

The background is a light blue gradient with several realistic water droplets of various sizes scattered across it. The droplets have highlights and shadows, giving them a three-dimensional appearance.

# FORMATION OF COMPANY :ROLE OF PROMOTERS

# Stages in Formation of a Company

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Promotion Stage

Incorporation Stage

Capital Raising Stage

Commencement of Business Stage

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# Who is a Promoter

- Promoter 'a person who takes the necessary steps to form a company'
- Promoter – not defined in the Companies Act



# PROMOTERS

“A PROMOTER IS A PERSON WHO ASSEMBLES THE MEN, THE MONEY AND THE MATERIALS INTO A GOING CONCERN”

-: GUTHMANN AND DOUGHALL



# PROMOTERS

- IDENTIFIED AS PROMOTER IN COMPANY'S PROSPECTUS OR AUDIT REPORT.
- PROMOTERS HAS CONTROLLING POWER OF A COMPANY. BECAUSE PROMOTERS APPOINT MAJORITY DIRECTORS OF COMPANY.
- PROMOTER GIVES ADVICE TO THE COMPANY .BOARD OF DIRECTORS ARE ACCUSTOMED TO ACT ON PROMOTER'S ADVICE.



## **Role of Promoters**

1. Promoters are the ones who come up with the idea of starting a business
2. They decide the objects of the business, amount of capital needed, scale of business operation etc
3. They prepare the various documents needed for incorporation of a company like Memorandum and Articles of Association
4. Approach investors for collecting capital for the company

## LEGAL POSITION OF PROMOTER

- Neither an Agent
- Nor a Trustee
- Fiduciary relation to the company



# Legal position of a promoter

- (i) **Quasi Trustee**
- (ii) **Fiduciary relationship (based upon trust & confidence)**

The relation is summed up as :

- (i) Not to make any secret profit
- (ii) Not to make any profit at the expense of the company
- (iii) To make full disclosure of interest
- (iv) To give benefit of negotiations to the company
- (v) Not to make unfair use of position

## *Legal Position of a Promoter*

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- Promoter stands in a fiduciary position towards the company.
- In other words, he is not allowed to make **secret profits**.

**Case:** *Gluckstein v. Barnes*

# GLUCKSTEIN V BARNES (1900)

## FACTS

- GLUCKSTEIN AND 3 OTHERS ALLEGEDLY PURCHASED PROPERTY **FOR £120,000** AND THEN PROMOTED A COMPANY TO WHICH THEY ON-SOLD THE PROPERTY FOR **£180,000**. Original profit margin is **60000**.
- THESE PERSONS THEN MADE UP THE FIRST DIRECTORS OF THE NEWLY FORMED COMPANY. THEY DISCLOSED **THE £40,000 PROFIT**, BUT NOT **ANOTHER £20,000 PROFIT AS THEY ORIGINALLY PURCHASED THE LAND FOR £120,000 AND NOT for £140,000**.

## ISSUES

HAD THE PROMOTERS BREACHED THEIR FIDUCIARY DUTIES TO THE COMPANY?

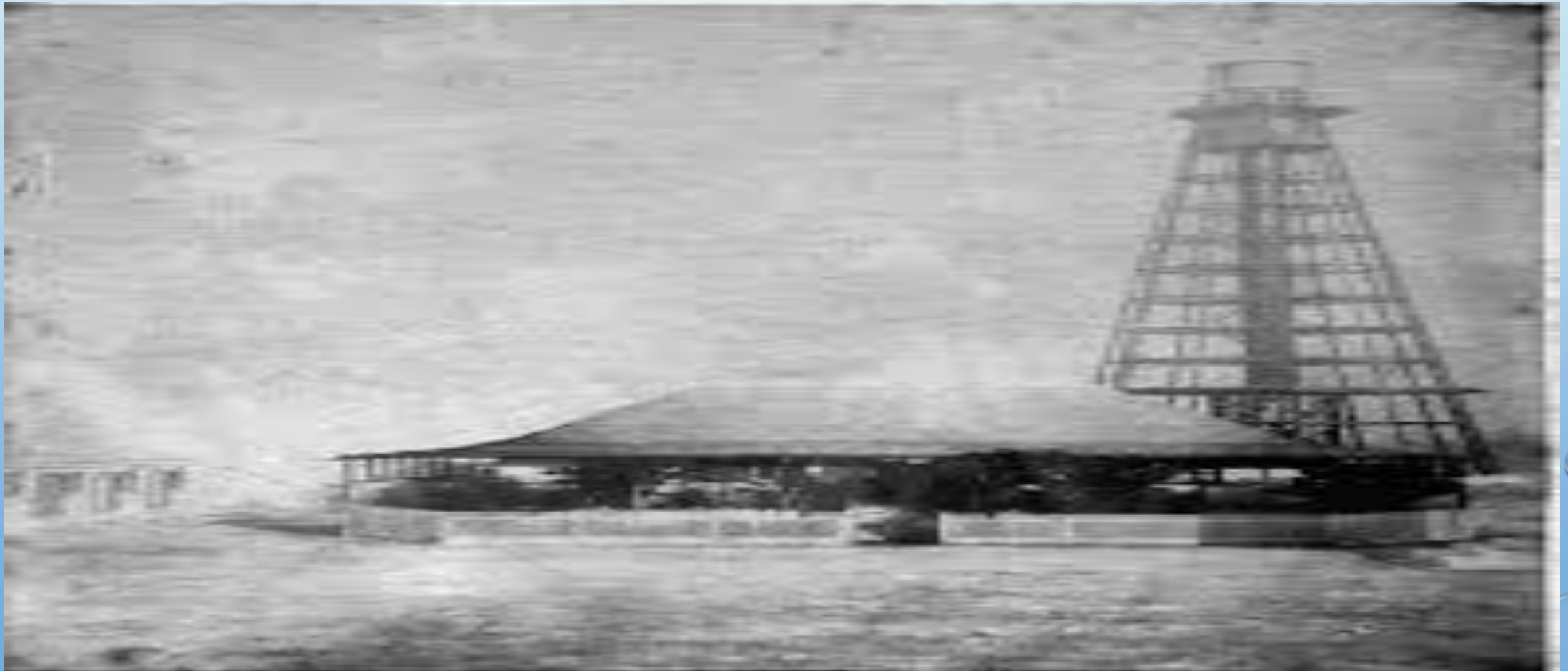
## HELD

**THE HOUSE** OF LORDS HELD THAT THE SYNDICATE HAD BREACHED THEIR FIDUCIARY DUTIES AND WERE LIABLE TO ACCOUNT TO THE COMPANY FOR THE SECRET PROFIT THAT THEY HAD MADE AS THE COMPANY LACKED INDEPENDENT DIRECTORS.

- It was held profit of £20,000 is a secret profit and promoters are bound to pay it to the company because the disclosure was not sufficient.

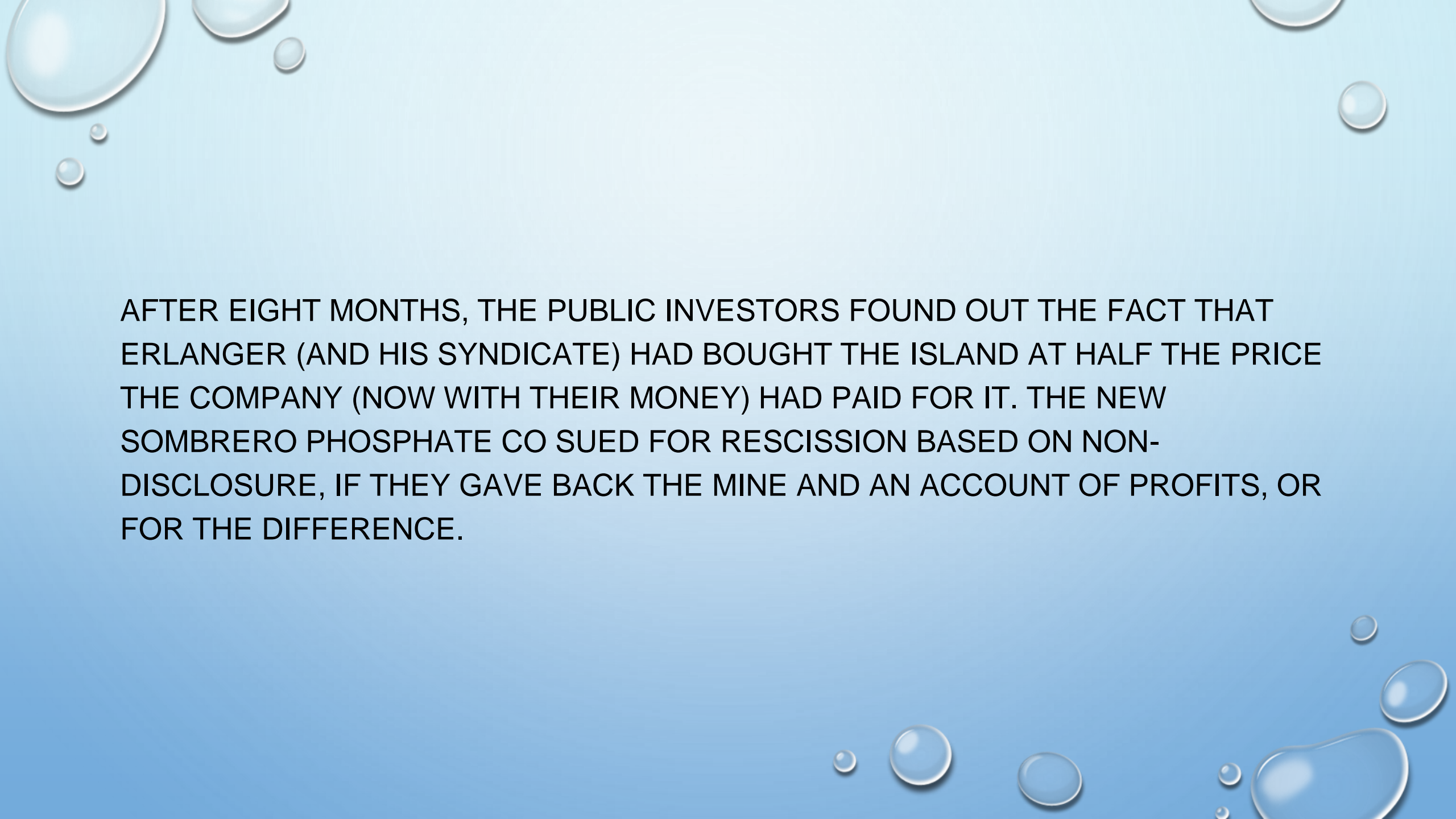


# ERLANGER V NEW SOMBRERO PHOSPHATE CO (1878)



# FACT

FRÉDÉRIC ÉMILE D'ERLANGER WAS A PARISIAN BANKER. HE BOUGHT THE LEASE OF THE ANGUILLA ISLAND OF SOMBRERO FOR PHOSPHATE MINING FOR £55,000. HE THEN SET UP THE NEW SOMBRERO PHOSPHATE CO. EIGHT DAYS AFTER INCORPORATION, HE SOLD THE ISLAND TO THE COMPANY FOR £110,000 THROUGH A NOMINEE. ONE OF THE DIRECTORS WAS THE LORD MAYOR OF LONDON, WHO HIMSELF WAS INDEPENDENT OF THE SYNDICATE THAT FORMED THE COMPANY. TWO OTHER DIRECTORS WERE ABROAD, AND THE OTHERS WERE MERE PUPPET DIRECTORS OF ERLANGER. THE BOARD, WHICH WAS EFFECTIVELY ERLANGER, RATIFIED THE SALE OF THE LEASE. ERLANGER, THROUGH PROMOTION AND ADVERTISING, GOT MANY MEMBERS OF THE PUBLIC TO INVEST IN THE COMPANY.



AFTER EIGHT MONTHS, THE PUBLIC INVESTORS FOUND OUT THE FACT THAT ERLANGER (AND HIS SYNDICATE) HAD BOUGHT THE ISLAND AT HALF THE PRICE THE COMPANY (NOW WITH THEIR MONEY) HAD PAID FOR IT. THE NEW SOMBRERO PHOSPHATE CO SUED FOR RESCISSION BASED ON NON-DISCLOSURE, IF THEY GAVE BACK THE MINE AND AN ACCOUNT OF PROFITS, OR FOR THE DIFFERENCE.

# Held

THE HOUSE OF LORDS UNANIMOUSLY HELD THAT PROMOTERS OF A COMPANY STAND IN A **FIDUCIARY RELATIONSHIP TO INVESTORS**, MEANING THEY HAVE A DUTY OF DISCLOSURE. FURTHER, THEY HELD, BY MAJORITY (LORD CAIRNS LC DISSENTING), THAT THE CONTRACT COULD BE RESCINDED, AND THAT RESCISSION WAS NOT BARRED BY LACHES.

## **The Remedies Available to the co. against the Promoter**

- Where the promoter fails full disclosure co. can:
  1. Rescission
  2. Recovery of secret profits
  3. Damages for breach of fiduciary duty





Profit is allowed, but not secret profit

- Disclosure of profit
    - Independent directors
    - Other shareholders
    - Prospectus
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