



The Power behind the Throne: Investigating the Position of the Founders in the Formation Process of a Share Company under Ethiopian Company Law

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Abstract: *The study examines about the founders of share companies in Ethiopia. In general, the study intends to assess the acts of the founders to form share companies. In particular, the study will focus to examine about the legal and the business connotation behind the term 'founder', and the roles exhibited by the founder at a company under formation in line with the legal inter actions that exist between and among the founders inter se and other persons. Thus, parallel to the Company Law of Ethiopia the researcher analyses the basic documents drawn by founders, other countries' laws and legal basis of appropriate government organs of Ethiopia that regulate the acts of the founders. As a result, the writer recommends that the law maker need to give special emphasis on the issues of founders in the legal and policy reform of Company Law. Furthermore, the writer also recalls that all appropriate stake holders of the formation process of share companies have to be cautious to play their roles and implement their powers as envisaged under the law to pave appropriate path for the current trends of the markets.*

Key Words: *Ethiopian Company Law, Founders, commitment, Formation of a share company*

Introduction

In Ethiopia share companies do not come over night to the attention of the legal environment of business. They are the fruits of persons who set the foundation processes of companies in motion. Founders are the persons responsible for such venture. Thus, companies come to operate with necessary legal rules. In line with these rules that founders have their own distinctive roles and positions to form share companies.

The founders may initiate either a marketable share companies or a non-marketable share companies.¹ The extent of rights and liabilities is not similar as to the types of companies to their marketability and non-marketability.² Likewise the 1960 Ethiopian Commercial Code (herein after the Commercial Code) provides that founders are persons who can

initiate the formation of share companies either between themselves or via public subscription.³

The Commercial Code fails to define the term 'founder' clearly; albeit, this Code puts different parameters for a person who can claim to get the status of the founder.⁴

In Ethiopia it is common to see that basic documents of share companies under formation are used to apply the term 'founder' and 'promoter' interchangeably. Under foreign literature the term promoter uses as equal as the term 'founder'. Hence, the promoter is "the person who is responsible for the company is coming in to existence."⁵ Thus, in such a way that the term promoter means, "the one who undertakes to form a

¹ B. M. Richard, *International Encyclopedia of Comparative Law*, 2012, at 3.

² Ibid

³ See Arts. 316 and 317 of the Commercial Code of the Empire of Ethiopia (herein after the Commercial Code), Pro. No. 166, *Negarit Gazette*, Year 19, No. 3, 1960.

⁴ Id, Art. 317

⁵ D. Janet, *Company Law*, 2001, at 86.

company with a reference to a given project and to set it going and who takes the necessary steps to accomplish that purpose.⁶

In fact, the formation of share companies needs necessary knowledge, time and finance of different persons. There are different persons who are taking part in the formation process of the company. The founders of the company enter into contracts with different persons to facilitate the formation of share companies.

Therefore, the status of being a founder has its own advantages and responsibilities. Thus, there are peculiar legal and contractual duties levied on the founders of the company. Furthermore, there are limited and known benefits of the founder to form a company. The founder of a company forms a special relationship with the under formation companies. There are commitments entered into by the founders with external persons and other founders. Further, the founder also can enter into contractual dealings with potential shareholders to sell shares. These relationships need to be revisited by regulators vis á vis the interests of future shareholders.

In Ethiopian Company Law there are commitments entered into by the founders of the company to establish a company.⁷ In addition, founders may incur various costs to do so. Thus, the founders of share companies reimbursed for such costs after the establishment of a share company upon approval of the general meeting of the subscribers.⁸ At the same time whether a company is successfully established or not there may be liabilities of founders for the company, third parties and potential share buyers.⁹

⁶ Ibid

⁷ See Art. 308 of the Commercial Code, supra note 3.

⁸ Id, Art.308 (2)

⁹ Id, Art.309

On top of that, there is a benefit derived by the founders of companies from the profit of a future company.¹⁰

The formations of share companies require considerable capital pull from the vast public. The routine processes of share companies' formation have proved the existence of commitments on the side of the founders. Hence, the founders have to take due care and comply with the law. In one hand, Ethiopia Company Law and its institutions are over there to regulate the actions of the founders. In another hand, the practice in which the founders are acting shows its own facade.

In Ethiopia different regulatory bodies of the government have the power to control and supervise the acts of the founders. Thus, the country has its own mechanism of supervision and oversight under her Commercial Code, various legislations and directives made by appropriate executive branches of the government. For instance, the National Bank of Ethiopia (herein after the NBE) supervises and controls the companies under formation of monetary and financial institutions.¹¹ Whereas, the Ministry of Trade controls and supervises the operation of share companies other than financial institutions.¹²

1. The concise essence of a company

The term 'company' comes from two Latin words; namely 'com' and 'panis' in which the first word implies 'being with or together', whereas the latter

¹⁰ Id, Art.310

¹¹ See Art.5 (7) of the National Bank of Ethiopia Establishment Proclamation as amended (herein after Pro. No. 591/2008), Pro. No. 591, *Federal Negarit Gazette*, Year 14, No. 50, 2008.

¹² See Art. 12 (5) of the Commercial Registration and Business Licensing Proclamation (herein after Pro. No. 686/2010), Pro. No. 686, *Federal Negrit Gazette*, Year 16, No. 42, 2010.

word implies 'bread'.¹³ The term company had been referred as an association of persons who took their meals together.¹⁴ However, in a modern way companies have a legal existence in their own right, apart from and independent of their member.¹⁵ The term corporation and company are used to apply interchangeably in some other jurisdictions. Thus, one writer provides that corporation is understood as an entity, something that has a distinct existence separate and apart from the existence of its individual members.¹⁶ The Black's Law Dictionary defines a corporation as "an entity having authority under law to act as a single person distinct from the shareholders...has legal personality distinct from the natural persons who make it up...and has the legal powers that its constitution gives it."¹⁷

The Commercial Code opts to provide the essences of private limited and share companies. Thus, a private limited company is a company whose members' liabilities are limited solely to the extent of their contribution.¹⁸ Whereas, "a share company is a company whose capital is fixed in advance and divided into shares and whose liabilities are met only by the assets of the company."¹⁹ These provisions do not provide the full picture of what are the appropriate essences of a company before the law.

At all a share company will attain such essences after it is duly formed. The concept of limited liability is the inherent distinctiveness in which a

¹³The Institute of Company Secretaries of India, *Company Law Module II Paper 4*, 2008, at 1.

¹⁴ Ibid

¹⁵ K. David, H. Mann and H. Ruth, *Business law*, 2002, at 341.

¹⁶ A. John D. and A. Janet E., *Law for Business*, 2011, at 374.

¹⁷ G. Bryn A., (ed. in Chief), *Black's Law Dictionary*, 1999, at 341.

¹⁸ See Art. 501 (1) of the Commercial Code, supra note 3.

¹⁹ Id, Art.304 (1)

company is established. "The limited liability corporation is the greatest single discovery of modern times. Even steam and electricity are less important than the limited liability company."²⁰

In a nutshell, in Ethiopia business organizations shall be deemed to be of a commercial nature where their objects under the memorandum of association or in de facto that they are traders as per the Commercial Code's definition.²¹ However, share companies and private limited companies shall always be deemed to be of commercial nature whatever their objects are provided otherwise.²² However, in France almost all business organizations are trading companies by virtue of their form, irrespective of their objects.²³ Hence, in this nation the form and purpose of the company shall be determined by the company's memorandum and articles of association.²⁴

²⁰ D. Janet, supra note 5, at 1. It is said by Professor N. M. Butler, President of Columbia University (quoted by A. L. Diamond in Orhnia (ed.), *Limited Liability and the Corporation* (Law Society of Canada, 1982) p. 42; see also Len Sealy, *Company Law and Commercial Reality* (Sweet & Maxwell, 1984) p. 1.).

²¹ See Art. 10 (1) of the Commercial Code, supra note 3, which provides that business organizations shall be deemed to be of a commercial nature where their objects under the memorandum of association or in fact are to carry on any of the activities specified in Art. 5 of this Code. Hence, Art 5 of the Commercial Code stipulates trading activities of persons regarded as traders who are doing trade as a profession and for profit.

²² See Art. 10(2) of the Commercial Code, supra note 3.

²³ See Article L210-1 of the *French Commercial Code* which provides that the commercial nature of a company shall be determined by its form or by its objects. General partnerships, limited partnerships, limited liability companies and joint-stock companies are trading companies by virtue of their form, irrespective of their objects.

²⁴ See Article L210-2 of the *French Commercial Code* which provides that the form, duration, which may not exceed ninety-nine years, the business name, the registered office, the purpose of the company and the amount of the registered capital

2. Founders of a share company

Across the literatures various terms are under use in tandem with the persons who form a share company. The founders of a share company are persons who work for the legal creation of a share company as a special tool in the market.²⁵ Inside different literature the term 'promoter' is used to replace the term 'founder' which includes a person who undertakes to form a company in order to procure the rights, instrumentalities and capital for the same.²⁶

In fact, the term 'promoter' is neither a term of art, nor a term of law.²⁷ However, Palmer defined the term 'promoter' as: "a person who originates a scheme for the formation of the company, has the memorandum and articles prepared, executed and registered and finds the first directors and settles the terms of the preliminary contracts and prospectus (if any) and makes agreements and advertising and circulating the prospectus and placing the capital."²⁸

The term 'incorporator' is also in use for a person who founds a company. In USA, "one or more persons may act as the incorporator(s) of a corporation by delivering articles of incorporation

shall be determined by the company's memorandum and articles of association.

²⁵ See D. Janet, supra note 5 at 1, a huge proportion of the world's wealth is generated by companies. Companies will generally require an injection of money which can be achieved by inviting more people to contribute to the capital sum which the business uses to fund its activities.

²⁶ M. Robert, "Incorporation of Companies," (http://www.jstor.org/stable/840908?seq=1#page_scan_tab_contents/Stable/URL:<http://www.jstor.org/stable/840908>) last visited on October 12, 2013, at 8

²⁷ K. R. Bulchanadani, *Business Law*, 2001, at 409.

²⁸ Ibid

to the secretary of State for filing".²⁹ Conversely, one may perceive that, the promoter work is just an act of promotion and facilitation for company's incorporation.³⁰ OHADA's Business Law of Africa prefers to use the term founder for the person who establishes a company.³¹

The Commercial Code does not define the term founder directly. Thus, the founders of a share company either form share companies among themselves or via public subscription.³² Hence, if persons sign the memorandum of association and subscribe the whole amount of the capital, they shall have the legal status of the founders.³³ Nevertheless, in case of publicly subscribed company the situation is somehow become complex. Thus, it is because mainly different persons may involve in the formation process of the company. These persons may assume different responsibilities and enjoy privileges in the period of a company under formation.³⁴

The Commercial Code elucidates four alternative conditions in which the founders can acclaim the status of founders in a case of a company created via public subscription of shares.³⁵ It reads as follows. "... persons who sign the prospectus,

²⁹ "American Bar Foundation, Law, and Business,"

(http://www.americanbar.org/groups/business_law.html) last visited on August 13, 2013.

³⁰ M. Robert, supra note 27, at 2.

³¹ *Uniform Act Relating to Commercial Companies and Economic Interest Group (herein after OHADA rules)*, 1997, Art.102: "all persons who actively participate in transactions leading to the formation of a company shall be deemed to be founders thereof..."

³² See Arts.316 and 317 of the Commercial Code, supra note 3.

³³ Id, Art. 307 (2)

³⁴ See sub articles 3 and 4 of Article 307 of the Commercial Code, supra note 3. These provisions elaborate the functions of different persons, who may claim the status of the founders in relation to the formation of a share company.

³⁵ Id, Art. 307 (3) and (4)

bring in contributions in kind or are to be allocated a special share in the profits shall have the status of founder.”³⁶ Firstly, the original founding persons who signed the prospectus of the company to be found have priority to get status of founders. Hence, due to their efforts trying to form a share company that the law gives them a credit and assigned them the status of the founders. Secondly, the members of the company who contribute properties in kind are also entitled the status of the founders. In fact, these provisions seem unfair in relation to members who contribute in cash for the coming in to existence of the company.³⁷ On top of that, the third alternative condition goes on to say that persons who can claim a special share from the profit of the company can have the status of the founders. Finally, the law provides two alternative and open-ended conditions to entitle the status of the founders for the persons who can prove their efforts for the formation of a company.³⁸ These are namely, the people who participate in the initiation

³⁶ Id, Art. 307 (3)

³⁷ See Aklilu Wolde Amanuel and Tewodros Mihret , "Comments and Recommendations Regarding Provisions of Book Two of the Commercial Code of Ethiopia and the Revised Draft Version of the Proposed by the Ministry of Justice," *Addis Ababa Chamber of Commerce and Sectoral Association Private Sector Development(PSD) Hub , Recommendations and Position Paper of the Business Community on the Revision of the Commercial Code of Ethiopia*, Prepared by a Team of Fourteen National Expert , July 2008, point 17 , at 25 : ‘Why do Articles 307(3) of the Code and the Draft consider a person who contributes in kind as a founder because of the type of contribution alone? In what respects is such person materially different from a person who contributes in cash? Why the law considers the first person as a founder while disregards the latter? It is suggested that the term “founder” be reserved for a person who plays a role in setting up a company. At least the law among shareholders because of the kind of contribution should make no distinction. So those who have paid fully in cash should also be considered as founders so that the discrimination could be avoided.’”

³⁸ See Art. 307 (4) of the Commercial Code, supra note 3.

of plan or facilitation of a company in which whether the founder would be a shareholder or not.

The Commercial Code seems giving little attention for the exact parameter to decide over the legal status of the founders. For instance, OHADA rules provide the two basic elements of participation of founders in the formation process of the company.³⁹ These are namely: an active participation and such participation shall lead the formation of a company. Likewise, under the Common Law literature there is a parameter to decide over the issue whether the person is a promoter or not. Thus, such literature provides that: ‘...however, it is possible for a promoter not to have been obviously active. If he is the real power behind the throne, he will be held to have been a promoter.’⁴⁰

Overwhelmingly, investment of time or money in the enterprise to be established will always be considered.⁴¹ Thus, persons who are acting in a purely professional capacity who have been instructed by a promoter, for example, a lawyer or accountant, auditor are not promoters.⁴² As a result, the issue whether person is a promoter or not is a question of fact.⁴³ Notwithstanding that the issues of legal terminology of the term 'founder', unlike the French Commercial Code under Ethiopian Company Law there is no rules on the founders' duty to decline along trade backgrounds of the founders.⁴⁴

³⁹See Article 102 of OHADA rules, supra note 31. It provides that all persons who actively participate in transactions leading to the formation of a company shall be deemed to be founders thereof....

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⁴⁰ D. Janet, supra note 5, at 86.

⁴¹ K.R.Bulchandani, supra note 27, at 410.

⁴² Ibid

⁴³ M.Robert, supra note 26, at 2.

⁴⁴ See Paragraph 3 of Art. L225-2 of *the French Commercial Code* which provides that persons who

3. Founding stages of a share company and the legal requirements

The share company has its own stages of formation to get involved in the legal environment of business. The founders are usually active actors under the two known periods of formation of a share company.

3.1. Under formation period of a company and the legal preparation of the founders

In Common Law countries the period before the legal formation of a share company is usually referred as a pre-incorporation stage of a company or in short it is referred as pre-incorporation.⁴⁵ This period can be also referred as under formation period of a company.⁴⁶ In Ethiopia one of the legislations on area of company law uses the term 'under formation period' to refer the pre formation period of a share company.⁴⁷ To add, the Proclamation on Banking Business uses the term 'prospective company' to refer a bank under formation.⁴⁸

Concisely, the Commercial Code provides general requirements in respects of formation of a share company.⁴⁹ Thus, such requirements are conditions to form a share company in which founders shall

have forfeited the right of directorship or management of a company or who are disqualified from holding these offices may not be founders.

⁴⁵ B. Nicholas, *Essentials of Company Law*, 2000, at 3.

⁴⁶ Ibid

⁴⁷ Art.12 (1) of Pro. No. 686/2010, supra note 12.

⁴⁸ See Article 4(1) (F) of the Banking Business Proclamation (herein after Pro. No. 592/2008), Pro. No. 592, *Federal Negarit Gazette*, Year 18th, No. 56, 2008.

⁴⁹ See Art. 312 of the Commercial Code, supra note 3.

assume responsibilities in the period known as under formation stage of a share company.⁵⁰ From the outset, a share company shall not be formed until the capital has been fully subscribed.⁵¹ As a result, at least one quarter of par value of shares has been paid up.⁵² Further, such capital has been deposited in a bank in the name and to the account of the company.⁵³

The law which amends the Commercial Code in some aspects of commercial registration and business licensing requires the founders or their legal agent to submit various documents for the registering organ during the time lodging an application for registration of the company.⁵⁴

In the formation process of a share company, as may be appropriate together with the application that the founders or their attorney, if any, shall submit two categories of documents to the registering organ.⁵⁵ These are namely personal identification and company's basic documents.⁵⁶

⁵⁰ Id, Art.346

⁵¹ Id, Art.312 (1) (A)

⁵² Id, Art.312 (1) (B)

⁵³ Ibid

⁵⁴ See Art.12 of Pro. No.686/2010, supra note 12.

⁵⁵ Id, Art.12 (1)

⁵⁶ Id, Art.12 (1) (A). It provides that where the application is signed by an attorney that the original copy of power of attorney given by all the founders, photocopies of *Kebele* identification card or passports of the attorney and the manager together with the passport size photographs of the manager taken within six months shall be handed over to the registering organ. In addition, Art. 12 (12) (1) (B) - (F) says the following companies' basic documents shall be produced by the founders or their attorney to the screening organ which registers a company under formation. These documents are, inter alia; a bank statement, original copies of minutes of resolution of the subscribers and other documents if any, original copies of memorandum and articles of association, investment permit and valid pass port for foreigner as if he or she would be a shareholder, and if the office of his business is his own a title deed or if it is a leased one an authenticated contract of lease and a verification issued by *Kebele* Administration

Thus, the founders could do with checking all important documents shall be submitted to the registering organ after authentication is done by appropriate government organ.⁵⁷ As a result, the registering office shall write a letter to the bank, for a quarter of the capital of the share company under formation to be deposited in the bank in a blocked account.⁵⁸ In case of the foreign company get involved in the formation of a company the rule is different.⁵⁹

In case of financial institutions the NBE shall license and regulate banks, insurance companies and other financial institutions in accordance with the relevant laws of Ethiopia.⁶⁰ In the same token, foreign nationals or organizations fully or partially owned by foreign nationals may not be allowed to acquire the shares of Ethiopian insurers.⁶¹ Likewise the law on banking business provides that foreign nationals or organizations fully or partially owned by foreign nationals may not be allowed to acquire the shares of Ethiopian banks.⁶² Furthermore, the legal capital rule for banking and other financial institutions has to be met by the founder which is

different from the rule under the Commercial Code.⁶³

The proclamation on banking business provides the following conditions shall be fulfilled by the founders to obtain a banking business license.⁶⁴ Inter alia; a duly completed application formats of the NBE, publication of notice of intention, payment of investigation fee, submission of memorandum and articles of association before registration by appropriate body to be approved by the NBE, all its issued shares shall be subscribed and, at a minimum one-fourth of the subscribed shares shall be fully paid in cash and the minimum paid-up capital prescribed by the National Bank shall be paid in cash and deposited in a blocked account in a bank in the name of the prospective bank.⁶⁵ The same rules are provided for the opening

as to the address of the office with the exact address of the head office and branch offices.

⁵⁷ Id, Art.12 (1) (G)

⁵⁸ Id, Art.12 (3)

⁵⁹ Id, Art. 11 (1) (C) and Art.12 (1). "Where there is a foreign juridical person involved in the business organization under formation; its certificate of incorporation, originals and authenticated copies of its memorandum and article of association or similar document, a notarized minutes of resolution passed by the authorized organ of the juridical person to join the business organization and an investment permit where the juridical person is a foreign business organization."

⁶⁰ See Art.14, Pro. No. 591/2008, supra note 11.

⁶¹ See Art. 10 of Insurance Business Proclamation (herein after Pro. No.746/2012), 2012, Pro. No. 746, *Federal Negarit Gazette*, Year 18, no.57.

⁶² Pro.No.592/2008, supra note 48.

⁶³ See Art. 306(1) of the Commercial Code, supra note 3. Minimum amount of capital shall not be less than 50,000 Ethiopian Birr. See NBE, "Bank Supervision Directorate Information kit," (<http://www.nbe.gov.et/pdf/service/bankingbusiness.pdf>) last visited on October 12, 2013, at 1. In case of banking industry an evidence for payment of minimum paid-up capital of birr 500 million in cash shall be adduced by the founder to have a license for operation of banking business in Ethiopia. However, , the share capital should not be less than 3,000,000 Birr for general insurance business; 4,000,000 Birr for long term insurance business and finally 7,000,000 Birr if the business to be done both for general and long term insurance business. See also Art.2 (14) of Pro. No. 746/2012 which defines general insurance business. It means all classes of insurance business other than long term insurance business. In addition, see Art.2 (24) (a) (b) (c) (d) (e) of the same Proclamation. Long term insurance business is defined as an insurance business of life insurance, annuity, pension, permanent health insurance, personal accident or sickness and the like as provided under the legislation.

⁶⁴ See Art. 4 (1) (A) - (F) of Pro. No. 592/2008, supra note 48.

⁶⁵ Ibid

of insurance businesses under the insurance business proclamation.⁶⁶

In the formation process of a share company, that the founders are obliged to deposit important documents of the company in the registry.⁶⁷ These are namely; the memorandum of association, the articles of association, the prospectus and the minutes of subscribers meeting and all complimentary documents.⁶⁸ In England the memorandum and articles of association are considered as the core constitutional documents of a company.⁶⁹ The articles of association are rules which govern the internal management of the company.⁷⁰ Whereas, broadly speaking the memorandum of association defines the position of a company vis à vis the outside world.⁷¹

Thus, formation of a share company shall be held by public memorandum.⁷² The phrase 'public memorandum' under the Amharic version of the Code provided as 'the association shall be established by a document known by law'. That is why the Code says Share Company is one of the six business organizations and its formation shall be in writing.⁷³

The law provides that the content of the public memorandum with thirteen different elements, among others; the name, address and nationality of the shareholders, value of shares and holding of shares, purposes of the company, profit allowed for

the founders and reason for such payment, value for in kind contribution with its detail description and duration of company's life.⁷⁴ The founder shall draw the articles of association as per the law.⁷⁵ Articles of association govern the operation of the company and shall be deemed to form part of the memorandum of association.⁷⁶ It shall be attached to the public document.⁷⁷

Therefore, before applying for commercial registration founders or members of a business organization shall sign their memorandum and articles of association at the Documents Authentication and Registration Office according to standardized samples of memorandum and articles of association sent to the same office by the Ministry of Trade.⁷⁸ Where shares are not offered for public subscription and the company is formed among the founders that, they shall show in the memorandum of association in which certain conditions shall be complied to the law.⁷⁹

Consequently, at the earliest formation period the following conditions shall to be fulfilled. First, all the shares have been allocated to the founders.⁸⁰ Second, the quarter amount of sums of the capital has been deposited to the bank.⁸¹ Third, the provisions of the law in relation to contributions in kind have been applied.⁸² Finally, all the founders have assigned persons for the administrative organs of the company.⁸³

⁶⁶ See Art. 4 (1) (A)- (F) of Pro. No. 746/2012, supra note 61.

⁶⁷ See Art. 323 of the Commercial Code, supra note 3.

⁶⁸ Id, Art.323 (2) (A) - (D)

⁶⁹ J. James, *Q & A Series Company Law*, 2003, at 32.

⁷⁰ T. LE, *Critical Company Law*, 2008, at 63.

⁷¹ J. James, supra note 69, at 32.

⁷² See opening paragraph of Art.313 of the Commercial Code, supra note 3.

⁷³ Id, Arts.212 and 214

⁷⁴ Id, Art.313 (1) - (13)

⁷⁵ Id, Art.314 (1)

⁷⁶ Id, Art.314 (1) and (2)

⁷⁷ Id, Art.314 (3)

⁷⁸ See Art. 6 (7) of Pro. No. 686/2010, supra note 12.

⁷⁹ See Art. 316 the opening provision of the Commercial Code, supra note 3.

⁸⁰ Id, Art.316 (1)

⁸¹ Id, Art.316 (2)

⁸² Id, Art.316 (3)

⁸³ Id, Art.316 (4)

In France there is different style of particulars provision under the public documents of the company formation with and without public offering.⁸⁴ In Ethiopia, formation of a company by public subscription the formality is totally different from a share company formed among the founders.⁸⁵ Thus, an offer to subscribers shall be made via a prospectus (with its complete legal nuts and bolts) signed by all the founders, to provide a form to be filled application for shares with its place of deposit and to call subscribers meeting.⁸⁶ The founders are under mandatory instruction of the law to communicate the company under formation for the public via prospectus.⁸⁷ As a result, an offer to subscribers shall be made via the prospectus and such document shall contain particulars provided under the law.⁸⁸

⁸⁴ See Paragraph one of Article L225-2 of the *French Commercial Code* in case of formation of with public offering in which the law provides that the draft memorandum and articles of association shall be drawn up and signed by one or more founders, who shall file one copy with the clerk of the Tribunal de commerce of the district in which the registered office is located. In addition, See Article L225-14 of the *French Commercial Code* about Formation without a public offering. It reads as follows. The memorandum and articles of association must contain an evaluation of any contributions in kind. This shall be carried out by an auditor of the formation proceedings, who shall draw up a report under their own responsibility to be annexed to the memorandum and articles of association. The same procedure must be followed if special benefits are specified.

⁸⁵ See Art.317 of the *Commercial Code*, supra note 3.

⁸⁶ Id, Arts.318, 319 and 320

⁸⁷ Id, Art.318

⁸⁸ Id, Art. 318 (1) (A) - (G). The prospectus shall contain the text of the draft public memorandum, a summary of the principal provisions of the articles of association, date of obligations of the subscribers discharged, par value of share, the amount paid until the general meeting, and the place where application for share and payment is made by the subscribers.

3.2. Formation of a share company and its legal implication

Applications for shares shall be made on the form provided and deposited.⁸⁹ The applicant for shares shall to declare that he has read the prospectus and the expert report, if any.⁹⁰ He shall state on the form his name and address, the number of shares applied for and the date of application.⁹¹ In the process of subscription of shares there are rules in paying up of cash shares. Thus, shares subscribed in cash shall be paid upon subscription as to one fourth of their par value or a greater amount if so provided in a public document and where appropriate as to the whole of the premium.⁹² Hence, shares to be registered shares that they have to be fully paid.⁹³ Therefore, the payment for such balance may be spread over a period of five years from the date of registration of the company.⁹⁴

The *Commercial Code* gives an emphasis that after the time of application for shares is expired, and then founders of the company shall to call the subscribers meeting.⁹⁵ One of the purposes of such calling is to decide over the memorandum and articles of association of the company.⁹⁶ Subscribers who came for this meeting draw up the final text of the constitutive documents of the company.⁹⁷

On top of that, the meeting has also a purpose to make all appointments for the management of a company required under the memorandum of

⁸⁹ Id, Art.319 (1)

⁹⁰ Id, Art.319 (2)

⁹¹ Ibid

⁹² Id, Art.338 (1)

⁹³ Ibid

⁹⁴ Id, Art.338 (2)

⁹⁵ Id, Art.320

⁹⁶ Id, Art.321 (2)

⁹⁷ Ibid

association.⁹⁸ To add, such meeting has a purpose to verify about the compliance of the requirements of formation of companies.⁹⁹ Finally, the meeting has also a purpose to approve the contribution in kind and special profit of founders, if any.¹⁰⁰

Any person or business organization carrying out commercial activities within Ethiopia shall to be registered.¹⁰¹ An application for registration is compulsory.¹⁰² As a result, as to the Commercial Code without publicity a business organization shall have neither legal existence nor personality.¹⁰³ This rule is repealed by the new law that is no publicity.¹⁰⁴ However, under previous law business organizations also shall acquire legal personality by registering in the commercial register without being publicized in a newspaper.¹⁰⁵

No person shall engage in any commercial activity that requires business license without being registered in the commercial register.¹⁰⁶ No person shall carry on a commercial activity without obtaining a valid business license.¹⁰⁷ Any person shall be registered in the commercial register, at the place where the head office of his business.¹⁰⁸ A commercial register is administered by Ministry of Trade, which has a nationwide application.¹⁰⁹ Each bureau (regional trade and industry bureau or another appropriate bureau or regional body empowered to issue investment permit) or the

Ethiopian Investment Agency, in accordance with the power delegated to it by this Ministry shall conduct commercial registration.¹¹⁰

Any commercial registration shall be effective from the date of the registration of the applicant in the commercial register.¹¹¹ This situation referred as an effective date of registration.¹¹² The commercial register of business organizations shall be made open for the reference of third parties.¹¹³ Thus, request for entries to the registry is a right granted for any person upon payment of appropriate fee.¹¹⁴ Therefore, registration is imperative act for the company to react against the prescribed functions of share companies. For instance, shares issued before registration of share companies in commercial registry shall be null and void notwithstanding that the liabilities arise thereof.¹¹⁵

The founders shall have registered a newly established share company within one year from paid up capital deposit in a bank.¹¹⁶ However, such period is amended by new legislation.¹¹⁷ Hence, the Ministry of Trade as to the necessity of the situations may grant a period of one additional year for the founder enabling them registering a company.¹¹⁸ Nevertheless, the banking and insurance businesses' legislations provide otherwise. Thus, the new commercial bank which secured permission to trade banking industry shall commence its operation within 12 months from the

⁹⁸ Id, Art.321 (4)

⁹⁹ Id, Art.321(1)

¹⁰⁰ Id, Art.321(3)

¹⁰¹ Id, Art.100 (1)

¹⁰² Ibid

¹⁰³ Id, Art.223

¹⁰⁴ See Art.9 (1) of Pro. No. 686/2010, supra note 12.

¹⁰⁵ See Articles 87, 219, 220, 223 and 224 of the Commercial Code, supra note 3.

¹⁰⁶ See Art.6 (1) of Pro. No. 686/2010, supra note 12.

¹⁰⁷ Id, Art.31 (1)

¹⁰⁸ Id, Art.(2)

¹⁰⁹ Id, Art.5 (1)

¹¹⁰ Id, Art.5(2)

¹¹¹ Id, Art.20

¹¹² Ibid

¹¹³ Id, Art.9 (2)

¹¹⁴ Id, Art.21

¹¹⁵ See Art.327 of the Commercial Code, supra note 3.

¹¹⁶ Id, Art.312 (3)

¹¹⁷ See Art.2 of the amended part under Art. 6 (6) of the Commercial Registration and Business Licensing (As amended), Pro. No. 732, *Federal Negarit Gazette*, Year 18, No.19. 2012.

¹¹⁸ Ibid

date of the issuance of the license by the NBE.¹¹⁹
The same kind of rule holds true for insurance
businesses.¹²⁰

4. The legal relations between and among the founders

In England founders may enter into a contract
among themselves regarding the management of
shares, remuneration, and other lawful matters as
such they are treated as partners.¹²¹ In one case they
are referred as joint adventurers under *Abrams v.*
Puziss, 235 (1963).¹²² Therefore, taking into
account whether they all are on equal footing as co-
founders, whether some are members of the
company and some are agents, or whether some
other actual relationship exists among founders will
become a complex factual issue.¹²³

The situation is worse in case of formation of
companies via publicly subscribed share. However,
the Commercial Code is not clear to deal with such
issues. In a more general term the Code provides
about the commitments entered by the founder for
the formation of share companies.¹²⁴

5. Commitments entered by the founders

The Commercial Code provides commitments
entered into by the founders of the company under
Article 308. The Amharic version of the Code uses
the term (*gedeitawoch*) which means obligations.
The Code provides obligations entailing the
creation of contracts in the earliest period of
formation of companies. However, the Code does

not provide definition for commitments entered by
founders at a company under formation.

In Common Law countries contract which is
entered into by founders with third parties to
acquire some property rights for and on behalf of a
company yet to be formed termed as pre-
incorporation contracts or preliminary contracts.¹²⁵
The legal status of a pre-incorporation contract is
not easy to define and, the general principle goes
that no contract is there if one of the parties to the
contract is not in existence at the time of entering
into the contract.¹²⁶ A pre-incorporation contract is
often incomplete in the sense that such a
contract will not normally provide for the effect
of the contract where the proposed company fails to
incorporate.¹²⁷

A common company form in Germany which is
established by subscription of shares is the
Gesellschaft mit beschränkter Haftung (GmbH).¹²⁸
This type of company has to be registered,
however, the company already has certain rights
and obligations even in its establishment stage
which is known as *Vor GmbH* (pre-*GmbH*).¹²⁹ It is
a legal entity *sui generis*, but is recognized by the
law and all obligations of the *Vor-GmbH* will
transfer to the *GmbH* when the company is
registered as such.¹³⁰

Under the Commercial Code there are two effects
of contracts performed by the founder at a pre

¹¹⁹ See Art.7 (1) of Pro. No. 592/2008, supra note
48.

¹²⁰ See Articles 5 (1) - (3) and 7 (2) Pro. No.
746/2012, supra note 61.

¹²¹ M. Robert, supra note 26, at 8.

¹²² Ibid

¹²³ Ibid

¹²⁴ See Art. 308 of the Commercial Code, supra
note 3.

¹²⁵ K. Esther, "Business Law Notes,"
([http://www.dphu.org/uploads/attachements/books/
books_3498_0.pdf](http://www.dphu.org/uploads/attachements/books/books_3498_0.pdf)) last visited on 23/9/2013.

¹²⁶ Ibid

¹²⁷ Ibid

¹²⁸ P. Eric et al, "German and Canadian Company
Law-an Overview," 2012,
([http://www.poltenassociates.com/Resource/Links/
Polten-CompanyLaw-English-rev.pdf](http://www.poltenassociates.com/Resource/Links/Polten-CompanyLaw-English-rev.pdf)) last visited
on October 16, 2013.

¹²⁹ Ibid

¹³⁰ Ibid

formation period of a company. The company which is successfully established either rejects or accepts the contracts with their legal consequences. Thus, the law provides that the company shall takeover commitments entered by the founders and refund the founders with all the expenses made by them.¹³¹ However, the company shall perform such obligations insofar as such commitments and expenses were necessary for the formation of the company or approved by the general meeting of the subscribers.¹³²

6. Conclusion

The Commercial Code of Ethiopia has to be amended and then would have to provide a clear demarcation among the person who took initiative to form a company, paid subscribed shares as per the time frame limited by the founders, participated in the professional capacity and signed under the prospectus being de jure founders of company and promoters in general at a company under formation. This demarcation will solve the dilemma between the identification of the founders and promoters of the company and other professionals who are actively participated at the company under formation in which this measure will ease to understand the rights and obligations of all persons who are actively engaged in the formation process of share companies.

The law has to make appropriate strata of sharing special profits from the company and about the commission of share subscription derived by the founder. To add, the law has to provide the exact beginning time of the period of founders' special profit. However, in practice the public documents of most companies are used to solve such issues,

but the law fails to say so. Thus, the Company Law of Ethiopia has to provide the legal definition and effects of pre incorporation contracts and to provide its effect in a more plausible manner. In addition, the taking over of such contracts' based on their concluding time, such as: before registration, after registration and before commencement of businesses of share companies. The relationships among the founders, with other promoters, professionals and legal persons serving as agent or promoters of the company have to be reconsidered by the law maker.

The extent of liability of founders shall be extended as to the level of duties introduced by the law and to identify the persons working with the founders at a company under formation their participation to the damage sustained for company or any third parties. Further, the law maker has to introduce the auditing system at a company under formation in order to inspect the same before commencement of a business.

In a nutshell, the writer also calls on all responsible and relevant institutions to play their roles as envisaged by the law. Predominantly, the Ministry of Trade and Documents Registration and Authentication Office are required to discharge their duties they owe under the laws in relation to supervision of the deposit and signing of prospectus, authentication of basic constitutional documents of a share company and other essential documents of the same.

In relation to signing of public documents it is better to adopt the method that signing by officials of the company under formation rather than calling and signing many share holders at authentication.

¹³¹ See Art.308 (2) of the Commercial Code, supra note 3.

¹³² Ibid

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