless authorised by Board resolution, Corporate officers lacked authority to execute promissory note on behalf of the corporation. ***See also the case of Lee V Jenkins Bros (1959) 268*** where it was held that, implied and apparent authorities of corporate officers are limited to matters arising in ordinary course of business.

In Nigeria the ***Companies and Allied Matters Act 2004, Sections 63, 64, 65, 66*** made provisions on acts by or on behalf of the company as it relates to company's powers. ***Section 63 CAMA 2004*** provides that a company shall act through its members in general meeting or its Board of Directors or through officers or Agents appointed by Board. ***Section 65 CAMA 2004*** provides that any act of members in general meeting, the Board of Directors or the Managing Director/Chief Executive Officer shall be treated as acts of the company itself and the company shall be liable to the extent as if it were a natural person.

Section 283 (2) CAMA 2004 provides that a Director shall, when acting within his authority and powers of the company be regarded as Agent of the company under part III of this Act. Part III deals with exercise of powers of the company.
In view of this provision, Directors have the following duties: -

1. ***S 279(1)*** A director stands in 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. ***S 280(1)*** The personal interest of a director shall not conflict with any of his duties as director.

3. ***S 280(3)*** A director shall be accountable to the company for any secret profit made by him.

4. ***S 281*** The fact that a director holds more than one directorship shall not derogate from his fiduciary duties to each company including duty not to use property or information in the course of management of one company for the benefit of the other company or to his or others advantage.

5. ***S 282(1)*** Every director shall exercise the powers and discharged the duties honestly in good faith and in best interest of the company. This is duty of care and skill. Failure leads to action for negligence and breach of duty.

6.08 Ultra Vires Rule

Definition: The Osborn's Concise Law Dictionary defines "Ultra vires" as an act in the excess of authority conferred by law and therefore invalid.

The general rule of ultra vires doctrine is to the effect that transactions which fall outside the ambit of a company's object or powers as stated in its memorandum of Association, is void ab nitio and unenforceable on either side. The underlying principles of the doctrine of ultra vires are that; -

1. An act can be ultra vires by the Board of Directors but intra vires the company itself, in which case the company are general meeting can ratify.
2. The question is not the legality of the contract/transaction but as to the competency and power of the company to make the contract or the transaction.
3. Since the capacity of the company is so restricted, it follows that no officer or organ of the company can act on its behalf outside its objects or ratify same acts.

Basis and Application of the Ultra Vires Rule

The purpose/basis of the ultra vires rule is to protect the Investors and creditors who have put money in the company. The company needs to be restricted to its objects to ensure certainty of nature of business the money is invested in or borrowed for, as it would be unfair for a person to invest or lend money for particular object only for the money to be channeled to other objects un-contemplated. Thus, it helps to minimize risks of investment.

Position at Common Law

Transactions which did not fall within the objects clause were null and void and incapable of ratification. This is the result even if the other party did not know that the act was beyond the company's authorized object but could have discovered it by consulting its memo and Articles- the doctrine of constructive notice. By making the contract which is void ab initio, the ultra vires doctrine made it impossible for a 3rd party who has performed his own side of transaction to compel performance by the company and vice versa. ***In the case of Continental Chemist Ltd V Dr. Ifeakandu (1966) 1 ALL NRI*,** I Bairamian JSC held that "'after" the memorandum becomes the charter of activities, anything done outside stated objects is ultra vires the company; it is invalid and cannot be ratified by the members.

Position of Company Under CAMA

S 38(1) CAMA endows every company with powers of a natural person. Consequently, a company can only enjoy this power like a natural person to contract but must be within the scope of its objects. The combined effect of ***S 38(1) and 39 (1) CAMA*** is the restoration of full operations of the ultra vires doctrine by restricting a company to only businesses and powers authorized by its memo and permitted by ***CAMA*** to which it cannot exceed.

However, ***S 39(3)*** validates the executed ultra vires contract. Thus, the common law position as in the case of *Continental Chemist Ltd v Dr. Ifeakandu (Supra)* is no longer a good authority in Nigeria- this position is strengthened by the abolition of the ***Doctrine of Constructive notice by S 68 CAMA*** to the effect that both the company and the 3rd party need not question validity of corporate transactions on ground of ultra vires. Also ***S. 69 CAMA*** codified in the rule in ***British Royal Bank V Turquand (1856) 6 EB 327*** to the effect that any person dealing with a company is entitled to a presumption of regularity. This means that a third party cannot just suffer losses because the contract with the company is null and void on ground of ultra vires doctrine. The early view of ultra vires was unfair as it allows a corporation to accept benefits of a contract and then refuse to perform obligations on ground that the contract was ultra vires.

Over time some principles were developed that prevented the application of the ultra vires doctrine. These principles included the following: -

1. Ability of shareholders to ratify an ultra vires transaction.
2. The application of estoppel which prevented defense of ultra vires when transaction was fully performed by one party.
3. When an agent of corporation commits a tort, the corporation could not defend on the ground that the act was ultra vires.

From the above, it is clear that these new strategies and principles have helped to mitigate the harsh effects of the application of the ultra vires doctrine.

6.09 Review Questions

1. In what ways does the ultra-vires rule- (a) Protect interest of corporate shareholders; (b) Imperil their interest in efficient operations.
2. Examine the different shades and forms of Corporate agents. To what extent is the differentiation aimed at protecting corporate businesses?
3. "He who does a thing through another, does it himself" Discuss the implication of this statement for business growth and development.

MODULE 7

7.00 THE DEVELOPMENT OF COMPANY LAW IN NIGERIA

7.01 Learning Outcomes

On successful completion of this module, students should be able to:

i. Evaluate the Nature of Corporate Law in Nigeria and analyse its basic principles;

ii. Examine the critical areas of company law in Nigeria;

iii. Sketch the commencement process of a business in Nigeria;

iv. Analyse the nature and duties of Company Directors;

v. Deconstruct the duties of a Company Secretary.

7.02 Commencement of a Business

To commence business in Nigeria it is mandatory to incorporate or register the business under Part A of the Companies and Allied Matters Act 2004 which deals with Companies or under Part B which deals with Business names or under Part C which deals with Incorporated Trustees. First, the procedures which is common to all parts is to reserve a unique name at the Corporate Affairs Commission via completing Form CAC 1 which is for Availability check and Reservation of Name. Procedures for reservation are contained at Section 32 of CAMA. After obtaining the name, you can now proceed with other steps of the incorporation or registration. This topic is purely a practical one and will be treated as such.

Incorporation of Companies (Part A CAMA 2004)

Sections 18 to 38 makes various provisions for formation and incorporation of Companies. After the unique name has been reserved at Corporate Affairs Commission, the next stage is the preparation of incorporation documents like Articles and Memorandum of Association. These incorporation documents are thereafter stamped at Federal Inland Revenue Service stamp duty office. The next action is to notorize the declaration of compliance with the requirements of CAMA (CAC 4).

The next thing is to register the company with Corporate Affairs Commission submitting the following incorporation documents: -

i. Form CAC I Availability check and reservation of name
ii. Form CAC 2 statement of share capital and return of allotment of shares (if applicable).
iii. Form CAC 2.1 particulars of Company Secretary.
iv. Form CAC 3 Notice of registered address.
v. Form CAC 4 Declaration of compliance.
vi. Form CAC 7 Particulars of Directors.
vii. Photocopy of information page of International Passport or National Identity Card for each Director and Subscriber.
viii. Evidence of payment of necessary fees.

After the processing, the Certificate of Incorporation is issued by CAC and the Company may commence business after making a company seal and registration with Federal Inland Revenue Service for Income tax, VAT and PAYE. It is mandatory that all companies register their Business premises with the State it is located.

7.03 Registration of Business Name (Part B CAMA 2004)

Registration of Business is covered by Section 652 to 671, CAMA 2004. To commence business via Business name, you need to reserve a name and register under Part B of the Corporate Affairs Act 2004. The following are the requirements for registration of Business name:

Form CAC I Availability check and Reservation of name.

i. Form CAC/BN/I Application for Registration of Business name.
ii. Two passport photographs in case of individual and copy of Certificate of Incorporation together with Certified True Copy of resolution in case of corporate body.
iii. Payment of filing fees.

iv. Payment of fees for Certified True Copy of Certificate for display at each disclosed Branch office.

v. Where a Magistrate, Legal practitioner or Police officer of the appropriate rank signs a Business name registration application and one of the partners is a minor, the Magistrate, Legal practitioner or Police officer shall state his full name, address and telephone number.

After processing, a Certificate of Registration is issued to signify commencement of business. It is a requirement to register the premises in the state of operations.

7.04 Incorporation of Trustees (Part C CAMA 2004)

Section 673 to 695 covers incorporation of Trustees. The following are the requirements for incorporation of Trustees: -

i. Form CAC I Availability check and Reservation of Name.

ii. Form CAC/IT I – Incorporated Trustees Application Form signed by Chairman and Secretary.

iii. Extracts of minutes of General meeting appointing Trustees signed by Chairman and Secretary.

iv. Two printed copies of the Constitution.

v. Trustees declaration form duly deposed to by each Trustees in the High Court.

vi. Impression of the common seal on the application Form.

vii. Notice of the situation of the address or any change therein.

viii. Payment of filing fees.

ix. The extract of minutes shall list member's present and voting pattern.

Ix. Cuttings (or National Liberty Certified Copy) of publication page of notice of application for registration in two daily newspapers, one of which must circulate in the locality of the Association and the other a National newspaper.

x. The notice of application published in the newspapers shall state the name and objects of the Association, the full names of the Trustees and invite objections to the name, object or persons stated as Trustees within 28 days of publication.

xi. Thumb prints by an illiterate Trustee or Officer shall be accompanied by an illiterate jurat.

In the absence of any objection the application is processed, and certificate issued for the incorporated Trustee to commence business.

7.05 Fiduciary Duties of a Director

Fiduciary duty is a duty to act for someone else's benefit while subordinating one's personal interest to that of the other person. This type of duty has to do with trust on the person acting for the interest of another. A Director of a company stands in a fiduciary relationship towards the company and shall observe utmost good faith towards the company in any transaction with it or its behalf S 279(1) CAMA 2004. By Section 279(2), a director shall owe fiduciary relationship with the company in the following circumstances: -

a. Where a Director is acting as Agent of a particular shareholder.

b. Where, even though he is not an Agent of any shareholder, such a shareholder or other person is dealing with the Company Securities.

See the case of Bamford V. Bamford (1970) CH 212. In that case, to prevent a take over bid the Directors allotted 5000 shares to another company. The article provides that all uninsured shares were to be at the disposal of the Directors. Two shareholders sought a declaration that the allotment was void because it was not made for the benefit of company. Court held allotment valid and for interest of company. Section 280 CAMA 2004 provides that the personal interest of a Director shall not conflict with any of his duties as Director under this Act. A director shall not in the course of management of affairs of the company or in utilization of the company's property, make any secret profit or achieve other unnecessary benefits. A director shall be accountable for any secret profit or benefit made by him. Section 281 of CAMA 2004 provides that, the fact that a person holds more than one directorship shall not derogate his fiduciary duties to each company including a duty not to use the property, or opportunity or information obtained in the course of management of one company for the benefit of the other company or to his own or other person's advantage.

7.06 Statutory Duties of a Director

As the name indicates, statutory duties are those duties or liabilities imposed on the Directors by some statutes. In Nigeria, all duties imposed by the Company and Allied Matters Act 2004 including fiduciary and duty of care and skill are statutory. Section 334 CAMA 2004 provides that in every company, the Directors shall in respect of each year prepare the Financial Statements for the year. Section 342 CAMA 2004 provides that in the case of every company they shall be prepared in respect of each year a report by Directors. Going by Section 345 CAMA 2004, it is the Director's duty to lay before the company in general meting, copies of the Financial Statements of the company. Section 227 CAMA 2004 makes provisions imposing duty on Directors to disclose interests in contracts at the meeting of Directors of the company.

Section 252 CAMA 2004 imposes duty on Directors to the effect that, any person who is appointed or to his knowledge proposed to be appointed Director of a public company and who is seventy or more years old shall disclose this fact to the members at a general meeting. From the above it is clear that many statutes have imposed various duties on Directors and the above duties are just few examples.

Duty of Care and Skill

Section 282 CAMA 2004 has made several provisions on Directors duty of care and skill. This Section at S282 (1) provides that 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 circumstance. By S. 282(2) CAMA 2004, failure to take reasonable care shall be a ground for an action for negligence and breach of duty. By S. 282(3) CAMA 2004, each Director shall be 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. In S. 282(4) CAMA 2004, 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.

See the case of Re-City Equitable Fire Insurance Co. Ltd (1925) ch 407.

7.07 Company Secretary: Qualification, Appointment and Removal

Section 293 to 298 CAMA 2004 made provisions for a Company Secretary. By section 293 (1), every company shall have a Secretary. S 293 (2) provides that, where the office of Secretary is vacant, his assistant or deputy secretary can act and in their absence, any officer of the company authorized can act. The Secretary is the Chief Administrative officer of the company who serves at the Board and participates in the day to day running of the company. ***See the case of Wimpey Nigeria Ltd V Balogun (1986) 4 NWLR pt 28 324CA.***

Qualifications

Section 295 CAMA 2004 provides that, it shall be the duty of a Director to ensure that the Secretary of the Company is a person who appears to him to have the requisite knowledge and experience to discharge the functions of a Secretary of a Company. This is the only qualification required of a Secretary of a private company.

For Public Companies, he shall be:

a. A member of the Institute of Chartered Secretaries and Administrators.

b. A legal practitioner

c. A member of the institute of Chartered Accountants of Nigeria or such other bodies of Accountants as are established from time to time by an act. From 1993, members of Association of National Accountants of Nigeria (ANAN) are qualified for appointment as Secretary of a Public Company as well as Private Companies.

d. A person who has held the office of the Secretary of a Public Company for at least three years of the five years immediately preceding his appointment in a Public Company.

e. A body corporate or firm consisting of members each of whom is qualified under paragraphs (a) (b) (c) or (d) of this section.

Appointment and Removal of Secretary

Section 296 CAMA 2004 provides that a secretary shall be appointed by the Directors and may be removed by them. ***See the case of Adebesin V May and Baker Nig. Ltd (1973) FRCR 232.***

For a private company, there is no official procedure for removing a secretary but for a public company, S. 296 (2) provides that the Board shall give him notice:

a. Stating that it intends to remove him.

b. Setting out the grounds on which to remove him.

c. Giving him a period of not less than seven working days to make his defense.

d. Giving him option to resign within seven days.

Where the Secretary refuses to resign or make a defense, the Board may remove him and make a report to the next general meeting: S 296 (3). Where the Secretary makes a defense, but the Board does not consider it sufficient, if the ground:

a. Is that of fraud or serious misconduct, the Board may remove him and report to the next general meeting and,

b. If the ground is other than fraud or serious misconduct, the Board shall not remove him without approval of general meeting but may suspend him.

7.08 Powers and Duties of a Secretary

The duties of a secretary are what he has powers to do. By S. 298 CAMA 2004, the duties of the secretary shall include the following: -

a. Attending meetings of the Board and rendering all secretarial services and giving advices.

b. Maintaining the registers and other statutory records.

c. Render proper returns and giving notification to the commission required under this Act.

d. Carrying out administrative and secretarial duties as directed by the Director of the company. By Section 298 (2) CAMA 2004, the secretary shall not without the authority of the Board exercise any powers vested in the Directors.

7.09 Liability, Restriction and Disqualification Orders

Section 21, CAMA 2004 provides that an incorporated company may be either a company: -

a. Having the liability of its members limited by the memorandum to the amount if any unpaid on the shares respectively held by them (in this Act referred as "a company limited by shares or;
b. Having liability of its members limited by memorandum to such amount as members may respectively undertake to contribute to the assets in the event of its being wound up (in this Act termed "a company limited by guarantee")
c. Not having any limit on the liability of its members (in this Act referred to as "unlimited company").

As it relates to Directors and officers, Section 290 CAMA 2004 provides that, where a company:

a. Receives money by way of loan for specific purpose or,
b. Receives money or other property by way of advance payment for execution of contract or project and,
c. With intent to defraud, fails to apply the money or property for the purpose it was received, every Director or officer who is in default shall be personally liable.

Where personal liability of a Director or officer occurs, such a Director or officer may face restriction or disqualification orders by the court of law. In Nigeria disqualification may be by law and not by court alone. Section 257 of CAMA 2004 provides that the following persons are disqualified from being Directors.

a. An infant (i.e. a person under 18 years).
b. A lunatic or person of unsound mind.
c. A person disqualified under Section 253 CAMA 2004 (i.e. an insolvent person).

d. A person disqualified under Section 254 CAMA 2004 (i.e. a fraudulent person).

e. A corporation other than its representative appointed to the Board for a given term.

f. A person disqualified under section 258 of this Act which provides that, the office of the

Director shall be vacated if the Director: -

i. Ceases to be director by virtue of Section 251.

ii. Becomes bankrupt

iii. Becomes prohibited from being a Director by any order made under Section 254.

iv. Becomes of unsound mind

v. Resigns his office by notice in writing to the company.

On the other hand, the law places restriction on the fraudulent persons from becoming a Director of the company. Section 254 of CAMA 2004 provides that any person convicted by a High Court of any offence in connection with promotion, formation or management of a company or guilty of fraud, the court shall make an order restricting that person from being a director for a period not exceeding ten years. It should be noted that where there is a court order of restriction or disqualification of any Director, the Corporate Affairs Commission must be notified. While restriction prevents, disqualification terminates the continuity of an individual from becoming a Director. The main objective of disqualification is to seek out those who abuse the privilege of limited liability Companies. A director may face disqualification order on application to court by outsiders due to criminal, fraudulent activities or personal liability for debts.

In Ireland, section 90 and 160 of their companies Act 1990, the court has right to disqualify individual from acting as company Directors in the following circumstances:

i. Where a person is convicted of fraud or dishonesty

ii. Where a person is convicted while restricted

iii. Where the person is an undischarged bankrupt

iv. Where the person is a director of company as there has been a failure to notify the company's registration office.

By Section 150 of their Companies Act 1990, any person who acts as Director of an insolvent company within 12 months of its going into liquidation is restricted from being an officer of another company up to the period of five years.

7.10 Review Questions

1. Examine critically the procedure for the appointment and removal of (a) A Company Director; (b) Company Secretary.
2. Under what circumstance would the court lift the veil of incorporation to punish an erring Director of a public company.
3. Critically review the fiduciary and statutory duties of a director

MODULE 8

8.00 ADMINISTRATION OF COMPANY: THE DIRECTORS, SECRETARY, ANNUAL RETURN, ACCOUNTS AND AUDIT, MERGERS, ARRANGEMENT AND TAKE-OVERS

8.01 Learning Outcomes

On successful completion of this module, students should be able to:

i. Asses and interpret the key terminologies in the administration of a company;
ii. Investigate the key procedures in the administration of a company in Nigeria;
iii. Evaluate and discuss the forms of corporate offences;
iv. Interpret the implication of liability.

8.02 Directors

Section 244, CAMA 2004 defines Director as persons duly appointed by the company to direct and manage the business of the company. By Section 246, CAMA 2004, every company shall have at least two Directors while Section 247 provides for appointment of first Directors by subscribers of the memorandum of Association. The members at annual general meeting shall have power to appoint subsequent Directors (Section 248 CAMA 2004).

By S. 262 of CAMA, a company may by ordinary resolution remove a director before expiration of his tenure. Section 279 makes provisions for the duties of Directors which we have already discussed. Section 267 provides for remuneration and other payments to Directors.

8.03 Secretaries

By Section 293 CAMA 2004, every company shall have a Secretary. Section 294 provides that no one person shall do what should have been done by a Director and Secretary. Section 295 makes provisions as to the qualifications of a Secretary which we have already discussed in detail. By Section 296, a Secretary shall be appointed by the Directors and may be removed by them. Section 297 CAMA 2004 provides for fiduciary interests of a Secretary while Section 298 makes provisions for duties of Secretary which we have already discussed in detail.

8.04 Annual Returns

Sections 370 to 378 make provisions for annual returns by companies. Every company is required at least once in every year, to make and deliver to the commission an annual return in form and containing the matters specified in Sections 371, 372 or 373 as may be applicable. It is required that annual returns be filed within 42 days after the annual general meeting in the following forms: -

- Schedule 8 for companies having capital other than small companies
- Schedule 9 for small companies
- Schedule 10 for companies limited by guarantee

The following are the contents of Annual returns:

a. Address of the registered office
b. Situation of register of members and register of debenture holders
c. Summary of share capital
d. Particulars of indebtedness
e. List of past and present members
f. Particulars of Directors and Secretary.

8.05 Documents to Accompany Annual Returns

a. Copy of balance sheet
b. Copy of Auditors, and Directors reports.
c. Statement signed by Director and Secretary that the Company has not, since incorporation or since last returns made any invitation to public to subscribe for any shares.

Accounts and Audit

Accounts

Sections 331 to 355 CAMA 2004 make provisions for financial statements and accounts of companies. Section 331 provides that every company shall cause accounting records to be kept to show and explain transactions of the company including all assets and liabilities of the company. The Directors under Section 334 has the duty to prepare financial statement for each year which should include the following.

a. Statement of accounting policies
b. Balance sheet
c. Profit and loss accounts or income and expenditure for non-profit entities
d. Notes to the accounts
e. The Auditors report
f. The Directors report
g. A statement of sources and application of fund
h. Value added statement
i. A five-year financial summary.
j. In the case of a holding, the group financial statement. The financial statement of a private company need not include matters in paragraphs (a), (g), (h) and (i) above

Under section 344, the following are entitled to receive the company financial statements:

i. Every member of the company.
ii. Every holder of company debenture.
iii. Other persons so entitled.

Section 345, CAMA 2004 provides that, it is the duty of Directors to lay the financial statements of the company in the general meeting.

Audit

Sections 357 to 359 make provisions for audits of the Company. Section 357 provides that every company shall at each annual general meeting appoint auditor to audit the financial statements of the company. Where at an annual general meeting, no auditors are appointed or re-appointed, the directors may appoint a person to fill the vacancy.

Auditors Duties and Powers

Section 360 CAMA 2004.

1. It shall be the duty and power of the company's auditors in preparing their report to carry such investigations as may enable them form an opinion whether: -
   a. Proper accounting records have been kept and proper returns adequate for audit have been received.
   b. The company balance sheet and profit and loss agree with accounting records.
2. If proper records have not been received or balance sheet and profit and loss are not in agreement with records, the auditors shall state that fact in their report.
3. The auditors shall have access to company books and records.
4. If the requirements of part v and vi of schedules 3 and part i to iii of schedule 4 are not complied with, it is the auditor's duty to include it in their report.
5. It is auditors' duty to state whether the Directors' reports are consistent with records.

8.06 Remuneration of Auditors

Remuneration of auditors shall be fixed by Directors if they were appointed by them and by general meeting if appointed by general meeting.

Removal of Auditors

Section 362, CAMA 2004 provides that a company may by ordinary resolution remove an auditor before expiration of tenure.

Resignation of Auditors

Section 365, CAMA 2004 provides that an auditor may resign his office by depositing a notice at the company's registered office.

8.07 Liabilities of Auditors for Negligence

Section 368 of CAMA provides that a company auditor shall exercise care, diligence and skill in performance of his duties. But where a company suffers loss or damages as result of failure by auditors to discharge their fiduciary duty, the auditor shall be liable for negligence.

8.08 Mergers, Arrangements and Procedures

Merger means any amalgamation of the undertakings or any part or interest of two or more companies (section 590 CAMA). Mergers are regulated by section 590 to 613 of CAMA 2004, securities and exchange Act sections 6 and 8, investment and securities Act 1999 sections 100 to 102.

Procedures of Merger

Under the Securities and Exchange Act (SEC), there are three steps in the merger procedures:

Step 1

1. The merger proposal shall be prepared and approved by the separate Boards of the merging companies.
2. A pre-merger notice is sent to members and SEC.
3. Each company shall apply to court to sanction proposal.
4. The court shall order separate general meeting of the companies.

Step 2

1. 3/4 majority of members approve the scheme at each separate meeting after which scheme is referred to SEC for approval.
2. If approved by securities and exchange commission and shareholders of affected companies, any of the merging company may then make application to court to sanction the scheme.

Step 3

1. Every company affected shall cause an office copy of the court order to be delivered to SEC for registration within 7 days after the order.

2. Notice of order is published in the official gazette of the Federation and at least one newspaper.
3. Notify SEC of completion of the merger.

Examples of Merger in Nigeria

a. Lever Brothers and Lipton Nigeria Ltd
b. ELF and Total Nigeria Ltd
c. Lever Brother and Chesebrough Products Ltd.

Arrangements

Arrangement, by Section 537 CAMA 2004 means any change in the rights or liabilities of members, debenture holders or creditors of the company or class of them in regulation of a company other than a change effected under any other provision of this Act by unanimous agreement of all parties affected thereby. It follows from this definition that where the Act makes provisions for change or where the parties unanimously agree, there is no need for a scheme of arrangement. It is only for those cases where there are no statutory provisions and some members do not agree that a scheme of arrangement is designed.

Procedures

1. Where arrangement is proposed between a company and its creditors, and its members, the court may on application of a creditor, or member or in case of a company being wound up, of the liquidator, order a meeting.
2. Notice summoning meeting will be sent along with statement explaining the effect of arrangement.
3. Where 3/4 majority of members agree to the arrangement, it will be referred to Securities and Exchange Commission (SEC) which shall appoint inspectors to investigate the fairness of arrangement and make a report to court.

4. If the court is satisfied, it shall sanction it and the arrangement becomes binding on members, creditors and the company and for company being wound up on contributories and liquidator.
5. The court order sanctioning arrangement will not take effect unless and until a certified copy of the order has been delivered to corporate Affairs Commission for registration.
6. A copy of such order shall be annexed to every memo of the company issued after the order.

8.09 Reconstruction

Reconstruction scheme is covered by Section 591 to 593 of CAMA 2004 and the investment and securities Act 1999; Sections 100 to 102. Reconstruction is a general term indicating a re-Organisation in the equity holding of the company. It is a structural change which may take the form of merger or take-over. Its procedures are thus same as for mergers we have discussed above.

8.10 Take Over Bids

A take over means the acquisition by one company of sufficient shares in another to give the acquiring company control of the acquired company. ***Section 99 of Investment and securities Act 1999 and sections 590 and 594 CAMA 2004.*** The main difference between a merger and a take over is that, while a take over is an acquisition which enables the entity acquired to continue as a subsidiary, a merger is a combination of undertakings which sometimes gives birth to a new company.

Procedures

1. The Offeror or company makes an offer (bid) to existing shareholders of a target company or to one or more classes of them to acquire their shares for a consideration in form of cash or securities.
2. Application is made to Securities and Exchange Commission (SEC) and if approved, approval is valid for 90 days.

3. Copy of approval must be registered with the Corporate Affairs Commission.
4. Where SEC refuses to approve the bid, the applicant company may approach the court to compel registration.

Note that where despite refusal of the bid by directors of a target company, the biding company insists on making direct contacts with the share holders of the target company, such is called hostile take over bid. Take over bids are still unpopular in Nigeria as we are yet to witness any.

8.11 Corporate Offences: Fraudulent Trading, Reckless Trading, Insider Trading and Money Laundering

Corporate offences as the name indicates are offences committed by corporate entities some of which are hereby discussed below.

Fraudulent Trading

Where a corporation carries on business with the intent to defraud or cheat the public, it is said to have engaged in fraudulent trading. A business activity that is deliberately designed to defraud creditors is fraudulent trading. For example, a manufacturing plant taking deposits for large order of product knowing that the company will be unable to deliver due to impending bankruptcy. In Nigeria there are no explicit provisions in our laws on fraudulent trading but under the English law ***the rule in Foss V Harbottle (1843) 2 HL 4612*** became a good example.

In the case, 2 shareholders brought action on behalf of themselves and others against defendant (5 Directors, a Solicitor and an Architect) alleging illegal and fraudulent dealings particularly that the Directors purchased their own over priced land for the company. The court dismissed plaintiff action that only the company could institute action. This rule though gave the majority total control but encouraged fraudulent corporate transactions.

To reduce the harsh effects of this ruling, exceptions were developed and one of which is that the rule does not hold where fraud has been committed by the company. Section 299 CAMA 2004 seems to be a direct import of the rule in Foss V. Harbottle where it stated that where irregularity has been committed or a wrong done, only the company can sue to ratify the irregularity. Nigerian courts are not left out in the bid to reduce the harsh effects of the rule in Foss V. Harbottle. ***See the case of Edokpolor & Co V. Sam-Edo Wire Industries Ltd (1984) 7, SC 119.*** Section 312, CAMA 2004 has given the courts wide powers to make orders as it thinks fit to give relief against fraudulent trading. Such orders may include an order to wound up the company, cause investigation of fraudulent trading, order to prosecute directors involved, etc.

Reckless Trading

Where the Directors knowingly carries on business despite serious risks of losses or damages, ignoring the risks because of the selfish desire to keep the company alive, that amounts to reckless trading. In Nigeria there are no provisions in our laws yet. In United Kingdom, Section 297A of companies Act 1963 makes provisions on reckless trading. Any Director found guilty of reckless trading will be held liable to the extent that his actions in continuing to trade caused foreseeable loss to the company. For example, if the company had debts amounting to ₦100,000.00 and you decided to continue trading in circumstances which were reckless and incurred further loss of ₦25,000.00 the Director shall be held liable for the loss of ₦25, 000.00 while the debts of ₦100,000.00 remains as the debt of the company.

Insider Dealing

Insider trading is simply the buying and selling by someone who has access to material, non-public information about the security. Insider trading or dealing can be illegal or legal depending on when the insider makes the trade. It is illegal when the material information is still non-public but legal once the material information has been made public at which time the insider has no direct advantage over other investors. Sections 614 to 621 CAMA 2004 have made provisions relating to insider dealings. Section 615 CAMA 2004 prohibits an individual who is an insider of a company from dealing in the securities of the company which are offered to the public for sale or subscription.

Section 616 CAMA 2004 prohibits abuse of information obtained in official capacity. A public officer or former public officer who had obtained certain sensitive information in his official capacity shall not deal in any relevant securities or counsel or procure any other person to deal in any such securities. Section 620 CAMA 2004 provides for civil liability of an insider who is liable to compensate any person who has suffered a direct loss. Section 621; CAMA 2004 provides for criminal penalty that any individual guilty of insider dealing shall be liable to imprisonment for 2 years or a fine of ₦5, 000.00 or both.

Money Laundering

Money laundering is an arrangement for concealment of investment or transfer of the proceeds of a criminal conduct. For example, proceeds of drug trafficking. In Nigeria, the money laundering (prohibition) Act Cap M18 2004 made several provisions on money laundering.

In ***ATUCHE Vs F.R.N (2015) 4 NWLR part 1449,*** it was defined as the act of transferring illegally obtained money through legitimate people or accounts so that its original source cannot be traced. By the Act, any deposit of ₦1,000,000.00 and above for individual and ₦5,000,000.00 and above for Corporate body must be reported by financial institutions to central Bank. Similarly, international transfer of funds exceeding US $10,000.00 must be reported to central bank.

Casinos are required to keep records of their transactions and financial institutions must get proper details before opening accounts and they are required to undertake special surveillance on certain transactions. Where an offence under this Act has been committed by a body corporate the court may order the entity be wound up and Assets forfeited to the Federal Government. Only the Federal High court shall have the power or jurisdiction to try offences under this Act.

8.12 Liability of Company in Respect of Unauthorized or Irregular Transactions in Both Tort and Criminal Law

A contract may be fully within the capacity of a company and hence not affected by the ultra vires rule. But an outsider may still be unable to enforce the contract against the company because the person who entered into it on behalf of the company was not authorized to do so. Again, a contract may be within the capacity of the company and yet unenforceable because some condition as to its validity has not been complied with. Thus, it may be fully within the powers of the company to borrow money but only with the sanction of a resolution of the members. If such a resolution is not passed the contract may be unenforceable. It must be emphasized that these two categories of contract are not instances of contracts which are ultra vires as they are within capacity of the company, but they are unauthorized and thus irregular.

Although there are no explicit provisions in Nigeria on this matter, the CAMA 2004 has in several sections attempted to discuss what may be called unauthorized and irregular transactions. Section 562, CAMA 2004 provides for civil liability for misstatement in the prospectus. Where it provides that, where a prospectus invites persons to subscribe for shares in a company, the following persons shall be liable to pay compensation to all persons for losses or damages they may incur by reason of untrue statement included in it. Every person:

i. Who is a Director
ii. Who is named in the prospectus
iii. Being a promoter
iv. Who authorized the issue of the prospectus.

Such an untrue statement renders the transaction irregular. On the other hand, Section 563 imposes criminal liability for misstatement in prospectus where it provides that where a prospectus includes an untrue statement, any officer who authorized the issue shall be guilty of an offence and liable on conviction to imprisonment for 2 years or a fine not exceeding N5000.00 or both. Section 567, CAMA 2004 provides that no allotment shall be made unless minimum subscription has been received. Based on this provision, irregular allotment arises where:

1. Allotment is made before minimum subscription is received.
2. Allotment is made before payment on application which should not be less than 5% of the price of the shares.
3. Allotment is made without a statement in lieu of prospectus where applicable.

The effect of irregular allotment is that it is voidable at the instance of the applicant within a month after holding the statutory meeting of the company or if allotment is made after the statutory meeting, within a month after the date of such allotment and not later (Section 571 CAMA 2004). See Smith V. Chadwick (1884) 9 APF Cases 187. From the above, it is clear on where the liability lies for unauthorized or irregular transactions in both tort and criminal law.

8.13 Review Questions

1. Critically review the role of auditors in ensuring corporate accountability.
2. Under what circumstances may auditors be charged with negligence.
3. Reconstruction, Mergers and Acquisitions, Take-Over Bids are measures to enhance the financial health of a firm. Discuss.

RECOMMENDED FUTHER READINGS

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