COMPANY LAW

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PREFACE

Welcome to this comprehensive guide on **Company Law**, specifically designed to support your journey in preparing for the **Certified Public Accountants (CPA) Examination – Paper No. 7**. This book provides a detailed and practical understanding of company law, covering the principles and legal frameworks that govern business entities.

Our aim is to equip CPA candidates with essential knowledge and skills, offering a thorough exploration of the foundational aspects of company law. Whether you're learning about corporate governance, share capital, the duties of directors, or the legal obligations of members, this book is structured to be accessible and easy to understand.

This textbook is organized with a practical approach in mind, focusing on real-world applications and clearly defined concepts. The content is presented with clarity to ensure that complex topics are broken down into manageable, digestible sections. A particular emphasis has been placed on providing illustrative examples that will help you connect theory to practice.

The material draws upon international company law principles and frameworks, with special attention paid to the key legal structures, governance practices, and statutory regulations that govern companies. This will not only support your exam preparation but also provide valuable insights for your professional career as a CPA.

As you progress through the chapters, you will encounter a balance of theory, case studies, and practical examples, all designed to foster a comprehensive understanding of company law. The text is developed with a straightforward approach to ensure that the material is accessible, even as it delves into the more technical aspects of corporate law.

A GOODWILL MESSAGE TO CPA STUDENTS

To all the aspiring CPA students, congratulations on taking a significant step towards a successful and impactful career. Your decision to pursue this qualification marks the beginning of an exciting journey, one that will challenge you to grow both professionally and personally.

Company law is a cornerstone of the business world. As you study this book, I encourage you to dive deep into the content, understand the legal principles, and consider their real-world applications. The knowledge you gain from this subject will not only help you succeed in your exams but will also lay a strong foundation for your future career as a CPA, where you will be trusted to make sound, legally informed decisions in the business world.

The road to becoming a CPA is undoubtedly challenging, but it is also immensely rewarding. Remember, each concept you master brings you one step closer to achieving your professional goals. Stay focused, stay diligent, and trust that your hard work will pay off.

Wishing you the best of luck as you progress in your studies and take on the challenges ahead. Your dedication and commitment to learning will be the keys to your success.

CPA Ronoh Benson Benhard
Synapse Global Institute
2025

DEFINITION OF TERMS

1. **Articles of Association:**
   A document that outlines the rules and regulations governing the internal management of a company. It defines the rights and duties of shareholders, directors, and other stakeholders within the company.
2. **Beneficial Owner:**
   An individual or entity who enjoys the benefits of ownership in a company, such as receiving dividends or voting rights, even though the legal title may be held by another party, such as a nominee shareholder.
3. **Board of Directors:**
   A group of individuals elected by shareholders to oversee the activities and management of a company. The board is responsible for making high-level decisions, including approving budgets, appointing executives, and ensuring the company's compliance with laws.
4. **Capital:**
   The funds raised by a company for its business operations. This can be in the form of **share capital** (equity raised through issuing shares) or **debt capital** (borrowed funds).
5. **Certificate of Incorporation:**
   A legal document issued by a regulatory body (such as the Registrar of Companies) confirming the creation of a company as a separate legal entity. It serves as proof that a company is officially registered and authorized to conduct business.
6. **Company Secretary:**
   A person responsible for ensuring that a company complies with all legal and regulatory requirements, such as filing annual returns and maintaining records of meetings and corporate documents.
7. **Directors:**
   Individuals appointed to manage the affairs of the company. Directors make strategic decisions and ensure the company operates according to its goals, policies, and legal obligations.
8. **Dividends:**
   A portion of a company's profits distributed to its shareholders as a reward for their investment. The amount and frequency of dividends depend on the company's financial performance and the decisions made by the board of directors.
9. **General Meeting:**
   A meeting held by a company to allow shareholders to discuss important matters, such as approving financial statements, electing directors, and making key corporate decisions. It can be **Annual General Meeting (AGM)** or **Extraordinary General Meeting (EGM)**.
10. **Memorandum of Association:**
    A document that outlines the company's objectives, powers, and scope of operations. It is a fundamental document for company formation and outlines the company's legal capacity and activities.
11. **Nominee Shareholder:**
    A person or entity that holds shares on behalf of the actual or **beneficial owner**, often for reasons of privacy or convenience. The nominee shareholder holds legal title to the shares but does not benefit from them.
12. **Preference Shares:**
    A class of shares that provides its holders with priority over ordinary shareholders in receiving dividends and, in the event of liquidation, in the distribution of company assets.
13. **Proxy:**
    A person authorized by a shareholder to attend and vote at a company's meeting on their behalf, especially when the shareholder is unable to attend the meeting in person.

14. **Public Limited Company (PLC):**
    A company whose shares are publicly traded on a stock exchange. A PLC can raise capital from the public through the issuance of shares.
15. **Registrar of Companies:**
    A government official or office responsible for registering and overseeing the incorporation, management, and dissolution of companies. In Kenya, this is done through the **Business Registration Service (BRS)**.
16. **Share Capital:**
    The total value of shares issued by a company in exchange for capital. Share capital is used as a source of funding for the company's operations and is a key indicator of a company's financial structure.
17. **Shareholder:**
    An individual or entity that owns shares in a company and is entitled to receive dividends and vote at general meetings. Shareholders have rights and obligations depending on the class of shares they hold.
18. **Special Resolution:**
    A resolution passed by a company's shareholders with a higher majority (usually two-thirds or three-quarters of the votes) for certain significant decisions, such as changing the company's name or amending the **Articles of Association**.
19. **Statutory Meeting:**
    The first meeting of a company held after its incorporation, where the company's directors present the formation process, share allotment, and other administrative matters to the shareholders.
20. **Transfer of Shares:**
    The process by which a shareholder sells or transfers their shares to another individual or entity, subject to the company's **Articles of Association** and any legal restrictions.
21. **Voluntary Liquidation:**
    The process by which a company dissolves itself by selling off its assets, paying off creditors, and distributing any remaining funds to shareholders, typically following a decision by the shareholders.
22. **Voting Rights:**
    The rights of shareholders to vote on matters affecting the company, such as the election of directors, changes to the **Articles of Association**, or approval of financial statements. Voting rights are usually proportional to the number of shares held.
23. **Winding-Up:**
    The process of closing a company, liquidating its assets, paying off creditors, and distributing any remaining assets to shareholders. Winding-up can be either **voluntary** (by decision of the company's shareholders) or **compulsory**(ordered by a court).

ABBREVIATIONS AND ACRONYMS

1. **AGM - Annual General Meeting**
2. **BRS - Business Registration Service**
3. **CMA - Capital Markets Authority**
4. **CPA - Certified Public Accountant**
5. **CPC - Companies (Public Company) Regulations**
6. **EGM - Extraordinary General Meeting**
7. **ICPSK - Institute of Certified Public Secretaries of Kenya**
8. **KICA - Kenya Information and Communications Act**
9. **KPMG - Klynveld Peat Marwick Goerdeler**
10. **NSE - Nairobi Securities Exchange**
11. **PLC - Public Limited Company**
12. **PSC - People with Significant Control**
13. **SEC - Securities and Exchange Commission**
14. **SHE - Social, Health, and Environmental Regulations**
15. **TDR - Transaction Disclosure Regulation**
16. **UK - United Kingdom**
17. **US - United States**
18. **VAT - Value Added Tax**
19. **WTO - World Trade Organization**
20. **XBRL - Extensible Business Reporting Language**

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CHAPTER 1

NATURE AND CLASSIFICATION OF COMPANIES

1.1: NATURE AND CHARACTERISTICS OF A COMPANY

A **company** is a legal entity formed by individuals or other entities to carry out business activities, enter into contracts, own assets, and take on liabilities. It is distinct from its shareholders and directors, meaning that the company itself can own property, sue or be sued, and exist independently of its owners. The nature of a company as a separate legal entity and its characteristics as a business structure provide it with a unique identity and functionality within the framework of corporate law.

1. Definition of a Company

A **company** is defined as a form of business organization that is incorporated under the laws of a particular jurisdiction and has a separate legal identity from its owners. This means the company can own property, enter into contracts, and be held liable for its debts and obligations, independent of the personal liabilities of its shareholders.

- **Example:** In the UK, a company is a legal entity registered under the **Companies Act 2006**. It is formed when a group of individuals (shareholders) come together, incorporate the business, and adopt a legal structure (e.g., a private limited company or a public company).

2. Key Characteristics of a Company

The characteristics of a company determine its functionality and legal standing. These features are what distinguish a company from other forms of business entities, such as partnerships or sole proprietorships.

1. **Legal Personality:**
    - A company has its own legal identity, separate from its shareholders and directors. This means it can own property, incur debts, and be held liable for its actions. The concept of legal personality allows the company to operate as an independent entity.
    - **Example:** If a company is sued, the legal action is taken against the company itself, not its directors or shareholders, unless personal liability is involved (e.g., fraud).
2. **Limited Liability:**
    - One of the key features of a company is limited liability, where shareholders are only liable for the debts of the company to the extent of their investment in the company's shares. This protects personal assets of shareholders from the company's liabilities.
    - **Example:** If a company goes bankrupt, the shareholders lose their investment in the company but are not personally liable for the company's debts.

3. **Perpetual Succession:**
    - A company has **perpetual succession**, meaning that its existence continues even if its shareholders or directors change. This allows the company to operate continuously regardless of the changes in its ownership or management structure.
    - **Example:** If a shareholder sells their shares or a director resigns, the company still continues its operations, as it is a separate legal entity.
4. **Transferability of Shares:**
    - In most companies, shares are transferable, meaning that shareholders can sell or transfer their shares to other individuals or entities. This provides flexibility and allows for the buying and selling of ownership in the company.
    - **Example:** In a public company, shares are traded on the stock exchange, enabling shareholders to easily buy or sell shares in the company.
5. **Separate Property:**
    - A company owns property in its own name. This means that assets acquired by the company are its property, and they cannot be transferred to the personal assets of the shareholders or directors unless legally authorized.
    - **Example:** A company can purchase land, buildings, and intellectual property in its name, and these assets are legally distinct from the personal assets of its owners.
6. **Capacity to Sue and Be Sued:**
    - A company has the capacity to initiate or defend legal actions in its own name. It can sue individuals or other entities and can also be sued in its own name, which is a key feature that separates a company from its shareholders.
    - **Example:** If a company breaches a contract, it can be sued by the other party in a court of law.
7. **Centralized Management:**
    - A company is managed by its board of directors, who are appointed by the shareholders. The directors have the authority to make decisions on behalf of the company, while the shareholders typically have limited involvement in day-to-day operations.
    - **Example:** In a publicly traded company, the board of directors oversees the company's strategy, while shareholders vote on major decisions, such as mergers or amendments to the company's charter.

3. Company Structure

A company is typically structured to include various components that work together to ensure its operations run smoothly. The two key components of a company's structure are its **shareholders** and **directors**.

1. **Shareholders:**
    - Shareholders are the owners of the company. They invest capital in exchange for shares in the company, which represent a portion of ownership. Shareholders may receive dividends and can vote on key company matters, such as the appointment of directors.
    - **Example:** In a private limited company, the shareholders are often the founders or a small group of investors, while in a public company, shareholders may be individual investors who purchase shares on the stock market.
2. **Directors:**
    - Directors are appointed by the shareholders to manage the company's day-to-day operations and make decisions on its behalf. They have fiduciary duties to act in the best interests of the company and its shareholders.

- **Example:** The CEO of a company is often one of the directors, responsible for overseeing the company's operations and executing the strategies approved by the board.

3. **Company Secretary:**
   - The company secretary is responsible for ensuring that the company complies with all legal and regulatory requirements, including corporate governance practices, financial reporting, and filing of returns. In many jurisdictions, the appointment of a company secretary is mandatory for certain types of companies.
   - **Example:** The company secretary ensures that meetings are properly conducted, that shareholder resolutions are recorded, and that filings are made with the appropriate regulatory bodies.

4. Types of Companies

There are several different types of companies, each with its own legal structure, purposes, and responsibilities. The most common types of companies are:

1. **Private Limited Company (Ltd):**
   - A private limited company has a limited number of shareholders, and its shares are not available for public trading. It offers limited liability to its shareholders, and its management is usually more centralized.
   - **Example:** Many small to medium-sized businesses are set up as private limited companies, as they provide a balance of liability protection and operational control.
2. **Public Limited Company (PLC):**
   - A public limited company is a company whose shares are listed on a stock exchange and can be bought and sold by the general public. These companies are subject to strict regulatory oversight and must comply with a variety of corporate governance standards.
   - **Example:** Large corporations, such as multinational companies, often operate as public limited companies, raising capital by issuing shares on the stock exchange.
3. **Sole Proprietorship:**
   - A sole proprietorship is a business owned and operated by a single individual. While it is not technically a company, it is an important form of business structure where the owner has unlimited liability.
   - **Example:** A freelance consultant or small local shop may operate as a sole proprietorship, where the business and owner are legally inseparable.
4. **Partnership:**
   - A partnership involves two or more individuals or entities sharing ownership and management of a business. In a general partnership, all partners share equal responsibility for the company's liabilities, whereas limited partnerships may have both general and limited partners.
   - **Example:** Professional services firms, such as law firms or accounting firms, often operate as partnerships, where the partners share the profits and liabilities of the business.

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