

Law of Traders and Business Organizations

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Chapter SIX

**Private Limited Company
And**

One Person PLC

Arts. 495-533, 534-545

PLC: Definition and Nature: 495

PLC is a BO whose **capital is fully paid-up in advance**, divided up into shares and **members are not liable for the debts and liabilities of the company** so long as they have **paid up their contributions (495/1)**.

- ✓ Shares of the company may not be made open to public subscription.
- ✓ A private limited company **may not have less than two or more than fifty** members.

In such cases, if member is reduced to one, the PLC will be **dissolved or be registered as a One person company (498/2)** within six months.

- ✓ The company may not issue transferable securities.
- ✓ **Min capital**: 15,000 thousand ETB-496/1
- ✓ **Min par value** of one share: 100 ETB and all shares shall be of equal value. (496/2)

PLC: Nature

- ✓ PLC is instituted when its capital is paid-up fully and the memorandum of association is entered in the commercial register (499/1).

The par value of shares which are sold in cash shall be deposited in a bank account opened in the name of the company under formation before the registration of such company.

- ✓ **MoA:** Art. 500
- ✓ **Contribution** (501): Article 186 with the exception of skill contribution shall be applicable.

When **contribution** is made **in kind** (502) it has to be valued and members are jointly and severally liable to 3rd parties for overvaluation.

Shares & Rights & Duties of Members

A PLC may only issue registered shares in the name of the members (503).

- ✓ Where a share is given as a usufruct or pledge, it will be the pledgee or the usufructuary that will exercise voting rights at meeting (5050).

Members of the company have the right to inspect and make inquiry about documents of the company (504/1)

- ✓ Transfer of shares **is free** unless restricted by MoA and shall be made **in writing** and **also registered** so as to bind third party (508/1/2)

However, a transfer of shares **outside the company** shall be **approved** by members representing at $\frac{3}{4}$ of the capital **unless** unanimity is adopted (509).

- ✓ The same rule applies when the cause of the sale is execution of judgment (510).

The shares of a **deceased** member devolve upon his heirs, unless MoA provides otherwise (511/1).

Management of PLC

- ✓ PLC may be managed by **3-7 directors** when it is required by the MoA (515/1).

The provisions on BD in r/n to SC shall *mutatis mutandis* be applicable to BD of PLC (513/3).

- ✓ A PLC shall have one general manager **appointed** by GM or the BD, if any, which can be member or not (514/1/2).

The **manager** shall have full powers to act in the name of the company in the realization of the business purposes of such company, **in the absence of BD** (515/2)

The manager shall be **liable** to the company, members and third parties for any breaches of his duties under the law or the Mo and in the absence of due care& diligence (516/1/3).

A manager may be **dismissed** by the organ appointing him (517/1)

- ✓ Where a PLC consists of ten and more members or the value of its total assets amounts to five million Ethiopian Birr, it shall have an **auditor** elected by the GM....343-354 shall be applicable *mutatis mutandis* (518)

Meetings in PLC

- ✓ Meetings of a PLC can be ordinary or extraordinary (519)
- ✓ Members can conduct the meeting by an electronic means (520)
- ✓ OGM shall be conducted once annually within 4-6 months from end of each financial year (521/1/2).
- ✓ The meeting may be called by BD, Managers, Auditors or by members having 50% of the capital (521/3).
- ✓ If the members are less than ten, meeting may not be necessary (523).
- ✓ Each member may present or be represented at a meeting and vote in person or through electronic means and **entitled to a number of votes equal to the number of shares (524) .**

Quorum and Majority

In OGM members representing $\frac{1}{2}$ of the capital has to be present (525/1).

Decisions in an OGM are taken by a **simple majority** of shares representing the capital (525/3)

Quorum and majority in Extra-OGM (526)

- ✓ **Unanimous** decision: to **change in the nationality or increase in the capital** of the company by raising the par value of existing shares
- ✓ **$\frac{3}{4}^{\text{th}}$ majority** of the members representing capital of the company to amend MoA (526/2)

Accounts

Legal Reserve: 5% of the profits shall be transferred each year to the LR until such fund amounts 10% of the capital (528).

Members are required to repay a fictitious dividend, if any, within 5 years (529/1/2).

Dissolution and Winding-up

- ✓ When it achieved its purpose, fixed period expires, members agreement, by court at request of members for good cause (181) (532/1)
- ✓ Loss of 3/4th of its legal capital and thus BD or managers cause members decide for dissolution (532/1)

In relation to **winding-up**, articles 473-491 shall be applicable as appropriate (533)

One Person PLC: Nature and Justification

OPPLC is a BO incorporated by the **unilateral declaration** of a single person (534/1).

The company has **legal personality separate and distinct from that of the member**. Thus, the owner enjoys Limited Liability.

- ✓ The member/sole owner/ shall not be personally liable for debts due by the company in so far as he has fully made his contribution (534/3).

Why OPPLC?

- The introduction of the OPPLC solves the age old problem of **bonding with a partner for the sole reason of meeting the minimum number** of two shareholders.
- Such problem **was even more challenging for foreign investors who must find partners from local investors for non business reasons**. Often, the companies are run as one member Company, and there was no meaning in requiring a minimum of two members.

OPPLC Contd.

- The capital of OPPLC shall not be less than 15,000 (fifteen thousand) Ethiopian Birr (535).
- The **unilateral declaration(UD)** incorporating a OPPLC shall be **made before an authority entrusted with authentication of documents** and entered into the commercial register (536/1).

Contents and forms of the UD : Read (536/2)

A OPPLC may not be formed unless the **nominee?** has declared his acceptance of the nomination before an authority authorized to authenticate documents (537).

- ✓ OPPLC Can be formed **by converting sole proprietorship** to OPPLC (538/1).
- ✓ In such cases, the sole proprietor **shall remain personally liable for all debts incurred prior** to the formation of the one person private limited company through conversion (538/2)

OPPLC Contd.

It is prohibited that the sole shareholder cannot itself be a PLC-Article 539. i.e OPPLC by itself cannot form another OPPLC (539/1).

If any, such fact can be cause for dissolution (539/2) of the OPPLC formed by such violations.

- There seems no prohibition against other forms of business organizations (Share companies, PLCs) to set up a one member company. **But, should they be allowed?**

The sole member in OPPLC can make **in kind contribution** (340).

- OPPLC shall have a **general manager** who may or may not be the member (owner) of the company (541/1).
- The **manager** of OPPLC shall have the same powers vested in GM of the PLC (541/2).
- The member of the company shall exercise the powers of the **GM of shareholders** in a PLC (542/1-4).

OPPLC: Liability and Dissolution

Even though the sole **member** of the OPPLC is entitled to Limited Liability (334/3), he/she shall be **jointly and severally** liable **with the company** where he is found to have committed one of the following (343:

1. **commission of unlawful act** intentionally that jeopardizes the interests of the company or creditors of the company;
2. **merger** of the assets of the company with his property;
3. **failure to separate his own legal personality** from that of the company;
4. release of information on the financial status of the company **to deliberately mislead the creditors** of the company;
5. **make use of the assets of the company** w/t payment or agreement for his personal benefits or that of third parties;
6. payment of dividends that exceeds the limit set by the law;
7. commission of other similar acts.

OPPLC: Dissolution -544

- ✓ When a OPPLC is dissolved and **all its debts are settled** all the assets of the company shall be assigned to the member **without liquidation of assets taking place (544/1)**.
- ✓ If a if claimants appear after the dissolution the member himself shall be liable for all the debts and obligations of the company (544/2).
- ✓ Claims of such creditors after dissolution shall be barred after **five years** from the date when the aggrieved party knew of the dissolution and will **absolutely be barred** after **ten years** from the date when the transfer of the assets of the company to the member took place (544/3).
- ✓ It is possible that the member may **choose to follow the route of liquidation** upon the dissolution of the company (544/4).

Every rules governing PLC may be applicable to OPPLC *mutatis mutandis* (545)

Chapter Seven

Conversion of BO

Group of Companies

Merger and Division of BO

Branches of Foreign BOs

Conversion of BO

Articles 546-549

1. Conversion of BO 546-549

A BO ones formed can be converted in to another form.

- ✓ Thus, when a BO is converted in to another form it does not cause creation of a new legal personality, but amendment of MoA (546/1).

Conversion may be decided by unanimous or majority as required by the law or MoA.

When conversion is successful, the rules relating to formation of the relevant new BO shall apply (546/3)

The conversion so made has to be **published** in a news paper and on the website of the company.

- ✓ Conversion **shall not deprive** in whole or in part, **membership right or increase liability of a shareholder w/t** their consent (546/3).
- ✓ If a shareholders dissent to the conversion, they may **withdraw by selling their shares to the BO (547).**

Conversion of BO Contd.

Rights of Creditors 548

- ✓ Rights and duties of the former firm shall pass to the new BO from the date of its registration
- ✓ Thus, up on registration of the new BO, creditors of the former firm shall establish their claim forthwith (548/2).

Liability of Partners 549

- ✓ The conversion **shall not discharge** members **with UL** of their liability **for undertaking by the firm before its conversion**, unless the creditors approve such conversion (549/1).
- ✓ If a SC, PLC or a OPPLC is converted in to partnership, the partners may not be liable for a liability of the company before its conversion
- ✓ **Conversion** is deemed to be **approved** if creditors fail to object to the conversion within 30 days after informed of the decision of conversion through a letter.

Group of Companies

Articles 550-564

2. Group of Companies 550-564

Group of Companies aka **Corporate Group** is a collection of parent and subsidiary corporations that function as a single economic entity through a common source of control.

- ✓ The group of companies may be owned by a **holding/parent company** which may have no operation itself.
- ✓ If the corporations in the group **engage in entirely different businesses**, the group is called **conglomerate** (E.g. **MIDROC** with over 80 group & affiliate companies).

The new commercial code recognize the practice of group companies and tries to regulate certain practice in relation to GC in a more refined and comprehensive way.

Group Companies: Definition 550

A “**group**” is a set of companies comprising of the parent company and **all its national and foreign subsidiaries**, unless otherwise indicated (550/1).

A “**subsidiary**” is a company **subjected to the control of another company**, the “parent” company, **either directly or indirectly through another subsidiary**.

A “**parent**” is a company **that has subjected another company to control** either directly or indirectly through the instrumentality of another company.

A ‘**wholly-owned Company**’ is a company **with no other shareholders except** its parent company and any other subsidiary of its parent company or persons acting on behalf of its parent or such other subsidiaries.

What constitutes control? 552.

Group Companies: Parent Subsidiary Control

□Control is the power to govern, alone or with other shareholders, the financial and operating policies of a subsidiary (552/1).

Control of a subsidiary exists where a company owns, directly or indirectly, **more than half of the voting rights** in that subsidiary(552/2)

✓ **Exceptionally**, it may be proved that such ownership does not constitute control (552/2).

What if one company holds half or less than half of the voting right in another company?

In such cases, control exists if the company has the right to **(552/3/a-d)**:

1. Exercise more than half of the voting rights by virtue of an agreement with other sh/holders
2. Control financial& operating policies of a company under the MoA or any agreement

Parent Subsidiary Contd.

3. **Appoint or remove the majority of the members of the governing body**, & this body has control of the business (**for 2 successive years**)

4. **Exercise actual majority votes at GM** and thus the actual control of the business (**for 2 S years**).

The Relevant Company is deemed to have effected such appointments if, during that financial year, it **held a fraction of the voting rights greater than 40%**, and if no other shareholder directly or indirectly held a fraction greater than its own (552/4).

Duty to disclose control: The management of the parent company **must inform in writing** the management of a subsidiary as soon as control has been established or removed (554/1).

✓ The subsidiary on the other hand must inform without delay the parent company of **the number of shares and voting rights held by it** in the parent company, and in any other companies (554/2).

Parent Subsidiary Contd.

Rights of the Parent Company

- ✓ A parent company has the **right to give instructions to the organs of management of its subsidiaries** (556/1).

However, directors and managers of the subsidiary who are not appointed by the parent company may not be bound by any of such instruction.

- ✓ The BD and management of the PC has the **right to obtain information from the subsidiary**, unless such information violates laws of the country of the subsidiary or 3rd party-557
- ✓ **Right to squeeze-out**: the PC controlling more than 90% of the shares & votes of the subsidiary has the right to purchase the remaining shares (558+294/2-7)

Shareholders of the **PC** have the **right to** get information, access reports of BD and balance sheet as well the right to demand special investigation as per articles 355, 358, 381/1/a&b)

Parent Subsidiary Contd.

Rights of the Subsidiary Company

1. **Right to corporate opportunity:** When a subsidiary is not a wholly owned company, the PC must not itself or through another subsidiary exploit a **corporate opportunity** of the subsidiary **w/t approval** of the BD or the non controlling shareholders of the subsidiary(560)
2. **Right to demand special investigation:** Shareholders of a subsidiary that hold voting shares that **represent 10% of the capital** can request a special investigation in the PC in relation to a **decision which has affected that subsidiary (561)**
3. **Right to sell out:** when the PC own in/directly more than 90% of shares with voting rights in the subsidiary, the sh/holders may request that their share be purchased (562+292)

Reciprocal/Cross Holding of Shares

Cross holding is a situation in which two companies hold share in each other.

Without the need to have parent-subsidary relationship, companies may have a cross holding.

Thus, in such cases, where 5% or more of the capital of the 1st company is held by the 2nd company, the 1st company may not hold shares in the 2nd company (55/2).

✓ Thus, the **max amount of cross holding shares is 5%** of the capital of the company.

If both companies held more than 5% of each others share, they are required to report their holding to the Ministry of Trade and thus **reduce** the same to 5%. (555/3&4)

✓ A subsidiary may not hold any shares directly or indirectly in the parent company (555/1)

Merger and Division of BO

Articles 565-577

3. Merger and Division

Merger of a BO is an operation whereby two or more BO merge into one.

The merger may take place in either of the following two forms:

1. Merger by **formation of a new BO**: whereby two or more BO are wound up without liquidation by transferring all their assets and liabilities to the new BO they themselves form (565/2).
 2. Merger by **Acquisition**: whereby one or more BO are wound up w/t liquidation by transferring all their assets & liabilities to a pre-existing organization (565/3).
- ✓ A BO under liquidation to dissolve may merge with another organization before distribution of assets takes place.
 - ✓ Merger may take place between any forms of business organizations.

3. Merger and Division

Division is the operation whereby a BO is wound up w/t liquidation by transferring its assets and liabilities to more than one BO.

- ✓ Thus, division can also be by acquisition or formation of a new BO (566/1-3).
- ❑ Division by **acquisition** is the operation whereby a BO is wound up without liquidation by transferring all its assets and liabilities to more than one other preexisting BOs.
- ❑ Division by the **formation of new** BO is the operation whereby a BO is wound up without liquidation by transferring all its assets and liabilities to BO formed by it.

Dividing/giving a certain portion of asset means separating a business unit that can subsist separately or part of assets of organization and transferring the same to a BO that is under formation or to an existing organization **by way of contribution (566/4)**.

Merger and Division: The Process

Plan: The **BD** or in their absence the **general manager** of the BO participate in the Merger or Division are required to **draw a merger/division plan**.

✓ The **details** of the plan has to include the list of 567/2/a-m.

Report: The BD or the GM of each merging or dividing BO shall draw up a detailed written **report**

Examination: The merger or division plan, report and other necessary conditions for the merger or division shall be **examined** by an independent and impartial expert to be appointed by each BOs involved (569).

Approval: The merger or division must be **approved** by the **general meeting** of each of the BOs participating in the merger or division (571) and preferred shareholders **special meeting**, if any.

Publication: the approved plan of M/D has to be publicized via a news paper/website once a month for two months (572/1/2).

Merger and Division: Effect

Merger or Division shall be **effective** as of date of entry in to the commercial register of the new BO created as a result of M/D or amendment of MoA of the pre-existing BO if the M/D is by way of acquisition. (573)

Merger and Division shall have the ff effects:

- ✓ **Winding-up** of the BO that ceases to exist w/t the need for liquidation
- ✓ **Transfer of asset& liabilities** of the BO that ceases to exist owing to M/D to the acquiring/new BO
- ✓ **Issuance of shares** in exchange to the sh/holders or partners of the BO that is wounding up **in the** acquiring/newly formed BO.

Annulment of M/D: If there a need be, the merger or division may only be annulled by order of the **court** for **failure to comply with the procedural requirements** (574/3&4).

Rights of Creditors & Debenture Holders during M&D

Creditors **whose claims against the BO** participating in M/D **antedate** the publication of the M/D plan in a newspaper and **have not fallen due** at the time of such publication may petition the court to grant them adequate securities if (576):

- ✓ When they are not sufficiently protected a/r the merger/division and the same is concluded by the impartial expert
- ✓ The financial standing of the BO involved in M/D poses a particular risk to the rights of creditors

Such creditors must bring their claim within **two months** after the plan to M/D is approved and publicized.

- ✓ If the debenture holders of the BO involved in M/D oppose to the M/D via their meeting, the debtor BO shall **redeem the debenture by paying its par and interest due** (577/1&2).

Branches of Foreign BO

Articles 578-587

Branch

Branch is a fixed establishment of a foreign BO or a similar entity that is **staffed and set up to pursue economic activity for gain on behalf and for the account of the said BO** or similar entity for a **definite or indefinite** period (778/1).

- ✓ The branch does not have an autonomous legal entity distinct from that of the business organization or the similar entity that owns it.
- ✓ The rights and obligations arising from its activity shall be part of the assets of the business organization or the similar entity that owns it.

A foreign BO or similar entity incorporated abroad may operate via branch in Ethiopia a/r registration in the commercial register (779).

A **branch** must have its own **manager** and if it is a foreign business, with a power to represent the BO in legal proceedings (581).

Branch Deregistration 583

A branch shall be removed from the Commercial Register if any of the following occurs:

1. The foreign BO or similar entity is dissolved
2. The foreign BO closes the branch
3. The branch **has no manager** and this is not remedied within **six** months from the removal of the previous manager
4. The branch manager has failed to file, as soon as reasonably possible, accounting documents and other statements regarding the foreign business organization or entity as required under Article 582 of this law and
5. A branch **creditor establishes that his claim cannot be satisfied** out of the foreign BO assets within Ethiopia.

Applicability of Ethiopian Laws

1. **Real Seat Theory:** a BO formed abroad may be recognized but will be made **subject of the law of the host state** and has to go through the **registration** process.
2. **Incorporation Theory:** a BO formed fulfilling the law of the place of incorporation is recognized everywhere. Thus it will be subject of the law of the place of incorporations.

BO incorporated abroad or sole proprietorships established outside Ethiopia and whose head office or principal place of business is in Ethiopia shall **be subject to the relevant provisions of this code and other laws of Ethiopia (584)**. (Real seat Theory)

- ✓ The commercial code shall apply to BO or sole proprietorships incorporated or established pursuant to Ethiopian law and operating abroad (585)
- ✓ Firms incorporated abroad having a form differs from those recognized by the code, shall be subject to provisions governing share company as appropriate in relation to **registration, Sh GM, and liability** of directors (586).

Minority Shareholders Protection

Who are they?

Minority Shareholders Protection

Who are Minority shareholders?

OECD: are those sh/holders **who collectively own 10% or lesser** of the legal capital of the company.

✓ The old commercial code remained weak in terms of protecting minority investors in companies.

This new commercial code introduces remarkable improvements in this regard.

From the FDI promotion perspective, **the desire of improving the doing business rank** was the major impetus behind these change.

Some of these **changes/protection** are the following:

1. Article 292: Requirement of mandatory (redemption) bid:- when a single shareholder acquires 90% or more of the shares of a company, a minority shareholder can compel such controlling shareholder to buy his/her shares **at a price proposed by the minority** shareholder or failing agreement, at a price **fixed by an expert appointed by the court.**

Minority Shareholders Protection Contd.

2. Article 328: **The right to institute action against directors:** *Ethiopian law doesn't allow derivative suit by shareholder on behalf of the company.*
 - If the Sh GM fails to adopt a resolution to prosecute directors or the company fails to prosecute a/r such resolution, **shareholders representing 10%** of the *shares* can institute the action. *It was 20% in the old code.*
3. Article 351: **Requiring Auditor to Convene a meeting:** minority shareholders representing **at least 10%** of the share capital can request the auditor of the company to convene a general meeting of shareholders. *It was 20% in the old code.*
4. Article 366(3): 5% of shareholders can **request Court to Order Convocation of GM:** it was 10% in the old code.

Minority Shareholders Protection Contd.

5. Article 381 & 382: **access to documents**:- the biggest obstacle for minority shareholders is accessing documents to prove suspicions of mismanagement.

The old code allows limited set of documents such as audit reports, attendance sheets, shareholder lists, and minutes of resolutions. But the new code includes the **list of related parties, compensation paid to executives, and copies of suspected transactions** - Article 328(4).

6. Article 396: **Can have a special inspection/audit appointed** :- shareholders representing 10% shares can **request the company or the court to appoint a special inspector** to investigate certain transactions which they suspect to be harmful to the company.

The End of the Beginning

Thank You!