Classification of Companies under Nigerian Law: An Interrogation of the Bases.

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Abstract

The classification of companies by law is crucial for purposes of effective and efficient regulation of companies, particularly in the areas of securities trading, information disclosure, control of anti-competition practices, and several other unethical corporate behaviours. Despite this, Nigerian company law has lumped up together all categories of company with different functions and roles and regulates them under a single legal regime. This situation places heavy regulatory burden on the small and medium sized private companies. Indeed, such regulation might not be suitable to them. Using the doctrinal method, which involves the analysis and interpretation of statutes, cases and scholarly works, this article has examined classification of companies under Nigerian law to find out the bases and appropriateness of such classification particularly, in relation to the characteristics of these companies and the challenges which the different types of companies pose to regulation. The article has found that the classification is not ideal because the bases for it are not economic structures and functions of the corporate entities operating in Nigeria, and that different types of companies are regulated under a single legal regime. Therefore, this article recommends that the bases for classification of companies in Nigeria should be economic structures and functions, and not legal formula. Further, the one-man company should be given legal recognition in the companies' statute and distinct legal regimes provided to regulate the different types of companies in Nigeria.

Key words - Classification, One-man Company, Public Company, Groups, Multinationals.

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Introduction

Classification of companies is important for purposes of effective and efficient regulation of companies particularly, in the areas of securities trading, information disclosure, control of anti-competition practices, and several other unethical corporate behaviours. Under Nigerian law however, classification of companies has ignored the differing functions and roles of the various types of companies operating on the Nigerian corporate scene. In many continental European countries (except the United Kingdom), there is separate legislation for public and private companies.[1] Under Nigerian law, like that of the United Kingdom, different types of companies are lumped together and regulated under a single legal regime. Under the circumstance, small and medium sized private companies suffer regulation that was designed for large publicly owned companies as well as group and multinational companies. Relaxation of regulation in favour of small private companies is only in the area of financial disclosure. This article interrogates the bases and appropriateness of classification of companies under Nigerian law particularly, in relation to the existing corporate structures and the challenges they pose to regulation with a view to addressing the regulatory hiccups and advocating for an ideal regulatory framework.

Approaches to Classification of Companies

Different disciplines approach classification of companies from different perspectives, for example, accountants, economists and lawyers have different indices for classifying companies. Economists see companies as units of ownership and production. From the economic concept of a company, it is a firm within the structure of capitalist production and purely a method of raising capital[2]. From a legal point of view, the difficulty is directly related

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1 In the United Kingdom, unlike in many continental European countries, there is no separate legislation for public and private companies. Whereas the German *Aktiengesetz* applies to public companies and to relieve private companies of the demands of the *Aktiengesetz,* a separate and more flexible statute has been enacted for private companies (the *GmbHGesetz*), English company law deals with both types of companies in the same Act. See: Paul L Davies (ed) *Davies' and Gower's Principles of Modern Company Law* (8th edn, Sweet & Maxwell 2008), 14

2 JH Farrar and N Furey and B Hannigan, *Farrar's Company Law* (2nd Edn, Butterworths1988), 24

to the definition of a company itself. The lawyers look at companies in functional terms, that is, their differing roles and put emphasis on the particular legal forms rather than production[3]. The lawyers' attempt to equate the concept of the firm and company through the conferment of abstract legal personality on the latter leads to severe strains and tensions in legal decision making because the logic of corporate legal personality sometimes conflict with the practicability and justice of the factual situation[4].

It is submitted that the law cannot ignore all the diverse approaches as one way or the other, all the views appear in the classification of companies. Farrar, submits that "economic reasoning may sometimes afford a corrective to abuses of legal logic, even though "the purposes of classification may differ." Under such circumstances, the law should not hesitate the corrective measures as the two are not mutually exclusive.[5] The interface, for instance, although economics is concerned with a variety of purposes including analysis, explanation, prediction and evaluation in connection with making rational choice and allocation of scarce resources while the law is principally concerned with social control and regulation, a sound regulatory scheme should go on a rational basis and economics in its broadest sense supplies an instrumental approach which is compatible with the law pursuing non-economic objectives.[6]

Classification of Companies Based on Size

Firms and companies are classified by economists and lawyers in different ways. One factual classification is based on size, and using size, economists classify companies into three broad categories – the small company, the medium company; and the large company.[7]

Under the UK Companies Act 2006, a division is made on the basis of size by the Act which gives dispensations from certain accounting requirements to 'small' and 'medium-sized' companies

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3 Ibid

4 Ibid

5 Ibid

6 C Veljanovski, 'Legal Theory, Economic Analysis and the Law of Torts' in W Twining *Common Law and Legal Theory* (1986), 215, 216; JH Farrar and N Furey and B Hannigan (n2)

7 JH Farrar and N Furey and B Hannigan (n2)

and groups[8]**.** Further, the Act exempts 'very small' companies from the obligation to have their accounts audited[9], and since 1992, it has been possible for private companies in the UK to have a single member as against the former minimum number of two (2) members[10]. These companies are subject to some special rules under the Act, for example, section 3 which requires decisions taken by a single member to be in writing[11].

The criterion of size however, begs many questions relating to the criteria for measuring size. Should size be based on the amount of assets, the aggregate market value of shares, turn over or net income after tax, the return on capital or the number of shareholders and the number of employees? Each of these basis for measuring size has its own problems, for example, the use of assets gives a disproportionate prominence to capital intensive industries and consequently, sales are often taken as an index for some companies,[12] and whatever criteria are used, some companies are so large that they transcend the corporate form and the nation state. Such companies are called multinationals.[13]

Large companies participate in the market for investment capital and the market for corporate control provides ways of monitoring performance of the management of such companies as the price of the company's securities reflects many factors, but prominent among which is the market's appraisal of efficiency of management. If the price declines, particularly if it falls below asset valuation, it will attract the attention of a bidder who will feel that he can make more efficient use of the assets. These market forces all affect the relevant legal norms. Large companies are thus, essentially different from small companies in matters other than size[14]. The size classification bears little relevance on the legal regulation of various enterprises.

Farrar submits that the size and capital raising characteristic of a firm are useful starting points for legal classification since larger

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8 United Kingdom Companies Act 2006, Sections 444 and 465

9 Ibid, Section 475

10 Len Sealy and Sarah Worthington, *Cases and Materials in Company Law* (8th edn, Oxford University Press 2008), 21

11 Ibid

12 JH Farrar and N Furey and B Hannigan (n2)

13 Ibid

14 Ibid

companies usually have specialized management; separation of ownership and control; provide a market for investment capital; participate in the market for corporate control more regularly, and it is patently unjust to subject a small firm to a disclosure regime appropriate to a large company or multinational with different structural problems.[15]

In Nigeria the Companies and Allied Matters Act (CAMA)[16] defines a small company for purposes of qualifying to deliver a modified financial statement, and from the provisions of section 351 of the same Act, there are three (3) quantitative indices-turnover; participation; and level of assets. Such a company must be a self-owned and self-managed enterprise with no alien or government participation, with net assets of less than ₦1 million and turnover of less than ₦2 million. The pertinent question is whether or not Nigerian law should have used the provisions separating other companies for purposes of financial disclosure to develop distinct legal regimes for the regulation of these various sizes of companies? This question is pertinent because in strict legal theory, the fact of incorporation is presumed to convey the same status on small and large companies alike, for example, members of these sizes of companies are entitled to enjoy the privilege of limited liability. In practice however, the dangers to which creditors and third parties dealing with these various sizes are exposed are significantly different, for example, the limited liability of members effectively transfers the risk of business failure from them to the creditors. In practice this means trade creditors and involuntary creditors, since finance creditors usually take security and personal guarantees in case of small firms. In the case of firms where a large and fluctuating number of members is involved, the company has distinct advantages in organizational form[17] and the limited liability greatly facilitates capital raising from the public[18]**.** Besides, the basis of association and organization of the various sizes of companies are significantly different. Notwithstanding all these, Nigerian law seems to suggest no necessity for separate legal regime for various sizes of companies.

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15 Ibid, 17

16 CAMA 2004, Section 567(1)

17 Paul L Davies (ed.), Gower and Davies' *Principles of Modern Company Law* (8th edn Sweet & Maxwell 2008), 6

18 JH Farrar and N Furey and B Hannigan (n2), 31

Indeed, the only difference in rules applying to different types of companies appear in the provisions relating to financial disclosure[19].

Under these provisions, a private company is exempted from filing certain information relating to their financial disclosure, for example, under section 334(3) of Companies and Allied Matters Act, 2004, the financial statements of a private company need not include a statement of its accounting policies; a statement of the source and application of fund; a value added statement for the year; and a five-year financial summary. Such information is given by a public company in its financial statement. In addition, under section 350(1) of the Act, a small company may deliver modified financial statements in respect of a year.

Classification of Companies Based on Function

From a functional view point, there are three types of companies:

i. Companies formed for purposes other than the profit of their members, that is, those formed for social, charitable or quasi-charitable purposes. In this case, incorporation is merely a modern and convenient substitute for the trust.
ii. Companies formed to enable a single trader or a small body of partners to carry on a business. In these companies, incorporation is only a device for personifying the business and, normally divorcing its liability from that of its members despite the fact that the members retain control and share the profits. In such a case, the company is often a substitute for a partnership. A single trader or partner would have carried on the business without registration in the circumstances and the essence of incorporation is no more than to insulate the traders from personal liability.
iii. Companies formed in order to enable the investing public to benefit from the profits of the enterprise without taking any part in its management. This type is economically, but not numerically, the most important company. It is again a device analogous to the trust, but this time it is designed to facilitate the raising and putting to use of capital by enabling a large number of owners to entrust it to a small number of expert managers.[20]

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[19] Companies and Allied Matters Act Cap C20 LFN, 2004, Sections 334-336

[20] Paul L. Davies (ed) (8th edn, 2008) (n17), 12

Under the Companies and Allied Matters Act, 2004 the company limited by guarantee is provided for use for cases coming under the first category[21]. The company limited by shares is the framework for the second and third categories. Such a company is usually registered as private company under the second category[22] while the public company is registered under the third category[23].

Legal Classification of Companies Under the Companies and Allied Matters Act, 2004.

The companies and Allied Matters Act, 2004 adopts two basic systems of legal classification of companies, neither of which is directly concerned with size, but both of which have some bearing on the raising of capital. These are (1) by reference to the liability of the members and (2) the private and public company dichotomy. Dealing with (1), a registered company may be: (i) a company limited by shares; (ii) a company limited by guarantee; and (iii) unlimited company[24].

In a company limited by shares, a member is not liable for the company's debts beyond the amount remaining unpaid on his or her shares[25]. In a company limited by guarantee, a member is only liable to make a contribution to the assets of the company in the event of its being wound up,[26] and the total liability of a member to contribute to the assets of the company shall not be less than N10,000.00[27]. A guarantee company is however, an unsuitable framework where the primary object is to carry on a business for profit and to divide that profit among the members. Despite the availability of a guarantee company for non-profit purposes, it has a limitation in terms of its financing since it is not registered with share capital and there are no shares to be sold[28] and must either operate on the basis that it needs no long-term working capital and rely simply

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21 CAMA 2004, Section 26
22 Ibid
23 Ibid, Section 22 (2-5)
24 Ibid, Section 24
25 Ibid Section 21(1)
26 Ibid, Len Sealy and Sarah Worthington (n10), 21
27 Len Sealy and Sarah Worthington (n26)
28 CAMA 2004, Section 26 (7).

on members' subscription or resort to borrowing as a means of raising its capital[29].

Due to the limitation of the company limited by guarantee, in the United Kingdom, the Government in part 2 of the Companies (Audit, Investigations and Community Enterprise) Act, 2004[30] created a new type of company called the 'Community Interest Company' (CIC) to which provisions of the companies Act, 2006 apply subject to modifications made in the 2004 Act[31]**.** Such a company can be either a company limited by shares or by guarantee but its purposes are limited to pursuit of community interests[32]**.** Community Interests Companies (CICs) were introduced in Great Britain with the intention of making it simpler and more convenient to establish a business whose profits and assets are to be used for the benefit of the community. There is a statutory "lock" on the profits and financial assets of CICs and, where a CIC is limited by shares power to impose a "Cap," that is, statutory limit, on any dividend[33]**.** Due to the fact that distributions to members and the payment of interest on debentures are subject to a 'cap' and its assets are 'locked in', the investors have less incentive to exercise control over the company because their potential rewards are limited[34]. As such, an independent Regulator of Community Interest Companies is given potentially extensive powers of intervention in CIC's affairs under the enabling Act[35].

A limited liability company wishing to register as a CIC must be approved by the Regulator, who must be satisfied that the company meets the 'community interest' test and is not an excluded company. A company meets the community interest test if a reasonable person might consider that its activities are being carried

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29 Ibid, Section 26(2); Paul L Davies (ed) (8th edn, 2008) (n17), 10

30 UK Companies (Audit, Investigations and Community Enterprise) (C(AICE) Act 2004, Section 26(1)

31 UK Companies Act, 2006, Section 6(2)

32 Paul L Davies (ed) (8th edn, 2008) (n17), 10-11

33 Explanatory Memorandum to the Companies Act 2006 (commencement No.2, Consequential Amendments, Transitional Provisions and Savings) Order No. 1093, 2007 and The Companies Act (Unregistered Companies) Regulations No. 318, 2007 <http://www dti.gov.uk/bbf/co-act-2006/index.html> accessed 12 April, 2015.

34 Paul L Davies (ed) (8th edn, 2008) (n17), 11

35 Ibid

out for the benefit of the community[36]. Excluded companies are companies devoted to political campaigning[37]. Clearly, there is no such palliative for or alternative to a company limited by guarantee with a limitation in terms of its financing, under Nigeria law. In Nigeria therefore, such companies rely on leviations or subscriptions of its members and loans.

An unlimited company has no limit on the liability of its members. There is no limit, provided by the shares or a guarantee, on the liability of its members[38]. In other words, the members can be called upon to satisfy personally the whole of its liabilities to its creditors[39]. Under the Companies and Allied Matters Act,[40]an unlimited liability company shall be registered with share capital in order to provide working capital and to measure each member's right in the company but that capital no longer acts as a limit on liability[41]. However, in the United Kingdom, only a private company can be unlimited, a public company must be limited by shares or guarantee[42].

It is indeed curious that limited liability which is the advantage and drives entrepreneurs' decision to adopt the corporate form is forgone by the Companies and Allied Matters Act in respect of this category of company. It is little wonder that such companies are quite rare on the Nigerian corporate scene[43] and it has never been suggested that there should be separate legislation for such companies[44]. Yagba[45] argues that one way of making this category more practically attractive is to exempt it from most of the rigorous disclosure requirements of the companies Acts. The privilege of limited publicity would cut down administrative costs since in any event, the main logic of publicity is to warn creditors that only the company's assets would be available in satisfying their claims where the members have limited liability. This not being the case in

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36 Ibid, C(AICE) Act 2004, Section 26(3)
37 Len Sealy and Sarah Worthington (n10), 21; C(AICE) Act 2004, Section 35(2)
38 Ibid
39 Ibid; Paul L Davies (ed) (8th edn, 2008) (n17), 18
40 Cap C20 LFN, 2004, Section 25
41 Paul L Davies (ed) (8th edn, 2008) (n39)
42 UK Companies Act, 2006, Section 3(4)
43 TAT Yagba and BB Kanyip and SA Ekwo, *Elements of Commercial Law* (Tamaza Publishing Company Ltd, 1994), 224; Paul LDavies (ed) (8th edn, 2008) (n39)
44 Ibid
45 Ibid, 225

unlimited companies, disclosure should be limited to matters affecting members, employees, and the public interest. It is pertinent to note that while an unlimited liability company is a going concern, it is basically the same as a limited liability company because a creditor cannot directly enforce a debt against a member of such unlimited company except at insolvent liquidation.

Nevertheless, the current law does not take the view that there should be some separate legislation for unlimited companies, and this according to Davies,[46] is true in particular regard to the obligation to publish its accounts since creditors of such companies can rely on the credit of the shareholders, and the prohibition on a company acquiring its shares (which is also a potential threat to creditors who are restricted to the company's assets for satisfaction of their claims). Consequently, this form may be attractive to those shareholders who are willing to stand behind their company and for whom the advantage of privacy and flexibility of capital structure are important.

Finally, a company may be limited by shares or by guarantee by an appropriate limiting provision in the company's constitution that is, the liability is restricted by law to an amount fixed by the terms of the issue of the shares or by the company's constitutional documents. Where there is no such limiting provision on the liability of the company's members, a company is an unlimited company[47]**.** Clearly, companies under the Companies and Allied Matters Act, 2004 are classified on the basis of liability of members and on whether they have or do not have share capital. The legal question of policy is why the Act should lump together all these organizations which have nothing in common in legal and economic terms? From the foregoing, classification of companies into three by the Companies and Allied Act, may emerge two broad types of companies, either a private company or a public company[48].

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46 Paul L Davies (ed) (8th edn, 2008) (n39)

47 Len Sealy and Sarah Worthington (n10), 19-20

48 CAMA, 2004 Section 21(2)

Private and Public Companies Under the Companies and Allied Matters Act, 2004.

A private Company under the Companies and Allied Matters Act[49] is one which is stated in its memorandum of association to be a private company. This provision in the memorandum is by no means an exhaustive criterion. To qualify as a private company, the company must impose restrictions on the members' right to transfer their shares in the articles of association; it must not have a total of more than fifty (50) members (excluding *bonafide* present and past employees who are members by virtue of their employment) and it must not solicit for funds or investment from the public[50].

A public company under the Act is any company other than a private company and its memorandum must state the fact that it is a public company[51]. This is the converse of United Kingdom Companies legislation which defines both 'private' and 'public' companies in the same section in the following terms: "a 'private company" is any company that is not a public company; and a 'pubic company' is a company with a certificate of incorporation that states it as a public company, and has complied with all the necessary provisions of the Act (or Former Companies Acts) as regards registration or re-registration as a public company"[52].

Farrar[53] argues that the public/private company dichotomy was introduced by the Companies Act 1907 and the introduction of the private company was almost by accident. Originally, the Loreburn Committee had simply intended it as a basis of exemption from the statement in lieu of prospectus but in the House of Lords it was successfully proposed that it should be exempted from filing a balance sheet. Citing Schmitthoff[54], Farrar argued that English Law did not, like German law, recognize the private company as an institution, *sui generis* but simply as a species of the genus, the limited company. The basis of the difference was restrictions on offers to the public of its shares, share transfer and the number of shareholders. Thus, to some extent, size entered into the

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49 Ibid, Section 22(1)

50 Ibid, Section 22(2-5); TAT Yagba and BB Kanyip and SA Ekwo (n43), 222

51 Ibid, Section 24

52 UK Companies Act, 2006, Section 4; Len Sealy and Sarah Worthington (n10), 20

53 JH Farrar and N Furey and B Hannigan (n17), 31

54 CM Schmitthoff, 'How the English Discovered the Private Company' in P Zonderland (ed) *Quo Vadis, Jus Societatum* (1972), 183.

classification- the private company was intended for small businesses, the public company for large businesses. However, the method of raising capital was fundamental to the classification[55].

The distinction between private and public companies is said to be important not just for the obvious fact that companies which do not offer their shares to the public need not be concerned with the rules governing the offer process. Rather, whether a company is public or private is taken more generally as an indication of the social and economic importance of the company, so that the public company is more tightly regulated than the private company in a number of ways which do not directly concern the offering of shares to the public[56]. The law assumes a closer relationship between the members in a private company than in a public company and so private companies commonly restrict in the articles of association the membership of their company to those approved by the directors[57]. In essence, if a member wishes to leave the company by selling his shares or a member has died, the directors have a say in who replaces him, if any one[58]. There may also be a pre-emption clause in the articles which means that if a member wishes to sell his shares he must first offer the shares to the other members[59].

Private companies can also adopt an elective regime which is designed to recognize that often in private companies the directors and the members of the company are one and the same and so requirements for meetings, timing of meetings and laying of accounts can be suspended to streamline the operation of the private company[60]. Under English Law, these companies are subject to some special rules which allow informal decision making process. For example, section 357 of U.K. Companies Act, 2006 which requires decisions taken by the single member of a private company to be recorded in writing[61]. This is a relaxation of the regulation regime as it dispenses with the requirement of company meetings and procedure for public companies and makes decisions in a private company informal. Private companies are barred from inviting the

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55 JH Farrar and N Furey and B Hannigan (n53)
56 Paul L Davies (ed) (8th edn, 2008) (n17), 14
57 Alan Dignam and John Lowry, *Company Law* (4th edn, Oxford University Press 2006), 8
58 Ibid
59 Ibid
60 Ibid
61 Ibid, Len Sealy and Sarah Worthington (n10), 21

public to buy their shares, but they also have no real minimum capital requirements[62]. Under the Companies and Allied Matters Act[63] too, in the case of a private company, a written resolution signed by all the members entitled to attend and vote shall be as valid and effective as if passed in a general meeting.

Although this translates into unanimity of corporate decision making which might be considered impracticable for a private company with membership running up to fifty (50) due to the fact that not every member may give his assent, the provision remains the law until it is amended. This is more so that the legislative intent behind the provision is to remove the procedural obstacles to decision making in private companies which are mostly, owner-managed and controlled. Besides, most private companies are closely held family-controlled companies and their membership do not rise up to the statutory maximum of fifty members. Such companies often tend towards informality and provided all the members know about and agree to a decision which is within the capacity of the company, it is binding even though no meeting is held to pass the resolution.[64] Section 234 of CAMA is a mere endorsement of this informality.

Public companies can secure investment from the public. In offering their shares to the public, they must issue a prospectus giving a detailed and accurate description of the companies plans[65]. Further, because members of the general public are involved and need to be protected, the initial capital requirements for the public company are more onerous than for a private one. In the U.K, there is no minimum capital requirement for a private company while the minimum capital requirement for a public company is €50,000[66]. In Nigeria, the minimum capital requirement for a private company is N10,000 while that for a public company is N500,000[67].

The distinction between private and public companies is embodied in the Companies and Allied Matters Act[68]. Yagba submits

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62 Ibid

63 Cap C20 LFN 2004, Section 234

64 JH Farrar and N Furey and B Hannigan (n2), 295; TAT Yagba and BB Kanyip and SA Ekwo (n43), 259

65 Investments & Securities Act, No. 29, 2007, Sections, 71,72, 73, 77, 80-87; Alan Dignam and John Lowry (n57)

66 U.K. Companies Act, 2006, Sections 761 & 763

67 CAMA, 2004 Section 27(2)(a)

68 Ibid, Section 22(2-5)

that the restrictions placed on the private company under the Act emphasize that the private company is merely designed to afford small traders or families the advantages of corporate personality and limited liability so that they may carry on businesses on a status higher than that of a business name.[69] Such a company is therefore not a means for achieving the ambitious objectives or elaborate structural organization of a public company[70].

The clear distinction between private and public companies therefore, rests on the fact that the latter are not subject to the limitations of the former under section 22 relating to the maximum number of members and the marketability of the company's shares and debentures[71]. The restriction on public solicitation of investment in a private company limits its access to capital for expansion and preserves the intimacy of the original corporators or their families[72]. However, under the new regime of accounting and disclosure under the companies and Allied Matters Act[73], the most significant distinction between private and public companies relates to the relaxation of the rules in favourr of private companies from preparing and filing inter alia, a statement of Accounting Policies; a Statement of the Source and Application of Funds (which gives information on generation and utilization of funds by the company during the year); the Value Added Statement (which reports on the wealth created by the company during the year and its distribution among various interest groups such as employees, the government, creditors, proprietors and the company) and the five year financial summary. It is only in the area of accounts, audit and financial disclosure that separate rules are made for private companies. Barring this, Nigerian law continues to treat and regulate private and public companies as different species of the same genus,[74] Limited liability Company. The same requirement of two members is now stipulated for the formation of either type of company[75]; each must have at least two directors[76]. Each must keep the various registers

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69 TAT Yagba and BB Kanyip and SA Ekwo (n43), 222-223

70 Ibid

71 Ibid, 223

72 Ibid

73 Cap C20 LFN, 2004, Section 334(3)

74 TAT Yagba and BB Kanyip and SA Ekwo (n43), 223; JH Farrar and N Furey and B Hannigan (n2), 31

75 CAMA 2004, Section 18

76 Ibid, Section 246

and documents required to be maintained at its office by the Act and also file or register resolutions, returns or particulars stipulated by the Act with the Corporate Affairs Commission[77].

English company law, unlike that of most other European countries, deals with both public and private companies in the same Act[78]. This is the approach adopted by the Companies and Allied Matters Act, 2004 which has embedded both companies. Many continental European countries have however, demonstrated ambitious regulatory goals for public companies in separate legislation. For example, German public companies have a two-tier board structure – a supervisory board (*Aufsichtsrat*) to control the basic policy of the company and a management or executive board (*Vorstand*) to manage its operations. The supervisory board appoints the management or executive board but otherwise the two are distinct and a member of one may not be a member of the other.[79] *Aktiengesetz* (the German Code of Company Law), that applies exclusively to public companies, divides the board of directors into two bodies- the supervisory board and the management board- and deals in some detail with the allocation of functions between them and the mode of appointment of their members. Other legislation requires the mandatory presence of employee representatives on the boards of large public companies, but this applies also to boards of large private companies[80]. By contrast, the British and Nigerian Companies Acts say little about what the board is to do or how members are to be appointed, and certainly do not require the creation of separate supervisory and management boards[81]. These matters are left to be decided by each company itself in its constitution though both Acts contain important provisions enabling an ordinary majority of the shareholders to remove any director at anytime[82]. As a result, different sizes and types of company can

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77 TAT Yagba and BB Kanyip and SA Ekwo (n43), 223

78 Paul L Davies, (ed) (8th edn, 2008) (n17), 14; Len Sealy and Sarah Worthington (n10), 20

79 Paul L Davies (ed), *Gower's Principles of Modern Company Law* (6th edn, Sweet & Maxwell 1997), 64; Tom Hadden, *Company Law and Capitalism* (2nd edn, Weidenfeld & Nicolson 1977), 448; COO Oyediran, 'Achieving Transparency in Corporate Governance: Issues, Modalities and Challenges' in O Alo (ed.) *Issues in Corporate Governance* (FITC, 2003), 63

80 Ibid

81 Paul L Davies (ed) (8th edn, 2008) (n17), 14

82 U.K. Companies Act, 2006, Section 168 and CAMA, 2004, Section 262

adjust these matters to suit their own particular situation, whereas in Germany to relieve private companies of the demands of the *Aktiengesetz* has been seen to require the enactment of a separate and more flexible statute for private companies – *Gesellschaft Mit beschränkter Haftung* (*GmbH Gesetz,* meaning private company)[83].

In Nigeria, the Securities and Exchange Commission (SEC) Code of Corporate Governance 2011 which was in existence before the Nigerian Code of Corporate Governance (NCCG) 2018 was issued by the Financial Reporting Council of Nigeria (FRCN), and the NCCG 2018 have recognized the importance of board composition in companies. The NCCG 2018 has indeed made specifications for board structure and composition but this is with regard to only public companies.[84] This does not in any way solve the problem of lumping together private and widely-held public companies with different roles and functions, and regulating under a single regime.

The question of whether regulation intended for public companies should be applied, either in a modified form or at all, to private companies received the attention of the Company Law Review in the United Kingdom which said in its Final Report that "small and medium-sized companies suffer regulation that was designed for large, publicly owned companies[85]. However, it did not introduce a separate Act for private companies, but rather a review, which it carried out, of the provisions applying to private companies to see which could be removed from them or applied only in a modified form. An example of its proposal was the removal of the prohibition on a company giving financial assistance for the acquisition of its shares from private companies. It also proposed a re-ordering of the Companies Act so as to make more transparent provisions applying to private companies, a task to some considerable degree carried out by the UK Companies Act, 2006[86].

It has been argued that given the importance of the distinction between public and private companies in the UK Companies Act 2006 and the likely increase in the importance of that distinction in the future, the choice between a public and a private

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[83] Paul L Davies (ed) (8th edn, 2008) (n17), 14; The Nation Newspaper Vol. 5, No. 1,584, (Friday, November 19, 2010), 54

[84] Nigerian Code of Corporate Governance (NCCG) 2018, Principle 2

[85] Ibid

[86] Ibid

company is one for the corporators themselves or, after incorporation, for the shareholders as a company originally incorporated as private may, subject to certain safeguards, transmogrify into a public one[87]. In fact the default rule being that the company is private, unless the company states that it is to be registered as a public company; it will be a private company[88].

The same is not the case under the companies and Allied Matters Act[89] wherein a public company is defined in residual category[90]. Yagba[91] submits that the latter requirement in the section that the memorandum of a public company should state the fact that it is a public company appears to be destitute of any practical value in view of section 23 of the Act which provides that if a private company defaults in complying with the limitations imposed by section 22, it will cease to be entitled to the privileges and exemptions of private companies. The Act then applies to it as if it were a public company. He further submits that in effect, the relevant authorities may presume that all companies are public and the burden should be on those claiming to the contrary to establish compliance with section 22. Such presumption would strengthen the regulatory powers of the Corporate Affairs Commission particularly in enforcing the requirements as to annual financial statements and annual returns. It is submitted that the simplest way out is for the Companies and Allied Matters Act to define a public company explicitly and a private company by exclusion as done under the U.K. Companies Act, 2006.

Today, there is a major shift from the position which obtained when the idea of the private company was introduced by the companies (Consolidation) Act, 1908. The view then was that, because a private company was exempted from some of the publicity provisions of the Act, access to that form or status should be restricted. Hence, a company could qualify as a private on only if it:

i) limited its membership to fifty (50)
ii) restricted the right to transfer shares, and
iii) prohibited any invitation to the public for its shares[92].

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[87] Ibid
[88] U.K Companies Act 2006, Section 4(2) (a).
[89] Cap C20 LFN, 2004, Section 24
[90] TAT Yagba and BB Kanyip and SA Ekwo (n43), 223
[91] Ibid
[92] Paul L Davies (ed), (8th edn, 2008) (n17), 15-16

The first two conditions have been abolished in the United Kingdom and only the third has survived into modern law as a requirement for private status. This modern approach, which led to the abandonment of the rational basis of classification of the 1900s, was introduced by the UK Companies Act 1980, which implemented the Second EC Company Directive on the raising and maintenance of capital[93].

It is rather curious that, the limitation of membership and restriction of the right to transfer shares which are importations of the repealed English Company Law into Nigeria, have remained part of Nigerian Companies legislation in the twenty-first century, and have continued to restrict access to private status. A clarion call has been that the law should be reframed so that each category of company has its own statute, or that the law should go even further to accommodate the special needs of the smallest businesses by having a separate, simplified, legislative regime designed for them (as has been done by the Close Corporations Act in South Africa)[94]. However, there appears to be no support for such a proposal in Nigeria. Yagba[95] submits that the present approach does not fully reflect the varied and distinct needs of, or demands of the two kinds of companies in the practical world of commerce and the equally different challenges of public regulation which they pose to the supervisory authorities. This is especially so when the private company is a one-man concern or the public company is quoted on the Stock Exchange. The present approach only takes away with the back hand the advantages of incorporation which the law confers on private companies in so far as the costs outweigh the practical benefits of incorporation in most cases[96].

Listed and Other Publicly Traded Companies

Public Companies are permitted to offer their shares to the public but such companies may not in fact have chosen to do so and even if they have, those shares may or may not be traded on a public

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93 Directive 77/91/EEC (1977) OJL26/1 (implemented by Section 542 (1), (2) U.K. Companies Act, 2006)

94 Len Sealy and Sarah Worthington (n10), 20

95 TAT Yagba and BB Kanyip and SA Ekwo (n43), 223-224

96 Tom Hadden, *Company Law and Capitalism* (2nd edn, Weidenfeld & Nicolson, 1977), 224-230

share market as the Stock Exchange[97]. Offering shares to the public and arranging for those shares to be traded on a public market are two different things, though the public's willingness to buy the shares is likely to increase if the shares will be traded on a public market. This is because a public market makes it much easier for a shareholder subsequently to sell his or her shares to another investor, or to buy shares in the company, should he or she wish to do so. Consequently, public offerings of shares and the introduction of those shares to trading on a public market go together[98].

It is important to note, however, that, public companies are not necessarily listed on the Stock Exchange. A listing is essentially a private contractual arrangement between a public company and the Stock Exchange (itself a listed public company) to gain access to a very sophisticated market for its shares[99]. By and large, the Companies and Allied Matters Act makes no differentiations at all according to whether a public company's shares are offered to the public or are infact publicly traded. Put differently, Nigerian law does not reflect the fact that of public companies, some are quoted on the Stock Exchange while others are not.

Parent or Holding Companies and Subsidiaries

The companies and Allied Matters Act[100] defines 'holding company', 'subsidiary company' and wholly owned subsidiary in terms of control of the composition of the board of directors or ownership of more than half in the nominal value of the equity share capital of a company, or where the first-mentioned company is subsidiary of any company which is that other's subsidiary. A company shall be deemed to be a holding company of another, if the other is its subsidiary[101]; and a body corporate shall be deemed to be wholly-owned subsidiary of another, if it has no member except that other and that other's wholly-owned subsidiaries are its or their nominees[102]. These companies belong to a group.

With the larger companies, group structures become increasingly complex and sometimes the legal picture is not an

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97 Paul L Davies (ed), (8th edn, 2008) (n17), 16

98 Ibid

99 Alan Dignam and John Lowry (n57), 9

100 Cap C20 LFN, 2004, Section 338 (1) (a) (i) (ii) & (b)

101 Ibid, Section 338 (5) (a)

102 Ibid, Section 338 5(b)

accurate reflection of the actual organizational structure[103]. Sometimes subsidiaries may be little more than shells or may be run as agents for other companies in the group[104]. Some groups operate a division structure which is super imposed on the legal group structure and management may be organized on a divisional basis rather than a company basis. This may make the monitoring of management performance by external agencies more complex. Both the group structure and the other more elaborate structures pose difficulties to outside creditors[105]. Normally these only manifest when the difficulties give rise to insolvency. Here, the *de jure* separation of entities may be contradicted by *de facto* both by business operations and the practice of finance creditors of taking group guarantees and security[106].

Despite the potential difficulties groups pose to regulation, Nigerian law does not reflect on the fact that a private company may be floated as a subsidiary of another company. Neither has it reflected on the fact that some private companies are owner-controlled while others are not where there is external share holding. The law has ignored these structures and has neither contemplated a distinct legal regime for them nor made elaborate provisions for their regulation.

Possible Classification of full Range of Registered Concerns Based on Eight Characteristics and Qualifications

It is possible to classify companies today depending on eight (8) characterizations and distinct qualifications for purpose of regulation.[107] In this direction, the full range of registered concerns begins with the one-man company to the giant transnational and in between these, other categories could be located. The rationale for this classification is to situate and identify each type of company according to the economic function it performs in the society and the consequences of such function on diverse interests so as to make the task of regulation of companies easier. As it stands now, regulation of companies overlap and one has to wade through a mass of legal

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[103] JH Farrar and N Furey and B Hannigan (n2), 33
[104] Ibid
[105] Ibid, 33, 37
[106] Ibid
[107] Tom Hadden (n96), 38-46; Len Sealy and Sarah Worthington (n10), 20-21; Paul L Davies (ed) (8th edn, 2008) (n17), 13-32; 79-83

statutes to decipher whether certain legal rules apply to some types of companies or not. Under the circumstances, small and medium-sized companies suffer regulation that was designed for the large quoted companies. The following companies fall within the eight categorizations:

The One-Man Company

The decision of the House of Lords at the end of the nineteenth century in *Salomon v Salomon & Co Ltd*[108]in effect allowed the incorporation of a company with a single member, the other six members being bare nominees for the seventh (Mr Salomon). This judicial decision preceded by nearly a century the adoption of EC Directive 89/667[109], which required private companies to be capable of being formed with a single member[110]. Ultimately, the facility was extended to public companies by the U.K Companies Act 2006[111]. Under Ghana's Companies Code Act[112] and Jamaica's Companies Act[113], one or more persons may form a company. Thus, in *Politis v Okudzeto*,[114] where two persons formed a company and one died, the Ghana High Court held that it was proper for the sole surviving member to hold a meeting with himself without the need for a notice of meeting or quorum. The decision in *Salomon's* case was followed in the subsequent case of *Lee v Lee's Air Farming Company Limited*[115] where Lee who had formed an aerial company was himself a pilot of the company, the controlling shareholder and sole governing director with all the powers of management vested in him. Both the cases and the statutes have therefore, legalized the one-man company in other jurisdictions.

Even though Nigerian Law,[116] like that of the Bahamas,[117] requires a minimum of two (2) persons to form and incorporate a company, it is not mandatory for the second person to have any

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[108] (1897) AC 22 (HL)
[109] (1989) OJL 395/40
[110] Paul L Davies (ed) (8th edn, 2008) (n17), 5
[111] UK Companies Act, 2006, Section 7(1) which has not confined the single member company to private companies
[112] Ghana's Companies Code Act (No. 179) 1963, Section 8
[113] Jamaica's Companies Act (No.10) 2004, section 3(1)
[114] (1967) 3 ALR (Comm.) 178
[115] (1961) AC 12
[116] CAMA, Cap C20 LFN 2004, Section 18
[117] The Bahamas Companies Act (No.18) 1992 section 3(1)

tangible or real interest in the enterprise. The second person's name may only be added to satisfy the legal requirement, and this renders the requirement entirely artificial[118]. In this regard, Chianu,[119] submits that "what we find is not incorporated company but incorporated individual who conducts his business, using the form of a company." This fact notwithstanding, the extant law assumes that this type of company shall be operated and regulated in the same way and subject to the same limitations and restrictions as applied to the company with a hundred shareholders, despite the numerous and significant differences between the two types of companies. There is therefore, need for legislative action to respond to the reality of the commercial world. Interestingly, many one-man companies are operated in complete ignorance and disregard of the contents of the constitutional documents and of elementary rules and principles of company law.[120]

From the decision in Salomon's case, the fact that some of the shareholders are only holding shares as a technicality is irrelevant, the machinery of the Companies Act may be used by an individual to carry on what is in economic reality his business[121]. The Companies and Allied Matters Act should therefore, give the 'one-man company' the full legal recognition that judicial authorities and statutes in other jurisdiction accord it.

The participant or partnership company

Here, shares are held exclusively by those directly concerned in the management of the company, or by their close relatives. According to Hadden**[122],** this takes care of all small businesses which form the corporate pyramid. He adds that for some purposes it may be useful to draw a distinction between the 'one-man company' and the partnership company in this context, but the formal nature of the company as a business enterprise is not normally affected by the number of persons involved in running it.

Referring to the Bolton Committee Report on small companies, he said the committee reported that ninety-nine percent of small firms in their sample, whether companies or not, had five or

118 TAT Yagba, BB Kanyip and SA Ekwo (n43), 225
119 E Chianu, *Company Law* (Pan African Institute of Paralegal Studies 2012), 184
120 Ibid
121 Alan Dignam and John Lowry (n57), 21
122 Tom Hadden (n96), 44

fewer participators; roughly forty percent had a single controlling owner; forty-five percent two controlling shareholders/partners and the remainder more than two. If the upper limit is set at five participants, it is probable that about six in ten of all existing companies, or some 300,000 in all, fall in this group, of which about one-third might be one-man companies and the rest partnership companies, formed and operated to manage individual property assets in the most advantageous and convenient way.

The Extended Partnership Company

This develops naturally from the participant/partnership company because of making over shares from all shareholders, who cease to actively participate in the operation of the company's business, to their close relatives- wives and children, either for tax purposes or on the retirement or death of the original participants[123].

The large Unquoted Company or Private Family Company

At a certain stage of size or development, it only becomes natural to think of the company as a continuing entity rather than merely a device through which the participants carry on their business. This will depend on the age of the company, the size of its business and the number of participants and external shareholders. This type of company, in some cases, remains exclusively in the hands of one or two families, and may appropriately be termed a private family company[124]. In other cases, such a company may have a fairly widespread shareholding and floated as a means of investment or property management[125]. In the latter situations, a company which was formally controlled wholly by the members of a particular family may bring in one or two outside financiers (sometimes called "business angels") in order to expand the business and these outsiders will naturally want a share in the control of the company[126]. At a later stage, the family members may retire from active management of the company and bring in professional

[123] Ibid, 45
[124] Ibid
[125] Ibid
[126] Paul L Davies (ed), (8th edn, 2008) (n17), 12-13

managers (to whom shares are allocated) to run the company but the family members remain the predominant shareholders[127].

Quoted Public Companies

In this category, there is a genuine public market in the shares of the company through the mechanism of the stock market. There is therefore, an important additional element of public interest which differentiates this type of company from the large family private company[128]. However, this type of company is not to be confused with the purely legal distinction between private and public companies under the Companies and Allied Matters Act[129].

Subsidiary Companies

These consist of a residual group of subsidiary companies which are wholly owned and controlled by other companies[130]. This group straddle the distinction between public and large private companies because subsidiaries of both types are included, and there is also an appreciable number of subsidiaries which would otherwise fall within the first two groups[131]. Many subsidiaries retain an independent existence, as operational or accounting divisions while others are swallowed up by the parent organization[132].

Non-Commercial Concerns

This is an entirely separate group of companies incorporated for non-commercial purposes, for instance to hold the property of clubs and societies, or to carry on charitable activities[133]. The Companies and Allied Matters Act[134] has long provided for this form of company, the company limited by guarantee, which may be suitable for conducting a not-for-profit business. However, the guarantee company and the company limited by shares are regulated fundamentally in different ways. It is usually to form and register such a company without share capital since there is no question of

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127 Ibid
128 Tom Hadden (n96), 45
129 Cap C20 LFN, 2004, Sections 22 & 24
130 Tom Hadden (n96), 46
131 Ibid
132 Ibid
133 Ibid, 46 & 123; Len Sealy and Sarah Worthington (n10), 20
134 Cap C20 LFN, 2004, Sections 21 (1) (b) & 26

dividend payment. The British company law has developed a hybrid of this type of company as Community Interest Company (CIC) whose activities are carried out for the benefit of the community.

Group Multi-National Company

This consists of companies with significant trading, ownership or managerial links under a centralized management. This type of company carries on directly or indirectly business in more than one country[135]. Multi-national corporations generally have the following characteristics:

i. they extend production and marketing across national boundaries usually through foreign subsidiaries or joint venture companies;
ii. they are large in size;
iii. they tend to have centralized management and integrated production and marketing[136].

In 1969 in "Companies Legislation in the 1970s", four of the main accountancy institutes called for a new classification of proprietary as opposed to stewardship companies[137], and in 1980 some accounting firms recommended same fundamental changes in the classification of companies for purposes of regulation. They suggested that companies should be classified into two:

i. proprietary companies instead of private companies.
ii. stewardship companies.

By the Bolton Committee Report,[138]a proprietary company would be defined as one:

a) which is managed and controlled substantially by the same persons;
b) which is not under the control of another company which is not itself a proprietary company;
c) which limits the right to transfer its shares;
d) which prohibits any offer of its shares to the public;
e) which limits the number of members to twenty-five (25);
f) whose average number of employees per week does not exceed two hundred (200).

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135 JH Farrar and N Furey and B Hannigan (n2), 649
136 Ibid
137 JH Farrar and N Furey and B Hannigan (n2), 484
138 The Bolton Report, 314

g) which has an annual turn over not exceeding €500,000.

The object of the new classification was to exempt proprietary companies from the more onerous accounting requirements, some which purposes were achieved by the U.K. Companies Act, 1981[139]. Using these indices above, all large private companies which are not effectively managed by their owners and all public companies (with a disconnection between ownership and control) would fall into the category to be known as 'stewardship companies'. This approach has been adopted in Australia because companies are classified in that country as proprietorship or stewardship companies[140].

The Bolton Committee in England found this as a good idea so the Companies Bill 1980 introduced two types of companies in England called 'proprietary company' and others, and therefore emphatically adopting the proprietary company model. The proprietary company is supposed to meet the needs of small firms and to relax many statutory provisions applicable to both private and public companies. Perhaps, this same approach has informed the introduction of the 'small private company' under Section 351 of the Companies and Allied Matters Act,[141] which enjoys exemption, under section 353(2) of the Act, from the disclosure requirement in regard to financial statements imposed on large public and private companies. This is, however, by no means, an explicit adoption of the stewardship company, as a corporate form, in Nigeria. It will be better if classification of companies in Nigeria is based on economic structures (which are simple and comprehensible to the unsophisticated investor) and function, and not on legal formula. This will make regulation easy and obviate the problem of small companies having to contend with complex statutory rules inappropriate to them, and also reduce the cost of compliance.

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139 JH Farrar and N Furey and B Hannigan (n137)

140 The Australian Companies and Securities Law Review Committee's 'Report on Forms of Legal Organization for Small Business Enterprises', September, 1985

141 To qualify as a small Company under the provision the company must satisfy certain conditions to wit: It must be a private company having share capital; the amount of its turn over for that year should not exceed N2million; its net assets value shall not be more than N1million, none of its members should be an alien; and it should not have a government corporation or agency or its nominee as a member.

Conclusion and Recommendations

Against the backdrop of the foregoing analysis, Hadden's approach to classification of companies should be adopted with modifications to suit the local circumstances. Thus, the one-man company (proprietary company) deserves to be given statutory recognition to enable unsophisticated petty traders who operate as sole traders to conduct business in the corporate form without the burden of the statutory provisions applicable to both private and public companies. Group companies and multinational companies should also be clearly distinguished under Nigerian law and a distinct legal regime provided to regulate them as obtains in the Bahamas. Under the statute law of the Bahamas, there are two separate regimes for incorporation of domestic and international companies. While the Bahamas Companies Act, 1992 regulates the incorporation and operation of domestic companies, her International Business Companies Act, 2000 provides for the incorporation and operation of international business companies. A company which is incorporated under the Companies Act or under the laws of a jurisdiction outside the Bahamas shall be a company incorporated under the latter Act.