

# ETHIOPIAN BANKRUPTCY LAW: A COMMENTARY (PART I)

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*The bankruptcies came to us from Italy, \_bancorotto, bancarotta, gambarotta e la giustizia non impicar\_. Every merchant had his bench (\_banco\_) in the place of exchange; and when he had conducted his business badly, declared himself \_fallito\_, and abandoned his property to his creditors with the proviso that he retain a good part of it for himself, be free and reputed a very upright man. There was nothing to be said to him, his bench was broken, \_banco rotto, banca rotta\_; he could even, in certain towns, keep all his property and balk his creditors, provided he seated himself bare-bottomed on a stone in the presence of all the merchants. This was a mild derivation of the old Roman proverb--\_solvere aut in aere aut in cute\_, to pay either with one's money or one's skin. But this custom no longer exists; creditors have preferred their money to a bankrupt's hinder parts.*

*Voltaire, Philosophical Dictionary, 'Bankruptcy'*

## Introduction

It is no exaggeration to state that Ethiopian Bankruptcy Law (tucked away in the last Book of the Commercial Code) is the least known and hence the least practiced in Ethiopia. Since the coming into force of the Commercial Code in 1960, cases having to do with bankruptcy have been few and far in between.<sup>1</sup> Why might this be? Is the defect in the law or in the economic environment? Is Ethiopian business environment immune from the natural laws of bankruptcy or has it always gone bankrupt without ever being noticed by the public or mediated by the law?<sup>2</sup> The Economist magazine recently quipped that imagining capitalism (business enterprises) without bankruptcy

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<sup>1</sup> The incidence of bankruptcy cases is reportedly picking up in recent times. For example, a regional high court recently declared a flour factory bankrupt in accordance with the bankruptcy provisions of the Commercial Code; in re. Shafi Kemal and Family Private Limited Company, Eastern Shoa Zonal High Court (Oromia), File No. 08477/98 E.C.

<sup>2</sup> Bankruptcy is a natural law of business. It is not that businesses in Ethiopia do not go bankrupt. But when they go bankrupt, the old law of the superior creditor seems to rule supreme in practice. Banks, for example, have developed a practice of private receiverships through private loan contracts. In this arrangement, borrower-businesses agree to submit their business to an employee or a consultant installed by the bank. The employee or consultant of the creditor bank manages the financial operations of the debtor and attempts to restore the latter to solvency. This practice is seen by some as a snub to the formal bankruptcy proceedings; see USAID: Ethiopia Commercial Law & Institutional Reform and Trade Diagnostic, January 2007, p. 53;

is like imagining Christianity without hell.<sup>3</sup> Perhaps, that is what happened in Ethiopia.

The questions of why bankruptcy laws have become dormant are troubling questions. However, as troubling they are, they cannot be answered in categorical terms. An answer to these questions would require an extensive empirical study of the business environment and the historical factors that might have kept the bankruptcy laws of Ethiopia from having to see the light of the courts.

There is no shortage of theories as to why bankruptcy cases are not as common as the failure of businesses would suggest. One theory puts the blame on the freezing of commerce in the aftermath of the 1974 Ethiopian Revolution, tying the (mis)fortunes of the bankruptcy provisions to the Commercial Code in general.<sup>4</sup> The problem with this theory is that it only explains why bankruptcy fell into disuse between 1974 and 1991. It does not explain the situation after 1991 when the economy of Ethiopia was more or less liberalized (seventeen years and counting!).

Another theory is lack of familiarity (of the legal community) with the provisions of bankruptcy in the Commercial Code. Lawyers are a critical piece in the application of the law. If lawyers do not know or understand the law, it is unlikely that the law will ever come to courts even if it were included in the Code. It is what Emperor Haile Sellassie I was emphasizing in his speech on the inauguration of the Journal of Ethiopian Law:

*... We have observed that Ethiopia's rapid progress demands the services of a large number of legal experts... capable of insuring the effective application of the law.*<sup>5</sup>

In a recent report commissioned by the USAID, this matter has been aptly emphasized:

*There is little demand for change from the debtor side because so little is known about bankruptcy protection. The possibility of reorganization or*

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<sup>3</sup> See, The Economist, Business Bankruptcies, Waiting for Armageddon, March 27, 2008.

<sup>4</sup> Ato Tamiru Wondimagegnehu, who was a judge during the Imperial times, believes that the history of the Commercial Code in general and that of the bankruptcy law would have been completely different had the Revolution not taken the country along a completely different ideology of socialism. He remembers some cases of bankruptcy that started coming before courts; although the judges were not familiar with the bankruptcy provisions, they referred to the bankruptcy provisions to adjudge businesses bankrupt; conversation with Ato Tamiru Wondimagegnehu, November 28, 2008.

<sup>5</sup> Journal of Ethiopian Law, Vol. 1, No. 1, Summer 1964, p. V

*protection arises not only from law, but from knowledge of the law, and that is quite limited.*<sup>6</sup>

The third theory points to the foreclosure laws and practices of Ethiopia as probable reasons for the eclipse of bankruptcy. According to the USAID Commissioned report:

*...lenders are using foreclosure law and practice instead of bankruptcy. Secured lenders can institute accelerated proceedings to repossess and liquidate security and do not need to start a bankruptcy action. Frequently, borrowers are captive to a single lender, with few other commercial obligations than their bank loan, so that foreclosure effectively deals with most of the debtor's liabilities, although it does not permit rehabilitation or reorganization and often results in liquidation.*<sup>7</sup>

Foreclosure powers were granted to banks and selected other creditors only in the last decade and could not entirely explain why bankruptcy practices are not so common.<sup>8</sup> It is perhaps nearer to the truth to conclude that multiple factors were conspiring to keep bankruptcy out of the limelight of the practice.

Although cases of bankruptcy have rarely been taken to courts, there are several reasons why one should write about Ethiopian bankruptcy law. First, it is barely known even among the otherwise savvy and seasoned lawyers of Ethiopia. Second, it has now been offered as an independent course for the last five or so years without any reference material. And lack of reference material is always a legitimate inspiration for writing (even if it were just an article). Third, since 1991, Ethiopia has taken on an economic policy whose driving engine is the participation of the private sector, and the private sector needs laws not just for its formation but also for its orderly winding up and possibly for its rehabilitation after bankruptcy.<sup>9</sup> It is not that Ethiopia lacks these laws but they are unknown even among those who earn a living from their knowledge of the law.

This commentary is divided into two parts. In the first part, I intend to treat subjects like the background of Ethiopian bankruptcy law, its organization and structure, scope and meaning, and the tests for commencement of bankruptcy under Ethiopian bankruptcy law. In the second part, I intend to throw light on some of the other basic

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<sup>6</sup> See United States Agency for International Development (USAID), Ethiopia Commercial Law and Institutional Reform and Trade Diagnostic, January 2007, p. 56

<sup>7</sup> Ibid, P. 53

<sup>8</sup> See Property Mortgaged or Pledged with Banks Proclamation No. 97/1998 and a Proclamation to Provide for Business Mortgage Proclamation No. 98/1998

<sup>9</sup> It is difficult to see how an economy can thrive without an effective bankruptcy law; for objectives and goals of bankruptcy law, See United Nations Commission on International Trade Law (UNCITRAL), Legislative Guide on Insolvency Law (2005), p. 14 ; See also Elizabeth Warren, the Untenable Case for Repeal of Chapter 11, Yale L. J., Vol. 102, No. 2, pp 467, 478

features of Ethiopian bankruptcy law and related subjects of composition and schemes of arrangement.

At the end of each part, I will provide some concluding remarks on what I think would be striking features of Ethiopian bankruptcy law. For these commentaries, I have relied upon as wide a range of literature on the subject of bankruptcy as I could get my hands on. But as repeated quotes and references in the footnotes show, I am indebted primarily to the 2005 UNCITRAL Legislative Guide on Insolvency Law of 2005 (hereinafter simply 'UNCITRAL' Guide').<sup>10</sup> As far as I am concerned, 'UNCITRAL Guide' offers the latest and most comprehensive reference on the subject of bankruptcy. The 'UNCITRAL Guide' also provides alternative approaches on controversial points of bankruptcy, something one can rarely find in many other sources.

## I. Background

The history of bankruptcy law in Ethiopia (at least in its modern sense) dates back to 1933. That was the year when Emperor Haile Sellassie I passed a bankruptcy law containing 96 articles.<sup>11</sup> It is not clear as to how much of a resource material this law was for the drafter of Book V of the Commercial Code, but there was no doubt the drafter was aware of its existence, as the background documents show.<sup>12</sup> Along with the Business Organization Law of 1933 and Registration Decree of 1928, the Bankruptcy Law of 1933 represents the Emperor's first attempt to modernize Ethiopian law relating to business or commerce.<sup>13</sup>

Under the 1933 law, 'every person registered in the commercial register' and who suspends payment might be declared bankrupt.<sup>14</sup> Suspension of payment triggers a proceeding of bankruptcy only when the obligation of payment arises out of what the

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<sup>10</sup> United Nations Commission on International Trade Law (UNCITRAL), Legislative Guide on Insolvency Law (2005).

<sup>11</sup> The Commercial Code of 1960 had three 'domestic' legislative predecessors: Registration Decree of 1928, Law of Business Organizations of 1933 and Law of Bankruptcy of 1933; see Peter Winship (ed. and trans.), Background Documents to the Commercial Code of Ethiopia of 1960, Faculty of Law, HSIU, 1974 Appendix III (Manuscript), Pp. 185-220

<sup>12</sup> In the Background Documents compiled and translated by Peter Winship, the drafter acknowledges borrowing from the French, Italian and other bankruptcy laws. He also referred to the 1928 Registration Decree and the 1933 Business Organization Law; See Peter Winship (ed. And trans.), Background Documents to the Commercial Code of Ethiopia of 1960, Faculty of Law, HSIU (1974); pp. 45 and 54

<sup>13</sup> It is striking to note that this first attempt, what one might call the first phase of legislative modernization, was rather piecemeal and uncommitted. It was on the second phase that the Emperor took more drastic and systematic approaches to modernizing Ethiopian law and Ethiopian legal system, with the promulgation of Penal Code in 1957, the Civil Code, the Commercial Code and the Maritime Code in 1960, the Criminal Procedure Code in 1961 and the Civil Procedure Code in 1965.

<sup>14</sup> Art. 1 of the 1933 Bankruptcy Code

law calls an 'executory document' ('titre exécutoire').<sup>15</sup> An executory document is narrowly defined in the 1933 law. It refers to three documents only:

- a) a judgment against the debtor in a court of last appeal;
- b) a minute of a conciliation proceeding in which the debt is recognized without reservation;
- c) a commercial instrument signed or accepted by the debtor accompanied by a protest for non-payment regularly drawn up.

The 1933 Bankruptcy law allowed initiation of bankruptcy only against debtors who suspended a payment which was a sum certain, liquid and in all respects evidenced by a written document. Incidentally, with the exception of a court judgment, these documents would have permitted creditors to seek order through the special route of summary proceedings, and the notion of 'titre exécutoire' is more often used today in connection with summary or accelerated proceedings.<sup>16</sup>

Apart from the commencement standard (which was very stringent), two other features distinguish the 1933 bankruptcy law from the Commercial Code of 1960. One is that the 1933 law did not have provisions for 'schemes of arrangement'.<sup>17</sup> The other is that the 1933 law contained penal provisions.<sup>18</sup>

It is not certain if the 1933 Bankruptcy law was ever applied in practice. Even the otherwise reliable account of the period, Mahteme Sellassie's *Zikra Neger*, says nothing about the 1933 Bankruptcy Law. This is rather surprising because it mentions other similar laws passed at the time, such as the Law of Business Organizations of 12 July 1933, and the Registration Decree of 25 August 1928.<sup>19</sup>

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<sup>15</sup> Ibid; Compare with OHADA Uniform Act on Simplified Recovery Procedures and Enforcement Measures (1998): Article 33. According to the Uniform Act, only the following are defined as enforceable rights (titre exécutoire): a court decision which has been declared enforceable, a foreign deed or court decision or an arbitral award that cannot be suspended by any type of appeal and that has been declared enforceable by a court decision in the State where the enforcement is sought; official minutes of conciliation, signed by a judge and the parties; a notarized deed that has been declared enforceable; or a decision which, under the national law of the Member State concerned, has the same effect as a court decision; See Boris Martor et al, *Business Law in Africa, OHADA and the Harmonization process*, 2002, P. 232.

<sup>16</sup> Compare with Article 284 of the Ethiopian Civil Procedure Code; summary procedure is designed to prevent full trial when there is no material issue of fact to be tried; See Notes, *Factors Affecting the Grant or Denial of Summary Judgment*, *Columbia Law Review*, Vol. 48 (1948), p. 780.

<sup>17</sup> The 1933 law has provisions regarding 'composition', see Chapter 12, Articles 68-84

<sup>18</sup> See Chapter 13, Articles 85-93 of the 1933 Bankruptcy law; the Commercial Code has no provisions regarding offenses related to bankruptcy, leaving these matters to the Penal Code of 1957, Articles 625-633

<sup>19</sup> Incidentally, the Law of Business Organizations and the Bankruptcy Law were passed on the same date; See Mahteme Sellassie W/Meskel, *Zikra Neger* (1962 E.C. in Amharic). About the 1928 Decree, the first drafter of the Commercial Code writes: "The Decree was not applied effectively outside Addis Ababa and several towns." See Escarra, *Book I Expose des Motifs* (2 September 1954), in Winship, *Supra Note 12*, P. 45; See also the preamble of the Commercial Code of 1960.

The first drafter of Book V of the Commercial Code, Professor Escarra, used the French Bankruptcy Legislation (as revised in 1955) as the primary source for drafting Book V of the Commercial Code, with one important difference.<sup>20</sup> The French law of the time provided for two procedures, namely bankruptcy and judicial administration<sup>21</sup>, but Professor Escarra removed judicial administration<sup>22</sup> from his Ethiopian draft and supplanted it with the 'scheme of arrangement systems' accepted in many jurisdictions, such as in Italy.<sup>23</sup> The schemes of arrangement sections (Book V, Title V, Articles 1119-1166) were primarily borrowed from the Italian law of 1942, which the drafter at the time considered the most technically complete.<sup>24</sup> The composition sections (Articles 1081-1100) were also inspired in part by the Italian law of 1942.<sup>25</sup>

Professor Escarra was not able to complete the drafting of the Commercial Code due to his untimely death in 1954. The task of completing the drafting of the Code fell upon Professor Jauffret. At the time of his death, Professor Escarra had completed the drafting of Book V of the Commercial Code, and Professor Jauffret accepted this draft, in his words, 'with minor revisions and innovations of his own.'<sup>26</sup> These 'revisions and innovations' of Professor Jauffret included:

- i) *clarifications (redrafting) of provisions on the scope of bankruptcy, conditions of bankruptcy, bankruptcy in fact, court jurisdiction and harmonization of the rules of bankruptcy with those on commercial register;*

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<sup>20</sup> Winship, Supra Note 12, P. 109; Professor Escarra drafted the texts of Book II (Business Organizations), IV (Negotiable Instruments and Banking Transactions) and V (Bankruptcy and Schemes of Arrangement). Professor Jauffret took over the drafting of the Commercial Code (upon Professor's Escarra's death) and produced Books I and IV, See Winship, Supra Note 12, p. 33.

<sup>21</sup> Judicial administration or judicial arrangement under the French system is in many ways similar to the schemes of arrangement under Ethiopian law. In a French system, a debtor and creditors may enter into agreement and submit the same to court. If the agreement is confirmed by the court, it enables the debtor to continue the operation of its enterprise; see Jacques M. Raffin, Commercial Laws of France, in the Digest of the Commercial Laws of the World, 1972.

<sup>22</sup> One interesting note about this is that Professor Escarra himself was a member of the French Commission on the revision of the French Commercial Code and recommended the adoption of the scheme of arrangement for France, but his proposal was rejected. Well he was not disappointed for ever, as he put that in the Ethiopian Commercial Code, with little opposition; See Winship, Supra Note 12, p. 109.

<sup>23</sup> Winship, Supra Note 12, P. 109

<sup>24</sup> Ibid.

<sup>25</sup> The drafter thought he took a huge risk in this regard, because at the time the Italian war and occupation was fresh on the minds of the Imperial Government; He writes "The valid resentment which the Italian occupation has left in Ethiopia should not blind one tot he technical value of some of the Italian laws, which should be studied correctly." See Winship, Supra Note 12, p.105. There was no evidence that the Government officials of the time held anything against him for borrowing from the laws of Italy. No body took action against the roads constructed by Fascist Italy, and if any thing, people were grateful. The drafter, through his statements, sought to preempt any possible backlashes against his recourse to Italian law. After all, what had Italian fascism to do with 'composition' and 'schemes of arrangement'? Nothing!

<sup>26</sup> Winship, Supra Note 12, PP. 109-110

- ii) *incorporation of the principle of 'suspension of individual suits' upon declaration of bankruptcy (Article 1026);*
- iii) *provision of a definition for the phrase 'universality of creditors' (Article 1025);*
- iv) *addition of rules relating to business, in particular the rule regarding the right of universality of creditors to have a mortgage upon business in Article 1007 cum 1089 (legal mortgage), and rules regarding the rights of creditors secured by mortgage on the business in the distribution of the residue (Articles 1069-1072) and a rule that extinguishes the right of business mortgagees to seize the business after the opening of compulsory winding-up (Article 1105),<sup>27</sup>*
- v) *incorporation of rules regarding the rights of sellers with ownership reserved (Articles 1063 cum 1076)*

Apart from these, Professor Jauffret considered the draft prepared by Professor Escarra 'satisfactory' and submitted the final draft with his report on 1 March 1958, four years after Professor Escarra passed away. Two years later, i.e. in 1960, the Commercial Code was promulgated as a law, containing, among others, Law of Bankruptcy, as one of the five books of the Code. The final version of Book V, as officially promulgated, contains 202 articles arranged in five titles:

Title I: General Provisions

Title II: Bankruptcy

Title III: Schemes of Arrangement

Title IV: Special Provisions Concerning Bankruptcy and Schemes of Arrangement with Respect to Business Organizations

Title V: Summary Procedure

## **II. The Structure (Organization) of Ethiopian Bankruptcy Law**

On the structure of Ethiopian bankruptcy law, three general statements can be made.<sup>28</sup> First is its distinct preference for bankruptcy, in the sense of its preference for liquidation to rehabilitation of the debtor's business. This is an inference from the arrangement of the provisions, rather than an explicit statement of policy expressed in any of the provisions of Book V of the Commercial Code. The provisions regarding bankruptcy precede the provisions on composition and schemes of arrangement. In addition, the largest number of provisions is devoted to the liquidation of the business of the debtor for the collective interest of creditors. Only on occasions is the law interested in saving the business of the debtor from dismemberment by creditors.

<sup>27</sup> Professor Jauffret claims to have invented these rules, as he found no parallel elsewhere, but justified in Ethiopian law; See Winship, *Supra* Note 12, P. 110

<sup>28</sup> Having been drafted by two drafters at different times, Book V of the Commercial Code strikes one as lacking in unity. This lack of unity makes it difficult to make categorical statements about the Code.

Once a bankruptcy proceeding is set in motion, the law presumes that the debtor is culpable, not just unlucky, to have been declared bankrupt.<sup>29</sup> In all cases, the law strips the debtor of his power and right to manage his business.<sup>30</sup> The law requires the appointment of third parties, like trustees and commissioners, for the purposes of temporarily managing the debtor's business, collecting debts and distributing the proceeds among creditors.<sup>31</sup> All these point strongly towards the Code's preference and partiality for bankruptcy. The USAID Diagnostic made a similar observation in the following words: 'The [Ethiopian] bankruptcy law provides for liquidation and reorganization (sic), but in tone and practice clearly favours liquidation.'<sup>32</sup>

Secondly, the Commercial Code appears to chart two separate (at points related) procedures for debtors in financial difficulties.<sup>33</sup> A debtor and other parties may either pursue the route of bankruptcy or schemes of arrangement, and although there are possibilities for conversion in the course of proceedings, each route has its own separate rules and proceedings.<sup>34</sup> Each proceeding sets forth its own access and commencement requirements, with different possibilities for conversion between the proceedings at some stage.<sup>35</sup>

This approach of the Commercial Code contrasts with what the 'UNCITRAL Guide' calls the 'unitary' approach. In a unitary approach, a single commencement requirement leads the business through reorganization and liquidation.<sup>36</sup> Ordinarily, the business in financial difficulties goes through reorganization attempts, and only when that fails will one proceed to liquidation.

Recent bankruptcy reforms in some countries have moved in the direction of the unitary approach.<sup>37</sup> And more and more countries are opting for a wait and see period, known as the 'observation period', to determine the direction of the proceeding for a business in financial difficulties.<sup>38</sup> During the 'observation period' no presumption is made as to whether the business will be eventually reorganized or liquidated.<sup>39</sup> This

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<sup>29</sup> See, for example, Articles 1019 – 1023 of the Commercial Code

<sup>30</sup> See Article 1023 of the Commercial Code

<sup>31</sup> See Articles 991-993 and 994-1001 of the Commercial Code

<sup>32</sup> USAID, *Supra* Note 6, p. 53

<sup>33</sup> I use 'financial difficulties' deliberately because the debtor's current inability to pay debts may lead to bankruptcy and imminent inability to pay debts may trigger a scheme of arrangement; see Articles 968 and 1119 of the Commercial Code.

<sup>34</sup> For example, a debtor as well as creditors, court or the public prosecutor may apply for bankruptcy while it is only the debtor that can apply for a scheme of arrangement; compare Article 975 with 1119 of the Commercial Code.

<sup>35</sup> UNCITRAL, *Supra* Note 4, p. 17

<sup>36</sup> *Ibid*; See also the French Commercial Code where a single proceeding takes a business in financial difficulties through safeguard proceedings, reorganization, and liquidation; Vogel, Louis, and Perochon, Françoise, trans. French Commercial Code.

<sup>37</sup> UNCITRAL, *Supra* Note 10, pp 17-19

<sup>38</sup> *Ibid*, p. 19

<sup>39</sup> *Ibid*



approach is quite reasonable, because, in practice, it is often impossible to provide an accurate diagnostic as to the viability of the business.<sup>40</sup> A separate proceeding may lead more often than not to a misdiagnosis of the financial situation of the business, leading courts to misconstrue temporary financial shortfalls for a permanent problem and vice versa. Misdiagnosis can become costly, as it would mean the court might have to go back on its initial judgments. And this error in judgment can be irreversible. In its adoption of separate proceedings, the Commercial Code seems to open a way for this kind of error.

A third prominent feature of the Commercial Code is that, by the explicit preference of the drafters, the Code follows a 'dual' system of bankruptcy and schemes of arrangement, setting down separate rules in a separate title for business organizations.<sup>41</sup> This does not, however, mean that the general rules of bankruptcy, such as those in Articles 974 to 1118 do not apply to business organizations. Many of these rules apply to business organizations, but in addition to these rules and at times as exceptions to these rules, there are special rules that apply to business organizations only. It is for these 'special rules' that a separate title has been included in the Commercial Code. It will be seen that this approach is more about where these rules should be put than anything else. If these rules were inserted in the general provisions, we would not be talking about dual approach in this instance.

There are other distinct features which strike us when we read Book V, but these, to my mind, are minor. These features include, for example, the heavy accent on the punitive element in the bankruptcy regime and the rules on discharge. These features of the Commercial Code will be emphasized in their appropriate places.

As alluded to before, Book V of the Commercial Code is arranged into five titles. Title I, with the smallest number of articles (just six Articles), is appropriately entitled "General Provisions." This title lays down general rules for the whole Book. It defines the scope of Book V and sets down the conditions for bankruptcy and schemes of arrangement. Title II, with the largest number of articles (154 Articles in all), is devoted to 'bankruptcy' and 'composition.' This is the most important title in the whole *corpus* of Book V. Title III deals with schemes of arrangement, and its aim is, in contradistinction to Title II, the saving of the business of the debtor. Title IV contains special rules of bankruptcy and schemes of arrangement for business organizations. The last title in Book V (Title V) deals with small and simplified (as well as accelerated) bankruptcy proceedings.

### **III. On the Meaning of Bankruptcy**

As Voltaire's quote at the beginning of this article notes, the word bankruptcy is etymologically derived from an old Italian word "banca rotta" which signified the

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<sup>40</sup> Ibid, p. 18

<sup>41</sup> See Title IV of Book V of the Commercial Code, Articles 1154-1165

medieval practice of breaking tables/benches on a trader who absconded with the money or goods of creditors. The etymological meaning of the term today survives as a relic of a brutal past, and nothing more.

There is some confusion and inconsistency in bankruptcy literature in the use of the term 'bankruptcy' and cognate concepts like 'insolvency' and 'reorganization.' Part of the confusion is that the term bankruptcy is sometimes used interchangeably with insolvency, and sometimes the two terms are technically distinguished. Some use insolvency to refer to the fact of inability to pay debts and restrict bankruptcy to the judicially recognized proceeding following one's inability to pay debts. Black's Law Dictionary, for instance, defines insolvency as "the condition of being unable to pay debts as they fall due or in the usual course of business" and limits bankruptcy to 'the statutory procedure, usually triggered by insolvency, by which a person is relieved of most debts and undergoes judicially supervised reorganization or liquidation for the benefit of that person's creditors.'<sup>42</sup> Similarly, Encyclopedia Britannica defines insolvency as 'the inability to meet debts' and bankruptcy as 'the status of the person who has been declared by judicial process to be unable to pay his debts.'<sup>43</sup>

Some writers use insolvency for a similar proceeding for debtors other than traders, in the sense of civil bankruptcy. For these, bankruptcy refers to a proceeding respecting traders and commercial business organizations. In P Ramanatha Aiyar's Concise Law Dictionary, for example, we have this:

*The leading distinction between a bankruptcy law and an insolvency law, in the proper technical sense of the words, consists in the character of the persons upon whom it is designed to operate, the former contemplating as its objects traders of a certain description, the latter insolvents in general, or persons unable to pay their debts.*<sup>44</sup>

For some, the distinction between bankruptcy and insolvency does not even seem relevant. The 'UNCITRAL Guide', for example, uses the term 'insolvency' to mean both the fact of inability to pay debts and more importantly the formal proceedings for either liquidation of the debtor's assets or rehabilitation of the debtor's business.<sup>45</sup>

There is also some confusion over the scope of bankruptcy. Sometimes, bankruptcy is used broadly as to include both proceedings of liquidation and reorganization of

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<sup>42</sup> See Black Law Dictionary, Bryan A. Garner (ed. 1993), s.v. "Bankruptcy"

<sup>43</sup> See Encyclopedia Britannica, 2005 Edition, s.v., "Bankruptcy"; Arthur Leff defined bankruptcy as 'a legal proceeding...in which an insolvent debtor by surrendering his non-exempt assets for distribution to his creditors may be granted a discharge from substantially all his obligations'; See Arthur Leff, the Leff Dictionary of Law: A Fragment, Yale Law Journal, Vol. 94, No. 8, p 2132

<sup>44</sup> P. Ramanatha Aiyar, Concise Law Dictionary, With Legal Maxims, Latin Terms and words and Phrases, 2006

<sup>45</sup> See UNCITRAL, Supra Note 10, p 5

a business.<sup>46</sup> When bankruptcy is used in this sense, the various proceedings available for bankrupt business are distinguished by the use of terms like 'liquidation', 'composition', 'reorganization,' all as constituent elements of bankruptcy as an overarching procedure. If the aim of a proceeding in a particular instance is to liquidate the bankrupt business (and distribute the proceeds among creditors), terms like 'liquidation' or 'straight bankruptcy' are used.<sup>47</sup>

Sometimes bankruptcy is used in a narrow sense of only referring to liquidation proceedings. In this sense, bankruptcy is synonymous and interchangeable with liquidation, and reorganization proceedings are treated as if they were a separate proceeding from bankruptcy.<sup>48</sup> This association of the term bankruptcy with liquidation of the debtor's business is now less common.

The Ethiopian Commercial Code (of 1960) uses the term 'bankruptcy' almost exclusively. There is only one article in the entire Commercial Code where insolvency is mentioned alongside bankruptcy, not as an interchangeable word but possibly as the fact of inability to pay debts.<sup>49</sup> That article is Article 542(3) where insolvency is stated as not a ground for dissolution of a company 'unless otherwise expressly provided in the articles of association.'<sup>50</sup>

The Commercial Code uses 'bankruptcy' in a narrow sense of 'straight bankruptcy' referring to proceedings that involve the liquidation and winding-up of the business of the bankrupt debtor. Book V itself is entitled 'Bankruptcy and Schemes of

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<sup>46</sup> Black's Law Dictionary, for example, defines bankruptcy as having two forms: liquidation and reorganization. The Dictionary also concedes that the terms 'straight bankruptcy' and 'bankruptcy' often are used to describe liquidation because the vast majority of bankruptcy cases are liquidation cases; See Black's Law Dictionary, ... Edition, s.v. "Bankruptcy" ....; similarly the late Professor Arthur Leff seems to subscribe to this broad construction of bankruptcy. He writes "the [US] Bankruptcy Act also provides for reorganization of debtors, i.e., a procedure for the rehabilitation rather than liquidation of the debtor's estate or business"; Arthur Leff, *the Leff Dictionary of Law: A Fragment*, Yale L. J., Vol. 94, No. 8, p 2132.

<sup>47</sup> The UNCITRAL Legislative Guide defines liquidation as 'proceedings to sell and dispose of assets for distribution to creditors in accordance with the insolvency law.' See, UNCITRAL, *Supra* Note 10, p 5

<sup>48</sup> See Black's Law Dictionary, *Supra* Note 46

<sup>49</sup> The Commercial Code avoids 'insolvency' even for a fact of inability to pay debts. Instead, the Code uses 'suspension of payment' or 'bankruptcy in fact' to refer to the fact of inability to pay debts; See Articles 969, 970 and 971 of the Code.

<sup>50</sup> The Civil Code of Ethiopia, on the other hand, uses the term 'insolvency' in some provisions (see, for example, Articles 1019 and 1757) and 'bankruptcy' in others (see Articles 1932 and 1947 of the Civil Code); the Civil Code is not helpful in distinguishing bankruptcy from related concepts. But, Article 1019 (2) of the Civil Code unearths the intention of some of the drafters of Ethiopian Codes to develop parallel procedures (of insolvency) for civil debtors in the Ethiopian Civil Procedure Code. For some unknown reasons, the 1965 Ethiopian Civil Procedure Code failed to incorporate detailed rules for insolvency of civil debtors. If this intention (of the drafters) were realized, we would have provisions for insolvency of civil debtors (non-traders, consumers) in the Code of Civil Procedure and bankruptcy proceedings for traders in the Commercial Code. Now we only have the latter.

Arrangement” to separate the ‘scheme of arrangement’ part from the ‘bankruptcy’ part. Title II of Book V, entitled ‘bankruptcy’, includes provisions that eventually lead to the liquidation and winding-up of the bankrupt’s business, tempered only by the provisions of ‘composition.’<sup>51</sup> ‘Tempered’, because once bankruptcy is set in motion, composition and payment in full are the only ways out from the liquidation of the debtor’s business.<sup>52</sup> With the exception of the possibility for opting out of bankruptcy through composition, all the rules of Title II regarding bankruptcy are aimed at liquidating and winding-up of the business of the bankrupt debtor. The following definition of bankruptcy offered by the first drafter by and large confirms this narrow sense of bankruptcy:

*Bankruptcy can be defined as both a collective and universal mode of execution: collective in the sense that it puts secured and unsecured creditors more or less on an equal footing, universal in the sense that it applies to the total estate of the bankrupt person. The goal of this procedure is either to save the enterprise by a composition with creditors or to liquidate it, which may bring into play different losses of rights or penalties for the debtor in bad faith in particular.*<sup>53</sup> (Emphasis mine)

It is not difficult to see that the first drafter did not see ‘schemes of arrangement’ as part of a bankruptcy proceeding. As to why the drafter preferred the term ‘bankruptcy’ to be used in this narrow sense, instead of a more common expression such as ‘liquidation’ or ‘straight bankruptcy,’ it is for anyone to speculate.<sup>54</sup> It is not as if the term ‘liquidation’ was not on offer at the time. Other Books of the Commercial Code use the term ‘liquidation’ to refer to procedures aimed at dissolving and winding-up a business.<sup>55</sup>

Although bankruptcy may be more appropriately used in the broader sense, as shown above, we ought to conform to the narrow construction of the drafter in this article, and unless the context otherwise shows, bankruptcy is used in this article to denote straight bankruptcy or liquidation, distinguished from cognate procedures of ‘composition’ and ‘schemes of arrangement.’

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<sup>51</sup> See Articles 1081-1100 of the Commercial Code

<sup>52</sup> See Article 988 of the Commercial Code; for composition, later

<sup>53</sup> Winship, *Supra* Note 12, p. 105

<sup>54</sup> It may have something to do with the fact that the drafters of the Commercial Code were two. The first drafter, Professor Escarra, completed the drafting of Books II, IV and V before his untimely death in 1954 and the second drafter, Professor Jauffret, completed the other Books (I and III), See Winship, *Supra* Note 12, P. 33

<sup>55</sup> See, for example, Articles 496, 499-509 of the Commercial Code

## IV. Scope of Ethiopian Bankruptcy Law

### 4.1 In General

Modern bankruptcy law grew out of the practices of the mercantile cities of Northern Italy and for a long time bankruptcy was seen as a status that applied only to merchants.<sup>56</sup> Bankruptcy law has come a long way since then. Many countries have now abandoned this restriction of bankruptcy to traders. Their bankruptcy regimes are often extended to all classes of persons, whether these are engaged in trade or not.<sup>57</sup> There are, however, some countries (which inherited their laws from the French tradition) which still restrict bankruptcy to traders.<sup>58</sup> Ethiopia, by the conscious choice of the drafters, belongs to the group of countries which apply bankruptcy only to traders.<sup>59</sup>

Article 968 delimits the scope of Ethiopian Bankruptcy law:

*The provisions of this Book (i.e. Book V) apply to any trader within the meaning of Article 5 of this Code and to any commercial business organization within the meaning of Article 10 of this Code with the exception of joint ventures.*<sup>60</sup>

A cursory reading of Article 968(1) would show that Book V of the Commercial Code is narrower in scope of application than other provisions of the Code. As far as individual traders are concerned, Book V is co-extensive with the scope of the Commercial Code itself. All traders as defined by Article 5 of the Commercial Code

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<sup>56</sup> In this connection, the first drafter writes "The different laws of bankruptcy have many points in common. ... Moreover, they can trace their history to common historical sources, among which the practices of the mercantile cities of Northern Italy..." See, Escarra, Book V: Expose des Motifs (2 September 1954), in Winship, Supra Note 12, p. 105

<sup>57</sup> These countries include Germany, Austria, Japan, the USA and Canada; see Encyclopedia Britannica, supra note 43; although these countries extend the status of bankruptcy to all persons, it does not mean that the specific rules of bankruptcy are the same across the board for all classes of persons; see also UNCITRAL, Supra Note 10, P. 38

<sup>58</sup> It is interesting to note that France, responsible in the past for trader-only regimes of bankruptcy, now extends its bankruptcy regimes to all persons even if they are not traders; Article L620-1 of the French bankruptcy law states: "The safeguard procedure shall apply to traders, persons registered with the craftsman's register, farmers, other persons running an independent professional activity, including an independent professional person with a statutory or regulated status or whose designation is protected, as well as private-law entities." See also Article L631-2 and Article L640-2 of the French Commercial Code, which provide for similar rules. See also, Encyclopedia Britannica, Supra Note 43

<sup>59</sup> The drafter was fully aware of this distinction on the scope of bankruptcy laws. For instance, he writes "...the Germanic and Anglo-Saxon countries (Germany, England, USA) extend the rules of bankruptcy to all debtors, while the Latin countries (Argentina, Belgium, Brazil, France, Italy, Spain) apply bankruptcy only to traders." Nonetheless, he chose a trader-only regime of bankruptcy for Ethiopia; see Winship, Supra Note 12, P. 100

<sup>60</sup> Article 1155 (1) repeats Article 968 for business organizations. The drafter repeated this probably for emphasis. A separate title is reserved to provide for special provisions applicable to business organizations, and that is how the repetition came about. If a separate title were necessary, a repetition would be necessary; see Title V of Book V, Articles 1154-1165 of the Commercial Code.

are subject to the provisions of bankruptcy, i.e., may be declared bankrupt. When it comes to business organizations, however, there are limitations. Article 968(2) has explicitly excluded 'joint ventures' from its applications. In addition, Article 968(1) uses the phrase 'commercial business organization,' which would obviously mean that non-commercial business organizations<sup>61</sup> are excluded, however viewed they may be. Business organizations assume the mantle of 'commercial' organization for either of two reasons,<sup>62</sup>

- i) *if they carry on activities specified in Article 5 of the same Code or if their memorandums of association indicate that as their objective*
- ii) *if they are organized as private limited companies or share companies;*

Businesses organized as private limited companies and share companies are always subject to bankruptcy, regardless of the objectives for which they are established. It does not matter that their objectives do not fall under the list under Article 5 of the Code. If a business is organized as one of the three other forms of business organizations (ordinary partnership, general partnership, and limited partnership), the question of whether the business organization in question is subject to the provisions of bankruptcy will turn on whether the business organization is engaged in activities listed under Article 5 of the Commercial Code or its memorandum states this as the objective of the firm. Non-commercial business organizations (sometimes called civil business organizations) may be covered by the other provisions of Commercial Code, but not Book V of the Code.

The Commercial Code is surprisingly (and perhaps unwittingly) vague about the status of civil business organizations. Article 10 of the Code talks about commercial business organizations, suggesting that there are "non-commercial" business organizations. It even prescribes that private limited companies and share companies are always commercial business organizations, whatever their objectives. Article 213 of the Code provides that any of the business organizations recognized by the Code may be a commercial business organization except for an ordinary partnership. For some reason, the upshot of Article 213 is that ordinary partnerships are prohibited from carrying on activities under Article 5 of the Code<sup>63</sup> or they are no longer named ordinary partnerships when they do so. By a process of exclusion, other business organizations (i.e., general partnerships and limited partnerships) may carry on activities other than those listed in Article 5 in which case they acquire the status of 'non-commercial' business organizations. The Commercial Code says very little about how non-commercial business organizations are regulated and which rules of the Commercial Code (if any) apply to them,

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<sup>61</sup> The distinction between civil and commercial business organizations is not unique to the Ethiopian Commercial Code; See Seyed M. Hosni, Commercial and Civil Companies in UAE law, Arab Law Quarterly, Vol. 7, No. 3 (1992), pp 159-174

<sup>62</sup> See Article 10 of the Commercial Code

<sup>63</sup> See Everett Goldberg, J. Eth. L., Vol.8, No.2 (1972), pp 500-501

Incidentally, the 1933 Law of Business Organizations is much clearer in this regard than the Commercial Code. First of all, it is explicit in its reference to civil business organizations.<sup>64</sup> It devotes a separate title to this form of business organizations.<sup>65</sup> Secondly, it regulates the rights and obligations of partners, and fixes their liabilities.<sup>66</sup> In view of this, it is a little surprising that the Commercial Code leaves much to be desired in its distinction of commercial business organizations from non-commercial ones.

## 4.2 Bankruptcy and Banking Business

Once the general scope of a bankruptcy law is settled, the next issue is whether the rules of bankruptcy should apply uniformly to all traders or whether there is a need for special treatment of certain classes of traders. Neither Article 968 nor Article 1155 of the Commercial Code addresses this issue.<sup>67</sup>

One of the sectors which have often required special treatment in some countries is banking.<sup>68</sup> There is no uniformity in the approach of bankruptcy regimes towards banks. Some countries (e.g. the USA) have developed a special law of bankruptcy for banks, removing banks from general regime of bankruptcy completely.<sup>69</sup> Many countries (notably those in Europe), however, have not gone so far as developing special rules of bankruptcy for banks.<sup>70</sup> Instead, these countries have developed special rules of banks which apply as supplements or exceptions to the general rules of their bankruptcy law. In other words, in these countries, the general rules of bankruptcy apply to banks so long as the general rules are compatible with the special rules of

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<sup>64</sup> See Title II of the 1933 Law of Business Organizations, Articles 20-31.

<sup>65</sup> *Ibid*

<sup>66</sup> See, for example, Article 20 of the 1933 Law which states "Members of a civil business organization are jointly and severally liable for the debts regularly contracted by the business organization."

<sup>67</sup> There is no evidence that the drafters were concerned about traders requiring special treatment during bankruptcy. In all likelihood, the drafters intended Book V to apply to all classes of traders, without any privileges or dispensations.

<sup>68</sup> A variety of arguments have been put forward in support of special regimes of bankruptcy for the banking sector. Banks deserve special treatment because they 'typically hold highly liquid liabilities in the form of deposits repayable on demand' and 'long term loans' which, unlike the deposits, are not easily and immediately convertible into cash, resulting in a mismatch of maturity. A crisis of confidence, which may be set off by a rumor, can result in massive withdrawal of deposits, causing liquidity shortfalls. In addition, banks 'perform financial services that are fundamental to the functioning of an economy' by extending credit, taking deposits and processing payments. In many countries, banks are the primary source of liquidity for most financial and non-financial institutions. Lastly, banks are the 'transmission belt' for the implementation of monetary policy. For arguments for or against special dispensations for the bankruptcy of banks, see Eva Hupkes, *Insolvency – why special regime for banks?* in *Current Developments in Monetary and Financial Law*, Vol. 3, Pp. 2-4; See also UNCITRAL, *Supra* Note 10, pp 40-41

<sup>69</sup> See Eva Hupkes, *Insolvency – why special regime for banks?*, in *Current Developments in Monetary and Financial Law*, Vol. 3, p. 8

<sup>70</sup> See *Ibid*, p. 7; Under Italian Law, for example, the Italian banking law sets forth several special rules for bank insolvency while the provisions of the Italian bankruptcy law continue to apply 'in so far as they are compatible' with the banking law. The same obtains in Norway, see *ibid*.

bankruptcy set forth in their banking laws. There are also countries, for example the UK, where no special dispensation is available to the banking sector. The UK treats banks like any other business for bankruptcy purposes.<sup>71</sup>

While this article was being readied for publication, the Banking Business Proclamation which was in force since 1994<sup>72</sup> was repealed and replaced by a new Banking Business Proclamation (No. 592/2008), with far reaching implications for bankruptcy. The Banking Business Proclamation that was just repealed contained few provisions addressing the bankruptcy of banks, leaving several issues of bankruptcy to the general law of bankruptcy in Book V of the Commercial Code.<sup>73</sup> If the comments of this article were to draw upon or stick to the trajectory of the repealed Proclamation, they would (as they should) be relegated to a mere historical relic, such is the extent of the change in the area of bankruptcy of banks as a result of the new Proclamation. The repealed Proclamation's approach would have placed Ethiopia among a group of countries which subject banks to the general rules of bankruptcy save for a few special rules contained in banking business laws.

All that is history now. By virtue of the new Banking Business Proclamation, Ethiopia can now stake a claim to having a special bankruptcy law for banking business, superseding and overriding the general rules of bankruptcy in the Commercial Code. The New Proclamation devotes a whole part to what it calls 'Revocation of License, Receivership and Liquidation.'<sup>74</sup>

The new Banking Business Proclamation breaks with the Commercial Code not just in substance but even in the very terms it uses. Instead of the terms 'bankruptcy', or 'schemes of arrangement', 'liquidation' and 'receivership' are used. In stead of the term 'trustee' for a person who manages a bankrupt business, we have a 'receiver' to manage a bank in bankruptcy.<sup>75</sup> The institution of 'commissioner,' which incidentally is an important office in general bankruptcy proceedings, does not even get a nod in the new Banking Business Proclamation (in all likelihood, it is abrogated). The National Bank of Ethiopia appears to have taken the place of the 'Commissioner.'<sup>76</sup>

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<sup>71</sup> Eva Hupkes, *Supra* Note 69, p. 7

<sup>72</sup> Licensing and Supervision of Banking Business Proclamation No. 84/1994 (repealed)

<sup>73</sup> The repealed Proclamation required prior notice to be given to the National Bank of Ethiopia before bankruptcy proceedings were initiated against a bank. In addition, the National Bank is authorized to appear before the court hearing the case and petition for bankruptcy to safeguard the interests of creditors. The National Bank also recommends a liquidator (trustee) for the bank in times of bankruptcy; see Article 26 of the now repealed Proclamation No. 84/1994.

<sup>74</sup> Proclamation No. 592/2008 has nine parts, and 61 Articles. Of this, Part Eight (the part dealing in part with bankruptcy of banks), contains sixteen articles (Articles 32-48).

<sup>75</sup> See Article 33 of the Banking Business Proclamation No. 592/2008

<sup>76</sup> See Article 34(1) of Banking Business Proclamation No. 592/2008



The new law appears to have broken a new ground in the details with which it deals with bankruptcy of banks. The Proclamation lays down rules for commencement of 'receivership' proceedings, thus replacing a cartload of Commercial Code provisions pertaining to commencement of bankruptcy, composition and schemes of arrangement (Articles 1071, 1072, 1081, and 1119, among others).<sup>77</sup> The Proclamation provides for rules regarding 'parties responsible for receivership proceedings' involving banks, thus replacing Articles 989-1003 of the Commercial Code.<sup>78</sup> The Proclamation lays down special rules for the 'suspect period' and fixes the fate of transactions concluded during this period, thereby replacing the Commercial Code provisions in this regard (for example, Articles 1029-1034). The Banking Business Proclamation also lays down rules for submission and settlement of claims, priority of claims, and conclusion of receivership proceedings involving a bank, essentially superseding Articles 1041 to 1118 of the Commercial Code.

The new Banking Business Proclamation has even changed the trajectory of bankruptcy proceedings under the Commercial Code. Continuation of banking business, as opposed to its liquidation for distribution of proceeds among creditors, is of utmost importance under the new Banking Business Proclamation. The 'receiver' is directed by the Proclamation to 'continue the operation of the bank' when the 'bank is viable' and 'return [the bank] to the previous owners or to previous owners and other partners'.<sup>79</sup> Liquidation is clearly a measure of last resort, something which appears to reverse the overall tone of the general bankruptcy law under the Commercial Code.

After all the special rules of bankruptcy involving banks, it is a little surprising that there is still an allowance made for the application of the Commercial Code. In Article 48 of the Proclamation, it is stated that the 'Commercial Code and other laws will remain applicable in so far as they are not inconsistent with the provisions of Part Eight of the Proclamation. Frankly, this is a 'just-in-case' provision. It is difficult to conceive what rules of Book V of the Commercial Code remain unscathed after the extensive regulation of bankruptcy involving banks in the new Banking Business Proclamation. It would be fair to conclude now that Ethiopia has a special bankruptcy regime for banks. Recourse to Book V of the Commercial Code is still open (courtesy

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<sup>77</sup> Insolvency is one among the seventeen grounds for commencement of receivership proceedings against a bank. Some of the other grounds include revocation of banking license, substantial dissipation of assets, involvement (of a bank) in a pattern of unsafe and unsound practices, refusal to submit books of accounts to inspection, failure to meet minimum capital requirement of the National Bank, and undercapitalization; see Article 33(1) of Proclamation No. 592/2008.

<sup>78</sup> The parties responsible in cases involving receivership of banks being the 'receiver', the National Bank of Ethiopia, an advisor or expert appointed by the receiver, certain creditors, shareholders and of courts; See Articles 39-46 of the Proclamation No. 592/2008; the parties responsible in ordinary bankruptcy proceedings are the trustee, the commissioner, the court, creditors, and sometimes the debtor; see Articles 989-1003, for example.

<sup>79</sup> See Article 40(1) of Proclamation No. 592/2008

of Article 48 of the new Proclamation), but recourse would in most instances be unnecessary.

### 4.3 Bankruptcy and Public Enterprises

The final question regarding the scope of Book V of the Commercial Code is its applicability to public enterprises.<sup>80</sup> Public enterprises are primarily regulated by a special law<sup>81</sup> and secondarily by the Commercial Code. The special law regulating public enterprises provides that they are subject to the rules of the Commercial Code.<sup>82</sup> But by virtue of the special law, public enterprises exhibit certain special features that their private counterparts do not have. Unlike their private counterparts, for instance, public enterprises are invariably established not by a memorandum of association but by regulations.<sup>83</sup> They are wholly owned by the state and the composition of their board is determined not according to the rules of the Commercial Code but by the special law.<sup>84</sup>

After all these special rules, it may come as a surprise that bankruptcy is one of the subjects in which the special law defers to the Commercial Code. It seems that public enterprises are spared nothing in this regard. The Public Enterprises law says the provisions of Book V of the Commercial Code shall apply, *mutatis mutandis*, to the winding up of public enterprises.<sup>85</sup> In the same law, bankruptcy is stated as one of the grounds for dissolution of public enterprises.<sup>86</sup> The only notable exception made is that the court may pursue 'summary procedure' (sometimes also known as 'simplified bankruptcy procedure' or 'petty bankruptcy') regardless of the value limitation stated in Article 1166 (1) and (2) of the Commercial Code.<sup>87</sup>

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<sup>80</sup> The applicability of bankruptcy proceedings to state enterprises should be restricted to state enterprises which compete in the market as distinct economic or business operations and otherwise have the same commercial and business interests as privately owned enterprises. This would exclude administrative agencies of governments, sub-national governments, and municipalities. See, UNCITRAL, *Supra* Note 10, P. 40

<sup>81</sup> See Public Enterprises Proclamation No. 25/1992

<sup>82</sup> See Art. 4 of Public Enterprise Proclamation No. 25/1992

<sup>83</sup> See Article 6 of Public Enterprises Proclamation No. 25/1992

<sup>84</sup> See Article 12 of Public Enterprises Proclamation No. 25/1992; The general assembly of workers have the right to elect up to one-third of the directors of the Board. The rest of the Board is appointed by the supervising authority; Article 12(20) of Public Enterprises Proclamation No. 25/1992. This is contrasted with the rule in the Commercial Code which permits only members of the company (shareholders) to be directors of the Board; See Article 347(1) of the Commercial Code.

<sup>85</sup> Article 40 of Proclamation No. 25/1992

<sup>86</sup> See Article 29(6) of Proclamation No. 25/1992

<sup>87</sup> Article 40(2) of Proclamation No. 25/1992; It will be seen that the Commercial Code permits summary bankruptcy proceedings only when the value of assets of the debtor do not exceed one thousand Birr. It is unlikely that any bankruptcy of a public enterprise will ever proceed in a summary proceeding without this exception. This exception is therefore significant although it is not clear when the court will decide a summary proceeding instead of a regular bankruptcy proceeding.

This is as far as the law goes. As any one following the recent history of public enterprises in Ethiopia can observe, the practice has gone a different way. Since 1992, after the country officially adopted an economic policy based on private sector participation, over two hundred public enterprises, big as well as small, have been privatized by the Government.<sup>88</sup> These enterprises have been privatized through the modalities of asset sale, employee and management buy out (MEBO), joint venture with a strategic investor, management contract, competitive sale of shares, restricted tender and negotiated sale.<sup>89</sup> Bankruptcy and schemes of arrangement are conspicuously absent in the list of modalities of privatization. Why did the Ethiopian government not choose the path of bankruptcy in spite of this wave of privatizations in the 1990s and 2000s? The answer to this question should obviously await empirical research, but one thing is certain. The Ethiopian Government has not chosen to abandon even the most troubled public enterprises to the rigors of bankruptcy regime.<sup>90</sup> It cannot be because bankruptcy and schemes of arrangement are devoid of merits. The 'UNCITRAL Guide' clearly favours subjecting public enterprises to bankruptcy regime:

*... insolvency regime has ... the advantages of subjecting them to the discipline of the [Bankruptcy] regime, sending a clear signal that government financial support for such enterprises will not be unlimited and providing a procedure that has a potential to minimize conflicts of interest.*<sup>91</sup>

Whatever may be the merits of the application of bankruptcy regime to public enterprises, we have yet to see Ethiopian Government pursuing bankruptcy options for some of its troubled public enterprises. This is neither for lack of law authorizing such a path, because the public enterprise law explicitly provides for bankruptcy. Nor can it be because the Government tenaciously holds onto public enterprises, for better or for ill, because there is plenty of privatization going on.

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<sup>88</sup> Ethiopia: An Investment Guide to Ethiopia, Opportunities and Conditions, March 2004, P. 10

<sup>89</sup> Ibid.

<sup>90</sup> The privatization drive did not proceed as vigorously as expected, largely because of the (in)capacity of the private sector to absorb large public enterprises offered for sale; for others reasons, see, Ethiopia: an Investment Guide to Ethiopia, Opportunities and Conditions, March 2004, P. 10

<sup>91</sup> UNCITRAL, Supra Note 10, P. 40; It is not all state enterprises that should be subject to bankruptcy proceedings. Exceptions are made for some state enterprises for which the government has 'adopted explicit guarantee in respect of liabilities as part of its shift in the overall macroeconomic policy, such as during large scale privatization' or where the state enterprises are involved in such sensitive sectors of the economy as utilities (electricity and water); ibid.

## V. Commencement Standards

### 5.1 In General

The standard to be met for commencement of bankruptcy proceedings is central to the design of any bankruptcy law.<sup>92</sup> Commencement standard is what sets the process in motion, what charts the path forward for a business in financial difficulties, and what determines, initially at least, the balance of power among the parties involved in bankruptcy proceedings, particularly the creditors vis-à-vis the debtor. The pendulum of bankruptcy may tilt in favor of debtors or creditors depending on the liberality or stringency of a commencement standard.<sup>93</sup>

While it is ultimately upto the law of each country to fix its commencement standards in what ever way it sees fit, commencement standards should be crafted in consideration of the virtues of 'accessibility', 'flexibility' and their capacity to prevent 'improper' use of proceedings.<sup>94</sup> Accessibility is measured by the ease with which all 'stakeholders' can apply for and set bankruptcy proceedings in motion.<sup>95</sup> Flexibility is measured by the types of bankruptcy proceedings available: liquidation of the business, composition, reorganization, and a combination of these.<sup>96</sup> The need to make the proceedings 'accessible' should be balanced against the possibilities of abuse by those bent on using the proceedings for 'improper' motives, for example, to twist the hand of the debtor or quite simply cause the debtor embarrassment. Commencement standards may be used by debtors, who are not really in financial straits, in order to take advantage of 'automatic stay' in a bankruptcy law.<sup>97</sup> They may also be used by creditors to 'disrupt the debtor's business' and 'gain competitive advantage'.<sup>98</sup> The standards should therefore be crafted so as to prevent both debtors and creditors from using the bankruptcy regime for motives other than collection of debts.

The 'UNCITRAL Guide' identifies two types of formulations in establishing conditions for commencement of bankruptcy proceedings against debtors:<sup>99</sup> the 'liquidity, cash flow or cessation of payments' test, and the 'balance sheet' test.

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<sup>92</sup> UNCITRAL, Supra Note 10, p 45

<sup>93</sup> It should, however, be noted that a commencement standard, while important, is not the only factor for characterizing a bankruptcy regime as either 'debtor-friendly' or 'creditor-friendly,' or something in between.

<sup>94</sup> UNCITRAL, Supra Note 10, P. 45

<sup>95</sup> Ibid

<sup>96</sup> Ibid

<sup>97</sup> Ibid

<sup>98</sup> Ibid

<sup>99</sup> Ibid, Pp 45-47

## 5.2 'The Liquidity, Cash Flow, or Cessation of Payments' Test

The first, and most extensively used commencement standard is variously called 'liquidity' or 'cash flow' or 'cessation of payments' test. This test allows parties to apply for bankruptcy proceedings based on evidence of inability of a debtor to pay debts as they fall due. In other words, bankruptcy proceedings may be set in motion when a debtor 'has generally ceased making payments and will not have sufficient cash flow to service existing obligations as they fall due in the ordinary course of business.'<sup>100</sup> The cessation of payments may relate to outstanding 'rents, taxes, salaries, employee benefits, trade accounts payable or other essential business costs.'<sup>101</sup>

The 'cessation of payments' test is obviously a liberal standard, particularly when it is viewed from the vantage point of creditors. Bankruptcy proceedings are triggered upon simple evidence of suspension of payments by the debtor. It is maintained that the liquidity test has two principal advantages:<sup>102</sup>

1. It puts the factors that trigger bankruptcy within the reach of creditors as the facts constituting grounds for initiation of bankruptcy are fairly accessible and within the reach of creditors; and
2. It activates proceedings early thereby minimizing the risks of dissipation of assets by the debtor in collusion with creditors;<sup>103</sup>

The 'liquidity' or 'cash flow' or 'cessation of payments' test has been appropriately called a creditor-friendly test, and included in some laws with the interest of creditors in mind. It is not, however, without criticism. Those who disapprove of the test argue that the test, so easily established, might instigate bankruptcy proceedings against otherwise healthy businesses upon what they call a 'false signal' of mere suspension of payments.<sup>104</sup> Critics of the test point out that the test makes it easier for creditors to initiate bankruptcy proceedings against debtors solely on grounds of 'temporary cash flow or liquidity problem.'<sup>105</sup> As a creditor-friendly test, there is a fear that the test might lend ammunition to creditors bent on using bankruptcy proceedings as 'debt enforcement' scheme<sup>106</sup> or twisting the arm of debtors using the threat of bankruptcy proceedings.

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<sup>100</sup> Ibid, P 45-46

<sup>101</sup> Ibid, P 46

<sup>102</sup> Ibid

<sup>103</sup> There is a natural propensity by the debtor or other creditors to act irresponsibly after suspension of payments; the debtor may engage in risky activities or creditors may want to arrogate special privilege to themselves to the detriment of other creditors, hence dissipation of assets. For a detailed analysis of the objectives of bankruptcy, see UNCITRAL, *Supra* Note 10, p 46

<sup>104</sup> UNCITRAL, *Supra* Note 10, p 46

<sup>105</sup> Ibid

<sup>106</sup> Ibid, p 45

### 5.3 the 'Balance Sheet' Test

The second type of commencement standard, adopted by some countries, requires a more rigorous test for commencement of bankruptcy. It is called the 'balance sheet' test.<sup>107</sup> The 'balance sheet' test requires whoever wishes to commence bankruptcy proceedings to 'show an excess of liabilities over assets.'<sup>108</sup> Mere suspension of payments by the debtor is not enough. The burden is upon the person applying for bankruptcy to show that the debtor has not only ceased payments but also that the debtor's balance sheets show an excess of liabilities over its assets. This often forces an applicant to hire 'an expert who reviews books, records and financial data to reach a determination of the fair market value of the business' of the debtor.<sup>109</sup> The merit of this test, which is debtor-friendly, is that bankruptcy proceedings are not initiated against a debtor solely on grounds of cessation of payments. The test is also an accurate reflection of the debtor's financial status and prevents commencement of bankruptcy proceedings upon false signals of temporary cash shortfalls.<sup>110</sup>

The 'balance sheet' test has however been criticized for putting the commencement standards beyond the reach of most creditors.<sup>111</sup> It 'relies on information under the control of the debtor' and it 'is rarely possible for other parties to ascertain the true state of the debtor's financial affairs until the difficulties have become irreversible.'<sup>112</sup> Ascertainment of an excess of liabilities over assets of the debtor takes time. Delays are inevitable from the involvement of an expert to establish an excess of liabilities over assets.<sup>113</sup> In addition, critics of the 'balance sheet' test charge that the test is unfair to small businesses and other businesses already mired in cash shortfalls. It imposes an onerous burden upon these businesses to hire experts, who may be both hard to find and afford.<sup>114</sup>

To many people, the balance sheet test might seem more accurate than the cessation of payments test, but it too can give a misleading indication of the debtor's financial situation.<sup>115</sup> The valuation method used in a particular case may yield different numbers depending on whether the liquidation value or going concern value of the business is taken into account.<sup>116</sup> The accounting standards and valuation techniques

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<sup>107</sup> Ibid, P 46; German bankruptcy law is often cited as an example of the balance sheet test. In Germany, a debtor is over-indebted when the value of his liabilities exceeds the value of its assets. The value of assets is ascertained by a reference to a prevailing market value; See Julian R. Franks, Kjell G. Nyborg and Walter N. Torous, A Comparison of US, UK and German Insolvency Codes, *Financial Management*, Vol. 25, No. 3, 1996, p. 92

<sup>108</sup> UNCITRAL, *Supra* Note 10, P 46

<sup>109</sup> Ibid

<sup>110</sup> Ibid

<sup>111</sup> Ibid

<sup>112</sup> Ibid

<sup>113</sup> Ibid, P 47

<sup>114</sup> Ibid, P 46

<sup>115</sup> Ibid

<sup>116</sup> Ibid

may produce results that do not reflect the fair market value of a debtor's assets. Besides, the market for some assets may not be sufficiently developed or stable to enable the fair market value of a business to be established.<sup>117</sup>

Classification is often a ploy employed for illuminating certain standards. The purity of tests that classifications project is not to be found in the actual laws on the ground. Cognizant of the strengths and weaknesses of the two tests above, some countries have opted to use both tests in different combinations.<sup>118</sup> In those countries which mix both tests to establish conditions for commencement of bankruptcy, a party applying for bankruptcy must show that 'the cessation of payments by a debtor reflect difficult financial situations that are not temporary.'<sup>119</sup> These systems, called 'intermediate' approaches, have not avoided criticisms either. The intermediate approaches have been criticized because they too cause 'delay, uncertainty and expense' in the commencement of bankruptcy proceedings.<sup>120</sup>

As all the tests in existence have been criticized for one defect or another, it seems that there is no perfect test of commencement of bankruptcy out there. Each country should adopt a test that best mirrors its business environment, in particular based on the availability of expertise for establishing some facts and the information that is accessible to a community of creditors.

#### **5.4 Commencement Standard under Ethiopian Law**

Where does Ethiopian law fit in all this? Article 969 states the basic rule. It provides: "Any trader who has suspended payments and has been declared bankrupt shall be deemed to be bankrupt." Article 969 lays down two conditions for commencement of bankruptcy. First, a trader should suspend payments. And secondly, the trader should be declared bankrupt. Let's deal with the second condition first. The second condition is inserted to prevent labelling debtors as 'bankrupt' solely on grounds of 'suspension of payments.' Only a court that has jurisdiction to adjudicate bankruptcy<sup>121</sup> has the authority to first establish 'suspension of payments' and then declare the debtor 'bankrupt.' Ethiopian law calls mere suspension of payments without declaration by court of bankruptcy 'bankruptcy in fact.'<sup>122</sup>

The law emphasizes importance of the declaration by court in Article 970(1) which provides: "Where no judgment in bankruptcy is given, bankruptcy 'shall not result from mere suspension of payments' (Emphasis mine)

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<sup>117</sup> Ibid

<sup>118</sup> See Ibid, Pp 47-48

<sup>119</sup> Ibid, P 47

<sup>120</sup> Ibid, P 47

<sup>121</sup> See Art. 974 of the Commercial Code

<sup>122</sup> See Art. 970 of the Commercial Code

Bankruptcy has far-reaching legal and factual consequences upon the business of the debtor, and the cumulative requirement of suspension of payments and declaration by court of the bankruptcy of the debtor should be seen as a protection of the rights and interests of debtors who have suspended payments.<sup>123</sup> Only a court having jurisdiction can give its imprimatur to the bankruptcy of debtors and all the consequences that ensue from declaration of bankruptcy.<sup>124</sup>

Bankruptcy in fact or factual bankruptcy or mere suspension of payments does not have any legal consequences except in one case.<sup>125</sup> The exception is provided in Article 970(2). A criminal court may pass conviction and impose sentence upon the debtor or others involved in bankruptcy 'in respect of bankruptcy or any offense connected with bankruptcy notwithstanding that the suspension of payments has not been established by a judgment in bankruptcy.'<sup>126</sup> A debtor may, for instance, be convicted and fined or face simple imprisonment, where he/she has 'intentionally concealed the fact that he is insolvent and contracts an obligation knowing that he is unable or unwilling to execute it.'<sup>127</sup> A criminal division court, before which a case is pending, does not have to wait for a bankruptcy court before it passes a criminal conviction and sentence.

### 5.5 When is there 'Suspension of Payments'?

A court which passes a judgment of bankruptcy should establish that there is a 'suspension of payment' by the debtor. What is, and more precisely, when is there a 'suspension of payments'? Article 971 describes the facts constituting 'suspension of payments' in the widest construction possible. It reads: 'Suspension of payments shall result from any fact, act or document showing that the debtor is no longer able to meet the commitments related to his commercial activities' (Emphasis mine).<sup>128</sup>

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<sup>123</sup> Depending on the gravity of the particular bankruptcy, the dire consequences of bankruptcy may include the loss and liquidation of the debtor's assets, criminal penalties and loss of civil rights.

<sup>124</sup> On court jurisdiction in bankruptcy, later

<sup>125</sup> 'Bankruptcy in fact', 'factual bankruptcy', 'mere suspension of payments' or 'insolvency' are interchangeably used to refer to inability to meet liabilities without or before the declaration by bankruptcy by court.

<sup>126</sup> For offenses connected with bankruptcy or suspension of payments, see Arts 725-731 of the New Criminal Code of 2004

<sup>127</sup> See Article 725 of the New Criminal Code of 2004

<sup>128</sup> It is interesting to contrast the generality of the terms used in Article 971 to describe 'suspension of payment' with the Anglo-American tradition of enumerating what are known as 'acts of bankruptcy.' In the Anglo-American tradition, it has been customary to list acts of debtor which might, as it were, raise presumption of suspension of payment. They are conditions precedent for any party to initiate bankruptcy proceedings against a debtor. These acts include 'a transfer with actual intent to hinder, delay, or defraud, or one which leaves the debtor with an unrealistic small amount of capital,' 'failure to discharge a lien by legal proceedings within a reasonable time,' 'equity receivership,' 'a general assignment for the benefit of creditors,' 'an admission by the debtor of an inability to pay his debts,' 'failure to discharge judgment within a reasonable time.' In continental systems, the standard is to allow creditors to initiate bankruptcy proceedings so long as the debtor is unable to pay his debts as



Standing alone, Article 971 would seem to permit the commencement of bankruptcy proceedings upon submission (to the judgment of the Court) of 'any facts, acts, or documents' that show the debtor is no longer able to meet the commitments related to his commercial activities. Just what might these 'facts, acts, or documents' be? Are the facts in the following hypothetical examples sufficient to have a debtor declared bankrupt? Are they even relevant in an application for bankruptcy?

Example 1:

ABC S.C., an import/export company, has failed to pay outstanding tax due to the Federal Inland Revenue Authority. It has been in arrears for one year of tax due (including penalties and fines).

Example 2:

XYZ S.C., a manufacturing company, has been involved in some reckless activity lately. Not only has the company entered into a multimillion supply contract with a foreign company of dubious background, its management has also been suspiciously raising the salary of senior management and the fees of the board members, and generously donating money to so many causes in just one year.

Example 3:

The general manager and deputy manager of NOP Company, engaged in construction business, have absconded to a foreign country and sought asylum in that country, after questions have been raised about their style of management and their extravagant personal lifestyle. After they have absconded, the Federal Ethics and Anti-corruption Commission filed a criminal charge against the general and deputy manager of NOP Company.

Example 4:

Mr. X, the sole proprietor and executive manager of a well-known supermarket in Addis, has lately taken steps to disassociate himself from the active management of the supermarket, by allowing his two sons and wife to take over, citing illnesses.

The acts of the debtors in the above hypothetical examples may raise the suspicion of creditors. But are they the 'facts, acts or documents' Article 971 talks about?

Members of the Drafting Commission anticipated that the construction of Article 971 might give rise to problems of interpretation, but the first drafter was not troubled by it, as the following statements of his attest. In the Background Documents of the Commercial Code edited and translated by Peter Winship, we read:

*Mr. Roberts (then president of the High Court) asked if...the acts of bankruptcy were enumerated as is done in the English Law. Mr. Escarra*

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they mature. For critical analysis of the 'acts of bankruptcy', see Notes, "Acts of Bankruptcy" in Perspective, Harvard Law Review, Vol. 67 (1954), pp. 500-508.

*replied that the enumeration of specific acts was not of any practical significance, because the phrase "suspension of payment" ... is broad enough to include all specific acts.*<sup>129</sup>

Further down we read:

*When asked by Mr. Roberts if a judgment of execution would be considered as a case of suspension of payments, Mr. Escarra (the drafter) stated that the adjudication of bankruptcy is left to the court to decide because each case presents different facts... it is for court to rule whether one act or series of acts is necessary for adjudication of bankruptcy.*<sup>130</sup>

In order to put the responses of the drafter in context, one needs to review the two approaches he refused to adopt for the Commercial Code of 1960: the commencement standard under the 1933 bankruptcy law and the Anglo-American approach. As quoted previously, the 1933 law set a rather restrictive commencement standard for initiation of bankruptcy proceeding. Article 2 of that law states: "A suspension of payments exists when the debtor does not pay an obligation which he has by virtue of an executory document (titre exécutoire)."

Under the 1933 Bankruptcy Law, only obligations evidenced and supported by executory documents entitle the creditor to apply for bankruptcy. And these documents are exhaustively listed under Article 2 of that law. The drafter was probably aware of this law (which he thought constricting) but he was reluctant to adopt a similar approach for the Commercial Code of 1960.

In addition, the drafter was reluctant to adopt the Anglo-American tradition of listing what are known as 'acts of bankruptcy.' An adoption of the Anglo-American tradition of enumerating 'acts of bankruptcy' would have produced a provision similar to the 1966 Bankruptcy Act of Australia where a debtor is said to have committed an 'act of bankruptcy' when he:<sup>131</sup>

1. *makes a conveyance or assignment to trustees for the benefit of his creditors generally;*
2. *makes a fraudulent conveyance, gift, delivery or transfer of his property;*
3. *makes a conveyance which would be void as a fraudulent preference if he became bankrupt;*

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<sup>129</sup> Winship, *Supra* Note 12, P. 107

<sup>130</sup> *Ibid.*

<sup>131</sup> See J. Adrian Redmond, *The Commercial Laws of the Commonwealth of Australia*, in the *Digest of Commercial Laws of the World* (1967)

4. *departs from or remains from out of Australia or departs from his dwelling place of business with intent to delay or defeat his creditors;*
5. *if execution has been issued against the debtor under process of a court and any of his property has in consequence either been sold by a Sheriff or held by the Sheriff for 21 days or execution has been issued against the debtor under process of a court and has been returned unsatisfied;*
6. *is adjudged bankrupt in any court of the Queens Dominion within the British Commonwealth having Jurisdiction in bankruptcy;*
7. *consents to present a petition at a meeting of creditors and does not do so within 7 days;*
8. *admits at a meeting of creditors that he is insolvent and refuses to surrender his estate or admits at a meeting of creditors that he is insolvent and having been requested by a resolution of a majority of the creditors to bring his affairs under the Act does not within;*
9. *days present a debtor's petition or make an arrangement with his creditors without sequestration;*
10. *files a declaration of his inability to pay his debts;*
11. *fails to comply with a bankruptcy notice served on him by a creditor who has obtained a final judgment;*
12. *gives a notice to any of his creditors that he has suspended or is about to suspend payment of his debts.*

The approaches of the 1933 Ethiopian law of Bankruptcy and the Anglo-American tradition of listing 'acts of bankruptcy' are similar in form, if not in substance. Both enumerated objectively acts or documents which led to initiation of bankruptcy. The first drafter of the 1960 Commercial Code was reluctant to go down this path, no matter how predictable these approaches felt to the rest of us. In what appears to us nonchalant, the first drafter expressed his reluctance in the following words:

*The circumstances in which bankruptcy can be declared are defined in general terms by the laws of Latin and Germanic countries. In Anglo-Saxon countries, the definition is replaced by a limiting enumeration of acts of bankruptcy. In fact, however, the difference between these two approaches is negligible and refers more to the method than to the substance, because the enumeration in Anglo-Saxon laws covers in*

*practice the same area as that covered by the general definition found in the other countries.*<sup>132</sup>

The first drafter decided to settle with the general phrases of Article 971 (inclining towards the Latin and Germanic systems of the time) because he was convinced that in practice the two systems led to the same conclusions: in both cases debtors were declared bankrupt for similar set of facts.

This approach of the drafter left the issue of 'suspension of payments' wholly to the discretion of the courts. The drafter's reluctance to adopt a limitative language was understandable, to an extent. But it is legitimate to ask whether he was right in reposing so much faith in our courts. And in ceding too much discretion to courts by the construction of such a wide language as Article 971, didn't he perhaps place an unwarranted trust in the wisdom of our courts to make judgments based on the 'facts of each case?'

At the time of writing, more than half a century after the drafter submitted Book V to the Drafting Commission, there is certainly no basis for relying upon the wisdom of courts to determine, based on the facts of each case, whether there is a suspension of payments, as that expression is 'defined in Article 971. The fear is that courts may adjudge a debtor bankrupt solely on grounds of 'facts, acts, or documents' which may cast suspicion on the ability of the debtor to meet commercial commitments. That may turn out to be too hasty a judgment on the part of the court and too costly for the debtor. Whether founded or not, the association of the debtor with bankruptcy can impinge negatively upon the ability of that debtor to freely draw resources from the market in order to continue as a viable business. Bankruptcy has dire consequences for the debtor, such as liquidation of his assets, possible criminal penalties and possible loss of civil rights.<sup>133</sup>

Who is to say that creditors will not apply for improper motives such as to disrupt debtors' business and gain competitive advantage? Although it is less likely, who is to say that debtors themselves may not apply for bankruptcy for improper motives, like to take advantage of 'stay of execution'?<sup>134</sup> It is in view of these dangers that one hoped the drafter would have thought twice before giving that much discretion to the courts to establish 'facts, acts, or documents' constituting suspension of payments.

In fairness to the drafter, however, it must be said that the adoption of such a general phraseology in Article 971 is not entirely without merits. Such a general language would permit courts to calibrate the commencement of bankruptcy proceedings to as

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<sup>132</sup> Escarra, Book V: Expose des Motifs (September 2, 1954), in Winship, *Supra* Note 12, p. 101

<sup>133</sup> Encyclopedia Britannica, *Supra* Note 43

<sup>134</sup> Given the punitive attitude of Ethiopian bankruptcy law, it will be foolhardy for any debtor to apply for anything other than for proper motives of equitable treatment of creditors and possible reliefs through composition and schemes of arrangement.

widely divergent situations as one can expect from the cases that might come before the courts. It would allow parties, especially creditors, to petition for institution of bankruptcy proceedings based on 'facts, acts or documents' that establish that the debtor is 'no longer able to meet his commercial commitments', in the process forestalling possible dissipation of assets. It is a language wide enough to embrace all sorts of factual situations that indicate the inability of the debtor to pay its commercial liabilities.

What is provided for in Article 976 might help to temper the fears expressed in connection with the language of Article 971. Article 976 authorizes (but does not require) the court to conduct what it calls 'preliminary investigation.' The court may appoint a 'judge for the purpose of investigating into the affairs and activities of the debtor.'<sup>135</sup> The judge may also be assisted by a trustee for purposes of establishing whether there is a suspension of payment by the debtor.<sup>136</sup> Although the professional competence of judges, as we know them, in ascertainment of 'suspension of payments' is doubtful, there is no question here that these additional rules in the bankruptcy law are intended to ensure that courts rely on actual facts to adjudge a person bankrupt.<sup>137</sup>

The courts should not be deceived by the generality of Article 971, and should rely on the language of Article 976 in all but too obvious cases of suspension of payments.<sup>138</sup> The judgment of bankruptcy should be the result of careful investigation of the real situation facing the debtor and full appreciation of the implications and consequences of an adjudication of bankruptcy. Any erroneous adjudication of an otherwise viable business should be avoided by the liberal use of the investigative power under Article 976. Courts which use their discretion under 976 in all situations but the few obvious cases would certainly fulfil the trust laid upon them by the drafter.

Based on the generality of the phrase used in Article 971 of the Code, there can be little doubt about where Ethiopian commencement standard should be classified. Article 971 puts Ethiopia among those countries which pin commencement of bankruptcy upon 'shortage of cash' or 'liquidity problem.' This position of Ethiopian law is strengthened by Article 972, which requires debtors to notify court of 'suspension of payments' within fifteen days of the suspension.

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<sup>135</sup> Article 976(1) of the Commercial Code

<sup>136</sup> Article 976(2) of the Commercial Code; the practicality of assistance by trustee is doubtful, for at this stage, the Court has not yet appointed a trustee; unless the drafter had in mind what is elsewhere known as 'interim trustee.'

<sup>137</sup> Ascertainment of suspension of payments may require financial expertise to examine balance sheets of the debtor. Judges are professionally qualified to read and interpret balance sheets and other financial statements.

<sup>138</sup> Ato Tamiru Wondimagegnehu (who served as a judge during Imperial times) told me that the court required the balance sheet of four preceding years before it adjudged a business bankrupt; conversation with Ato Tamiru Wondimagegnehu, November 28, 2008

An easy access to bankruptcy proceeding based on cessation of payments is justified by the reality of Ethiopian business environment. The recent surge of business activities notwithstanding, Ethiopia's business environment is still undeveloped. We do not as yet have general disclosure requirements in our laws. The activities of many businesses (even the big companies) are still shrouded in secrecy. Information regarding the financial situations of most businesses is not available in the public domain. Ethiopia does not have a stock exchange market, which would have allowed the general public to access some financial information about companies that operate in the stock market. Even if these types of information were available, the country has neither the know-how nor the resources to process and analyze financial information. All these realities about the country militate against the adoption of the so-called 'balance-sheet' test, however accurate that test might appear.

The statement that Ethiopian bankruptcy law adopts 'cessation of payments' as a commencement standard needs some qualification. Sub-article (1) of Article 973 requires the debtor giving notice under Article 972 to annex some documents to his notice. These documents, when they are available at the time of notice, include the 'balance sheet,' 'the profit and loss account' and the 'lists of commercial credits and debts with the names of the creditors and debtors.' Why would the law require the submission of these documents by the debtor were it not for helping the court base its judgment not just upon mere suspension of payments but upon what the balance sheet and the profit and loss accounts of the debtor show?<sup>139</sup>

There is no escape from the conclusion that these documents are required as additional commencement standards, although Ethiopian reality would not permit adoption of the balance-sheet test in its rigorous form. And the mild requirement of 'preliminary investigation' by a 'judge' aided by the trustee would strengthen the view that Ethiopian law inclines towards the 'intermediate test' of combining the 'liquidity test' with the 'balance sheet' test. However, Ethiopian law takes no firm position on commencement of bankruptcy. It all depends on the disposition of the court in a particular case. The court may declare a person bankrupt based on simple evidence of suspension of payments. The court is also at liberty to require additional evidence, like the balance sheet of the debtor. It would therefore be safe to conclude that the Commercial Code permits both liquidity test and the intermediate test in equal measure.

### **5.6 Why Notify Court of 'Suspension of Payments'?**

In thinking about commencement standards under Ethiopian bankruptcy law, we should distinguish two situations. One is the requirement of 'notification' under Article 972 of the Commercial Code and the other is the 'institution' of bankruptcy

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<sup>139</sup> These documents have a utility beyond establishing the seriousness of suspension of payments; they might help the court fix the date of suspension of payments, which, as shall be seen later, is important for determining the retrospective effect of bankruptcy; see Winship, *Supra* Note 12, p 108

proceedings under Article 975 of the same code. The notice provision of Article 972 imposes a duty upon the debtor to 'notify' or 'inform' the court of the fact of 'suspension of payments.' Article 975, on the other hand, talks about a serious application, with parties listed therein having a categorical intent to commence proceedings of bankruptcy. The notification under Article 972 may or may not lead to commencement of bankruptcy proceedings. The debtor simply states the fact of 'suspension of payments' and submits the notice to the court.

What the court will do with that notice is something we will have to explore. Unfortunately, the language of Article 972 is not much of a help:

*Any trader who suspends payment of his commercial debts shall within fifteen days file a notice to this effect with the registrar of the Court... with a view to the institution of bankruptcy proceedings or the approval of a scheme of arrangement.*

Reading the first part of this provision, one may conclude that the provision is intended merely for the purpose of informing the court of suspension of 'commercial debts.' But reading it up to the end, as one should, one is thrown into a dilemma as to why this provision is inserted in the Code.<sup>140</sup>

There are two possible ways of dealing with Article 972. One way to read it is to understand it as a 'commencement' provision, as surely as Article 975 is. The other way to read it is to understand it as a 'notice' provision, merely intended to 'inform' the court and possibly 'commence' bankruptcy proceedings if and when other facts, showing the seriousness of the problem, are established.

There are words and clauses in Article 972 which support both of the above positions. As the debtor is required to notify the court within 'fifteen days' of suspension of payments, which is clearly too early to say whether the suspension is ripe for initiation of bankruptcy proceedings, one would be taken to task if one were to conclude that Article 972 is a commencement provision. The most liberal of approaches to commencements could not have allowed the commencement of bankruptcy proceedings upon the fact of suspension of payments for just 'fifteen days.' It would clearly be too premature to base the commencement of bankruptcy proceedings upon mere showing of suspension of payments for a period of fifteen days. In a business cycle, fifteen days is too short a period to gauge whether the suspension of payments warrants the commencement of bankruptcy proceedings. In addition, assuming debtors

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<sup>140</sup> By the way, this kind of provision is fairly common in bankruptcy laws of other countries; for example, Article L640-4 of the French Code provides "The Commencement of these [liquidation] proceedings must be requested by the debtor at the latest within forty-five days following cessation of payments...", Louis Vogel and Francoise Perochon, trans., French Commercial Code; similarly Article 25 of OHADA law states "The declaration shall be made within a period of thirty days following the cessation of payments..."; See OHADA, UNIFORM ACT ORGANIZING COLLECTIVE PROCEEDINGS FOR WIPING OFF DEBTS, 1998.

are conscientious about their duties under Article 972, the flood of notifications coming from debtors about suspension of payments would be too overwhelming for the registrar of the court to handle.<sup>141</sup> Every time the registrar receives notice of suspension of payments, it will have to refer the matter to the court for commencement of bankruptcy proceedings.

As the law says little on what the registrar will do with the 'notice of suspension of payments,' we are left to struggle with the real meaning and purpose of Article 972 of the Commercial Code. A suggestion that such 'notice' automatically triggers the commencement of bankruptcy proceedings would be too destabilizing to businesses and too overwhelming for our work-ridden courts. For that reason, the suggestion should be resisted.

The language of Article 972, particularly the last phrase that reads 'with a view to the institution of bankruptcy proceedings or the approval of a scheme of arrangement' complicates our task of properly situating the meaning of the Article. After reading this phrase, one would be tempted to conclude that Article 972 is as much a commencement provision as Article 975. The explanations provided by the drafter in connection with the notice requirement under Article 972 are unfortunately vague. He wrote:

*... the debtor must inform the court as soon as possible about his situation by annexing the documents set out in Article 2 (973) so that the court will be in a position to open proceedings either for bankruptcy or for a scheme of arrangement – latter procedure requiring in addition an express application from the trader in accordance with Article 139(1119).<sup>142</sup>*

The drafter seems to regard the notice requirement as a possible prelude to the institution of bankruptcy or schemes of arrangement. But he says nothing about what the court should do with the notice, and in particular, whether the court should commit the case to either bankruptcy or schemes of arrangement. Nonetheless, there are reasons which urge us not to regard the notice provision as the automatic initiation of bankruptcy. First of all, the Article itself is entitled 'notice of suspension of payments,' which indicates that the purpose of the Article is to serve as a vehicle for 'notification' without attaching the requirement of commencement of bankruptcy proceedings. Secondly, Article 975 lists the debtor as the first party with the vested interest to petition bankruptcy proceedings. If Article 972 were a commencement provision, it would not be necessary to repeat the debtor in Article 975. Thirdly, the short notice period of fifteen days could not have been intended to be a reliable standard for commencement of bankruptcy proceedings. At this stage of the suspension of payments, no one can foresee if the suspension of payments is a temporary shortage of cash or a more serious and permanent problem warranting the commencement of

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<sup>141</sup> The flood of notifications may not materialize as feared, for it depends on the default rate on debts in the market. In times of economic crisis, it may be overwhelming.

<sup>142</sup> See Winship, *Supra* Note 12, p. 107



bankruptcy proceedings. All these reasons and more force us to relegate Article 972 to just a 'notice' provision, not a commencement standard. Having notified the court of suspension of payments 'within fifteen days,' the debtor or other parties indicated in Article 975, will have to decide whether to petition for institution of bankruptcy proceedings. Until then, the notice under Article 972 will just remain what it is: a notice. That does not mean it is unimportant. The notice can be an important source of information for parties listed in Article 975 in order for them to decide whether to institute bankruptcy proceedings.

Instead of asking what the court will do with the notice of suspension of payments, we should perhaps more appropriately be asking what the consequence would be to the debtor of not giving the notice within fifteen days as required by Article 971. As far as Ethiopian bankruptcy law is concerned, it does not make much of a difference whether a debtor has notified the court within fifteen days or not. The rules on discharge in Book V<sup>143</sup> are equally harsh on debtors who notify the court of suspension of payments. There is nothing in these rules to encourage debtors to be conscientious about their obligations to give notice to court. It makes no difference how the bankruptcy came about: discharge is not available because of good behaviour on the part of the debtor.<sup>144</sup> We should therefore not search for clues in Book V itself, for there we will find nothing.

Not giving notice may have consequences under criminal law, though. Article 725 of the New Criminal Code of Ethiopia provides that a debtor who 'intentionally conceals the fact that he is insolvent and contracts an obligation knowing that he is unable or unwilling to execute it' is guilty of 'fraudulent bankruptcy' and punishable with a fine. Concealment of insolvency alone is not sufficient, but it is a material fact in the conviction and punishment of a debtor in criminal proceedings. A criminal division court may view failure by the debtor to notify the court within 15 days under Article 971 as evidence of concealment of insolvency.

### 5.7 What are 'Commercial Commitments'?

Finally, one special requirement for commencement of bankruptcy proceedings under Ethiopian law merits some treatment. Article 971 in part provides 'the debtor is no longer able to meet the commitments related to his commercial activities.' One would have dismissed the use of 'commitments related to his commercial activities' as an accidental slip had the expression not been repeated in Article 972. Article 972 in part reads 'any trader who suspends payment of his commercial debts shall...' Reading the two articles, one is in no doubt about the seriousness of the requirement that the inability should relate to 'commercial debts,' or 'commercial commitments'.

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<sup>143</sup> See Articles 1113-1118 of the Commercial Code

<sup>144</sup> On discharge, later

Why is the law particular about this requirement? The additional requirement of the debts having to do with commercial commitments seem to issue from the scope of application of Book V of the Commercial Code, as defined in Article 968. Article 968 uses language that restricts the application of bankruptcy to traders and commercial business organizations (except joint ventures). A consistent application of such 'trader-only' regime of Ethiopian law would logically restrict Book V to cases where 'the 'suspension of payments' was the result of 'commercial commitments.' The drafters were careful not to allow the intrusion of 'non-commercial' debts into their rigidly defined scope for bankruptcy application. They wanted to design a tightly fenced bankruptcy regime that applied to traders in respect of their trade commitments only. This take on the scope of Book V is consistent with the original intent of the two drafters of the Commercial Code. It is difficult to write about the intent of the drafters with any degree of certainty but there is some evidence that they were serious about circumscribing the Commercial Code to the status of traders and their activities arising from their status as traders. It might even be contended that the trader-only drift is not a sudden detour in Book V. Their preference for the 'subjective' approach, in contradistinction to the 'objective' approach of some other systems, may have led to the requirement that only 'commercial' debts should result in initiation of bankruptcy.

The following passage taken from the Background Documents, written by Professor Jauffret, might be taken as one such evidence. Professor Jauffret writes:

*Professor Jean Escarra did not hide his preference for the subjective system..... I believe it very desirable to follow the intention of Professor Escarra on this point. Thus, Book I, which I drafted, is devoted to this subjective concept<sup>145</sup>: the point of departure is found in the definition of trader in Article 5 and the definition of Commercial Business Organizations in Article 10. Book I, in sum, is devoted for the most part to the status of traders, a status supplemented by the bankruptcy provisions of Book V (Emphasis mine).<sup>146</sup>*

The two drafters saw the Commercial Code as a body of rules regulating the status of traders and opted for the subjective standard with that aim in mind. It is quite possible that the additional requirement of commercial commitments stemmed from their conviction to restrict bankruptcy to the status of traders. The additional requirement would prevent a commencement of bankruptcy against a trader for suspension of debts not having to do with the trader's commercial commitments. If we accept the drafters' circumscription of bankruptcy to traders, it is easy to accept their other limitation, i.e., that the debt should be commercial, whatever that may mean.

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<sup>145</sup> The subjective vs. objective dichotomy is based the applicability of the Commercial Code to traders and only traders (subjective) or certain acts, called acts of commerce (objective), see Winship, Supra Note 12, pp. 35-36

<sup>146</sup> Jauffret, Report on the Completion of the Draft of the Avant-Project of the Commercial Code of the Empire of Ethiopia (1 March, 1958), in Winship, Supra Note 12, p. 36.

The additional requirement may also be rooted in the drafters' conviction to restrict the possible liquidation of a trader's business for commitments directly related to commerce. The schema makes sense if we see bankruptcy through the lens of the drafters. That lens is decidedly a narrow one. It endows bankruptcy as a status (not an enviable one, to boot) for traders only and it is only reasonable that traders should fall by the 'sword of bankruptcy' only for their acts having to do with their status as traders. What happens after the business falls is quite another matter.

The additional commencement requirement of 'commercial commitments' would give rise to two sets of problems. One is the definition of 'commercial commitments.' The second problem is whether the exclusion of 'non-commercial commitments' from Articles 971 and 972 would affect these commitments.

It would be vain to search for a definition or even clues to 'commercial commitments' in the Commercial Code. In the absence of a definition, how would one fix the meaning of 'commercial commitments' or 'commercial debts'? The following hypothetical cases illustrate the problem:

- a. XYZ is a general partnership, with X, Y and Z as its general partners. X entered into a private contract with N unrelated with the activities of the general partnership. X was unable to perform his obligations towards N, and N obtained a judgment against X. Can N apply for the bankruptcy of XYZ, of which X is a partner?
- b. Mr. D has a boutique in Piazza area. Mr. D, unrelated to his boutique, was fined 500 Birr for violating traffic rules while driving in Addis Ababa. Supposing D failed to pay the fine as ordered, is that sufficient to trigger bankruptcy proceedings against Mr. D?
- c. Mr. E was recently divorced from his estranged wife, and the court ordered him to pay maintenance allowance for their children, amounting to 1000 Birr every month. Mr. E has a bookstore in Arat Kilo. If Mr. E fails to pay the allowance, can his former wife (as a guardian of the children) bring suits against Mr. E to have him declared bankrupt?
- d. Suppose in C above, his wife brought action against Mr. E for a division of their common property, of which the book store in Arat Kilo formed one. Can she institute bankruptcy proceedings against Mr. E?
- e. X, an employee of XYZ Company, caused injury to Mrs. N for whom the Company is vicariously liable under Ethiopian extra-contractual liability law. Should the court declare XYZ bankrupt upon the application of Mrs. N?

When does a commitment or liability acquire the label 'commercial'? How directly should it be connected with the business? Nothing in the language of the Code gives us a hint on how to draw the line between commercial and non-commercial commitments. As the hypothetical cases above illustrate, it is not always easy to classify a debt or a commitment as commercial or non-commercial, and in practice, as

long as the requirement of 'commercial debt or commitment' remains in the Code, courts are bound to struggle to find an appropriate means of distinguishing 'commercial debts' from 'non-commercial' ones. Perhaps, the drafters refrained from a definition of these terms in order to give courts the discretion to decide cases based on the circumstances surrounding each case.

In some cases, a debt, defined broadly, would be so unrelated with the commercial activities of the debtor that the court should reject any attempt to institute bankruptcy proceedings on grounds of 'suspension of payment.' Such is the case in 'b' and 'c' of the hypothetical examples given above. The use of the expression 'commercial commitment' or 'commercial debt' would be rendered meaningless if a person were declared bankrupt because of suspension of payment of fine or maintenance payments. In other cases, as in the hypothetical example 'd' above, the distinction is not so easy. To be sure, marriage and its breakdown 'divorce' are as personal and non-commercial as they can get. Mr. E's marriage to C has no relationship with the commercial activities of Mr. E. But, divorce has the effect of division of property, which may include the commercial establishments of the divorcees. Mr. E's bookstore may have formed part of the common property of the spouses while their marriage lasted. Should that lead to the bankruptcy of the divorcee?

In the hypothetical cases given above, the creditors in each case may seek execution (enforcement) according to the Ethiopian Civil Procedure Code.<sup>147</sup> In that case, the court will simply order execution of judgment in accordance with the Civil Procedure Code, without, it may be added, declaring the judgment debtor bankrupt. The effect of the order may be liquidation of the debtor's business along with other assets, if there are any. If that is the path chosen by the creditor, we won't be having any problem, at least as far as the Commercial Code is concerned.

But what happens when the creditor or groups of creditors, or even the debtor, applies to have the debtor declared bankrupt? What if the debtor applied for bankruptcy protection?<sup>148</sup> It is in situations like these that the courts will have difficulty distinguishing commercial debts from non-commercial ones. The courts will have to continually make judgments about the commercial nature of certain debts or other wise, for they are left to themselves to make judgments based on the facts and circumstances of each case.

The second question in relation to the issue of 'commercial commitments' or 'commercial debts' is whether non-commercial debts are excluded from participation

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<sup>147</sup> See Paragraph 3, Articles 394-461 of Ethiopian Civil Procedure Code

<sup>148</sup> This has happened elsewhere. The American company, Texaco, filed for bankruptcy in order to dispute a large court award. Other companies in the USA opted for bankruptcy protection in order to withdraw from expensive collective agreements; see, Julian R. Franks, Kjell G. Nyborg and Walter N. Torous, A Comparison of US, UK and German Insolvency Codes, Financial Management, Vol. 25, No. 3, 1996, p. 92.

in bankruptcy proceedings even at a later stage of the proceedings. For this, we may need to distinguish two groups of debts. There are those that are responsible for setting bankruptcy in motion (the triggers of bankruptcy). There are, on the other hand, debts (claims) that are submitted upon declaration of the debtor's bankruptcy. We can all agree, based on the preceding discussions, that non-commercial debts are not part of the first group of debts. These debts cannot set bankruptcy proceedings in motion.

Does this also mean that 'non-commercial' debts cannot be submitted for proof in bankruptcy proceedings after the bankruptcy has been declared by court? There are two ways of looking at this problem. One approach is to interpret the above provisions so that 'non-commercial' creditors are excluded from bankruptcy proceedings in all cases and at all times. This approach would be implausible for a number of reasons.

In many instances, bankruptcy has the effect of liquidating and winding up the business of the debtor.<sup>149</sup> At the end of a bankruptcy proceeding, i.e., upon distribution of the proceeds of the debtor's assets among creditors, the debtor may have little left for himself and family let alone for non-commercial creditors. The exclusion of non-commercial creditors from the proceedings of bankruptcy is, therefore, as good as denying them any recourse to recover their debts.

Secondly, exclusion of non-commercial creditors from participation in bankruptcy proceedings is an acknowledgment that bankruptcy law imposes a limitation of liability based on characterizations of debts as commercial and non-commercial debts. If there is such a thing in bankruptcy law, it will indeed be odd, to say the least. Limitation of liability is a privilege accorded by law and the circumstances in which limited liability is accorded are exhaustively listed in the law. A case in point is the limited liability that private limited companies and share companies enjoy.<sup>150</sup> It is not the objective (and it has never been the objective) of bankruptcy law to legislate limited liability rule.

Thirdly, Articles 1041ff of the Commercial Code, which incidentally deal with the submission of claims by all sorts of creditors during bankruptcy, never use terms like commercial or non-commercial debts. These provisions nowhere discriminate between commercial and non-commercial debts. All kinds of debts owed by the debtor are admissible provided they are supported by evidence. The trustee, who takes over the management of the bankrupt estate upon declaration of bankruptcy, has the duty to admit all debts.<sup>151</sup> The Commercial Code of Ethiopia does not even exclude foreign debts from admission in bankruptcy as some foreign jurisdictions do.<sup>152</sup> The drafters would have inserted 'commercial debts' in all provisions following Articles 1041ff if

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<sup>149</sup> See Articles 1035-1040, 1041-1080 and 1101-1118 of the Commercial Code

<sup>150</sup> Even these privileges are sometimes taken away in 'piercing the corporate (company) veil' cases; See, for example, Article 309 of the Commercial Code

<sup>151</sup> See Article 1041 of the Commercial Code

<sup>152</sup> See UNCITRAL, *Supra* Note 10, p 51

they had really intended to keep non-commercial debts out of bankruptcy proceedings. It is therefore reasonable to assume that 'non-commercial' debts, while excluded from debts that trigger bankruptcy, are entitled to participate equally with commercial debts after the declaration of bankruptcy.

## VI Conclusion

From the discussion of Ethiopian bankruptcy law so far, we may conclude the following:

1. Ethiopian law uses bankruptcy in a narrow and restrictive sense of liquidation and treats 'schemes of arrangement' as separate from bankruptcy proceedings. This may have stemmed from its treatment of the two proceedings as separate, having their own rules of entry and procedure. In any event, this restrictive definition of bankruptcy is at variance with the accepted meaning of the term elsewhere.
2. Ethiopian law gives a preference for bankruptcy in contradistinction to a scheme of arrangement which would have looked to the saving of the business of the bankrupt as opposed to its dismemberment for the satisfaction of the claims of creditors. This is an inference more from the arrangement of provisions in the Commercial Code than an explicit policy expressed in any of the provisions. Unfortunately, Book V of the Commercial Code has seldom been tested in practice since the promulgation of the Code. The question of whether the Code favours liquidation to reorganization of businesses cannot be, therefore, buttressed by hard evidence of cases litigated in courts. In any case, in its inclination towards bankruptcy in the sense of liquidation of the business of the bankrupt, Ethiopian law is again at variance with developments in bankruptcy in the rest of the world. It does not encourage debtors to view bankruptcy as a scheme of protection against liquidation and winding up of their business. This may have to do with the fact that the Code is comparatively old. At the time of writing, the Code is more than half a century old, if we count the time the draft was first submitted by the first drafter, i.e., 1954. The conclusion that Ethiopian bankruptcy law appears to favour liquidation over continuation of the business needs one qualification. The new Banking Business Proclamation (No. 592/2008), which devotes a whole part to bankruptcy involving banks, seems to overturn the general tendency of Ethiopian bankruptcy regime. The new Banking Business Proclamation directs that banks that are deemed 'viable' should be given the chance to continue business.
3. Although by no means peculiar to Ethiopian law, its distinctive feature nonetheless is that bankruptcy applies only to traders and commercial business organizations. This is to be expected, as bankruptcy is found in the Commercial Code, which is a special law for traders. In terms of scope,

however, the Commercial Code and Book V are not co-extensive. In this respect, Book V may be said to have provided for special rules of application. Book V does not apply to joint ventures. Nor does it apply to non-commercial or civil business organizations, however they may be distinguished. Perhaps more significant and possibly unique to Ethiopian law is the requirement that the suspension of payment that triggers bankruptcy proceedings should be 'commitments related to commercial transactions.' Traders are therefore distinguished, for purposes of bankruptcy application, not only by their status as traders but also by the specific transactions they enter into. If the transaction does not qualify as 'commercial', it does not lead to initiation of bankruptcy even though the debtor is a trader. This additional restriction is clear enough although courts will have a hard time distinguishing commercial from non-commercial transactions. Again in its restriction to traders and commercial business organizations, the Commercial Code appears to be at variance with recent developments in bankruptcy application. Even countries which used to associate bankruptcy with the status of traders or merchants (France is a very good example in this regard) have now abandoned this restrictive approach and have made bankruptcy applicable to non-traders as well. Should Ethiopia follow suit?