COMPANY LAW

CPA SECTION 4
CS SECTION 3
CCP SECTION 3

STUDY NOTES

KASNEB SYLLABUS

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CHAPTER ONE

NATURE AND CLASSIFICATION OF COMPANIES

OBJECTIVES

By the end of this chapter, the student should be able to:

• Explain the various types of companies
• Describe nature and characteristics of a company
• Give classification of companies.
• Explain principle of legal personality and veil of incorporation
• Distinguish between companies and other forms of business.

INTRODUCTION

This chapter starts by appreciating that besides the company there are other forms of business associations, such as cooperatives, partnerships and sole proprietorships. It then distinguishes these other forms of business associations from the company, which is our main focus. The chapter then goes ahead to look at the law governing other forms of business associations with special attention to cooperative societies.

KEY DEFINITIONS

• **Sole proprietorship**: Simplest form of business what is also called one man business
• **Partnership**: A business owned by a minimum of two and a maximum of twenty people
• Cooperative: An association in which people pool their resources for their common good
• **Incorporated association**: An artificial person that has a legal identity
• Limited liability: This is a company whereby any liability members in times of liquidation of the company is limited to the amounts if any unpaid on member's shares

TYPES OF COMPANIES

There are different types of companies which are based on the basis of formation, liability ownership , domicile and control.

1Types based on the basis of formation or incorporation.

A) **Chartered companies.**

Companies which are incorporated under special charter issued by the head of state e.g. Chartered Bank.

b) Statutory companies.

Are Companies which are incorporated by a special act of parliament. The activities of such companies are governed by their respective acts and are not required to have any memorandum or articles of association.

c) Registered companies

Are those companies incorporated through registration under the companies act.

2 Types of companies based on the basis of liability

a) companies with limited liability

Are companies where capital is divided into shares and liability of members is a company limited by shares. Others are limited by guarantee where shareholders promise to pay a fixed amount to meet the liabilities of the company in the case of liquidation.

B) Companies having unlimited liability.

They do not have any limit on the liability of members as in the case of partnership.

3) Types of companies based on ownership.

a) Government companies.

Are companies where at least 51% of the paid up capital has been subscribed by the government.

b **)Non-governmental companies.**

If the government does not subscribe a minimum of 51% of the paid up capital, the company will be a non-governmental company.

4.Types of companies on the basis of domicile

a) National companies

It’s a company which is registered in a country by restricting its area of operations within the national boundary of that country.

b) Foreign companies.

Are Companies having business in a country but not registered in that country.

c) Multinational companies

They have their presence and business in two or more countries

5. Types of companies on the basis of control.

a) Holding companies

These hold all or majority of the share capital in one or more companies so as to have a controlling interest in such companies.

b) Subsidiary company

Is a company which operates its business under the control of another company i.e. holding company.

NATURE AND CHARACTERISTICS OF A COMPANY.
A company is defined by the two fundamental principles of company law as discussed below:
• Legal/Corporate personality
• Theory of limited liability

1. Legal/Corporate personality
2. A company is a legal person distinct and separate from the subscribers to the memorandum

A company thus has rights and duties similar to those of human beings
This principle holds that when a company is incorporated it becomes a legal person distinct and separate from its members and managers. It becomes a body corporate with an independent legal existence with limited liability, perpetual succession, capacity to contract, own property and sue or be sued. The principle of legal personality was first formulated by the House of Lords in its famous case of Salomon v Salomon and Company limited where Lord Macnaghten was emphatic that the company is at law a different person from the subscribers to the memorandum. This principle is now contained in section 16(1) of the Companies Act which provides *inter alia* that from the date of incorporation, the subscribers to the memorandum together with such other persons that may become members of the company are a body corporate by the name contained in the memorandum capable of exercising the functions of an incorporated company with power to hold and having perpetual succession and a common seal.
The decision in Salomon's case lay to rest certain principles:
1. That even the so called one man companies were legal persons distinct and separate from the members and managers
2. That incorporation was available not only to large companies but to partnerships and sole proprietorships as well
3. That in addition to membership, it was possible for a member to subscribe to the company's debentures
2. Theory of limited liability
Liability means the extent to which a person may be called upon to contribute to the assets of the company in the event of winding up. In company law, the liability of members may be limited or unlimited. If limited it may be limited by shares or by guarantee as shall be explained later in this chapter.
CLASSIFICATION OF COMPANIES
>>Private company
Is one which restricts the right of transfer of its shares , it limits the number of its members to fifty and it cannot invite the public to subscribe for its capital.
>>Public company
It does not restrict the transfer of shares to of the company, it imposes no restriction on the maximum number of members and it invites the public to subscribe for shares.

PRINCIPLE OF LEGAL PERSONALITY AND LIFTING THE VEIL OF INCORPORATION
• Exceptions to the rule in **Salomon v Salomon** constitute lifting the veil of incorporation.
• There are common law and judicial exceptions.

The decision in **Salomon v Salomon** established that when a registered company is incorporated it becomes a legal person distinct and separate from its members and managers. It becomes a body corporate with an independent legal existence. This is referred to as the veil of incorporation.

As a general rule the law does not go behind the veil to the individual members. However, in exceptional circumstances the law ignores the separate legal personality of the company in favour of the realities behind the facade. These circumstances are collectively referred to as lifting the veil of incorporation. They are exceptions or modifications to the rule in **Salomon's case**. Such instances may arise under statutory provisions or case law.

Statutory provisions/legislative/parliamentary

The following are the sections of the Kenya Companies Act which correspond to those sections of the English Companies Act 1948 which are usually listed in English Company law textbooks as

the instances in which the veil of incorporation will be lifted under express statutory provisions:

(a) Section 33: Reduction of number of members

This section provides that a company's member is personally liable for the company's debts incurred after the six months during which the company's membership had fallen below the statutory minimum, provided he was cognisant of the fact that the membership had so fallen. The section is regarded as an instance of "lifting the veil" because it modifies the principle established in **Salomon v Salomon & Co Ltd** that a member is not liable for the company's debts, and permits the company's creditors to sue him directly in order to recover the debts. Liability under the section may arise on the death of a member if the death reduces the membership below the statutory minimum for the particular company and:

(i) No transferee is registered as a new member, and

(ii) The personal representative of the deceased member does not elect to be registered as a member, within the prescribed six months.

It should be noted that the section limits a member's liability to debts contracted after the six months. It does not make the member liable for any debts incurred during the six months, which follow the reduction of membership. Neither does it make a member liable for any tort committed by the company during the relevant time.

(b) Section 109 (4): Non-publication/Mis-description of a company's name

Subsection (1) of Section 109 of the Act requires a company's officers and other agents to write its name on its seal, letters, business documents and negotiable instruments. This is to be done primarily for the benefit of third parties who might contract with a limited company without realising that it is a limited company.

Subsection (4) of the section provides that any officer or agent of the company who does not comply with the aforesaid statutory requirements shall be liable to a fine not exceeding Kshs.1000, and shall further be personally liable to the holder of any bill of exchange, promissory note, cheque or order for goods which did not bear the company's correct name, unless the amount due thereon is duly paid by the company.

The imposition of personal liability on the company's agent is what is regarded, in a somewhat loose sense, as "lifting the veil of incorporation". A probably better view would be to regard the section as a codification of the common law rule which makes an agent personally liable under a contract which he enters into with a third party without disclosing that he is acting for a principal. That, in effect, is what happens if a company's

agent does not comply with the statutory requirement.
Liability under this section is illustrated by **Nasau Steam Press v Tyler & Others** (7) and **Penrose v Martyr** (8). In the latter case the plaintiff told the court that she was NOT aware that the company was limited till after the bills were accepted. She had, therefore, been misled as to the legal status of the company. It should, however, be noted that the section does not require that the third party suing the company's officer should have been misled by the officer's failure to write the company's name correctly.

(c) Section 150: Group accounts

Section 150 requires a company which has subsidiaries to lay before the company in general meeting accounts or statements dealing with the state of affairs and profit or loss of the company and the subsidiaries at the time when the company's own balance sheet and profit and loss account are laid before the company's general meeting. The group accounts are to be prepared in accordance with the provisions of Sections 150-154 and paragraphs 17-18 of the Sixth Schedule to the Companies Act so as to appear "as the accounts of an actual company".
These provisions constitute what is regarded in a loose sense as an instance of "lifting the veil" because a member (the holding company) is obliged to incorporate into its balance sheet the assets and liabilities of the company of which it is a member (the subsidiary company) as if they were its own assets and liabilities. This is a modification of the general principle that a company's assets and liabilities are not a member's assets and liabilities and would not, therefore, be incorporated into the member's own balance sheet.

(d) Section 167: Investigation of Company's Affairs

Section 167 gives an inspector appointed by the court powers to investigate the affairs of that company's subsidiary, or holding company, if the inspector thinks it necessary to do so for the purpose of his investigation. An investigation instituted pursuant to this power would be regarded, in a loose sense, as an instance of "lifting the veil" because the order to investigate a company sufficed to investigate the company's member, or vice versa, as if they were one entity.
Generally speaking, a company and its member (in this case, the holding company) are altogether separate entities and a court order to investigate the affairs of a subsidiary company would not authorise an investigation of its holding company, and vice versa.

(e) Section 173 (5): Investigation of Company's Membership

Section 173(1) empowers the registrar to appoint one or more competent inspectors to investigate and report on the membership of any company for the purpose of determining the true persons who are or have been financially interested in the success or failure of the company or able to control or materially to influence the policy of the company.
For the purpose of that investigation, Subsection 5 of the section confers on the inspector, or inspectors, power to investigate the membership of the company's subsidiary or holding company for the same purpose. A company and its subsidiary, or subsidiaries, are thereby regarded as one entity for the purpose of the investigation, and the veil of incorporation thereby lifted.

(f) Section 210: Take-over Bids

Section 210 provides that where a scheme or contract involving the transfer of shares or any class of shares in a company to another company has been approved by the holders of not less than nine-tenths in value of the shares whose transfer is involved, the transferee company may, at any time within two months after the expiration of four months after the making of the offer by the transferee company, give notice in the prescribed manner to any dissenting shareholder that it desires to acquire his shares. The dissenting shareholder must then apply to the court within one month from the date on which the notice was given for an order restraining the transferee company from compulsorily acquiring his shares. The court order may, in an appropriate situation, lift the veil of incorporation. This is illustrated by **Re: Bugle Press Ltd** (9) in which an offer made by a company was regarded as having been made, in substance, by the company's members. The court thereby lifted the veil of incorporation by treating the company and its members as one entity for purposes of acceptance of the offer.

(g) Section 323: Fraudulent Trading

Section 323 provides that if, in the course of the winding up of a company, it appears that any business of the company has been carried on with intent to defraud creditors of the company or creditors of any other person, or for any fraudulent purpose, the court, on the application of the official receiver or the liquidator or any creditor or contributory of the company may, if it thinks proper so to do, declare that any persons who were knowingly parties to the carrying on of the business in manner aforesaid shall be personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company as the court may direct.

The personal liability of the person concerned for the company's debts is what constitutes, in an extremely loose sense, an instance of lifting the veil of incorporation. The corresponding section of the English Companies Act is invariably cited in English company law textbooks as an instance of lifting the veil. The citation, though hallowed by English academic tradition, is logically untenable.

No Kenya case appears to have been decided under the section. However, the relevant English cases do suggest that to be "knowingly parties" to fraudulent trading under the section some positive step must have been taken by those concerned: **Re: Maidstone Building Provisions Ltd** (10).

It should be noted that, on its literal construction, Section 323 appears to be wider than Section 33 because it also covers liabilities other than debts, such as liability in tort, or damages for breach of contract. It can also be invoked against directors, members or anybody else who participated in the fraudulent trading. However, the obvious limitation of the section is that it can only be invoked on a winding up and the applicant must prove fraud.

If the liquidator applies to the court any money received is distributed to creditors generally and forms part of the general assets of the company: **Re William C Leitch Ltd** (No 2) (II). However, if a creditor applies the court may award him his actual loss or, alternatively, order the defendants to pay his actual debt: **Re: Cyona Distributors Ltd** (12).

COMMON LAW OR JUDICIAL EXCEPTIONS

Numerous English cases have been variously classified by English writers as instances of "lifting the veil of incorporation". A few of these cases are summarised below. But it should be noted that the particular judges were merely ascertaining the facts of the case before them and making the appropriate decision rather than consciously or deliberately "lifting the veil of incorporation". It is the writers who have categorised the said cases as instances of lifting the veil because the decisions in those cases appeared to them to be a modification of the principle in Salomon's case. These cases may be explained under the following headings.

(a) Agency/Trustee/Nominee

One of the ratio decidendi in **Salomon's case** was stated by Lord Macnaghten that "the company is not in law the agent of the subscribers". This proposition was affirmed by the English Court of Appeal and extended to associated companies in **Ebbw Vale Urban District Council v South Wales Traffic Area Licensing Authority** when Lord Cohen stated:

"Under the ordinary rules of law, a parent company and a subsidiary company, even a 100% subsidiary company, are distinct legal entities, and in the absence of an agency contract between the two companies, one cannot be said to be the agent of the other. That seems to me to be clearly established by **Salomon v Salomon & Co Ltd** (3).

From this statement, it can be inferred that, if a court held that a company acted in a particular instance as an agent of its holding company, the veil of incorporation would have been lifted. This is illustrated by the decision in **Firestone Tyre & Rubber Co v Llewellyn** (12) in which it was held, on the basis of the trading arrangements between the holding company and its subsidiary, that the subsidiary was the agent of the holding company.

(b) Fraud or Improper Conduct

English courts have intervened on numerous occasions and lifted the veil of incorporation in order to circumvent a fraudulent or improper design by a bunch of scheming promoters or shareholders. This is illustrated by the decisions in **Jones and Another v Lipman and Another** (13) and **Gilford Motor Co Ltd v Horne** (14). The court's order in the latter case is usually cited as an instance of lifting the veil but it should be noted that the defendant (Horne) was not a member of the company and, in principle; no veil existed between him and the company, which would have been lifted by the court. It is rather an instance of the court regarding the company as Mr Horne in another form ("alter ego").

(c) Enemy Character

A company may be regarded as an enemy if, *inter alia*, all or substantially all of its shares are held by alien enemies. This is illustrated by **Daimler Co Ltd v Continental Tyre & Rubber Co (Great Britain) Ltd** (15). Since there appears to be no Kenya case on the point, the principles summarised by Lord Parker may be useful guidance to a Kenyan who might have to determine, in a given case, whether a particular company is to be regarded as a friend or enemy of Kenya.

(d) Ratification of Corporate Acts

A number of English cases which are regarded as instances of lifting the veil are those relating to informal ratification by the members of acts done on behalf of the company. In each of these cases the court regarded a decision of the members as the decision of the company itself and thereby lifted the veil of incorporation. This is illustrated by **Re: Duomatic Ltd** (16) and **Re: Express Engineering Works Ltd** (17).

(e) Group Enterprises

Numerous cases have been decided by English courts the general tenor of which is to regard a subsidiary and its holding company as one entity. There is no basic principle governing the lifting of the veil in these instances and each decision was based on the facts of the particular case. Examples are **Harold Holds worth & Co Ltd v Caddies** (18), **Hellenic and General Trust Ltd** (19) and **DHN Food Distributors v London**

Borough of Tower Hamlets (20).

(f) Determination of Residence

Like an individual, a company has a residence where it carries on business and keeps on house. To ascertain a company's residence entails lifting the veil of incorporation. This is because a company resides in the country in which its affairs are controlled and managed from. In **DeBeers Consolidated Mines td. V Howe,** the court was emphatic that a company's residence is the country in which its central management and control actually abides.

FORMS OF BUSINESS ORGANISATIONS

- **Sole proprietorship** also sole trader- one man business
- **Partnership** - business consisting of between two to 20 people owned business
- **Company-** A legal person has duties and rights
- **Cooperative –** "Harambee" (Pooling resources)M

A business is any activity carried on for the purpose of making a profit. A business may include the following activities:

- Commercial e.g. running a shop or kiosk
- Agricultural e.g. farming
- Direct services e.g. barber, tailor

There are four main forms of business associations in Kenya, though there may be others in existences, which are beyond the scope of this book. These forms are:

- Sole proprietorship/sole trader
- Partnership
- Companies
- Cooperative

. **SOLE TRADER**

This business is owned and controlled by one person. The owner is in complete control and thus receives all profits and suffers all losses. It's very easy to start as all that one needs is capital and a trading license obtained from the relevant local authority. This form of business is found in retail trade and service industries such as hair cutting, plumbing, painting, kiosks, and vegetables among others.

ADVANTAGES

1. Owner receives all profits and is in complete control of the business
2. It has no major legal and administrative formalities in starting as all one requires is a trading license
3. A sole trader is his own master and thus makes all decisions, he does not have to consult another person, which tends to delay decision making in other business entities.

DISADVANTAGES

1. Owner has to provide all the capital
2. Owner bears and suffers all the losses
3. Owner has to work for long hours to increase profits and this in the long run affects his health
4. There is no scope in sharing ideas for the improvement of the business

PARTNERSHIP

This is a business is owned by at least two people or more but not more than 20 people. Section 3 (1) of the Partnership Act defines a Partnership as the relationship, which subsists between

persons carrying on a business in common with a view to make a profit.
Under Kenyan law there are two types of Partnerships, namely General and Limited. The General partnership operates quite similarly to a sole trader but in a Limited partnership the liability of the partners is limited. A partnership deed regulates the relationships among the partners.

ADVANTAGES

1. Partners provide capital on terms agreed. They share the net profit or bear the losses in proportions as set out in the partnership agreement
2. More capital is available and there is a scope of expanding business
3. Sharing of ideas by the partners leads to growth and improvement of business

DISADVANTAGES

1. Disagreement among partners sometimes can ruin the business
2. Business may stop temporarily after death of one of the partners.

COOPERATIVE SOCIETIES

This is an association of people who come together with a common objective. It is a form of self-help organisation. It's formed by at least 10 people and there is no maximum membership is open to any number of people required to start a cooperative society. Members hold shares in the society

STRUCTUAL FRAMEWORK OF THE COOPERATIVE MOVEMENT IN KENYA

The structural framework of the cooperative is organised in a four-tier system consisting of:

• The Primary this has been defined as a cooperative society whose membership is restricted to individual persons. Examples include

1. Harambee Cooperative Savings and Credit Society Limited, formed by the employees of the Office of the President
2. Afya Cooperative Savings and Credit Society Limited, formed by employees of the Ministry of Health

• The secondary this is a cooperative whose membership comprises Primary societies.

• The National Cooperative Movement (NACOS) The NACCOS offer specialised services to their affiliates.

The services include insurance and banking currently there are nine NACCOS, namely:

• Cooperative Bank of Kenya
• Kenya Union of Savings and Credit Cooperative Limited (KUSCCO)
• National Housing cooperative union Limited (NACHU)
• Kenya Cooperative Creameries (KCC)
• Kenya Planters Cooperative Union Ltd. (KPCU)
• Kenya Farmers Cooperative Association Limited (KFA)
• Cooperative Data and Information Centre (CODIC)
• Cooperative Insurance Company Limited (CIC)
• The Apex organisation: The apex organisation in Kenya is the Kenya National Federation of Cooperatives. It is the mouthpiece for Kenyan cooperatives to preserve and propagate (both in the country and abroad) the cooperative principles and values on which the movement was founded.

The movement cuts across all sectors including finance, agriculture, livestock, housing, transport, construction and manufacturing and consumer industry. The concentration is however within agriculture and finance sectors. In the agriculture sector cooperatives are largely involved in marketing of Agricultural produce. The financial sub-sector provides savings and credit facilities to their members. Cooperatives also provide transportation, bookkeeping, stores for resale, education and training.

BENEFITS OF COOPERATIVE ORGANISATIONS

Basically cooperatives are vehicles for social economic development. They contribute to economic growth and development in many ways. The major benefits that come out of cooperative organisations can be summarised as follows:

1. Collection, transportation, processing and marketing agricultural produce.
2. Mobilisation of savings and channelling the income of individual members to specific development projects
3. Support to agricultural production through distribution of farm inputs
4. Dissemination of applied technology to members
5. Assisting in income distribution by participation through enabling large sections of the population to engage in various income generating economic activities
6. Provision of credit to members for defraying urgent expenses at affordable rates and costs
7. Creating employment directly through hiring of various cadres of staff besides providing self-employment for farmers, artisans among others.

DISTINCTION BETWEEN COMPANIES AND OTHER FORMS OF BUSINESS ORGANISATIONS

We will pay attention to the main differences between a company and a partnership. The basic differences between registered companies and partnerships are as follows:

(a) Formation

Registration is the legal pre-requisite for the formation of a registered company: Fort Hall Bakery Supply Co v Wangoe (1).

The Partnership Act does not prescribe registration as a condition precedent to partnership formation. A partnership may therefore be formed informally or, if the partners deem it prudent, in writing under a Partnership Deed or Articles.

(b) Legal Status

A registered company enjoys the legal status of a body corporate, which is conferred on it by the Companies Act.

A partnership is not a body corporate and is non-existent in the contemplation of the law. Such business as appears to be carried on by it is, in fact, carried on by the individual partners.

(c) Number of Members

A registered private company must have at least two members under section 4 of the Companies Act and a maximum of 50 members (excluding current and former employees of the company who are also its members), under section 30 of the Act. A public registered company must have at least seven members under section 4 of the Companies Act but without a prescribed upper limit. A partnership cannot consist of more than 20 partners.

(d) Transfer of Shares

Shares in a registered company are freely transferable unless the company’s articles

incorporate restrictive provisions.
A partnership has no shares as such but a partner cannot transfer his interest in the firm to a third party unless all the partners have agreed to the proposed transfer.

(e) Management

A company's members have no right to participate in the company's day-to-day management. Such management is vested in the board of directors.
Partners have the right to participate in the firm's day-to-day management since section 3 of the Partnership Act requires the business to be carried on "in common". The right of participation in the firm's management is, however not given to a partner who has limited his liability for the firm's debts.

(f) Agency

A member is not, *per se*, an agent of the company (Salomon v Salomon & Co Ltd (3). A partner is an agent of the firm because the business is carried on "in common" by the partners themselves. The Partnership Act, section 7 also expressly provides that every partner is an agent of the firm and his other partners for the purpose of the partnership.

(g) Liability of members

A company's member is not personally liable for the company's debts because, legally, they are not his debts.
A partner is personally liable for the firm's debts. This rule has been codified by section 11 of the Partnership Act, which provides that "every partner in a firm is liable jointly with the other partners for all debts and obligations of the firm incurred while he is a partner", unless the partner is a limited partner.

(h) Powers

The ultra vires doctrine limits a company's powers to the attainment of the company's objects under its memorandum of association. Partnerships are not affected by the ultra vires doctrine and partners enjoy relative freedom to diversify the firm's operations.

(i) Termination

A member's death, bankruptcy or insanity does not terminate the company's legal existence whereas a partner's death, bankruptcy or insanity may terminate the partnership unless the partnership agreement provides otherwise.

(j) Borrowing money

A company can borrow on the security of a "floating charge". A partnership cannot borrow on a "floating charge".

(k) Ownership of property

A company's property does not belong to the shareholders, either individually or collectively. Consequently, a member cannot insure the property since he has no insurable interest therein: Macaura v Northern Assurance Co (4). A firm's property is the property of the partners who can, therefore, insure it and, in the case of cash, make drawings from it.

LAW RELATING TO OTHER ORGANISATIONS

COOPERATIVES

Cooperatives in Kenya are governed by the Cooperative Societies Act Chapter 490 of the laws of Kenya enacted in 1966.They are also governed by the Cooperative Society Rules enacted in 1969.The rules provided for the following matters:
1. Registration of cooperatives and maintenance of related documents

2. Contents of by-laws and amendment procedures
3. Society membership
4. Maintenance of books
5. Services to be rendered by district cooperative unions
6. Financial control through meetings
7. Property and funds of the society
8. Arbitration

PARTNERSHIPS

The law relating to partnerships in Kenya is contained in the Partnership Act Chapter 29 of the laws of Kenya and the Limited Partnership Act chapter 30 of the laws of Kenya. The Partnership Act is based on the English Partnership Act 1890.These two statutes codify the law on partnerships in Kenya.

CHAPTER SUMMARY

There are four main forms of business associations in Kenya, though there may be others in existence, which are beyond the scope of this book. These forms are:

• Sole proprietorship/sole trader
• Partnership
• Companies
• Cooperative

The structural framework of the cooperative is organised in a four-tier system consisting of:
The primary
The secondary
The National Cooperative Movement (NACOS)
The apex organisation

The major benefits that come out of cooperative organisations can be summarised as follows:

8. Collection, transportation, processing and marketing agricultural produce.
9. Mobilisation of savings and channelling the income of individual members to specific development projects
10. Support to agricultural production through distribution of farm inputs
11. Dissemination of applied technology to members
12. Assisting in income distribution, by participation, through enabling large sections of the population to engage in various income generating economic activities.
13. Provision of credit to members for defraying urgent expenses at affordable rates and costs
14. Creating employment directly through engaging various cadres of staff besides creating self-employment for farmers, artisans among others.

The main distinction between a company and other forms of business organisations is to be found in the two fundamental principles of company law
Legal/Corporate personality
Theory of limited liability

Cooperatives in Kenya are governed by the Cooperative Societies Act Chapter 490 of the laws of Kenya enacted in 1966

The law relating to partnerships in Kenya is contained in the Partnership Act Chapter 29 of the laws of Kenya and the Limited Partnership Act Chapter 30 of the laws of Kenya

CHAPTER QUIZ

1. Name two forms of business organisations
2. What are the two fundamental principles of company law?
3. What is the maximum number of persons in a sole trader?
4. What chapter number of the laws of Kenya is the Cooperatives Societies Act?

ANSWERS TO QUIZ

1. Sole proprietorship and partnership
2. Limited liability and Legal personality
3. One (1)
4. 490

SAMPLE OF EXAM QUESTIONS

QUESTION ONE

Discuss any four forms of business associations present in Kenya today

QUESTION TWO

What are the main differences between a partnership and a company in Kenya?

QUESTION THREE

Discuss the various laws governing cooperatives and partnerships.

CHAPTER TWO
MEMBERSHIP OF A COMPANY

OBJECTIVES

By the end of this chapter, the student should be able to:

• Appreciate promoters and pre-incorporation contracts
• Describe the process of forming a company.
• Explain the memorandum and articles of association
• Describe certificate of incorporations
• Explain the legal consequences of incorporation
• Explain the doctrine of ***ultra vires***

INTRODUCTION

This chapter mainly deals with formation of a company that is the procedures that those who wish to form a company should follow in order to be incorporated. It outlines all the formalities including documents to be prepared. It later focuses on promoters who, simply put, are charged with the responsibility of ensuring all the formalities are in place.

KEY DEFINITIONS

• **Incorporated association**: An artificial person that has a legal identity
• **Limited liability:** liability of members is limited to the amounts if any unpaid on their shares
• ***Ultra vires*** - A Latin term which means beyond the contracting powers of a company
• **Articles of Association -** A document which regulates the internal affairs of a company
• **Memorandum of association** - A document which regulates the affairs of the company and outsiders
• **Natural person** - An individual/ human being
• **Artificial person** - A person created by law through the process of incorporation in other words incorporated associations.

EXAM CONTEXT

The examiner has tended to be very fond of this topic in certain years than in others. Being the topic that brings the company into existence understanding it will be crucial in understanding of the other chapters as well. Between 2000 and 2002 the examiner set many questions from this area. A brief analysis showed that the topic was being featured in the following sittings 12/01; 12/00; 07/00; 12/00; 06/12; 05/02; 06/01 (year, month)

PROMOTERS AND PRE-INCORPORATION CONTRACTS.

PROMOTERS

There is no general statutory or judicial definition of the word "promoter". This is so because the lawmakers in England as well as the English judges were of the view that a comprehensive definition of the word would be limiting, and might prevent the court from catching "the next ingenious rogue" who might be brought to the court to account for his actions as promoter. Kenya has adopted the applicable English law.

English judges have, however, described the word 'promoter' in varying terminology of which the following may be quoted:

(a) A promoter is "one who undertakes to form a company with reference to a given project and to set it going and who takes the necessary steps to accomplish that purpose" (per Cockburn, J): **Twycross v Grant**.

(b) "The term 'promoter' is a term not of law, but of business, usefully summing up in a single word a number of business operations familiar to the commercial world by which a company is generally brought into existence", (per Bowen, J): **Whaley Bridge Calico Printing Co v Green**.

It should be noted that Section 45 (5) of the Companies Act does not contain a general definition of 'promoter'. It merely defines the word for purposes of sub-section (1) of Section 45 by excluding from the category of promoters persons who give professional services in connection with the formation of a company.

The answer to the question "who is a 'promoter?' must, therefore, depend on the facts of a particular case.

Legal Status

A promoter is not an agent of the company he promotes as it does not exist and at common law one cannot be an agent of a non-existent principal. A promoter is not a trustee of the company in formation as it does not exist However, the English courts have held that he stands in a fiduciary relationship to the company he promotes, just as an agent stands in a fiduciary relationship to his principal: In **Erlanger v New Sombrero Phosphates company limited** Lord Cairns stated “they stand in my opinion in a fiduciary position they have in their hands the moulding and creation of a company.” This is an equitable relationship based on trust, confidence and good faith. It imposes on promoters certain equitable obligations.

Duties/obligations of promoters

A promoter’s duties fall into two main categories:

- Fiduciary
- General/common aw duties

Fiduciary duties

1. Bona fide - Promoters are bound to act in good faith for the benefit of the company in formation. Their acts must be guided by the principle of utmost fairness.
2. Proper accounting: - A promoter is bound to explain the application of money or assets coming to his hands from the date he becomes a promoter. The account must be complete and honest.
3. Disclosure: - As a fiduciary promoter must avoid conflict of interest by disclosing any personal interest in contracts made on behalf of the company in formation. The disclosure may be made to an independent board of directors or to all members in the prospectus. Any secret profit made without disclosure must be accounted to the company. If a promoter makes a secret profit without disclosure the company is entitled to rescind the contract or sue for the recovery of the profit.

General/common law duties

1. To determine and settle the company’s name
2. To prepare the constitutive and other documents necessary for incorporation
3. To cause registration of the company
4. To secure the services of directors
5. To meet the preliminary expenses
6. To ensure that the company in formation has an independent board of directors
7. To prepare the prospectus, if any
8. To acquire the assets for the use by the company
9. To enter into business transactions on behalf of the company.

PRE-INCORPORATION CONTRACTS

A pre-incorporated contract is an agreement that is entered into, usually by a promoter or promoters, on behalf of a company at a time when the company’s formation has not been completed by its registration. As a general rule, a re–incorporation contract is generally unenforceable. Few cases have been contested in English courts regarding the effect of such agreements. The following rules were enunciated by the judges in the course of deciding the said cases:

1. Before incorporation a company has no legal existence it can’t contract or have agents (it was so held in **Kelner v Baxter)**
2. At common law a person who purports to contract as an agent but who at the time has no principle is personally liable on the contract. This is necessary to give effect to the contract. In **Kelner v Baxter,** it was held that where a contract is signed by one who professes to be signing as an agent but who has no principle existing at the time the contract would altogether be inoperative unless made binding upon the person who signed it. A stranger cannot by a subsequent ratification relieve him from the responsibility.

3. At common law, a contract purporting to have been entered into by or with a nonexistent person is void. For a contract to exist there must be at least two parties.
4. At common law a company can't, after incorporation, ratify a pre-incorporation contract, this is because it could not have entered into the contract before it was formed. It was so held In **Price v Kelsal.**
5. At common aw the mere adoption or confirmation by directors of a re-incorporation contract creates no contractual relationship between the company and the other party
6. At common law, a pre-incorporation is enforceable by or against the company if after incorporation, the company enters into a new contract similar to the previous agreement. The new contract may be express or implied from the conduct of the company when incorporated.

REMUNERATION OF PROMOTERS

A promoter is not entitled to remuneration for incorporating a company nor is he entitled to recover the expenses incurred in the process. This is because there is no contractual relationship between him and the company hence the company could not have contracted for the services. However, in practise the articles provide for the recovery of the expenses. For instance Article 80 provides that the directors may recover the expenses of incorporating the company. This article is unenforceable by a promoter by reason of Section 22 of the Act. However, promoters may be rewarded in other ways:
1. Upon disclosure, the promoter may sell the undertaking to the company at a profit.
2. Upon disclosure, a promoter may sell an undertaking to the company in return for fully paid shares.
3. A promoter may facilitate a transaction between a third party and the company for a commission, which must be disclosed.
4. A promoter may be afforded the option to take up extra shares at their par value after the market price has risen.
5. Traditional promoters have been rewarded by being offered deferred or founders or management shares,
6. A promoter may be appointed one of the first directors

PROCESS OF FORMING A COMPANY

A. RESERVATION OF NAME

Under Section 19(1) of the Act, the registrar may on written application reserve a name ending the registration or change of name of a company .The name is reserved for 30 days at first instance during which time its unavailable to other persons. However, the registrar is empowered to extend the reservation by any number of days not exceeding thirty. Under Section 19 (2), the registrar can't reserve a name or register a company by a name, which in his opinion is undesirable.

B. PREPARATION OF CONSTITUTIVE AND OTHER DOCUMENTS

To facilitate company registration the following documents must be prepared:

(i) Memorandum of Association

Section 2 (1) of the Companies Act provides Memorandum means Memorandum of Association of a company as originally framed or as altered from time to time. This is the primary document for purposes of incorporation. It's one of the constitutive documents and must be prepared in all cases. It's the company's charter or external constitution. It regulates the relations between the company and third parties. Its contents include:

• Name of the company
• Objects
• Capital
• Liability
• Association
• Particulars of subscribers
• Date

The memorandum of a company may be limited by shares or by guarantee must state that the liability of the company's members is limited. The memorandum of a company limited by guarantee shall also state the amount "guaranteed" by each member of the company.

(ii) Articles of Association

This document contains the regulations for management of a company. Under section 2(1) of the Companies Act, Article means Articles of association of a company as originally framed or as altered by special resolution including so far as they apply to the company the regulations contained in Table A of the First schedule to the Act. Table A is a sample of the articles of a company limited by shares.

If the proposed company is to be limited by shares, the promoters need not deliver it for registration. The provisions of Part I of Table A in the First Schedule to the Act will be automatically applicable to the company.

The Articles of Association is thus a constitutive document that contains the rules of regulation. It contains the rules of internal management hence it is the internal constitution of the company. It regulates the relations between the company and its members.

(iii) Statement of the Nominal Share Capital

This statement is delivered for taxation purposes pursuant to Section 39 of the Stamp Duty Act. It sets out the name of the company and the capital with which the company purposes to be registered. It facilitates assessment and payment of duty for the purpose of incorporation.

(iv) Declaration of Compliance (Form No 208)

Form No 208, when duly completed and signed, constitutes the statutory declaration by the advocate engaged in the formation of the proposed company, or by the person named in the articles as a director or secretary of the company, that all the requirements of the Companies Act in respect of matters precedent to the registration of the company and incidental thereto have been complied with.

NOTE

The documents identified here in below must in law be delivered to the registrar within 14 days after registration of the company but which in practice must accompany the constitutive documents.

(v) Consent to act as director (Form No 209)

Under Section 182 (1) any person who has been appointed director must deliver to the registrar for registration his written consent to act as such; which must be signed by him in person or by an agent authorised in writing. This is a personal commitment by the director to act as such.

(vi) List of persons who have consented to be directors (Form No 210)

This form, when duly completed and signed, constitutes the statutory list of persons who have given their individual consents. It is to be delivered for registration only if the prospective directors have been appointed by the articles delivered for registration in lieu of Table A, or as complementary thereto. The document sets out:

- The names of directors
- Their postal addresses
- Occupation
- Date of birth
- Other directorships, if any

These particulars enable the registrar to ascertain whether the persons qualify as directors.

C. STAMPING OF DOCUMENTS

The memorandum, articles and statement of nominal capital must be delivered for stamping i.e. payment of the tax payable for the purposes of incorporation. On payment, the duty imprint is fixed on the documents.

D. PRESENTATION OF DOCUMENTS TO THE REGISTRAR

Under Section 15 of the Companies' Act the constitutive and other documents must be lodged with the registrar for registration of the company. The registrar must satisfy himself that the documents have been reared in accordance with the law.

E. REGISTRATION OF THE COMPANY AND ISSUE OF CERTIFICATION OF INCORPORATION

Under Section 16 (1), if the registrar is satisfied with the documentation, he registers the memorandum and issues certificate of incorporation under his name and seal. Thus certifying that the company is duly incorporated. Under Section 16 (2) from the date of incorporation mentioned in the certificate of incorporation, the subscribers to the memorandum and other persons who become members are a body corporate.

THE MEMORANDUM OF ASSOCIATION

Definition

In relation to companies registered under the Companies Act, a Memorandum of Association was judicially defined by Lord Cairns in **Ashbury Railway Carriage Co Ltd v Riche** as "the charter" which "defines the limitation of the powers of a company to be established under the Act".

Contents

The contents of a Memorandum of Association are prescribed by Section 5 of the Companies Act
comprise the following six clauses:

(a) Name clause
(b) Registered office clause
(c) Objects clause
(d) Limitation of liability clause
(e) Capital clause
(f) Association clause

The "Association clause" is not prescribed by Section 5 but is mentioned as one of the clauses in the first Schedule to the Act.

Statutory Form

Section 14 of the Act provides that the form of the Memorandum of Association of a company that is limited by shares shall be in accordance with the form set out in particular form.

FORM OF MEMORANDUM OF ASSOCIATION OF A COMPANY

LIMITED BY SHARES

1st — The name of the company is "The Lake Victoria Steam Packet Company Limited".
2nd — The registered office of the company will be situate in Kenya.
3rd — The objects for which the company is established are, "the conveyance of passengers and goods in ships or boats between such places as the company may from time to time determine, and the doing all such other things as are incidental or conducive to the attainment of the above object".
4th — The liability of the members is limited.
5th — The share capital of the company is two hundred thousand shillings divided into one thousand shares of two hundred shillings each.

We, the several persons whose names and addresses are subscribed, are desirous of being formed into a company, in pursue of this memorandum of association, and we respectively agree to take the number of shares in the capital of the company set opposite our respective names.

Names, Postal Addresses, and Number of shares
Signature of subscriber Taken by each Subscriber
Occupation of Subscribers

1
2
3
4
5
6
7

Total Shares taken

Dated the .... day of ...., 19.....

Witness to the above signatures

Table B is taken from the English Companies Act 1862 and has been modified in practice, especially as regards the 3rd clause.

THE NAME CLAUSE

Choice of Name

The promoters of a proposed company have freedom to choose its name but the freedom is limited by section 19 (2) of the Act, which provides that a proposed name must not, in the opinion of the registrar, be undesirable. The registrar of companies has not issued a circular explaining the criteria he is likely to use when deciding, in a particular case, whether a proposed name is undesirable under the section. However, it might be relevant to note that the registrar of English companies, pursuant to his powers under the corresponding section of the English Companies Act 1948, issued Practice Note No C 186 in which he stated that he would normally regard a proposed name as undesirable if:

i. It is too similar to the name of an existing company.
ii. It is misleading, for example, if the name of a company likely to have small resources suggests that it is going to trade on a great scale over a wide field.
iii. It suggests some connection with the crown or members of the Royal Family or royal patronage, including names containing such words as "Royal", "King", "Queen", "Princess" and "Crown".
iv. It suggests connection with a government department or any municipality or other local authority or any body incorporated by Royal Charter or by statute or with the government

of any part of the Commonwealth or of any foreign country.
v. It contains the words “British”, unless the undertaking is British-controlled and entirely or almost entirely British-owned and is also of substantial size and importance in its particular field of business.
vi. It includes “Imperial”, “Commonwealth”, “National”, “International”, “Corporation”, “Cooperative”,
“Building Society”, “Bank”, “Bankers”, “Banking”, “Investment Trust”, or
“Trust”, unless the circumstances justify the inclusion.
vii. It includes a surname, which is not that of a proposed director, unless the circumstances justify the inclusion.
viii. It includes words, which might be trademarks, unless a trade mark clearance has been obtained.
It is probably that the registrar of Companies in Kenya is guided by the above rules, modified *mutatis mutandis*, when deciding on the desirability of any proposed name.

Reservation of Name

To obviate the risk of choosing a name that ultimately turns out to be undesirable, the promoters should enquire from the registrar whether the name they intend to give the company is “too like” that of a company already in the register of companies. After obtaining confirmation that the name is a registerable one they should immediately make a written application for its reservation under section 19 (1) (a) of the Act. Any such reservation shall remain in force for a period of 30 days or such longer period, not exceeding 60 days, as the registrar may, for special reasons, allow. No other company shall be entitled to be registered with the reserved name.
These statutory provisions regarding the choice of a company’s name are intended to confer, on the company, legal monopoly of its name. Because it lacks physical attributes, which could assist its customers to differentiate it from another company with a similar name, a company can only rely on the legal monopoly of its name as its ultimate protection against what might constitute unfair instances of passing-off. They also avoid a situation in which two or more companies use one name with the resultant problem of identifying the company that is the contracting party in a commercial transaction.

Name to end with the word “Limited”

Section 5(1)(a) provides that the word “limited” must be the last word of the name of a company which is to be limited by shares or by guarantee. In **Durham Fancy Goods Ltd v Michael Jackson (Fancy Goods) Ltd** Donaldson, J, it is stated:
“The word “Limited” is included in a company’s name by way of “description” and not identification.
Accordingly, a generally accepted abbreviation will serve this purpose as well as the word in full. The rest of the name, by contrast, serves as a means of identification”.
The use of the mystic word “limited’ as the last word of a company’s name is explicable only in the context of the historical evolution of English Company law. It was prescribed for the first time for English companies in 1856 by the Joint Stock Companies Act of that year and, in the words of Professor Gower, “was intended to act as a red flag warning the public of the dangers which they ran if they had dealings with the dangerous new invention”. A member of the public dealing with a business organisation whose name ended with “ltd” was to be made aware that he was not dealing with a partnership and so could only blame himself if he burnt his fingers in the process. Its function may be likened to that of the ring on a married person’s finger.

Power to dispense with the word “Limited”

Although section 5 provides that the last word of the name of a limited company must be "limited", this would not be so if the Minister empowers the company to dispense with it. The Minister would do so "by licence" if he is satisfied that an association about to be formed as a limited company is to be formed for promoting commerce, art, science, religion, charity or any other useful object, and it is intended that its profits, if any, or other income would be used in promoting its objects and the payment of any dividends to the association's members is prohibited.

An existing registered company may obtain a licence to make, by special resolution, a change in its name so as to omit the word "Limited". This can be done only after proving, *inter alia*, that the company is formed to promote charity and is prohibited from paying dividends to its members.

A licence may be granted on such conditions as the Minister thinks fit and may, upon the recommendation of the registrar, be revoked by him subject to the company's right to be heard in opposition to the revocation. A company granted exemption under section 21 of the Act is also exempt from the requirements of section.109 (1) which relate to the publication of the company's name.

Change of Name

A company's name may be changed voluntarily or compulsorily

(a) Voluntary Change

A company's name may be changed voluntarily:

i. Under section 20 (1) if a special resolution is passed by the company for that purpose after obtaining the written approval of the registrar. The registrar's approval is required to ensure that he does not later on reject the proposed name on the ground that it is undesirable.

ii. Under section 20(2) if the name was inadvertently registered by a name which, in the opinion of the registrar, is too like the name by which a company in existence is previously registered. No particular type of resolution is prescribed by the section and the change may, therefore, be made by ordinary resolution.

Although the section does not make it mandatory for the company to change its name, it is advisable for the company to take immediate steps to effect the change as soon as it becomes aware of the situation. Any delay entails the risk of a passing-off action being instituted against the company.

iii. Under Section 21(2) if the Minister, by licence, authorises a company to make a change in its name. The change has to be made by special resolution so as to omit the word "limited" from the company's name.

(b) Compulsory Change

Section 20(2) of the Act provides that within six months of registration under a particular name, the registrar may direct a change in name if, in his opinion, the name is "too like" that of a preexisting company. In the event of such direction, the change shall be made within a period of six weeks from the date of the direction or such longer period as he may think fit to allow. A change of name under this section may be made by ordinary resolution.

Failure to comply with the registrar's directive is an offence punishable by a fine not exceeding

Kshs.100 for every day during which the default continues.
After a company changes its name under any of the above provisions, it shall give to the registrar notice within 14 days. Upon receipt of the notice, the registrar shall -
i. Enter the new name on the register in place of the former name,
ii. Issue to the company a certificate of change of name
iii. Publish the change of name in the Kenya Gazette.
Where a company changes its name either voluntarily or compulsorily, the change will not affect any of its rights or obligations or render defective any legal proceedings by or against it, and any such proceedings may be continued or commenced against it by its new name.
Publication of Name
Section 109(1) requires every company (except one exempted under section 21):
(a) To paint or affix its name in a conspicuous position on the outside of every office or place in which its business is carried on and to keep it so painted or affixed;
(b) To mention its name on all letters, notices, official publications, bills of exchange, promissory notes, endorsements, cheques, bills of parcels, orders, invoices, receipts and letters of credit of the company; and
(c) To engrave its name on its seal, this shall be in the form of an embossed metal die.
If a company does not paint or affix its name as prescribed, the company and every officer in default are liable to a fine not exceeding one hundred shillings and if the company does not keep its name painted or affixed as prescribed, the company and the officer in default shall be liable to a default fine.
In the event of failure to comply with (b) or (c) above, the company and the officer responsible shall be liable to a fine not exceeding Kshs.1000 and the officer may be made personally liable to any creditor who has relied on the document, if the company fails to pay. This personal liability has been explained in paragraph 1.10.1(b) above, under "lifting the veil of incorporation".
Business Names
If a company has a place of business in Kenya and carries on business under a business name which does not consist of its corporate name without any addition, the company must, within 28 days after commencing business under the business name, submit to the registrar of business names a statement, called the Statement of Particulars, which contains the following particulars-
(a) The business name.
(b) The general nature of the business.
(c) The full address of the principal place of business and the postal address of the company.
(d) The full address of every other place of business.
(e) The company's corporate name and registered and principal office.
(f) The date of the commencement of business.
Changes in the registered particulars (other than (e) and (f)) must be notified on the appropriate form within 28 days after such change.
If there is a default in registration, the persons in default are liable to a fine and, unless the court gives relief, the rights of the defaulter in relation to the business in question are unenforceable by the defaulter by action: Registration of Business Names Act, section10 - 11.
Restricted Names
Section 17(1) of the Registration of Business Names Act provides that no company shall

be registered under a business name:

(a) Which contains any word which, in the opinion of the registrar, is likely to mislead the public as to the nationality, race, or religion of the person by whom the business is wholly or mainly owned or controlled;

(b) Which includes any of the words "Imperial", "Royal", "Crown", "Empire", "Government", "Municipal" or any other word, which imports or suggests that the business enjoys the Queen's patronage or the patronage of any member of the Royal Family or of the government;

(c) Which includes the word "Co-operative" or its equivalent in any other language or any abbreviation thereof, or

(d) Which is identical with or is similar to that of a business or corporation existing, or is already registered under the Act or under the Companies Act, if in the opinion of the registrar, such registration would be likely to mislead the public.

Change of Business Name

Section 17(4) of the Registration of Business Names Act provides that if -

(a) Any company is, through inadvertence or otherwise, registered under a business name under which registration under the Act ought to have been refused; or

(b) Any change of ownership of a business occurs as a result of which a company carrying on a business under a business name, which, on an application for registration under the Act, ought to have been refused, the registrar shall, by notice in writing, require the company to change such business name within a time specified in the notice.

The registrar is empowered to cancel the registered business name if the company fails to change it after he directed it to do so.

Prohibition

Section 18 of the Registration of Business Names Act provides that the registration of a company's business name under the Act shall not be construed as authorising the use of a business name if, apart from such registration, the use thereof could be prohibited.

Publication of True Names

Section 23(1) of the Registration of Business Names Act provides that a company using a business name distinct from its corporate name must disclose its corporate name in all trade circulars and business letters on or in which the business name appears and which are issued or sent by the company to any person. Failure to comply with this provision renders the company guilty of an offence punishable by a fine not exceeding Kshs.1000.

THE REGISTERED OFFICE CLAUSE

Section 5(1) (b) provides that the Memorandum of Association shall state that "the registered office of the company is to be situate in Kenya". The situation of the registered office in Kenya fixes the company's nationality as Kenyan and its domicile as Kenya, though not its residence. Residence is decided by ascertaining where the company's centre of management and control is. Thus, a company may be resident in a number of countries where it has several centres of control in different countries. The residence of a company is important in connection with its liability to pay taxation to the Government of Kenya.

Function of the Registered Office

Section 107(1) provides that a company shall, as from the day on which it begins to carry on business or as from the fourteenth day after the date of its incorporation, whichever is the earlier, have a registered office and a registered postal address to which all communications and notices may be addressed. Section 108 (1) requires notice of the situation of the registered office and the registered postal address, and of any change therein, to be given within 14 days after the date of incorporation of the company or of the change, as the case may be, to the registrar for registration.

Failure to comply with the requirements of these sections renders the company, and every officer of the company who is in default, liable to a default fine.

The primary function of the registered office is to act as the company's official address. It provides a convenient place where legal documents, notices, and other communications can be served.

Section 391(1) provides that a document may be served on a company by; *inter alia*, leaving it at the registered office of the company.

The following registers and documents are also kept at the company's registered office:

i. The register of members, and if the company has one, the index of members, unless the register is made up elsewhere, in which case they can be kept where they are made up. Where the register and index (if any) are made up by an agent, they may be kept at the agent's office (Section 112 - 113).

ii. The register of directors and secretaries (Section 201 (1).

iii. The company's register of charges (if the company is a limited company) (Section105 (1).

iv. A copy of any instrument creating any charge requiring registration under Part IV of the Act (Section 104).

v. The register of debenture holders (Section 88 (1).

vi. The register of directors' interests in shares in, or debentures of, the company or associated companies (Section 196 (1).

vii. The minute books of general meetings (Section 146 (1).

The registers and documents are then subject to the following rights of inspection:

(a) The company's members are entitled to inspect them, free of charge, during business hours for at least two hours each day.

(b) Debenture holders of the company are entitled to inspect, free of charge, the register of debenture holders and, during the period beginning 14 days before the date of the company's annual general meeting and ending three days after the date of its conclusion, the register of directors' shareholding.

(c) Any member of the public is entitled to inspect the register of directors and secretaries and the register of debenture holders on payment of a prescribed fee not exceeding two shillings for each inspection.

THE OBJECTS CLAUSE

Reasons for Stating Objects

Section 5 (1) (c) requires the Memorandum of Association to state the objects of the company. The section does not, however, indicate why a company's objects have to be stated in the company's Memorandum of Association. In **Cotman v Brougham** (21) Lord Parker stated that the statement of a company's objects in its Memorandum of Association is intended to serve the following purposes:

(a) To protect subscribers who learn from it the purpose to which their money can be applied.

(b) To protect persons who deal with the company and who can infer from it the extent of the company's powers.

These propositions will become clearer after a study of the doctrine of *Ultra Vires.*

The Doctrine of *'Ultra Vires'*
Fast forward
Ø These are instances when the company acts beyond the powers in its objects clause
Ø The instances are either common law or judicial

The doctrine of *Ultra Vires* is a legal rule that was articulated by the House of Lords in the case of **Ashbury Railway, Carriage and Iron Co Ltd v Riche (22)** to the effect that, where a contract made by a company (usually by the directors on its behalf) is beyond the objects of the company as written in the company's Memorandum of Association, it is beyond the powers of the company to make the contract. The contract is void, illegal and unenforceable. Lord Cairns stated in an obiter dictum that such a contract cannot be ratified even by the unanimous consent of all the shareholders of the company. His Lordship observed that any purported ratification would mean that "the shareholders would thereby, by unanimous consent, have been attempting to do the very thing which, by Act of Parliament, they were prohibited from doing".

A company's objects are stated pursuant to the provisions of an Act of Parliament. It must therefore be deduced, for example, that a company whose object has been stated to be "gold mining" cannot engage in "fried fish" business. This is because: -

(a) Prospective investors who read the objects clause realised that the company was formed to mine gold. If they bought the company's shares they did so because they intended their money to be used in pursuance of the gold mining business. They did not give the money for any other business and the company does not have their consent to use it on any other business. If the company tries to use the money on a different venture, such as frying fish and chips, they can go to court for an injunction to restrain it from doing so.

(b) The statutory requirement that a company must state its objects in its Memorandum of Association would be rendered purposeless if, despite having stated the objects, the company was legally entitled to embark on any other activity. To prevent this happening, the courts concluded that the statement of objects would be taken to mean that what is not stated as an object cannot be pursued, or undertaken, by the company. In other words, the statutory requirement that the objects are to be stated implies that what has not been stated as an object cannot become a legitimate activity of the company.

IMPLIED POWERS

The statement of Lord Cairns in 1875 in **Ashbury Rail Co Ltd v Riche (22)** to the effect that a contract beyond the objects of the company "in the Memorandum of Association" is "beyond the powers" of the company gives the impression that a company has no legal power to do anything which is not written in the Memorandum of Association. That would be a startling proposition because, in practice, companies have to do so many things in the course of their business that if all those things were to be written down in the Memorandum of Association, the Memorandum would be such a gigantic document that nobody would print or read. It was, therefore, a welcome clarification of the legal position when, in 1880, Lord Selborne, L C, stated in **Attorney-General v Great Eastern Railway Co** that the doctrine of *Ultra Vires*, as explained in the **Ashbury** case, "ought to be reasonably, and not unreasonably, understood and applied". His Lordship then explained that it is not necessary for a company to write down in its memorandum everything that it would or could do in the course of its business because whatever may fairly be regarded as incidental to, or consequential upon, those things which have been stated in the memorandum ought not, and would not, be held by the courts to be *Ultra Vires*. The courts would regard such things as impliedly within the company's powers unless they are "expressly prohibited" by the memorandum. The range of transactions that could be encompassed within the "implied powers rule" was illustrated by Lord Buckley in 1907 when, in **Attorney - General v Mersey Railway Co**, he stated:

"To ascertain whether any particular act is *Ultra Vires* or not the (stated objects) must first be ascertained; then the special powers for effectuating those (objects) must be looked for, and then, if the act is not within either the (stated objects) as described in the memorandum, the inquiry remains whether the act is incidental to or consequential upon the (stated objects) and is a thing reasonably to be done for effectuating it ... By way of illustration, let me suppose that the (stated object) found in the Memorandum of Association of a (registered) company is to establish and carry on a hotel, and that express power is given to buy land at a particular place and to build and that as to anything further the... Memorandum of Association is silent. It is quite clear that all such acts as are reasonably necessary for effectuating that purpose are *intra vires*, such, for instance, as the purchase of furniture, and of linen, of provisions, and of wines and spirits, the hiring of servants, the payment of licences, the ownership probably of horses and carriages, the maintenance and working of an omnibus which shall attend at the railway station to take intending guests to the hotel and the like. In a large number of cases the maintenance of a garden and pleasure grounds would be *intra vires*... The maintenance of tennis lawns or of a bowling green would, in many circumstances, be legitimate. Under circumstances such as presently put, a golf links might be *intra vires*. All these and the like will without express mention be within the company's powers. Then I may instance other acts as to which it would be a question of fact in the case of the particular hotel whether it was such an act as was reasonably incidental or consequential. If, for instance, the hotel were at Bundoran or Rosapenna or elsewhere in the country it might be *intra vires* to lay out and maintain in good order a golf links or to acquire rights of fishing and to own boats and supply gullies for the purpose of fishing upon the lakes. It may be that in the particular locality, customers could only be reasonably expected or obtained by offering these attractions, and they might be as necessary as a smoking-room or a bowling green elsewhere. If the hotel in question were the Savoy Hotel in the Strand or the Great Central Hotel in the Marylebone Road, the proposition would cease to be true. So, again, if the hotel were situated in a place inaccessible unless special means of communication were provided say, at a lovely spot at the end of a Scotch Loch to which there is no road, or at a place to which there is access by road but which is not served by any coach or mail cart service it might be *intra vires* for that hotel to run a steam launch or a motor-car to bring its guests to their destination. It would in such a case be analogous to the omnibus, which the hotel in the country town sends to the railway station. The question is in each case a question of fact. Is the particular act in that case incidental to or consequential upon or reasonably necessary for effectuating the object, which the Memorandum defines?

The gist of Lord Buckley's statement, above, may be summarised as follows: The judges will not regard a transaction undertaken by a company as U*ltra Vires* merely because it is not written in the company's Memorandum of Association as one of the company's objects. They would in fact regard the transaction as *intra vires* by implication if:

i. It was reasonably incidental to any of the objects which have been written in the company's Memorandum of Association, and

ii. It was undertaken for the sole purpose of effectuating, or achieving, the written objects,