

ROLE OF PROMOTERS IN COMPANIES' FORMATION IN NIGERIA: CAMA  
2020 IN PERSPECTIVE

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**ABSTRACT**

*Promoter undertake among other things to incorporate the company and ensure that such incorporation complies with the rules of CAMA. At times, it is impossible for the promoter to separate his or her intention from that of the duty of his or her office, most especially where there is pre-incorporation contract(s). The study finds out that often times conflict of interest do occur and without recourse to provisions of Companies and Allied Matters Act, promoter do breach rules as it relates to pre-incorporation contract(s). The paper concluded that, for there not to be conflict of interest as it were, the rules have to be made as regards to means and ways of how pre-incorporation contracts be handled in order to prevent corrupt practices or conflict of interest that do occur at that stage. Doing this will bring sanity and transparency into the process of incorporation in Nigeria.*

**Keywords;**Role, Promoters, Companies, Formation, CAMA 2020

**1.0Introduction**

The importance of a company cannot be overstated because it is one of the most important discoveries of modern times as it generates a huge proportion of the world's wealth and as a result leads to economic growth and development. <sup>1</sup> A company can be defined as a legal entity established with a purpose or objective which is usually to make profit. Over the years, various companies have been established across different spheres and aspects of life. However, companies do not simply establish themselves; there are a series of processes that must be undertaken before a company can be fully formed.

By virtue of section 18 of the Companies and Allied Matters Act 2020, any two or more persons can form an incorporated company whether private or public. During the formation of the company, there is a person called the promoter who aids the formation of the company. The promoter is a person who conceives the idea of the formation of a company and does promotion for the company. It

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<sup>1</sup>CC Wigwe, *Introduction to Company Law and Practice* (2nd end, Princeton & Associates Publishing Co, 2022)

should be noted that the promotion of a company is a process by which the company is being formed and incorporated in accordance to the provisions of CAMA and this is the promoter's main aim.

According to the Oxford English Dictionary<sup>2</sup> a promoter is one who promotes, or takes the requisite steps in the formation of a Company. One who is a party to the preparation or issue of prospectus. The promoter is also an individual who initiates and organizes a business venture, particularly during the process of incorporation.

In corporate law, the promoter holds a vital position in establishing the foundation of a business by undertaking the necessary steps to set it up. This includes activities such as preparing essential documents, obtaining initial funding, and ensuring adherence to legal requirements. The promoter's work is crucial in transforming the business from a mere concept into a legally recognized entity.<sup>3</sup>

Section 85 of CAMA 2020 defines a promoter as

*“Any person who undertakes to take part in forming a Company with reference to a given project and to set it going and who with regard to proposed or newly formed company undertakes a part in raising capital for it, shall prima facie be deemed a promoter of the Company”*

Hence, it is evident from this section that anyone can become a promoter by performing functions that help initiate the formation of a company, such as negotiating preliminary agreements, issuing shares, and arranging for the appointment of directors.<sup>4</sup> Thus in *Gluskstein v Barnes*,<sup>5</sup> the court held that when a person purchased a property and later decided to form a property became a promoter from the time he took steps to form the company

According to the court in *Adeniji v Starcola*<sup>6</sup>, a Promoter is anyone involved in forming a company or raising capital for it, unless acting in a professional capacity. Hence anyone could act as a promoter excluding a person acting in professional capacity in the formation of a company such as a lawyer who makes the memorandum of association and an accountant who values the assets of a business.<sup>7</sup>

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<sup>2</sup> Oxford Dictionary Sixth Edition page 1214

<sup>3</sup> Legal Information Institute Wex Dictionary  
<<https://www.law.cornell.edu/wex/promoter>> accessed 4 December 2024

<sup>4</sup>(n 1)

<sup>5</sup>*Gluskstein v Barnes* (1900) AC 240

<sup>6</sup>*Adeniji v Starcola* (1972) 1 SC 202

<sup>7</sup>*Re Great Wheal Poolgooth Ltd* (1883) 53 LJ CH 42

It is worth noting that the promoter could be an individual or firm or association and what he majorly does is to promote the company.<sup>8</sup> Also, a person can also become a promoter after the company has been incorporated in the sense that such person issues prospectus for the company or procures capital to ensure that the company carry out preliminary agreement.<sup>9</sup>

The promotion of a company is very integral to the establishment of and it takes intentional and painstaking efforts to promote a company. This is why the promoter's job is very essential. Due to the importance of the promoter's job, he has a fiduciary position towards the intended company and its prospective shareholders however, he is not the agent nor the trustee of the company.<sup>10</sup>

The importance of a promoter cannot be overemphasized because a company cannot act on its own volition, it is dependent on a person to bring it into existence. In Nigeria, Promoters are recognized by Companies and Allied Matters Act and by initiating and organizing businesses, mobilizing capital, fostering innovation, and navigating complex regulatory frameworks, they contribute to economic growth, job creation, and entrepreneurship development in a dynamic and challenging environment.

### **1.1 Functions and Duties of Promoters**

A promoter is a person or group who initiates the formation of a business venture. He is any person who applies for the incorporation of a company. The promoter plays a crucial part in forming a company from its inception stage. A promoter initiates the formation of a company and is involved in every stage of a company's development. He plans, organizes and sets in motion all necessary steps to ensure the company comes into being.

In the case of *Twycross v Grant*<sup>11</sup>, Cockburn C. J. explained the term thus, "A promoter, I apprehend is one who undertakes to form a company with reference to a given project and to set it going, and who takes the necessary steps to accomplish that purpose."

Section 85 of the Companies and Allied Matters Act (2020) states that Any person who undertakes to take part in forming a company with reference to a given project and sets it going and who takes the necessary steps to accomplish that purpose or who, with regard to a proposed or newly formed company, undertakes a part in raising capital for it, is deemed a promoter of the company: Provided that a person acting in a professional capacity for persons engaged in

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<sup>8</sup>Kamange, 'Promoters of Companies As Necessary Evil in The Economic Life of A Nation' *MUNFLJ* [2021] 7(1)

<sup>9</sup> *ibid*

<sup>10</sup> *Garba v Sheba. Int. (Nig) Ltd* (2002) 1 NWLR (Pt.748) at 372.

<sup>11</sup> *Twycross v Grant* (1877) 2 CDD (36TCR 812) 469 at 541

procuring the formation of the company shall not be considered to be a promoter<sup>12</sup>

The work of a promoter is enormous, which is why Bowen J declared in the case of *Whaley Bridge Calico Printing Co v Green*<sup>13</sup> that, "the term Promoter is a term not of law, but of business, usefully summing up in a single word a number of business operations familiar to the commercial world by which a company is generally brought into existence."

### 1.2 Functions of a Promoter

The functions of a promoter are as follows;

1. Conceptualization and Feasibility Study: The promoter develops the business model for the company and conducts market and viability studies.
2. Legal Formalities: Promoters take care of all legal formalities, such as document drafting and filing, and require compliance with the respective law at the time of business incorporation with the relevant authorities.
3. Pre-Incorporation Agreements: Before the company is formally formed, the promoters enter into agreements such as tenancy arrangements or equipment purchases to meet preliminary requirements.<sup>14</sup>
4. Appointment of Directors: The promoters search for fitting individuals for important posts, like directors and other top-level positions, to ensure the business runs smoothly after its establishment.
5. Resource Acquisition and Fundraising: Promoters raise initial assets, including office space, machinery, or technologies, to start the business activities. They also negotiate with financial institutions, investors, or shareholders to obtain early funding for setting up the company.<sup>15</sup>

### 1.3 Duties and Obligations of a Promoter

Pre-incorporation arrangements, that is, activities to be carried out before the company is fully incorporated, are entirely in the hands of the promoters<sup>16</sup>. The following are the duties of a promoter;

1. Fiduciary responsibility: The duty of a promoter is a fiduciary duty, i.e., the duty to act with utmost good faith in the best interests of the

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<sup>12</sup>S. 85 Companies and Allied Matters Act (2020) as amended

<sup>13</sup>*Whaley Bridge Calico Printing Co v Green* (1880) 5 QBD 109

<sup>14</sup> Editorial, 'Promoter as per Companies Act: Meaning, Types, Duties & Rights Explained' *The Legal School* <<https://thelegalschool.in/blog/promoter-companies-act>> assessed 4 December 2024

<sup>15</sup> Ibid

<sup>16</sup> Editorials, 'PROMOTERS' *CJ Okoye Lawview* (2024) < <https://cjokoyelawview.com/law-533-company-law-i/topic-12-promoters>> assessed 4 December 2024

company. Lord Cairns in *Erlanger v New Sombrero Phosphates Co. Ltd*<sup>17</sup> explained the position thus: Promoters have in their hands the creation and molding of the company; they have the power of defining law and when and in what shape and under what supervision it shall start into existence and begin to act as a trading corporation." Since pre-incorporation arrangements are performed by the promoter, it is his duty to act with good faith and within the best interests of the company. Hence, his role is seen as a fiduciary one.

2. Duty to Disclose Hidden Profits: The promoters have a key duty, and that is to keep faith with the firm and refrain from wrongdoing. They should not hide or act covertly in such dealings as purchasing property and selling it for a profit without causing it to be considered something that has not been officially recorded. The promoters are not in any way barred from such profits as are earned through above methods; the only condition is that they must be declared. They should provide all relevant stakeholders in the firm with information on their earnings and profits.<sup>18</sup>
3. Duty to Disclose All Private Arrangements: Most transactions are private in order to form and maintain a corporation. However, such transactions must be disclosed by the promoters to the stakeholders. The promoters should disclose private transactions and their profit to the stakeholders.<sup>19</sup>
4. Duty Not to Obtain Secret Profits: Since the duty of the promoter is a fiduciary one, he also has the duty not to obtain secret profits. Whatever profits or rewards obtained by the promoter are required to be disclosed to the stakeholders of the company.

The Companies and Allied Matters Act 2020 provides for the duties and liabilities of a promoter in section 86 as follows;<sup>20</sup>

Section 86 (1) provides that, a promoter stands in a fiduciary relationship to the company and shall observe utmost good faith towards the company in any transaction with it or on its behalf and shall compensate the company for any loss suffered by reason of his failure to do so.

Subsection (2) provides that, a promoter, who acquires any property or information in circumstances in which it was his duty as a fiduciary to acquire it

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<sup>17</sup>*Erlanger v New Sombrero Phosphates Co. Ltd* (1878) 3 A.C. 1218

<sup>18</sup>Editorials, 'Promoters of a Company: Definition, Functions and Duties' *ClearTax* (2024) <<https://cleartax.in/s/promoters-of-a-company>> assessed 4 December 2024

<sup>19</sup> *ibid*

<sup>20</sup> S. 86 Companies and Allied Matters Act (2020) as amended

on behalf of the company, shall account to the company for such property and for any profit which he may have made from the use of such property or information.

Subsection (3) states that, any transaction between a promoter and the company may be rescinded by the company unless, after full disclosure of all material facts known to the promoter, such transaction shall have been entered into or ratified on behalf of the company by,

(a) the company's board of directors independent of the promoter;

(b) all the members of the company; or

(c) the company at a general meeting at which neither the promoter nor the holders of any share in which he is beneficially interested shall vote on the resolution to enter into or ratify that transaction.

Subsection (4) states that, no period of limitation shall apply to any proceeding brought by the company to enforce any of its rights under this section, but in any such proceeding, the Court may relieve a promoter in whole or in part and on such terms as it deems fit from liability if in all the circumstances, including lapse of time, the Court deems it equitable to do so.

## **2.0 Significance of Promoters in Nigerian Business Context**

The role of Promoters in companies cannot be overstated. Through these fiduciary persons, steps are effectively taken towards the successful formation and incorporation of companies. Promoters perform a wide range of duties. They may arrange for the appointment of a director, place shares, negotiate preliminary agreements or even sell their business to a new company which they have incorporated.<sup>21</sup> They not only form a company, but are also its creators to an extent. They find and qualify directors, prepare the prospectus, pay for printing and advertise the undertaking. They instruct solicitors to prepare the Memorandum and Articles of Association and register companies.

They are involved in the strategic planning and conception of the business idea. This is achieved through the identification and execution of business objectives and market opportunities. The principles established by promoters often influence the practices of the newly formed company, employee behaviour, stakeholder relationships, and overall corporate governance.

Promoters are primarily responsible for initiating the process of company formation. Section 85 of the Companies and Allied Matters Act<sup>22</sup> states that a promoter is any person who undertakes to take part in forming a company with

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<sup>21</sup> (n 1)

<sup>22</sup> S. 85 Companies and Allied Matters Act (2020) as amended

reference to a given project and to set it going and who takes the necessary steps to accomplish that purpose, or who, with regard to a proposed or newly formed company, undertakes a part in raising capital. They negotiate with investors, and raise capital that are sufficient for the commencement of company operations.

Although they operate only in the pre-incorporation phase, they are extremely crucial to the well-being of a company. They make up majority of the pre-incorporation staff of a company and prepare and file documents with the Corporate Affairs Commission (CAC). They are also responsible for negotiating pre-incorporation contracts which are subsequently ratified by the newly formed company, after which they become binding.

Promoters are required to conduct their activities in accordance with the law. They ensure that incorporation formalities required by the CAMA 2020 are fulfilled, and uphold transparency especially in offering public securities.

Promoters have a fiduciary duty to the company. This ensures the well-being of the company is prioritised. By virtue of Section 86 of the CAMA 2020, the promoter has a fiduciary duty to the company. He must therefore observe utmost good faith in all transactions entered by prioritising interests of the company. In the case of *Erlanger v New Sombrero Phosphate Co Ltd*<sup>23</sup>, it was held that a promoter is in a fiduciary relation to the company which he promotes or causes to come into existence. The implication of this relation is that a that promoter may choose to sell a property to the company, but he must make full and fair disclosure of his interest and position with respect to that property.

Furthermore, promoters embark on risk management. They often bear financial risks in the course of promoting the company. If the company makes any loss at this stage, the promoters shall compensate the company for any loss suffered by reason of his failure to do so. Given their position, they must act in compliance with the laws established and avoid practices that could harm investors or stakeholders. These risks are however mitigated by holding promoters accountable for their actions.

In the case of *Lagunas Nitrate Co. v Lagunas Nitrate Syndicate*<sup>24</sup>, a syndicate purchased an island for 55,000 pounds sterling which was believed to contain mines of phosphates. E, the head of the syndicate formed a company to buy this Island, and a contract was made between X, a nominee of the syndicate, and the company for its purchase at 110,000 pounds sterling. Since there had been no disclosure by the promoters of the profit they were making; the court held that

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<sup>23</sup> (n 17)

<sup>24</sup> *Lagunas Nitrate Co. v Lagunas Nitrate Syndicate* [1899] 2 Ch 392, 68 LJ Ch 699

company was entitled to rescind the contract and recover the purchase money from E and the other members of the syndicate.

Another significance of promoters is the accountability. The promoter must account for any profit he makes. In *Jubilee Cotton Mills v Lewis*,<sup>25</sup> it was held that a promoter who received a secret reward, which was an allotment of shares before filing a statement in lieu of prospectus, was liable to account for the profit made on the resale of the shares.

It can therefore be established that the role of Promoters are indispensable in the formation and incorporation of a company. They serve as the foundation of a company by from the conception of business ideas, up until the appointment of directors.

### **2.1 Pre-Incorporation Contract**

A company has no existence of any kind until it is registered.<sup>26</sup> However, there will be instances when promoters need to enter into contracts intended to benefit the company. Such contracts entered into when the company is still under formation are intended to be implemented by the company upon incorporation. The position of pre-incorporation contracts may vary depending on the jurisdiction and its operating legal regime. This means that the strict position under the common law has been modified in statutes of different jurisdictions.<sup>27</sup> In Nigeria, the operation of pre-incorporation contracts is governed by the Companies and Allied Matters Act (CAMA) 2020. The meaning, characteristics, importance, and regulation of pre-incorporation contracts under CAMA 2020 will be discussed below.

### **2.2 Definition of Pre-Incorporation Contract**

Pre-incorporation contracts are contracts entered into by any person on behalf of a company before its incorporation.<sup>28</sup> It refers to an agreement entered into specifically by promoters on behalf of a company that has yet to be formed or come into existence.<sup>29</sup> All agreements entered into on behalf of a company that has not been incorporated with the aim that the company will take over and be bound to implement the terms of the contract upon incorporation are classified as pre-incorporation contracts. Pre-incorporation contracts can take on many forms. They include promotion agreements, preliminary agreements, pre-

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<sup>25</sup>*Jubilee Cotton Mills v Lewis* [1924] AC 958

<sup>26</sup>(n 1)

<sup>27</sup>(n 1)

<sup>28</sup>(n 1)

<sup>29</sup> SA Kamdar, 'Pre-Incorporation Contracts and Its Enforceability Under Companies Act' (2020) <<https://lawbhoomi.com/pre-incorporation-contracts-and-its-enforceability-under-companies-act/>> accessed 5 December 2024.

incorporation agreements, formation agreements, shareholders agreements, memorandum of understanding, etc.<sup>30</sup>

### **2.3 Characteristics of Pre-Incorporation Contract**

1. The contracts are said to not be binding on the company until they have been ratified or adopted by the company.
2. They are made prior to the existence and incorporation of the company. In simple terms, the company does not exist as a legal entity when the contract is executed.
3. The contract is executed by its promoter. The promoters act as agents to make agreements on behalf of the proposed company.
4. Such contracts have conditional enforceability. This means that the enforceability of the contract depends on the subsequent incorporation of the company and, in some cases, ratification by the now-incorporated company.
5. Promoters are personally answerable under pre-incorporation contracts.

### **2.4 Importance of Pre-Incorporation Contract**

The importance of a pre-incorporation contract cannot be overemphasized. This contract plays a crucial role in the formation and operation of companies.<sup>31</sup>

1. They facilitate business preparations. Due to the existence of pre-incorporation contracts, promoters can secure essential agreements or assets before the incorporation of the company they act on behalf of.<sup>32</sup> These agreements lay the groundwork for the company's smooth operational takeoff period. An example would be releasing office space, purchasing equipment or engaging certain service providers.

2. They help secure strategic advantages. Early contractual agreements may provide the company with competitive advantages, such as favourable pricing, exclusivity agreements, or priority access to resources that are unavailable post incorporation.<sup>33</sup>

3. They help to reduce operational delays. Since pre-incorporation contracts are entered into before incorporation, the company is able to commence operations

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<sup>30</sup> (n 1)

<sup>31</sup> Wiseman Ubochioma, 'Pre-Incorporation Contract: A Comparative Analysis of the Canadian and Nigerian Corporate Law Regimes' *Corporate Law & Governance Review* [2021] 3(1), 29-42.

<sup>32</sup> Editorials, 'The Significance of a Pre-Incorporation Agreement' *Ogders Law Group* (Lean Lawyer, 2017) <[https://lean-lawyer.com/pre-incorporation-agreement/#:~:text=Pre%2DIncorporation%20Agreements%20\(or%20Pre,agreement%20and%20a%20confidentiality%20agreement.](https://lean-lawyer.com/pre-incorporation-agreement/#:~:text=Pre%2DIncorporation%20Agreements%20(or%20Pre,agreement%20and%20a%20confidentiality%20agreement.)> accessed 5 December 2024.

<sup>33</sup> *Ibid*

immediately upon incorporation.<sup>34</sup> In this way, delays caused by the need to negotiate agreements later are avoided.

## **2.5 Indications for Pre-Incorporation Contracts when necessary**

There may be a need for pre-incorporation agreements in the following circumstances where:

- i. payment of promoter's expenses and remuneration are needed
- ii. joint venture business is to be incorporated, especially between Nigerians and Aliens
- iii. the new company is to take over existing business or purchase property to be owned/ used by the new company
- iv. partnership business is to be converted to an incorporated company
- v. Shareholders' Agreement/Formation Agreement/Memorandum of Understanding is needed to secure the respective interests of the shareholders.
- vi. Promoter/directors' service contracts are to be executed before the company is formed.
- vii. Protection of technical or confidential information used for promotion activities is highly desired.
- viii. Regulatory permits and other steps are preconditions before the company can be incorporated or commence business.

## **2.6 Regulation of Pre-Incorporation Contracts Under CAMA 2020**

Under the Common Law, it was impossible for a company after its incorporation to ratify or adopt a contract entered into before its incorporation by a person purportedly on the company's behalf.<sup>35</sup> The rationale is that since a company has no legal existence before its incorporation, it is incapable of entering into a contract itself or even acting through an agent.<sup>36</sup>

However, this rule under the Common Law has been modified in Nigeria by virtue of the CAMA. By Section 96(1) of the CAMA 2020, upon incorporation, the company can ratify such a contract as if the company were in existence when the contract was entered into and a party to the contract from the outset.<sup>37</sup> This

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<sup>34</sup> *ibid*

<sup>35</sup> (n 31)

<sup>36</sup> *Newborne v Sensolid (Great Britain) Ltd.* (1954) 1 QB 45.

<sup>37</sup> S. 96(1) Companies and Allied Matters Act (2020) as amended

means that the company becomes bound and is entitled to the benefits and obligations contained in the contract. However, by section 96 (2) of the CAMA 2020, before such ratification, if there is no express agreement to the contrary, the person who purported to act in the name of or on behalf of the company shall be personally bound by the contract or other transaction and entitled to any benefit thereof.<sup>38</sup> In *Societe Generale Bank (Nig) Ltd v Societe Generale Favouriser*,<sup>39</sup> After reviewing the common law position, the Supreme Court of Nigeria stated that: "All that has changed in this country for section 96 (1) of the Companies and Allied Matters Act 2020 makes it possible for a pre-incorporation contract to be ratified by a company after its ratification and thereby becoming bound by it and entitled to the benefit thereof."

In *Garba v Sheba International (Nig) Ltd*,<sup>40</sup>the appellant and respondent formed a joint venture company called Jos Cable Satellite Ltd in 1993. The respondent paid \$40,000 and £35,000 to the appellant as part of its own contribution for shares. Not long after the incorporation, the respondent became dissatisfied with the venture and, upon withdrawal, wrote to the first appellant, asking for the repayment of the sum paid with the accruing interest and services rendered. In allowing the appeal, the Court of Appeal held *inter alia* that a promoter has no right against the company for payment of services rendered before the incorporation of the company, and a promise to pay is not enforceable since the consideration is past unless it was ratified or adopted by the company after incorporation.

Therefore, under CAMA 2020, pre-incorporation contracts are enforceable but subject to specific conditions. Just as seen in *Garba v Sheba International (Nig) Ltd*,<sup>41</sup> the company must expressly or impliedly ratify the agreement after incorporation before a pre-incorporation contract can be binding on it. This ratification must also be done within a reasonable period following incorporation to ensure enforceability. These conditions have certain implications under the CAMA 2020 for promoters, companies and third parties.

Promoters are personally liable for any applications incurred before the company ratifies the contract. Hence, they must act prudently and negotiate favourable terms. They also owe a duty of good faith and must ensure that the contracts they enter into are in the best interests of the proposed company.

On the side of the companies, they bear no risks or benefits until the contracts are ratified. This means that they cannot benefit or claim any rights when they have not ratified the contract. Once ratified, they must also bear any liability that may otherwise arise. There are also certain implications for third parties arising

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<sup>38</sup>S. 96 (2) Companies and Allied Matters Act (2020) as amended

<sup>39</sup>*Societe Generale Bank (Nig) Ltd v Societe Generale Favouriser* (1995) 3 NWLR (Pt. 384)

497 CA.

<sup>40</sup>(n 10)

<sup>41</sup>(n 10)

from the provisions of CAMA 2020 in a pre-incorporation contract.<sup>42</sup> These persons are assured of legal recourse against either the promoter or the company. This is because the CAMA ensures that third parties can enforce the contract once it is ratified by the company or hold the promoter personally liable if it is not.<sup>43</sup>

## 2.7 Nigerian Judicial Precedents on Pre-Incorporation Contracts.

*S.G.B. (Nig.) Ltd. v S.G.F. (1995)*:<sup>44</sup>In the High Court, the appellant, in the capacity of plaintiff, filed a lawsuit against the respondent, in the capacity of defendant, seeking damages for conversion and carelessness. In order to prevent the respondent from selling its interests in the appellant firm until a motion on notice filed in the matter was decided, an interim order of injunction was also obtained. After receiving notice of the interim order and motion, the respondent requested a stay of proceedings until the parties agreed to transfer the matter to arbitration. The promoters of the plaintiff company allegedly agreed to the agreement that was cited, which included the arbitration clause. The agreement, which was signed prior to the company's creation but was later approved by the Board of Directors, was designed to control the respondent's overall administration of the business.

The learned trial judge concluded, after taking into account all of the affidavit evidence and the arguments made by the attorneys, that the parties had entered into an implied new contract after incorporation whereby they were bound by the arbitration clause. The court was given the discretion to stay the action when it ordered reference to arbitration, so it did so. The appellant filed an appeal with the Court of Appeal, challenging the decision. Sections 72(1), 624, and 626 of the Companies and Allied Matters Act, 1990<sup>45</sup>, were cited in the ruling of the court

The court held (unanimously allowing the appeal): That under the common law, before the inception of the Companies and Allied Matters Act, 1990. <sup>46</sup>It is trite that a company is not bound by contracts purported to be entered on its behalf by its promoters or other persons before its incorporation, because at the time the transaction was affected, the company did not exist, and it cannot ratify or adopt any such contract after incorporation. The inclusion of the term of the pre-incorporation contract in the Memorandum of Association does not mean that the company is bound to execute the contract. Before such a pre-incorporation

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<sup>42</sup> Third parties are those who enter into the contract with the promoter acting on behalf of the company.

<sup>43</sup> S. 96 (1) & (2) Companies and Allied Matters Act (2020) as amended

<sup>44</sup>*S.G.B. (Nig.) Ltd. v. S.G.F. (1995)* 8 NWLR (Pt. 411) 52 at 67

<sup>45</sup> S. 72(1), 624, and 626 Companies and Allied Matters Act (1990)

<sup>46</sup> Companies and Allied Matters Act (1990)

contract can bind the company, a new contract must have been created post-incorporation.

A company wishing to enjoy a pre-incorporation contract should enter into a fresh agreement upon the same terms as the previous one after its incorporation. Even though a company cannot validly ratify a pre-incorporation contract, in appropriate circumstances, a company can make a new contract, and in some cases, it can be extended to include new contracts inferred from the conduct of the parties. The mere fact that the company might have derived some benefits or has rendered acts referred to as the pre-incorporation contract cannot be evidence of or amount to a new post-incorporation contract in the absence of offer and acceptance.

## **2.8 Significance of Courts' Decisions**

In arriving at a lesson from the above cases, it is paramount to note that agreements made on behalf of a business prior to its official formation are known as pre-incorporation contracts. Unless specifically signed after formation, these contracts are not legally binding on the company under common law or the Companies and Allied Matters Act (CAMA). In order to make pre-incorporation agreements legally binding, promoters should make sure that businesses formally embrace them after they are incorporated. The promoter bears personal responsibility for the terms of the contract until such ratification.

Drawing an inference from the case of *Okafor v. Ezenwa*<sup>47</sup>, it is essential to note that a promoter may be held personally accountable for the terms of a pre-incorporation contract if they act on behalf of a nonexistent principal (the company). They are personally liable for their acts on behalf of a company pre-incorporation. If at all possible, they should include a clause in agreements that states personal liability is not included in order to protect themselves.

According to CAMA Section 72(1),<sup>48</sup> companies can ratify pre-incorporation contracts after formation, but such ratification must be explicit. In *Garuba v. K.I.C. Ltd.*, the absence of evidence of ratification meant the contract did not bind the company.<sup>49</sup>

Hence promoters must be aware that ratification cannot be implied solely from a company's post-incorporation benefits derived from the contract.

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<sup>47</sup> (n 47)

<sup>48</sup> S. 72(1) Company and Allied Matters Act (2020)

<sup>49</sup> (n 48)

### 3.0 Legal Implications of Pre-Incorporation Contracts

Section 85 of the Companies and Allied Matters Act 2020 defines a promoter as “any person who undertakes to take part in forming a company with reference to a given project and set it going and who takes necessary steps to accomplish that purpose, or who, with regard to a proposed or newly formed company, undertakes a part in raising capital for it, is deemed a promoter of the company; provided that a person acting in professional capacity for persons engaging in procuring the formation of the company shall not be deemed to be a promoter.”<sup>50</sup> A promoter has a fiduciary relationship with the company and any necessary expense incurred by the promoter as a result of carrying out task for the company, would be covered by the company unless the expense is of such a nature that it could have been avoided by the promoter. A promoter has the right to be reimbursed for expenses incurred when carrying out task necessary for the incorporation of the company. They also have the ability to initiate pre-incorporation contracts on behalf of the company; however, these contracts are not binding on the company unless ratified upon incorporation by the members of the company after the promoter has disclosed relevant facts to them<sup>51</sup>. Before this, a promoter would be personally liable on the contract as seen in the case of *Garba v Sheba International (Nig) Ltd*<sup>52</sup> and by virtue of section 72(2) of CAMA 2020. Pre-incorporation contracts can simply be defined as any contract or transaction, entered into by a company or any person representing the company before its corporation, which may be ratified upon formation of the company thereby binding the company and allowing it to benefit from the contract as though the company had been in existence as a the date of the contract<sup>53</sup>. There are various types of pre-incorporation contracts such as:

1. Joint venture agreement
2. Memorandum of understanding
3. Shareholders agreement
4. Promoter’s/ Directors Service Contracts
5. Payment of promoters Expenses
6. Takeover agreement
7. Appointment of first Directors by Subscribers

#### 3.1 Ratification

Ratification is the adoption or confirmation of pre-incorporation contracts after the incorporation of a company. This process is provided for by virtue of section 96 of CAMA. Ratification is essential because it is what binds the company to fulfil the obligations of the pre-incorporation contracts. This is because, one of the

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<sup>50</sup> S. 85 Company and Allied Matters Act (2020) as amended

<sup>51</sup> S. 86(3) Company and Allied Matters Act (2020) as amended

<sup>52</sup>(n 10)

<sup>53</sup> S. 96(1) Company and Allied Matters Act (2020) as amended

essential features under the law of contract is offer and acceptance; for this to occur, the parties must be in existence as at the time of the contract as a person cannot enter into a contract with a non-existing party. Therefore, without the ratification process, the company is a stranger to the contract and cannot be held liable as they did not exist at the time the contract was formed as a contract cannot be formed with a non-existing party. This principle was applied in the case of *Kelner v Baxter*<sup>54</sup> where the promoters were held personally liable as the company was not in existence at the time of the contract making the company strangers to the contract. Erie J. stated in the case that “there must be two parties to a contract and the rights and obligations which it creates cannot be transferred by one of them to a third person who was not in a condition to be bound by it at the time it was made.”<sup>55</sup> Similar decisions have been made in other cases such as the case of *Caligara v Giovanni Satori & Co. Ltd*<sup>56</sup>.

The rule in *Kelner’s* case is consistent with the law of contract, agency and privity of contract and therefore made ratification impossible, allowing for companies to renege on their pre-incorporation contract obligation and making promoters personally liable for debts incurred from contracts they entered into while acting as an agent for the company.<sup>57</sup> This rule did not allow for ratification and a company was not allowed to enforce pre-incorporation contracts in an instance where the other party reneged on its own end of the contract as they were strangers to the contract and therefore not entitled to the benefits therein. As a result of this, there was a need to have a law to handle and enforce ratification of pre-incorporation contracts. Therefore, section 96(1) of CAMA 2020 provides that, “any contract or any other transaction purporting to be entered into by the company or by any person on its formation may be ratified by the company after its formation and thereupon the company shall become bound by and entitled to the benefit thereof as if it had been in existence on the date of such contract or other transaction and had been a party thereto.”<sup>58</sup> This section allows for the company to enforce pre-incorporation contracts and binds them to both the liabilities and benefits brought about by the contract by virtue of ratification.

The contract must first be ratified by the company before it becomes binding on it. However, CAMA 2020 does not specify the process or method through which pre-incorporation contracts can be ratified. Ratification may be written, oral or implied. This allows for companies to ratify pre-incorporation contracts through various means. The common way through which members of a company decide on matters is through a resolution, be it a simple or special resolution. Therefore, a pre-incorporation contract may be ratified through a resolution. A company can be said to have implied ratification even when no resolution has been passed

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<sup>54</sup>*Kelner v Baxter* (1878) 8 CH. D. 388

<sup>55</sup>*ibid*

<sup>56</sup>*Caligara v Giovanni Satori & Co. Ltd* (1961) 1 All NLR 534

<sup>57</sup> (n 59)

<sup>58</sup> S. 96 (1) Company and Allied Matters Act (2020) as amended

through its conduct such as performing the duties or obligations placed on it by the pre-incorporation contract. By virtue of section 86 (3) of CAMA 2020 there are certain persons that have the authority to ratify a pre-incorporation contract.<sup>59</sup> It may be ratified by;

- a. By the company's board of directors independent of the promoter<sup>60</sup>.
- b. By all the members of the company<sup>61</sup>.
- c. By the company at a general meeting at which neither the promoter nor the holders of any shares which he is beneficially interested shall vote on the resolution to enter into or ratify that transaction<sup>62</sup>.

### 3.2 Fiduciary Duties of Promoters

Promoters stand in a fiduciary duty to the company and are expected to act with utmost good faith towards the company<sup>63</sup>. As a result of these, promoters have duties and liabilities towards to company that they are expected to fulfil. Some of these include;

1. Duty to compensate the company where the company has suffered a loss as a result of his failure to act in utmost good faith towards the company<sup>64</sup>.
2. Duty to account for the profits or information he may have received as a result of the use of any property or information he acquired on behalf of the company in the fulfillment of his duties<sup>65</sup>.
3. Duty to return secret profits.

### 3.3 Legal Challenges and Risks Faced by Promoters in Nigeria

A promoter is a person or organization that proactively forms and establishes a business, carrying out the essential tasks prior to the business's incorporation. In the *Whaley Bridge Calico Printing Co v. Green*<sup>66</sup>, Bowen J. Said that, "The term promoter is a business term, not a legal term, that effectively condenses into a single word a variety of business operations that are common in the commercial world and that are typically used to establish a company."

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<sup>59</sup> S. 86 (3) Company and Allied Matters Act (2020) as amended

<sup>60</sup> S. 86 (3) (a) Company and Allied Matters Act (2020) as amended

<sup>61</sup> S. 86 (3) (b) Company and Allied Matters Act (2020) as amended

<sup>62</sup> S. 86 (3) (c) Company and Allied Matters Act (2020) as amended

<sup>63</sup> S. 86 (1) Company and Allied Matters Act (2020) as amended

<sup>64</sup> *ibid*

<sup>65</sup> S. 86 (2) Company and Allied Matters Act (2020) as amended

<sup>66</sup> *Whaley Bridge Calico Printing Co v. Green* (1880) 5 QBD 109

In *Erlanger vs. New Sombero Phosphate Co*<sup>67</sup>, Lord Cairns accurately described the promoter's stance: "A company's promoters unquestionably stand in a fiduciary position." They are in charge of the company's conception and development. They have the authority to specify how, when, what form, and under whose direction it will be established and start operating as a trading corporation.

The Companies and Allied Matters Act (CAMA) 2020 and other pertinent regulations present promoters in Nigeria with a number of legal risks and obstacles, despite their crucial role in company formation. The main hazards and obstacles are listed below:

1. **Personal Liability for Pre-Incorporation Contracts:** Before the business is formally registered, promoters frequently sign contracts (such as renting out real estate or employing services) on its behalf. However, contracts established prior to a company's formation cannot legally bind it. Promoters are held personally accountable for any pre-incorporation agreements under Section 96<sup>68</sup>, unless the firm specifically accepts the agreements after incorporation. The promoter is solely liable financially if the company declines to accept such agreements. For instance; Before the business is incorporated, a promoter negotiates an office space contract. The promoter might be held personally responsible for the leasing payments if the business decides not to accept the agreement after incorporation<sup>69</sup>.
2. **Breach of Fiduciary Duties:** Promoters have fiduciary obligations to act in the best interests of the newly established firm and in good faith, according to Section 86(1)<sup>70</sup>. Should a promoter partake in actions like: Keeping important facts hidden, Generating covert gains.....etc. They risk being sued for breach of duty by the business or its shareholders if they engage in self-dealing. For example, where a promoter sells the corporation personal property at a premium price without revealing their stake in the deal. Once this is found, shareholders may file a lawsuit for violation of fiduciary responsibility.
3. **Disclosure of Personal Interests:** During or after the business's formation, promoters are required to declare any interest they may have in transactions involving the company<sup>71</sup>. Lawsuits involving the revocation of the transaction or the payment of damages may result from failure to disclose

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<sup>67</sup> (n 17)

<sup>68</sup> Company and Allied Matters Act (2020) as amended

<sup>69</sup> BS Shoroye, 'Company promoters and pre-incorporation contracts: Delimiting the boundaries of liability under Section 96 of the Nigerian companies act 20', *JLL* [2021] 7 (5), 179 - 186

<sup>70</sup> S. 86 (1) Company and Allied Matters Act (2020) as amended

<sup>71</sup> S. 86 (2) Company and Allied Matters Act (2020) as amended

personal interests, such as profiting monetarily from a property sold to the business.

4. **Misrepresentation and Fraud:** Promoters are in charge of giving truthful information when the business is being formed, particularly when requesting investors or raising money. The promoter may be subject to criminal prosecution, damage lawsuits, and reputational damage if they make misleading claims, omit information, or fraudulently misrepresent the company's potential. In the instance whereby a promoter inflates the company's financial prospects in order to attract extra money. Investors may sue the promoter for fraud or misrepresentation if the business does not live up to their expectations.
5. **Unauthorized Acts:** When establishing the business, promoters may do actions that are outside of their purview. They risk personal accountability or legal repercussions if they commit to things they shouldn't or get into illegal arrangements. Additionally, these actions can put the company's future operations at risk. For example, where a promoter makes promises on behalf of the unincorporated business without the required authority, such actions could lead to legal issues or financial obligations.
6. **Regulatory and Compliance Issues:** Promoters must conform to tax regulations and other legal and regulatory obligations, such as registering with the Corporate Affairs Commission (CAC). Fines, delays in the legal process, or denial of incorporation may follow noncompliance with these conditions.
7. **Third-Party Liability:** If promoters break promises made during the pre-incorporation stage, third parties may hold them liable. If creditors or contractors are unable to collect losses or debts from the business after incorporation, they may file a direct lawsuit against the promoters. In a situation where a supplier delivers goods based on a pre-incorporation order made by the promoter. If the company doesn't honour the payment, the supplier may sue the promoter personally.
8. **Tax and Financial Risks:** During the company's inception, promoters might have miscalculated the company's tax or financial requirements. The promoter may feel under pressure to personally pay for unforeseen obligations resulting from mistakes in tax preparation or financial estimates.
9. **Reputational Risk:** The success or failure of the business in its early phases has a direct impact on a promoter's reputation. Claims of wrongdoing, carelessness, or deception may damage the promoter's reputation both personally and professionally, making it challenging for them to take on new projects.

10. Litigation Risk: Investors may sue promoters for poor management or for not living up to expectations. Co-promoters, as a result of disagreements about duties, profit-sharing, or tasks. Project delays and monetary losses can result from protracted litigation.

### **3.4 Remedies Available**

Nigerian promoters encounter a number of difficulties when forming a company, including as the possibility of fraud or deception, regulatory compliance, and personal culpability for pre-incorporation arrangements. As stated in Section 86 of the Companies and Allied Matters Act (CAMA) 2020, they must make sure that all pre-incorporation contracts contain provisions stating that the firm will adopt them upon incorporation in order to lessen these. For example, the contracting parties may be barred from holding the promoters personally accountable if they intentionally entered into the contract with them knowing the company's pre-incorporation status. In a similar vein, judges have discretion in allocating culpability if the promoters behaved honestly and in the unincorporated company's best interests. Promoters should give truthful information and consult with legal and financial professionals to mitigate the dangers of fraud or misrepresentation.

A seamless incorporation and liability limitation are ensured by following corporate governance principles and regulatory procedures, such as filing with the Corporate Affairs Commission (CAC) and abiding by tax regulations enforced by the Federal Inland Revenue Service (FIRS). The use of insurance, such as Directors' and Officers' (D&O) insurance, and careful financial preparation further shield promoters from unanticipated dangers. To avoid disagreements among co-promoters, promoters should also formally define duties and obligations in a Promoter Agreement. By using novation agreements to transfer responsibilities to the firm after incorporation and incorporating indemnification clauses into agreements, they can reduce their personal culpability. Additionally, promoters must prioritize the company's interests and maintain transparency in order to avoid breaches of fiduciary duties and fully disclose personal interests in deals.

While professional advice guarantees adherence to financial and legal commitments, alternative dispute resolution (ADR) techniques like mediation or arbitration can effectively settle disputes. Promoters can successfully handle the risks and difficulties involved in business formation, lowering potential liabilities and guaranteeing a successful incorporation procedure, by upholding transparency, behaving in good faith, and following these remedies<sup>72</sup>.

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<sup>72</sup> Editorial, 'Company Law: Promoters, their positions, powers, duties and liabilities' *An MHRD project* <[https://epgp.inflibnet.ac.in/epgpdata/uploads/epgp\\_content/law/04\\_corporate\\_1](https://epgp.inflibnet.ac.in/epgpdata/uploads/epgp_content/law/04_corporate_1)

### 3.5 Comparative Analysis of Pre-Incorporation and Promoter Parts in Nigeria and Other Purviews

#### 3.5.1 Nigerian System For Pre-Incorporation Contracts And Promoters

The direction of pre-incorporation contracts and the parts of promoters is basic in corporate law, as these early exercises shape a company's establishment. Nigeria's lawful system, represented by the Companies and Allied Matters Act 2020 (CAMA), offers a premise for directing these parts. Under section 72 of CAMA, pre-incorporation contracts may be approved by the company post-incorporation. Until confirmation, promoters are actually obligated, as asserted in *Kelner v. Baxter (1866)*<sup>73</sup>. Promoters owe guardian obligations to the company beneath Nigerian law, a guideline underscored in *Kelner v. Baxter*<sup>74</sup>. This incorporates an obligation to reveal fabric actualities and dodge clashes of intrigued.

#### 3.5.2 Trans-Jurisdictional Comparison

##### 1. United Kingdom:

The UK Companies Act 2006 receives a comparable approach, where pre-incorporation contracts tie as it were promoters until approved by the company. Be that as it may, the UK offers clearer cures for breach of guardian obligations by promoters, as seen in *Re Leeds & Hanley Theater of Assortments Ltd*<sup>75</sup>. Besides, the concept of "novation" permits more prominent adaptability in exchanging promoter commitments.

##### 2. United States:

Within the U.S., the Revised Model Business Corporation Act grants pre-incorporation contracts in case unequivocally authorized by state statutes. Promoters owe guardian and statutory obligations, and courts in cases like *Fletcher v. A.J. Businesses, Inc*<sup>76</sup> emphasize revelation and decency. Not at all like Nigeria, the U.S. forces more exacting punishments for breaches, advancing corporate straightforwardness.

##### 3. India:

The **Companies Act 2013** controls promoters more comprehensively, requiring divulgences of promoter assentions and liabilities. Indian courts, as seen in

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accessed 6 December 2024

<sup>73</sup> *ibid*

<sup>74</sup> *ibid*

<sup>75</sup> *Re Leeds & Hanley Theater of Assortments Ltd (1902)* 2 Ch 809

<sup>76</sup> *Fletcher v. A.J. Businesses, Inc (1968)* Civ. 24251

*Erlanger v. New Sombrero Phosphates Co. Ltd*<sup>77</sup> as received in Indian statute, stretch strict responsibility for promoters in guaranteeing no undue advantage is taken amid pre-incorporation exercises.

### **3.6 Conclusion and Recommendation**

In conclusion, the promoters are primarily important to the founding, development and growth of businesses in Nigeria. Their duties are way beyond basic formation or startups; their duties or obligations also entail capital raising, smart and quick decision-making, and compliance to laws such as the Companies and Allied Matters Act (CAMA). However, there are a lot of dangers and issues because of the complexity of pre-incorporation contracts and the legal implications of their conduct. The Nigerian government should consider re-evaluating and updating CAMA to give more understandable and comprehensive guidelines on the roles and responsibilities of these promoters, specifically with regard to pre-incorporation contracts, and to brush about awareness among potential promoters about their legal obligations and risks in order to improve the business environment or community in Nigeria and increase the effectiveness of promoters.

Companies and Allied Matter Acts must be amended from time to time so as to include any area(s) that is not included in the previous amendment, most especially, areas that deals with duties and function of promoter. Doing this will address unnecessary conflict of interest that do occur while promoter is performing the duty of his/her office.

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<sup>77</sup> (n 17)