

COMPLIANCE WITH LEGAL OBLIGATIONS BY BUSINESSES IN THE ADDIS ABABA MERCATO

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The Law imposes certain obligations on all persons who, being traders as defined by Article 5 of the Commercial Code, engage in commerce. Among the most important of these are the duties to register with the Ministry of Commerce, Industry and Tourism and to keep accounts of all business transactions. Also, in the event of failure of a business there may be a duty to file a statement of bankruptcy with the High Court if all commercial obligations cannot be met. In our survey of business practices in the Mercato¹ questions were asked to determine to what extent these duties are being fulfilled by traders in the Mercato.

a. Business Registration Requirements.

The Commercial Register. Prior to the enactment of the Commercial Code registration of businesses was required under the Business Enterprises Registration Decree.² The Code includes provisions for a Commercial Register³ but allows the prior law to remain in effect until an order is published in the *Negarit Gazeta* revoking it.⁴ This order has not been published yet, but the Decree has been replaced by the Business Enterprises Registration Proclamation of 1961.⁵ Under the Commercial Code only those businessmen classed as "traders" and organizations classed as "commercial" would be required to register, but every company and every person engaged in business for profit is required to register under the Proclamation. While failure to register under the Commercial Code will only prevent

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1. This Survey was undertaken primarily to uncover information concerning the extent to which the relatively sophisticated business law concepts imported into Ethiopia by the Commercial Code and various other codes, proclamations, and regulations have been absorbed by the average Ethiopian merchant and authorities charged with enforcement. The Survey was conducted by analyzing a selection of case files from various courts which it was thought would contain representative samples of all kinds of commercial cases now being litigated and by interviewing a selection of merchants and traders in the Mercato, Addis Ababa's principal market area. With the time and resources available it was calculated that about 150 interviews could be conducted. Therefore, for most types of business, interviews were sought in one out of 30 establishments while larger percentages were sought of importers, exporters and some retail businesses which, though small in number, appeared so significant that they should be represented in the survey. Altogether, 166 interviews were conducted but eight of these were disregarded because of their incompleteness. All of the interviews were with the owners or part owners of business establishments except in the case of a few branch outlets for industrial share companies where the managers were interviewed. A more complete report of the results of this survey is contained in the authors' paper "Legal Aspects of Doing Business in Addis Ababa: A Profile of Mercato Businessmen and their Reception of New Laws" published in January 1972 as Occasional Paper No. 1 of the *Journal of Ethiopian Law*.
2. Business Enterprises Registration Decree, 1957, Decree No. 27, *Neg. Gaz.*, year 17, no. 4.
3. *Comm. C.*, Arts. 86-123.
4. *Id.*, Art. 1174.
5. Business Enterprises Registration Proclamation, 1961, Proc. No. 184, *Neg. Gaz.*, year 21, no. 3.

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someone from holding himself out to be a "trader" to third parties in addition to being subject to criminal punishment under the Penal Code,⁶ the Proclamation provides that "no company or individual enterpriser shall be entitled to maintain any action in Ethiopia upon any contract made by it in Ethiopia unless before the making of such contract the company or individual enterpriser shall have registered in the Ministry of Commerce and Industry as provided in this Proclamation."⁷ In addition, no municipality may license a non-registered business and any company or individual who carried on business without registering or engages in a business that is not authorized by his registration is punishable in accordance with the provisions of the Penal Code of 1957.⁸ Thus, although the provisions of the Proclamation are more simple because they eliminate the necessity for making the subtle legal distinctions between "traders" and "non-traders" and require every business enterprise to be registered, the practical effects of failure to register may be much more harsh than those of the Commercial Code. Under the Code the only civil legal effects of non-registration of an individual trader seem to be that the trade name and distinguishing marks of his business are not protected,⁹ he is not able to voluntarily enter a scheme of arrangement instead of being declared bankrupt,¹⁰ and his account books are not admissible as evidence in his favor,¹¹ None of these sanctions are likely to ever be felt by the average small businessman. If the provisions of the Proclamation were literally applied by the courts, however, they would prohibit the enforcement of any contract made by any unregistered businessman.

Registration of Businesses Interviewed in the Mercato. The major purpose of Commercial Registers is publicity of the legal status and financial condition of persons and organizations registered.¹² Questions were asked, therefore, to find out if the people interviewed had registered and if they ever used the Commercial Register to obtain information about other businesses.

Forty-seven per cent of the people interviewed said that they were not registered with the Ministry of Commerce and Industry, but two of those not registered said that they looked at files of other businesses to get information. Forty per cent were registered but only four of these said they looked at other files to get information. Thirteen per cent did not answer the questions pertaining to registration. Among the retail businesses about 40 per cent of the clothing and textiles shops, 40 per cent of the hardware and utensil dealers, twenty per cent of those dealing in food products, and only one of the thirteen miscellaneous goods shops were registered. About 65 per cent of the bars, restaurants, and hotels were registered and 40 per cent of the handicraftsmen and people providing personal services.¹³ Among

6. Pen. C., Art. 428.

7. Business Enterprises Registration Proclamation, 1961, cited above at note 5, Art. 5.

8. Pen. C., Art. 746.

9. See Comm. C., Arts. 118, 127-141.

10. *Id.*, Art. 1120.

11. *Id.*, Art. 71.

12. *Id.*, Art. 88; A. Jauffret, *Manuel de droit commercial* (Paris, Librairie Général de droit et de jurisprudence, 1957), p. 60.

13. These may not be required to register under the Commercial Code because they are not "traders" or "commercial business organizations" but they are so required under the Business Enterprises Registration Proclamation, 1961, cited above at note 5.

the importing and wholesale businesses 70 per cent of the textile and clothing merchants and 65 percent of the hardware and appliance dealers said they were registered.

By type of business organization it was found that only 37 per cent of the individual enterprisers and 22 per cent of the partnerships without written agreements were registered.¹⁴ Of the partnerships with written agreements 63 per cent were registered, however, as well as five of the eight private limited companies, the one limited partnership, and one share company. Two of the six who said that they used the Commercial Register to investigate other businesses were private limited companies and the other four were individual enterprisers.

There are several reasons which may account for the lack of enthusiasm for use of the Commercial Register. Although the Proclamation says that the owner of a business which is not registered cannot bring an action on any contract in any court in the Empire and that no Municipality can grant any license to do business unless the business is registered, in practice these sanctions appear to be completely ignored. Practically all of the permanent businesses in the Mercato are licensed by the Municipality and it in fact owns many of the major buildings. The Commercial Register was mentioned only once in all of the cases examined in the Survey and that was in connection with whether or not a party could legitimately claim to be president of a share company because his name was not entered as such in the Register. If the registration law had been enforced many of the cases examined would probably have been dismissed because the plaintiffs were not registered. Many of those who were registered said that they received practically no benefit from having done so, but some said that it is easier to engage in foreign trade and to get loans and guarantees from the banks. A few bankers interviewed said that they check to see if a borrower is registered, but most bankers accept a valid license from the Municipality as sufficient evidence that he has a legitimate business. Among those merchants who were aware that the Commercial Register exists and that they might have some obligation to register but had not, there seemed to be a feeling that registration would insure an increase in their taxes since they would have to state the amount of capital invested in their businesses and to pay fees for registration itself. The fear regarding taxes may not be entirely unfounded. As will be discussed in the following section, taxes, although supposedly based on income or turnover are in many cases actually based on the amount of capital in the business.

In effect, therefore, there are two registration systems, that of the Ministry of Commerce, Industry, and Tourism and the other of the Municipality, and since actual penalties seem to be applied by the latter for non-registration and registering with the former is often feared to cause an increase in taxes, many businessmen in the Mercato consider the procurement of a license from the Municipality all the formality required for legitimately doing business.

b. Obligations to Keep Accounts and Their Use for Assessment of Taxes.

Requirements of the Commercial Code. Provisions are made regarding the kinds of accounts to be kept by all traders and commercial business organizations

14. For a discussion of the legal status of non-registered partnerships and those without written agreement see P. McCarthy, "De Facto' and Customary Partnerships in Ethiopian Law," *J. Eth. L.*, vol. 5 (1968), p. 105.

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in the Commercial Code.¹⁵ Generally any person¹⁶ or business organization carrying on trade must keep such books as are required in accordance with business practice and regulations, having regard to the nature and importance of the trade carried on.¹⁷ Petty traders may be exempted from keeping accounts under special regulations,¹⁸ but such regulations have not yet been issued and no definition of petty trader is found in the Commercial Code or elsewhere. Presumably then even the smallest trader is subject to the requirements being discussed.

As a minimum the Code requires that every trader and every business organization keep a journal where daily entries must be made of his or its dealings regardless of their nature. The book-keeper may, however, at least once a month balance the proceeds of such dealings but must preserve all documents necessary for checking these daily transactions.¹⁹ Every trader and business organization must also prepare an inventory and balance sheet, both when they begin to carry on trade and at the end of each financial year when they must also prepare a profit and loss account.²⁰ Anyone who fails or neglects to keep books and accounts regularly and in good order and to keep his correspondence, invoices, and other business papers for the prescribed time as required by law, regulation, or articles of association is punishable under the Penal Code with fine or arrest not exceeding one month.²¹

Accounting Requirements of the Income Tax Proclamation and Regulations. In addition to the requirements of the Commercial Code, people in business have obligations to keep accounts under the Income Tax Proclamation²² and Regulations.²³ These laws exempt small businesses from keeping accounts. The Minister of Finance may make regulations requiring taxpayers to keep certain books of account in certain forms²⁴ but he may prescribe regulations for certain taxpayers who are not required to keep records and books of accounts if their taxable income as estimated by the Tax Authority does not normally exceed E.\$6,000.²⁵ The Income Tax Regulations do provide for a category of taxpayers who do not have to keep accounts if the tax authority estimates their income to be below E.\$6,000.²⁶ Fifteen classes are provided within the category based on the amount of income which is estimated, and the amount of tax to be paid is prescribed for each category.

If no records and books of account are maintained by a taxpayer, if for any reason the records and books of account are unacceptable to the Income Tax Authority, or if a taxpayer fails to declare his or its income within the prescribed time, the Income Tax Authority may assess the tax, by estimation.²⁷

15. Comm. C., Arts. 63-85.

16. French version reads, "toute personne physique ayant la qualité de commerçant."

17. Comm. C., Art. 63.

18. *Id.*, Art. 64; see also the discussion of the Commercial Law Codification Sub-Commission on Oct. 20, 1954, *Procès-verbaux du sous-commission des lois commerciales* (1954, unpublished, Archives, Faculty of Law, Haile Sellassie I University), p. 58.

19. Comm. C., Art. 66.

20. *Id.*, Art. 67.

21. Pen. C., Art. 817.

22. Income Tax Proclamation, 1961, Proc. No. 173, *Neg. Gaz.*, year 20, no. 13.

23. Income Tax Regulations, 1962, Leg. Not. No. 258, *Neg. Gaz.*, year 22, no. 1.

24. Income Tax Proclamation, 1961, cited above at note 22, Art. 42.

25. *Id.*, Art. 43.

26. Income Tax Regulations, 1962, cited above at note 23, Reg. 30.

27. Income Tax Proclamation, 1961, cited above at note 22, Art. 40.

Accounting Practices Among the Businesses Interviewed in the Mercato. In order to obtain some idea of how the accounting requirements of the Commercial Code and Income Tax Proclamation are being followed and what effect they may have on business practices, the people interviewed were asked a series of questions about what kind of account books they keep, if any, and to what extent they are used for determination of the amount of tax they pay. The latter question seems particularly important because of the number of people who cited the arbitrary manner of tax assessment as the greatest problem faced by traders in the Mercato at present. Out of the 158 interviews all but eight people responded to these questions. Fifty-six of them said that they keep no books at all and that their taxes are assessed entirely by estimation. Five, however, said that they kept no books at all but paid no tax either. They failed to explain clearly why not. Fifty-one others said that they keep some kind of account books but that taxes are still assessed entirely on the basis of estimation. In most cases these books are only note-books or "exercise books" in which they record credit sales and purchases and keep some kind of basic inventory but are not complete enough to be used for an accurate evaluation of their profits and losses.

Some appeared to keep adequate account books but for various reasons they are not used for taxes. One merchant had had a course in accounting and kept all the appropriate books, but said that the tax assessors will not look at them but only estimate on the basis of invoices and their guess at the number of sales per year. Another also said he had been keeping accounts for a year but that the revenue service will not accept them. He had once gone to court to have the amount of his tax reduced. Still another said that he keeps all the journals and ledgers required and he had copies of the Commercial Code in both English and Amharic which he showed the interviewer, but he said his books are not used for tax assessment because they are not audited. Eleven said they keep some kind of accounts or at least receipts and invoices which are considered by the tax assessors but that the assessors supplement them with their own estimation.

Only one-sixth of those answering the questions said that they keep journals and ledgers which are used for assessment of their taxes without estimation on the part of the assessors. Three others said they keep journals and ledgers also but that their taxes had not been assessed yet because they had only recently begun business.

Accounts were not kept or those kept were not used for tax assessment by any of the miscellaneous goods dealers interviewed, by 90 per cent of the retail hardware and utensil dealers, 85 percent of the personal services businesses and handicraftsmen,²⁸ 80 per cent of the food produce dealers, 75 percent of the bars, hotels, and restaurants, and 67 per cent of the retail clothing and textile merchants. Accounts which were the basis of tax assessment or were considered along with estimation were kept, however, by 75 per cent of the importers and wholesale dealers in hardware, machinery and utensils, and by 70 per cent of the importers and wholesale dealers in clothing and textiles.

From the viewpoint of business organizational structure, 75 per cent of the individual enterprisers and 80 per cent of the partnerships without written agreements did not keep accounts which were used for tax assessment, while 65 per cent of

28. Most of these are not required to keep accounts under the Commercial Code, because of their "non-trader" status.

the private limited companies, and 70 per cent of the partnerships with written agreements did. Therefore, although most of the businesses which do not use any or adequate accounting practices are the smaller retail shops which are run by individual owners or an informal partnership, a significant number of larger import and wholesale businesses with more advanced forms of business organization seem to be lacking in this respect also.

The problem of inadequate accounting methods is not one which can be solved easily or quickly because a strict enforcement of the Commercial Code provisions would simply drive out of business many people who lack the education and ability to keep accounts and whose businesses are not large enough to justify hiring employees to do it for them. There is some effort being made by the tax authority to encourage traders to keep proper accounts since one person interviewed said that he had not kept accounts in the past, but would in the future because last year he had to pay a twenty per cent penalty for not having them. However, another trader noted that although he had to pay E. \$150 a year as a penalty for not keeping accounts, he would have to pay an employee more than E. \$150 a month to keep accounts for him. Therefore he naturally preferred the former. The lack of proper accounts is a serious threat to the stability of many businesses not only because it is needed to establish profitable prices and make wise investment decisions but because of the arbitrariness and inequity with which taxes may be assessed. There is an obvious temptation for tax assessors to demand and accept bribes when the tax assessed is based entirely on their estimation of how much the business appears to be earning and the taxpayer has no documentary evidence with which to challenge the estimation. Practically all of the businessmen who complained about tax problems said that most people in the Mercato who did not want to pay exorbitant taxes bribed the tax assessors and several even admitted that they bribed them themselves. An effort needs to be made, therefore, to encourage business owners to learn how to keep the accounts required by law, but it seems that an attempt suddenly to enforce the laws would probably have undesirable results.

c. Bankruptcy.

Code Provisions. Under the codes, when a non-trader does not have enough assets to meet all of his financial obligations his creditors may seize, upon proper execution of a court judgment, what property he has other than that deemed essential to his and his family's survival.²⁹ Those who come first may take what they find but the debts owed to those who find nothing are not extinguished and may be reasserted at any time. That is to say, a "non-trader" debtor apparently may not be legally excused from his debts under any codified procedure — he cannot be declared "bankrupt".³⁰ The debtor may not be imprisoned for refusal to obey a court judgment for payment of money if he is unable to do so.³¹ On the other hand, a trader or commercial business organization may be put into bankruptcy by a suit initiated by his creditors or himself.

29. Civ. Pro. C., Arts. 404-455.

30. *Id.*, Art. 392(2); extension of bankruptcy provisions to non-traders was discussed by the sub-commission but rejected at the instance of the Draftsman.
Proces Verbaux, cited above at note 18, p. 78.

31. Civ. Pro. C., Art. 389; Rev. Const., Art. 58.

Regardless of who initiates a bankruptcy action or when it is begun, a trader or commercial business organization which fails to meet payments must file a notice to this effect with the registrar of the bankruptcy court including the firm's balance sheet, its profit and loss account, and a list of its commercial credits and debts.³² Complex bankruptcy proceedings then begin in which the debtor either works out an agreement with his creditors for partial payment of his debts and remains in business, or the business is wound up and all of the remaining assets are distributed to them. If the debtor's assets do not exceed E. \$1,000 or cannot amount to more than one tenth of the liabilities, a summary procedure is available in which many of the normal steps are shortened or eliminated.³³ Rather than entering into bankruptcy proceedings, a debtor who is about to cease meeting obligations may voluntarily apply for a "scheme of arrangement" by which he works out a compromise agreement with his creditors.³⁴ To do so, however, he must file the same documents required for a notice of bankruptcy and show that he has been properly registered for the past two years since the opening of business.³⁵

Customary bankruptcy practice in the Mercato. As should be evident from the findings reported above these bankruptcy and scheme of arrangement provisions would be difficult to apply to most businesses in the Mercato because they often are not registered and rarely keep the accounts necessary for the provisions to apply. Only one bankruptcy case was found in the High Court and it involved the winding-up of a share company.

Bankruptcy is an institution recognized by custom among the businessmen in the Mercato, however, and as already mentioned the results of arbitration and conciliation proceedings often have the equivalent effect of adjudication in bankruptcy. One such proceeding was related by an Arab importer who held E. \$1,000 promissory note from another trader who was "bankrupt." The bankrupt had taken E. \$20,000 of goods from ten different people and had only E. \$10,000 remaining. Six elders were chosen whom all the parties knew well and all agreed on. The conciliation agreement was not written and the proceedings were only an attempt to bring the parties to a voluntary reconciliation. Four meetings were held, one every week. At first the debtor was unwilling to give up his last possessions, but finally he agreed under pressure from the elders and, after paying his taxes, the elders and the creditors discussed how to share his goods. A decision was reached by the elders that the creditors tear up their promissory notes and accept half the amount owed. The decision was not written but since the notes were torn up in front of the elders, it seems unlikely that a future dispute would arise from it. Everyone accepted the decision. The interviewee said he did not know what would have been done to any party who did not comply.

Another elder interviewed said that when traders become bankrupt it is customary for them to circulate notes among their acquaintances explaining why they are bankrupt and asking for contributions to pay off their debts. The elder had in his pocket one of these notes from someone whose shop had burned recently and he

32. Comm. C., Arts. 972-973.

33. *Id.*, Art. 1166.

34. *Id.*, Arts. 1119-53.

35. *Id.*, Art. 1120.

said that most people felt socially obliged to make these contributions. The *idit* associations also function in some cases as a form of bankruptcy insurance so that if a member is honestly bankrupt the association will pay his debts.

It is conceivable that the customary procedures used in cases of bankruptcy do not include all of the protections for both debtors and creditors which the bankruptcy law is designed to provide. It seems likely, however, that the elders who conduct these proceedings inquire into all outstanding debts and by knowing the bankrupt personally are familiar with his assets. Also, since the agreements reached usually have the legal effect of a "compromise,"³⁶ creditors should be unable to reassert their claim later in court.

In general therefore the bankruptcy provisions, because of their complexity and lack of correlation with many business practices, are among the least "received" of the foreign institutions of the Commercial Code, but the need of bankruptcy as an institution has produced customary practices which in most cases are legally recognizable.

Conclusion

The results of this survey have shown some major conflicts in the Mercato between law and practice. These conflicts appear to be due to lack of education or knowledge on the part of merchants with respect to accounting practices and registration requirements and reluctance on the part of authorities to enforce strictly many harsh legal provisions. However we detected little, if any, evidence of resistance to these laws on the basis that they are "foreign" to the customary way of doing things. It seems likely therefore that with a growing awareness on the part of businessmen these laws can be fully implemented and used.

36. Under the law, parties are not bound by the terms of a compromise arrived at through conciliation unless they have expressly so agreed in writing. Civ. C., Art. 3322(2). If they have so agreed the conciliator's decision has the force of *res judicata* without appeal and may not be contested by the parties on the ground of a mistake concerning the rights on which they have compromised, *id.*, Art. 3312, but there are certain grounds upon which a compromise agreement may be invalidated. *Id.*, Arts. 3313-15.