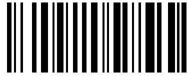

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Shareholder Voting Right under The Companies and Allied Matters Act, 1990: The Philosophy and Legal Overview

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Abstract: The right to vote at the general is one of the most important rights that belongs to shareholders. This right empowers shareholders to subject the board of directors to account for their stewardship and where the board is found wanting, the shareholders may exercise their voting right to remove and replace the board. In Nigeria, the CAMA 1990 recognised the right of shareholder to vote at the general meeting. However, very few literatures could be found in this area. This study seeks to examine shareholder voting right from both philosophical and legal perspective in order to lay a solid foundation for shareholder voting right in Nigeria. The study will emphasise on the theory of shareholder voting and its relevance to corporate governance by unveiling the objective of shareholder vote as well as the relevant theory to shareholder vote. The study employed doctrinal legal research methodology in obtaining the relevant data. The findings show that this study is one of the very few studies that tries to identify theories that are relevant to shareholder vote in Nigeria. The study maintains that there are various theories that will support the exercise of shareholder voting in Nigeria including the option theory, agency theory, transaction cost theory, contract theory among others. In the same vein, regulators in Nigeria also need to double their effort and ensure that shareholder voting right is duly exercised. Additionally, considering the significance attached to shareholder vote, this study suggest that the CAMA 1990 should make provisions that will ensure shareholder vote is duly exercise since there is both philosophical and legal basis for the exercise of shareholder vote.

Keywords: Board of Directors, Shareholder, Voting Right, General Meeting

Introduction

The CAMA 1990 under section 63 distributes corporate powers between the board of directors and shareholders at the general meeting. However, the board is comprised of both executive and non-executive directors, many of whom have other full-time employment, and therefore spend little time about issues affecting the company (Paul and Randall, 2014). The directors sometimes hardly employ the control rights that legislation provides them and therefore mostly delegate their responsibility to other officers of the company to exercise it on their behalf. Often in pressing time will the board exercise their ultimate power to approve, or override, corporate managers' key decisions about the prospect of the company (Paul & Randall, 2014). Shareholders, therefore, need to check the activities of the board which is exercise through their votes at the general meeting (Stewart & Randall, 1998).

On the other hand, there is inconsistency regarding what an articulate theory would suggest and what is real. While it is often appealing to take a view on this, this study will not automatically assume that the current arrangements are the most efficient. However, this study will at times argue that long-standing corporate arrangements be given the benefit of the doubt. To provide a full discussion regarding the philosophy underpinning shareholder voting, there is the need to at least first appreciate "Why are shareholders empowered to vote in a company?" Understanding the above question will certainly give room for good understanding of the philosophy and legal recognition of shareholder voting right.

In most of the public companies, shareholders are empowered to vote on number of issues given to them by the company's legislation. In this regard, section 81 of the CAMA 1990 provides: "Every member shall notwithstanding any provision in the articles, have a right to attend any general meeting of the company and to speak and vote on any resolution before the meeting." Furthermore, the CAMA 1990 provides: "Notwithstanding anything to the contrary in the terms or the articles, include the right to attend any general meeting of the company and vote at such a meeting," (section 114(b) CAMA 1990). At the meeting, shareholders can elect the members of the board of directors (section 247, 248, 249 CAMA 1999) approve proposed amendments to the company's article (section 47, 48 CAMA 1990) and remove directors (section 262 CAMA 1999) if the need arises. Additionally, shareholder vote equally empowers shareholder to approve annual report and accounts presented by the board (Stewart J. S. & Randall, S.T., 1998) among other powers. However, there is

need to examine this right from the philosophical perspective which little has been done in Nigeria.

Materials and Methods

This study mainly adopts doctrinal legal research methodology which is generally carried out in the library (Yaqin, 2007; Watkins & Burton, 2013). The materials in this study were obtained mainly from the library database and other archives of the Universiti Utara Malaysia and Bauchi State University, Gadau. These materials were mostly statutory provisions and decided cases that are relevant to the study. In addition, scholarly articles from the USA and other jurisdictions were equally referred to in this study. This is based on the fact that the relevant theories in this study largely originates from the USA.

Results and Discussion

The Philosophical basis for Shareholder Vote

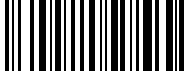
This sub-heading begins with the question, “Why are shareholders empowered to vote?” There are various justifications given over time. One of the earliest justifications given for the shareholder voting right was proposed by Easterbrook and Fischel (1991), where they argued that shareholders play the role of “gap fillers” in a company. Reason being, the shareholders hold the residual interest in the company. They have “the appropriate incentives … to make discretionary decisions…The shareholders receive most of the marginal gains and incur most of the marginal costs. They therefore have the right incentives to exercise the discretion” (Easterbrook and Fischel, 1991, at 68) through voting at general meeting. In other word, the right to exercise discretion through the right to vote, follows from the shareholder’s claim on the residual value of the company. That right might be delegated to the board of directors or managers of the company, for obvious reasons, but the board of directors may exercise authority subject to the agreement of the shareholders (Easterbrook and Fischel, 1991).

The conception of the shareholder voting as following from their claim on what is left (the residual value) of the company has been criticised for various reasons. From the theoretical perspective, the Options Theory argued that debt holders are also residual claimants, although in practice, we only see debt holders voting when the company is in distress (Stout, 2002). Furthermore, as a practical matter, one can argue that many other stakeholders of the company also have some claim on the residual value (Blair, 1995; Stout, 2012). Additional complicating matters is that the shareholder’s legal “claim” to the residual value of the company is at best conditional. Generally, shareholders cannot force the board to issue dividends. Shareholders can only be certain that they can tap into the residual value of the firm to the extent that the stock market values any advances that are made, leading to potential capital gains for them if they sell their shares (Stout, 2012). This is one of the rationale behind empowering shareholders with a voting right.

Under the Option Theory, the shareholders have the right to make all “gap-filling” decisions for the company. In any way, it is the directors that are shouldered with the governance role in the company. It is argued that it is exactly the above governance control of the company by the board that is the primary benefit of the corporate form (Bainbridge 2006). Undeniably, Easterbrook and Fischel’s theory is consistent with any observable behavior of the shareholders, either in support of their voting or their decision to delegate any (or all) decisions to the board.

Another argument for shareholder voting relates to Berle and Means’ observation of the separation of ownership and control of the modern companies (Berle and Means, 1932). The above argument was expatiated further by Jensen and Meckling, where they argued that the exchange of equity for capital creates a “principal-agent relationship” between the shareholders and the board of directors (Jensen and Meckling, 1976). There is temptation for the agent (the board of directors) to benefits from this relationship. The principal (shareholders) can minimise these costs by adjusting the cost of capital and engaging in some level of monitoring and checkmating the activities of the board of directors (Rashida and Mohammad, 2010). This is possible through shareholder voting as one mechanism by which monitoring is implemented, and the level of monitoring depends on the benefit the shareholders would gain (Baums, 2000).

However, the principal-agent popularly the Agency Theory (Jensen and Meckling, 1976) as the theoretical basis for shareholder voting will now be examined in respect of argument for and against. It is argued that the agency relationship between shareholders and directors does not meet the legal requirements of principal-agent relationship. The agency relationship “arises when one person, (principal) manifests assent to another person (agent) that the agent shall act on the principal’s behalf and subject to the principal’s control, and the agent manifests assent or otherwise consents so to act” (Restatement of the Law of Agency (Third), 2006, 1.01). It is argued that directors claim independence for all business decisions, it is



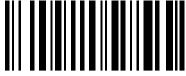
difficult to see how the directors assented to shareholders' control as required in an agency relationship. However, making inference from the provision of section 33 & 63 of the CAMA 1990 leaves no one in doubt that the board act on behalf of the shareholders since the article creates a contract between the shareholders and the directors.

On the one hand, the exercise of voting right at the general meeting is one way to check the board of director's excesses which equally implies that the shareholders are the principal. According to (Blair, 1995; Stout, 2012) there is evidence that the law requires the boards to "act on the shareholder's behalf," no matter how it is. Jensen and Meckling describe an agency relationship "as a contract under which one or more persons (the principal(s) engage another person (the agent) to perform some service on their behalf which involves delegating some decision-making authority to the agent" (Jensen & Mackling, 1976). To determine the agency relationship between shareholders and the board will depend on the nature of the transaction between the shareholders and the board of directors which is mainly regulated by the article of association (section 33 of the CAMA 1990). This provision indicates that a contractual relationship exists between the shareholders and the board of directors. The Court of Appeal of Nigeria re-affirmed that the article is a binding contract between the shareholders and the board which can only be amended by altering the article (section 47, 48 CAMA 1990; *Longe v. FBN PLC*, [2006] LPELR 7682)

According to Williamson's Transaction Cost Economics Model, shareholder vote is one way that the company lowers the cost of capital by providing some assurance to the shareholders that their investment will not be misappropriated (Williamson, 1989). However, if you consider the public offering by Google, the shares were non-voting shares but were still subscribed. Shareholders agreed to take shares in the company even though without voting right attached to the shares and no assurance of return. This is because, they had confidence that they would realize sufficient return even without controlling the directors through the exercise of voting. This is obviously not in line with the provision of the CAMA 1990 which prohibits the issuance of non-voting shares (section 116(1)(b) CAMA 1990). The section provides: "Where, at the commencement of this Act, any share of a company carries more than one vote or does not carry any vote at a general meeting of the company, such a share shall be deemed, as from the appointed day, to carry one vote only" (section 116(1)(b) CAMA, 1990). The above provision indicates that under no circumstance a company shall issue non-voting shares. This aims to sanction the right of shareholders to vote at general meeting. The confidence that shareholders have of getting return on investment without checkmating the board of directors through the exercise of voting right could be reasoned speculation and not justified. For example, shareholders might believe that Google, by paying their employees in stock have effectively secure a means to monitor the board (Paul & Randall, 2014). However, this has no place under the CAMA 1990 as mentioned (section 116(1)(b) CAMA 1990).

The Contractarian viewed shareholder vote as part of the contract between the shareholders and the company. The Court of Appeal of Nigeria (*Longe v. FBN PLC*, [2006] LPELR 7682) held that, the powers vested on the board of directors was a contractual one and can only be removed by amendment to the article. The memorandum and article signifies a binding contract between the company and its shareholders. However, if shareholders choose to invest in a company without voting rights and weak monitoring mechanisms, it is either the shareholders purchased the shares at a low price and so they have little fear that the board will avoid its responsibilities, or some combination of the two (Paul & Randall, 2014). However, the only option that is legally available under the CAMA 1990 is for the shareholders to choose among the various classes of shares. It provides: "Without prejudice to any special rights previously conferred on the holders of any existing shares or class of shares, any share in a company may be issued with such preferred, deferred or other special rights or such restrictions, whether with regard to dividend, return of capital or otherwise, as the company may, from time to time, determine by ordinary resolution" (section 119 CAMA 1990). In anyway, such shares shall not be without voting right.

Another issue relevant to the "principal-agent" relationship is the claim that shareholders "own" the company and that their right to vote follows from this ownership (Weide, 1996). Hansmann (1988) believed that "the shareholder franchise is the ideological underpinning upon which the legitimacy of directorial power rests" (Blasius, 1988). Some scholars rested their support of the shareholder franchise based on the model of shareholder democracy (Harris, 2011). On the one hand, (Lipton and Savitt 2007; Stout, 2007), argued that looking at a company from the perspective of options theory make any claim about "ownership" almost nonsensical (Partnoy, 2000). Shareholders



are unique in their relationship to the company. They are the sole stakeholders whose returns on investment is linked directly to the changes in the stock price of the company. That is the only way that shareholders can be sure of getting any positive return on their investment is by selling the shares at market price to realize a capital gain (or loss). They are not generally guaranteed any dividend or any other payment from the company. All the other including stakeholders, employees, debtors, suppliers knows their returns is attached to the risk the company may incur (Paul & Randall, 2014). Although this is somehow complicated when a director is to be compensated with stock. Such arrangements are usually a deliberate effort to create "pay for performance." In other words, since management is insufficiently attentive to shareholder interests, the compensation package should put them in the shoes of shareholders in order to protect the interest of shareholders. There is still argument as to compensating a director with shares can result in protecting the interest of shareholders (Core, Guay and Thomas (2005).

For most of the public companies, the stock markets are given sufficient information about the company's value so that it is accurately reflected in their share price. As a result, shareholders are the only corporate stakeholders whose return is dependent on both the residual value and the accurate functioning of the stock market (Joseph, 2009). Therefore, it is in the best interest of the shareholders to ensure that the residual value of the company is maximized. This is possible when directors know that shareholders have the right to remove them through exercising their voting right at the general meeting (section 263 CAMA 1990).

The Role of Regulators on Shareholder Vote

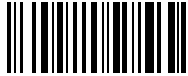
Regulators are expected to play a significant role in protecting the voting right of shareholders. In Nigeria, the Corporate Affairs Commission (CAC) established by section 7 of the CAMA 1990, the Securities and Exchange Commission (SEC) and the Nigerian Stock Exchange (NSE) which were established principally by the Investment and Securities Act, 2007 (ISA 2007) perform the regulatory oversight of companies in Nigeria. Furthermore, the Securities and Exchange Rules and Regulations, 2013 as well as the Rules and Regulations of the Nigerian Stock Exchange, 2015 also compliment the main legislation in sanction the voting right of shareholders.

Shareholders can use the monitoring function of the vote to help accomplish their aims and where the board is not complying with request of the shareholders, the board is subject to removal by shareholder vote through passing of resolution election at the general meeting (section 263 CAMA 1990; Mallin and Andrea, 2012). The requirement that shareholders approve mergers and sales of assets puts pressure on the board to realize the full value of the stock. Thus, shareholder vote is very beneficial in providing the shareholders with the ability to monitor the board so that their interest is protected. It is still arguable whether the current law governing the shareholder vote are adequate to empower shareholders to effectively monitor the act of the board (Bebchuk, 2006, 2007; Bainbridge, 2006; Strine, 2006; Lipton and Savitt, 2007; Stout, 2007; Mallin and Andrea, 2012).

Other Options Available to Shareholders

Shareholder vote may be one of the best way to protect their interests. This study will now examine why other options available to shareholders are not effective. As an alternative to shareholder voting, shareholders can always sell their stock or may sue the company's officers and directors in a court. But then, why are these two options still ineffective? Starting with the sale of shares by shareholders, if a shareholder is not satisfied with the way the directors are running of the company, he can inform the board and dispose of his shares. However, the concern that the shareholder has is the share price, and so the shareholder will be asked to accept a lower price than the value of his shares. To force the shareholder to give up return as the only means to monitor the board is certainly not an attractive option. In this regard, a shareholder would barely realize a fair valuation of his shares (Air Products, 2011). The selling shares may only be an effective monitoring device if the board of directors is also largely compensated by stock (Paul & Randall, 2014). This may have the potential to give shareholders much influence over the performance of the board of directors.

Regarding shareholder's option to sue in court. For general matters of corporate business, instituting action in court has very large transaction costs in terms of expenses. Moreover, there are serious questions of institutional competence when it comes to courts making decisions about corporate policy, which have led courts to develop the business judgment rule to dismiss shareholder litigation. Under the CAMA 1990 for example, the options of selling the shares and or suing the board of directors are not a good option, anyway. Although section 300 of the CAMA 1990 has stipulates certain situations that warrant a shareholder to institute an action against the company, it has continued to be a difficult issue in Nigeria. The principle of majority rule laid down in



(Foss v. Harbottle [1843) 2 Hare 461) has continue to hinder successful filing of cases by individual shareholders in Nigeria. Moreover, filing of cases in court takes too long from filing to judgement/order of court (Halima, 2016). Furthermore, since successful representative shareholder law suits are not getting higher, this may well increase the importance of corporate voting as a monitoring mechanism (Cox and Thomas 2009; Boilermakers Local, 2013). This leaves voting right as generally the most desirable form of giving voice to shareholders. Voting can be very useful in monitoring and conveying information to the board. In some circumstances, it allows shareholders to collect information and thus acts to correct board errors.

Thus, the justification for shareholder voting, then, is not based on the assumption that the shareholders hold the claim on the residual value of the firm. It is on the fact that the certainty of return to the shareholder is linked to improvements of the share price. The study maintained that the shareholder, whose return is influenced by the act of the board of directors should be able to give to effectively have a voice through their votes. This is likely the best reason to give shareholders a vote.

Conclusion

In this study, various theories supporting the exercise of shareholder vote were examined. Thus, shareholder voting as provided under the CAMA 1990 as well other rules and regulations on company meetings have theoretical basis underpinning same. In other word, shareholder vote is justified by its uniqueness in monitoring the activities of the board of directors and in maximizing the share price of the company as it creates their only non-discretionary return on their investment (Bebchuk, 2005). Furthermore, this study argued that, shareholder voting is justified in two other ways. Firstly, shareholders can act as cost-effective monitors of the activities of the board of directors. Secondly, shareholder vote will enable shareholders to get confidential information that will assist the board in reaching the informed decision. In conclusion, the right of shareholder to vote appears to be the best form of monitoring the activities of the board of directors as the two other alternatives of selling stock or filing action against the company were all not effective. In view of that, the CAMA 1990 should emphasise that the shareholder voting right must be respected and exercised accordingly. Finally, the various theories namely; option theory, agency theory, transaction cost and contract theory all appears to have some relevance or supporting the exercise the of shareholder vote as encapsulated under the CAMA 1990.

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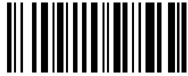

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