

# CPA

**Certified Public Accountant Examination**

**Stage: Intermediate 1.3**

**Subject Title: Company Law**

**Examination Format Revision Pack**



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# **I1.3 COMPANY LAW**

## **Intermediate Level I1.3 Company Law**

### **Institute of Certified Public Accountants of Rwanda**

#### **Examination Format Revision Questions & Solutions**

##### **Section A:**

You are required to answer **three** questions from this section, (Questions 1, 2 and **either** 3 or 4).

However, if you provide answers to **both** Question 3 and 4, you must draw a clearly distinguishable line through the answer not to be marked. Otherwise, only the first answer to hand for each of these two questions will be marked.

##### **Section B:**

You are required to answer **one** question from this section. However, if you provide answers to each question in this section, you must draw a clearly distinguishable line through the answer not to be marked. Otherwise, only the first answer to hand for each of these two questions will be marked.

##### **TIME ALLOWED:**

3 hours, plus 10 minutes to read the paper.

##### **INSTRUCTIONS:**

During the reading time you may write notes on the examination paper but you may not commence writing in your answer book.

Marks for each question are shown. The pass mark required is 50% in total over the whole paper.

##### **Start your answer to each question on a new page.**

You are reminded to pay particular attention to your communication skills and care must be taken regarding the format and literacy of the solutions.

The marking system will take into account the content of your answers and the extent to which answers are supported with relevant legislation, case law or examples where appropriate.

List on the cover of each answer booklet, in the space provided, the number of each question(s) attempted.

## **SECTION A**

### ***QUESTION 1***

- (a) List the 5 types of commercial companies within Rwanda
- (b) Describe “Private Limited Companies”
- (c) What should be included within the “Memorandum of Association”?
- (d) Describe “Constituent Ordinary Meetings”

**(25 Marks)**

### ***QUESTION 2***

- (a) Write an explanatory paragraph on “Shares”
- (b) Write a paragraph on each of the following:-
  - A “Public Company”
  - Memorandum of Association
  - Issue of Shares
  - Debentures

**(25 Marks)**

### ***QUESTION 3***

What are the main differences between a share-holder and a debenture holder?

**(20 Marks)**

### ***QUESTION 4***

Describe “Financial Statement” and “Annual Report”

**(20 Marks)**

## **SECTION B**

### ***QUESTION 5***

What are the circumstances an Inspector should be appointed, who appoints the Inspector and what are the duties of Inspector?

**(30 Marks)**

### ***QUESTION 6***

Discuss Liquidators Appointment and Duties

**(30 Marks)**

**END OF PAPER**

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# ***SUGGESTED SOLUTIONS***

## ***SOLUTION 1***

**(a)**

Rwanda law recognizes five types of commercial companies:

- 1) General partnership;
- 2) Limited partnership;
- 3) Partnership limited by shares;
- 4) Private limited company;
- 5) Public limited company.

These commercial companies are commonly separated into two groups: partnership or companies where the liability is not limited and a company or partnership whose liability is limited by shares. The former includes the companies of the first, second and fourth types, in which, in principle, the interests of the participants are neither assignable nor heritable. The rationale for the interest of the participants not being assignable nor heritable is that the personality of the participants is of paramount importance. The organisation with shares, on the other hand, which comprise, the third and fifth types, fulfil the same functions as the public limited company.

The company being the result of a contract comprising several persons, a couple i.e., husband and wife may by themselves or in association with other persons be partners in the same company and take part together or not in the management of the company. However a husband and wife may not be partners in the same partnership or private company in which they shall be jointly and separately liable without limit for the debts of the organisation.

**(b)**

### **Private company**

The law does not define what a private company is. However, article 6 enumerates the characteristics of a private company.

A private company shall have following characteristics:

1. Restricting the right to transfer its shares and debentures;
2. Limiting the number of its shareholders to one hundred, persons employed or formerly employed by the company not included;
3. Prohibiting any invitation to the public to subscribe for any shares or debentures of the company.

Consequently, in case of a private company, some restrictions should be imposed on members' right to transfer their shares, the maximum number of members should be one

hundred (100), and there should be no invitation to the public to subscribe for its shares or debentures. These restrictions must be clearly provided in the articles of association of the company. It is important to note here that, where two or more persons hold one or more shares jointly, they shall be treated as one single member.

The object of restricting the members' right to transfer their shares is probably to enable the company to keep the number within the prescribed limit of one hundred.

Generally, the restrictions on members' right to transfer their shares take the following two common forms:

- a) **Right of pre-emption:** this right means existing members' preferential right to purchase the shares of other members as and when sold. The articles of association of the company may contain a clause that when a member wishes to sell some or all his shares, he shall first offer to the other existing members at a price to be determined in the manner set out in the articles. It may, however be noted that under the pre-emption clause, a member is not bound to sell his shares to other members unless they (other members) or some of them agree to buy all the shares which he offers for sale.
- b) **Directors' powers to refuse to register transfer of shares:** the articles of association of the company may contain a clause giving powers to the directors to refuse to register the transfer of shares. However, this power must be exercised by the directors in good faith and for the benefit of the company.

(c)

### **The memorandum of association**

The first important document to be filed with the registrar General is the memorandum of association, briefly called "memorandum". As a matter of fact, the preparation of this document is the first step in the formation of company. It contains the fundamental conditions on which the company is to be incorporated.

In fact, this document is of great importance in relation to the affairs of proposed company. It may be called a "charter" or the "constitution" of the company as *it regulates the relationship of the company with the outside world.*

The memorandum of association lays down the powers and objects of a company, and the scope of the operations of the company beyond which its actions cannot go.

Additionally, the memorandum of association is the document which describes the scope of company activities. It must be signed by the required number of persons which are necessary for the formation of company, and who come forward to form it.



According to article 15, the memorandum of association must contain:

1. the name of the company
2. the head office of the company;
3. particulars of any business occupation;

Moreover the precedent article adds that a memorandum of association for a company limited by guarantee shall indicate that liability is limited. A memorandum of association for a company limited by guarantee shall also state that every member shall undertake to contribute to the assets of the company in the event of its being wound up. For the case of a company with share capital, the memorandum of association shall state the following:

1. the amount of share capital;
2. the number of shares making the share capital unless where the company is an unlimited company;
3. the full name and the number of shares of every shareholder.

**(d)**

#### **CONSTITUENT ORDINARY MEETING**

The final stage in the formation process is the holding of a constituent ordinary meeting.

Where there are articles of association all the promoters/founding members shall participate in signing the articles of association either in person or through their authorized agents. A constituent ordinary meeting grouping all the promoters or their nominees must be held. This meeting shall appoint not less than 3 and not more than 12 persons to be directors or ratify their appointment by the articles of association; it must also appoint one or more auditors whose function is to watch over the accounts in the interest of shareholders. The acceptance of their office by the directors and auditors marks the birth of the company. But it is still important for the legal validity of that birth that the company shall be entered in the ORG. Finally the principal documents must be published in the official gazette.

As regards a public limited company that offers its shares to the public, the business of the constituent ordinary meeting comprises:

1. Verification of the substantive requirements for the formation of the company;
2. Adoption of the final text of the articles of association, which it shall amend by special resolution of all the members being the subscribers and promoters;
3. Approval of the evaluation of shares in kind and the benefits given to the promoters which it shall be amended by a majority of the votes attached to the shares subscribed by the subscribers present excluding promoters;
4. Appointment of the organs of administration (directors) and control (auditors) and fix their remuneration;

5. A vote on the final formation of the company requiring a majority of the votes attached to the shares subscribed by the subscribers present excluding promoters.

The acceptance of their office by the directors and auditors marks the birth of the company. As it is the case with other commercial companies there must be registered in the ORG;

The memorandum and articles of association and minutes of the constituent ordinary meeting and a list of shareholders must be filed with the registrar of the CIF within whose jurisdiction the company proposes to establish its registered office. Finally the principal documents must be published in the Official Gazette.

The promoters are, notwithstanding any clause to the contrary jointly and severally liable towards third parties:

1. For the eventual difference between the share capital and the minimum capital as well as that part of the share capital which shall not be validly subscribed, they shall be deemed to be the subscribers for that part;
2. The effective payment for shares in accordance with the law;
3. Liable to pay damages which is the consequence of either the nullity of the company or inaccuracy in the wording of the articles of association or overvaluation of any shares in kind or insufficiency of capital;

## ***SOLUTION 2***

**(a)**

### **Shares**

In order to contribute to the formation of a share capital of the company, every shareholder must commit to make a share and is debtor of the share that he vowed to give. He owes to the company a guarantee similar to that of the seller in case of eviction. The share differs from a sale in that in return to the good of which properly transferred, a shareholder doesn't receive a price, but titles representing the share capital of the company which is the beneficiary of shares. Besides, to the difference of the sale that is a commutative contract, the share has an uncertain character because even though a shareholder knows the value of that he brings, he ignores the value of the share that he receives in return.

The company contract implies therefore putting together shares by each of the contracting parties. The share indeed, is the good which is transferred to the company by the shareholder in trade of which he is entitled some shares. In other words, it is good that the shareholder commits to put at the disposal of a company for a common exploitation. The notion of shares is instrumental to the constitution of a company, especially when it comes to corporations, where without share the whole idea of a company lacks substance. Article 31 of company law states Share capital shall mean all the shares received whether paid or not. The same article refers to other types of shares other than in cash without précising whether they are physical or know how as it was the case in the previous law.

A contract involving shares implies two kinds of successive contract:

- the commitment to issue a share: the subscription
- the actual performance of the obligation which entails the dispossession of share to the profit of company: fulfillment.

In principle, the proportion of share capital which must be availed at the time of the subscription and that of the date of the calls for the outstanding is determined by articles of association. In return for his contribution, the shareholder gets some shares. Article 77 of company law provides, any shares created or issued after the commencement of this Law may either be of par value or of no par value.

### *1. The share par value*

The share is said to be paid in cash or par value when the contribution is nothing other than money; which is the most usual and simplest of the shares.

### *2. The share no par value*

It consists in a contribution of a physical or incorporeal good. In other words, it is any share apart from those paid in money or in industry. The rule is that any goods that are legally in trade may be object of a share.

## **(b)**

### **Public Company**

Article 7 of the law relating to commercial companies says that any company is considered public, except if it is recorded as private company.

Besides the lack of a clear definition of public company, this terminology is likely to create much confusion strictly speaking. Traditionally the term public company as opposed to private company refers to the status of persons who own it. Thus, it would be called private if owned by individuals while it would be recognized as public if was owned by the State.

In case of a public company, there are no restrictions on the transfer of shares, on maximum number of members and on the invitation to the general public to subscribe for its shares.

### **The memorandum of association**

The first important document to be filed with the registrar General is the memorandum of association, briefly called “memorandum”. As a matter of fact, the preparation of this document is the first step in the formation of company. It contains the fundamental conditions on which the company is to be incorporated.

In fact, this document is of great importance in relation to the affairs of proposed company. It may be called a “charter” or the “constitution” of the company as *it regulates the relationship*

*of the company with the outside world.*

The memorandum of association lays down the powers and objects of a company, and the scope of the operations of the company beyond which its actions cannot go.

Additionally, the memorandum of association is the document which describes the scope of company activities. It must be signed by the required number of persons which are necessary for the formation of company, and who come forward to form it.

According to article 15, the memorandum of association must contain:

1. the name of the company
2. the head office of the company;
3. particulars of any business occupation;

A memorandum of association for a company limited by guarantee shall indicate that liability is limited. A memorandum of association for a company limited by guarantee shall also state that every member shall undertake to contribute to the assets of the company in the event of its being wound up. For the case of a company with share capital, the memorandum of association shall state the following:

1. the amount of share capital;
2. the number of shares making the share capital unless where the company is an unlimited company;
3. the full name and the number of shares of every shareholder.

## **Issue of Shares**

A share is issued when the name of the holder is entered on the share register (Art. 99).

It is the assembly of the shareholders that generally decides to issue some Shares. However article 86 of the law confers to the Board of directors the right to issue some Shares in these terms: "The Board of Directors of the Company may issue shares at any time, to any person, and in any number it thinks fit under the provisions of this Law and the company's articles of association.

Where the shares confer rights, other than those set out in the preceding articles or impose any obligation on the holder, the Board of Directors shall approve the terms of issue which set out the rights and obligations attached to the shares subject to an ordinary resolution of shareholders. The terms of issuing shares approved by the Board of Directors shall be consistent with the articles of association of the company, and to the extent that they are not so

consistent, shall be invalid and of no effect and deemed to form part of its constitution and may be amended in accordance with this Law.

The wording of article 87 clearly subjects the company to conform to within fifteen (15) days of the issue of shares, to the following conditions:

1. give notice to the Registrar General certifying:
  - a) the number of shares issued;
  - b) the amount of the consideration for which the shares have been issued, its value as determined by the Board of Directors; the amount of the company's share capital following the issue of the shares;
2. deliver to the Registrar General a copy of any terms of issue approved.

According to article 91, a company may, where its articles of association so provides, issue fractions of shares which shall have corresponding fractional liabilities, limitations, preferences, privileges, qualifications, restrictions, rights and other attributes as those which relate to the whole share of the same class or series of shares.

Notwithstanding the provisions of the articles of association, where a company issues shares which rank equally with, or in priority to existing shares as to voting or distribution rights, those shares shall be offered to the holders of existing shares in a manner which would, maintain the relative voting and distribution rights of those shareholders. An offer shall remain open for acceptance for a period, which shall not be more than fifteen (15) days (art. 92).

## **Debentures**

The debenture may be defined as a certificate of loan issued by the company, which creates or acknowledges an indebtedness of the company. The companies have to borrow the money for their extension or developments. The loan requirements may not be met by single money-lender. The loan may have to be split into several units. The most usual form of borrowing by a company in this way is by the issue of debentures. By the issue of debentures, the public is invited to lend money for a fixed period at a declared rate of interest to be paid on such money *e.g;* a company requires one million Rwandan francs. It may be divided into one hundred thousand units of RFW 1,000 each. A money-lender may purchase as many units as he please. The company will then issue certificate for the units purchased by a lender. A debenture is, therefore, a document issued by a company as an evidence of a debt due from the company, with or without a charge on the assets of the company. The Rwandan companies' law defines the debenture under article 2. 17° as 'a written acknowledgement of indebtedness issued by a company in respect of a loan made to it or to any other person or money deposited with the company or any other person or the existing indebtedness of the company or any other person whether constituting a charge on any of the assets of the company or not'.

### ***SOLUTION 3***

#### **Comparison between a share-holder and a debenture-holder**

N°	Share-holder	Debenture-holder
1	He is the member and joint owner of the company	He is simply a creditor of the company who has given some loan to the company
2	He has a right to vote at the meetings of the company	He has no right to vote at any meeting of the company.
3	He is entitled to get dividends only out of profits. The rate of dividends is not fixed. It varies from year to year depending upon the profits of the company.	He is entitled to fixed rate of interest whether there are profits or not.
4	He has full right to control company's affairs. In fact, the ultimate destiny of the company is in the hands of shareholders	He has no right to interfere with the business of the company. However, in case of company's default in paying their debts, he may enforce their security.
5	He cannot be paid back so long as the company is a going concern	He can be paid back unless he is perpetual debenture-holder.
6	He does not have any charge over the assets of the company	He generally has a charge over the assets of the company
7	In case of winding up of the company, he is paid after satisfying all other claims	In case of winding up, a secured debenture-holder is paid prior to the share-holder.

## ***SOLUTION 4***

### **Financial statement and annual report**

#### **Financial Statement**

The Board of Directors of every company shall ensure that, within three (3) months following the end of a financial statement the audit is made and signed by at least one representative of the company. Such an audit shall be submitted to the Registrar General (article 253).

The financial statements of a company shall comply with international standards. Members of the Board of directors shall provide such information and explanations as are necessary for auditing process to be conducted (art. 254).

Concerning registration of the financial statement, all companies, with the exception of the small private companies, must insure that in the thirty (30) days that follow the date required for the signature of the financial states of the company and the financial states of the whole group, the copies of these financial states accompanied by a copy of the audit report on these financial states are deposited to the office of the Registrar General for registration.

With regard to the content of the financial statement, article 266 states that the consolidated financial statements shall, in the case of companies which are required to comply with the International Accounting Standards, contain:

1. a consolidated balance sheet for the group as at that balance sheet date;
2. a consolidated income statement;

#### **Annual report**

The Board of Directors of every company shall, within six (6) months after the company's financial statement date, prepare an annual report on the affairs of the company during the accounting period (article 267 of the law) ending on that date.

The Board of Directors of a company shall cause a copy of the annual report to be sent to every shareholder of the company not less than fifteen (15) days before the date fixed for holding the annual meeting of the shareholders.



Concerning the format, every annual report for a company shall be in writing and be dated and shall:

1. describe, so far as the Board believes is material for the shareholders to have an appreciation of the state of the company's affairs and is not harmful to the business of the company or of any of its subsidiaries, especially any change during the accounting period in:
  - a) the nature of the business of the company or any of its subsidiaries;
  - b) the classes of business in which the company has an interest, whether as a shareholder of another company or otherwise;
2. include financial statements for the accounting period and any group financial statements for the accounting period completed and signed in accordance with this Law;
3. where an auditor's report is required in relation to the financial statements or group financial statements, included in the report, include that auditor's report;
4. state particulars of entries in the interests register made during the accounting period;
5. state the amount which represents the total of the remuneration and benefits received by or due and receivable from the company and any related corporation by:
  - a) executive directors of a company engaged in the full time employment of the company and its related corporations, including all bonuses and commissions received by them as employees;
  - b) separate statement, the non-executive directors of the company;
6. state the total amount of donations made by the company and other subsidiaries during the accounting period;
7. state the names of the persons holding office as directors of the company as at the end of the accounting period and the names of any persons who ceased to hold office as directors of the company during the accounting period;
8. state the amounts payable by the company to the person or firm holding office as auditor of the company as audit fees and, as a separate item, fees payable by the company for other services provided by that person or firm;
9. be signed on behalf of the Board of Directors by two (2) directors of the company or, where the company has only one director, by that director;
10. disclose related party transactions and full information about the nature and extent of the conflict of interest;
11. any other details that are necessary for the report to be well understood.

A Company whose subsidiary companies is located outside Rwanda shall also comply with the provisions of this article within eight (8) weeks after the dates contained therein.

## SECTION B SOLUTIONS

### ***SOLUTION 5***

#### **Investigation and appointment of an inspector**

Where the Minister in charge of companies is satisfied that:

1. for the protection of the public, the shareholders or creditors of a company, it is desirable that the affairs of a company should be investigated;
2. it is in the public interest that the affairs of a company should be investigated;
3. in the case of a foreign company, the appropriate authority of another country had requested that an investigation be made under this article in respect of the company; he/she shall issue the instructions to the Registrar General as to investigating into the business of a local company or of a foreign company having its branch in Rwanda (article 274).

***An inspector of the business of a company shall be appointed by the Registrar General and have the power to investigate the business of a company.***

The appointed inspector should be a qualified, skilled and experienced professional manager. This expert shall prepare a report according to the format required by the Registrar General (art. 175).

However, the article 283 allows a company, with the exception of a declared company can, to appoint an inspector by ordinary resolution, to investigate its business.

In the same vein, article 294 provides that a foreign company with subsidiary companies in Rwanda may appoint inspectors for such subsidiary companies and the Registrar General shall be notified thereof.

Expenses and operating cost of the inspection of a declared company are paid by the office of the Registrar General.

An inspection cannot be ordered by the Minister, in this case the article 277 The Registrar General may :

1. in the case of a company having a share capital, on the application of:
  - a) one shareholder or a group of shareholders holding at least one-tenth (1/10) of the issued shares;
  - b) debenture holders holding not less than one-fifth (1/5) in nominal value of the issued debentures;
2. in the case of a company limited by guarantee, on the application of not less than one-

- fifth (1/5) in number of the persons on the share register;
3. where he/she considers that the appointment of an inspector is necessary to safeguard the interests of shareholders or debenture shareholders or is necessary in the public interest, require an inspector to investigate the affairs of a company or such aspects of the affairs of a company as are specified in the instrument of appointment and in the case of a debenture agency deed, the conduct of the debenture holders' representative, and to make a report on his/her investigation in such form and manner as the Registrar General may direct.

### ***Publication or submission of copies of the reports***

The Registrar General may, where he/she is of the opinion that it is necessary in the public interest to do so, ask the organ that requested for the investigation to cause the report to be published (art. 280).

A copy of the inspector's report shall be forwarded to the Registrar General, at the registered office of the company and to those who requested for it. (art. 279).

On the conclusion of the investigation, the inspector shall report his/her opinion in such manner and to such persons as the company's general assembly indicated (art. 284).

### ***Procedure and powers of the inspector***

Every person concerned shall, if required to do so by the inspector, produce to the latter every book in his/her custody, control or possession and give to the inspector all assistance in connection with the investigation which he/she is reasonably able to give for the investigation to be smoothly carried out (art. 287).

An inspector may by written notice require any person concerned to appear for examination on oath in relation to the business of a subsidiary and the notice may require the production of every book in the custody, control or possession of the person concerned (art.288).

Where an inspector requires the production of a book in the custody, control or possession of a person concerned, he/she:

1. may take possession of those books;
2. may retain those books for such time as he/she considers necessary for the purpose of the accomplishment of his/her mission;
3. shall, where those books are in his/her possession, permit the company to have access, at all reasonable times to the book.

## ***SOLUTION 6***

### **Liquidators: Appointment and duties**

Note that a liquidator may be chosen from among the shareholders or third parties. In addition, the liquidator may be a corporate body.

However, where the shareholders are unable to appoint a liquidator within three months of the dissolution of the company he may be designated by a court decision at the request of any interested party. In default, the managers or directors of the company at the time or moment of dissolution shall, in relation to the third parties, assume any obligation and liabilities of the liquidators.

Note that in case of nullity e.g. where the Articles of Association does not take the form of a notarial act it is only the court that is competent to appoint liquidators.

The liquidators are clothed with the widest powers possible to realize the act of liquidation as well as to represent the company i.e., legal proceedings (liquidation proceedings). However, the liquidator cannot without the consent of the shareholders (under condition for amending the articles of association) or authorization of the court, as the case may be, sell real estate, borrow or give secured debts, transfer the assets of the company by private contract, assign or transfer the assets of the company to another company or stay the execution of a judgment.

Note that the effect of liquidation is to create concurrent rights between creditors of the company. As such, no cancellation of sale of movable property can be allowed against the interest of creditors.

The liquidator is empowered to pay creditors. Where the sums allotted to creditors have not been paid out, they shall be deposited in an account opened at the National Bank of Rwanda.

After paying off the creditors the balance available will then be shared among shareholders and any property that cannot be shared conveniently shall be handed over to the shareholders jointly.

In the course of performing his duties the liquidator is required to use the care and skill required of a paid agent. The liquidator is liable to the company as well as third parties for the actionable wrong resulting from any errors made by him in the exercise of his duties.

Each year the liquidator is required to submit to the general meeting a financial statement, profit and loss account as well as a written report in which he shall give an account of the

liquidation exercise during the year together with reasons hampering the closure of liquidation. Nonetheless, the general meeting of shareholders or the court may at any time request the liquidator to submit a written report containing the state of the liquidation exercise and the reason hindering the closure of liquidation.

**END OF SOLUTIONS**