

Legal Alert. November 2006. **Investment Clubs & Wealth Creation.**

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Business Motivational Quote.

"The Man who succeeds above his fellows is the one who early in life clearly discerns his object and towards that object habitually directs his powers" ? By Sir Henry Bulwer (Courtesy Tony Olukoyede's Article on "The wealth files - Part II").

Legal News.

There is a new Civil Aviation Law in Nigeria. This Law is more a response to calls for greater autonomy, independence and professionalism for the Nigerian Civil Aviation Authority particularly in the light of recent air disasters.

The Nigerian Senate has passed into Law the Information Bill. This Bill is to allow for more access to public information for the citizens of Nigeria. Also passed into Law is a Bill establishing a third Accountancy Body in Nigeria. This new body, to be known as The Institute of Certified Public Accountants of Nigeria, would regulate Accountants in the public service.

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Investment Clubs & Wealth Creation.

Introduction.

Raising costs of living and health care cost, inflation, insecurity of employment, unreliability of pension funds and systems, increase in levels of education, enlightenment on the importance of money and money management have all resulted in greater attention being paid to wealth creation. Information and myths on the benefits of investing in the stock market and sometime in the real estate market are now wide spread. Unfortunately, not many people have the discipline to take immediate and constructive action by making regular investments in these outlets. The emergence

of Investment Clubs may assist you in achieving your own wealth creation objectives.

What is an Investment Club?

An Investment Club usually consist of a group of individuals who pool their limited or stated funds on a regular basis and collectively invest these funds in a business enterprise like buying shares in the stock market or investing in the real estate market or providing thrift to its members. Central to the success of most Investment Clubs is the necessity for members to share similar values and invest the same amount of money regularly.

Benefits/Attributes of Investment Clubs.

1. Collective financial education, research and enrichment of the members of the Club.
2. Enjoyment of the company/association of other members of the Club.
3. Long term networking outlet for members of the Club.
4. Indoctrination of a savings and investment culture among the members of the Club.

Failure Attributes to Avoid.

- A. Failure of the members to have a long term commitment to the Club by attending Club meetings regularly, making contributions regularly, adhering to an agreed investment strategy, etc.
- B. Failure to manage the Club as a business by ensuring flawless book keeping and security of their investments.

Legal Vehicle of Investment Clubs.

Depending on the legal requirements in your jurisdiction, it is recommended that Investment Clubs should be created in the form of private limited liability companies. Some of the reasons for this recommendation for the creation of a private limited liability company include:

1. It limits the liability of each and every member of the Club.
2. It makes for continuity and easy liquidation of the investment of any or all the members of the Club in the event of an exit, for any reason, by any member of the company.
3. It makes for better tax management in the long term.
4. It makes for more growth potential for the investors and their investment.

This recommendation of establishing Investment Clubs as private limited liability companies does not in any way bar you from establishing an Investment Club either as a limited partnership ? which exposes the members to more liability - or as a company limited by guarantee ? which is cumbersome and does not allow the members to receive any profit.

Like most private limited liability companies, it is recommended that an Investment Club should have at least more than two members but not more than fifty members. This is because legally, a private limited liability company must not have more than fifty members. The ideal number of members, based on current practices, is an average of fifteen (15) members for each Investment

Club. There appears not to be any restriction on the number of Investment Clubs that you can join provided you make the regularly monthly contributions to each Club.

Most Investment Clubs usually have an initial life span of five (5) years. It is recommended that the members of each Club should consult among themselves to harmonise the tenure of their investments.

Tax Management of Investment Clubs.

The desire to reduce tax liability has led some Investment Clubs to contemplate starting as limited partnerships or as co-operative societies or as companies limited by guarantee.

The problem with the above tax strategy is that most tax laws in many countries require that, subject to exempted religious and charitable organisations which are non-profit based, all dividends, interest income, gains or any form of benefit deriving from any service or activity are liable to payment of tax to the government. The legal vehicle or description of the Investment Club is not relevant to the tax authorities because as already stated, all income from all sources, save for the ones exempted, are liable to payment of tax.

To protect the members of the Investment Clubs from double taxation of their income in the hands of the company - under the Companies Income Tax regime - and in the hands of the members of the Club - under the Personal Income Tax regime - the members of the Investment Clubs would do well to either retain a part-time licensed Accountant who is also a Tax Practitioner or admit one as a member of the Investment Club.

The admission of a Tax Practitioner/Accountant as a member of the Club would ensure proper handling of the accounts of the Club and its members. The further advantage is that most of the members of many Investment Clubs render professional services to their Clubs free of charge. Savings would therefore be made by such an admission.

Also on double taxation, mention must be made of the fact that all dividend income are liable to withholding tax deductions when the final dividend is received by the investor from the investing company. However, the additional or final tax to be paid by the investor on the dividend income, when he receives the dividend under the Personal Income Tax regime is less the upfront withholding tax already deducted by the paying company of the dividend income. For more information on withholding tax, you can visit our web site www.oseroghoassociates.com and read our Legal Alert on Withholding Tax.

Conclusion.

The benefits of encouraging the establishment of more Investment Clubs are enormous, both to the members of the Clubs and to the larger society. You are encouraged to join one or start one immediately or very, very soon.

It would be helpful if the government considers providing some incentives to Investment Clubs in the light of the fact that they are a good medium for encouraging savings, investments and thrift in our economy. The Investment Clubs should in turn be further registered and partly regulated by the Federal Board of Inland Revenue through the Federal Ministry of Finance so that the incentives to be provided are not abused by bogus Investment Clubs.