# Study Session 4

# Legal Personality & Partnership

## Introduction

Dear Learners, this session focuses on the personalities of business organizations. And the subsequent entitlements and duties of partnerships and business organizations. Moreover, the formation, registration and dissolution of business organizations will be discussed in view of the context of some of the partner countries.

## Study Session Outline

i. Legal personality
ii. Partnership
iii. Dissolution of a partnership
iv. Company Formation in Ethiopia, Somalia, South Sudan
v. Company Registration in Ethiopia

### Duration

This Study Session requires a 2 hours of formal study time.

## Learning Outcomes of Study Session 4

After attending this session students will be able to:

- *Explain different types of persons*
- *Describe the formation of different forms of businesses*
- *Identify the advantages and disadvantages of various forms of businesses.*
- *Distinguish the differences between the various forms of business*

## Unit 4: Law of persons as related to business

### 4.1 Law of Persons

The category of law that deals with persons is one category of private law that deals with the determination of legal subjectivity, and the subsequent rights and obligations, and questions of legal status (*Borg Barthet, 1971*). Thus, the goal of this unit is to familiarize students with the notion of legal personality, how it begins and ends, what it comprises, and the rights and obligations associated with it;

### Legal personality

Legal personality is an artificial personality given to non-living entities in order to perform juridical acts. Legal personality renders nonliving entities such as business organizations, companies, etc rights and duties under the law. For example, a corporation is a legal entity that exists independently of its members and administrators. It possesses a distinct legal/artificial personality. It is a legal entity with rights and duties. In *Salomon v. Salomon & Co Ltd (1897)* the House of Lords mentioned "...the company is a distinct legal entity from the subscribers to the memorandum." The case's ratio is that when a corporation is constituted, it becomes a legal entity (*Dahal, 2018*).

### 4.2 Types of persons: Natural and artificial person

**Natural person** refers to a biological human being recognized by law as a person because of his or her unique characters.

**A juristic person, or artificial person**, is a concept of law. It is created by the la and enjoys rights and duties given under the law. For example, companies, corporations or incorporated associations.

4.3 **Sole proprietorships**

In a sole proprietorship, a single owner is responsible for all of the company's financial and administrative decisions. Many people like to form Sole proprietorships among small business owners because of the ease with which they may be founded and broken up without the engagement of the government. Taken together, the benefits of sole proprietorship are rather persuasive. However, different business entity forms exist for a purpose; a single proprietorship may not be appropriate for every person or firm (*Mengistu, Molla. & Woldeyes, 2006*).

**Corporation**

A corporation is a business entity that is organized by group of people that has legal and financial rights and liabilities isolated from the individuals who established the corporation. (Mengistu,et al,2006)  Legally speaking, a corporation has many of the same rights and obligations as an individual in many situations. It has the authority to purchase, sell, and own real estate, and at the same time to enter into leases and contracts and to bring legal actions against others. It is a tax-paying entity. If a corporation violates the law, it may be prosecuted and penalized (naturally with fines). The basic advantage of a corporation is that it can continue to exist indeterminately, more than the lifetime of any member or inventor, and that it provides its owners with slight protection from individual liability.

## 4.4 **Partnership**

The other type of business organization is based on partnership agreement. Partnership is a kind of organization that involves the ownership and management of a business by two or more people or entities. Profits and losses are shared among partners. Prior to forming a business partnership, you should educate yourself on the many types of partnerships available and how they work (*Tesfay, 2008*).

### 4.4.1 Dissolution of a partnership

Dissolution of partnership is the stage where a partnership no more exists due to various reasons. For example, courts may dissolve a partnership upon application if it is convinced that:

A. A partner has become insane.

B. A partner has manifest incapacity to perform his/her functions as a partner

C. A party is perpetually liable for willful breach of the agreement under the partnership.

D. Any partner has acted in an unfavorable manner toward the firm, and his ongoing involvement with the firm is likely to destruct the firm’s good will.

E. The firm's operations can only be sustained at a loss.

F. Conditions exist that make it right and reasonable to wind up the business

## 4.5 Limited partnership/Limited companies

General partners and limited partners are both required in a limited partnership. General partners are personally liable for all debts and have complete managerial control over the business. Limited partners have little to no managerial engagement, but their liability is limited to the amount invested in the limited partnership.

**Limited Liability** -Liability is limited means, that creditors may not require any payment from your personal properties. The only claim that creditors can raise is against the assists of the company and nothing else. For example, if you are a partner and in a certain company and the company is sued to pay its debts, the creditors can't claim payment from your personal asset if the company doesn't have sufficient means to pay the debt.

**Limited company-** As discussed above, the liabilities of the members to a limited company, is only limited to the level of their contribution and share under the company. The formation of limited companies in general requires the following elements.

I. *Memorandum of association* –Stipulates mainly the organization's legal and institutional frame work

II. *Article of Association* –governs the relationship of each member among themselves and against the company

*III. Statement of nominal capital*

*IV. Declaration of Compliance*

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| ***Dear instructor and mentors***, would you demonstrate the above elements taking the context of the legal frame work of the country to which the student is a national? |

**Advantages and disadvantages of limited company (*Tesfay, 2008*).**

**Advantages**

1. Members of a registered company have restricted responsibility; Members to a limited company are personally not liable for the company's insolvency

2. ***Permanent succession***: Because a registered corporation is founded by law, its existence is determined by the law's intent. It is capable of perpetuity. This is beneficial where the business is flourishing. Additionally, it promotes enduring investment.

3. ***capacity to enter in to a contract and ownership of property***: After registration a company owns legal capability to own property and is capable of concluding contractual relationships as defined in the object's clause. Consequently, the corporation has the ability to invest in order to upsurge productivity.

4. ***Take legal action:*** A registered business has the ability to assert its rights through judicial action and may also be sued for breach of contract. That means it is not obligatory for members to directly engage in litigation representing the company and, in general, cannot be directly sued for the corporation's wrong doings unless they were delegated to act on behalf of the company.

5. *Transferability of shares*: In most cases any member's shares or other interests in the business are moveable property that may be transferred.

**Disadvantages** *(Tesfay, 2008)*

1. *Formalities*: The legal formalities and procedures that may exist in limited companies, such as formation, meetings, accounting, and winding up may be considered as obstacles for smooth operation of the business.
2. *Publicity*: Businesses are subjected to excessive publicity, for example, when their financial records are made public. Public firms are required to file annual financial statements. General public meetings are held. Dissolution is made in public.
3. *Expenses:* in terms of cost companies incur relatively higher costs for example while Forming, maintaining, and winding up a registered company.

4. *Ultra vires doctrine*: A corporation's authority is limited to the transactions specified in the objects and those that are implied from the object. As a result of this, other transactions are void as a result of being ultra vires.

5. *Corporation tax*: Corporations pay a comparatively higher rate of tax. This results in a decrease in the amount of profits accessible to members in the form of dividends

6. Management participation: the day to day activities of the business are handled by members who are not directors.

**Legal and Institutional framework regulating Business in Ethiopia**

Ethiopian Investment Body (EIA) is a government agency charged with the responsibility of promoting private investment and foreign direct investment (FDI) (Wijnands *et al.,* 2007). The Agency's whole operation is administered and controlled by an Investment Board chaired by the Minister of Industry. By considering procedural and legislative measures, the government has taken steps to improve investment in the country, in the aim of increasing foreign direct investment.

**Company Formation in Ethiopia**

The most common and preferred type of business partnership in Ethiopia is PLC (private limited Company). A PLC must have a minimum capital of Ethiopian birr 15,000 and at least two shareholders and one manager. The PLC is not allowed to function in financial sectors such as banking and Insurance.

A foreign firm wishing to invest in Ethiopia through a branch office must produce the necessary documentation to the Ethiopian Investment Commission. Foreign enterprises willing to establish liaison offices should apply to the Ministry of Trade and Industry (Wijnands *et al.,* 2007).

### Company Registration in Ethiopia – Licensing

An investor, domestic or foreigner, may obtain an investment permit form the Ethiopian Investment Agency in order to launch a new business or to expand or upgrade an existing one. According to the Investment Proclamation of Ethiopia, foreign investors and domestic investors looking for benefits must get an investment permit before investing in Ethiopia.

## End of Chapter Quizzes

1. What is the meaning of "Limited liability"?
2. What are the common features of Limited liability companies (LLCs)?
3. What are the similarities between Limited partnerships (LPs) and general partnerships?
4. To what extent are members in a limited company liable for creditors?
5. In what circumstances would a company prefer outsourcing of services?
6. what does legal personality means?