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POST GRADUATE PROGRAM
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**REGULATION OF FORMATION AND COMMENCEMENT OF
BUSINESS BY SHARE COMPANIES ESTABLISHED THROUGH PUBLIC
SUBSCRIPTION OF SHARES IN ADDIS ABABA:
THE LAW AND THE PRACTICE**

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DECLARATION

I, the undersigned, declare that the thesis comprises my own original work and has not been submitted to any University for any awards and, in compliance with widely accepted practices; I have duly acknowledged and referenced all materials used in this work.

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The thesis titled “Regulation of formation and commencement of business by share companies established through public subscription of shares in Addis Ababa; The law and the practice” by Mr. Metages Tewabe is approved for the degree of Master of Laws (LLM).

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Abbreviations

Art	Article
Arts	Articles
CEO	Chief Executive Officer
Com C	the Commercial Code of Ethiopia
CSRC	China Securities Regulatory Commission
E. g	is short for ‘exemplegracia’ which, in Latin, means for example.
ECCSA	Ethiopian Chamber of Commerce &Sectorial Association
Edn	edition
EPRDF	Ethiopia People Revolution Democratic Front
FDRE	the Government of the Federal Democratic Republic of Ethiopia
Ibid	is short for ibidem which, in Latin, means in the same place
Id	idem = the same, the same place but in different page
MOT	Ministry of trade
NBE	National Bank of Ethiopia
No	Number
OECD	Organization for Economic Development and Cooperation
P	Page
Pp	Pages
SEC	Securities and Exchange Commission’s
USA	United States of America
Vol	volume

CHAPTER ONE

1. Introduction

1.1. Background

This era is a period where multinational companies are getting trust in every sector of the economy and bringing the world together as ones. To defend against the challenges of commerce, nowadays, business in organized way is almost indispensable. Business people may chain themselves by business tie for various reasons. Some areas of business demand massive capital that may not be easily financed by a sole proprietor or with capital of few business persons. Hence, greater unity is essential when an area of investment is very capital incentive.¹

The share companies are suitable for large-scale economic activities with substantial resources. They were formed mostly by public subscription, which allows the public to contribute and become shareholders.² Companies often accumulate enormous capital from many shareholders. They generate a vast proportion of the world's wealth.³ Due to their limited liability, accumulation of enormous capital and transferability of share, companies are going to select a business organization. Furthermore, they are suitable for running commercial enterprise and they are the most comfortable way to work together.⁴

These companies are not something that comes into existence by themselves rather they are the result of huge planning and preparation of individuals.⁵ These individuals will be described as 'founders' of the company. Companies like human beings must be conceived before they are born. The conception and the gestation period of companies are managed by these categories of person. Before birth (incorporation), founders enter in to contracts on behalf of yet to be born company and undertake to perform all the necessary activities to bring the company into life. This power of founder is open for abusive, fraudulent and rent seeking practices and can

¹Lantera Nadew, Pre-incorporation management under the Ethiopian company law: the need to redefine the provision defining founders, [2007], vol 1 no 1, Jimma University, journal of law, p 1.

²Ermias Ayalew and Nega Mihretie, law of traders and business organizations, Bihar Dar University and Jimma University, by justice and legal system research institute 2010, p 73.

³Jaint dine & Marios Koutsias, *company law*, 7th edition, palgravemacmillan law masters, Florence Italy, 2009, p 1.

⁴Nigusies Tadesse, Major problems associated with private limited companies in Ethiopia: the law and the practice, (LL thesis, Addis Ababa university, 2009) p 32

⁵Sitelbenat Hassen, 'Some Remarks on the right and responsibilities of founder under the Ethiopian commercial code'[2017] vol 8, no 4 journal of social science and humanity, p1,

undermine permanently the success of the company unless well regulated⁶. After companies incorporated the board or director of companies, they manage the operation of share companies. Even if companies are owned by many shareholders, they are usually managed by few.⁷ In share companies there is separation of ownership and control. Such separation of ownership and management would ultimately trigger mismanagement of the numerous shareholders by the leaders unfairly and the company may fail in to his/her hands.

A share company comes to into existence when it is registered; a certificate of incorporation fulfilled and satisfied other formality that requires for the formation share companies. Then the company becomes entitled to commence its business.⁸Where the formation of a share company is as between the founders (closed corporation), the law in Ethiopia requires them to show in the memorandum of association that all the shares have been allocated and the sums have been deposited in a bank in the name of company. The other method of forming a Share Company is by public subscription whereby the public is invited with the view to raise money for the pre-fixed capital of the company.⁹ An offer to the subscribers should be made by a document called prospectus signed by all the founders and must show the indications under Art.318 (1) of the Commercial Code. Formation of a share company by public subscription also requires other formalities to be complied with.¹⁰

The formation process and beginning of operation of share companies are regulated for the protection of individual investors and to maintain the stability of the economies of the countries as a whole.¹¹ Regulation of the agents who control formation process and operation of the industries performs protection of investors, pre-incorporation creditors, public interest, countries resource, etc. Unless those who run the industry are well regulated, they should affect investors

⁶ Seyoum Yehonnes ,'on Formation of share company inEthiopia' [2008],XXII,1 journal of Ethiopian law P 102

⁷FekaduPetros, Emerging separation of ownership and control in Ethiopian share companies: legal and policy implications, [2010] ,vol 4 no.1, Mizan law review Addis Ababa university march, p 2

⁸AlamnehSinishaw, The nature and scope of private limited companies in Ethiopia: the law and practice focus on bankruptcy ,(thesis paper, St. Mary's university college2008), p 20

⁹ Commercial Code of the empire of Ethiopia, 1960, extra ordinary issue, Negaritgazetta, year 19th, no3, art 315 {hereinafter Commercial Code} Art 317, closed corporation is a firm whose all issued shares are held by a family or a small group of investors and is not be publicly traded.

¹⁰ Id supra note 10 art 318(1)

¹¹Goodhart.Cerra.E, Regulating financial services and market in the twenty first century : An overview,(1st ed published in north America by hurt published, 2001) p 25

by making fraud or damaging by using their controlling position to operate their business in a way that would threaten the soundness of the industry.¹²

Besides the establishment of regulatory frameworks, Public Authority Regulatory Organization is also areas of priority that the experiences of other countries revealed.¹³ As a result those investors subscribing to the shares would begin to worry and question about the entire legal system as to whether a proper mechanism is in place to protect their interest in case the formation process and operation of companies.¹⁴ A well-functioning regulatory framework minimizes the costs of business formation, operation and closure. The rules governing business an entry of public corporation play vital role encouraging investment and business operations. Regulation of formation and commencement of business of companies have the role of protecting and benefiting public at large¹⁵. It is therefore vital thus, the law regarding formation process and operation of companies should be clear¹⁶.

The Ethiopian commercial code of 1960 created a comprehensive law of business organizations in the country and served for the formation and operation of companies in the country.¹⁷ In addition, the government introduced the new commercial registration and business licensing proclamation No. 980/2016.¹⁸ The Previous proclamation, No.686/2010 has now been repealed by this proclamation to regulate business license and registration of companies. Currently Ethiopia is witnessing the explosion of companies which are offering share for public subscriptions¹⁹. Specifically companies are boosting from time to time rapidly in Addis Ababa.²⁰ However, the existing legal frameworks and institution were criticized for not

¹² Tikile Kemulachewu, Regulation of initial public offering of shares in Ethiopia, critical issues and challenges ,(LLM thesis paper Addis Ababa university unpublished ,2011) p 3

¹³ Ibid

¹⁴ Ibid

¹⁵ Michael Hantke, The public interest theory of regulation? , Non-existence or misinterpretation.[2003] vol 15 no2 European journal of law and economics, 2003 available at <https://link.springer.com/article/10.1023/A:1021814416688> accessed march 2018

¹⁶ Wilfred M. Estey, pre-incorporation contracts: the fog is finally lifting,[2002] vol 33, can ,bus, LJ, ,p 36

¹⁷ Getahun Seifu, revisiting company law with the advent of Ethiopia commodity exchange,[March 2010] Vol. 4 No.1 Mizan Law Review, p 103.

¹⁸ See commercial registration and business licensing proclamation no. 980/2016, fed Negaritgazetta 22th year no. 101, Addis Ababa, July 2016.

¹⁹ Id supra note 12, p 1, available unpublished available at www.Abyssinia Law .com

²⁰ Amhabekele and Zemedeneh, company registration in Ethiopia,[2005, Addis Ababa chambers of commerce, research paper,p1, available at www.ethiopianchamber.com/Data/Sites/1/psd.../company-registration-in-ethiopia.pdf accessed on march 3

adequately regulate the share companies and share company law provision are no supplemented by other legislation.²¹There are, however, many companies failed to operate the business after registration and on beginning of operation.²²

The Government of the Federal Democratic Republic of Ethiopia (FDRE) has prioritized private-sector growth as a means of alleviating chronic poverty and bringing about economic growth in line with international development thinking and economic good practices.²³To achieve an orderly private-sector growth, a range of institutional infrastructure, including statistical and regulatory infrastructure need to be put in place.²⁴As result the problem with regard to the legal frame work and institutional set up that regulated Fraudulent or careless practice in the formation and operation of companies, it may undermines permanently the success of the company. Such practice can also jeopardize the legitimate interests of future creditors of the company²⁵.Well developed and efficient formation and operation regulation is fuels for economic growth as well as the regulation of public companies help to protect investors, especially against fraudulent or manipulative behavior founders and other management of the company.

These are the main issues or tricky situations that made the writer to carry out this research on the title” *regulation of formation and commencement of business by share companies established through public subscription of share in Addis Ababa: the law and the practice*”. From interview with the expert from ministry of trade, companies after legally formed failed commencement of business for long period of time for different reasons especially in manufacturing sector.²⁶ However this action negatively affects the subscriber, pre-incorporation creditors, resource of the countries and lowering of investors’ confidence in buying shares in future share companies. Hence this study deals with deficiencies in the existing relevant laws and practice in addressing issues in the title. Thus, in this study the writer’s attempt was to identify whether the root cause of the problem is the gap in the law or institutional failure in practice and put possible recommendations to the aforementioned problem.

²¹ Interview with yosefAlamu, head of directorate, share companies and sector association follow up and support directorate, in ministry of trade, march 17,2010 and Gebeyaw Simachewu ,Ethiopian share companies in light of OECD principle of corporate governance, thesis paper, university of London, p 2,2012

²² Ibid

²³ Id supra note 20 p5

²⁴ Ibid

²⁵ Id supra note 6, P102

²⁶ ibid

1.2. Statement of the Problem

The development of public share companies in Ethiopia is a very recent phenomenon. The socialist system of governance which was overthrown in 1991 by current governance system and it was only after this regime change that country has experienced a market economy.²⁷ In Ethiopia, in between 2000 -2005E.C. fiscal year witnessed increasing of huge business organization in all corner of the country. Between these years the general public as well as the business community also began to engage in share companies which require cooperation and large investment. The number of companies registered within Addis Ababa within these years increased rapidly and forecasted to grow constantly by more than 10% for next few years.²⁸ But unfortunately the number of registered company was highly decreased in 2009 and 2010(nine month report) due to loss of confidence by general public on this type of companies.²⁹ These clearly indicate the less growth of share companies in the town currently.

Companies cannot operate successfully without adequate rules that govern formation and operation of companies. The 1960 Commercial Code of Ethiopia and commercial registration and licensing proclamation No 980/2016 incorporate provisions that related to regulating formation companies and operation.³⁰ However, such provisions are criticized for not adequately protect the right of innocent subscribers, 3rd party and company under formation itself.³¹

Specific Problem

- Problem related to regulatory framework and institutions. Even if currently massive and diversity sector of share company is formed with huge capital and thousands of investors are subscribing to those incorporating companies, the regulatory and institutional framework have criticized for not well regulating and limited capacity of the regulators to implement the relevant law and the proclamation in managing formation and operation of share companies in Ethiopia.

²⁷Assefa Aragay Sefera, Corporate governance rules in Ethiopia and Germany: A comparative analysis ,[LLM Thesis central European university] , 2015 available at

[https://www.google.com/search?ei=4dAYWe+governance+rules+in+Ethiopia+and+Germany%3A+A+comparative+analysis+%2C+\[LLM++Thesis+central++European+university](https://www.google.com/search?ei=4dAYWe+governance+rules+in+Ethiopia+and+Germany%3A+A+comparative+analysis+%2C+[LLM++Thesis+central++European+university) accessed on march 23

²⁸ Id supra note 20 p 61

²⁹ Interview with Abiy Mohamed, trade team leader share companies and sector association follow up and support in ministry of, march 12,2018 and from company Data and report of the office that acquires from ministry of trade Share companies and sector association follow up and support directorate office.

³⁰ Id supra note 18

³¹ Ibid supra note 21

- Problem associated with lack of commence the business by share companies in Addis Ababa for long period of time after their registration is ended and collect huge amount money from the public.³²
- Another problem is related to regulating individual participating in formation and beginning operation of share companies. I.e. currently though founders who operate the company are few in numbers, even the group founders may establish more than one company that might fail to start operation due to their fault, fraudulent, lack of capacity, skilled professional, etc. Even after the company they try to form had failed to commence the business due to these reasons, they passed to form another company. Though they have bad reputation from their deed, they run to affect the interest of public and individual resource.³³
- Problem associated to lack of support and follow up on behalf relevant authority. I.e. even if the law says registration has been affected within one year from deposit in a bank, practically most companies are registered after one year and some companies may not enter into business approximately up to 5 to 6 years after registration; lastly they could fail the operation after many resources are damaged. This show that as the practice of formation and operation of companies have problem.
- Additionally, the last Problem is related to lack of taking appropriate administrative measure by relevant authority during formation of companies and operation of share companies. Thus, when conflict created between founders or director and company under formation (subscriber), the plaintiff takes the case to the court to end up the dispute; but the court procedure may take 5 up to 6 years. During these time the relevant authorities may not take appropriate administrative measures even if those individual that manage the companies cause an harm to the company under formation or on the beginning operation of the business since the laws not conferred this right on them.

Fraudulent or careless practice in this formation process can undermine permanently the financial solidity, creditworthiness and profitability of the companies. Such practices can also lead to the risk of legitimate interests of future creditors of the company, willingness reducing of

³² Id supra Note 29

³³ Id Supra note 21

buying share among the society; it diminishes loss of confidence on companies under formation, unless granted by tight legal rules and regulation.

1.3. Literature Review

The Ethiopian commercial code, particularly Book II Title VI of the code tried to address issues of formation process and operation of share companies.³⁴ However, it have legal and practical problem that make formation of companies in Ethiopia less effective and inefficient. There is no supplementary and updated legal framework that dully ensures the success of the formation and operation of companies. In addressing formation of companies some work and studies have been published over the years and the writer is going to use some of those works and shows the point with which this study departs from those studies.

SeyoumYohannes³⁵ addresses the issues related to formation of companies under the Ethiopia company law. Seyoum in his article examines Ethiopia's company law with reference to nature and requirements formation of Share Company's .He argues that contribution in kind and valuation is exposed creditors to greater risk and contribution in service not expressly addressed n Ethiopian company law. His study focuses only on nature and requirements for formation of company under Ethiopian, more focused and not discussed directly and analytically issue related to the gap in law and institutional framework for failure of share companies in practice.

TikikileKumulachew,³⁶ on the other hand, in his article titled regulation of initial public offering of shares in Ethiopia, critical issues and challenges argues that Company Law seems neglected to be re-engineered with appropriate mechanisms to make the system successful. On his study examined that problems related to regulation of prospectuses, regulatory frame works and remedies. As a result, he commend that the law maker need to give special emphasis on the issues of regulation of initial public offering since it have vital role in economic growth and development. The writers, however, does not deal in their article directly and systematically the problems that raised in above.

³⁴ Id supra note 9

³⁵ Id supra note 6

³⁶ Id supra note 12

Serkalem Eshetie³⁷ in her article on the title of founders of share companies under the Ethiopian share company law: legal analysis. She argues that the Ethiopian share company law recognizes large number of persons as founders which is against the general convention in the area. Point out that not all founders in the law shall be held Responsible for the liabilities that may emanate from the activities pertaining to forming a share company. Serkalem in here article suggests that the law on founders should be revisited to avoid the pitfalls arising out of the process of establishing share companies. In her article, she does not address problem related to regulation of formation process of company and not addressed the issues raised question.

1.4. Research Objective

1.4.1. General Objective

The general objective of this research is to critically examine regulation of formation process and commencement of business by Ethiopian share companies established through public subscription of shares.

1.4.2. Specific Objectives

To attain the general objective and conditional on it, the research specifically was committed in the following specific objective:

- To investigate the prevalent practical challenges in formation and commencement of business by share companies established through public subscription of shares in Addis Ababa.
- To detect out the gaps of legal provisions that regulating formation process and commencement of business of share companies as well as recommended solutions.
- To examine the regulatory and institution framework that enforcing the existing laws of formation process and operation of share companies by assessing the practice.
- To recommend solution for practical problems in formation and commencement of business by s share companies that established through public subscription of shares.

³⁷Serkalemesheti, Founders of share companies under the Ethiopian share company law, Legal analysis,[2016] (vol 5, no 1,Haramaya university law review available at <https://www.ajol.info/index.php/hlr/issue/view/16160> accessed on February 3

1.5. Research Questions

To accomplish the above set of research objectives and searching the possible solutions to the legal and practical problems of formation process and operation of Share Company under Ethiopian company law, the writer addressed the following questions all the way through the research:

1.5.1 Central Question

Is the existing legal and institutional framework on formation and commencement of business by share companies established through public subscription of shares in Ethiopia is adequate and what are prevalent practical challenges in Addis Ababa?

1.5.2. Specific Questions

1. Are the existing legal framework governing formation and commencement of business by share companies that established through public subscription of shares adequate or strong enough?
2. What are the causes of the problems, and the possible solutions in formation and commencement of business by share companies that established through public subscription of shares in Addis Ababa?
3. Is the regulatory institution competent enough to enforce the existing legal regimes?

1.6. Significance of the Study

In Ethiopia, share companies are dramatically increasing in all corners of the country and its role in the economy of the country is also considerable. Share companies are practiced and operated in many sectors of the economy. Companies play paramount role to satisfy the taste, demand and interest of human beings as well as to bring a wide range of developments and structural transformations in a country.

The paper examined the formation and commencement of business by Share Company in Ethiopia and the practice particularly in Addis Ababa. Hence it was an input for the legislature to enact appropriate law of companies and expected to benefit the government in evaluating its laws and regulatory institution in implementing relation to the formation and commencement of business by share companies established through public subscription of shares. By so doing, it tries to show appropriate and effective legal framework that safeguard the interests of all parties

having interests in the formation process and operation of share companies. This, in turn, would facilitate the formation of Share Companies which are much needed in the country. Finally, it can also serve as a stepped stone for further research on the subject matter.

1.7. Methodology of the Study

The method emphasized in the investigation on regulating process of company formation and commencement of business based on the Ethiopian Commercial Code of 1960 and proclamation related to process of formation and commencement of business of share companies established through public subscription of shares. The samples study of the companies situate in Addis Ababa, refining to prospectuses, data and company files obtained from MOT, memorandum and articles of associations were used. Besides, it was also more suitable to analyze data gathered through interview and some types of texts that were relevant to this study. The study employed both doctrinal and empirical research methodologies. The study is qualitative in that it was devoted on the reasons, justifications and logical arguments on legal provisions.

Purposive sampling technique was chosen under this approach for interview purpose. The researcher employed expert sampling interviews during interviewing the experts from Ministry of Trade and chamber of commerce, founders and managers of share companies, academics based on the participants experience, position, expertise and other attributes to acquire general information that were vital to address the research questions of the study. The companies, which were part of this study, were selected by taking consideration into voluntariness of companies' founders and managers, purpose of the study and year of the companies' establishment.

Since there were many companies which were not commenced the business established between 2000-2008 E.C. fiscal years in the town, share companies registered between these years in Addis Ababa were taken. A qualitative data collection technique was used one-on-one interviews with selected respondents. Data were collected from primary and secondary sources. Primary data were gathered mainly through interviews. The secondary sources were legislations, domestic and foreign literatures related with the study and these secondary sources were collected through legal analysis.

1.8. Scope of the Study

This research is basically limited to the regulation of process of formation and beginning of operation of share companies established through public subscription of shares in Ethiopia and

its practice in Addis Ababa. The issues raised in the research are those which are directly related to the regulation of process of formation and commencement of business by share companies established through public subscription of shares. This research tried to incorporate the practice of companies' formation and the experiences of participants in connection to the formation of companies. Commencement of business would be understood in this research as all activities after the company get certificate of commencement of business to actual operation of business. In another word commencement of business indicates the beginning step of operation. As far as the geographical limitation of the study is concerned and as the title of the study indicates, the research was concentrated on companies whose head offices are placed in Addis Ababa city. Lastly financial sector of share companies were excluded from the study since they were treated independently.

1.9. Limitation

The main limitations of the study are twofold; shortage of times (since this research has to be accomplished within few months) and the willingness of the target respondents. The willingness of the respondents has abided limitations on this study. Specifically the founders and the directors of the company were not volunteer to give information accordingly. They fear to give the whole relevant and fact information for the researcher.

1.10. Organization of the Thesis

In this study an attempt was given to explore and explain regulating formation and commencement of business by share companies. Therefore, the paper was organized in to five chapters as follows: Chapter one deals with the proposal of the study. Chapter two provides a review of the literature on the general definition, formation and development of Share companies and discusses why we regulate share companies. Chapter three analyzed the prevalent practical challenges and legal gaps related to formation and beginning operation of share companies under Ethiopian law. In chapter four institutional frameworks and enforcement mechanism of this laws and limitations were discussed. The last chapter of this paper encompassed conclusion and recommendation.

CHAPTER TWO

2 .GENERAL OVERVIEW ON FORMATION AND COMMENCEMENT OF BUSINESS BY SHARE COMPANIES

2.1. Introduction

In the previous chapter, the research proposal of the research has been introduced. In this chapter, the general overview on formation and commencement of business by companies and regulation in general and in Ethiopia in particular were discussed. Thus, the definition of companies, meaning of Share Company, formation and commencement of business by share companies, Distinguishing Features of share Companies, need for regulation and general overview of regulatory body of companies in Ethiopia were described.

2.2. Definition and Development of Company

As the issue of companies established through public subscription of shares is a sub set of company it is preferable to begin by defining the latter. According to black's law dictionary, Corporation means "an entity usually a business having authority under law to act as a single person distinct from the shareholders who own it and having rights to issue stock and exist indefinitely...".³⁸The word "corporation" derives from corpus, the Latin term for body, or "a body of people", entities which carried on business and were the subject of legal rights found in ancient Rome.³⁹Its germ having is laid in a mode of thought resulting from the fact of living together. The word "corporate" has been defined as "united into one forming one body constituted of many individuals; to form into one body; to incorporate; to embody; to unite or to join in one body."⁴⁰

According to Chief Justice Marshall of USA, "A company is a person, artificial, invisible, intangible, and existing only in the contemplation of the law. Being a mere creature of law, it possesses only those properties which the character of its creation of its creation confers upon it

³⁸Bryan A. Garner (ed) black law dictionary 9th ed, west group st.paul 2009,p 341

³⁹Available at, [http:// en-wikipedia.org/wiki/corporation](http://en-wikipedia.org/wiki/corporation), accessed on March 2018

⁴⁰See the oxford English dictionary, 2nd ed. Clarend on press 1989, s.v "corporate". and berhang/mariam, the law of corporate taxation,2010, p 10 available at <https://www.scribd.com/document/246838657/The-Law-of-Corporate-Taxation-in-Ethiopia>

either expressly or as incidental to its very existence”.⁴¹ Another comprehensive and clear definition of a company is given by Lord Justice Lindley, “A company is meant an association of many persons who contribute money or money’s worth to a common stock and employs it in some trade or business, and who share the profit and loss (as the case may be) arising there from.”⁴²

None of these definitions incorporate all features of the company. Rather all include some important definitional elements that cannot tell the full-fledged meaning of a company alone. As of the above definitions, it can be preserve that a company is registered association which is an artificial legal person, having an independent legal, a common capital comprised of transferable shares, carrying limited liability, entity with a perpetual succession, a common seal for its signatures, and carrying limited liability.

Hence, a company is a fictitiously created legal person existing in contemplation of law. It cannot function to live up to its object without being spearheaded by the human kind since it has no mind of its own. As a result, the management of a company is carried out by the shareholders’ general meeting, board of directors and general managers. A company is after all a collection of assets which have arisen as a result of capital contributions from the shareholders and retained profits arising from the trading activities. As a result it may consist of two or more natural persons identified under common name; it can also be owned by a single person, or it can have hundreds, or thousands, of owners or shareholder.⁴³ It is “an incorporeal movable consisting of all movable property brought together and organized for the purpose of carrying out any of the commercial activities specified in Art.5 of Commercial Code.”⁴⁴

Thus, with the expansion of commerce, finding and they require for large scale business operation, it was understood that sole proprietorship and partnership are unsuitable for large scale businesses.⁴⁵ With the introduction of company form of business ownership the human kind has come up with an innovation that mitigates the shortcomings of sole proprietorship and

⁴¹-----, meaning, characteristics and types of a company p2 available at www.ddegjust.ac.in/studymaterial/bba/bba-2011 accessed on mach 12

⁴² Ibid

⁴³Kahsay giday, Remuneration of share company directors in Ethiopia ; the law and practice ,[LLM thesis Addis Ababa university, 2014] p 4

⁴⁴ Id supra note 9

⁴⁵Pistismarco, the purpose of commercial law,1 December 2005,p 1 available at <http://diritto.it/docs/21074>,accessed on February 3

partnership. The western world holds the credit for introducing company form of ownership which is the strongest form of business organization having a considerable breath on the economic and political affairs of a given country.⁴⁶

New Jersey was the first to adopt an enabling corporate law with the aim of attracting more business to the state.⁴⁷ Further, Delaware followed, and soon become known in the US after New Jersey raised taxes on the Corporations, even today, most major public corporations are established under Delaware law.⁴⁸ By the beginning of 19th Century government policy began to change as corporations were found to be riding the economic wave of the future, and they were also granted rights which they had not previously enjoyed or recognized.⁴⁹ Likewise, British legislation passed joint stock companies Act in 1844, and latter enshrined in to the law of the preeminent hallmark of modern corporate law the concept of limited liability.

In Ethiopia, the law that governs companies is the commercial code and it enacted in 1960. The share company law provisions are part of the commercial code under the heading of “Business Organizations”.⁵⁰ The endorsement of the Code had facilitated and triggered the formation of several private companies in the country until 1974.⁵¹ However, with the adoption of socialism from 1974-1991 it was utterly suspended due to the nationalization policy of the Dergue, where all incorporated companies had nationalized by a serious of proclamations and declarations.⁵² So the development of public share companies in Ethiopia is very recent phenomenon. The socialist system of government was over thrown by in 1991 and it was only after this regime change that the country has experience a market economy.⁵³ After EPRDF comes in to power, its function restored and different business organization start to form. Currently, Ethiopia is witnessing for the explosion of companies, which are offering shares for public subscription.⁵⁴

⁴⁶ Ibid

⁴⁷ Id supra note 6 p 91

⁴⁸ Available at <http://en-wikipedia.org/wiki/corporation>, accessed on march 12

⁴⁹ Ibid

⁵⁰, Commercial Code Arts 304-509

⁵¹ Gebeyaw Simachew Bekele , A Critical Analysis of the Ethiopian Commercial Code in Light of OECD Principles of Corporate Governance, (Institute of Advanced Legal Studies, University of London), pp. 2, accessed on, March 20, 2018. Available at http://sasspace.sas.ac.uk/4733/1/Gebeyaw_Bekele_LLM_ICGFREL_dissertation.pdf, accessed 2018

⁵² Ibid.

⁵³ Id supra Note 27

⁵⁴ Id supra notes 12, p 1, available at www.AbyssiniaLaw.com

2.3. Meaning of Share Companies

This research tries to investigate the law and practice of formation and commencement of business by share companies. Before directly rushing to the rules and regulations governing formation and commencement of business by share companies established through public subscription of shares, it is useful to explain the concepts behind share companies. Accordingly, to begin with definition, as to the 1960 Ethiopian Commercial Code, Share Company is a company whose capital is fixed in advance and divided into shares, and liabilities are only met by assets of the company. The aforementioned provisions envisage that company's capital is fixed and divided into shares before the coming into existence of the company.⁵⁵ This fixed capital of the company is known as legal capital and it cannot be reduced once it is registered without an amendment of the memorandum through extraordinary general meeting.⁵⁶ Further, the liability of the company is borne by the company itself, and shareholders are only liable to the extent of their shareholdings in the company.⁵⁷

Thus, Share Companies are the association of capital and this capital shall be fixed in advance and divided into shares. They are not the association of persons. Their existence do not depend on the identity of shareholders, so that they remain function despite the death, became incapability, etc of shareholders. Share Companies have their own legal existence and identity apart from the identity of their shareholders. Like other forms of companies, share companies involve shareholders who have limited liability. As stated under Article 304(1) of the Commercial Code, the debts and liabilities of the companies are met by the assets of companies.⁵⁸

2.4. Formation of Share Companies

Share companies come into existence by certain arrangements performed by founders. In this regards, there are three essential categories of promotional activities of founders in the formation of companies.⁵⁹ A founder has to prepare the relevant documents; set the object and purpose of the company; and advertise and circulate the prospectus.⁶⁰ A founder acts like an agent although,

⁵⁵ Commercial code art 312 (1)

⁵⁶ Commercial code art 304

⁵⁷ Commercial code art 304(2)

⁵⁸ Commercial code art 304(1)

⁵⁹ Id supra note 6 ,p 102

⁶⁰ Formation of company in India ,Legal Helpline India, December 26, 2014,available at <http://www.legalhelplineindia.com/formation-of-company-in-india/>

legally speaking, he/she is not an agent because of absence of a principal. Generally, a founder undertakes to perform all the necessary activities to bring the company into life.⁶¹

The formation of a company relates to a process where a company is brought into existence by an individual or by a group of individuals with the objective to form an association that will exploit business opportunities and where men, material, money and management are brought together or coincide.⁶² Share Companies may be formed in two ways as provided in Art 316, formation by public subscription and formation as between founders, due to certain arrangements done by founder.⁶³ Where the formation of a share company is as between the founders (closed Share Company), the law in Ethiopia requires them to show in the memorandum of association that all the shares have been allocated and the sums have been deposited in a bank in the name of the company. The founders are also expected to show in the memorandum of association that the valuation of contributions in kind shall be performed as per Art.315 of the Commercial Code and to have provided for the administrative organ of the respective share company.

The other method of forming a Share Company is by public subscription whereby the public is invited with the view to raise money for the pre-fixed capital of the company.⁶⁴ It not restricts to transfer of share of the company and on maximum number of the member. An offer to the subscribers should be made by a document called prospectus signed by all the founders and must show the indications under Art.318 (1) of the Commercial Code. Formation of a share company by public subscription also requires other formalities to be complied with.⁶⁵

Irrespective of the methods of formation, the minimum persons required in establishing a Share Company is five, but no maximum number is fixed.⁶⁶ The capital shall not be less than 50,000 Ethiopian dollars, and the amount of the par value shall not be less than ten Ethiopian dollars. Besides, the capital has to be fully subscribed and one quarter at least of the par value of the cash contribution has to be paid up and deposited in a bank in the name of the would be company.

⁶¹ Commercial code art 307

⁶² Nambasa Sharon, Formation of a company, what Uganda could learn from south Africa's modified system, (LLM Thesis, university of cape town, 2014) p 1

⁶³ The 1960 commercial code of Ethiopia uses this term with a different name called 'founder'. However, I do not see any distinction on the meaning of the two terms and possible to use them interchangeably

⁶⁴ Commercial code art 317

⁶⁵ Id supra note 41 p 26

⁶⁶ Commercial code art 307 (1)

Shares subscribed in kind, however, shall normally be paid at the time of formation of the company.⁶⁷

It is obvious that companies which are on the way to formation have no any legal ground to enter in to juridical acts and perform activities necessary for their formation.⁶⁸ It is founders who replace companies under formation and perform what is necessary for their formation. According to Article 307(2),(3)&(4)of the Commercial Code, founders prepare the legal documents of the firms such as the Memorandum and Article of Association, nominate initial directors, issue shares, and enter in to pre-incorporation contracts, etc. Again founder prior to the registration/incorporation of a corporation, it negotiate and go through into contracts on behalf of the projected or upcoming corporation, towards a smooth sailing into the corporate-hood.⁶⁹ Formalities of incorporation need to be attended, professionals must be instructed and salaried to prepare the necessary incorporation documents, and the business proposal needs to be appraised and initial finances raised.⁷⁰

Moreover, the founders are not agents to the companies they are setting up;⁷¹ However, they assume duties analogous to agents owe to their principals and has fiduciary duties.⁷² Thus, founders are required to fully disclose the whole profits, either collateral or direct profit, gained in the arrangement of the formation of companies to shareholders, actual or potential, or as alternative to the companies' directors.⁷³ This requirement prevents founders from engaging in fraud and other wrongful activities that would affect companies and future shareholders.⁷⁴

As raised in above, companies are come in to existent by certain arrangements performed by founders. This includes: First, the founders should inquire the business idea to be carried out and its' economic feasibility, and brings together the human and material resources necessary to run the business.⁷⁵ However, the founders to bring together the required human and material

⁶⁷ Commercial code art 339(1)

⁶⁸As cited in Janet Dine, company law 4th ed, palgrave ,2001 , p.87 ,Cuckburn CJ said in Twycross v garnt (1872) 2 CPD 469

⁶⁹ Gower, principles of modern law (Paul L. Daries ed 1997) P 144

⁷⁰ Available at https://www.sabinet.co.za/abstracts/ju_samlj/ju_samlj_v22_n1_a5.html

⁷¹Janet Dine, Company Law (4ed, Palgrave: New York, 2001), p.87

⁷²Ibid

⁷³As cited in alemayehu yisawu, Nicholas Bourne, Principles of Company Law(3ed, Cavendish Publishing Limited: UK, 1998), p.2

⁷⁴Janet Dine, supra note 87, p.87

⁷⁵ Id supra note 6, p.102

resources for the company, they may perform promotional activities through broadcast, print, or others medias.⁷⁶ They may enter in to pre-incorporation contracts with investors, accountants and others.⁷⁷ An invitation to pre incorporation of contracts have often been made via a document known as prospectus and it informs the investors perfectly about the natures as well as prices of shares, debentures or other securities issued and about the company under formation. As stated under Article 318 of the Commercial Code, we do observe the same in Ethiopian Companies which are formed through public subscription.

Second, the founders shall also prepare the constitution of the company, i.e. Article and Memorandum of Association. These documents regulate the relationships of companies with outside world or shareholders.⁷⁸ A Memorandum of Association is a basic document for incorporation of companies and includes the name of the original investors who initially subscribe the shares of companies.⁷⁹ This document defines the relationship between companies and the outside world and specifies the scope (objectives) of companies, so that it is not likely for companies to depart from this document and enter into juridical acts. It is, traditionally, required to include five clauses such as the name of companies, the location of the registered office/s, the objectives of companies, the liability of the members and the total shares of companies, the number of shares and the manner how profits and dividends are distributed.⁸⁰

An Article of association is subordinate to Memorandum of Association. It focuses on internal management of companies affairs⁸¹. It accepts the conditions set up under a Memorandum of Association and defines various rights, powers and duties of members involved in the Company. For instance, it incorporates rules on issuance, allotment and transfer of shares and basic regulations and procedures on general meeting, the voting rights of members, rights and duties of shareholders, directors and distribution of dividends and profits.⁸²

⁷⁶ As cited in Alemayewu yisawu, Roger Leroy Miller and Gaylord A. Jentz, Business Law Today text and cases: E-commerce, Legal, Ethical and Global Environment (8ed,Cengage Learning: USA, 2010), p.776

⁷⁷ Ibid

⁷⁸ Denis Keenan, Law for Business (12 ed., Pearson Education Limited: England, 2003), P. 49

⁷⁹ Commercial Code, Art.313and 517

⁸⁰ Id art.313 and.517

⁸¹ Id supra note 87

⁸² Commercial Code, Art .314 and 518

Third, the founders shall register and publicize the company under formation. The Ethiopian Commercial Code requires both the Memorandum and Article of Association to be deposited in the commercial registrar.⁸³ It also requires the notice to be published in a newspaper circulating at the palace where the head office is situated.⁸⁴

Thus, once the share company acquires legal personality, it issues shares to its subscribers. Shares can be issued either registered or unregistered bearer form and can be converted vice-versa per shareholders' interests unless prohibited by law or company's statutes.⁸⁵ The contents and manner of registration of shares are stipulated under articles 330 and 331 of the commercial code. Based on the statutes of the company or agreements of the general meetings, the company may also issue various classes of shares which confer different rights;⁸⁶ however it is prohibited to issue the same classes of shares which confer different rights. Classes of shares, preferred shares confer holders several priority rights over ordinary shareholders.⁸⁷

2.5. Distinguishing Features of Share Companies

Share companies have their own distinct features which makes them different from partnerships and sole traders. So, a business person who is interested to form a company has to consider these distinguishing features. Accordingly, companies have their own legal personality apart from their owners. Their identity is different from the identity of owners. So, if something wrong has been done by companies, it is the Companies which are questioned, not the owners and vice versa.⁸⁸ This means that even if the people administering the company are constantly changing, the company itself retains its character and the business need not be closed and restarted with every change in the managers or members (shareholders) of the business.⁸⁹ if the company is a limited liability company, not merely is the money owned by the company regarded as totally separate from the money owned by those running the company, but also the members of the company are not legally responsible for the debts of the company (except where the law has made exceptions to this rule in order to avoid fraudulent or unfair practices by those in charge).

⁸³Id, Art 219(2)(b), 221, 323 and 520

⁸⁴Id, Art 87 ,219, 220, 223,224 and 323(3

⁸⁵Id art 325 but the company cannot issue shares before its registration art 327.

⁸⁶Id art 335

⁸⁷ Id art 337

⁸⁸Cited in Alemayewu Yisamaw, Id supra note, David Sagar, Larry Mead and Philippa Foster Back, Fundamentals of Ethics, Corporate Governance and Business Law (Elsevier Ltd: USA, 2006), p.182

⁸⁹Id supra note 76, [available at https://link.springer.com/chapter/10.1007/978-1-349-14583-6_3](https://link.springer.com/chapter/10.1007/978-1-349-14583-6_3)

Members can only be called upon to pay the full price of their shares. After that a creditor must depend on the company's money to please his claim.⁹⁰

Here, each share is given a nominal value and a member of this form of company is liable only up to that full nominal value of each share he holds or has agreed to purchase. Most shares today are issued to shareholders on a fully paid up basis, so that, in the event of the company being wound up insolvent, there is no further liability on the part of the member, no matter how much the company owes to its creditors.

The other essential characteristic of companies is perpetual succession. Companies are association of capital and not an association of persons. They do also have their own legal existence and identity apart from their shareholders. Thus, companies exist and operate for a long period of time despite the death, incapability, bankruptcy or the transfer of shares by shareholders.⁹¹ These situations do not bring companies to an end because their assets remain intact.⁹² To say more, in western countries, the shares of large companies are sold and bought in stock markets every minute, but that does not alter the ownership of assets of companies. Their existences remain perpetual due to the succession of new persons who replace those who die, became incapable, go bankrupt or transfer their shares. Those persons who are initially concerned in setting up and organizing the business may desire to leave the business or to leave their 'share' of it to their beneficiaries on their death but, usually, all parties, particularly those remaining involved in the business, will want to affect the company as little as possible⁹³.

In respect of the incorporated company, in theory, changes of the shareholders can be accomplished suitably and with a minimum of distraction to the company's business. When a shareholder sells his shares to another person, that person becomes the new shareholder, and the only involvement of the company is to change the appropriate entry in the register of members. Thus, the new person becomes a new member. Furthermore, because the company is a corporate body and a recognized legal entity, it survives the death of one, or even all, of the members. The

⁹⁰ *ibid*

⁹¹ William F. Blake, *A Basic Private Investigation: A Guide to Business Organization, Management and Basic Investigation Skills for the Private Investigator* (Charles C Thomas Pub Ltd, 2011), p.17

⁹² Richard A. Mann and Barry S. Roberts, *Smith and Roberson's Business Law* (15 ed., Cengage Learning: USA, 2011), p.669

⁹³ Simon Goulding, *company law*, university of east Anglia, (second edition by routledge cavendish, 1999) p 47

shares of any deceased shareholder are simply transferred to their personal representatives. The company as a result has a potentially perpetual survival.⁹⁴

Share companies also have delegated management with board structure. It is almost universal practice for the article of association to vest power to manage the company in the hands of the board of the directors. Nevertheless, day to day corporate decision making is not usually carried out of board meeting. In ordinary course a company articles of association will authorize the board to delegate its powers to individual holding executive offices within companies. Correspondingly, decisions about hiring, firing, assigning work, launching, product lines and setting prices ordinarily made outside the board room.⁹⁵ A joint stock company is an autonomous, self governing and self-controlling organization. Since it has a large number of members, all of them cannot take part in the management of the affairs of the company. Real control and management is, then, delegated by the members to their voted representatives, identify as directors.

2.6. Commencement of Business by Share Companies

Business is the provision of product and/or service to satisfy customer requirements. Activities involved in the day to day functions of the business conducted for the purpose of generating profits. Everything that happens within a share company to keep it running and earning money is starting from commencement of business. The activities of a company can by no means be said to be an easy and smooth ride from point A to point B; activities should rather be regarded as a complicated web of processes. These processes fall under the collective term ‘business operations. A company’s success or failure relies heavily on the efficiency of operations.⁹⁶ Especially the first part of operation that means commencement of business by companies is very crucial. A company comes into existence, when it is registered and a certificate of incorporation is issued by the registration authority after it is licensed. Because art 21 of Commercial Registration and Business Licensing Proclamation state that no person shall carry on a

⁹⁴ ibid

⁹⁵ Brian R. Cheffins, companies law: theory, structure, and operation, (by Cambridge University of British Columbia ,1970), 95

⁹⁶ Matt Goldman, What the business operation are, available, <https://www.business2community.com/strategy/business-operations-company-01776850>

commercial activity without obtaining a valid business license.⁹⁷ Thereafter, the company becomes entitled to commence its business. Before commence and operate the business by share companies, it shall first fulfill the following requirement.

First, in order to commence business operations, a corporation needs assets. It normally acquires these assets-known as the initial “capital” of a corporation by issuing shares of stock in exchange for cash or other property or by borrowing.⁹⁸ The minimum amount of the capital of a share company shall not be less than 50,000 Ethiopian Birr and shareholders are required to make available to the company at least this much resources at formation. Second, Share Company formed by fixing capital in advance and divided into shares.⁹⁹ The founders will, through the feasibility studies they conduct and determine the amount of resources the shareholders will have to make available to the entity.¹⁰⁰ So, the capital is should be predetermined.

Third, the commercial code requires shares subscribed in cash be paid up upon subscription as to one fourth of their par value or a greater amount if so provided in the memorandum of association Fourth, the founder should be Adopt the Memorandum and Articles of Association. The Commercial Code of Ethiopia requires that the formation of a share company be by a public memorandum, known as the memorandum of association.¹⁰¹ As well as the by the document which sets out the constitution of the business organization, known as article of association.¹⁰² Lastly, a company comes into existence only when it is registered with the right organ of the state. The law requires that the final text of both the memorandum and the articles of association that are to be drawn up at the meeting of subscribers be deposited in this register.¹⁰³ It is only once the subscribers have signed these documents before a notary public and the same are deposited in the commercial register that the company becomes a legal person.¹⁰⁴

⁹⁷ Commercial registration and business licensing proclamation no. 980/2016, fed Negaritgazetta 22th year no. 101, Addis Ababa, July 2016.

⁹⁸ D.F.Vagts, 'Law and A.Conard, Accounting in Business Associations', (2nd ed International Encyclopedia of Comparative Law 2006) p 7

⁹⁹ H.G. Henn and J.R. Alexander, Law of Corporations,(3rd ed West Academic 1983) pp 236-238

¹⁰⁰ Commercial Code Art 304(1)

¹⁰¹ Commercial Code Art 313

¹⁰² Commercial code Art 363(2) and 457

¹⁰³ Commercial code Art 323(2) a & b

¹⁰⁴ Commercial Code Arts 323 and 223 read together.

Generally, share companies after fulfilling all the above requirements and get permission from authority as to start business directly pass to commence the business. Corporations have a set management structure to begin the business. The owners of a corporation are shareholders, who elect a board of directors, which then elects the officers. Other than the election of directors, shareholders do not participate in the operations of the corporation. The board of directors is responsible for managing and exercising the rights and responsibilities of the corporation. The board sets corporate policy and the strategy for the corporation, and elects officers usually a CEO, vice president, treasurer, and secretary to follow the policies set by the board, and manage the corporation on a day-to-day basis.

CHAPTER THREE

PREVALENT LEGAL AND PRACTICAL CHALLENGES AND GAPS RELATED TO FORMATION AND COMMENCEMENT OF BUSINESS BY SHARE COMPANIES UNDER ETHIOPIAN LAW

3. 1.Introduction

In this part of the paper, the writer dealt with the general trends in the formation of share companies in Ethiopia. The problems that are related in law and practice in formation and commencement of business by share companies established through public subscription of shares like: lack of commence the business for long period of time, unethical conduct of founders and absence of adequate legal framework were discussed.

3.2. General Trends in the Formation of Share Companies in Ethiopia

The private sector involvement in the economy may take the form of share companies. A share company is a form of business organization where, in most instances, a large group of people invest cash or in-kind contributions in a company (administered by strangers) in return for units of ownership representing a proportion of the company's capital in the form of shares.¹⁰⁵ Currently Ethiopia has number of companies formed by sale of shares to the wider public. The emergences of publicly held share companies in the country in turn give rise to multitude of complex practical legal and institutional issues.

The number and modalities in the formation of companies have direct relationship with the economic policy of the country.¹⁰⁶ The significant shift in Ethiopia's economic policy direction to encouraging private investment since the present government took power in 1991 had brought about a noticeable increase in the number of companies established in the country. For instance, before 1981 the total number of share companies registered at the Ministry of Trade and Industry was only 41 while the total numbers of share companies established through public subscription of shares registered at the Ministry have become 750 by the march 2018 G.C.¹⁰⁷ According to the

¹⁰⁵Bahakal and Micael, (2013)., Legal Perspective: Ethiopian Shareholders; locked in and locked out? Capital news (paper Addis ababa 2012) available at <http://capitalethiopia.com/2012/07/10/legal-perspective-ethiopian-shareholders-locked-in-and-locked-out/#.WwJIFuaPvio> accessed on march 24

¹⁰⁶Id supra note 20 p 1

¹⁰⁷ CompanyFiles Obtained from share companies and sector association follow up and support directorate , Ministry of Trade (March 11,2018)

data that writer got from ministry of trade, almost above 75 % of share companies were established through public subscription operating in Addis Ababa City.¹⁰⁸The number of share companies established through public subscription of shares in the past two decade increased in high parentage. Particularly the formation of share companies established through public subscription of shares were flourishing in the country between 2000-2005EC.¹⁰⁹ In these years it witnessed that the increasing of huge business organization in all corner of the country. Between these years the general public as well as the business community also begun to engage in share companies which required cooperation and large investment. The number of companies registered within Addis Ababa between 2000- 2004 E.C. were increased rapidly and forecasted to grow constantly by more than 10% for next few years.¹¹⁰ But unfortunately the number of registered company was highly decreased especially in 2009 and 2010(nine month report) due to loss of confidence by general public on this type of companies.¹¹¹ The ministry of trade conducted registration of companies established through public subscription of shares in 2009 only for 3 companies and in 2010(within nine month) only two companies were registered in the authority. These clearly indicate that the less growth of share companies established through public subscription of shares in the city currently.¹¹²

To analyze the problem of formation and commencement of business by share companies established through public subscription of shares in Addis Ababa one has to exhaustively see as much as possible in the city. But apart from the time and resource limitation, the lack of official system to identify whether companies after registration commence or not commence the business makes it is difficult to know the extent of share companies established through public subscription shares present in the city. The official in charge of company registration and licensing at the Ministry of Trade didn't know officially which of the companies were commencing the business and which of the companies didn't commence the business after registration. As the official said, unless you go and observe each and every company, it is not easy to know which companies are commenced the business or not.¹¹³ So, it was left for the

¹⁰⁸ Ibid

¹⁰⁹ Id supra note 20 p 61

¹¹⁰ Ibid

¹¹¹ Id supra Note 29, company Files and annual Report Obtained from share companies and sector association follow up and support directorate, Ministry of Trade.

¹¹² Ibid

¹¹³ Ibid

writer to check each and every company, which was time consuming for the writer to go through all individual companies at Addis Ababa. But there are many share companies established through public subscription of shares shareholders brought grievance to the authority as to the authority enforce the registered companies as to commence the business or to take other administrative measures.¹¹⁴ So because of time and resource limit, the grievance data those the members of share companies brought to the authority is considered in the research for knowing the cause of the problem they stay for long period of time without commence the business. When Ato Yosef Alamu in ministry of trade, share companies and sector association follow up and support directorate head, interviewed, he said that there is high problem during formation and the first step of operation of share companies that established through public subscription of shares. The importance of share companies is significant to the economic development of the country; however, practically failure to meet the objective of their establishment has become widespread.¹¹⁵

As stated earlier, organizational form of doing business is an ideal mechanism of bringing the scattered capital of the members of the society together in order to invest in enterprises that need a certain level of capital requisite. In this regard, there is a growing consensus that organized private sector investment-both domestic and foreign, and it has a vital role to play in diving economic growth and helping to alleviate poverty.¹¹⁶ In Ethiopia, the advancement of economic development is one of the ultimate goals of the Nations, Nationalities and peoples of Ethiopia¹¹⁷. In order to accelerate this goal, it has become necessary to encourage and promote investment. Currently, the population number in Ethiopia goes beyond 100 million. However, the total number of share companies established through public subscription of shares in all sectors of the

¹¹⁴ Ibid

¹¹⁵ Id supra note 24, shareholder bring grievance on share companies that note commence the business for long period of time like Heber shugar share company (established 2013) G.c, Yeblu Nile micro and small enterprise share companies(2013), BIS vegetables and fruits general trading share company (2012), Jacarada share company(2013). Comoros General trading share company(2011), Crystal leather share company(2012), Ardi mineral production share company (2011), Crystal leather share company, Access real state share company(2012), Mela specialized Hospital share company (2012), sunshine chemical share company(2013), Access capital service share company(2013), Tibeb Ethiopia general business share company(2014)), Ardi international logistics share company(2012) Hohiyat business share company (2011), sunshine chemical share company, Righteous school share company.

¹¹⁶ Nelson Jane, Leveraging the Development Impact of Business in the Fight Against Global Poverty, P.1, available online at http://www.brookings.edu/global/200508blum_nelson.pdf (accessed on 25 may 2018)

¹¹⁷ See Preamble of FDRE CONSTITUTION.

economy is just 750.¹¹⁸ If we compare the current number of companies in Ethiopia with the number of companies in two countries from the west, where there are more than 18 million companies in the United States and 1.5 million companies in the United Kingdom¹¹⁹, we get ourselves down near zero. So what is wrong in Ethiopia? What are the reasons for low participation in formation of Share Company established through public subscription of shares currently? Company law is crucial in market economies; it sets the legal environment for the creation and continuing operation of privately owned businesses. Good company law is especially critical in transition economy countries. It can encourage new investment and provide investor protection by setting forth clear and objective rules for a company's ongoing internal governance; it can encourage entrepreneurship by making it easy to start up and register a company; and it can encourage businesses to come out of the underground economy into the publicly registered. The previous experience of loss and bankruptcy because of bad management inflicts pain and may affect the future investment decision of individuals.¹²⁰ Exploitative managerial behavior, inadequacy of legal protection may also erode the confidence of the public.¹²¹ This all facts need regulation in the city some points will be made below with respect to practical and legal problem in formation and commencement of business share companies established by public subscription of shares. Specifically, some prevalent practical and legal problems are discussed below.

3.3. Regulating Foul Play Founder

3. 3.1. Who Is A Founder?

A founder is a person who forms a company satisfying all requirements of incorporation.¹²² Founders are also referred as an individual who assists in creating and organizing the corporation.¹²³ In other words, it is a person who undertakes to form a company with reference to a given project and setting a company in motion to accomplish company's

¹¹⁸ Company file that available at ministry of trade accessed on march 12

¹¹⁹ as cited in Berhane G/marim, the law of corporate taxation in Ethiopia, (LLM thesis, Addis Ababa university,2010) ,ewanmacIntyre, business law 475 (2nd ed. 2005).

¹²⁰ Id supra note 3

¹²¹ Ibid supra note 21, from the fact share holders brings grievances to ministry of trade on corporate founder and managements and data acquired from ministry of trade and interviewed experts.

¹²² Id Supra note 1,p 5

¹²³ Schneeman, A.Law of Corporation and Other Business Organizations [2010],5th ed, New York, Denmar Cengage Learnin ,p 286

designed purposes.¹²⁴ In general, founder can be described as a person who brings a share company into existence.¹²⁵ He/she is one who undertakes to form a share company with reference to a given object and to set it going and who takes the necessary steps to accomplish that purpose.¹²⁶

3.3.2. Roles of Founders

A founder as preliminaries incidental to the formation of a company usually engages in deciding the name, object, capital, and extent of liability of each member, the situation of the company's registered office and to incorporate this decision in the memorandum of association. He equally draws up the rules for the internal management of the company and arranged to embody it in the article of association of the company and arranges for the printing of same. The founder also nominates who the first directors are which in most cases are themselves, the auditors, bankers and even the company secretary. The company's director and or secretary nominated are those that would be responsible for the signing of most of the pre-incorporation documents meant for registration.¹²⁷

Equally, the founder prepares, print and issue prospectus where the company is a public company in bid to raise capital for the effective takeoff and management of the business, and finally goes ahead to register or prospectus where the company is a public company in a bid to raise capital for effective take off and management of the business, and finally goes ahead to ensure the registration of the company. ordinarily a founder will usually be in some sort of co position with regard to the companies affairs, both before and after it is formed and during the early stages of its existence and will be in a position analogous to of a director during that period¹²⁸.

¹²⁴Kestela, Y., &Madhuri, S. Triggering the Ethiopian Company Law Re engineering Aligned with Benefits and Burdens of the Founder to Form a Share Company.[2006] vol 3 no 1, International Journal of Multidisciplinary Advanced Research Trends, p 156

¹²⁵Sitelbenat Hassen, Some Remarks on the right and responsibilities of founder under the Ethiopian commercial code, ,[2017], vol 8 no 4 social science and humanity journal p1 available at <https://www.scirp.org/Journal/PaperInformation.aspx?paperID=80998&> accessed on march 3

¹²⁶Fentaw, A.&Gurmu, K. Law of Traders and Business Organizations. The Justice and Legal Research Institute Teaching Material,2009. P 96

¹²⁷Agbonika, john musa,alewo, the rising profile of a promoter in the life of a company, the Nigerian view point,[2014]vol.27,journal of law, policy and globalization ,

¹²⁸ibid

3.3.3. Position of a Founder

As the commercial code though not directly, placed the founder in a fiduciary position its relation with the company sort to be formed with third parties, although not seen as an agent of the company, and owes the company utmost good faith and duty to disclose any profit made, and interest had in its dealing with and in relation to the company.¹²⁹ Though all the transaction the founder enters with third party on behalf of the company with the aim of floating the formation, registration and eventual incorporation of the company, such transactions referred to by the marginal notes of Companies and as pre incorporation contract; binds the company upon it being incorporated as the company then attains a distinct personality different from that of the founder. Commercial code allows for ratification of such transaction if entered on behalf of the company by such a promoter after a full disclosure of all material facts known to the founder in respect of the transaction to the company.¹³⁰

3.3.4. Regulating Unethical Conduct of Founder (Foul Play Founder)

Founders, being fundamental individual in the formation as well as operation of company, she/he should carry out his/her duty with reasonableness and should deter him/herself from things that could adversely affect the interest of the company and which may create a conflict of interest between him/her and the company.¹³¹ Thus, the founder shall faithfully disclose all facts relating to the property transferred and contract entered to the future company.¹³²

Fraudulent and rent seeking practices in the formation process can undermine the financial solidity and profitability of the companies. Unless regulating unethical behavior of a business founder, it often leads to negative publicity which substantially affects positive corporate.¹³³ The existence of various contentions issues on the formation of company called the regulation aspects of founders and their activity. A person who forms Company with objective of foul play, may abuse the founder position for personal profit, to the detriment of the company and its

¹²⁹Id supra note 124 ,p 158

¹³⁰ Commercial code Art 308(2)

¹³¹Id supra note 124 p.158

¹³² Ibid supra note 125

¹³³BirukAyalew, Corporate governance practice landscape in Ethiopia: past, present and futuro,[2015] vol 6 no 12,International Journal of Research in Finance and Marketing and Dong-Hong Zhu Ya-Ping Cha, Negative Publicity Effect of the Business Founder's Unethical Behavior on Corporate Image: Evidence from china ,2012 available <https://www.jstor.org/stable/42001970>

shareholders.¹³⁴ There are founders and directors whom collect unfair interests and other benefits of shareholders money by not commencing business for five to six years and they gave unsatisfactory reasons for such of their activities.¹³⁵ One expert from ministry of trade said that, “Some shareholders those were aggravated by the deed of these founders and management, told me that, ‘the Ministry of Trade is registering Share Companies that cheat the public money through the name public subscription instead of properly regulating them’.”¹³⁶

Registered Companies are a major contributor to state’s socio-economic development. Although Ethiopia has been credited as one of Africa’s fastest and consistently growing economy country, its undesirable process of company formation has encumbered its development. Especially with related to foul play founder, currently though founders who operate the company are few in numbers, even a group founders may establish more than one companies that may failed to start operation due to their fault, fraudulent, lack of capacity and skilled professional etc.¹³⁷ Specifically in Addis Ababa the number founder that actively participating formation of company is 10 to 15.¹³⁸ But the practice of them shows as most of them are foul player. Even after the company they try to form is failed to incorporation due to this reason, they pass to form another company though they have bad reputation and they are going to affect the interest of public and individual resource.¹³⁹

Instead of being wealth generating/creating areas to the investors through entrepreneurialism, innovation, development and exploration, today Ethiopian share companies are become the area of battle field between the founder, management bodies and the shareholders due to lack of adequate company regulation rule and weak enforcement on the applicable laws.¹⁴⁰ Founder and Managers use their full control rights to pursue projects that benefit them rather than investors.

¹³⁴ -----, promoters and pre-registration contract, available on cdn-media.macmillan.com.au/palgrave/lecturer-restricted/Chapter4.pdf accessed on march 25

¹³⁵ Ibid supra note 21

¹³⁶ Interview with Henok Haile, expert, share companies and sector association follow up and support directorate, in ministry of trade, march 17, 2010

¹³⁷ Id supra note 21, for instance founder of MuluMesobe food share companies, founder of access real state and Access capital service share companies, founder of sunshine chemical and Commoros General trading share companies, founder of Crystal capital service and Crystal leather share company.

¹³⁸ Ibid

¹³⁹ Ibid

¹⁴⁰ Asnakech Getnet, Revisiting Ethiopian bank corporate governance system; glimpse of the operation of private banks, [2013] Law, social, justice and global Development p 7

This redundantly occurrence of their foul play has shown that founder and managers may misappropriate corporate assets whenever they get an opportunity to do so.

For example Ato Ermias Amelega is known business man and founder of many share companies in Addis Ababa; but he was over ruled from his position in different share companies for the breaching of rule and a potential conflict of interest.¹⁴¹ After this fact he formed another share company, Access Real Estate, and 25000 share holders of this company were defrauded by him and his associates.¹⁴²The company originally formed by five shareholders, with a 50,000 Br initial capital.¹⁴³Ermias Amelga was founder, CEO and chairman of the board.¹⁴⁴The huge amount of this fund came from unsuspecting homebuyers, who advanced 941.25 million Br, in the belief that the company would deliver affordable housing within one year of signing contracts.¹⁴⁵ But, five years after the company's formation no one who gave Access money for a home actually received one and he left the country for the US via South Sudan for 'a business trip' though no one has yet to say what the nature of the business trip was which took him out of the country at a time the company faced a mountain of troubles as a result of his bad decisions and shoddy business practices.¹⁴⁶

The auditors pronounced that those in charge of running the affairs of Access Real Estate have demonstrated gross financial mismanagement, for they have given out unsecured and unwarranted loans to associate companies, subsidiaries and individuals. Access Real Estate's management spent 64.5 million Br in commission and other administrative expenses. The company has invested 664.68 million Br in acquiring other properties, such as – the Imperial Hotel in Addis Ababa and Safari Lodge in Adama (Nazareth). A further 173.6 million Br was spent in buying shares in other real estate companies and 158.3 million Br was advanced to suppliers and contractors. Among such contractors were Living Steel Construction Plc and YBEL Industrial Plc, which have been paid in advance a total of 260 million Br. These companies could only account for 23.3 million Br in delivery of work, the audit firm has

¹⁴¹Tadeos Anteneh ,Ethiopia: Real Estate woes in Addis : the case of Access Real Estate, nazret.com news paper, (Addis Ababa ,July 2013)

¹⁴²Muluken Yewondwossen, Ethiopia: Access real estate home buyers meet with MoT to seek justice, sodere tube,

¹⁴³ Data of share companies established through public subscription of shares , that available ministry of trade

¹⁴⁴Elleni Araya, is there redemption for access real estate? fortune vol 14 ,no 686,(Addis Ababa, June 23, 2013)

¹⁴⁵ Ibid

¹⁴⁶FasikaTadesse, Unraveling access real estate audit report finalized last week established that the company is solvent but Ermias mismanaged it, fortune new paper vol 18 ,no 897,(Addis Ababa July 04,2017)

established. Shareholders of these companies, including Luchiano Framolin and Yonas Tadesse, established another real estate firm with Ermias by the name of Michot Real Estate Plc. From this amount, Access Capital Service received the lion's share followed by Pacific Link Ethiopia, Pioneer Agro Industry, Meri Real Estate and Mechat Real Estate. Access Capital was formed and lead by Ermias Amelega, who is a major shareholder and founder of the company and Access Real Estate, received a loan of close to 131 million birr and four other companies secured from 43 million to 22 million birr respectively.¹⁴⁷.

Again Mulu Mesob Foods share company firstly established with 60,000.00 Ethiopian birr by 6 people in 2000 E.C.¹⁴⁸ and latterly open this share company for public subscription on the prospects of Share Company. Mulu Mesob foods share company's objective was to offer modern food and biscuit in different restaurant that they would established in different place and offer foods for tourist and try to enter in to commence the business in to 2004 without the member is not fully subscribing to share for different reasons. However, for reasons of founder, board and chairperson mismanaged the company and other reason, the shareholders required injection of the property of the company from court and ministry of trade and dissolved lastly after many individuals and county resources were damaged.¹⁴⁹ But those individuals participated in formation of Mulu Mesob food Share Company is currently on the way of establishing another share company in Addis Ababa itself.¹⁵⁰

As it can be understood from these practices in Addis Ababa, the transactions during the formation process have big problem and call for legal regulations. If it will not be regulated in the time, incorporation share companies will bring personal and countries resource damage. Because those Persons have bad reputation and they cheat and mislead the public by organizing Share Company. Even those people who made such criminal acts, trend to form other share companies. When we see the real context of other countries, to tackle this type improper use of power they design special mechanism. For example, Nigerian designs proper mechanism to overcome this problem on their Company and Allied Matters Act vest in the Corporate Affairs

¹⁴⁷ *ibid*

¹⁴⁸ From Memorandum of association of Mulu Mesob food share companies that available at ministry of trade. share companies and sectoral association follow up and support directorate, march 12

¹⁴⁹ From Report document by share holders and management presents to ministry of trade, available at ministry of trade, share companies and sectoral association follow up and support directorate.

¹⁵⁰ *ibid supra* note 21

Commission (CAC). Under section 20(1), it states that the person willing to form a company shall:¹⁵¹

- a) Not be an un-discharged bankrupt.
- b) Not be disqualified from being a director of a company, and section. 254 of the Act are to the effect that
- c) Where a person is convicted by a High Court of any offence in Connection with the promotion, formation or management of a Company, or in the course of winding up of company it appears that a person:-
 - i. Has been guilty of any offence for which he is liable whether he has been convicted or not under Section. 513 of this Act or
 - ii. Has otherwise been guilty while an officer of the company of any fraud in relation to the company or any breach of his duty to the company cannot partake in the promotion, formation or management of yet another company.

However, 1960 commercial code with regard to Share Company established through public subscription of shares the law muted on who qualify for founder of Share Company. The Commercial Code didn't prescribe any formal qualifications for founder of companies as a result of which even fraudulent persons can become founder.

When we see the experience of financial sector also, the National Bank of Ethiopia (NBE) is the organ bestowed with the authority to issue directives to regulate the financial industry, i.e. Banking; hence it has issued directives that require qualification from founders of bank Share Companies in accordance with Article 4 licensing and supervision of banking business No. 56/2013;¹⁵² the directive states the information required from applicants for license, from the lists like: Curriculum vitae of the proposed chief executive, founders and/or directors including their age, marital status, education, employment history for the past ten years, their experience in business and financial affairs, their involvement in civic, social and charitable activities including any leadership position held. Specifically on article 4 the directive states the quality of

¹⁵¹ Companies and allied matters , Law of Federal republic of Nigeria, section 20(1) and John Musa Alewo Agbonika, The Rising Profile of a Promoter in the Life of a Company: (2014) The Nigerian View Point, 27 J.L. Pol'y & Globalization 111

¹⁵² National bank of Ethiopia licensing and supervision of banking business directive No. 56/2013, on art 4

founders.¹⁵³ To be organizer of bank such person should be honest, reputable and diligent. Additionally, the authority identifies record or evidence of previous conduct or activities of organizer such as whether he/she/it has been convicted for dishonesty or fraud, whether has record of withholding information from the public authority, whether it submission of incorrect financial statements and whether it have disciplinary measures. NBE based on this directives from story of the document if the person unable to carry out the formation banking or insurance, the Company shall be notified in writing that as he/she is not qualified to be founder of this sector.

The draft commercial code of Ethiopia tried to states the quality for the founders who need to organize company and on article 89.¹⁵⁴ This article states that the person willing to form a company shall have not been guilty of any offence for by theft, banditry and fraudulent. But when we compare this article with activity of founder currently done, the mentioned criteria in the article are not enough since founders are foul player as seen in above. The persons not able to pay their debts in many forms; they were prosecuted in connection with bankruptcy and the person disabled by court as not are a founder of Share Company is not included under this article. To protect the member of the public from dishonesty and fraudulent persons, these will be also good if they will be included under this article. As seen in above reality after the founders dissolve the company by their fault, they pass to form another share companies even if the business entity they try to form has failed, adjudged bankrupt and involved in court proceedings relating to dissolving companies they try to established, etc.

The draft commercial code has acknowledged what it refers to as the organizers as distinct from founders of a share company.¹⁵⁵ Individuals who take a prominent and leading role in setting up a share company are recognized. They may also be entitled to special payments in additional to what they get in their status as founders. Therefore, the person who is responsible for organizing the founding shareholders of the share Company must present their own story together with the document. Where the authority registering the share company based on the above criteria and found that unable to organize the share company, the authority shall be notified in writing that he /she unable to carry such activities based on public interest theory. This type of rule is necessary

¹⁵³ Ibid

¹⁵⁴ see Draft commercial code of Ethiopia article 89

¹⁵⁵ See draft commercial code art 89(307)

to protect the subscribers, the creditors and the company under formation. But this system is not currently introduced under the authority registering non-financial share company.

The writer interviewed from the ministry of trade, the share companies and sector association follow up and support directorate head,¹⁵⁶ on how to regulate this issue. Then he told to the researcher as they had prepared draft proclamation that regulates these issues and already transferred for federal public prosecutor. But the writer not believes this is proper way to regulate unethical conduct of founder and other issues. Since the ministry of trade is the main initiator of draft commercial code revision; the ministry currently is trying to enact other proclamation against the draft code in inappropriate way. Thus, the points that gotten from interview result shows that the draft proclamation repeat what are already incorporated in the draft commercial code.

Ethiopia is civil law countries; not common law country. Therefore, she needs codified code. The area of law should be laid down in one legislative document, with the aim of providing a closed, coherent, and consistent set of propositions. But it is better if the ministry enacts directive to regulate these activities and also by hastening the enactment of draft commercial code. On this issue the researcher asked the research and advocacy director in Ethiopian chambers of commerce and sectoral association;¹⁵⁷ then he said that, law that currently enacted in Ethiopia is the maximum life span is two years and repel. Again he said the law is promulgated with out for sight future change based on research and he recommend that the law should as to enact by most qualified person to solve the current problem in Ethiopia.

3.4. Problem Related To Not Commence the Business

The commercial code states that if the company is to be formed by public subscription first, an offer to subscription is made to the public through the prospectus.¹⁵⁸ It normally acquires the assets-known as the initial “capital” of a corporation-by issuing shares of stock in exchange for cash or other property, if the amount of minimum subscription is raised through new issue of shares, a public company applies to the Registrar of Companies for the issue of Certificate of

¹⁵⁶ Ibid supra note 21

¹⁵⁷ Interview with Million Feleke, Director of research and advocacy, in Ethiopian chambers commerce and sectoral of association(March 25, 2018)

¹⁵⁸ Commercial codec Art 317-318

Commencement of Business. In such case, founders are considered as organizers and take the initiative to make an offer for public subscription.¹⁵⁹

As Ato Yosef Alamu, in ministry of trade share companies and sector association follow up and support directorate head said,¹⁶⁰ currently concerning with the practice of establishing Share Companies, the law and the practice have difference. Additionally, he said that almost in Ethiopia there is no nonfinancial share companies directly established through public subscription of shares. The current practice shows that share companies are first established legally between founders as per article 316 of commercial code.¹⁶¹ Latterly after legally established between founders, they can widen their ownership base through subsequent offering of shares to the public without starting any business or almost immediately as the company is registered between founders.¹⁶²

Practically there is confusion between formation by public subscription and formation as between founders followed by capital increase by public subscription. Share companies that decided to increase their share by selling additional shares they should offer by prospectus. However, the element of prospectus during formation of companies by public subscription and when share company already formed decide increasing capital by selling shares have difference.¹⁶³ As we can understand from article 469 of commercial code, capital is increased after the company is already start business and not during formation stage of company. While the companies decided to increase the capital, there are the requirements those should be fulfilled first. Thus, whether the capital is fully paid, must be approved by general meeting and the prospectus should have element like the last profit and loss of account, balance sheet and auditor's report, dividend paid during the last five years or since formation and debenture of loans issued.¹⁶⁴ Thus we can infer from this element as the companies want to increase their capital they should stay in the business and have the history of loss and profit. Article 318 also clearly states the procedures of company are formed by public subscription which has some difference with article of 469 of commercial code.

¹⁵⁹ Available at , <http://www.qsstudy.com/business-studies/commencement-business-terms-company-law> accessed on March 25

¹⁶⁰ Ibid supra Note 21

¹⁶¹ Commercial code art 316

¹⁶² Ibid supra note 21

¹⁶³ Commercial code art 318 and 469

¹⁶⁴ Commercial code 465,468,469

Therefore, as we understand from the current practice, companies formed between few persons and selling share to the public immediately after formation is not legal way since not fulfilled the capital increasing requirements.¹⁶⁵ The company formed between founders and which immediately selling shares to the public have the effect of putting the shareholders at risk. Since formation share companies by public subscription, the funds obtained from share sales are deposited in a blocked account. But in case of capital increase by public subscription, there is no such requirement.

As observed from their memorandum of association, most of the share companies established between founders with the amount of initial capital which is between 50,000.00 to 60,000.00 Ethiopian birr. For example, Mulu Mesob Foods Share Company was firstly established by 60,000.00 Ethiopian birr by 6 people in 2000 E.C. and latterly it opened this share company for public subscription. However it didn't commence the business up to 2006 E.C. because of the reasons like management problem and the member's lacks of capacity to fully subscribing in to shares of the company and last year it was dissolved after many individuals and county resources were damaged.¹⁶⁶

As currently observed and interviewed, some officials and share companies founders, there are problem associated with lack of commence the business for long period of time after their registration were ended and collected huge amount money from the public. The founders and directors who had collected unfair interests and other benefits form Share Company provided unsatisfactory reasons for why they didn't commence business for five to six years.¹⁶⁷ Even if currently massive and diversity sector of share companies have being formed with huge capital and thousands of investors whom are subscribing to those incorporating companies, but most companies will not start their business for different reasons. Some of their reason is the capital is not fully subscribed; lack of good feasibility study and lack of land for their investment would be

¹⁶⁵ Ibid supra note 21, such as Habesha Cement share company, Habesha Breweries share company, MuluMesob, Access real Estate share company etc.

¹⁶⁶ From Report document by share holders and management presents to ministry of trade, available at ministry of trade, share companies and sectoral association follow up and support directorate. And see table 1 on last page of this chapter.

¹⁶⁷ Id supra Note 21, 29, 157 for instance Heber Shugar share compny, Yeblunile Micro and small enterprise Share Company.

some of the problem.¹⁶⁸ Thus, some points would be made below with respect to the cause for not start business for long period of time.

3.4.1 Absence of the Period of Limitation

After the share companies those established through public subscription of shares collect huge amount of birr from subscriber, it takes a long period of time to actually commence the business in Addis Ababa. The Ethiopian law fails to put clear period of limitation on this. On article 312(3) of commercial code, it states that where registration has not been affected within one year from deposit in a bank, the sum deposited shall be repaid to the subscriber and after one year such sums shall bear interest at the legal rate. Even if the company practically not collect money without approved by registration office, some people argue that this article is put period limitation on how long time should have to take actually enter in to work; however the article is not clear one.

But in practice share companies with high members also not enter into business for long period of time. When we see experience of other countries there is limitation of time when company to commence the business. In Lesotho new companies act 2011 on article 87(5) (a) and (6), state that if the share company fails to commence the business within 12 months of the issues of the certificate of incorporation the registrar may remove a company from the company register, except when it is due to delay relating to licensing or other legal requirements, or if the company had valid and reasonable grounds to the satisfaction of the registrar¹⁶⁹. National bank of Ethiopia (NBE) also enacted proclamation that obliged the bank and insurance as to commence the business within 12 months from the date of the issuance of the license on Article 6(2) and article 7(2) banks and insurance proclamation respectively.¹⁷⁰ For non financial share companies on article 11(1)(e) of commercial registration and business licensing proclamation states that registration office may cancel a commercial registration if the business license fails to obtain

¹⁶⁸ Ibid

¹⁶⁹ Formation of companies under new act of companies 2011,lesetho available at www.accaglobal.com/.../formation-of-companies-under-the-new-companies-act-2011 accessed on march 26

¹⁷⁰ Banking Business: Proclamation No. 592/2008, Federal Negarit gazetta of the Federal Democratic Republic of Ethiopia on art 6(2) and insurance business proclamation No 749/2012

$$384800 \times 5 \text{ year} = 1924000$$

- Hebere share company

$$\frac{597660000.00 \times 12}{100} = 71719200$$

$$\frac{597660000.00 \times 7}{100} = 41836200$$

$$71719200 - 41836200 = 29883000$$

$$29883000 \times 4 \text{ year} = 119,532,000$$

- ✓ Or if it is compound interest, we can see Hebere Share Company as the following:

$$\text{Future value} = \text{principal} \times (1+i)^n$$

Where i= annual interest rate

n =years

$$FV = 597660000.00 \times (1+0.12)^4 = 940429580.7$$

$$Fv = 597660000.00 \times (1+0.7)^4 = 783410343.3$$

$$\text{The difference} = 940429580.7 - 783410343.3 = 157019237.4$$

Additionally, the investors for the reason of not commencing the business may be affected in the following ways:

- By the depreciation amount of initial capital?
- If the money commences the business how much profit it brings to the subscriber?

From this fact it we can understood that currently the founder of Yeblu Nile Micro and small enterprise share company may cheat out 1924000 birr from subscriber and the founder Hebere share company they take 119532000/ 157019237.4 birr that part of the subscriber. There are many other share companies those not enter in to business for long period of time without unsatisfactory reason. In such situation, founder may exploit the principals' (shareholders') in different ways and slow down the speed of development in the Ethiopian economy. Therefore, to

overcome this problem and other scenario, the draft commercial code should be put the period of limitation in clear language since the problem is not solved in draft commercial code.

3.4.2. Undercapitalization

Presently other problem for not commence business in time in Addis Ababa is, related to difficulty of raised capital and most of they are undercapitalized.¹⁷⁵ The Code provides, a share company shall not be formed until the capital has been fully subscribed. However, as raised in above the practice of formation of share companies first formed between founder as per article 316 of commercial code¹⁷⁶ and latterly after legally established between founders, they can widen their ownership base through subsequent offering of shares to the public without starting any business or as almost immediately as the company is registered between founders. Then unable to rise the required capital and stay for long period of time without commencing the business.¹⁷⁷

The existing share companies in Addis Ababa are typically characterized by private subscription of share capital by founder and they can widen their ownership base through subsequent offering of shares to the public immediately after registration. When they try to increase their capital, the absence of well-developed stock market hinders them to start their business.¹⁷⁸ The existence of well-structured and organized stock market is crucial bedrock for companies to become a public company. It is a meeting place and playground for issuing companies and potential public investors¹⁷⁹. Stock market by creating a market for stock trading, gives relief for companies running here and there to find buyers of shares.¹⁸⁰ As a guarantee for liquidation of shares, stock market facilitates the formation of public companies and encourages privately held companies to become a public company by subsequent public issuance of shares.

¹⁷⁵ Ibid supra note 21 and 29 and for instance interview with, Dr bekele Meserasha , one of founder of Mela specialized Hospital, march 13, companies files available at ministry of trade, share companies and sectoral association follow up and support Directorate, Interview with Taddesse Ameza ,former manager of zmar general industry share company, March 16, Interview with Taddesse Girma, founder and manager of Dalol oil share companies, march 16

¹⁷⁶ Commercial code art 316 and share companies data that available at ministry of trade, most of share companies established between founder initial capitals are 50,000.

¹⁷⁷ Ibid supra note 21

¹⁷⁸ Ibid, Alemeneh Abebe, is Ethiopia ready to institute stock exchange market? (Master thesis, Addis Ababa university,2015) p 23

¹⁷⁹ Araya and Tadewos, Towards the development of capital market in Ethiopia: problems and prospects of private sector development, p. 22

¹⁸⁰ Ibid

In the economies of developing countries, there exists an apparent shortage of capital and this puts a constraint on the realization of economic development.¹⁸¹ In this regard, securities markets play a significant role in economic development through mobilizing capital and channeling it to the most productive enterprises. Recognizing such role of securities markets, more than a dozen African countries have established stock markets, but Ethiopia is not one of them.¹⁸² Unlike its neighbors, Ethiopia still neither has a stock market nor is its firms allowed to be listed in foreign stock markets.¹⁸³ As a result, valuation and price discovery of the existing companies is problematic in Addis Ababa.

Stock market enables the public to be informed of where and how much to buy shares and which companies are issuing shares to the public thereby enhance the public investment in shares. An organized stock market, by recording and modifying the price of shares, provide price discovery mechanisms. The upward and down ward variation of the price of shares in stock market is an indication of managerial and financial performance of companies.¹⁸⁴ A well-structured stock market enables companies to offer small fractions of their capital and control price manipulations. In doing so, it enables small investors of the public to buy shares. All these are the prospects of well-structured and organized stock market in boosting and solving lack of capital share companies established through public subscription of shares. Stock markets give a wide spectrum of people a chance to buy shares and therefore become part owners (shareholders) of profitable enterprises.¹⁸⁵ Thus, absence of security market in the countries is one of the causes for share companies not commence the business in time.

3.4.3. Problem With Regard To Feasibility Study

The commercial code states that if the company is to be formed by public subscription that public subscription should be made by a prospectus.¹⁸⁶ Public offering of shares should disclose all material information, and the regulation of public issuers should be based on the principle of full, timely and accurate disclosure of relevant information to the public and the

¹⁸¹Asrat Tessema. Prospects and Challenges for Developing Securities Market in Ethiopia: An Analytical Review. (2003) *R & D Management*, 15(1) p.50.

¹⁸² Ibid.

¹⁸³Minga Negash. Rethinking Corporate Governance in Ethiopia, *Journal of Economics Literature classification*: (2008) p.5

¹⁸⁴Ibid

¹⁸⁵ Ibid

¹⁸⁶The Commercial Code, Art 317-318

shareholders.¹⁸⁷ It may not be feasible or profitable to convert all identified business opportunities into real projects. The founder, therefore, undertake detailed feasibility studies to investigate all aspects of the business they intend to start.¹⁸⁸

From article 318 commercial codes understand that the issuers are required to disclose all material facts and register the prospectus and shares before offering it to the public. However, as other countries do there is no organ that reviews prospects that prepared by founder in which responsible to regulate and registers prospectuses in order to ensure that it is fair and honest before the issuers make a final offering of shares.¹⁸⁹ In other countries the concerned authority goes beyond disclosure and registration and assesses whether the disclosed information is fair and doesn't create damage to the public. If the draft prospectus is false, or may cause damage to the purchasers of securities, or the office suspends the public offering process.

In the present time, when we see practice the other problem for not commence the business in time by share company in Addis Ababa is the absence good feasibility study and non existence body that review the prospects. Under office of ministry and branch office that registered share companies there is no expert that examine whether the business is feasible enough to become a real business.¹⁹⁰ Currently, the founder of share companies brings an over ambitious and defective prospectuses towards the office and the office itself are registering these prospectuses without review.¹⁹¹

For example, most of the businesses that need land for the investment their founders simply put in prospectus as the land would be offered for their investment from the government. However, this act is against with the land policy of the country and it makes the formation shares company problematic.¹⁹² This premise of the investment is the back bone of the business. According to current land policy of Ethiopia, whether it is rural or urban land, it granted for investor based on lease. Depend on the location of the investment premise; the land may be acquired through

¹⁸⁷A.Carvajal and A. Elliott, On strengths and Weaknesses in Securities Market Regulation: A Global Analysis,2007, internationally monitory fund research paper p. 6

¹⁸⁸ Available at <https://edurev.in/studytube/NCERT-Textbook-Chapter-7-Formation-of-a-Company-Clas-s-11-Business-Studies/fb0f6535-3459-4fe2-a14f-6f5fbd14f6ea> accessed on march 23

¹⁸⁹ Joseph.F,Deniels, Comparing U.S. and Hong Kong Public Offering Regulation: How Cost Effective is China's Primary Capital Market? ,(1995), p. 1826 available at heinonline.org/hol-cgi-bin/get_pdf.cgi?handle=hein.journals/scal69§ion=53 accessed on march 12

¹⁹⁰ Ibid supra note 29

¹⁹¹ Ibid, Ibid supra note 21

¹⁹² Ibid supra note 21

competitive lease. Especially, the amount of birr the lease land acquired in Addis Ababa is currently very high and the founders who not investigate whether acquiring land by lease in Addis Ababa is feasible or not for the business it leads the business to crises. So, the founders simply put as they would get the land from the government which is against with the land policy of the countries and it is assumed as cheating the investors.¹⁹³

3.5. Inadequate Legal Protection of Investors

The legal infrastructure plays a pivotal role in the formation and operation of share companies. Legal protection of public investors here refers to all legal rules enacted to protect the public investors (shareholders) from company founder, managers and controlling shareholders. The legal frame work that empowers and governs the regulator and the rules for the regulation is cornerstone of the existence and development of the share companies. Currently, the 1960 Commercial code of Ethiopia is applicable throughout the country and the principal sources of law for legal protection of investors. Accordingly, the code deals with, among others, the formation of share company, the rights and duties of shareholders and the management organs of the share company.

The level of legal protection afforded to investor significantly influences the investment decision of public investors. It is unquestionable that the more the legal regime is protective of investors, the more the small investors of the public build confidence on the legal system. The more the small investors relied on the legal system also means that they are ready to subscribe or buy shares, which in turn leads to development of Share Company in country. OECD principles also suggested that for effective corporate governance, legal and regulatory framework should integrate effective corporate laws, regulations and voluntary codes and standards. However, existing legal frameworks failed to address the issues in relation to the regulation of a share companies.¹⁹⁴

In the absence good legal protection of investor of share companies, the business is affected in different ways. Currently, the directors and board members in Share Companies are mostly the founders themselves and on the first step of operation (on beginning of the business) the share

¹⁹³ See, Urban Land lease proclamation No 721/2011 ,18years no 4, 28th art and interview with Dr Daniel Bahailu, Lecturer in law at Hawassa university ,may 28,2018

¹⁹⁴OECD (2017), OECD Corporate Governance Factbook 2017 p 15

holders are exploiting by them.¹⁹⁵ They can do as they like under the cover of Memorandum and Articles of Association drafted by themselves. The managers, who are expected to represent the interests of the shareholders, often engage in the pursuit of self-interest that hurt the owners. The managers can do this because they are in control of the firm's assets and resources, and they possess insider knowledge that the shareholders do not have.¹⁹⁶ Unavailability of lack of corporate governance policy framework, qualified professionals, results problem of transparency and disclosure, conflicts of interest, lack of adequate protection of minority's rights, etc is some of problem.

There are founders and directors who collect unfair interests and other benefits of shareholders money by not commencing business for five to six years without giving unsatisfactory reasons. For example, when we see the case of Mela Specialized Hospital Share Company, which is established in 2014, most of the members are doctors; however, still now they didn't enter in to the business. The boards and directors of the share company are the same persons and they set for themselves the high amount of remuneration.¹⁹⁷ After the subscriber identifies such case and brings the case to ministry of trade as it solves it, but the ministry couldn't solve the problem. Then they took their case to court. But the case is still pending in the court. In this case, the Memorandum/ Articles of associations of Mela Specialized Hospital Share Company didn't comprise a provisions or the need for remuneration policy. They set remuneration for themselves against the requirement of the commercial code which demands the general meeting to decide the amount of board and directors' remuneration.

The Commercial Code does not require the transparency of remuneration setting process guide, disclosure and shareholders' approval of remuneration policy and remuneration report which allows shareholders and other stakeholders to properly exercise their role in the corporate governance.¹⁹⁸ In the absence of disclosure obligations and lack of procedural requirements for the remuneration setting process and its amount, coupled with the absence of independent

¹⁹⁵ Ibid supra note 37, For instance Mela specialized hospital share company, Sky bus share company, Sunshine chemical share company, Commoros General trading share company, crystal capital service share company, crystal leather share company, Access real state share company, Acss capital service share company,

¹⁹⁶ ToyinIsholaLasisi The Relationship between Corporate Governance and Organizational Performance in Nigerian Companies (thesis paper, *Walden University*, 2017) available at <http://scholarworks.waldenu.edu/dissertations>

¹⁹⁷ Ibid supra note 24 and 37, memorandum and article of association of melaSpecilazed Hospital that acquired from ministry of trade March 12, 2018

¹⁹⁸ Adrian Fong, Practicing Corporate Governance through Corporate Disclosure?, Working Paper, (Faculty of Law, Chinese University of Hong Kong), p9

professional directors and competent remuneration committees, there might be arbitrary remuneration decisions though there is no accurate empirical evidence in that regard. If boards of director are empowered to determine the amount of their remuneration, there will be conflict of interest and its fairness and reasonability would be questioned as the chairperson might reward his/her self or crew members excessively.

The Commercial Code empowers the Ministry of Trade to reduce an excessive remuneration by taking account into the special benefit which have been allocated to directors having the status of founders, and taking in to account the position of the company and the salaries and benefits of its employees.¹⁹⁹ However, presently these legal rules are not properly enforced. Simply leaving directors' remuneration to mere market forces regulation would open a wide room for abuses by directors and influential shareholders which would result in unjustifiably rewarding themselves.²⁰⁰ To prevent this excessive payment and corrupt business environment, regulatory intervention of the Ministry of Trade is highly important. Although there are public out cries and prolonged litigations, no one has paid serious attention to the problem. The only solution is court dispensation of cases which is last resort in commercial dispute resolution methods. This fact make it complicated the in corporatization if Share companies.

Again, the commercial code and other relevant laws do not require share companies to have independent non-executive directors. Even if non-executive directors play a significant role in providing independent and objective guidance and direction of management and company, the Commercial Code and other relevant laws do not require companies to have independent non-executive directors and do not distinguish the roles of the board from that of the management. The law does not define the independence of board of directors. Allowing one and the same person to wear four or more hats at the same time encourages a person to abuse power and paved the way for a person to exploit and abuse the assets of Share Company. Fama and Jensen suggested that effective company boards would be composed largely of outside independent directors, and that effective boards have to separate the functions of management and control.²⁰¹

¹⁹⁹ Commercial code Art.353 (7)

²⁰⁰ Interviews Ato Yosef Alamu, id supra note 21, for instance the case, Mela Specialized Hospital share company, which case is pending on the court by setting high remuneration for themselves

²⁰¹ E. F. Fama and M. C. Jensen , Separation of Ownership and Control, Corporations and Private Property, [1983], vol 26, no 6 ,*Journal of Law and Economics*, pp 301-325. (available at <http://links.jstor.org/sici?sici=0022-2186%28198306%2926%3A2%3C301%3ASOAC%3E2.0.CO%3B2-A> accessed o march 23

They argued that “if the CEO was able to dominate the board, separation of these functions would be difficult” to the disadvantage of shareholders and that “outside directors are able to separate these functions and exercise sound decision control.”²⁰² When we see experience of financial companies (particularly banks), Proclamation No.592/2008²⁰³ and NBE Directives prohibit general manager/s or CEOs from concurrently holding the positions of CEO and membership in the board of director.²⁰⁴ But non-financial share companies do not have clear law on these issues; as a result this opens the door for director to exploit the shareholders, especially on the beginning of their business.

The Board plays a crucial role in controlling entrenched power of the management and in minimizing the agency costs. In this regard, the perplexity of the commercial code is that it does not make a clear separation between the executive decision-making roles and the managerial supervisory roles.²⁰⁵ It paves the way for the General Manager to simultaneously assuming membership in the board. In fact, this is practically seen in most of the share companies in Addis Ababa city.²⁰⁶ In the absence of independent structure and objective composition of the board, shareholders of share companies in the city cannot be protected from the exploitation of general managers. The simultaneous existence of the same person in executive decision-making position and board membership position make managerial supervision impossible and puts other shareholders in a disadvantaged position. This is because of the shortfall of the commercial codes which neither clearly preclude general manager from simultaneous membership of the board nor not clearly separate the role and function of general manager from that of the chairman of the board.²⁰⁷

Furthermore, the commercial code fails to states as the regulatory body as take the administrative remedies on those breaches of the rules governing Share Company. Thus, the remedies are the

²⁰² Ibid

²⁰³ Banking Business proclamation provides that on Article 15(3) of “... chief executive officer of a financial institution may not, at the same time, serve as a director of a bank.”

²⁰⁴ NBE Directives, No.SBB/49/2013, Limits on Board Remuneration and Number of Employees Who Sit on Bank Board”,.

²⁰⁵ See, The Commercial Code, Art.384(4)

²⁰⁶ Id supra note 21 and for instance Dr Gobenza is the chair of board and General manager of Both Crystal Capital service and Crystal Leather share company, Ato Ermiyas Amalka also the member of the board the director of Access real estate and Access capital Service and Ato Tezera also the member of the board and director of Sunshine Chemical and Commoros General trading share companies

²⁰⁷ For example we can infer this fact from Mulu Mesob food Share Company and Mela Ethiopian Specialized Hospital

rights of the victim to request the concerned organ to take one or more of the administrative measures like suspension or removal of individual directors or the whole board, issuing of warnings, taking over of management, revoking the license. On the other hand, regulators in some countries are given the discretion to impose administrative measures, such as fines and other more severe sanctions, to ensure compliance.²⁰⁸ The share company law failed to allocate adequate and sufficient regulatory and supervisory powers to regulators of share companies to take measures on those corrupt and fraudulent officials, on those Failure to comply with the provisions of the code and do activities that harms the interests of the share company and shareholders offenses. Having such a regulatory power has the benefits that would early solve the disputes, reducing of unwarranted litigation costs and protecting the interest of the company and its shareholders.

Lastly, Even though the commercial code does not prescribe any formal qualifications for directors and board members of companies, but the draft commercial code on article try to solve the problem. However, the office under the ministry of trade is the way enacting proclamation similar to Draft proclamation.²⁰⁹ As raised in above it is not the right way rather than hastening the enactment draft commercial code to solve the problem. The regulators should facilitate shareholders activism by letting them to be more attentive in appointing only people with perfect integrity and adequate qualifications as directors of companies they invest in. The ministry of trade should support the shareholders as appoint managers and board members who have adequate managerial experience in business and person with honesty, integrity, diligence and reputation to the satisfaction.

Generally, due to the above fact, currently the establishment of Share Company through public subscription of shares is decreased in Addis Ababa as seen in above. Lack of public confidence on the existing legal framework is a major impediment for extensive shareholding participation of the public in Addis Ababa. The previous experience of loss and bankruptcy because of bad management inflict pain and affect the investment decision of individuals living in Addis Ababa. The managerial (board and managers) exploitation and loss on the people whom they know and by news rotated in the city in newspapers is another factor discouraging some potential public

²⁰⁸Getachew Redae T ,The regulation of related party transactions in the Ethiopian financial sector: with special focus on banks(LLM thesis Addis Ababa university2013)

²⁰⁹ Ibid supra note 21 and 29

investors. It open the door as people consider that investing business in Share Company is like simply give money for thieves.²¹⁰ Hence, formulating an appropriate and efficient share company law that reflects the modern business realities and accommodates the demands of different market players in the country is very importance.

While it is indisputable that shareholders' power is a result of law, contract, and informal rules, the board and management often have absolute power over the affairs of the firms. First, stockholders are usually widely dispersed and may not have the time, information, or willingness to form a critical mass to challenge the directors. Secondly, management has a clear advantage; being in possession of superior information and proxy powers, they could use the leverage to oppress the shareholders.²¹¹ Whereas the managers are employed to maximize returns to shareholders and also look after the interests of all other stakeholders, they often pursue self-interest to the detriment of the financial interest of their principals the pursuit of self-interest by managers.²¹² .

²¹⁰ Ibid supra note 29

²¹¹ ToyinIsholaLasisi ,The Relationship between Corporate Governance and Organizational Performance in Nigerian Companies, Walden University thesis paper2017available at <http://scholarworks.waldenu.edu/dissertations> accessed on march 13

²¹² Ibid

CHAPTER FOUR

REGULATORY BODY, INSTITUTIONAL FRAMEWORK AND ITS LIMITATIONS

4.1. Introduction

The regulation goal of the public listed companies that discussed in unit two achieved through regulatory body in many countries. Company law is considered by some as a common domain of company practice, interpretation and sometimes interference by courts; in some countries a certain degree, company law is also administered and created by regulators.²¹³ Most effective regulatory bodies, whatever the jurisdiction in which they operate, have clear responsibilities and objectives, adequate powers, adequate resources, transparency, and accountability.²¹⁴ Generally, the responsibilities and objectives of such a body depend in part on the regulatory model in place and the role the regulator has been established to fulfill.²¹⁵

Many countries today consider enforcement of the rules for the share company industry to be part of the function of a regulator. Enforcement is a necessary product of the process of authorization and supervision, in the sense that a regulator must enforce compliance with rules.²¹⁶ Requiring a regulator to enforce rules entails giving the regulator responsibility for carrying out inspections, investigations, and surveillance, and imposing remedial action and penalties.²¹⁷ In jurisdictions where this occurs, regulators normally have powers to request information, impose sanctions, seek orders from courts or other tribunals and suspend business operations or trading.²¹⁸ International standard setting bodies have been promoting the importance of domestic regulators having adequate enforcement powers.

²¹³Klaus J. Hopt, Modern Company Law Problems: A European Perspective Keynote Speech, max pls nk institutes for foreign and private and private international law, Hamburg ,Germany,[2000], p 11

²¹⁴Mwenda, Kenneth Kaoma, Legal Aspects of Financial Services Regulation and the Concept of a Unified Regulator world bank research paper, 1/2006, p 14 available at siteresources.worldbank.org/.../Legal_Aspects_of_Financial_Sces_Regulations.pdf accessed on march 12

²¹⁵ Ibid

²¹⁶ Id p 15

²¹⁷K. K. Mwenda, Legal Aspects of Corporate Finance: The Case for an Emerging Stock Market, (PHD dissertation paper, University of Warwick, 1998); and K. K.Mwenda, Zambia's Stock Exchange and Privatization Programme : Corporate Finance Law in Emerging Markets, by African economic and social development, Edwin Mellen Press 2001,pp192–218

²¹⁸ Ibid

4.2. Share Company Regulatory Body in Ethiopia

In Ethiopia, economic regulation has had its root since the imperial regime²¹⁹. In the post 1991 period, the newly established government of the Federal Democratic Republic of Ethiopia, along with the ongoing privatization and economic reform, established several sectoral regulators with various regulatory functions. The sectoral regulators have been established in the form of ministries, authorities, agencies, commissions and offices as regulators of the market for the supply of goods and services.²²⁰ In each sector of the economy, the particular laws provide for requirements that firms and business persons have to comply with before their engagement in the production and provision of goods and services to the public.²²¹ The compliance requirement begins from getting the required permit before engagement in that particular service or production sector concerned. The regulation is also continues during the operation of the business activity.

Currently, there is no extra government body that insures the predictability and supervisory role of the companies.²²² The share company law only provides regulatory and supervisory powers to the Ministry of Trade as to regulate the formation, ongoing functions and governance of companies. The Ministry has the following regulatory and supervisory powers on share companies.²²³ These are registering newly formed companies, depositing companies' statutes and other periodical reports, Regulating crossholdings of shares among holding companies, reduce the remunerations of directors upon the application of shareholders not less 10% of the share capitals of the company and by its initiation or upon the application of shareholders, order to conduct investigation of the companies' scandals and nominee shareholders.²²⁴

Under ministry of trade there is 23 directorate offices and from them share companies are regulated under the office of share companies and sector association follow up and support directorate.²²⁵ The ministry of trade is making institutional framework changes and formed

²¹⁹Solomon Abay, Designing the Regulatory Roles of Government in Business: The Lessons from Theory, International Practice and Ethiopia's Policy Path,[2009]Vol. XXIII, No.2 Journal of Ethiopian Law, p.66

²²⁰ Ibid

²²¹ Ibid p 67

²²²Dawit Endeshaw, Ethiopia: Ministry Proposes Regulatory Agency for Share Companies, (Addis Fortune, Addis Ababa, 14 June,2016)

²²³ Id supra note 51 p 7 <https://www.abysiniaweb.com/blog-posts/item/1471-ethiopian-share-company-law-in-light-of-oecd-principles-of-corporate-governance>

²²⁴ Commercial Code arts 90, 323, 447,344, 353(7), and 318-387

²²⁵ Ibid supra note 21

corporate regulator directorates that can follow up and support corporate. However, challenges are still exist today because the code hasn't given enough regulatory power to regulate share companies and there is no place to file a complaint by shareholders for mismanagement of share companies except taking the case to court.²²⁶

This regulatory system cannot be a reliable system to effectively control the corporate frauds in the context of booming of share companies in Ethiopia. Companies do not seem to apply principles and best practices of corporate governance voluntarily. For instance, share companies engaged in financial business, despite rigid regulation of the NBE, are not free from frauds as evidenced by their former top executives being criminally prosecuted.²²⁷ This indicates that the regulating and controlling of frauds in companies by employing a soft law is difficult. As a result, both weak market and the conduct of Ethiopian companies point to the ineffectiveness of voluntary code to ensure good corporate governance in Ethiopia.²²⁸ One of the proponents of mandatory code in US argues that the world needs a strict corporate regime, which it able to eliminate fraud, corruption and other misdeeds and practices.²²⁹

In the same way, in Ethiopia also need regulatory body which binds all companies and proper penalties should be imposed on those companies fail to comply with the law. Since, currently in Ethiopia there are number of companies formed by sale of shares to the wider public. The coming out of publicly held share companies in the country in turn gives increase to huge number of complex issues. Ownership separates from control of dispersed shareholders and goes into the hands of few managers. In such situation, agents (managers) may exploit the principals' (shareholders') investments as they have more information and knowledge than the principals.²³⁰

²²⁶ Ibid

²²⁷ See Addis fortune, volume 12 No.575, (May 8, 2011). For instance, on May 6, 2011 witnesses testified against Awash International Bank's Leikun Brehanu, former president, and nine other former employees who had been brought up on charges of mishandling letters of credit and approving a little over 6.1 million dollars in credit outside of the bank's foreign currency procedures.

²²⁸ Hussen Ahmed, reforming corporate governance in Ethiopia appraisal of competing approaches Oromia law journal [2006], vol 3, no. 1, Oromia law journal p 205

²²⁹ Anita I. Anand, Voluntary vs. Mandatory Corporate Governance: Towards an Optimal Regulatory Framework, (2005). American Association law school, Washington DC, Working Paper, 566, p 4 available at

https://law.utexas.edu/wp-content/uploads/sites/25/anand_voluntary_adoption_corporate accessed on march 24

²³⁰ Ibid

4.3. Power of Ministry Of Trade as Implementation Institution

As the Ministry of Trade and Industry is the primary regulator under the Company Law, their most important duties are those relating to registration of companies, including initial registration and registration of other acts and documents (e.g., checking and approval of company names, amendments of articles of incorporation, mergers, and dissolutions).²³¹The Ministry's personnel were courteous during the mock company registration. There is no ongoing company regulation or monitoring such as is provided in other countries.²³²

The share company law provides regulatory and supervisory powers solely to the Ministry of Trade.²³³However, it is failed to mandate sufficient powers to the Ministry for regulating public companies from their incorporation to ongoing operations.²³⁴The Ministry has very limited regulatory powers: registering and receiving companies 'reports, regulating share transfers between holding companies, reducing boards' remuneration and ordering investigation of companies' scandals based on shareholders petition.²³⁵ The Ministry's supervisory roles are almost omitted in the provisions. Even after the finding of the investigation of companies' criminal acts, there is no provision that allows the Ministry to take appropriate disciplinary action on the failure of companies. This absence of sufficient power by ministry of trade leads to inadequate to protect investors and to avoid market inefficiencies.²³⁶

In addition to this, as per article 21 of a proclamation of powers and duties of the executive organs of the Federal Democratic Republic of Ethiopia proclamation no. 916/2008 give power to ministry of trade on the issues like commercial registration, business licensing services, control the use of business licenses for unauthorized purposes and promote the expansion of domestic trade.²³⁷Specifically, on article 6 and 7 it states that the power of ministry is on share company by stating in the way that the ministry provides commercial registration and business licensing services in accordance with the relevant laws, control the use of business licenses for

²³¹Commercial code , Arts.99, 323, and 447, 353(7), 314(2),344 and 318-387

²³²Boonz,Allen and Hamilton, Ethiopian commercial law and institutional reform and trade diagnostics united states agency for international development, p 21, 2007,Available at <http://egateg.usaid.gov/sites/default/files/ethiopia.pdf> last accessed on 13 march 2018.

²³³Ibid

²³⁴ Id supra note 51 ,p21

²³⁵Commercial Code art 32-35

²³⁶ Id supra note 51, p23

²³⁷Definition of Powers and Duties of the Executive Organs of the Federal Democratic Republic of Ethiopia, Proclamation,916/2015, fed Negarit gazetta 22th year no. 12, Addis Ababa, December 2015 art 21

unauthorized purposes and give support for²³⁸ and monitor the establishment and operation of share companies with a view to protect the interest of share holders and the society.²³⁹ However, the proclamation does not clearly give power to the ministry as it takes disciplinary measure on those who commit crime while doing their work.

At present, there are only few regulatory roles of the Ministry of Trade to enforce the law and prevent excessive remunerations and payment related abuses.²⁴⁰ As laws and regulations have not been enforced, they have fallen in to disuse and often been forgotten as precisely being observed in the fate of the Commercial Code provisions in regulation of the share company provisions. Hence, currently there is public authority not actively regulating the formation and operation in Ethiopia to protect investors. For that matter, the regulatory body which is responsible to regulate the share company in Ethiopia is not having enough power. The presently practice of enforcement relies on the traditional approach of civil laws and remedies. These traditional remedies constitute the civil claims of private parties based on private laws including agency law, contract law, extra- contractual liability law, and enforcement of property law.

4.4. Limitation Associated With Regulatory Body and Enforcement Mechanism

The OECD Principles urge government policy makers should craft their institutional bases that ensure the effective and efficient corporate governance framework. The principles suggested three prerequisites for effective corporate governance framework; from them the one of principle recommended that the institution regulate share companies should supplemented by clearly allocated regulatory and supervisory powers with robust implementing institutions.²⁴¹ Sound regulatory institution framework fosters market integrity, improves economic efficiency, growth as well as builds investor confidence, create incentives for market players and promote transparent and efficient market.²⁴² To smooth the progress of new investment and provide adequate investors' protection the formulated good regulatory body should have the overall economic impact and foster market integrity which meets the new market development and creates incentive to different market players. The OECD principles advocate that the legal,

²³⁸ Ibid art 21(6)

²³⁹ Id art21(7)

²⁴⁰ Ibid supra note 21

²⁴¹ OECD (2017), OECD Corporate Governance Factbook 2017 p 16

²⁴² Ibid

regulatory and institutional framework of country that shapes the corporate governance of companies should be adjusted with the new developments of markets.²⁴³

Presently, Ethiopia is attracting foreign investors as well as encourages domestic investment and economy; because it has been at a stage of transformation, the reforms during the last couple of decades brought market economy and corporate business.²⁴⁴ There is a noticeable increase of investments and share companies are seen raising large amounts of capital from the public through offers of shares in new business ventures. This is an indication of a changing landscape on business ownership and business operation that requires good regulation practices in the country.

The writer approached the Ministry of Trade experts to know how share companies established through public subscription of shares are being regulated. Admitting that shareholders are expressing their frustrations on the regulatory role of the Ministry and its practical repercussions on the governance of nonfinancial Share Companies,²⁴⁵ Ato Yosef Alamu the head of share companies and sector association follow up and support directorate in ministry of trade states that Ministry of Trade is playing only a passive role in regulating share companies. It is not really exercising its real power of regulating Share Companies like other countries do. Although individuals or group of shareholders lodge a complaint, against founder, director and other management body, most of the time the Ministry is not intervening to solve the problem and to play its true regulatory role.²⁴⁶ The Ethiopian company law of the 1960s also does not have adequate legislative provisions on how regulate Share Company through regulatory body. Today Ethiopian share companies are instead of being wealth generating/creating areas to the investors through entrepreneurialism, innovation, development and exploration they are becoming the area of battle field between the management bodies and the shareholders due to ineffective applicable laws and weak enforcement on the applicable laws.²⁴⁷

²⁴³ Ibid

²⁴⁴ A note on development of foreign direct investment in Ethiopia, Ministry of finance and economic cooperation, Fiscal policy Directorate, April 2017 available at <http://www.mofed.gov.et/documents/20182/48147/Note+on+Development+of+FDI.pdf/2bc67cb4-6181-4ab6-b85f-7330ca06a3bc> accessed on may 18

²⁴⁵ Ibid supra note 29

²⁴⁶ Ibid supra note 21

²⁴⁷ Id supra note 51 p

Correspondingly, Ato Abiy Mohamed, the team leader of share companies and sector association follow up and support directorate in ministry of trade, states that if the founder, directors and other major shareholders act in conformity with the commercial code or Memoranda/Articles of association, there would be no mechanism that the Ministry would intervene in the internal affairs of the business. Even if, shareholders are complaining about excessive and unfair benefit of directors and founders in the Share Companies but they are told to go to court rather than getting remedies from the Ministry; since they have no legal ground that permit for the office as to take administrative measure up on them.²⁴⁸ He reported that, the only thing that they can do is writing letter for the management of company as the person who commit such acts keep himself from such act that affect the company and subscribers.

One of the problems of enforcement mechanisms is the commercial code and other laws that regulate Share Company's fail to state specifically the power of the regulatory body of Share Companies. Prof. Mahari argues that the Commercial Code part that regulates Share Companies has been forgotten for it was side lined by the policy change of the Dergue.²⁴⁹ The officials of the Ministry of Trade fail to remember that they have a duty to regulate Share Companies.²⁵⁰ The lack of power by regulatory body makes it fail to control the formation process, founder, directors and other posts of management body. Considering these legal problems, a person wearing at least three or four of the hats in a Share Company has a chance of abusing assets of the company. But yet the ministry of trade has no legitimate procedure for it to take measures up on this kind of improper and dishonest performance of founder, director and board of director.

Second, keeping these legal problems in mind, the other problem that magnifies or amplifies this issue is legal gap on the way commercial code try to regulate Share Companies. The question of whom and in what ways regulate market misconducts is the issues left unsettled. For instance, Shareholders representing at least one tenth of the share issued can as a right require the Ministry of trade and industry to appoint or more qualified inspector or control and check the auditors' act where there is a resolution of General Meeting.²⁵¹ However after appoint general auditor and

²⁴⁸ Ibid

²⁴⁹ As cited in Kashay Giday, Remuneration of share company directors in Ethiopia. the law and practice(LLM thesis, Addis Ababa university 1014) p 98, Interview with Mahari Redae (Assistant Professor), Addis Ababa University School of Law, done at his office, on November 22, 2013

²⁵⁰ Ibid

²⁵¹ Commercial code Art 353(7)

identified the some problem and fraud what type of measure it takes by the authority is not clearly stated in the law. For instance, the share holder of two share companies: Cristal Capital Service share company and Cristal Leather company brings grievance to ministry of trade on Dr. Gobenaza who is the chair of the board of director and general manager in both share companies and after the office under ministry of trade identified the problem of conflict of interest only send letter to this person as to he keep himself from create conflict of interest.²⁵²

Additionally, the law says general meeting must be conduct once in a year. Moreover as per article 320 of commercial code when time for making application is expired, the founder shall call a meeting of subscribers as to verifying requirement relating to formation of the company have been complied with and to approve contribution in kind.²⁵³The question here is what if the founder or director of Share Company not conduct general meeting in due time. The law not governs whether the regulatory body calls meeting by its own initiation or up on grievance not is clearly addressed in the code. Regulatory body in order to protect the general public should call general meeting as the share holder should give decision on the issue. Unless it will open the door for founder and for other management of share companies as they exploit the companies. For example, the case of Access Real State which is discussed in above, the founder, the board member and directors are governed by similar group of individuals. These groups of founders did not call general meeting for long period of time without unsatisfactory reasons, and lastly they put company under crises.²⁵⁴ What is more, if the members of boards appoint their families as auditor can ministry of trade has the power to take administrative measure on it? These issues generally are not clearly settled in the code.

Third, the way of handling the meeting and counting vote, the percentage of share holder calling to meeting, group conflict created in the meeting and unlawful decision on meeting also the area that requires regulation.²⁵⁵Thus, even if they prepare meeting, the ways in which the founders and managers commit crime is very confidential and organized. As one expert raised this point, if one subscriber oppose with the inappropriate technical and secret decision of founders and/or directors, they fire with his birr illegally. However, the regulatory body yet has no legal base to

²⁵² Memorandum and article association crystal capital service Share Company and crystal Leather Company available at ministry of trade, sector association follow up and support directorate. accessed March 2018

²⁵³ Commercial code Art 320

²⁵⁴ Ibid supra note 29

²⁵⁵ Ibid

take administrative measure after they assign observers to the meetings and identify act not done according to the law. The code has no provision for a regulatory body to take appropriate measure on wrongdoers and there is no place to file a complaint by shareholders for mismanagement of share companies except taking the case to the court which too cost and despair.

Fourth, absence of follow up and efficient oversight in behalf of the regulatory body on Share Company is another problem. One of the aims of establishment of share companies sector association follow up and support directorate under ministry of trade is to facilitate the formation and operation process of Share Company from birth to death in order to protect the public interest.²⁵⁶ However, the regulatory body is due the shortage of human power and organizational setting problem, not effectively facilitate Share Company's formation and operation process. The share companies sector association follows up and support directorate have 15 staff members and from this only 5 staff worked on share companies: one director, one team leader and three experts.²⁵⁷ When we compare to the China companies regulatory body CSRC, which organization has one chairman, five vice chairmen, 16 functional departments, and three supporting centers. In total, the CSRC has about 1,800 staff members, whose average age is 35 years. About 40 percent of the staff has attained a master's degree or PhD.²⁵⁸ Even though the economic development of both countries is not equal, but it shows that directorate under the ministry is proportionally very small and its left with many jobs in the future.

As to the 2010 plan and action report of the office, it is only planned to supervise 56 share companies out of 750 share companies that established through public subscription of shares and in nine month they only supervised 29 share companies.²⁵⁹ This clearly shows that as to there is a problem with regard to facilitating share company's establishment and ongoing operation on behalf of the authority. This office as its organization setting found only under the head of ministry of trade and does not have branch office on regional state and Addis Ababa as

²⁵⁶ *ibid supra* note 21

²⁵⁷ *Ibid supra* not 29

²⁵⁸ Nicholas C. Howson, Regulation of Companies with Publicly Listed Share Capital in the People's Republic of China, (2005),38 *Cornell Int'l L.J.* 237) p 239

²⁵⁹ Report plan of 2010(nine month), in ministry of trade, share companies and sector association follow up and support directorate.

city.²⁶⁰ Even if regional state and Addis Ababa city they register share companies established through public subscription of shares under trade and industry bureau, but there is no focal person or expert that oversight formation and operation process of Share Companies.²⁶¹ Moreover there is no data recording system which holds the point like history of fraudulent founders, directors and accountant etc between the office, regional state and Addis Ababa. Therefore this all problem make the office as not efficient oversight all share companies established in the countries including Addis Ababa. The 2010 plan and report of nine months of office show the facts as the following.

Table I: Data showing performance supervision by companies' sector association follow up and support directorate in ministry of trade 2010 E.C./nine months)

Goal	Major Activities	Annual plan	9 Months Plan	9 Months Activity	Comparison by %
Customer Increasing client perspectives 85% per cent	Share companies that established through public subscription of shares prior to sold the capital to the public, insuring that prospectus done according to the law and giving permissions as to advertise	4	3	2	67
	Following upon the establishment of the Companies' following up and supporting the implementation of their business pursuant to the Commercial Law, Establishment and By-Laws,	56	42	29	69
	Consulting and resolving grievance shareholders and other stakeholder based on research and problem solving,	36	27	16	59
Ensure the benefits of consumers and stakeholder	Consulting, Supporting and Supervising to solve the disputes between Shareholders and Management of Shares of Share Company according to	24	18	12	67

²⁶⁰ Ibid supra note 21

²⁶¹ Ibid

rs 80%	the law,				
	Attend the general meeting, advice as they work according to the law and follow as well as give support for them.	48	46	38	82

Source: Ministry of Trade and Industry, companies' sector association follow up and support directorate (april16, 2018)

Based on this tabular fact, we can conclude that as the needed follow and support of the ministry is not much significant. Therefore, the ministry should assign enough inspectors which have capacity and knowledge's in implement the relevant law. This inspectors provide support, supervision and Carry out the verification of the existence of defects in the formation and operation of a share company. Additionally they follow as the company is going pursuant to the laws and decrees of the Trade laws and directives and provide consultancy on the laws and procedures governing the share company.

The authority also should assign suffice observers to the general meetings and investigating potential violations and disciplining individuals and firms that violate laws. If possible the authority giving training, technical assistance to management of share companies to protect the public interest and facilitate share companies those not commence the business for long period of time. For example blue Yeblu Nile micro and small enterprise Share Company which was established in 2013 by 769600.00 initial capitals still now it has not entered into business.²⁶² But the managerial body of the business are living by renting office in the middle of Addis Ababa on Golagul Tower and setting high salary for themselves for around six year up to know without starting business for unsatisfactory reason.²⁶³ Again, Sometimes also the founder or director for being fear the risk, not inter into work after collecting huge amount of birr from share holder and they put it simply in the block account for long period of time.²⁶⁴ This has some fact for not starting the business. The founders have the initiation to inter into business activities; but for the lack of the facilitating from the concerning body they stay for long period of time. However, their reason is much satisfactory that should be solved by the body that ought to support them.

²⁶² Ibid supra note 29

²⁶³ Ibid

²⁶⁴ Ibid

Thus, the ministry of trade should assist and take necessary measures on them by identifying existence defects to protect share holders.

Lastly, lack of national principles and up to date codes, directives, which can serve as public policy instruments to assist in their efforts to evaluate and improve regulatory and institutional framework for corporate sectors is another problem.²⁶⁵ This instrument helps by assisting regulators in their efforts to evaluate and improve the regulatory and institutional framework for corporate sectors. Therefore it is good if the ministry enacting some directives like bank sector that help it regulate non financial share companies.

The Financial sector is successful in Ethiopia when compare to other than non financial share company due to they have good regulatory body.²⁶⁶ When we take the experience of supervisory authority of the NBE, it has full power that regulate financial sector. NBE is the instance that decided on quality of organizer, approve of appointment of Directors and Officers, issued directive on qualification to be fulfilled by directors, number of directors in the membership of the board, the duties, responsibility director, limit maximum remuneration of directors and Suspend or remove a director, a chief executive officer or a senior executive officer. It takes corrective measures where an inspection of a bank results in a finding that the bank has failed to comply with the relevant laws and directives of the bank. It can also take the following measures like Call a meeting of its shareholders or board of directors, assign one or more of its officers to watch the proceedings at any meeting of the shareholders, board of directors or any committee instruct in writing corrective measures to be taken by the bank.²⁶⁷ Order the dismissal or suspension of one or more directors, the chief executive officer or senior executive officers of the bank, or impose fines on such persons in accordance with its directives prescribed for such purpose and prohibit the bank from opening new branch offices, restrict, suspend or prohibit payment of dividends by the bank and put the bank under receivership.²⁶⁸

Therefore, the standard power given to the NBE is seems sufficient to regulate financial sector. Even if it is an undeniable fact that non-financial companies are not as serious as banks, but the

²⁶⁵ Id supra note 21

²⁶⁶ Id supra note 140

²⁶⁷ Mokenen kassahun, Financial regulation and supervision in Ethiopia,[2014] vol 5 no 17 ,journal of economic and sustainable development , available at <https://www.slideshare.net/AlexanderDecker/financial-regulation-and-supervision-in-ethiopia> accessed on march 27

²⁶⁸ Ibid supra note 21

former should not be left at the mercy of directors and major shareholders. Thus, the ministry of trade should possess some supervisory power as properly regulate non financial share companies. The economy does not stand on banking business alone. Rather, all share companies should be given reasonable attention from the perspective of enhancement, regulation and supervision.

Generally, the current practice show that institutional framework is defective to offer incentives to market players and failed to foster market integrity and promote effective and efficient system to shape the relationships between the state, citizens and businesses. These all problems show as that the share company law failed to allocate adequate and sufficient regulatory and supervisory powers to regulators. This passive involvement of the Ministry of Trade is worsening the situation of formation and commencement of business by share companies at their early stage of business operation. Due to these gaps there have been various news headlines in the press and many court cases that discourage establishment and operation of Share Companies. For instance Real Estate Companies are the predominant²⁶⁹. Thus; the Ministry of Trade should have clear allocation of regulatory, supervisory powers and administrative mechanisms subject to avoiding conflict of interest, mal administration and for closing the door from those who abuse the resources of share companies. The regulatory body whom is the body permit formation of company, it should also regulates and supervise corporation from birth to death.

4.5. Impact of Good Regulatory Authority on Performance of Share Companies

The OECD principles suggested some prerequisites for effective corporate governance framework. From them it should be supplemented by clearly allocated regulatory and supervisory powers with robust implementing institutions are the one and the main principle.²⁷⁰ Ethiopia has undergone rapid economic transformation and able to make changes in business environment in the past twenty years. This changing business environment requires the positive reaction of good regulatory body which must respond to the needs of the different stages of reform that the country is doing on business operations.²⁷¹

²⁶⁹For instance see Eleni Araya , Board Members Seek Government Support in Access [Real Estate] Debacle, Addis Fortune Vol.14, No.697, September 08, 2013

²⁷⁰ Id supra note 51, p 22

²⁷¹ Ibid supra note 241

Regulatory body *inter alia* facilitates access to development of share companies by making company performance visible and reliable. As Ethiopia's developmental and poverty alleviation pursuits require stronger share company that can generate and increase employment opportunities, produce goods and services and create profit for the investors. It needs strong regulatory body that is supplemented by real law and power that protect the public interest and develop public confidence in the share companies.²⁷² To achieve these objectives, companies must regulate as to have good and effective system of company formation and corporate governance and must also be perceived to be properly managed.

The country is expected to care about the quality of regulatory body in future to maintain sustainable economic growth or for the sake of healthy business developments in the country. Poor implementing institution of Share Company can harm national economic performance and financial stability. The financial crises in Asia, Russia and somewhere else have confirmed this.²⁷³ Though situation differed, what crisis countries all had in common was distorted governance structures that led to inefficient economic decision-making. Therefore, the government should change regulatory and institutional framework regarding regulatory authorities and making them ready to make awareness creation on the subject. For preventing dilemma that happen in share companies formation and commencement of business, the regulators should prepare guidelines and monitor their compliance with regard to founder and directors' integrity, experience and expertise, foresight, directing qualities and ability to understand the overall company performance, composition and structure.

²⁷² Ibid

²⁷³ Mwenda, Kenneth Kaoma, Legal Aspects of Financial Services Regulation and the Concept of a Unified Regulator world bank research paper, 1/2006, p 14

UNIT 5

CONCLUSION AND RECOMMENDATIONS

5.1. Conclusion

Companies established through public subscription of shares offer an opportunity for extensive number of individuals to collectively engage in business activities and mitigate income inequalities. They are characterized by the accumulation of capital from hundreds and thousands of investors and their involvement in huge economical ventures. By doing so, widely held companies play a key role in state's socio-economic development and in bringing broad based socio-economic transformation at both individual and national level.

Although Ethiopia has been credited as one of Africa's fastest and consistently growing economy, its undesirable process of company formation and commencement of business have been encumbered its development. The Ethiopian share company law, regulatory and institutional framework apparently failed to intend to achieve these outcomes. The legal problem combine with other practical problems have paved the way for a person to exploit and abuse the assets of Share Company. Especially this is taken place during formation and commencement of business of Share Companies established through public subscription of shares.

Regulation of share companies refers to the set of rules, controls and processes established by public authorities with the aim to prohibit certain behavior, decision making and transactions in the share companies. It ensures that the share companies business to be fair, transparent, efficient, effective and free from manipulation and fraud. Thus, the ultimate significance of the regulation is to make the share companies play a vital role in the economic growth. Good regulation of companies can encourage new investment and provides investors protection by setting forth clear and objective rules for corporate ongoing internal governance. Especially, in order to get this benefit, the legal, regulatory and institutional frame work should protect investors, against fraudulent and it promotes private sector investment and increases confidence of public.

In the conducting this study, the writer has discovered tribulations of share companies established through public subscription of shares. The first problem of share companies established through public subscription of shares is the absence of regulation of foul play

founder. Currently though founders who operate the company are few in numbers, a group founders may establish more than one companies that may failed to start operation due to their fault, fraudulent, lack of capacity, skilled professional, etc. They collect unfair interests and other benefits of shareholders money by not commencing business for five to six years and they gave unsatisfactory reasons for such of their activities. Even after the company they try to form is failed to incorporation due to this reason, they pass to form another company though they have bad reputation and they are going to affect the interest of public and individual resource.

The other point that takes the researcher's attention is the problem of not commence the business for long period of time. The companies established through public subscription of shares and which their head office is in Addis Ababa have problem associated with lack of commence the business for long period of time after their registration is affected and collect huge amount money from the public. The founders and directors collect unfair interests and other benefits form Share Companies which not commencing business for long period of time giving unsatisfactory reasons. Even if currently massive and diversity sector of share company is formed with huge capital and thousands of investors are subscribing to those incorporating companies, but most companies not start their business for different reasons. Some of the reasons not to commence the business are absence of the period of limitation, undercapitalization and problem with regard to feasibility study.

The additional tribulation in the share companies is inadequate legal protection of public investors. The legal frame work that empowers and governs the regulator and the rules for the regulation is cornerstone of the existence and development of the share companies. However, existing legal frameworks fails to address the issues in relation to the regulation of a share companies. Currently, by and large, the directors and board members in Share Companies are mostly the founders themselves and on the first step of operation or on beginning of commencing the business the shareholder are exploited by managers and board members. The managers, who are expected to represent the interests of the shareholders often, engage in the pursuit of self-interest that hurt the owners. The commercial code and other relevant laws do not require share companies to have independent non-executive directors. Allowing one and the same person to wear three or more hats at the same time and paved the way for a person to exploit and abuse the assets of Share Company. Furthermore, the commercial code fails to state the regulatory body as take the administrative remedies on those breaches of the rules governing Share Company.

The last problem that the writer has discovered in the study is related to regulatory body and institutional framework. Currently, there is no extra government body that insures the predictability and supervisory role of the companies. The share company law only provides regulatory and supervisory powers to the Ministry of Trade as to regulate the formation, ongoing functions and governance of companies. However, the code failed to mandate sufficient powers to the Ministry for regulating public companies from their incorporation to ongoing operations and corporate governance.

The code has no provision for a regulatory body of share companies and there is no place to file a complaint by shareholders for mismanagement of share companies except taking the case to court. The questions of whom and in what way regulate market misconducts is the issues left unsettled. For instance, after the ministry of trade appoint general auditor and identified the some problem and fraud or founder and director of Share Company not conduct general meeting in due time, what type of measure it takes by the authority is not clearly stated in the law. The way of handling the meeting and counting vote, the percentage of shareholder calling to meeting, group conflict created in the meeting and unlawful decision on meeting also the area that not well regulated. Absence of follow up and efficient oversight in behalf of the regulatory body on Share Company is also another problem.

5.2. Recommendations

Having thoroughly analyzed the legal and practical problem surrounding share companies established through public subscription of shares in Ethiopia, the researcher would like to recommend the following points.

As per the analysis, some share companies are suffering from poor formation and commencement of business, where founders, directors and executives of share companies are found pursuing their own interests rather than the interest of shareholders. The reform of the forthcoming Commercial code should be comprehensive to have modern and business friendly rules and principles that encourage international and national competitive companies rather than making fragmented amendments or enact proclamation which repeats what are already incorporated in the draft commercial code to accommodate continuous demands of changes by anticipating the current and future developments. Because, the multiplicity of laws scattered here and there brings confusion.

- ❖ The reform of the forthcoming Commercial code should allocate adequate and sufficient regulatory and supervisory powers to regulator of share companies.
 - ✓ The question of who and in what way regulate market misconducts should set clear manner.
 - ✓ The code should provide for a regulatory body to take appropriate measure on wrongdoers, subject to avoiding conflict of interest, mal administration and for closing the door from those who abuse the resources of share companies.
- ❖ The future law reform shall deal clearly and sufficiently with issue related to foul play founder. There is no legal mechanism to check about their background to open a new project like National Bank of Ethiopia that does such quest as custom in which the founders are asked their past business and ownership history. Currently foul player founders after dissolve the company by their fault, they pass to form another share companies even if the business entity they try to form has failed, adjudged bankrupt and involved in court proceedings relating to dissolving companies they try to establish, etc. By taking the experience of other countries, element like the persons who not able to pay

their debts in many forms and they were prosecuted in connection with bankruptcy should be included under article 89 of draft commercial code.

- ❖ Presently there is practical problem of not commence business for long period of time in Addis Ababa. This doesn't emanate only from the fraudulent act of founders or managers Share Company rather from the existing legal, institutional and policy framework. Thus:
 - ✓ The government should promote and facilitate the creation of formal stock market and the legal rules that are necessary to boost the confidence of the public must be enacted.
 - ✓ Commercial code should put period of limitation on commencement the business after registration or licensing in order protect the business as founder not cheat out the part of the subscribers' money by collaborating with bank managers and in other way.
 - ✓ Regulatory authority should screens offerings (prospectus) not only on the basis of disclosure; but also in terms of economic viability.
- ❖ The legal and regulatory framework is not adequate to protect the public and boost the confidence of the public to invest in shares.
 - ✓ The commercial code should give legal power for regulatory body as take the administrative remedies on those breaches of the rules governing Share Company.
 - ✓ The commercial code should have clear demarcation between requirements for formation and capital increase.
 - ✓ Lastly, the instrument that help and assist regulators in their efforts to evaluate and improve the regulatory and institutional framework for corporate sectors such as, the national principles, up to date codes and directives which can serve as public policy instruments should be taken place by concerning organ.
- One of the aims of establishment of share companies sector association follow up and support directorate under ministry of trade is to facilitate the formation and operation process of Share Company from birth to death and for protection of public interest. Thus, the authority should assign enough inspectors which have capacity and knowledge's in implement the relevant law. They should also provide support, supervision and Carry out the verification of the existence of defects in the formation and operation of a share company.

- ✓ The authority also should assign suffice observers to the general meetings and investigating potential violations and disciplining individuals and firms that violate laws.
- ✓ The authority should assign the observer in general meeting and take corrective measures on the unlawful issues like handling the meeting, counting vote, the percentage of shareholder calling to meeting and decision taken by them.
- ✓ The regulators should facilitate shareholders activism by letting them to be more attentive in appointing only people with perfect integrity and adequate qualifications as directors of companies they invest in.

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Annex I

✓ Questions for Interview (for Ministry of trade)

1. What are the powers and functions of the share companies and sector association follow up and support directorate is concerned?
2. How do you regulate share companies?
3. What is legal and practical problem encountered during formation and commencement of business by share companies?
4. What do you think the cause for not commence the business by share companies for long period of time?
5. Do you inspect and investigate Share Company established through public subscription of shares once the company registered and operate?
6. Does your office have enough legal power and resource capacity to regulate share companies?
7. What measures do you take when the company violates the Code and their own rules?
8. Do aggrieved shareholders often have recourse?
9. Don't you think that the existing laws in Ethiopia are inadequate in the regulation formation and commencement of business?
10. Do you plan to issue directives that help to regulate share companies in the near future?