Ethiopian Bankruptcy Law: A Commentary (Part II)

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The market doesn't recognize desert. Initiative, enterprise, innovation, hard work, ruthless dealing, reckless gambling, the prostitution of talent: all these are sometimes rewarded, sometimes not.

Michael Walzer[1]

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[1] Michael Walzer, "Spheres of Justice", in Tom L. Beauchamp and Norman E. Bowie (eds.), *Ethical Theory and Business* (University of Phoenix, Special Edition Series, 1997), at 640

♦ Editor's note: The long and detailed nature of this article has made it necessary to include a contents outline in order to make it easier for readers to follow the analysis.

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1. Introduction

In writing this sequel article, the greatest challenge was to prevent the second part from falling apart by a commentary that sprawls and meanders without any unifying theme to hold it together. It is impossible to canvass more than 200 articles (202 articles to be exact) in a two-part commentary. One would have to choose the 'salient' provisions of the bankruptcy law to give one a fairly representative feature of Ethiopian bankruptcy law. The author has picked what he considers to be the salient aspects of Book V of the Commercial Code and left out those parts which he thinks are purely procedural, technical and ephemeral.[2] The author did not follow an article-

[2] The provisions regarding 'proving of debts' (Chapter 5, Title II, Book V of the Commercial Code), for example, have been left out of this commentary. This omission is not a grievous one – in the order of things – because this chapter is familiar to those who are acquainted with Civil Procedure. Besides, the tenor of these provisions can be captured at first reading quite easily.

by-article commentary in the first part, and the approach is not followed in this part either. The author is fully aware that Book V (along with the whole of the Commercial Code) will be revised soon (perhaps substantially)-some steps have already been taken both by the government (the Ministry of Justice) and some members of the business community to that effect.[3] This article is written therefore not just with the intent to elucidating Ethiopian bankruptcy law but also with a view to showing the possible way forward for what needs to change. Since there is a dearth of materials on Ethiopian bankruptcy law-both the literature and cases are sorely lacking-the author has relied upon comparative bankruptcy law and literature to both understand and illuminate the provisions of Ethiopian bankruptcy law. Unlike the first part, however, the author has cast about a fairly diverse body of comparative materials on bankruptcy law to write the second part. Those who seek to find correspondence between the organization of this commentary and the organization of the bankruptcy rules in Book V of the Commercial Code will be sorely disappointed (in case they need to be forewarned). In a commentary of the whole Book V of the Commercial Code, reorganization (not to be confused with one of the subjects treated in this commentary) is unavoidable. This commentary is organized around some major themes of bankruptcy: the actors, the effects, and the alternatives to bankruptcy.

Some issues in bankruptcy are better left untouched in a general commentary like this. Wherever appropriate, a passing remark is made about these issues (with a nudging to others to think writing about these issues). The digression that ensues a proper treatment of these issues is simply too distracting in a commentary that is already bursting at the seams. The issue of jurisdiction over bankruptcy in the context of the federal structure of courts in Ethiopia is one such issue. Jurisdiction over bankruptcy raises collateral issues of court jurisdiction in general, federalism, cross-border issues of bankruptcy proceedings, issues which will take us far away from the matter at hand.

This commentary is divided into four parts. Part I deals with the persons and institutions responsible for the conduct of bankruptcy. Part II will address the important question of the effect of bankruptcy upon various

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[3]See Federal Democratic Republic of Ethiopia, Ministry of Justice, *Draft Commercial Code*, (unpublished); Tilahun Teshome and Taddese Lencho (eds.) *Position of the Business Community on the Revision of the Commercial Code of Ethiopia* (Addis Ababa Chamber of Commerce and Sectoral Associations, PSD Hub Publication No. 8, July 2008).

parties connected with the bankrupt debtor (including the debtor). Part III will deal with the equally important question of 'distribution' (and priorities of creditors) for which the whole bankruptcy proceeding is designed. Part IV will deal with the alternative schemes to straight bankruptcy, namely, composition and schemes of arrangement. Finally, the article will end with a conclusion.

I

2. Persons/Institutions Responsible in Bankruptcy Proceedings

The Commercial Code mentions four persons or institutions as responsible for the conduct of bankruptcy proceedings.[4] They are:

1. The Court of Bankruptcy (Articles 989-990)
2. The Commissioner (Articles 991-993)
3. Trustee/s (Articles 994-1001)
4. Creditors' Committee (Articles 1002-1003)

Although the Commercial Code mentions only these as responsible, we understand from the reading of other provisions of the Code that other persons are involved in various capacities at different stages of bankruptcy proceedings. The other persons involved in the conduct of bankruptcy proceedings include the judge,[5]the public prosecutor,[6] the bankrupt debtor,[7] the receiver,[8] 'competent authorities',[9] and of course individual creditors.[10] The role of these other persons is not closely and systematically regulated by the Commercial Code but their role is no less significant. The smooth and efficient conduct of bankruptcy proceedings can only come about with all these persons carrying out and fulfilling their assigned roles. The machinery of bankruptcy operates to the satisfaction of all parties involved when the individual roles assigned to these persons are carried out efficiently.

We shall follow the lead of the Commercial Code and treat the role of the court, the commissioner, the trustee/s, creditors' committee, and other persons in that order. The relationship among these persons or institutions is both vertical (hierarchical) and lateral. The following diagram represents their relationship:

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[4] See Commercial Code of Ethiopia, 1960, *Negarit Gazetta* – Extraordinary Issue No. 3 of 1960, Addis Ababa, Articles 989-1003.

[5] Id, Article 976(1).

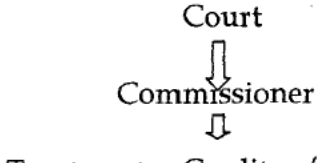
[6] Id, Article 1017.

[7] Id, Articles 1021, 1024.

[8] Id, Article 1039(3).

[9] Id, Article 991(3).

[10] Id, see Articles 1041-1046, 1082-1085.



The diagram above represents the simple relationship between these persons or institutions. But, as often happens, the relationship between them in the real world is more complex than what is indicated in the diagram.

a. Court of Bankruptcy

As the diagram above (simple as it is) shows, the court of bankruptcy occupies the apex of hierarchy of relations in a bankruptcy proceeding. By court, we mean the court that has declared the debtor bankrupt. Another way of distinguishing the court of bankruptcy is to describe it as the judicial body competent to control or supervise bankruptcy proceedings.[11] We must avoid the expression 'bankruptcy court' for that would convey the misleading notion that such a court is recognized in our court structure when it is not. But for purposes of this article, we may use 'court of bankruptcy' to avoid a more tedious expression 'court which has declared the debtor bankrupt' and to distinguish the court under consideration from other courts which may be involved in hearing and settling disputes related with bankruptcy. Besides the court of bankruptcy, we can imagine other courts getting involved in cases having something to do with bankruptcy. These courts include a criminal division court,[12] which hears and settles criminal cases involving bankruptcy, labour division courts[13] which hear and settle labour disputes (such as dismissal or reduction of workers as a

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[11] United Nations Commission on International Trade Law (UNCITRAL), *Legislative Guide on Insolvency Law* (United Nations, New York, 2005), p. 4, glossary (i); UNCITRAL is a subsidiary body of the UN General Assembly which prepares international legislative texts for use by commercial parties in negotiating transactions. This body has prepared texts on subjects like international sale of goods, international commercial arbitration, procurement of goods, construction and services, and of course on insolvency law; see ibid.

[12] The Code itself mentions some of these courts related with the court of bankruptcy. Article 970 of the Code mentions a criminal (division) court on offenses connected with bankruptcy; Article 1075 of the Code mentions a court involved in the cancellation of a contract of sale; for offenses related with bankruptcy, see new Criminal Code of the Federal Democratic Republic of Ethiopia Proclamation No. 414/2004, Articles 725-733.

[13] See the Labour Proclamation 377/2003, *Federal Negarit Gazetta*, 10th year, No. 12, Articles 24, 25 and 29.

result of bankruptcy) and civil division court which hears and settles personal cases against a bankrupt debtor. These courts make decisions which may have a bearing on the course of a bankruptcy proceeding but they are not the courts the bankruptcy law refers to as court of bankruptcy. A court of bankruptcy may be indistinguishable from ordinary courts which deal with non-bankruptcy matters in its organization and even the qualifications of judges who man it. The court of bankruptcy is not even mentioned in the laws dealing with the powers and organizations of courts.[14] However, the nature of bankruptcy proceedings marks out a court of bankruptcy as peculiar, if not entirely unique, from the ordinary courts. First, a court of bankruptcy deals with collective proceedings. The very nature of collective proceedings imposes its own peculiar stamp upon the way a court of bankruptcy goes about its business. A court of bankruptcy potentially handles cases of tens, sometimes hundreds, of creditors against a bankrupt debtor. These creditors are not just numerous, they are also heterogeneous – some are suppliers, some are trade creditors, some are finance creditors, some are employees, etc. Their interests diverge as their classes. A court of bankruptcy is expected to strike a balance among these diverse groups of creditors.

Secondly, the consequence of a collective proceeding is that a court of bankruptcy gravitates to itself many disparate suits that are pending or about to be filed against the bankrupt debtor.[15] This phenomenon may be described as 'the gravitational force' of bankruptcy proceedings. As we shall see later on in this article, one of the immediate effects of bankruptcy proceedings is the suspension of all individual suits, which is followed by the attraction of these suits or actions to the court of bankruptcy. All creditors whose suits have been suspended or who are barred from bringing individual suits are then required to bring their suits to the court of bankruptcy.[16] In a manner of saying, the suits coalesce into a collective proceeding to be managed by a court of bankruptcy. A confrontation with

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[14] The Civil Procedure Code of 1965 is an exception in this regard; Article 15 of the Code (which is now superseded by other laws) assigns the jurisdiction over bankruptcy to the High Court; See Civil Procedure Code of Ethiopia (1965), *Negarit Gazetta* – Extraordinary Issue No. 3 of 1965; bankruptcy is not mentioned as one of the subjects that falls under federal court jurisdiction in the Federal Courts Proclamation of 1996; see Federal Court Proclamation No. 25/1996, *Federal Negarit Gazetta*, 2nd year, No. 13, Article 5.

[15] See Commercial Code, supra note 4, Article 990.

[16] Id, see Articles 1041ff.

multiple creditors is prevented through orderly presentation of claims in a collective proceeding of bankruptcy.
Thirdly, a court of bankruptcy is different from most other court proceedings because the court handles bankruptcy proceedings through the intermediation of other persons - commissioners, trustees, among others (see below). The court of bankruptcy handles few of the cases directly. Most issues arising in bankruptcy proceedings are handled by the trustees and commissioners.

Some of the peculiar features of the court of bankruptcy flow from the nature of actions required to bring bankruptcy proceedings to a successful conclusion. Bankruptcy proceedings are not just about hearing and settling disputes. Bankruptcy proceedings are also about collection of debts, verification of claims, investigation and examination of accounts, settlement of debts and management of businesses (albeit temporarily).[17] Courts may be qualified to oversee others to do these, but they are not qualified to run the day to day business of a bankrupt business. The institutional arrangement for handling bankruptcy proceedings is an acknowledgement of the complexity of bankruptcy. That is why we have a division of labour (or more appropriately, assignment of functions) among the various persons and institutions responsible for the conduct of bankruptcy.

All that remains to do is to confirm the peculiar roles of the court of bankruptcy by reference to some of the provisions of Ethiopian bankruptcy law. It is the court of bankruptcy that sets the whole machinery of bankruptcy in motion -without the imprimatur of the court of bankruptcy, bankruptcy proceedings have not really begun. It is the court to which an application is first made and which orders preliminary investigation before it declares the debtor bankrupt, that declares the debtor bankrupt and fixes the date of suspension of payments, that makes all the appointments as well as removals or replacements of persons who are responsible for running the bankrupt estate.[18]

The bankruptcy court also plays supervisory roles over the activities of the persons appointed to run the bankrupt estate. We may cite several examples of this. The court receives reports or deposits of reports over the activities of these other persons responsible from time to time.[19]

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[17] Id, see Article 1018 and Articles 1035ff.
[18] Id, see Articles 975, 976, 977, 981, 993, 998, 999, and 1002(4).
[19] Id, see Articles 1014, 1015(3).

The third most important role of the court of bankruptcy is to make orders on matters which the other parties cannot. The court decides on the weighty matters affecting the bankrupt estate. The court of bankruptcy gives orders on all matters which are outside the jurisdiction of commissioners, such as sale of business, continuation of business, provisional admission of contested debts and closure of the bankruptcy proceedings. [20] The court of bankruptcy also acts as an appellate body for appeals from the orders of commissioners.[21]

b. Commissioner

The Commercial Code does not define a commissioner. Who is a commissioner, an officer of the court, an outsider? What are the qualifications and characters of a commissioner? The Code offers no clue to these questions. Book V of the Commercial Code is not the only place in Ethiopian laws where a commissioner is mentioned and used. The Ethiopian Civil Procedure of 1965 devotes a section to a commissioner.[22] However, since the Commercial Code came before the Civil Procedure Code, it is doubtful that the Commissioner mentioned in the Commercial Code is the one mentioned in the Civil Procedure Code. The first drafter of Book V of the Commercial Code expressed uneasiness about drafting some provisions because he could not anticipate what the Civil Procedure Code would provide. He actually named some of the provisions 'provisional' expecting them to be eventually superseded by the Civil Procedure Code.[23] Perhaps the case of a commissioner is one of them.

Another way of looking at the office of a commissioner is to treat it as another layer of trustee as a recent report of USAID suggested.[24] Although we are uncertain about the proper place of a commissioner in the Commercial Code, we know where the name came from. The commissioner in bankruptcy is a derivation from the early bankruptcy practice in England, where bankruptcy is taken out of the common law courts and arrogated to the Lord Chancellor of England who appointed five commissioners to make initial adjudications of bankruptcy issues.[25] The

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[20] Id, see Articles 989 1037, 1039, 1049, and 1107.

[21] Id, see Articles 992(2), 1001(2), for example.

[22] See Civil Procedure Code, supra note 14, Articles 122-136.

[23] Peter Winship (ed. and trans.), *Background Documents of the Ethiopian Commercial Code of 1960* (Haile Selassie I University, 1974), at 102 and 104.

[24] United States Agency for International Development (USAID), *Ethiopia: Commercial Law & Institutional Reform and Trade Diagnostic*, January 2007, p. 54.

[25] See Thomas E. Plank, *Why Bankruptcy Judges Need Not and Should Not be Article III*

commissioners were appointed from among the list of bankruptcy commissioners, who were lawyers.[26] The adversarial procedures of the common law courts were deemed unsuitable for bankruptcy proceedings, involving as they did issues of adjusting relationships between an insolvent debtor and his/her many creditors.[27] The commissioners, in the early British bankruptcy practice, dealt with most issues involving bankruptcy proceedings like administering the bankrupt estate, determining the eligibility of the bankruptcy, allowing claims of creditors, distributing the bankrupt estate and discharging the insolvent debtor.[28] They also had important quasi-judicial powers like summoning the bankrupt and others, including the power to put in prison those who refuse their orders.[29] There is reason to believe that the commissioners in the Ethiopian bankruptcy law might have been inspired by this practice in the early English bankruptcy history.

There are three provisions in Book V of the Commercial Code devoted exclusively to the office of the Commissioner. Unfortunately, these provisions betray no hint as to what qualifications and characters are needed for the court to appoint one as a commissioner. There is a phrase in Article 993 of the Code "by another of its members" which seems to imply that a commissioner is appointed from the members of the court (possibly judges themselves). In practice, courts appoint commissioners from members of the public and do not heed the phrase 'by another of its members' in Article 993 of the Commercial Code.[30]

Current laws dealing with the internal administration of Ethiopian court system are silent about commissioners. This silence about commissioners may lead to administrative problems, because their office is not well regulated. We may argue that the commissioners should always be drawn from among the members of the judiciary. Perhaps that is why we find no provisions prescribing the character and qualifications of a commissioner.[31]

Judges, 72 Am. Bankr. L. J. 567 (1998).

[26] Ibid.

[27] Ibid.

[28] Ibid.

[29] Ibid.

[30] See *Selam Public Transport Share Co. vs. Ethio Investment Group PLC* (Federal First Instance Court, Com/File/No. 131125, 2001 E.C., in Amharic, unpublished).

[31] It is interesting to note on the other hand that the qualifications as well as the character of a trustee in bankruptcy are described and prescribed in some detail; see below.

Although the USAID Report casts doubt over the utility of commissioners as additional layers over the trustees, the additional layer is not really uncommon in different bankruptcy systems.[32] OHADA Uniform Bankruptcy Act, for example, requires the appointment of an 'official receiver' 'from amongst the judges of the court' who shall supervise the activities of a receiver or receivers in the conduct of liquidation (bankruptcy) proceedings.[33] The 'official receiver' is the equivalent of the 'commissioner' under Ethiopian bankruptcy law. His/her task is to 'ensure the rapid conduct of the proceedings and look after the interests at stake'.[34] Similarly, under French law, the court appoints a supervisory judge whose task is to 'supervise the speedy progress of the proceedings and the protection of parties' interests.[35] While the names used in different systems vary, it appears that the office of a commissioner might be necessary in bankruptcy proceedings. In fact, in some systems, there are multiple layers of supervision and roles in bankruptcy proceedings. Under the French law, for example, the bankruptcy court appoints not just an administrator

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[32] Interestingly, there was a debate about the utility of a commissioner in the drafting commission, but it was apparently accepted after some debate; see Peter Winship, supra note 23, at 107.

[33] See OHADA Uniform Bankruptcy Act, 1998, Article 35; OHADA is an acronym of the French '*Organisation pour l'Harmonisation du Droit des Affaires en Afrique*' which is translated in English as the 'Organization for the Harmonization of Business Law in Africa'. The Organization was established in 1993 by fourteen Francophone African countries and has since then added two other members. At present, the members of OHADA are Benin, Burkina Faso, Cameroon, The Central African Republic, Chad, the Federal Islamic Republic of Comoros, Congo, Cote d'Ivoire, Equatorial Guinea, Gabon, Guinea, Guinea-Bissau, Mali, Niger, Senegal, and Togo. OHADA has developed a number of uniform acts: General Commercial Law, Commercial Companies and Economic Interest Groups, Collective Proceedings for the Clearing of Debts, Securities, Simplified Recovery Procedures and Enforcement Measures, and Arbitration; see Boris Martor et al, *Business Law in Africa: OHADA and the Harmonization Process* (Eversheds, 2002), at 4-7. The situation might have changed since then in Bahrain, but a dated article on Bahrain bankruptcy law states a similar arrangement under Bahrain bankruptcy system. Under the Bahrain bankruptcy law, bankruptcy judges – the equivalent of commissioners in Ethiopia, are appointed by court to supervise progress of bankruptcy proceedings and make all necessary arrangements for safeguarding the bankrupt's assets; see Richard Price and Christopher Walsh, *the Bahrain Bankruptcy and Composition Law*, 3Arab Law Quarterly3, 254, 256 (Aug. 1988).

[34] See OHADA, supra note 33, Article 39.

[35] See Louis Vogel and Francoise Perochon (trans.), *French Commercial Code*, as updated 03/20/2006, Articles L621-4 and L621-9.

(trustee) and supervisory judge but also court nominees, auctioneers, bailiffs, notaries or accredited commodity brokers.[36]

Whether commissioners are indispensable in bankruptcy proceedings is open to debate, but what they do once they are appointed in bankruptcy is not in doubt. Article 991 of the Commercial Code lists most of the functions of the commissioners in bankruptcy proceedings. Their most important role is one of supervision of the activities of trustees (who as we shall see carry out most of the day-to-day functions) and serving as bridges between the court and the trustee, and the creditors' committee and the trustee.[37] Since commissioners resolve many a dispute that would have ended up in court of bankruptcy, their role in saving judicial time should not be underestimated.

c. Trustees

One of the curious encounters of reading about the trustee in different bankruptcy systems is the multiplicity of names used to refer to the 'person responsible for administering bankruptcy proceedings': administrator, trustee, liquidator, supervisor, receiver, curator, official, judicial manager, commissioner.[38] Sometimes the same legal system adopts multiple names to refer to the person who does the same thing in different contexts. Ethiopian bankruptcy law uses the word 'trustee'; Banking Business Regulation Law uses the word 'receiver'.[39] The Commercial Code uses the word 'liquidator' to refer to a person who does similar things during the dissolution and winding up of companies for other reasons.[40] The Civil Code uses the word trustee in a different context.[41] Even the bankruptcy provisions use the word 'liquidator' and 'receiver' in some instances.[42] Whether it is appropriate to use multiple names is beyond the scope of this piece, but it is something to think about.

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[36] Id, see Article L621-4.

[37] For details, see Commercial Code, supra note 4, Articles 987(1) (d), 987 (2), 991-993, 994(3), 995-999, 1000(3).

[38] See UNCITRAL, supra note 11, p. 174, para. 35.

[39] See Banking Business Proclamation No. 592/2008, *Federal Negarit Gazetta*, 14th year, No. 57, Article 2(16).

[40] See Commercial Code, supra note 4, Articles 495-509.

[41] See the Civil Code of Ethiopia (1960), *Negarit Gazetta*, Gezette Extraordinary, 19th year, No. 2, Articles 516-544.

[42] See Commercial Code, supra note 4, Articles 1039 (3) and 1145.

Given the centrality of trustees to bankruptcy proceedings, it is generally agreed that trustees should be closely regulated in terms of qualifications, appointments, duties and liabilities.[43] In the area of qualifications - i.e., in terms of knowledge, experience and personal qualities required to occupy the office of a trustee, there are inevitably differences in how strongly and minutely the trustee is regulated by bankruptcy laws or laws related with bankruptcy law.[44]

While the complexity of bankruptcy proceedings in general makes it desirable to seek an 'appropriately qualified' trustee with knowledge of the law and adequate experience in commercial and financial matters,[45] one must be pragmatic in what qualified persons may be found in the market to occupy the positions of a trustee. Where the pool of qualified persons is limited, the courts should have enough latitude to draw trustees from the available pool. Depending on the depth and quality of the pool, the thresholds for qualifications may include requirements for 'professional qualifications and examinations', licensing, specialized training courses and certification examinations, and experience in some areas like finance, commerce, accounting and law.[46]

In some countries, strict regulation of the qualification of trustees may be facetious and unrealistic, given the limited pool of qualified persons to fill the position of trustees. It may be desirable in these countries to leave the qualification to the discretion of courts. Ethiopian bankruptcy law recognizes this limitation and leaves the matter to the Ministry of Commerce and Industry. Trustees are to be 'selected from the list of qualified persons of good repute resident in Ethiopia'.[47] The 'list of qualified persons' is to be prepared by the Ministry of Commerce (now Trade) and Industry but the Ministry has done nothing of the kind so far.

Perhaps, more important than the professional qualifications of a trustee are the personal qualities. The name trustee is evocative of some one who 'holds property in trust for the benefit of another and owes a fiduciary duty',[48] which ordinarily means that the trustee must possess certain

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[43] UNCITRAL, supra note 11, p. 174, para. 35.

[44] Id, pp. 174-176, paras. 36-43; see also *Collier's Bankruptcy Manual* (3d edition), p. 321.02

[45] UNCITRAL, supra note 11, p. 175, para. 39.

[46] Id, p. 175, para. 40.

[47] See Commercial Code, supra note 4, Article 994(1).

[48] See Bryan A. Garner (ed.), *Black's Law Dictionary* (7th edition, West Group, 1999)

personal qualities, like 'integrity, impartiality, independence and good management skills'.[49] Integrity requires that a person selected as a trustee has 'sound reputation and no criminal record or record of financial wrongdoing' and in some cases 'no previous insolvency or removal from public administration'.[50]

Impartiality and independence generally require the trustee to be free from conflicts of interest-what the UNCITRAL Legislative Guide (hereinafter simply the Guide) calls 'independence from vested interests, whether of an economic, familial or other nature'.[51] Conflicts of interest may arise from prior or existing relationships.[52] The Guide gives a full spectrum of instances in which the conflicts may arise:

> Prior ownership of the [business of] debtor; a prior or existing business relationship with the debtor (including being a party to a transaction with the debtor that may be subject to investigation in the insolvency proceedings and being a creditor or debtor of the debtor) a relationship with a creditor of the debtor; prior engagement as a representative or officer of the debtor; prior engagement as an auditor of the debtor; and a relationship with a competitor of the debtor...[53]

Ethiopian bankruptcy law does not list the positive qualities possessed of trustees like 'integrity', 'impartiality' or 'independence'. But some of these qualities are intimated. For example, the Commercial Code proscribes certain persons from the position of trustee - persons who have been declared bankrupt and persons who are deprived of civil rights [54] - because it presumes that these persons lack the integrity required to fulfill the roles of a trustee. The Code also proscribes persons who are related to the bankrupt debtor either by consanguinity or affinity from being appointed as trustees;[55] it also prohibits the appointment of creditors of the debtor[56] because these persons lack the 'independence' required to carry out the duties of trustees. Even after trustees are appointed, they are prohibited

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[49] UNCITRAL, supra note 11, p. 175, para. 41.
[50] Id, p. 176, para. 41.
[51] Id, p. 176, para. 42.
[52] Id, p. 176, para. 43.
[53] Ibid.
[54] See, Commercial Code, supra note 4, Article 994 (4) (a) & (b).
[55] Id, Article 994(4) (c).
[56] Id, Article 994(4) (d).

from 'self-dealing' (from acquisition of goods of the debtor) [57] because their 'impartiality' will be compromised through self-dealing.

A cursory comparison of the prohibitions in the Ethiopian bankruptcy law with the Guide reveals that cases in which conflicts of interest may arise or cases which compromise the integrity, impartiality or independence of trustees are not exhausted in the Ethiopian law. The integrity of a trustee may be vitiated by prior or existing business relationships (not necessarily creditor-debtor relationship), prior ownership of the debtor, a relationship with a creditor of the debtor, prior associations with the debtor as a representative or officer of the debtor, or even a relationship with the judge of court of bankruptcy, etc.[58] The provision that proscribes relatives from being appointed as trustees may be appropriate for natural persons but it does not cover business affiliations or relationships. These business affiliations may affect the integrity or impartiality of the trustee as much as the bonds of blood or marriage.[59] Although Ethiopian bankruptcy law is not exhaustive, it is not limiting. Courts may consider some of these additional factors in their appointments of trustees. Detailed regulations in this regard are not necessarily desirable anyway. Excessively prohibitive rules may circumscribe the options of courts as to dry up the available pool of qualified persons altogether. It may sometimes be appropriate for courts to appoint qualified persons as trustees in spite of the risks of conflicts of interest and then exercise powers of removal or replacement when a trustee so appointed has compromised his/her integrities.

d. Creditors' Committee

Like the name of trustees, different bankruptcy laws use different names to refer to an organ tasked with the functions of creditor's committee. Some laws use the expression 'bankruptcy controllers' or simply 'controllers', which may be a more apt name, given the role of creditor's committee in bankruptcy proceedings.[60] Under French law, the controllers (five in

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[57] Id, see Article 994 (5).

[58] See UNCITRAL, supra note 11, p. 176, para. 43; see Tilahun and Taddese, supra note 3, at 90; under the US Bankruptcy Code, a relative or even a person connected with the bankruptcy judge may not be appointed trustee; US Bankruptcy Code, Rule 5002(a), quoted in Collier's Bankruptcy Manual, supra note 44, p. 321.03.

[59] Compare Article L621-5 of French Code in this regard, which states 'No relatives or affines, up to a fourth degree included, of the head of the business or the managers, if the debtor is a legal entity, may be appointed to any one of the positions provided for ... except where this provision prohibits the appointment of an employee's representative.' See French Commercial Code, supra note 35.

[60] See Richard Price and Christopher Walsh, supra note 33, at 256.

number) are appointed by the supervisory judge (commissioner) 'from among those creditors requesting to be appointed'.[61]
OHADA Uniform bankruptcy Act uses a less common expression - assignees.[62]

The establishment of creditors' committee is recognition of the need to facilitate creditors' participation in bankruptcy proceedings.[63] As the first drafter of the Commercial Code stated, the creation of the creditors' committee is borne of the realization that 'general meetings of creditors would be too cumbersome to operate and too difficult to convene'.[64] The existence of the committee is not necessary in all bankruptcy proceedings, although Ethiopian law makes no exceptions.[65] It is clearly appropriate to have one where there are a very large number of creditors with diverse interests.[66]

One issue that needs to be resolved is what creditors are entitled to be appointed to the committee.[67] Particularly where the debtor has large numbers of creditors, disputes may erupt over the selection of some creditors for the committee. What factors should then be taken into account to qualify a creditor for the committee membership? Approaches to the formation of creditors' committee vary among different bankruptcy laws.[68] Some bankruptcy laws restrict membership to those creditors whose claims are verified and admitted.[69] Others make restrictions on location of creditors, presumably to overcome the challenges of distance for frequent meeting of the committee members.[70] Some systems permit the formation of separate committees for different categories of creditors (trade creditors, finance creditors, etc).[71] French bankruptcy law requires that at least one of

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[61] See French Commercial Code, supra note 35, Article L621-10; incidentally, French bankruptcy law uses 'creditors' committee' to refer to a creditors' committee set up to review and approve a reorganization plan - which is a much more specific act; see Articles L626-29 to L626-31 of French Code.
[62] See OHADA, supra note 33, Articles 48-49.
[63] UNCITRAL, supra note 11, p. 197, para. 99.
[64] See Peter Winship, supra note 23, p. 108.
[65] UNCITRAL, supra note 11, p. 197, para. 99.
[66] Ibid.
[67] Id, pp. 197-198, para. 101.
[68] See id, pp. 197-198, paras. 101-106.
[69] Id, p. 198, para. 101.
[70] Ibid.
[71] Id, p. 198, para. 102.

the creditors be from among secured creditors and one from among unsecured creditors if several member-creditors' committee is constituted.[72] Ethiopian bankruptcy law is clear in some respects and vague in others. We know that the committee members are to be selected by the commissioner from among all the creditors. And we know that the total number of members in a committee is either three or five -always an odd number to prevent ties from stalling committee decisions or opinions.[73] We also know that the committee is constituted after the list of creditors is deposited with the registrar.[74] The list includes both claims of creditors that are admitted and those that are rejected. It will be extraordinary if the commissioner chooses a creditor whose claims are rejected in the said list.

This much is clear. What is not clear is what factors the commissioner will take into account to select committee members. It appears that the commissioner has full discretion in this - may even afford to be arbitrary (there is nothing wrong if he casts lots to select members). The only restriction on the discretion of the commissioner is the rule that proscribes the selection of creditors who are related to a debtor either by consanguinity or affinity up to a fourth degree.[75]

Another issue is the role of the Committee. The Commercial Code does not make any distinctions among the different roles of the creditors' committee, but it is useful to divide the role of the committee into three roles: advisory, control and decisive functions.[76]

In its advisory roles, the opinion of the committee is sought when some issues affecting the bankruptcy proceedings are on the table. These include compromise and arbitration of claims concerning the bankrupt estate;[77] a proposal of composition by the debtor;[78] lump sale of assets during compulsory winding up[79] and a proposal of distribution upon compulsory

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[72] See French Commercial Code, supra note 35, Article L621-10.

[73] Commercial Code, supra note 4, Article 1002(3).

[74] Id, see Article 1044.

[75] Id, see Article 1002(5).

[76] Under different bankruptcy laws, the creditors' committee may undertake a range of functions: (i) advising a trustee of the wishes of creditors with respect to issues like the sale of business assets outside the ordinary course of business; (ii) consulting with a trustee on issues like the existing management of the bankrupt estate; and (iii) supervising a trustee; see UNCITRAL, supra note 11, pp. 200-201, paras. 110-112.

[77] Commercial Code, supra note 4, Art. 1038(1).

[78] Id, Art. 1082(1) and (4).

[79] Id, Art. 1107.

winding up[80]. On these issues, the opinion or recommendations of the committee carry some weight, but they are not decisive of the results. Those who make the ultimate decisions (the commissioner, the trustee, the court, etc) must take the opinion of the committee into account, although they are not bound by them. The committee's opinion is clearly a factor in how they reach a decision.

The second function of the committee is control.[81] In its control function, the committee participates in bankruptcy proceedings by having presence during verification of claims.[82] The third function is the strongest of all the powers of the committee: it is decisive. There is one instance - if the bare language of the Code is to be believed- in which the Committee assumes a decision making role during bankruptcy proceedings, and that is when assistance is to be given to the debtor and family after the compulsory winding up is commenced.[83]

e. Other Persons in Bankruptcy Proceedings: the Public Prosecutor, the Debtor, and others

Other persons responsible in bankruptcy proceedings -albeit in minor capacities- are mentioned in various provisions of the Ethiopian bankruptcy law -although no specific section is devoted to any one of them in particular. We have, for example, some provisions mentioning the public prosecutor. The public prosecutor is mentioned as one of the parties that can initiate bankruptcy proceedings against debtors, most likely as result of criminal investigations into the financial affairs of debtors.[84] The public prosecutor may also be called into action when a debtor, summoned to appear, fails to appear during the closing of the debtor's books.[85]

The bankrupt debtor has been stripped off most of his/her powers during bankruptcy, but s/he is not out of the picture completely. Even when the debtor is responsible for the bankruptcy, it is impossible to conduct bankruptcy proceedings without the presence and action in some capacity of the bankrupt debtor. Ethiopian bankruptcy law takes this reality into account and authorizes trustees to 'employ' the bankrupt debtor 'on such

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[80] Id, Article 1109(2).

[81] That is why in some bankruptcy systems, the committee has a name of controllers - which is an apt expression, see above.

[82] Commercial Code, supra note 4, Article 1043(1).

[83] Id, see Article 1102; note that before the compulsory winding up, the decision over the matter rests with the commissioner; id, see Article 1020.

[84] Id, see Article 975(c).

[85] Id, see Article 1004(4).

terms and conditions as the commissioner' shall fix.[86] The assistance of the debtor is critical in the successful winding up of the bankrupt business particularly when a decision is made to sell the business as a going concern, in which 'the debtor's detailed knowledge of the business and the relevant market or industry, as well as its ongoing relationship with creditors, suppliers and customers' might come in handy.[87] Apart from these limited cases, the debtor is mostly passive during bankruptcy proceedings - for legitimate reasons - the bankrupt estate needs protection from the bankrupt debtor. In the alternatives to the bankruptcy proceedings - composition and schemes of arrangement - the debtor is decidedly more actively involved both in the initiation of these proceedings and in getting the proposals approved (see below).[88]

Ethiopian bankruptcy law also anticipates that other persons might be needed during bankruptcy proceedings. Article 1015 of the Commercial Code authorizes trustees (with the consent of commissioner) to employ 'suitable persons' for 'preparing the inventory and valuation of the debtor's property'.[89] The 'suitable persons' have names in other bankruptcy laws. The French Code, for example, has a list of names for those persons who participate in taking inventory and valuation of the debtor's property: auctioneers, bailiffs, a notary or an accredited commodity broker.[90] We may need the services of these other persons in some large and complex bankruptcy proceedings.

II

3. Effects of Bankruptcy

The Commercial Code treats the effects of bankruptcy in Chapter 4 of Title II of Book V (Articles 1019-1040). The effects are divided into two - effects as regards the debtor (Section I) and effects on the management of the property (Section II). Closer reading of Section I (effects as regards the debtor) will reveal that the section covers more than just the effects upon the debtor. The judgment of bankruptcy affects not just the debtor but also creditors and at times even third parties. The effects as regards the management of property address various issues that are better treated under various subjects. These effects have already partly been dealt with above in connection with the power of trustees, and we will have occasion

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[86] Id, see Article 1021.

[87] UNCITRAL, supra note 11, p. 162, para. 3.

[88] See Commercial Code, supra note 4, Articles 1081, 1119 and 1132, among others.

[89] Id, see Article 1015(4).

[90] See French Commercial Code, supra note 35, Article L621-4.

to deal with them below under the section on the effects of bankruptcy on contracts and leases (see below).

It is helpful to break Section I of Chapter 4 down to three parts based on the simple criterion of the person/s affected by bankruptcy. The title of section II of Chapter 4 of Title I of Book V is, in a sense, misleading. It makes more sense if the said section is divided as follows:

> Section I: Effects of Bankruptcy upon the Debtor
> Section II: Effects of Bankruptcy upon the Creditors of the Bankrupt Debtor
> Section III: Effects of Bankruptcy upon Third Parties (or more appropriately, Invalidation of Certain transactions during the Suspect Period).

We will deal with the three parts separately.

a. Effects of Bankruptcy Upon the Bankrupt Debtor

The Commercial Code lists the effects of bankruptcy upon the bankrupt debtor in a more or less haphazard manner. It would again make sense to classify these effects into two: personal and proprietary (pecuniary) effects.

i. Personal Effects of Bankruptcy

1. Restriction of Personal Freedom

The personal effects of bankruptcy are stated in Articles 1019 and 1022 of the Code. The personal effects (some of them in any event) are a reflection of the times during which the Code was written.[91] The first drafter of Book V was perfectly aware of this orientation of Ethiopian bankruptcy law. Having weighed the options out there, whether to view bankruptcy as 'blameworthy' or only as a 'simple accident of commercial life,'[92] the drafter went for the idea that bankruptcy should be associated with blameworthiness.[93] Articles 1019 and 1022 are inserted in the Code to stress

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[91] See Peter Winship, supra note 23, at 103.

[92] Id at100.

[93] Id at 103; 'faulliti sunt deceptores et fraudotores' (bankrupts are deceivers and frauds) is how bankrupts were labeled in medieval Italy, from which bankruptcy practice emerged; see Volkmar Gessner et al, *Three Functions of Bankruptcy Law: The West German Case*, 12Law & Society Review4, 499, 531 (Summer, 1978).

this fact about Ethiopian bankruptcy law.[94] They project bankruptcy as something of a stigma and they are built upon suspicion.[95]

Article 1019 of the Code provides that bankruptcy results in the restriction of the freedom of movement of the debtor. The bankrupt debtor 'may not leave the area in which he resides without the permission of the commissioner.' Article 1019 of the Code appears to make the 'restriction of freedom' automatic. And, the restriction appears to apply to all bankrupt debtors, which means that a judgment of bankruptcy does not have to make specific reference to it. Be that as it may, the enforcement of the restriction leads to some practical difficulties.

There is reason to doubt if the restriction on debtor's movement is an automatic consequence of bankruptcy. First of all, the delimitation of the 'area in which the debtor resides' would require a specific order to that effect. For the restriction to be meaningful, we must expect the court of bankruptcy to make a specific order that the bankrupt debtor not leave an area whose geographical limits are known. Although this is not specifically mentioned as one of the orders the court of bankruptcy makes in its judgment of bankruptcy,[96] it would appear that the specific order is necessary if Article 1019 of the Code is to take effect. Secondly, Article 1019 refers us to Article 433 of the Penal Code of 1957 (now Article 440 of the new Criminal Code of 2004) for dealing with debtors who have violated the restriction under Article 1019. Article 433 of the 1957 Penal Code (and Article 440 of the new Criminal Code) talks about the offense of 'resisting authority'.[97] The material element of the offense of 'resisting authority' is a violation of a 'specific order given by either a public servant' or a 'lawful decision of a competent authority'. Without the specific order or a lawful decision, the offense itself does not exist. We cannot expect the material element of the offense to change just to accommodate the ambiguous language of the Commercial Code. Therefore, although the language of Article 1019 of the Code appears to automatically attach the restriction of the debtor's freedom of movement, the nature of the offense forces us to

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[94] See Peter Winship, supra note 23, at 103.

[95] These are just the beginning of punitive elements in Ethiopian bankruptcy law; as we shall see later, the punishment may even extend beyond the closing of bankruptcy proceedings; See, discharge, below.

[96] See Commercial Code, supra note 4, Article 977.

[97] The new Criminal Code prescribes a simple imprisonment of not exceeding one year or a fine not exceeding one thousand Birr; the punishment was one month or a fine not exceeding one hundred Birr under the 1957 Penal Code.

accept that the personal restriction attaches only if there is a specific order of the court to that effect. If the specific order can be adduced, it is possible to determine whether the bankrupt debtor has violated that order and it is possible to characterize that violation as an 'offense of resisting authority' under the new Criminal Code.

In any event, at present the questions surrounding Article 1019 should not really be about its various shades of meaning but whether it is necessary at all. First, Article 1019 makes no distinction between a debtor who, through his actions, is responsible for bankruptcy and a debtor who is quite simply a victim of unfortunate turn of events and finds himself in bankruptcy. Secondly, as we shall soon see, the debtor is dispossessed of his power to administer upon declaration of bankruptcy anyway and his whereabouts are in many instances irrelevant. Thirdly, survey of the bankruptcy laws of some other countries reveals that personal restriction of freedom of movement is no longer a feature of modern bankruptcy systems. Although some bankruptcy laws still retain some form of restriction of freedom of movement as a consequence of bankruptcy, many modern bankruptcy laws do not even mention it.[98] There are still countries which have retained restriction of freedom in their bankruptcy laws but they are in the minority.[99]

Even if the physical presence of the bankrupt debtor were necessary, the matter could be left to the discretion of the court of bankruptcy. The court might order some restrictions in cases where there is a real threat that the debtor might abscond while the bankruptcy proceeding is pending. It is also possible that where the debtor is inclined to abscond, the criminal justice system might have caught up with him for offenses related with bankruptcy. If alertness on both sides is warranted, it might be argued that both the bankruptcy court and the criminal division court should be able to restrict freedom of movement where absconding is a real and distinct possibility.

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[98] See French Commercial Code, supra note 35, Articles L653-1 to L653-11; OHADA, supra note 33; see also Richard W. Maloy, *Comparative Bankruptcy*, 24 Suffolk Transnat'l L. Rev.1 (Winter, 2000).

[99] In Poland and Taiwan, the bankrupt debtor cannot leave his or her residence without the permission of the court, and in Mexico, the bankrupt debtor is confined to the boundaries of the court's venue unless he or she is granted permission to leave; see Richard W. Maloy, supra note 98

Article 1019 is not merely a reflection of its time, but also of the modus operandi of the drafting of the different Codes in the 1950s. On the one hand, the drafters were reluctant to incorporate penal provisions in the Commercial Code,[100] but on the other hand, they were anxious not to leave anything to chance - hence at least a mention of the restriction in the Commercial Code. This however has an unintended consequence of uncertainty as to when and in what context the restriction is to be imposed.

2. Prohibitions and Forfeitures

Article 1022 of the Commercial Code (which incidentally should come immediately after 1019) adds another restriction, which might be taken to have both personal and proprietary effects. Article 1022 uses general expressions to denote these restrictions: prohibitions and forfeitures. But unlike Article 1019, which as we have seen uses a strong language of peremptory nature, Article 1022 uses a permissive language and defers these prohibitions and forfeitures to other laws: 'The bankrupt [debtor] may be subjected to such prohibitions or forfeitures as are provided by law.'

The restrictions, whatever form they might take, depend on other laws. The prohibitions or forfeitures are not defined in the Commercial Code. The second sentence of Article 1022 itself gives a hint as to what form these restrictions might take: 'Unless otherwise provided by law, such prohibitions or forfeitures shall cease to be effective where the convicted bankrupt is reinstated.'

The use of the expressions 'convicted bankrupt' and 'reinstated' immediately brings to mind cases in which a convicted person is subject to additional penalties by a criminal division court.

Prohibitions or forfeitures resulting from bankruptcy are found scattered in other laws of Ethiopia. We will just take two examples. The first example of a prohibition is offered in the bankruptcy law itself, although no direct reference is made in Article 1022 of the Code. Article 994 (4) (a) of the Code proscribes a person declared bankrupt from occupying the position of a trustee. This proscription does not obviously apply to the bankrupt debtor, for a debtor may not be appointed a trustee in his own bankruptcy in any case, but it applies to all persons other than the bankrupt debtor who were declared bankrupt previously.

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[100] Peter Winship, supra note 23, at 102.

The second example of prohibition or forfeiture is to be found in the Criminal Code. Articles 121-128 of the Criminal Code of Ethiopia (of 2004) provide examples of prohibitions that might ensue from declaration of bankruptcy. Unlike the possible rendering of Article 1019, these effects (what the new Criminal Code calls 'secondary punishments')[101] are not automatic. The 'secondary punishments' take effect only if the 'court has expressly so directed.' In so directing, the court may be guided by their aim and the result they would achieve on the safety and rehabilitation of the criminal.[102] These 'punishments' are typically ordered in practice in addition to the primary punishments like fine and imprisonment.

Secondary punishments, according to the new Criminal Code of 2004, include caution, reprimand, admonishment and apology, and 'where the nature of the crime and the circumstances under which the crime was committed justify' a deprivation of rights of the offender.[103] The deprivation of rights include civil rights, such as the 'right to vote, to take part in any election, or to be elected in any public office... to be a witness or a surety... to serve as an assessor',[104] the right to exercise family rights, such as parental authority, tutorship or guardianship,[105] and the right to exercise a profession, art, trade, or to carry on any industry or commerce.[106]

Of the long list of the deprivation of rights in the Criminal Code, the ones that seem reasonably likely to be ordered by a court in connection with bankruptcy is the deprivation of the right to exercise a profession, trade or to carry on any industry or commerce. The offenses that have some affinity with bankruptcy are 'fraudulent insolvency,'[107] 'irregular bankruptcy,'[108] and 'fraudulent bankruptcy'.[109] A debtor who has been convicted of any of these offenses under the Criminal Code may be subject to the secondary punishment of the right to run any business (not just his current business, which as we shall soon see, is automatic).

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[101] See the New Criminal Code of Ethiopia (2004), supra note 12, the Title of Section II.
[102] Id, see Article 121.
[103] Id, see Articles 122(1) and 123.
[104] Id, Article 123 (a).
[105] Id, Article 123 (b).
[106] Id, Article 123 (c).
[107] Id, Article 725.
[108] Id, Article 726.
[109] Id, Article 727.

These deprivations of rights may be permanent or temporary, depending on the discretion of the court.[110] Where temporary, deprivation may last from six months to five years.[111] Except in gravest of instances, none of the offenses connected with bankruptcy is ever likely to lead to permanent loss of rights.

Because of the dual organization of Ethiopian bankruptcy law (it has separate section dealing with additional rules of bankruptcy regarding business organizations),[112] we may forget that the effects of bankruptcy attach not just to debtors but also to partners jointly and severally (in the case of partnerships) and 'any person who has carried out commercial operations on his own behalf and disposed of company funds as though they were his own and concealed his activities under the cover of such company' (in case of share companies and private limited companies).[113] In the case of business organizations, the restriction of freedom of movement may not apply to the business organizations but where the judgment of bankruptcy names the partners (in the case of partnerships) and the managers and possibly directors (in the case of share companies and private limited companies) as commonly bankrupt with the business organization, the individuals named are subject to the effects of bankruptcy. Their freedom is restricted; and the prohibitions and forfeitures apply to them.

Whatever the specifics of prohibitions or forfeitures might be, the Commercial Code, true to the determination of the drafters to keep criminal provisions out of the Code, simply defers these matters to other laws, such as the Criminal Code.[114] This approach of the Commercial Code contrasts sharply with some other bankruptcy laws in the modern times. The French Commercial Code, for instance, lists the types of what it calls 'disqualifications and forfeitures' in the Commercial Code itself.[115] These disqualifications are the equivalent of our 'prohibitions and forfeitures'. They, for example, include disqualifications from running, managing, administering, controlling any business organization, denial of voting

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[110] Id, see Article 124.

[111] Ibid.

[112] See Commercial Code, supra note 4, Title IV, Book V, Articles 1154-1165.

[113] Id, see Article 1158 and 1160.

[114] See Myron M. Sheinfeld ,Teresa L. Maines, and Mark W. Wege, *Civil Forfeiture and Bankruptcy: The Conflicting Interests of the Debtor, Its Creditors and the Government*, 69 Am. Bankr. L.J. 87 (Winter, 1995)

[115] See the French Commercial Code, supra note 35, Articles L653-1 to L653-11.

rights, forced sales of shares, ineligibility for public offices, prohibition from issuing cheques and ineligibility for public procurement contracts.[116] Similarly, OHADA Uniform Bankruptcy Act (1998) has a separate section devoted to what it calls 'personal bankruptcies'.[117] The prohibitions resulting from personal bankruptcy in the OHADA Uniform Act of 1998 include a general ban to trade, direct, manage, administer or control an individual business or corporate body, a ban to hold an elective office or to be an elector for the said public office; a ban to hold any administrative, legal or professional representation office.[118]

Where the prohibitions or forfeitures are found or listed might be more a matter of approach than of substance, but listing these in the Commercial Code has the virtue of treating these matters as directly flowing from bankruptcy proceedings and avoids the risk of neglecting these matters whenever bankruptcy proceedings are set in motion.

ii. Proprietary Effects of Bankruptcy

The most significant effect of bankruptcy under Ethiopian law is the dispossession of the bankrupt debtor.[119] In this the bankruptcy law leaves no discretion whatsoever. However the bankruptcy has come about (or whether the bankruptcy is the making of the debtor or not), the debtor is deprived of his right to administer or dispose of his property. As usual, there is no better way of approximating its meaning than analyzing its language. Article 1023 of the Commercial Code states: 'A bankrupt shall not administer or dispose of his property, however acquired, from the day he is declared bankrupt until he is discharged'.

A number of questions may be treated in connection with the issue of dispossession of the bankrupt debtor (an article in its own right). For the purposes of this article, we wish to address ourselves to two important questions:

i) What is the extent of the debtor's dispossession; in other words, what is the scope of the bankrupt estate, from whose administration the debtor is removed?

ii) How does one effect dispossession in the case of business organizations where the persons who run the organization are not really the debtors?

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[116] Id, see Article L653-2, L653-8, L653-9.

[117] See OHADA, supra note 33, Part III, Chapter I, Articles 196-203.

[118] Id, Article 203.

[119] Commercial Code, supra note 4, Article 1023.

Let us address ourselves to the first question first. It is quite striking that although the word 'property' is frequently mentioned in several places in Book V,[120] no attempt is made to define the scope of property for purposes of bankruptcy, perhaps leaving the matter (as is often the custom) to general laws of Ethiopia. But it is quite possible that the term 'property' is not given to uniform definition and a general meaning of it in the Civil Code might not be suitable for bankruptcy purposes. Article 1023 talks about the consequences of bankruptcy upon the debtor without properly defining what his property consists in. A definition (at least of listing property included in a bankrupt estate and excluded from it) would have been desirable but we find none of that in our bankruptcy law.

A clear definition of the property subject to bankruptcy proceedings is critical for obvious reasons.[121] The identification of property subject to bankruptcy proceedings (preferably from a general definition) will "determine the scope and conduct of the proceeding" and "ensure transparency and predictability for both creditors and the debtor".[122] As is to be expected, the Guide supplies the best definition in this regard. According to the Guide, the bankrupt estate may:

> ... include all assets of the debtor, wherever located, whether in the forum or a foreign state, whether or not in the possession of the debtor at the time of commencement [of bankruptcy proceeding], and including all tangible (whether movable or immovable) and intangible assets... the debtor's rights and interests in encumbered assets in third party owned assets.... Assets acquired by either the debtor or the insolvency representative [trustee] after commencement of the insolvency proceedings (subject to specific exclusions that would apply in the case of natural person debtors....) and assets recovered through avoidance or other actions..... [123]

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[120] Id, see for example, Articles 1026, 1028, 1035.

[121] See Michael M. Parker, *Bankruptcy Primer*, 24 Colorado Lawyer, 1561 (July 1995).

[122] UNCITRAL, supra note 11, p. 75, para. 3.

[123] UNCITRAL, supra note 11, pp 75-76, para. 4; see also Felix Lopez, *Creditors' Rights under Spanish Law, 33 Am J Comp L2, 259, 272 (1985);* under Spanish law, goods and assets which are in debtor's possession but not owned by the debtor are set aside and transferred to their owners; certain secured creditors (pledges, ship mortgagees, ordinary mortgagees) are entitled to retain the collateral and to initiate a foreclosure in order to recover the amount of their claims; see also Pamela Krauss, *Unsettled Existence: The Fate of Licensed Intellectual Property Rights upon the Bankruptcy or Insolvency of the Licensor*, 19 Intellectual Property Journal, 149 (June, 2005).

At the other end of the spectrum we find property excluded from the bankruptcy proceedings. Their identification is equally (if not more) important. Again, we turn to the Guide for identification of these assets in general:

> ...assets owned by a third party that are in possession of the debtor ... such as trust assets and assets subject to an arrangement (whether contractual or otherwise) that does not involve a transfer of title but rather the use of the assets and return to the owner once the purpose for which they were in the possession of the debtor has been fulfilled....assets subject... to reclamation, such as goods supplied to the debtor before commencement but not paid for and recoverable by the supplier....[124]

And, where the bankrupt debtor is a natural person:

> ... post-application earnings from the provision of personal services by the debtor or monies received for public works by the debtor, assets ... necessary ... to earn a living and personal and household assets, such as furniture, household equipment, bedding, clothing and other assets necessary to satisfy the basic domestic needs of the debtor and his family.[125]

Between these opposite poles of inclusion and exclusion, there are many types of assets,[126] whose treatment are ambiguous and controversial (and ultimately depend on the choice made by a particular bankruptcy law of a country). These types of assets include encumbered assets, joint assets, assets located in a foreign country, some intangible assets, third-party-owned assets, in which the debtor has an interest.[127] The Guide supplies a number of alternative approaches to the treatment of these 'borderline' assets.[128] On the treatment of joint assets, just to give one example, the Guide provides approaches of complete exclusion from the bankrupt estate or inclusion of the part (or portion) belonging to the bankrupt debtor.[129] In any event, it is desirable that (whatever approach is taken in any particular case), the position of the law is expressed in clear language. The approach taken is not purely a matter of taste but one of policy and expedience. The

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[124] UNCITRAL, supra note 11, p. 80, para. 17; see also *Property of the Estate*,1 Bankr. Dev. J. 331 (1984).

[125] UNCITRAL, supra note 11, p. 80, para. 18.

[126] In this context, I use 'assets' to refer generally to property. I prefer assets to property because it is flexible to use both in the singular and plural.

[127] See, UNCITRAL, supra note 11, pp 76-79, 81, paras. 7-14 and 20-21.

[128] Id, see pp. 77-81, paras. 20-21.

[129] See id, p. 81, para. 21.

choice between different approaches may depend on laws other than bankruptcy law (e.g. family law), and "factors such as the ease with which the assets may be divided"[130] in the case of joint assets.

As alluded to before, Article 1023 of the Code supplies a less than satisfactory definition to the concept of "bankrupt property" (and obliquely as that): '... his [debtor's] property, however acquired...'

Since Article 1023 was intended by the drafter as a provision stating one of the effects of bankruptcy upon the debtor, it was never intended as a definition of a property subject to bankruptcy. It might therefore be a perversion to call it by something other than what it was intended for. Although we have no definition of property included in a bankrupt estate and excluded from it under Ethiopian law, we have hints in many provisions of Ethiopian law of both varieties. Let us look at some of them. Article 1018 of the Commercial Code is one of these provisions. One of the first tasks of trustees is the preparation of 'a balance sheet based on the books, documents papers and other information as available to them'.[131] The balance sheet is prepared with full knowledge and acknowledgment of the debtor.[132] Upon the completion of the inventory, there is a formal 'ceremony' of handing over of the debtor's property to the trustee. The lists of property to be 'handed over' include "all goods, money, securities, books, papers and documents, furniture and chattels of the debtor...".[133] Such handing over is verified by a note at the foot of the inventory (in which all parties involved attest by their signature of what property has been handed over).[134] In all likelihood a property that has been handed through a formal 'ceremony' is part of the bankrupt estate. It does not mean that the handing over will be smooth but once it is signed by the parties involved, it is an evidence that the trustee shall thenceforward exercise full powers over such property.

But that is not all. At the time of the handing over, there is a lot of property potentially belonging to the debtor but not in a position to be handed over physically[135] because such property is in the hands of third parties.

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[130] Ibid.

[131] Commercial Code, supra note 4, Article 1014.

[132] Commercial Code, supra note 4, see Article 1015(1).

[133] Id, Article 1018.

[134] Ibid

[135] By the way, the process of handing over is by no means clear. UNCITRAL Guide provides two approaches. In some countries, legal title over the assets is transferred to

Bankruptcy does not come after the debtor has collected all property interests in the hands of third parties and put all his affairs in order. In recognition of this reality, Ethiopian law authorizes the trustee to collect all debts from third parties owing to the debtor.[136] The question is which debts? At the time of the judgment of bankruptcy, the bankrupt debtor may be owed a variety of debts, some directly related to the business which has now gone bankrupt and some personal to the debtor (where the debtor is a natural person). We may all agree that the trustee should collect debts owed in connection with the business. But how about debts owed to the debtor for personal torts like defamation, for injury to credit or reputation or personal bodily injury inflicted upon the debtor? Under Ethiopian bankruptcy law, although the distinction is made between 'debts relating to' the debtor's commercial activities and other debts for purposes of commencement of bankruptcy, this distinction is not maintained once the debtor is declared bankrupt.[137] If one is to go with the literal meaning of Article 1035(2) of the Code, therefore, the trustee is authorized to collect even personal debts owed to the debtor at the time of the commencement of the bankruptcy.[138]

There is another species of property belonging to third parties (or in the hands of third parties) which the law again authorizes the trustee to recover/reclaim for the interest of creditors of the bankrupt estate.[139] These are assets transferred by the debtor at the time when his bankruptcy became imminent. This period, known as 'suspect period' (see below), is a period when the debtor is suspected to have acted in connivance with third

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trustees while in others the bankrupt debtor remains the legal owner of the assets but his powers to administer and dispose of these assets is limited, See UNCITRAL, supra note 11, p. 75, para. 2.

[136] Commercial Code, supra note 4, Article 1035(2).

[137] See Taddese Lencho, *Ethiopian Bankruptcy Law: Commentary (Part I)*, 22J. Eth. L.2, 57, 89-94(Dec. 2008); the UNCITRAL Guide states that some countries do not allow trustees to recover debts of personal nature like defamation for the benefit of the bankrupt estate. The debtor, in these countries, "remains personally entitled to sue and retain what is recovered in such actions", See UNCITRAL, supra note 11, p. 80, para. 18; for the contrary position, see *Collier's Bankruptcy Manual* (2d Edition Revised, Matthew Bender & Company, Inc., 2010), at 541.07.

[138] By the way, these controversies will not arise in connection with business organizations unless the court ordered the bankruptcy of members (partners) or officers (managers) of the business organization along with the bankruptcy of the business organization itself; see Commercial Code, supra note 4, Articles 1158 and 1160 of the Code.

[139] See Felix Lopez, supra note 123, at 273.

parties to diminish the value of the bankrupt estate and to undermine the chances of creditors of recovering their debts. Under ordinary circumstances, the debtor (who transferred property to third parties) is owed nothing (the third parties are not debtors, as in the case above) but because the transfer was fraudulently made, the trustee is authorized by Ethiopian law to recover the assets so transferred by invalidation of fraudulent transfers.[140] The trustee may recover these assets, which will form part of the bankrupt estate.[141]

On properties excluded from the bankrupt estate, we have answers (again less satisfactorily overall) in various provisions haphazardly scattered in Book V of the Commercial Code. We may proceed from the clear cases to the not-so-clear ones.

Of the clear cases, we might cite the following examples. "Negotiable instruments or other securities which have been handed to the debtor for purposes of collection for the benefit of the owner" and "remittances specifically made by the owner to be appropriated to specified payment,"[142] goods consigned to the debtor for deposit or for sale on behalf of the owner" if these goods "exist in kind, in whole or in part,"[143] goods the sale of which has been cancelled before bankruptcy,[144] movables sold with ownership reserved,[145] goods transmitted to the debtor but not yet delivered to the debtor's warehouse or to his agent at the time of bankruptcy.[146] Third party sellers are entitled to retain the goods sold to the bankrupt debtor "where such goods have not been delivered to the debtor" or not consigned "either to him or to third persons on his behalf."[147] Subject to the right of the trustee to exercise power of redemption of the property pledged (see below), pledgees have the right to sell the property for the satisfaction of their claims secured by pledge.[148]

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[140] For invalidation of transfers during suspect period, see below.

[141] See Commercial Code, supra note 4, Articles 1029-1034.

[142] Id, Article 1073.

[143] Id, Article 1074(1).

[144] Id; Article 1075.

[145] Id, Article 1076.

[146] Id, Article 1077.

[147] Id, Article 1078; see, however, Article 1079, where the trustee is authorized to require delivery by sellers as required by their contract under certain conditions specified therein.

[148] Id, Articles 1058 and 1059; for the rights of different categories of creditors against the bankrupt estate, see below.

What all these provisions do (they are fairly straight forward provisions and unlikely to lead to controversies in practice) is exclude all the properties mentioned therein from the authority of the trustee. They may be taken as definitions and/or enumerations of assets excluded from the bankrupt estate. These exclusions spare the owners/claimants from the unpleasant choice of having to stand with several other creditors to share from the now dwindling bankrupt estate.[149]

A less than satisfactory solution is provided for the treatment of encumbered properties held by mortgages and creditors secured by immovables or mortgages on the business.[150] In some provisions, Ethiopian bankruptcy law gives the impression that secured creditors are unaffected by the commencement of bankruptcy proceedings. Article 1026 of the Code, for example, suspends all individual suits of creditors included in the universality "except creditors whose claim is secured by "a special privilege, pledge or mortgage".[151] Article 1026 (together with Article 1025) gives the impression that secured creditors are not affected by bankruptcy proceedings. Carried to its logical conclusion, this may mean, for example, that the secured (encumbered) property held by these creditors is not part of the bankrupt estate and hence outside the jurisdiction of the trustee. We are compelled (at least partially and half-heartedly) to withdraw this conclusion or at least question our initial hunches when we come to Articles 1065-1072 of the Code. These provisions are couched in an unfortunate language of the order of sale of encumbered property vis-à-vis the 'unencumbered' bankrupt estate instead of stating the power of the trustee over encumbered assets (or even better stating whether encumbered assets are part of the bankrupt property).[152]

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[149] Where their claims exceed the value of the properties excluded above, they are reduced to the fate of other 'unlucky' creditors for the remainder of their claims; id, see Article 1059, for example, where it is stated: "where the price of sale [of the pledged property] is less than the amount of the debt, the pledgee may prove his claim for the difference as an unsecured creditor".

[150] Id, see Articles 1065-1068 and 1069-1072.

[151] Id, read Article 1026 together with Article 1025 of the Code – the latter *a contrario*.

[152] The word 'encumbered' is used here as a generic term referring to all property securing the debt owed by the bankrupt debtor. In other contexts, the words 'encumbered' or 'encumbrances' are as ponderous in pronunciation as their meanings but in this context these words are shorter than the words the Code uses, such as 'secured by immovables,' 'mortgage on the business'; see Commercial Code, supra note 4, the titles of Sections 4 and 5 of Chapter 5, Title II of Book V of the Code, Articles 1065-1072.

The language of Articles 1065-1072 is motivated by the desire to achieve the mathematical exactness of order rather than by the definition of who does what and when. As a result, these provisions are the most difficult provisions as any can be found in the whole body of Book V of the Code.[153] What these provisions say in so many but less elegant words is that secured creditors maintain exclusive power over the 'proceeds' of 'encumbered' assets sold to satisfy their principal claims- at least they do not have to share the proceeds up to the amount of the principal claims. What is more, secured creditors are entitled to participate in the share of spoils of the 'unencumbered' bankrupt estate, this time 'demoted' to the position of unsecured creditors.

Reality is chaotic. There is no reason for expecting that the order of sale (of encumbered as well as unencumbered assets) should fall exactly as the orders set in Articles 1065-1072. If all parties are left to their own devices, the orders may be disturbed. If secured creditors have their way, they may call the shots in ways that are patently unfair and unreasonable to unsecured creditors. Since their individual claims are not affected by the onset of bankruptcy (if we believe Article 1026 of the Code), secured creditors may stall the process of settlement of the bankruptcy proceeding by controlling the time of sale of the encumbered property. Such a leisurely approach is not compatible with ordinary bankruptcy proceedings. If the trustee has no power to force the sale of encumbered property, a disproportionate amount of property may lie out there while the unfortunate unsecured creditors are scavenging the worthless carrion of unencumbered assets. Even more galling, shameless secured creditors may participate in this scavenging while holding back the sale of encumbered assets. The encumbered assets will be sold eventually (secured creditors cannot permanently hold others hostage, if that is a relief) but by then so much has elapsed for unsecured creditors to be recalled to share in the proceeds of the remainder.

The silence of the Commercial Code on the power of the trustee over encumbered assets is a potential source of distraction as trustees should move to assert the interests of unsecured creditors against secured creditors who refuse to have collaterals sold in bankruptcy. Even when courts decide in favor of trustees, the very fact that trustees might be dragged to courts over this matter is a cause for concern. This could have been obviated had the Commercial Code had a provision somewhat similar to the French

[153] The price one pays in writing mathematical order in words is the loss of simplicity.

Code which authorizes trustees to sell encumbered assets on condition that the amount owed to secured creditors is set aside in a special fund - preserving the absolute priority of secured creditors in this regard. OHADA Uniform Bankruptcy Act gives trustees the power to sell encumbered property within three months from the date of declaration of bankruptcy, and upon the expiry of three months, secured creditors will have the right to sell encumbered property to satisfy their individual claims.[154]

We have seen that all the assets that are excluded from the bankrupt estate (at least not available to distribution among creditors) are excluded because these assets do not belong to the debtor in the first place (the debtor happens to be in possession of these assets on behalf of third parties as a bailor, etc) at the time of the adjudication of bankruptcy. On the exclusion of these kinds of assets, Ethiopian bankruptcy law is fairly straightforward and consistent with the practice in other bankruptcy systems.

But how about the property owned by the debtor? In other words, are any assets of the debtor exempted from the reach of bankruptcy? Let's explore the approach of some other bankruptcy systems before we turn to Ethiopian law.

The scope of exempt property under bankruptcy laws varies from country to country.[155] Under Australian law, for example, exempt property is limited to household furnishings, tools of trade, a motor vehicle up to a certain amount.[156] Under Spanish law, 'benefits that may be claimed only by the debtor (e.g. the right to alimony)' are exempted from the reach of bankruptcy estate.[157] Under the US bankruptcy laws, debtors have the right to choose between federal exemptions and state exemptions.[158] Under the federal exemption, the so-called 'homestead exemption' allows the debtor to exempt his aggregate interest up to a certain amount in real or personal

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[154] See OHADA, supra note 33, Articles 148 and 150.

[155] Michael M. Parker, supra note 121; see also Richard W. Maloy, supra note 98.

[156] See Nathalie Martin, *Common Law Bankruptcy Systems: Similarities and Differences*, 11 Am. Bankr. Inst. L. Rev. 367 (Winter 2003).

[157] See Felix Lopez, supra note 123, p. 272; Spanish law might have changed since 1985; for American law, see *Exemptions*, 1 Bankr. Dev. J. 297 (1984); *Exemptions – Section 522*, 2 Bankr. Dev. J. 41 (1985); in other bankruptcy systems, the extent of exempt property is regulated not by the bankruptcy law but by other laws; this approach appears also to be the case under the OHADA Uniform Bankruptcy Act and French Commercial Code for we find no specific provisions in this regard.

[158] See 1 Bankr. Dev. J.(1984), supra note 157, and 2 Bankr. Dev. J.(1985), supra note 157

property that the debtor and dependents use as residence.[159] For married couples, the exemption amount is doubled if both parties elect to take federal exemptions.[160]

Many other laws of Ethiopia exempt certain types of debtor property from attachment by creditors. The Ethiopian Civil Procedure Code exempts 'wearing apparels, cooking vessels, bed and bedding, tools, instruments of any kind used by the debtor, cattle and seed grain (for farmers), food and money as may be necessary to enable the debtor and family to sustain themselves for three months, pensions and alimonies, and two-thirds of the debtor's salary, and any other property declared to be exempt by other laws'.[161] Article 45 of the Public Servants Proclamation exempts benefits received under the Pensions Law from attachment except for the payment of 'public fines, fees or taxes' or the 'fulfillment of maintenance obligations'. Similarly, the Labor Proclamation of 2003 exempts employee benefits payable as a result of employment injuries from attachment, deduction or assignment.[162] In addition, the Labor Proclamation puts two-thirds of the monthly wages of a worker beyond the reach of attachment.[163]

The Ethiopian bankruptcy law does not mention exemption - not directly anyway. There is an allusion to exemption in Article 1010 of the Commercial Code -which exempts from seals 'movable property and chattels by the debtor and his family as have been set out in the list submitted to the commissioner'- but the cited Article does not specify which types of property are exempted from seals. Some of the provisions of the Commercial Code give the impression that no property of the debtor is exempted from the reach of bankruptcy. Article 1020 of the Code provides that the commissioner may give permission to the trustee to apply part of the bankrupt estate to the support of the debtor and his family. This holds for the period before the winding up of bankruptcy. After the winding up of bankruptcy, the creditor's committee must agree that assistance be given to the debtor and family from the bankrupt estate.[164] The provision that deals with priority of creditors - Article 1110 - puts the assistance to be given to the debtor and family before the claims of preferred and unsecured

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[159] 1 Bankr. Dev. J.(1984), supra note 157, at 299.

[160] Ibid.

[161] See Civil Procedure Code, supra note 14, Article 404.

[162] Labour Proclamation, supra note 13, Article 112.

[163] Id, see Article 59(2).

[164] See Commercial Code, supra note 4, Article 1102; the amount is fixed by the commissioner once the creditors' committee agrees.

creditors.[165] The assistance has priority over all creditors except secured creditors and cost and expenses of bankruptcy. It is clear that Ethiopian bankruptcy law has not neglected the welfare of debtors and their families - but not in an exemption sense. There is an apparent conflict between other laws of Ethiopia which exempt certain types of property, and the bankruptcy law, which caters for the welfare of debtors but does not talk about exemptions.

One way of dealing with this conflict is to give effect to the provisions of Ethiopian bankruptcy law and disregard the other laws (in other words, no exemption will take effect in bankruptcy proceedings). Another approach is to view the two systems as separate and give effect to both - in other words, give effect to the exemption requirements of other laws and recognize that assistance may in addition be provided in accordance with the rules of bankruptcy law.

Exemption provisions are expressions of public policy and therefore of peremptory nature. The provisions that deal with exemptions use a strong language and do not seem to admit of any exception. It seems unlikely that these provisions will be set aside in bankruptcy proceedings and it is reasonable to assume that whatever assistance is to be provided for the debtor and family, it is in addition to the property of the debtor that enjoys exemptions by the operations of other laws of Ethiopia. There is, in any case, an allusion to exemption in Article 1010 of the Code - which might be taken to have authorized exemption in accordance with other laws of Ethiopia.

We have seen cases in which Ethiopian bankruptcy law supplies answers (albeit in a haphazard manner) but there are many other cases for which an answer has to be sought elsewhere (other laws of Ethiopia), for we find no clear provision in the bankruptcy law in this respect. One such case is the treatment of joint and/or common assets upon the declaration of bankruptcy. What is, for instance, the effect of bankruptcy of a debtor upon the property of his/her spouse? A provision comparable to the following French bankruptcy provisions is not to be found in Ethiopian law:

> The spouse of a debtor subject to safeguard proceedings [bankruptcy proceedings] shall specify the content of his/her personal property, in compliance with the rules of matrimonial regime...

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[165] Id, see Article 1110(b).

> .... The administrator [trustee] may, if he proves by all means that the assets acquired by the debtor's spouse have been paid by money provided by the debtor, request the inclusion of these assets in the debtor's assets. [166]

French bankruptcy law clearly includes in the bankrupt estate the common property of the debtor and his/her spouse but personal property of the spouse is excluded (unless it is the fruit of a contribution made by the bankrupt debtor). US Bankruptcy law includes in the bankrupt estate the interest of the other spouse in 'community property' but not the separate property of non-debtor spouse.[167]
What about under our law? It will take another article of its own to attempt to provide an answer to this question. I will not attempt here but it is clear that an answer to this question is to be found in Articles 16-21 (Book I) of the Commercial Code and perhaps in the multiple family laws of Ethiopia.[168] Since bankruptcy is a federal matter, it would have been desirable to provide one uniform solution to this problem. Incidentally, the first drafter of the Commercial Code (Professor Escarra) thought about including a provision on this matter but decided against it because he was uncertain about what the Civil Code would say about the effect of marriage upon property in general.[169]

The treatment of joint properties is similarly consigned by default to the solutions possibly provided in the Ethiopian laws of property. The Guide mentions two options for the treatment of joint assets, including assets of the other spouse.[170] One is to exclude them completely from the bankrupt estate.[171] The other option is to treat the 'mutual assets belonging to the other spouse' as part of the bankrupt estate.[172]

The dispossession of the debtor can be effected without a hitch when the debtor happens to be a natural person. How is dispossession effected when

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[166] French Commercial Code, supra note 35, Articles L624-5 and L624-6.
[167] See *Collier's Bankruptcy Manual* (2d Edition Revised, Matthew Bender & Company, Inc., 2010) at 541.07; also see OHADA, supra note 33, Article 99 for a similar treatment.
[168] Since family law is a jurisdiction of regional states, one can anticipate multiple (and at times contradictory) answers to this question.
[169] He wrote: 'for the spouse of the bankrupt, I have not drafted any provision because I have no knowledge at all about the Civil Code provisions on the property effects of marriage', see Peter Winship, supra note 23, at 104.
[170] UNCITRAL, supra note 11, p. 81, paras. 20 and 21.
[171] Id, p. 81, para. 21.
[172] Ibid.

the bankrupt debtor is a business organization? To whom does it take effect (if at all) - managers, members of board of directors? In other bankruptcy laws, there are additional rules regarding the effect of dispossession when the bankrupt involved is a business organization. French bankruptcy law, for example, provides that managers of business organizations 'shall remain in office unless the articles of association or a resolution passed by a shareholders' or partners' meeting provide otherwise', and only in case of need will the court appoint a representative.[173]

Again due to the dual organization of Ethiopian bankruptcy law, the effect of dispossession upon business organizations seems to have been forgotten. Where a trustee is appointed for a business organization, a dispute may arise between a trustee who wants to take over the management of the property and the managers and directors who have been in charge. The law makes no exception for the appointment of a trustee in case of business organizations. In the case of businesses organized as partnerships, there will be no problem, for the bankruptcy of the partnership automatically entails the bankruptcy of the general partners - which means that the partners will lose their right to administer and dispose of their property and the property of the partnership.[174] Where the bankruptcy involves companies, however, it will be difficult to upstage managers or board directors from the management unless the court declares them bankrupt in common with the business organization.[175] Can the court order the removal of the management of a company without implicating them in the bankruptcy? If the court does not say anything in the judgment of bankruptcy regarding the position of the management of the bankrupt company, can the trustee move to take over the management of the company as adverse party to them? These issues are not settled under Ethiopian bankruptcy law, and it may have been forgotten as a result of the dual organization of Book V of the Commercial Code (with separate rules on business organizations). If courts are compelled to declare members of the management staff bankrupt for the sole purpose of removing them from management, the action of the courts will certainly be an overkill and totally unnecessary. The common declaration of bankruptcy will bring about an avalanche of consequences upon the management staff out of

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[173] See, French Commercial Code, supra note 35, Article L641-9; OHADA Uniform Act simplifies the issue by equating the bankruptcy of a business organization with its dissolution, paving the way for trustees (liquidators) to take over; see OHADA, supra note 33, Article 53.

[174] See Commercial Code, supra note 4, Article 1158.

[175] Id, Article 1160.

proportion to what is required in the circumstances, which is their removal and replacement by trustee/s or their full collaboration with the trustee/s appointed by court.

In a bid to prevent this, it is perhaps desirable to resort to the general provisions of the Commercial Code relating to the dissolution and winding-up of companies[176] - which are related procedurally to bankruptcy (although the causes are different). The affinity between the sections on 'dissolution and winding-up' and the Bankruptcy Book is not just wishful association. We have authority in Article 498 of the Commercial Code, which, upon referring the winding-up of companies that are declared bankrupt to Book V of the Commercial Code, declares that 'the directors' powers shall be restricted to representing the company if necessary'.[177] In addition, Article 497(2) of the Code states that 'the organs of the company shall restrict their activities to acts necessary to facilitate the winding-up and *which are not acts within the scope of the liquidator's (italics added)*. Courts may rely upon the general provisions of the Commercial Code already cited to restrict (if not completely remove) the involvement of managers and directors, in stead of declaring them bankrupt in common.

b. Effects of Bankruptcy upon Creditors

The provisions of Ethiopian bankruptcy law pertaining to effects on creditors only deal with the effects in so general language that it is impossible to get the full force of the effects by just reading these provisions. We need to plow deep into the provisions to get the full meaning of what bankruptcy means to creditors in general and to some categories of creditors in particular. We need specially to look at provisions that treat special category of creditors, like pledgees, lessors, mortgagees and others. These provisions are located far away from the provisions that talk about the effects of bankruptcy, but that is no bar to seeing these provisions for what they really are: they talk about the effect of bankruptcy upon these categories of creditors.

This part is divided into three sections. Section I will deal with the effect of bankruptcy upon creditors in general. Section II will deal with the effect of bankruptcy upon contracts in general. Section III will deal with the effect of bankruptcy upon some creditors: pledgees, lessors, sellers and creditors secured by mortgage on business and immovable property.

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[176] Id, see Articles 495-509.

[177] Id, Article 498 (1)& (2).

i. the Effect of Bankruptcy on Creditors in General

Bankruptcy affects not just the debtor; it affects the rights and interests of creditors as well. It results in the 'modification of the rights of creditors'.[178] Creditors, who hitherto had the right to exercise their remedies independently, including court actions and executions, are now subject to the constraints of bankruptcy.[179]

The first sign of this modification is the inclusion in a 'compulsory class (la masse),' the so-called 'universality of creditors', 'in the name of which the collective rights and interests of creditors are to be exercised and defended'.[180] In the apt words of Francois Gore, the rights of creditors 'are absorbed in a large measure by this class', creditors 'losing their rights of individual pursuit'.[181] As regards the universality of creditors, Article 1025 of the Commercial Code calls it 'a legal entity', which 'acquires rights and incurs liabilities' and is represented by the trustee.[182] The entity represents all creditors 'whose claims are not secured by a special privilege, a pledge, or a mortgage'.[183]

Since the Code names it boldly as a 'legal entity', we may be wondering about what type of entity it is. Since bankruptcy affects all kinds of businesses - from the sole proprietorships to share companies- we may be asking what sort of transformation the creation of a legal entity named 'universality of creditors' brings to the underlying business hitherto owned by the bankrupt debtor. Does it lead to any transformation at all? Does the new entity require the registration - as most business organizations in the Commercial Code do? Does it require the rewriting or writing anew of a memorandum of association? If we are looking in the Commercial Code for answers to these questions, we will be sorely disappointed - for the Code says nothing more than stating that the 'universality' is a legal entity.

The Commercial Code lays down no formalities for the creation and indeed formalization of the 'legal entity'. The trustee needs do nothing to formalize

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[178] Francois Gore, *the Administrative Autonomy of Creditors and French Legislation on Bankruptcy*, 17 Am. J. Comp. L1, 5, 6 (Winter1969).
[179] Ibid.
[180] Ibid.
[181] Ibid.
[182] See Commercial Code, supra note 4, Article 1025(2).
[183] Id, see Article 1025(1).

and publicize the entity.[184] The appointment of the trustee by the court is sufficient for the trustee to represent the universality.[185] The nature of the business of the debtor is not changed as a result of the bankruptcy. The trustee takes over the business as he found it and runs it on behalf of creditors. If it is a sole proprietorship, it continues as a sole proprietorship; if a share company, as a share company. What is transformed is the individuals at the helm of the business and for whom the business is run. Now the trustee is at the helm of the business in stead of the debtor, and the business is run for the interest of creditors rather than the debtor (shareholders in the case of companies, for example).[186] There is even no need to transfer title to property of the bankrupt debtor to the trustee. The trustee's appointment is enough to vest title in the trustee and take legal actions on the debtor's property.

The closest affinity one can find to the notion of 'legal entity' being latched onto the 'universality of creditors' is to be found not in the Commercial Code but in the Civil Code. The Civil Code devotes a section to 'trusts' under a chapter of what it calls 'property with specific destination'.[187] The bankrupt estate may be taken as 'property with specific destination', whose beneficiaries are creditors and representative is a trustee. In that context, it is appropriate to call the universality a 'legal entity'. It is also appropriate to call it such to signify that the creditors acquire a collective identity, united into a body known in French 'la masse'.[188]

The other most important effect of bankruptcy on creditors in general is the suspension[189] of all suits by creditors, except secured creditors.[190]

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[184] Of course, it is not entirely moot that the legal entity requires no further formalities, as the debate over the nature of this 'entity' elsewhere shows; for the debate, see, Stephen McJohn, *Person or Property? On the Legal Nature of Bankruptcy Estate*,10 Bankr. Dev. J. 465 (1993-1994).

[185] All that the trustee needs to do is take possession of property from the bankrupt debtor; see Richard W. Maloy, supra note 98.

[186] Elsewhere, it has been held that the trustee does not represent the debtor; nor does he owe the debtor any fiduciary duty; see Collier's Bankruptcy Manual, supra note 44.

[187] See Civil Code, supra note 41, Section 3, Chapter 3, Title III.

[188] See Boris Martor et al, supra note 33, at 173; Francois Gore, supra note 178, at 6.

[189] The use of the word 'suspension' is apt. Many other laws use the word 'stay' to refer to the same effect. They both signify that suspension is temporary, lasting until a discharge (if any) is entered, at which point those creditors whose debts are discharged are permanently prevented from pursuing the debtor; see Richard W. Maloy, supra note 98.

[190] Commercial Code, supra note 4, Article 1026.

Maximizing the value of the bankrupt estate being one of the overriding objectives of bankruptcy, the suspension of individual actions ensures 'a fair and orderly administration of the proceedings', giving trustees the breathing time to avoid making forced sales, to take stock of the debtor's situation and to achieve a result that is not prejudicial to the interests of the debtor and creditors.[191]

No definition of suits is offered in Article 1026 of the Commercial Code. All it says in a typical general language is that individual suits are suspended. We are inclined to associate suits with pending legal actions in courts, but reference to the bankruptcy laws of some other countries indicates that the word might have a far wider meaning than just a legal action in courts.
The approach of bankruptcy laws to the scope of suspension of suits is as diverse as can be.[192] Some laws suspend 'all remedies and proceedings against the debtor ... whether administrative, judicial or self help'.[193] Some other laws allow initiation or continuation of certain actions but bar enforcement or execution of judgments or orders.[194] Still others limit the actions that may be continued and allow the initiation of certain actions, like actions by employees.[195] Some countries draw distinction between regulatory and pecuniary actions- allowing the former to continue in spite of bankruptcy proceedings.[196]

Under French law, the following actions are suspended (stayed) upon the initiation of bankruptcy proceedings:[197]

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[191] UNCITRAL, supra note 11, pp. 83-84, para. 27.

[192] *Recent Developments - Automatic Stay Exceptions - Section 362(b)*, 4 Bankr. Dev. J. 43 (1987); see also Richard W. Maloy, supra note 98.

[193] UNCITRAL, supra note 11, p. 84, para. 30.

[194] Id, p. 86, para. 34.

[195] Ibid.

[196] Regulatory actions are actions taken 'to protect vital and urgent public interests, restraining activities causing environmental damage or activities that are detrimental to public health and safety'; see UNCITRAL, supra note 11, p. 86, para. 34; under US law certain actions, such as criminal actions, actions to enforce environmental law, governmental actions to prevent fraud, and domestic relations actions are exempt from suspension; see Richard W. Maloy, supra note 98.

[197] See French Commercial Code, supra note 35, Articles L622-28 and L622-30; the UNCITRAL Guide enumerates the types of actions that may be suspended: actions for the execution of judgments, actions to make security interests effective against third parties, recovery by owner or lessor of property that is used or occupied by, or in possession of the debtor, payment or provision of a security in a respect of a debt incurred by the debtor prior to the commencement of bankruptcy proceeding;

(i) order against the debtor to pay a sum of money;
(ii) the rescission of contract on the grounds of non-payment by the debtor;
(iii) all proceedings for enforcement filed by the creditors in respect of movable and immovable property belonging to the debtor;
(iv) the running of period of limitation;
(v) the accrual of legal and contractual interest;
(vi) any action against sureties and co-obligors;
(vii) registration of mortgage, pledge or lien;

Similarly, OHADA Uniform Bankruptcy Act is more specific and far more detailed than the Ethiopian law in this regard. Under OHADA law, 'all individual lawsuits for acknowledgement of rights and claims', 'all measures of execution' on the debtor's movable and immovable property', the running of a period of limitation or prescription are suspended upon initiation of bankruptcy proceedings.[198] Although Ethiopian bankruptcy law does not specify the suits that are suspended and those that are not, there are hints in some provisions (far away from Article 1026) that some suits are not affected by the commencement of bankruptcy. We, for example, read from Article 970 of the Commercial Code that criminal proceedings will continue unabated despite the bankruptcy proceedings.[199] Similarly, in Article 1050 of the Code we may have a case in which ordinary civil proceedings may commence (and in fact where bankruptcy proceedings may be stayed) where an objection contesting a debt is lodged.[200]

Both the French bankruptcy law and OHADA list actions that are not suspended by the initiation of bankruptcy proceedings, something the Ethiopian bankruptcy neglects to do. Under French law, all actions that are not listed as subject to suspension may be continued.[201] Under OHADA law, lawsuits for 'nullity' and 'resolution' are not suspended,[202] although it is not clear what these actions mean.

The other general effect of bankruptcy upon creditors in general (again excepting secured creditors) is the acceleration of the due dates of debts and

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termination, suspension or interruption of supplies of essential services (e.g. utilities - water, electricity and telephone); see UNCITRAL, supra note 11, pp. 84-85, para. 31.

[198] OHADA, supra note 33, Article 75.

[199] See Commercial Code, supra note 4, Article 970(2).

[200] Id, see Article 1050(1).

[201] See French Commercial Code, supra note 35, Article L622-23.

[202] OHADA, supra note 33, Article 75.

the interruption of the bearing of interest.[203] These effects are too obvious to require further explanation.

ii. The Effects of Bankruptcy on Executory Contracts

Bankruptcy descends on the parties while many transactions remain unsettled. There may be signs that the business is running into financial difficulties but generally bankruptcy catches the parties unawares. In view of this fact, one of the issues bankruptcy laws address (or ought to) is the effect of bankruptcy upon contracts. At the time of the declaration of bankruptcy, we can envision three distinct states (or statuses) of contracts. There are contracts in which the bankrupt debtor has performed his part of the obligation, but the other party has not. There are contracts in which the other party has performed his part of the obligation, but the bankrupt debtor has not. There are also contracts in which both parties have not performed their obligations (the so-called executory contracts).[204] These executory contracts may include collective bargaining agreements, unexpired leases and insurance policy -to name but a few of the contracts which are likely and routinely to remain unfulfilled.[205] Of course, this is putting it very neatly. In practice, some contracts may be partially performed, raising questions of whether one should regard them as executory contracts or not. [206]

In the first instance, the debtor is a creditor and there is a clear rule in the bankruptcy law to resolve this issue: the trustee is authorized to collect the debts owed to the bankrupt debtor.[207] In the second instance, the other

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[203] For a comparative perspective, see Richard W. Maloy, supra note 98.

[204] There is no agreement over the precise meaning of executory contracts. In the United States, the widely accepted definition is proffered by Professor Vern Countryman who defined them as a "contract under which the obligation of both the bankrupt and the other party to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing the performance of the other." See Martin J. Bienenstock, *Executory Contracts and Unexpired Leases under the Bankruptcy Code*, Practising Law Institute Real Estate Law and Practice Course Handbook Series PLI Order No. N4-4580 May 5-6, 1994.

[205] See *Administration of the Estate*, 2 Bankr. Dev. J., 81, 89 (1985).

[206] In one case, a US Court held that if a contract has been substantially performed by one side, it is no longer an executory contract; Re2522 South Reynolds Corp., 33 Bankr. 616 (Bankr. N.D. Ohio 1983), quoted in id, at 89, see foot note 65.

[207] Commercial Code, supra note 4, see Article 1035(2).

party is a creditor and again there is a clear rule on how creditors may go about collecting their claims against the bankrupt debtor.[208]

It is the executory contracts that pose special challenges and (may) call for special rules in bankruptcy law. The treatment of contracts during bankruptcy cannot be seen lightly. From the vantage point of the bankrupt estate, the executory contracts may promise potentially valuable assets.[209] But interference with established contractual principles -as special rules of bankruptcy in this regard are likely to do - may harm the predictability of commercial and financial relations and increase the cost and diminish the availability of credit.[210]

Whichever side of the fence bankruptcy law falls, competing and conflicting policy issues are going to be at stake.[211] While a common solution for all kinds of contracts is generally preferred (and followed in many bankruptcy systems), exceptions for some contracts are unavoidable.[212] The ability of trustees to interfere with labor contracts are generally restricted (by other laws).[213] Other contracts for which special rules may exist include contracts for personal services (for which the identity of the parties who perform the contract is of particular importance) and financial contracts.[214]

On the treatment of contracts in general, we find two general approaches. We have, on the one hand, laws which leave this question to the general rules of contracts or other laws or the agreement of the parties.[215] The treatment of a contract after the commencement of bankruptcy in these systems is to be resolved by recourse to these other laws. If a contract between the parties contains a clause of termination or acceleration of the contract in the event of bankruptcy, for example, the clause is honored

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[208] Of course, it depends on the status of a creditor; if the other party is a secured creditor, he has the right to enforce his rights against the collateral, untroubled in many instances by the commencement of bankruptcy proceedings; if the other party is an unsecured creditor, he joins the universality of creditors; Commercial Code, supra note 4, see Articles 1025 and 1026.

[209] UNCITRAL, supra note 11, p. 120, para. 108

[210] Id, p. 120, para. 110.

[211] Ibid.

[212] Id, p. 121, para. 113.

[213] Id, pp. 121-122, para. 113; see French Commercial Code, supra note 35, ArticleL622-13.

[214] See UNCITRAL, supra note 11, p. 122, para. 113.

[215] Id, p. 120-121, paras. 110 and 111.

during bankruptcy.[216] Under the other approach, the bankruptcy law provides for special rules that override the clauses in a contract between the parties.[217] French law, for instance, has special rules on the treatment of executory contracts, restricting the right of the other party to terminate the contract as result of the commencement of bankruptcy proceedings, and giving trustees the option to continue or terminate the contract, as the case may be.[218] Similarly, under US law, a trustee may, with court's approval, reject, assume or assign executory contracts, provided the trustee agrees to cure 'any defaults and provides adequate assurance of future performance'.[219]

What is the position of Ethiopian law on the treatment of contracts during bankruptcy? Ethiopian bankruptcy law follows the first approach (of deferring the matter to be resolved by other laws - such as, general rules of contract in the Civil Code). There are, of course, exceptions to this general approach. The exceptions are provided for continuation businesses, leases, and possibly sales contracts (for leases and sales contracts, see below).

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[216] A number of factors support this position: the desirability of respecting commercial bargains; the need to prevent the debtor from selectively performing contracts that are profitable and rejecting those that are not, etc; see UNCITRAL, supra note 11, p. 122, para. 115.

[217] This interferes with the general principles of contract law, but it may be justified by the policy of maximizing the value of the bankrupt estate; see UNCITRAL, supra note 11, p. 122, para. 116.

[218] See French Commercial Code, supra note 35, ArticleL622-13; under French law, the trustee has the right to require the other party to perform an executory contract, in exchange for the performance of the bankrupt debtor's obligations under the contract. Upon the commencement of the proceedings, the other party has the right to give notice (of one month usually, but may be extended to two months) to the trustee to inform him of whether the trustee would wish to continue or terminate the contract. If the trustee does not respond to the notice or declares that the contract is terminated, the contract will automatically terminate. The trustee must move judiciously in deciding to either continue or terminate the contract, for the continuation of the contract entails performance by the trustee promptly. If he does not have the necessary funds at his disposal, termination is a better option. This holds not just for one time payment but also for installment contracts, in which case the trustee must ensure that he will have the necessary funds to satisfy payments of the successive terms; see ibid.

[219] Michael M. Parker, supra note 121; see also George G. Triantis, *The Effects of Insolvency and Bankruptcy on Contract Performance and Adjustment*, 43 University of Toronto Law Journal 3, 679, 690 (Summer 1993).

There is a special provision involving continuation of business during bankruptcy.[220] The continuation of the debtor's business during bankruptcy is not automatic. The trustee must obtain authorization from the court, which must decide on the matter only after hearing the report of the commissioner and the recommendations of creditors' committee, and authorize continuation if that is in the public or creditors' interest.[221]

Continuation of business may entail the continuation or termination of existing (executory) contracts or the entering into of new contractual agreements –that is why authorization of continuation has a direct bearing on the continuation or rejection of executory contracts. It is not clear if the authorization of continuation of business may be read as the authorization of existing contracts. Can the trustee use the authorization to prevent the cancellation of the contract by the other party pursuant to a clause of cancellation in the contract?

iii. Effects of Bankruptcy on Some Creditors

1. Pledgees

Pledgees do not have to stay in line to share from the proceeds of the bankrupt estate. This much we can learn from the general provision of Article 1026, which, as pointed out before, exempts secured creditors from the effects of bankruptcy. The full implications of this provision do not become apparent until we get to the provisions that treat the effect of bankruptcy on secured creditors like pledges. These provisions are found in a section on 'submission of claims' but they are better understood if they were placed in sections treating effects of bankruptcy.[222]

In an expansion of the provision that states that 'bankruptcy shall have no effect on secured creditors,' Article 1058 restates the same effect in a different language: a pledgee can sell the pledge (the property) without having to wait in line with other 'unsecured' creditors.[223] If the sale yields an amount more than the debt owed by the bankrupt debtor, the pledgee has the duty to claw the excess back to the bankrupt estate – in effect, return it to the trustee.[224] In reality, it is the trustee who should watch out for this

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[220] See Commercial Code, supra note 4, Article 1039.

[221] Id, see Article 1039(1).

[222] There are reasons why they are covered in sections on 'submission of claims' of course. They make sense there too, because we can view these provisions in light of the issue of submission of claims.

[223] Commercial Code, supra note 4, Article 1059.

[224] Id, Article 1059.

and collect the excess from the pledgee. If the sale yields insufficient funds even for the satisfaction of the pledgee, the pledgee is reduced to the status of 'unsecured' creditor for the balance.[225]

The right of the pledgee to effect sale is not unlimited. The trustee has the power to redeem the pledge by paying the debt in full to the pledgee.[226] A trustee, as a fiduciary representing the best interest of unsecured creditors, should seek to maximize the value of the bankrupt estate by exercising the right of redemption. A dispute may arise between a pledgee who wants to exercise his power of sale and a trustee who wants to exercise his power of redemption. Which of them takes precedence? That is not resolved.

2. Lessors

Article 1060 of the Commercial Code treats the case of lessors. The treatment of lessors in the section that covers pledgees may be confusing at first reading, but there is a reason why the two cases are related. Under the Civil Code, lessors have the legal right of pledge, and the bankruptcy law is there to define the scope of this right of preference during the bankruptcy.[227] In ordinary circumstances, lessors have a legal right of preference over the movables which furnish the immovable leased.[228]

The effect of bankruptcy upon lessors is different from other creditors, for that matter even from other preferred creditors. Leases (particularly commercial leases) are often subject to special rules in many bankruptcy laws.[229] The reason has to do with the economic significance of leases for bankrupt estates. If the lease is below market price, the lease may be sold and return a benefit to the estate.[230] On the other hand, if the lease represents a losing concern to the business, the trustee may unburden the bankrupt estate by terminating the lease,[231] thus fulfilling one of the cardinal objectives of bankruptcy - which is maximizing the value of the bankrupt estate.

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[225] Id, Article 1059, second sentence.
[226] Id, Article 1058.
[227] See Civil Code, supra note 41, Articles 2896-2961.
[228] Id, see Article 2924.
[229] See OHADA, supra note 33, Article 97; French Commercial Code, supra note 35, ArticleL622-14 to L622-16, and Article L641-12; UNCITRAL, supra note 11, p. 129, paras. 137-138.
[230] UNCITRAL, supra note 11, p. 129, para. 137.
[231] Id, p. 129, para. 137.

Lessors do not have the right to terminate the lease simply because the lessee has been adjudged bankrupt.[232]The bankruptcy provisions take away the right of termination from lessors and give the option to the trustee - to continue or terminate the lease. The trustee must notify the lessor of his decision within 15 days from the deposit of inventory.[233] Although there are special rules regarding leases, these effects are really a continuation or extension of the general effect of bankruptcy upon creditors – suspension of suits (or stay of actions).[234] The lessor's right to terminate the lease is suspended awaiting the decision of the trustee whether to continue or terminate the lease.

If the trustee decides to continue the lease (as he is most likely to do), the lessor may apply (to court?) within 15 days to cancel the lease.[235] On what grounds the cancellation request is to be granted, the law does not say. In addition, the lessor loses his right to distrain movables until the trustee informs him of his decision either to continue or terminate the lease.[236] During bankruptcy, the lessor would probably be pleased to hear from the trustee that the lease has been terminated because he does not want to face the uncertainty that bankruptcy brings with it.

It appears that it is from this consideration (that the lessor is not at liberty to do what he wishes as a result of the bankruptcy proceedings) that the bankruptcy provisions compensate the lessor by giving him special rights of preference. In the event of the termination of the lease, the lessor has a preferential right covering all the claims arising out of performance of the lease contract and the contingent damages for the two years of lease prior to

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[232] Commercial Code, supra note 4, Article 1040(1); an interesting side note about this effect is that the bankruptcy affects not just commercial or industrial leases but also, it appears, residential leases for the bankrupt and his family; Article 1040(1) in part reads: "leases of immovable property used for the business or industrial operations of the debtor, including premises forming part thereof and occupied by him or his family..."

[233] Commercial Code, supra note 4, Article 1040(2).

[234] See Nancy Ann Connery, *Negotiating Commercial Leases: How Owners and Corporate Occupants Can Avoid Costly Errors* (Real Estate Law and Practice Course Handbook Series, November-December, 2006)

[235] Commercial Code, supra note 4, Article 1040(5); it is not clear to whom the application is made, but it is quite reasonably to the court.

[236] The word 'distrain' is defined in the dictionary as 'to seize goods and chattel as security for the payment of any obligation for which such action is made lawful'; see P. Ramanatha Aiyar, *Concise Law Dictionary, with Legal Maxims, Latin Terms & Words and Phrases* (3rd edition, 2006).

the adjudication of bankruptcy and for the current year.[237] If the lease is not terminated, the lessor has the preferential right for all unpaid rents.[238] With all outstanding rents paid, the lessor cannot force himself on an already distressed business by seeking payment for the current period and any rent to fall due.[239] All he can ask for is to seek the continuation of the guarantees given on the making of the contract (in other words, he cannot seek additional guarantees using the bankruptcy proceeding as an excuse).[240] Throughout the continuation of the lease after bankruptcy proceedings are commenced, the lessor can only seek that the premises leased are properly furnished with movables of sufficient value and the payment (or fulfillment) of the obligations at the end of each letting period.[241] The replenishment of the movables in the premises leased is regarded as sufficient guarantee for the lessor. Unlike pledgees, lessors do not have the right to sell the movables over which they have preferential claims. The trustees have control over these movables. Where the movables are sold or removed from the premises, however, the preferential right of lessors will kick in. The proceeds of the sale should first be used to cover the claims of lessors. Lessors have preferential claims covering two years prior to the adjudication of bankruptcy and two years from the adjudication of bankruptcy.[242]

In addition to the power to continue or reject leases (over the reluctance of lessors), trustees also possess the power to assign leases. Assignment powers of the trustee carry some unpleasant or onerous consequences to the other party (lessor). They undermine the contractual rights of the other party.[243] They force the lessor to transfer the lease to a sub-lessee who may not be known to the lessor or with whom the lessor may not wish to do business.[244] Some bankruptcy laws take away the right of the lessor to invoke non-assignment clauses in the lease contract.[245] Others leave the matter to the rules of general contract.[246] Still others require the court to

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[237] Commercial Code, supra note 4, Article 1060(1).

[238] Commercial Code, supra note 4, Article 1060(2). Article 1060(2) is couched in an unfortunate language of negative expression, but the *'a contrario'* reading of it is inescapable.

[239] Ibid.

[240] Ibid.

[241] Id, see Article 1062.

[242] This is a joint reading of Articles 1060(1) and 1061.

[243] UNCITRAL, supra note 11, p. 129, para. 140.

[244] Ibid.

[245] Ibid.

[246] Id, p. 129-130, para. 140.

authorize assignment where the lessor does not consent to the assignment of the lease contract or require the trustee to show that the lessor will not be disadvantaged by the assignment or that the assignee can adequately perform the obligations under the lease contract.[247]

Ethiopian bankruptcy law lays down the same conditions for continuation and assignment of leases: i) the trustee or the assignee shall keep the premises furnished with movables of sufficient value; ii) the trustee or the assignee shall carry out all obligations arising out of the law or the lease agreement; and iii) the purposes for which the premises are utilized may not be changed.[248]

3. Sellers and Other Creditors with Rights of Recovery

The bankruptcy provisions start by removing all of the guarantees that are given to sellers in the Civil Code.[249] Any agreement to the contrary is not valid.[250] One obvious guarantee of the seller which is affected by the onset of bankruptcy is the right to demand payment.[251]

What the bankruptcy provisions take away with one hand, they return with the other, for sellers are granted certain though limited rights of recovery in spite of the bankruptcy proceeding pending against the buyer.[252] Sellers have the right to recover the goods sold - and therefore do not have to wait in line to share from the bankrupt estate - if their condition falls under one of the following three situations:

(i) if the contract of sale had been cancelled before the adjudication of bankruptcy or even if the cancellation is order after adjudication, if the proceedings for recovery of the goods or for cancellation of the contract were brought before the adjudication of the bankruptcy;[253]

(ii) if the contract of sale is a 'sale with ownership reserved' and the reservation had been registered in accordance with Article 2387 of the Civil Code;[254] or

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[247] Id, p. 130, para. 140.

[248] See Commercial Code, supra note 4, Article 1062.

[249] Id, Article 1063.

[250] Id, Article 1063(2).

[251] See Civil Code, supra note 41, Article 2333, where the right of the seller to demand payment is stated, except where the seller has the customary option of getting the price through compensatory sale.

[252] See Commercial Code, supra note 4, Articles 1075-1079.

[253] Even then, the seller has to show that the good exists in kind; see id, Article 1075(1) and (2).

[254] Id, Article 1076.

(iii) if the goods subject to the contract of sale have not been delivered yet to the debtor or to his agent either because they have not yet been sent or because they are in transit.[255]

These rights of recovery indicate that, with respect to bankruptcy, sellers enjoy the rights of secured creditors in certain limited situations. In bankruptcy, this is no mean right.

The right of sellers to recover the goods sold is counterbalanced by the power of trustees to demand delivery of the goods provided the trustees are willing to pay the agreed price to the seller.[256] This does not diminish the right of sellers - had bankruptcy not occurred, they would have the obligation to deliver the goods anyway. The right of trustees to demand delivery is subject to certain conditions. First, the trustees can demand delivery only in cases where the goods are still in transit or in the hands of the seller and the contract is not the subject of cancellation under Article 1075 or the contract of sale is not one with 'ownership reserved'.[257] And secondly, the trustees must obtain authorization from the commissioner(s) to demand delivery from sellers.[258]

Trustees who have opted not to exercise the right to demand delivery have the right to collect any advances received by the seller, including any advances for the freight, transport, commission, insurance or other expenses of the contract.[259] This, we note, is simply an extension of the power of the trustees to collect all debts owed to the bankrupt estate under Article 1035 of the Commercial Code.

Sellers, who do not have the right to claim recovery of the goods, have the right to claim the payment of the price and of the damages arising from the performance of the contract. This is not an enviable position to be in for sellers, for in this regard sellers are treated like all unsecured creditors, and therefore should stand in line with all other unsecured creditors to share from the distribution of the proceeds of the bankrupt estate.[260]

Sellers are not the only creditors with the right to recover the goods from the trustees without having to stand in line to share from the proceeds of

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[255] Id, see Articles 1077 and 1078.
[256] Id, Article 1079(1).
[257] Ibid.
[258] Ibid
[259] Id, Article 1079(2).
[260] Ibid.

the bankrupt estate. Articles 1073 and 1074 list two types of creditors who have the right to recover their goods. In both instances, the bankrupt debtor is not the principal debtor. It is because the goods that are in the hands of the bankrupt debtor do not actually belong to him by ownership right that these provisions entitle the owners of the goods the right to recover the goods.[261] The first instance is where the bankrupt debtor has been entrusted with possession of negotiable instruments, including cash (remittances) for the benefit of a third party owner.[262] This is the case where the bankrupt debtor has been appointed to cash negotiable instruments for the benefit of a third party owner and before the cash is collected, the agent (the debtor) has been declared bankrupt. The negotiable instruments do not belong to the bankrupt debtor and it is appropriate that they are recovered by the rightful owners.

The other case is where goods are sent/consigned to the debtor for deposit or for sale on behalf of the owner and the goods can be identified in kind (in part or in whole) at the time of the adjudication of the bankrupt (the agent, consignee).[263] The creditors who may benefit from the rights of recovery recognized under Article 1073 include lessors of chattels,[264] bailors[265] and purchasers bound to the debtor by a warehouse contract.[266]

4. Creditors Secured by Mortgage on Immovables and Businesses

Although the Commercial Code devotes separate provisions to these categories of creditors, the rules relating to these creditors are virtually identical, justifying their treatment under the same heading. On the effect of bankruptcy upon mortgagees, there are different approaches. There are laws that allow secured creditors in general to enforce their security interests, untroubled by the commencement of bankruptcy.[267] This approach is common in those systems which exempt secured creditors from the application of stay (suspension of suits).[268] There are also, on the other

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[261] See UNCITRAL, supra note 11, p. 80, para. 17; see also Civil Code, supra note 41, Article 1145(2), which gives creditors rights similar to that stated in Articles 1073 and 1074 of the Commercial Code

[262] See Commercial Code, supra note 4, Article 1072.

[263] Id, Article 1073.

[264] See Civil Code, supra note 41, Articles 2727ff.

[265] Id, see Articles 2779 ff.

[266] Id, see Articles 2806ff; see also the Proclamation to Provide for a Warehouse Receipts System No. 372/2003, *Federal Negarit Gazetta*, 10th year, No. 2.

[267] UNCITRAL, supra note 11, p. 107, para. 83.

[268] Ibid.

hand, laws which include encumbered assets in the bankrupt estate, to be controlled by trustees, subject to some conditions.[269] French law may be cited as an instance in this regard. French law authorizes trustees to sell encumbered property subject to the condition that the proceeds of sale are placed in a special deposit account, which are paid out to secured creditors upon the confirmation of a reorganization plan.[270] In some laws, the power of trustee over encumbered assets is dependent upon the nature of the proceeding: liquidation or reorganization.[271] A trustee has an unlimited power to sell encumbered assets when the proceeding involved is a reorganization while trustee's power to do so is limited by a period of time in a liquidation proceeding.[272]

We start with Article 1026 - which exempts secured creditors in general from one of the effects of bankruptcy - suspension of individual suits. As already alluded to, what a suit means in particular cases is not clear from the language of Article 1026, but in one respect, what is included in the suspension is beyond dispute - the suit includes an action for attachment of debtor's property.[273] A *contrario* reading of Article 1026 will lead us to conclude that secured creditors can attach (and foreclose in some cases) the collateral which they hold as security. But does that lead to a conclusion that mortgagees are not affected by the onset of bankruptcy proceedings? Before we conclude, we need to examine other provisions of Ethiopian bankruptcy law. Two sections of the bankruptcy law are devoted exclusively to the rights of mortgagees.[274] These provisions contain some clues as to what bankruptcy may signify to mortgagees.[275] These provisions

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[269] Ibid.

[270] French Commercial Code, supra note 35, Article L622-8.

[271] UNCITRAL, supra note 11, p. 107, para. 83.

[272] Ibid; there are also ancillary issues like whether the trustee can sell encumbered assets free and clear of encumbrance; Id, see p. 108, para. 85.

[273] Commercial Code, supra note 4, see Article 1026, second sentence.

[274] Id, see Sections 4 and 5, Chapter 5, Title II of Book V, Articles 1068-1072.

[275] These provisions are found in a section dealing with submission and proof of claims in bankruptcy. Part of the reason why location of these provisions is controversial is because these provisions can be read as having double, even triple purposes/imports at a time. They may as a result be found to be at home immediately after Article 1026 (or in a section dealing with the effects of bankruptcy in general) or in a section dealing with distribution of the proceeds of bankruptcy (Articles 1101ff) or where they are now (in a section dealing with submission and proof of claims in bankruptcy). The complexity of these provisions at first reading is in part attributable to their compression of multiple purposes.

are found far away from the provisions and sections dealing with the effects of bankruptcy but it will be seen that they are in a way an extension of the general provision of Article 1026. Where they are located is not as important (after all we are better off having them in the Commercial Code than not having them at all) as their bearings on the question of the effect of bankruptcy on secured creditors.

We conclude generally from the joint reading of Article 1026 with Articles 1068-1072 that mortgagees are largely unaffected by bankruptcy. The provisions as they now stand may be read as denying the trustees access to encumbered property with an unpleasant result that the mortgagees might be able to call the shots over their collaterals and still be able to participate in the distributions from the bankrupt estate. Mortgagees can pursue their rights over their collaterals untroubled by bankruptcy proceedings. And their right to participate in the distributions from the bankrupt estate depends to a large extent upon the order of distributions from encumbered or unencumbered assets. As pointed out before, the ambiguity of Ethiopian bankruptcy law on this matter can lead to frequent disputes between trustees and secured creditors over collaterals and may result in substantial loss of time as trustees seek to yank encumbered property from the control of secured creditors for the benefit of unsecured creditors (universality of creditors).[276]

c. Effects of Bankruptcy on Third Parties - Avoidance/Invalidation of Transactions during the Suspect Period

The third effect of bankruptcy might also be termed 'effects upon certain creditors,' but this confuses the peculiar effect treated here under with the effects of bankruptcy upon creditors in general (already treated under preceding sections). Some creditors (third parties is a better word) are singled out by bankruptcy law because of the shady deals they make with the debtor as the bankruptcy of the debtor becomes imminent. These shady transactions are in some laws called 'preferential transfers'[277] because their

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[276] For possible solutions, see the section above dealing with the proprietary effects of bankruptcy.

[277] See Notes, *Preferential Transfers and the Value of the Insolvent Firm*, 87 Yale L. J.7, 1449; the avoidance rules in bankruptcy law have the objective of enriching the bankrupt estate by recovering assets paid to creditors, redistributing them among creditors according priority rules and the rules of equality among creditors and controlling creditor behavior during insolvency; id, see at 1449-1450; Michael M. Parker defines them as 'tools by which a trustee can persuade (or force) a beneficiary of a debtor's

aim is to accord preference in favor of certain creditors at the expense of the rest of creditors. If left unchecked by law, some creditors may exploit the existing business transactions, or the terms of their contracts or a special personal relationship with the debtor; they may extort a preference, which will impair either the priority rights or the right to equal distribution of the asset of the bankrupt debtor. Creditors, knowing or expecting that the business might soon be in financial difficulties, may engage in the scramble for the assets of a troubled business in what one writer calls 'race of diligence'.[278]

The bankruptcy laws of many countries provide that the transactions that accord preference of one form or another to one or more creditors to the detriment of other creditors would be avoided.[279] The avoidance of certain transactions is consonant with the basic principle of bankruptcy. Bankruptcy systems are built on the assumption that collective actions are more efficient in maximizing the assets available to creditors than a system that leaves creditors free to pursue their individual remedies.[280] The provisions that permit avoidance of certain transactions 'help to create a code of fair commercial conduct that is part of appropriate standards for the governance of commercial entities'.[281]

The avoidance provisions help to overturn certain transactions to which the bankrupt debtor was a party or involving the debtor's assets.[282] These suspect transactions are perfectly normal and acceptable when they occur outside the context of bankruptcy. These transactions would not have been invalidated under the ordinary rules of contracts, such as on grounds of mistake, or lack of object or some of the other grounds of invalidation of contracts under the Civil Code.[283] Needless to say, the other remedies creditors or the trustee might have to invalidate transactions under the general rules of contract in the Civil Code or the Commercial Code will

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generosity to return the benefit to the bankruptcy estate'; Michael M. Parker, supra note 121.

[278] Notes, supra note 277, p. 1465.

[279] See UNCITRAL, supra note 11, pp. 135-155, paras. 148-203; OHADA, supra note 33, Articles 67-71; see also Notes, supra note 277, at 1449; Michael M. Parker, supra note 121; Richard W. Maloy, supra note 98.

[280] UNCITRAL, supra note 11, p. 136, para. 151.

[281] Id, p. 136, para. 152.

[282] Id, p. 135, para. 150.

[283] See Civil Code, supra note 41, Articles 1696-1730.

remain unaffected by the existence of the special rules of bankruptcy to invalidate transactions entered into during the suspect period.[284]

Generally two approaches have been discerned in describing transactions that are subject to avoidance.[285] The first - objective approach - is to describe objectively the types or characteristics of transactions that are liable to avoidance.[286] These features include the value paid (or the consideration) paid for the transaction (e.g. was the consideration paid by the creditor adequate), or whether the performance was for a debt that is due or whether the transaction was made between two related persons. The establishment of any of these facts renders a transaction liable to avoidance. For example, a mere proof of the fact that the value of property was less than a fair market value at the time of the conclusion of the transaction is sufficient to overturn the transaction. Similarly, if the transaction was concluded between two related persons (natural or juridical), it would be sufficient to overturn the transaction as invalid even though the value given in the transaction were fair.

The other approach is the subjective approach. The subjective approach relies upon evidence which can only be established by reference to mental state of the parties with respect to a specific case. Under the subjective standard, the person needs to provide evidence showing the intent to hide the asset from other creditors, knowledge on the part of the creditor about the insolvency of the debtor, etc. The proof required is a mental state of the parties about the circumstances surrounding the transaction.[287]

Both standards have been subjected to criticism for one reason or another.[288] The objective standard, while easier to establish, has been criticized because of its tendency to produce arbitrary results.[289] Legitimate and useful transactions may be avoided by a mere showing of, for example, relationship,[290] and fraudulent transactions may escape this fate because they were entered into outside the suspect period.[291] The subjective standard may overcome some of the problems of the objective standard, but

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[284] UNCITRAL, supra note 11, p. 136, para 153.
[285] Id, see pp. 137-138, paras. 156-158.
[286] Id, pp. 137-138, para. 157.
[287] Id, p. 138, para. 158.
[288] Id, see p. 137, para. 157.
[289] Ibid.
[290] Id, pp. 137-138, para. 157.
[291] Id, p. 138, para. 157.

it is difficult to establish the subjective mental states like intent and knowledge to overturn a transaction.[292]

Few bankruptcy laws follow either the objective or the subjective criteria in their pure forms for invalidating transactions.[293] Some laws adopt a two-tiered approach of combining a short period (say of three or four months) within which all transactions are invalidated and no defenses can be presented by other parties, with a longer period (say a year or two) in which certain additional elements have to be proved by trustees, such as showing that the transaction was not in the ordinary course of business.[294]

Another form of combining the objective and subjective criteria is to apply the objective test for invalidating some transactions, such as undervalued transactions, and the subjective test to transactions that are aimed at defeating or hindering other creditors.[295] Accordingly, transactions like gifts can be invalidated through the objective criteria while others can be invalidated only if the subjective elements of knowledge or intent are established.[296]

Ethiopian bankruptcy law follows a combination of the objective and subjective tests for invalidation of transactions during the suspect period. For some transactions or acts, the fact that the transaction occurred during the suspect period is sufficient to overturn the transaction. The transactions that are objectively 'suspect' are 'gratuitous assignments', 'payments of debts not due', 'payments of debts due otherwise than in cash, by negotiable instruments or by bank transfers', and securities set up on the property of the debtor' for debts contracted before the setting up of such securities.[297] These acts of the debtor during the suspect period are invalid no matter what the subjective knowledge or intent of the parties was at the time of the conclusion of the acts. The suspect period is fixed by the law to be between fifteen days before the date of suspension of payments and the date of adjudication of bankruptcy.[298] Since the court of bankruptcy has the power to fix the date of suspension of payments as far back as two years

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[292] Id, p. 138, para. 158.
[293] Id, p. 138, para. 159.
[294] Id, p. 138, para. 160.
[295] Id, p. 138, para. 161.
[296] Ibid.
[297] Commercial Code, supra note 4, see Article 1029(a-d).
[298] Id, see Article 1029(d).

before the date of adjudication of bankruptcy,[299] the suspect period can be as long as two years and fifteen days.

Other acts (i.e., payments of debts due and all acts for consideration), can be invalidated only if the subjective test is met. It is not enough that these acts occur during the suspect period (for these acts, incidentally, the suspect period is slightly shorter, by fifteen days - for it runs from the date of suspension). The trustee must show that 'the parties who have received payment or have dealt with the debtor did so knowing that suspension of payments had taken place'.[300] It should be noted that all that a trustee has to show is evidence showing that the other party had knowledge of the suspension of payments by the debtor.[301]

The subjective criterion under Ethiopian law is close to the objective criteria. The trustee does not have to show that the other party was complicit to the debtor's conspiracy to smuggle property away from the reach of other creditors. Nor is the trustee required to prove that the parties had the intention of defeating or hindering the interests of other creditors. This makes the job of the trustee much easier than otherwise. But it puts at risk so many transactions that are carried out as a matter of course, as a necessity of ordinary business relationships, like payments of utility bills and premiums to insurance companies.

The relief is that the court has the discretion to refuse trustee's request for invalidation on subjective grounds. While invalidation requests on objective grounds must be granted by courts, invalidation requests on subjective grounds may be refused. The court may look at the circumstances surrounding the facts of the transaction and refuse to grant invalidation, and one of the instances in which the court should refuse happens to be when the payments are a matter of ordinary course of business.[302]

III

4. Distribution, Priority of Creditors and Discharge of the Bankrupt Debtor

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[299] Id, see Article 977 and 978(3).

[300] Id, see Article 1030.

[301] Whether the suspension must lead to the bankruptcy that is now pending or whether any ordinary suspension will do, the law does not say.

[302] Article 1029 of the Code, which applies, as seen above, the objective standard uses a peremptory phrase 'shall be invalid' in contradistinction to Article 1030, which applies the subjective standard and uses a permissive phrase 'may be invalidated'.

a. Distribution in General

Equitable distribution of the assets of a bankrupt estate is one of the principal goals of a bankruptcy proceeding.[303] Equitable does not of course mean equal treatment. It means creditors with similar legal rights should be treated fairly, receiving a distribution on their claim in accordance with their relative ranking and interests.[304] Once the claims of various creditors are properly admitted and verified,[305] the stage is set for distribution of the proceeds of the bankrupt estate among the various creditors of the bankrupt debtor.

Creditors are not a homogenous group. Some of them had contractual relationships with the debtor prior to the onset of bankruptcy.[306] And there are those whose relationship with the debtor was not contractual - the so-called involuntary creditors, such as the tax authorities and tort claimants.[307] Distribution among these diverse creditors is about balancing the competing and conflicting interests of them. Distribution is not just about the application of bankruptcy rules - although the rules of bankruptcy are central; it is as much about giving effect to the various laws respecting the rights of the diverse creditors. Giving effect to other laws means that bankruptcy laws must at times respect the commercial bargains creditors struck with the bankrupt debtor.[308] It is held that that way the bankruptcy system 'preserves legitimate commercial expectations, fosters predictability in commercial relationships and promotes equal treatment of similarly situated creditors'.[309]

In addition to the legal and commercial relationships that establish some pecking orders of distribution, the rules of distribution in bankruptcy must also 'reflect the choices that recognize public interests,' like the protection of employment.[310] Needless to say, there are different approaches to the

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[303] Equitable treatment permeates and informs many provisions of bankruptcy laws, including provisions regarding the application of suspension of suits, voting, etc; see UNCITRAL, supra note 11, p. 11, para. 7; see also Donald K. Korobkin, *Rehabilitating Values: A Jurisprudence of Bankruptcy*, 91 Columb. L. Rev. 717.

[304] UNCITRAL, supra note 11, p. 11, para. 7.

[305] The admission and verification of claims in bankruptcy has not been addressed in this article. For rules on admission and verification of claims, see Commercial Code, supra note 4, Articles 1041ff.

[306] UNCITRAL, supra note 11, p. 266, para. 51.

[307] Ibid.

[308] Id, p. 267, para. 52.

[309] Ibid.

[310] Id, p. 267, para. 53.

ranking of different classes of creditors in bankruptcy. We shall look at the ranking of various classes of creditors under Ethiopian bankruptcy law below -as usual, with frequent reference to comparative experience.

b. Priority of Creditors

i. Priority Rights of Secured Creditors

Secured creditors enjoy absolute priority over the collateral they hold in many bankruptcy systems.[311] The collateral is commonly a specified property (immovable or movable) but in some countries, security over the general funds of the debtor is recognized.[312] The norm in virtually all countries is to permit secured creditors to seek payment out of their collateral by withdrawing the collateral from the estate.[313] However, some countries authorize trustees to sell the collateral and distribute the proceeds to secured creditors on priority basis after payments of the administrative costs of sale. [314]

In those systems where absolute priority is recognized, secured creditors enjoy priority not just against unsecured creditors but secured creditors who hold security over a collateral other than the one under consideration.[315] The only time their priority is in any danger of competition is when other secured creditors hold security over the same collateral.[316] While there are many possibilities of ordering or ranking these conflicts, the principle that is frequently in use in such cases is the 'first in time, first in right' principle.[317] It is a simple timing principle which gives precedence to a creditor who obtains security interest first.[318]

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311 See Thomas H. Jackson and Anthony T. Kronman, *Secured Financing and Priorities among Creditors*, 88Yale L. J.6 1161-1162 (May 1979); UNCITRAL, supra note 11, p. 269, para. 62; Barbara Morgan, *Should the Sovereign be Paid First? A Comparative International Analysis of the Priority of Tax Claims in Bankruptcy*, 74 Am. Bankr. L.J. 461 (Fall, 2000).

312 UNCITRAL, supra note 11, p. 269; a security scheme that attaches to a class of debtor's assets is called a floating charge. The assets covered by security change from time to time and the debtor is allowed to trade in these assets until a creditor takes a step called crystallization to attach whatever assets happen to be in the hands of the debtor at the time of attachment; see Vanessa Finch, *Security, Insolvency and Risk: Who Pays the Price?*, 62Modern Law Review5, 639, 658 (1999).

313 See Richard W. Maloy, supra note 98.

314 Richard Maloy cites Turkey as an example; see Richard W. Maloy, supra note 98.

315 Jackson and Kronman, supra note 311, p. 1162.

316 Ibid.

317 Ibid.

318 Ibid

Not all bankruptcy systems recognize the absolute priority of secured creditors.[319] In some systems, the claim of secured creditors is made subordinate to certain claims like bankruptcy expenses, employee claims and tax claims.[320] Under French law, for example, employees have one of the strongest positions among creditors. Salaries and sums due to employees rank above secured creditors.[321] There is still another approach to the ranking of secured creditors - namely partial absolute priority for secured creditors. In this, secured creditors are obliged to share some losses along with unsecured creditors.[322] Needless to say, these approaches are a reflection of different public policies in different bankruptcy systems.[323]

What is the position of Ethiopian bankruptcy law in this regard? The language of the main priority provision of the Commercial Code - Article 1110 - is unnecessarily ambiguous about the rank of secured creditors in bankruptcy proceedings. It is necessary to quote Article 1110 in full to understand its import:

> Article 1110 - Distribution of Proceeds of Winding-up
> After deduction of:
> (a) costs and expenses;
> (b) sums applied for the support of the debtor or his family; and
> (c) sums paid to preferred creditors;
> the net proceeds of the winding-up shall be distributed to all the creditors in proportion to the their debts proved and admitted, subject to the provisions of Articles 1065, 1066 and 1068.

Article 1110 can be read in two senses:

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[319] UNCITRAL, supra note 11, p. 269, para. 63.

[320] Id, p. 269, para. 63.

[321] Jay M. Goffman and Evan A. Michael, *Cross Border Insolvencies: A Comparative Examination of Insolvency Laws of Industrialized Countries*, 12J. Bankr. L. & Prac.5 (2003); employees have also the right to be paid during the 'observation period' while other creditors do not have the right; see ibid.

[322] UNCITRAL, supra note 11, p. 269, para. 63; for partial absolute priority, see Lucian Arye Bebchuk and Jesse M. Fried, *the Uneasy Case for Priority of Secured Claims in Bankruptcy*, 105 Yale L.J.4 (Jan. 1996).

[323] For a review of the different justifications given for priority of secured creditors and their critiques, please see Lynn M. LoPucki, *Unsecured Creditors' Bargain*, 80Virginia Law Review, at 1947-1963 (1994); Vanessa Finch, supra note 312, at 637-643. According to Finch, the rationale of security rests on three main arguments: that the security agreement has been freely bargained or contracted for (freedom of contract argument); that it does not deprive the company of value; and that relevant parties are given due notice of security agreements and therefore have no reason to complain; see id, at 660.

i) the position of secured creditors is subordinate to the creditors accorded priority in the bankruptcy law itself (i.e., priority creditors mentioned in Article 1110 (a) (b) &(c));

ii) the position of secured creditors is subordinate to none, save prior secured creditors over the same collateral.

These rival interpretations are made possible by the language of Article 1110 - which, instead of unequivocally placing the position of secured creditors vis-à-vis other creditors, leaves their position ambiguous. Besides, Article 1110 is incomplete. It does not mention some secured creditors who enjoy similar positions in other parts of the Commercial Code - e.g., creditors secured by mortgage on business are not even mentioned, although these creditors enjoy the same position in other matters.[324] We have treated these two classes of creditors (creditors secured on mortgages on immovables and creditors secured by mortgages on business) together because we are convinced that their position is virtually identical in bankruptcy proceedings (see part II, 3(c) (iii) (4) above).

Are we then to conclude that something is missing in Article 1110 of the Code? It is fair to say that something is indeed missing. There is no reason why creditors secured by mortgage on business should be excluded from priority when in other respects they belong to the same league with creditors secured by mortgage on immovables.[325]

Of the two rival interpretations of Article 1110, there are reasons to believe that the second interpretation is the correct one. The absolute priority of secured creditors has already been acknowledged in Articles 1065-1072 of the Commercial Code - to which we are referred at least partially in Article 1110. Creditors secured by mortgage (either on immovables or business) are paid in priority over all other creditors from the proceeds of encumbered assets. They rank with unsecured creditors only when they are not fully paid out of the proceeds of encumbered assets.[326] To be sure, the language of Articles 1065-1072 is not free from ambiguity either,[327] but in one respect their meaning is clear - secured creditors are subordinated or demoted to

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[324] Compare articles 1065-1068 with Articles 1069-1072.

[325] The discordance in the language of some provisions of the Commercial Code is not entirely unexpected; after all the first drafter died prematurely in 1954, leaving the drafts to the second drafter.

[326] Commercial Code, supra note 4, see Articles 1065 and 1069.

[327] Not the least of which, these Articles seem to use 'preferred' creditors in the same breath with 'secured' creditors'.

the position of unsecured creditors only when they are not fully paid out of the proceeds of encumbered property.

We may also cite Article 1026 to strengthen the position that secured creditors enjoy absolute priority under Ethiopian bankruptcy law. Article 1026, as repeatedly mentioned, exempts secured creditors from one of the effects of bankruptcy - suspension of individual suits. Many bankruptcy laws that exempt secured creditors from the effect of suspension also grant secured creditors absolute priority over their collaterals.[328] It will indeed be odd if Ethiopian bankruptcy were to exempt secured creditors from the effect of suspension and then turn around to subordinate their claims to other creditors.

In practice, secured creditors (particularly mortgagees) have invoked the provisions of the Civil Code to support their claims of priority over other creditors. Article 3076 of the Civil Code appears to support the absolute priority right of mortgagees in respect of 'the registered amount of the claim', which shall include interest, the necessary expenses and insurance premiums, and costs of attachment proceedings.[329] The language of the Civil Code is clear in granting absolute priority to mortgagees for it brooks no competition to mortgagees other than other mortgagees who have registered their claim on the same immovable property - in which case, the rule of first registered breaks the tie.[330]

However, the apparent clarity of the language of the Civil Code has not prevented controversies from arising in practice as to the priority rights of secured creditors' vis-à-vis other creditors. Secured creditors frequently found themselves asserting their priority rights against tax authorities, employees and judgment creditors. *Inland Revenue Authority vs. Fissehaye W/Gebriel, Housing and Thrift Bank and Addis Ababa Abattoirs*,[331] for example, involved a four-way dispute over priority of creditors. Fissehaye took all the trouble of finding and attaching the property of a debtor (which was the house of the debtor), but when the property was up for sale, other creditors came into the scene and demanded payment from the proceeds of the sale. Fissehaye argued that he was entitled to priority because he took all the trouble and should be rewarded with priority as a result of his diligence as

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328 See UNCITRAL, supra note 11.

329 See Civil Code, supra note 41, Articles 3077-3080.

330 Id, see Article 3081.

331 (Supreme Court, Civ/App. No. 13/1984), in Supreme Court Cases, Vol. 3, in Amharic, pp. 595-598

a judgment creditor. Housing and Thrift Bank claimed priority because it was a secured creditor (although in this case, its collateral was a garage not the house in question). Inland Revenue Authority (the Tax Authority) invoked a 1947 law which allegedly granted priority to government claims. Although this case involved the case of a secured creditor (the Bank) arguing priority over a property which was not its collateral, it is an illustration that the clear language of the Civil Code is no guarantee for the absolute priority rights of secured creditors, particularly when the competition comes to be against preferred creditors who are granted priority by other laws of Ethiopia. Perhaps partly as a result of this long line of disputes over priorities,[332] some recent laws of Ethiopia have clarified the priority rights of secured creditors vis-à-vis some preferred creditors. The tax laws of Ethiopia issued in 2002 have ended the long-time speculation over the priority of tax claims vis-à-vis secured creditors. Article 80 of the Income Tax Proclamation -which incidentally is reproduced verbatim in other tax laws of Ethiopia promulgated in 2002[333] - subordinates tax claims to the 'prior secured claims of creditors' in no uncertain terms. The tax laws strengthen the Civil Code's 'absolute priority' doctrine in respect of at least tax claims.

ii. Priority of Administrative Costs and Expenses

Ethiopian bankruptcy law accords the first priority (after secured creditors over their collaterals) to the satisfaction of what it calls costs and expenses.[334] Administrative expenses are granted priorities in many other bankruptcy laws as well.[335] The policy underlying their priority is the desire to ensure proper payment for the parties acting on behalf of the bankrupt estate - without whose diligence, the bankruptcy proceedings would not have been successful.[336]

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[332] See *Commercial Bank of Ethiopia vs. Inland Revenue Authority*,(Supreme Court, Civ./App. No. 562/69), in Supreme Court Cases, Vol. 1, in Amharic), at 17-18; *Abyssinia Bank vs. Inland Revenue Authority* (Tax App. Case No. 543, 1996 E.C.), in Amharic, (unpublished).

[333] See Article 32(1) of the Value Added Tax Proclamation No. 285/2002, *Federal Negarit Gazetta*, 8th year, No. 33; Article 14 of the Turnover Tax Proclamation No. 308/2002, *Federal Negarit Gazetta*, 9th year, No. 21, and Article 11(1) of the Excise Tax Proclamation No. 307/2002, *Federal Negarit Gazetta*, 9th year, No. 20.

[334] Commercial Code, supra note 4, Article 1110(a).

[335] See UNCITRAL, supra note 11, p. 270, para. 66; see also *the Priority Provisions*, 1Bankr. Dev. J. 282, 283 (1984).

[336] UNCITRAL, supra note 11, p. 270, para. 66.

Ethiopian bankruptcy law does not define what costs and expenses are. A debate may therefore arise as to what 'costs and expenses' qualify for priority under Ethiopian bankruptcy law.[337] Once again the Guide supplies the best enumeration of what expenses may qualify as administrative expenses in bankruptcy: remuneration of the trustee and any professionals employed by the trustee; debts arising from the proper exercise of the trustee's functions and powers; costs arising from continuing contractual obligations (e.g., labor and lease agreements); costs of the proceedings (e.g. court fees).[338]

A trustee may be authorized, as we saw above, to continue the business of the bankrupt debtor,[339] and once continuation of business is authorized, it invariably gives rise to a special category of creditors - post-bankruptcy creditors. Post-bankruptcy creditors are usually more demanding than creditors under ordinary circumstances, because they deal with a distressed business. Many of them are unlikely to enter into contracts with the bankrupt business unless they are paid in cash or guaranteed a security.[340]

In recognition of the serious difficulties trustees face in getting the business going, Ethiopian bankruptcy law accords post-bankruptcy creditors a rank above unsecured creditors. Although the Commercial Code declares them to be 'creditors of the universality' (in other words, unsecured creditors), the Code exempts them from some of the harsh consequences of bankruptcy, such as the operation of suspension of suits. Post-bankruptcy creditors are not bound by the operation of suspension of suits under Article 1026, which means that they can bring suits for the payment against the bankrupt estate as the claims fall due. And, more importantly, they have priority of payment before unsecured creditors.[341] We may have problems locating the exact ranking of post-bankruptcy creditors under Article 1110 of the Code. It is not clear from the language of Article 1039(2) if the priority of post-bankruptcy creditors is good against all other

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[337] The Amharic version is more expressive. Literally translated the Amharic version states 'expenses and costs incurred for bankruptcy proceedings'.

[338] See UNCITRAL, supra note 11, p. 270, para. 66; sometimes, a claim may be characterized either as a lower order (ranked) priority claim or a higher order (ranked) claim. For example, taxes incurred during and as a result of the administration of the bankrupt estate may be considered as lower order claims (as taxes) or higher order claims (as post bankruptcy expenses); see 1Bankr. Dev. J.(1984), supra note 335, at 288.

[339] See Commercial Code, supra note 4, Article 1039.

[340] In some systems, trustees are permitted to give security to secure post-bankruptcy financing; see UNCITRAL, supra note 11, pp. 115-117, paras. 100-104.

[341] See second sentence of Article 1039(2).

unsecured creditors or subordinate to some unsecured but preferred creditors. A problem of ranking may, for example, arise between the claims of post-bankruptcy creditors and the claims of tax authorities, which are preferred/priority claims (see below).

In other bankruptcy systems, the claims of post-bankruptcy creditors are regarded as the costs and expenses of the bankruptcy and are usually given priority ranking over all other unsecured creditors.[342] The costs and expenses of bankruptcy are also ranked first over all other unsecured creditors in Ethiopia. If we follow the trend elsewhere, it would appear that post-bankruptcy creditors are first priority creditors under Ethiopian bankruptcy law too. Since these creditors come into contact with the business of the bankrupt post facto, they might even demand security before entering into contracts with the trustee, in which case they will elevate themselves even higher to the absolute priority status of secured creditors.

iii. Priority for Sums for the Support of Debtor and Family

Before the winding up of the bankrupt estate, the commissioner may permit the trustee to apply part of the estate to support the debtor and his family.[343] Upon the winding up of the estate, the commissioner 'shall fix amount of assistance to be given to the debtor and family where the assistance is agreed to by the creditors' committee.[344] In terms of the timing as well as the procedures required, the two assistances to debtor and family are clearly different, but it is not clear if both or only one of them is applicable at a time. There is little doubt that both are discretionary, and as such may not be ordered at all. Once assistance to the debtor and family is ordered and the amount is fixed, however, the claim for assistance acquires a priority status, subordinate only to costs and expenses of bankruptcy (outside secured creditors, that is). This priority is not unique to Ethiopian bankruptcy law. French bankruptcy law, for example, accords priority to 'the subsidies granted to the head of the business or managers and their families.[345]

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[342] See UNCITRAL, supra note 11, p. 116, para. 101.

[343] Commercial Code, supra note 4, Article 1020.

[344] Id, Article 1102.

[345] French Commercial Code, supra note 35, see Article L643-8; a question may of course arise as to who qualifies as a debtor, as the French law compels us to raise. Can the provisions of Article 1020 and 1102 of the Ethiopian Commercial Code be used to authorize assistance for managers of business organizations?

iv. Priority of Preferred Creditors

Outside secured creditors, the Commercial Code grants the third rank to preferred creditors – one rank above unsecured creditors. We have neither a definition nor even a description (not even a hint) about who these creditors are. We would have been better off if the Code left it as that, but the Code makes the task of identifying these creditors complicated by using 'preferred' creditors interchangeably or in the same league with secured creditors. Articles 1065-1067 of the Code appear to place 'preferred' creditors on par with secured creditors on the distribution of proceeds from encumbered and unencumbered assets.[346] Both cannot be true. Either preferred creditors are accorded priority on par with secured creditors (as Articles 1065-1067 seem to intimate) or they are subordinate to not only secured creditors but also priority claims like costs and expenses.[347]

Unable to make sense of the language of Articles 1065-1067, we cannot but incline to the latter view – i.e., that preferred creditors are subordinate to secured creditors. Who are preferred creditors? Article 1110(c) seems to take it for granted that we know what is meant by preferred creditors. We must look elsewhere to understand preferred creditors.

Some unsecured creditors are routinely accorded priority (preference) in various bankruptcy laws.[348] One type of unsecured claims that are frequently granted priority is tax claims.[349] The justifications that are given for the priority of tax claims are first that tax claims represent the claims of

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[346] Article 1065, for example, states in part 'where the distribution of the proceeds of sale of immovable takes place before or at the same time as that of the proceeds of the sale of movables, *preferred or secured creditors*....rank equally with the unsecured creditors...' (italics mine); the other articles repeat the reference to preferred creditors along with secured creditors; see, Commercial Code, supra note 4, Articles 1066, 1067 and 1068.

[347] There is an unfortunate and careless use of the expressions 'preferred creditors' with 'secured creditors. Sometimes, the expression 'preferred creditors' is used interchangeably with 'secured creditors' (see Article 1065); and at other times, it is used to refer to unsecured creditors but priority creditors (see Article 1110 (c)). The dictionary meaning of 'preferred creditors' is that of creditors having superior right to payment, which may mean both secured creditors and priority creditors. Secured creditors are creditors who have the right to proceed against a collateral and apply it to the payment of the debt. And priority creditors are creditors who are given priority in payment from the debtor's assets; see Black's Law Dictionary, supra note 48.

[348] See UNCITRAL, supra note 11, p. 270, para. 67;see also Jackson and Kronman, supra note 311, at 1161-1162.

[349] UNCITRAL, supra note 11, p. 273, para. 74; see also Volkmar Gessner et al, supra note 93, at 508.

the community and therefore deserve priority on that account and second that the government is an involuntary creditor, unable to choose its debtors and/or obtain security for its claims.[350] The third argument often raised in connection with the priority of tax claims is that many tax claims represent claims for payment of taxes from a debtor who has been holding the taxes in trust. For instance, a claim for the payment of VAT is made against a debtor that collects VAT from consumers on behalf of the government. The debtor of VAT is a collection agent for the government and is not an owner of the VAT claimed. This argument is partly true - for there are also taxes which are directly claimed from debtors (e.g., income taxes) for which the priority rules (if they exist) equally apply.[351] Ethiopian tax laws recognize this distinction between taxes collected by bankrupt debtors in trust and taxes owed by bankrupt debtors. Taxes collected by bankrupt debtors in trust (for example, taxes withheld by withholding agents) do not even form part of the bankrupt estate and may be not attached by creditors of the bankrupt debtor.[352] Whatever and however convincing the justifications may be, the priority of tax claims is not without its critics.[353]

The other types of unsecured claims that are commonly accorded priorities are employee claims.[354] The first argument in favor of granting priority to employee claims is the 'involuntary' creditor thesis. It is contended that employees must hire themselves out without being in a position to get security for their claims and the nature of their relationships makes it difficult to initiate an action against their employers.[355] The moral case in

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[350]See Volkmar Gessner et al, supra note 93, at 508; this contention that the government is an involuntary creditor can be easily refuted: the government is not the only involuntary creditor out there; there are many creditors who are involuntary creditors and yet remain unsecured and un-preferred (e.g., tort creditors are involuntary creditors).

[351] There is a solution for recovery of tax claims from debtors who hold the taxes in trust; the government does not even have to stand in line for the collection of VAT from the debtor via priority provisions; the provisions relating to recovery of goods and money from a debtor who holds the goods and money in trust may be used to recover the taxes; see Commercial Code, supra note 4, Article 1073.

[352] See Income Tax Proclamation No. 286/2002, *Federal Negarit Gazetta*, 8th year, No. 34, Article 82.

[353] The critics fear that priority to tax claims may encourage tax authorities to be complacent about monitoring debtors and collecting debts in a commercial manner; see UNCITRAL, supra note 11, p. 273, para. 74.

[354] See UNCITRAL, supra note 11, p. 272-273, paras. 72-73; see Volkmar Gessner et al, supra note 93, at 508.

[355] Hahn, 1881, 348, quoted in Volkmar Gessner et al, supra note 93, at 508.

favor of priority for employee claims is compelling. In times of bankruptcy, employees are threatened with not just the loss of money but their means of livelihood - their jobs.[356] In recognition of this, the International Labor Organization (ILO) sponsored and succeeded in getting ratified an International Convention granting priority rights to employee claims.[357]

Many countries are not content with just signing the Convention and have included in their national laws provisions that grant priority to employee claims.[358] There are differences among countries in their approach to the ranking of employee claims. In many bankruptcy laws, employee claims are ranked higher than most other priority claims, and in some countries, employee claims are ranked higher than even secured creditors.[359] Under French law, for example, employees have one of the strongest positions among creditors. Salaries and sums due to employees rank above secured creditors.[360]

Preferred creditors may not have been identified in the bankruptcy law of Ethiopia with expectation that other laws will identify them. Indeed there are many other laws of Ethiopia which grant priority to some creditors. We will review some of these other laws to analyze what the priority might mean in light of Ethiopian bankruptcy law.

One of the laws that extend priority is the Labor Proclamation of Ethiopia. Article 167 of the Labor Proclamation extends priority to any claim of payment of workers arising from employment. Almost all of the tax laws of Ethiopia grant priority to tax claims.[361] Article 80 of the Income Tax Proclamation, which incidentally is the rule for all other taxes like VAT, states: 'From the date on which tax becomes due and payable under [this] Proclamation, subject to prior secured claims of creditors, the Authority has

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[356] Volkmar Gessner et al, supra note 93, at 510.

[357] See Protection of Wages Convention, 1949 (No. 95).

[358] See International Labor Organization, *Protection of Workers' Claims in the Event of Insolvency of their Employer* (International Labour Conference, 78th Session, Report V (1), 1991), p. 76, accessed at http://books.google.com.et/books, last accessed on October 24, 2010.

[359] Ibid.

[360] Goffman and Michael, supra note 321; employees have also the right to be paid during the 'observation period' while other creditors do not have the right; see ibid; see French Commercial Code, supra note 35, Article L625-1 to L625-8.

[361] See the Value Added Tax Proclamation, supra note 333, Article 32; the Turnover Tax Proclamation, supra note 333, Article 14; the Excise Tax Proclamation, supra note 333, Article 11.

preferential claim over all other claims upon assets of the person liable to pay the tax until the tax is paid.'

The Tax Proclamation even goes further in authorizing the Tax Authority to register tax claims over any property of taxpayers, thus elevating simple priority over unsecured creditors to priority over later secured creditors.[362] Preferred creditors are lumped together in an undifferentiated mass under Ethiopian bankruptcy law, although they comprise a diverse (not to say disparate) groups of creditors. These creditors - however diverse - occupy third place in the ranking of priority claims. That is where the problem begins. We will notice that many of the other laws granting priority use such a powerful and peremptory language that they do not appear to admit of any kind of competition. Let's examine some of the provisions. The already cited Article 167 of the Labor Proclamation: 'Any claim of payment of a worker arising from employment relationship shall have priority over other payments or debts.'

The priority provision of the income tax law as can be read from the citation above uses such a strong language as to admit of no competition whatsoever from other creditors (save prior secured creditors). If the creditors were not such a diverse group, we would have settled for a solution of proportional distribution of the proceeds among them. Compounding the problem is the fact that these laws came out at different times in Ethiopian history. The public policies that generated these priorities are not even related. Chances are the priorities to one group of creditors (e.g., employees) were granted without any consideration for the priority rights of other preferred creditors. The strong language used in the priority provisions of these other laws suggests that these priorities brook no competition. When tax claims compete with employee claims in bankruptcy, do we resort to pro rata distribution of the balance of the bankruptcy proceeds among them or do we have recourse to the rule of interpretation that gives precedence to later laws? As the law stands right now, there seems to be no better option for courts than ordering a pro rata distribution among diverse preferred creditors. That at least is more reasonable than simply applying the rule of interpretation that gives precedence to later laws over earlier laws. An adoption of the rule of interpretation that gives precedence to later laws leads to absurd conclusions in these cases, for the genealogy of the laws is not even related.

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[362] See Income Tax Proclamation, supra note 352, Article 80(2) - (4).

The priority provisions of the Commercial Code are in need of revision in this regard, perhaps along the lines of the priorities developed in the new Banking Business Proclamation of 2008. The new Banking Business Proclamation ranks claims against insolvent banks in the following order: 1) remuneration of the receiver and expenses of receivership (the equivalent of costs and expenses); 2) post-receivership (bankruptcy) creditors; 3) claims of non-managerial employees; 4) deposits; 5) taxes owed to the Federal and Regional Governments; 6) other claims against the bank and 7) interest on claims. [363] As can be readily seen, the new Banking Business Proclamation unpacks preferred/priority creditors and subordinates one to the other making it easier for courts to rank priority claims. We cannot say the same thing about the priority rules of the Commercial Code.

v. Ordinary and Unsecured Creditors

Ordinary unsecured creditors receive the balance of the proceeds of the bankrupt estate once the claims of all secured and priority creditors have been satisfied.[364] It is easy to view these creditors as homogenous (and prescribe a pro rata distribution among them) but some bankruptcy systems create lower order subordination among these creditors as well.
For business organizations in particular, shareholders may be seen as creditors of the company. Nonetheless, many bankruptcy laws subordinate the claims of owners and equity holders (including claims of interest) to the claims of ordinary, unsecured creditors.[365] Another possible subordination from ordinary unsecured creditors is the claim of related persons – creditors who have familial or business relationships with the debtor.[366] Some countries subordinate these claims in all cases and others subordinate them only when fraud is involved.[367] Finally, some countries subordinate claims such as gratuities, fines and penalties (whether administrative, criminal or some other type).[368] Some countries exclude these claims completely from the share of the bankrupt estate.[369]

Ethiopian bankruptcy law does not directly address the subordination of some claims of ordinary unsecured creditors at all. The conclusion we can draw from this is that all ordinary, unsecured creditors enjoy equal status

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[363] See Banking Business Proclamation, supra note 39, Article 45.
[364] UNCITRAL, supra note 11, p. 273, para. 75.
[365] Id, p. 273, para. 76.
[366] Id, p. 274, para. 77.
[367] Ibid.
[368] Id, p. 274, para. 78.
[369] Ibid.

and benefit from the pro rata distribution of the balance remaining after secured and priority creditors. However, the claims of owners and equity owners – to the extent they are treated as creditors – are subordinated to ordinary and unsecured creditors. Article 501 of the Commercial Code prohibits distribution of the assets among members of a company 'until the creditors of the company have been paid or provisions for payment made'. As for creditors that are excluded from the share of the proceeds of the bankrupt estate, the only creditors one can think of are the bankrupt co-guarantors who are jointly and severally liable.[370]Bankrupt co-guarantors may not claim against one another 'unless the total amount of dividends paid in the several bankruptcies exceeds the total amount of the claim'.

c. Discharge of the Bankrupt Debtor

Discharge, or the circumstances under which it is granted at all, is one of the central questions of any bankruptcy system. Discharge is described by one writer as 'the greatest gift that can be bestowed' by a bankruptcy regime, for it provides fresh start to honest debtors.[371] The prospect of discharge gives an otherwise submissive debtor the leverage to negotiate with creditors.[372] Failure of a business is increasingly seen as a natural feature of modern economies; businesses, good or bad, may fail even in circumstances where responsibility is not involved, and more importantly, once doomed is not always doomed, and in fact studies have shown that persons who have tasted the 'bitter pill' of failure are often more successful in later business ventures.[373]

Rafael Efrat, who studied and compared the bankruptcy systems of several countries, divides these systems into three based on their policy of discharge after the end of bankruptcy: conservative, moderate and liberal – echoing the common language in describing political parties.[374] In the conservative camp are countries marked for the conspicuous absence of debt forgiveness in their bankruptcy laws.[375] Moderate bankruptcy systems are distinguished by the availability of debt forgiveness for bankrupt debtors but the decision to forgive is in the discretion of the judges and is

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[370] See Commercial Code, supra note 4, Article 1056.

[371] See Michael M. Parker, supra note 121; see also *Exceptions from Discharge*, 1Bankr. Dev. J. 307, 308(1984).

[372] Michael M. Parker, supra note 121.

[373] See UNCITRAL, supra note 11, p. 281.

[374] See Rafael Efrat, *Global Trends in Personal Bankruptcy* 76 Am. Bankr. L.J. 81 (Winter, 2002).

[375] Ibid.

therefore fraught with some uncertainty.[376] The countries of the liberal camp offer discharge 'with high degree of certainty and with relative promptness'.[377] The United States is generally regarded as a country with the most generous regime of discharge in bankruptcy systems of the world.[378]

Although the Guide does not characterize discharge systems as conservative, moderate or liberal like Efrat did, it too identifies more or less three approaches to discharge.[379] There are systems where a debtor cannot be discharged until all debts are paid.[380] There also systems in which a number of conditions and restrictions attach before the debtor is discharged or upon which the debtor is discharged.[381] At the other extreme, there are systems that 'provide for complete discharge of an honest, non-fraudulent debtor immediately following distribution' in bankruptcy.[382]

No bankruptcy system grants blanket discharge to bankrupt debtors. Even countries that are regarded as 'liberal' in granting discharge often provide for exceptions. The US bankruptcy Code has a long list of exceptions to discharge, classified conveniently as government liabilities, tort liabilities and family support liabilities.[383] Of government liabilities, all income and excise taxes for three years prior to the bankruptcy are deemed non-dischargeable.[384] Of tort liabilities, damage claims arising from the debtor's willful and malicious injury to another person or property are not dischargeable.[385] Of family support liabilities, child support and alimony payments for the maintenance or support of a former spouse are deemed not dischargeable.[386]

Under French law, individual claims of creditors are terminated and the debtor is discharged upon closure of bankruptcy proceedings.[387] French law enumerates the conditions in which the debtor is not discharged upon

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376 Ibid.

377 Ibid.

378 Ibid, see also see Richard W. Maloy, supra note 98.

379 UNCITRAL, supra note 11, p. 282, para. 4.

380 Ibid.

381 Ibid; the debtor may be discharged on condition that he no longer acts as director or manager of a business organization.

382 UNCITRAL, supra note 11, p. 282, para. 5.

383 1Bankr. Dev. J. (1984), supra note 371, at 307.

384 Id at 308.

385 Id at 319.

386 Id at 316.

387 French Commercial Code, supra note 35, see Article L643-11.

closure of bankruptcy proceedings. These conditions may be generalized as conditions related to the nature of the claims, and those that are related to the qualities or attributes of the debtor. Of the conditions related to claims that are not dischargeable upon closure of bankruptcy proceedings, French law mentions claims of creditors arising from criminal convictions of the debtor and claims attached to the person of the debtor.[388] The conditions related to the qualities or attributes of the debtor are personal disqualifications and convictions from fraudulent bankruptcy and being at the helm of a business which was previously submitted to bankruptcy within the last five years (in other words, no discharge on second bankruptcy).[389] OHADA Uniform bankruptcy Act of 1998 leaves the possibility of discharge open to all debtors except in one case: where a person is convicted of a felony or a misdemeanor leading to a prohibition to carry on a trade.[390]

Before we characterize Ethiopian bankruptcy law in its approach to discharge of debtors, we need to explore certain provisions of the Commercial Code to check whether discharge is available. The first provision to mention discharge is Article 987 (1)(b) of the Code - which incidentally deals with preliminary orders in the judgment of bankruptcy that are not open to set aside or appeal. Although Article 987 mentions 'discharge' as one of these orders, we have reason to be suspicious about the possibility of discharge at this early stage of the bankruptcy proceedings.[391] Another early provision of the Ethiopian bankruptcy law that promises discharge is Article 1023, which as early in this article fixes the period for which a bankrupt remains dispossessed of his property. That period of dispossession runs from the date of the declaration of bankruptcy to the time of the debtor's discharge. Again we cannot rely upon this provision for our opinion on the state of discharge under Ethiopian bankruptcy law - because this provision simply holds out a promise of discharge, which hinges on the 'real' provisions of discharge.

We need to look for discharge towards the end of the bankruptcy provisions. One provision in particular holds out perhaps the strongest

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[388] See ibid; according to the UNCITRAL Guide, claims that attach to the person of the debtor include tort claims, maintenance claims, penalties, etc; see UNCITRAL, supra note 11, p. 282, para. 7.

[389] French Commercial Code, supra note 35, Article L643-11.

[390] See OHADA, supra note 33, Articles 204-215.

[391] It is interesting to note that all the other matters dealt with in Article 987 are preliminary matters - like appointments, fixing the date of suspension, etc.

promise of discharge - Article 1107(5) of the Commercial Code. There it is stated that approval of a lump sale of assets shall result in the discharge of the debtor to creditors. However, the promise of discharge in the cited sub-article is too feeble a comfort for the debtor, compared in particular to the analogous provisions in the bankruptcy laws of other countries.
The authorization of lump sale of assets occurs under conditions very similar to composition - in other words, it is contingent upon the agreement of a substantial number of creditors. The trustees are required to consult creditors, who shall approve of the proposal (for lump sale of assets). The Amharic version of Article 1107(3) makes it very clear that three-fourths of creditors shall approve of the lump sale of assets for the sale to be confirmed by the court, which makes it an extremely stringent condition to overcome. That is why it is appropriate to consider this form of sale as something analogous to composition or schemes of arrangement, in which, as we shall see below, discharge is available if a certain percentage of creditors has approved the proposals (for composition or schemes of arrangement).

The natural homes of discharge are Articles 1113, 1114 and 1117 of the Code, all of which address the closing of bankruptcy proceedings. If discharge is available under Ethiopian bankruptcy law, it should have been mentioned in one of these provisions.

Article 1113 of the Commercial Code enumerates three grounds for closure of bankruptcy proceedings - distribution of the assets, insufficiency of assets, and absence of claims against the bankrupt debtor. Articles 1114 and 1117 state the consequences of closure of bankruptcy by reasons of the two grounds stated: insufficiency of assets and absence of claims against the bankrupt estate respectively - we are not told as to what happens when the bankruptcy comes to an end (as it often does) upon the distribution of the assets of the bankrupt estate.

Article 1114 puts it in no uncertain terms that where bankruptcy proceedings come to an end by reason of 'insufficiency of assets', the debtor will not be discharged. In fact, the creditors are thenceforward restored to exercising their individual rights and the debtor remains under the 'special incapacities' of bankruptcy.[392] Article 1117 states that the debtor is discharged when there are no more claims against the bankrupt estate. But that is because the debtor has paid all the claims against him. That is a

[392] Commercial Code, supra note 4, see Article 1114(2) &(3).

foregone conclusion even if we did not have Article 1117 of the Code – a debt discharged upon payment is one of the cardinal principles of contract.[393]

Where does that leave us on the question of whether Ethiopian bankruptcy law grants the relief of discharge to bankrupt debtors? The position of Ethiopian bankruptcy law on bankrupt debtors is in general pretty well known. The law attaches blameworthiness to all bankrupt debtors. Its restriction of freedom of movement and attachment of various prohibitions and forfeitures to debtors are abundant evidence of the position of Ethiopian bankruptcy law. Although some provisions seem to hold a promise of discharge (they are accidental slips, it turns out), the truth of the matter is that discharge occurs only if the bankrupt debtor has fully paid all the claims of creditors or creditors have consented to the discharge of the debtor.

IV

5. Composition and Schemes of Arrangement

The primary objective of bankruptcy as liquidation proceeding is to maximize the value of the bankrupt estate and distribute the proceeds among creditors – in other words, to liquidate the business of the bankrupt debtor.[394] Debtors who seek to escape the harsh conditions of straight bankruptcy or liquidation have other options available to them. The purpose of alternative proceedings to bankruptcy is different or should be different from straight bankruptcy or liquidation. It is 'to maximize the possible eventual return to creditors' and 'to preserve viable businesses as a means of preserving jobs for employees and trade for suppliers.[395]

In its inevitability as a procedure for liquidating the business of the debtor and distributing the proceeds among creditors, the results of a bankruptcy may satisfy the interests of some creditors – who may not necessarily be the majority of creditors as such. Creditors are not a homogenous group. Some creditors, such as customers or suppliers, may prefer the continuation of

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[393] See Civil Code, supra note 41, Article 1806, where it is stated 'an obligation shall be extinguished where it is performed in accordance with the contract'.

[394] That is why liquidation is sometimes alternatively used with bankruptcy; see Taddese Lencho, supra note 137, 57, 65-68; French Commercial Code states the objective of liquidation (the equivalent of our bankruptcy) as '...to end the business activity or to sell the debtor's assets through general or separate sale of its interests and property'; see French Commercial Code, supra note 35, Article L640-1.

[395] UNCITRAL, supra note 11, p. 209, para. 3; business rehabilitation is a recent development in bankruptcy theory; see Richard W. Maloy, supra note 98.

business with the debtor to rapid repayment of their debt.[396] Others may prefer quite the opposite. Debtors who find themselves in financial difficulties are as diverse as can be. For some, liquidation may be the only cure, but there are businesses which should be given another lease of life. Alternative procedures to bankruptcy fulfill the need to cater for the diverse needs of creditors as well as debtors - thus maintaining the balance that would have been upset by the dominance of liquidation in the market.

As suggested already, the alternatives to bankruptcy may take many forms: a simple composition (an agreement to pay creditors as a percentage of their claims, usually over time); continued trading of the business and its eventual sale as a going concern (and for the debtor to then be liquidated); transfer of all or part of the assets of the estate to one or more existing businesses or to businesses that will be established; a merger or consolidation of the debtor with one or more other business entities; a sophisticated form of restructuring of debt and equity.[397] As there are multiple alternatives for rehabilitation of businesses, there are multiple names in different legal systems. Indeed, one of the striking features of the alternatives to straight bankruptcy is the bewildering variety of the language used to describe these procedures under various legal systems. In England, they are known by the names 'Administration', 'Company Voluntary Arrangement' and 'Schemes of Arrangement', in the Netherlands by 'Suspension of Payments (Reorganization)' and 'Debt Rescheduling', in Japan by 'Corporate Reorganization' 'Civil Rehabilitation' and 'Company Arrangement'.[398] In the US, the various alternatives available in the US bankruptcy system are better known by their chapters in the US Code - Chapter 7 (which is a straight bankruptcy procedure), Chapter 11 (for reorganization of businesses) Chapter 13 (for Adjustments of Debts).[399] OHADA Uniform Act has two alternative procedures to liquidation; preventive settlement (*regalement preventif)* and legal redress

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[396] UNCITRAL, supra note 11, p. 209, para. 3; see also Richard W. Maloy,supra note 98; as Maloy writes 'supplier creditors prefer it in order to keep alive a good customer' and employees 'to keep their paychecks coming'; see ibid.

[397] UNCITRAL, supra note 11, p. 210, para. 4.

[398] See in general, Goffman and Michael, supra note 321; some countries use the expression 'schemes of arrangement' like Ethiopian law to describe one of the alternatives to bankruptcy - England, Israel, see Ronald J. Silverman, *Israeli Insolvency Law Moves to Encourage Reorganization* 25American Bankruptcy Institute Journal, 18-6, (July/August 1999) and Sandy Shandro, *U.K.'s Chapter 11 Plan: Schemes of Arrangement,* 25American Bankruptcy Institute Journal3 (April 2006).

[399] See Collier's Bankruptcy Manual, supra note 44.

(*redressement judiciaire*).[400] The French Code has an elaborate system for rescuing troubled businesses, even going to the extent of providing for a system to prevent future insolvencies through group insurance.[401] The Guide uses the word 'reorganization' to refer to all the alternatives. The Guide defines reorganization as 'the process by which the financial well-being and viability of a debtor's business can be restored and the business continue to operate, *using various means possibly including debt forgiveness, debt-rescheduling, debt equity conversions and sale of the business (or parts of it)* (italics supplied).[402] In this sense, reorganization embraces simple debt adjustment like composition as well as plans involving serious and fundamental reorganizations or restructuring of the business itself.[403]

The Ethiopian bankruptcy system envisages two forms of settlement for debtors who are either already in bankruptcy or about to go into bankruptcy (imminent bankruptcy): composition and schemes of arrangement.[404]

It is justified to look at the two alternative procedures in bankruptcy under one section - in order not only to sort out the differences but also to examine their similarities and as shall be suggested at the end of this article to press for the merger of the two procedures. Of course we have a definition of neither of the alternative proceedings. We will need to read all the provisions regarding composition and schemes of arrangement in order to understand the nature of these proceedings. Before we conclude, we

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[400] See OHADA, supra note 33, Article 2; Boris Martor et al, supra note 33, at 158.

[401] Under French law, all persons subject to the bankruptcy system may join the so-called 'prevention group,' which provides members with a confidential analysis based on the data supplied to it by these members. The group will notify members of their financial difficulties and recommends experts to be assigned to look into their difficulties. Accredited 'prevention groups' may enter into agreements with credit institutions and insurance companies with a view to preventing financial difficulties; see French Commercial Code, supra note 35, Article L611-1.

[402] UNCITRAL, supra note 11, p. 7.

[403] Some authors draw a fine line between reorganization and mere adjustments of debts. Adjustment of debts schemes 'adjust' or change the amount and/or the time and manner in which debts are paid, while reorganization schemes go deeper than that; see Richard W. Maloy, supra note 98.

[404] Banks have in practice developed the scheme of 'private receivership' in which they place their own employees or consultants inside the debtor's business to manage the financial operations and attempt to restore the debtor to solvency; see USAID, supra note 24, p. 53; the New Banking Business Proclamation has effectively created a receivership scheme for banks in insolvency cases; see Banking Business Proclamation, supra note 39, Articles 32-48; see also Taddese Lencho, supra note 137, at 72-74.

need to sort out the major differences between the two. The following table gives the gist of the differences as well as the similarities:

Table: Comparing Composition with Schemes of Arrangement

No.	Composition	Schemes of Arrangement
1	**Commencement Time** After suspension of payments and upon the expiry of the period under Article 1046 (see Article 1081)	**Commencement Time** Upon imminent suspension of payment or after suspension of payment (see Article 1119)
	Content of Proposal Percentage of payment, period of payment, guarantees, legal costs and remuneration of trustees to be offered in the proposal not specified by law (See Article 1081(2)	**Content of Proposal** The proposal should include an undertaking to pay not less than 50% within one year, or 75% within 18 months, or 100% within three years, with material or personal guarantees or a proposal to assign all assets held by the debtor (see Article 1121).
	Proposal to Whom? Commissioner (see Article 1082)	**Proposal to Whom?** Court (See Article 1119)
	Creditors' Vote 2/3rds of creditors representing 2/3rds of the debts should approve the proposal	**Creditors' Vote** A majority of creditors representing 2/3rds of all non-preferred or unsecured creditors should approve the proposal
	Confirmation by? Court	**Confirmation by?** Court
	Supervision The commissioner, the trustee(s) and the creditors' committee	**Supervision** The commissioner (and to some extent) the delegate judge
	Results of Confirmation by Court Binding on all creditors others than those holding security in rem and unsecured creditors whose claims have arise during the bankruptcy proceedings (post-bankruptcy creditors)	**Results of Confirmation by Court** Binding on all creditors, except secured creditors unless they voted upon giving up their security

Source: Tilahun Teshome and Taddese Lencho (eds.), *Position of the Business Community on the Revision of the Commercial Code of Ethiopia* (Addis Ababa

Chamber of Commerce and Sectoral Associations, PSD Hub Publication No. 8, 2008), at 108-109.[405]

The differences between composition and schemes of arrangement are in the main procedural, not substantive. Composition is a post-bankruptcy procedure while a scheme of arrangement is a pre-bankruptcy or at least contemporaneous procedure. There are also differences in the number of votes required of creditors for approval of each (see table above). But in terms of the contents of the proposals, there are virtually no differences between the two proceedings. They both are about adjustments of debts in absolute amounts or period of payment. In that sense, our conclusion that both are simple debt adjustment schemes was warranted.[406] Indeed, it won't be bold to call 'schemes of arrangement' a composition by another name. Do we need two separate titles in our bankruptcy system for what is at bottom a simple adjustment of debts? This is a question for policy makers, but let's point out what is missing in Ethiopian bankruptcy law in this regard by reference to other bankruptcy laws.

As pointed out before, the Guide adopts a definition that encompasses simple debt adjustment schemes as well as schemes for reorganization of the bankrupt business. It offers creditors as well as debtors a wide variety of options that are acceptable to both. There are times when simple adjustment of debts is not enough, just as liquidation is not an appropriate solution for all bankrupt businesses. There is no better way of conveying the content of reorganization as directly quoting from the Guide:

> Information relating to what is proposed by the plan could include, depending upon the objective of the plan and the circumstances of a particular debtor, details of classes of claims; claims modified or affected under the plan and the treatment to be accorded to each class under the plan; the continuation or rejection of contracts that are not fully executed; the treatment of unexpired leases; measures and arrangements for dealing with the debtor's assets (e.g., transfer, liquidation or retention); the sale or other treatment of encumbered assets; the disclosure and acceptance procedure; the rights of disputed claims to take part in the voting and provisions for

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[405] In our recommendations to the Business Community, we pointed out these differences and concluded that these differences did not warrant having separate titles in the bankruptcy law of Ethiopia; see Tilahun and Taddese, supra note 3, at 104 and 108-109.

[406] See id, at 109.

> disputed claims to be resolved; arrangements concerning personnel of the debtor; remuneration of management of the debtor; financing implementation of the plan; extension of the maturity date or a change in the interest rate or other term of outstanding security interests; the role to be played by the debtor in the implementation of the plan and identification of those to be responsible for future management of the debtor's business; the settlement of claims and how the amount that creditors will receive will be more than they would have received in liquidation; payment of interest on claims; distribution of all or any part of the assets of the estate among those having an interest in those assets; possible changes to the instrument or organic document constituting the debtor (e.g., changes to by-laws or articles of association) or the capital structure of the debtor or merger or consolidation of the debtor with one or more persons; the basis upon which the business will be able to keep trading and can be successfully reorganized; supervision of the implementation of the plan; and the period of implementation of the plan, including in some cases a statutory maximum period. [407]

Under French law a reorganization plan should include not just a request for adjustments of debt but also matters like prospects for employment, replacement of one or more managers, modifications of share capital, and increase or reduction of capital.[408] Similarly, OHADA Uniform Act requires debtors to include in the plan proposals for reorganization of the debtor's business, such as 'replacement of managers', 'economic layoffs', and commitments by shareholders or partners to increase the capital of the business organization, etc.[409]

Detailed plans are required by these other laws for a reason. Creditors to whom these proposals are presented are more likely to be swayed in the debtor's favor when they see credible proposals on the table. Creditors are less likely to vote for a proposal that simply asks them to adjust debts, while being mum (vague) on other aspects of the business. There might be instances where creditors are willing to go along with simple adjustments of debts (for which composition shall remain an option), but in many instances, creditors will need an assurance that the debtor is in a position to pay the debts in their adjusted state. This is where real reorganization of the

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[407] UNCITRAL, supra note 11, p. 215, para. 19.

[408] French Commercial Code, supra note 35, see Articles L626-1 to L626-4.

[409] OHADA, supra note 33, see Articles 6 and 7.

bankrupt business may be demanded by creditors. Ethiopian bankruptcy law does not prevent debtors from presenting detailed plans for reorganization. But there would have been some credence to the two alternatives in Ethiopian law if one of them (particularly the schemes of arrangement) has provisions resembling reorganization elsewhere.

The provisions of bankruptcy law may be as expansive as can be imagined, but it must be remembered that the content of the reorganization plan is not a matter that is entirely left to bankruptcy laws alone. Other laws may impinge on what can be presented for approval by creditors. To give but one example, the inclusion of the proposal to lay off workers on economic grounds is not just a matter of bankruptcy law but also of labor law. Creditors cannot approve of a plan of reorganization that violates the mandatory provisions of the Labor Proclamation.[410]

Whatever the differences might be between composition and schemes of arrangement, they must offer viable alternatives to bankruptcy. What is in it for a debtor to opt for schemes of arrangement in the first place or later a composition? If the two alternatives to straight bankruptcy (liquidation) are no better, there is no incentive for a debtor to propose any one of them.

The proposal of composition has a number of advantages to commend it. First and foremost, the proposal, if accepted, will be binding on all unsecured creditors (including those who dissented or voted against the proposal) and secured creditors who have participated in the votes thus relinquishing their security.[411] Secondly, the proposal of composition suspends (but does not completely terminate) most of the effects of bankruptcy.[412] Restrictions on debtor's movements are lifted; the debtor will resume full control of his property.[413] However, forfeitures and prohibitions, if any, will remain and the debtor although resuming control of his property will conduct his affairs under the supervision of trustees, commissioner and creditors' committee.[414] Besides, acts transacted during composition may not be invalidated unless there has been fraud on the part

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[410] For the interface between bankruptcy law and other laws in this regard, please see UNCITRAL, supra note 11, pp. 215-216, paragraphs 21 and 22.

[411] Secured creditors are not obliged to participate in the votes.

[412] Commercial Code, supra note 4, Article 1090.

[413] Ibid.

[414] Id, Article 1090 (1).

of the creditors[415] - in other words, the bar for suspicion of the acts of the debtor is raised thus giving the debtor greater freedom to transact.

After the confirmation of the composition by the court, the debtor is restored to the management of his property, subject to the now less onerous supervisory controls of the trustees, the commissioner, and the creditors' committee[416]. The supervisory controls are now much attenuated to just ensuring whether the debtor is complying with the detailed instructions contained in the judgment confirming the composition.

The debtor gets to enjoy the positive consequences of the bankruptcy proceedings without having to suffer from the negative ones. A scheme of arrangement suspends the actions of creditors. Creditors may not distrain, acquire a preferred right over the debtor's property or register a mortgage.[417] Prescriptions, preemptions and forfeitures against the debtor are suspended.[418] But most of the negative consequences of bankruptcy do not attach. The debtor who proposes a scheme of arrangement prevents the possibility of losing the management of his property to a trustee.[419] This is incentive enough for debtors to propose the scheme of arrangement rather than face the onerous conditions of a bankruptcy proceeding.

For debtors, a scheme of arrangement presents a more attractive option than a bankruptcy proceeding. But, what about creditors? For creditors, bankruptcy proceedings provide a more secure guarantee and protection than schemes of arrangement - at least this is the case in the immediate aftermath of these proceedings. But all is not lost in the camp of creditors, either. Some of the effects of bankruptcy are replicated in schemes of arrangement. Although the debtor remains in the management of his property, he is subject to supervision of the commissioner and the delegate judge,[420] who may inspect the debtor's books and accounts at any time

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[415] Id, Article 1096.

[416] Id, see Article 1090 (1) together with Article 1088 (1).

[417] Id, see Article 1131(1).

[418] Id, Article 1131(2).

[419] Id, Article 1132.

[420] In a scheme of arrangement, the debtor retains the management of his/her property (one of the perks of a scheme), but the debtor remains under the 'supervision of a commissioner and guidance of a delegate judge'. Unlike bankruptcy proceedings, the procedures for the appointment and other issues like qualifications are not laid down in the provisions dealing with schemes of arrangement. It is not clear if the commissioner in the schemes of arrangement is the same commissioner identified in bankruptcy proceedings. But it appears that the commissioner in schemes of

during the proceedings.[421] Certain acts considered detrimental to the interests of creditors (e.g. gifts and gratuitous acts by the debtor) are not valid against creditors in the schemes of arrangement as well; the only difference being the length of the suspect period is shortened to run from the date the scheme of arrangement is proposed by the debtor.[422] And some acts require the approval of the delegate judge.[423] The delegate judge may not give his approval unless the necessity is clear.[424]

These restrictions apply to the debtor until the scheme is confirmed by court. Even after the scheme is confirmed, however, the debtor will continue to be under some restrictions. For example, the debtor 'may not dispose of or charge his immovable property', encumber his property by pledge or 'set aside any part of his assets otherwise than as required by the nature of his business until he has fully carried out' his duties under the scheme'.[425] The debtor will also continue to be under the supervision of the commissioner.[426] So generally, while the debtor enjoys greater liberty under composition and schemes of arrangement, it must be remembered that his freedom to transact is restricted in both proceedings.[427]

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arrangement has duties similar to that of a trustee in bankruptcy. S/he prepares an inventory of the debtor's estate, checks the list of creditors and debtors and prepares a detailed report on the affairs and conduct of the debtor on the proposed scheme and the guarantees offered to creditors; see Article 1135; compare Article 1135 with Articles 1014 and 1082; the delegate judge in a scheme of arrangement seems to take the position of a commissioner in a bankruptcy proceeding. The delegate judge presides over creditors' meetings in a scheme of arrangement; see Article 1136(1); the commissioner reports to the delegate judge over 'any fact likely to prejudice the creditors'; see Article 1151(2). Apart from these rules, we have no clue whatsoever about from where the commissioner and the delegate judge are selected.

[421] Id, Article 1132.

[422] These acts are compromise, arbitration and assignment not falling within the exercise of the business, mortgages, and pledges; id, see Article 1133.

[423] Id, Article 1133(2).

[424] Id, Article. 1132(2).

[425] Id, Article 1146(1).

[426] Id, Article 1151.

[427] It is perhaps disingenuous to present the rosy aspects of composition and schemes of arrangement and neglect to mention the real hurdles involved in getting either a composition or a scheme of arrangement approved. The two proceedings are filled with more uncertainties than straight bankruptcy proceedings. The debtor is at the mercy of creditors in both proceedings. There is no guarantee that the debtor's proposals will be treated kindly when they are presented for the votes of creditors.

The most important benefit of both composition and schemes of arrangement is they hold out a promise of discharge if they are successfully carried out. The confirmation of the composition is binding upon all creditors save secured creditors who have not participated and post-bankruptcy creditors.[428] Similarly, confirmation of the scheme of arrangement binds 'all creditors prior to the opening of the scheme'.[429] Since discharge is not available under the bankruptcy provisions of Ethiopian law, it is in the best interest of debtors to submit composition or schemes of arrangement plans rather than submit themselves to the harsh consequences of a straight bankruptcy proceeding.

6. Conclusion and Recommendations

Bankruptcy regimes vary in their orientations. Some systems are dubbed creditor friendly while others are dubbed debtor friendly.[430] Some bankruptcy systems set their priorities differently from others. For example, French bankruptcy regime's priorities are described as first saving the enterprise, second preserving jobs and lastly paying creditors.[431] Ethiopian basic codes in general were drafted in a vacuum of overarching public policies. The public policies to be served by the enactment of the codes were if any thing afterthoughts and often came through the speculations of the drafters themselves as to what suited Ethiopia's needs at the time. The first drafter of the Commercial Code acknowledged that he could have prepared five or six laws on bankruptcy (given the options out there) but he settled on the one he produced because 'the conditions of Ethiopia' 'both for the present and the immediate future' demanded a bankruptcy system with 'a theme of severity'.[432] In the choice of paradigms out there, the drafters were making conscious decisions about the direction of bankruptcy laws in Ethiopia. Drafting of bankruptcy law for Ethiopia should be the end product of serious deliberations over the policies and objectives the bankruptcy system should reflect. Once the policies are clearly identified, the details and technicalities can be handled by drafters or drafting commissions. In case there is any doubt over the role and function of

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[428] Commercial Code, supra note 4, see Article 1089(1); it is interesting to note that the confirmation does not affect the creditors' rights against persons jointly and severally liable with the debtor; id, see Article 1089(3).

[429] Id, see Article 1150(1); although the provision just cited says 'all creditors', the scheme, like composition, does not have a binding effect upon secured creditors unless they decided to vote in the scheme; see Article 1140 (2).

[430] Goffman and Michael, supra note 321.

[431] See ibid.

[432] Peter Winship, supra note 23, at 106.

bankruptcy, reference may be made to a growing literature on this subject elsewhere, from which policies appropriate for Ethiopia may be drawn.[433] Some provisions of Ethiopian bankruptcy law may have aged well, but there are some rules or orientations of Ethiopian bankruptcy law which - more than fifty years later - strike us as quaint and archaic. The first drafter of Book V of the Commercial Code acknowledged that he chose 'blameworthiness' to be associated with bankruptcy because that was the weltanschauung of continental legal systems towards bankruptcy at the time.[434] This outlook treated bankruptcy not merely as a simple accident of commercial life but as a blameworthy act, deserving of sanctions against the bankrupt debtor. It is argued in this article that this orientation of Ethiopian bankruptcy law is an orientation whose time has passed and needs to be revisited. The continental legal systems from which Ethiopian bankruptcy law was derived have since then reformed their bankruptcy laws and Ethiopia should follow suit.

Ironically, while the drafters wished to emphasize the punitive aspects of bankruptcy, they appear to have neglected an area which requires punishment- i.e. the apportionment or assignment of punishment to debtors and persons associated with debtors who might have been morally responsible for bringing down bankruptcy upon the business. The Commercial Code, placed along side modern bankruptcy regimes, is striking for its silence on liabilities, disqualifications, prohibitions or personal bankruptcies (whatever we might call them) resulting from moral responsibility for bankruptcy. The modus operandi of the drafting process, which operated on a strict division of labour between civil/commercial matters on the one hand and criminal matters on the other might have contributed to this lacuna in the Commercial Code.[435] There is a need to move away from the presumptuous blameworthiness of the Commercial Code to a regime of assigning punitive consequences to debtors and others that are responsible for the bankruptcy.

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[433] The UNCITRAL Guide cites some nine general objectives of bankruptcy systems: provision of certainty, value maximization, striking a balance between liquidation and reorganization, equitable treatment of similarly situated creditors, timely, efficient and impartial resolution of proceedings, preservation of the bankrupt estate, transparency and predictability, recognition of existing creditors' rights and establishing a framework for cross-border bankruptcy; see UNCITRAL, supra note 11, pp. 10-14, paras. 3-14; see also Elizabeth Warren, *Bankruptcy Policy Making in an Imperfect World*, 92Mich. L. Rev.2 (1993).

[434] See Peter Winship, supra note 23, pp. 100 and 103.

[435] See id at 102.

The first drafter of the Commercial Code, Professor Escarra, designated many rules of Book V of the Commercial Code 'provisional'. For example, Escarra meant Articles 979 and 980, 1055-1080 as provisional articles ultimately to be superseded by the provisions of the Civil Code and the Civil Procedure Code or at least to be re-written in light of the Civil Code and the Civil Procedure Code.[436] There is no evidence that that happened. Escarra also omitted provisions on the effects of bankruptcy on the spouse of the bankrupt because he was uncertain about what the Civil Code would provide for the effects of marriage on the property of the spouses. It is evident that many of the provisions of Ethiopian bankruptcy law were drafted without the benefit of hindsight of the rules of the Ethiopian Civil Code and Ethiopian Civil Procedure Code, among others. It is by no means necessary that the rules of bankruptcy should mirror the rules of the Civil Code or Procedure Code, but this must be a matter of conscious choices rather than random and arbitrary departures or coincidental affinities.

Priority provisions - in particular Article 1110 of the Code - will require some redoing as they do not address cases in which preferred creditors might come into competition with one another. Several Ethiopian laws have since the promulgation of the Commercial Code asserted the priority claims of some creditors (like employees and tax authorities) and these laws perhaps not surprisingly use a very strong language in asserting the priority claims of these creditors. In its current state, Article 1110 of the Commercial Code is indifferent to the strongly-worded priority rights asserted in different laws of Ethiopia. There is reason to believe that even preferred creditors should have ranking among themselves, as can be attested by the new Banking Business Proclamation of 2008. Article 1110 of the Code will need revision along these lines.

The dual organization of the bankruptcy law, with separate title for business organizations, is not helpful at all. There is reason to believe that this form of organization was responsible not only for needless repetition of identical rules, but also for neglect of some rules regarding business organizations. A case in point is the personal effects of bankruptcy upon business organizations. For obvious reasons, the personal effects cannot apply to business organizations as entities, but there is no reason why these cannot take effect upon the representatives of a business organization. Similarly, the rules pertaining to dispossession of the debtor in the event of

[436] Id at 103.

bankruptcy say nothing when the debtor involved is a business organization.

For bankrupt debtors, discharge is the real crown jewel in an otherwise dreary landscape of bankruptcy. But discharge is not really available under Ethiopian bankruptcy law even when the debtor is innocent. The absence of discharge in Ethiopian bankruptcy law may make the bankruptcy system less appealing to debtors. It is important to recognize that traders and businesses fail for any number of reasons, as they succeed for any number of reasons. As the American philosopher Michael Walzer put it, the market does not really recognize desert (see the quote at the beginning of this commentary). Some businesses fail for reasons of their own making and others fail for reasons beyond their control. The extension of discharge to those traders who fail for reasons beyond their control gives them another shot at life by allowing them to start another business with a clean slate. The bankruptcy provisions of the Commercial Code are thus in need of reform in this regard. Whether the conditions for discharge should be stringent or lax is a matter for policy makers to decide.

Ethiopian bankruptcy law offers two alternatives to straight bankruptcy - composition and schemes of arrangements. A close examination of these two schemes has revealed that these two schemes are similar on fundamental matters. They are both at bottom simple debt adjustment schemes. It is argued in this article that while simple adjustment schemes in bankruptcy qualify as 'alternatives' to straight liquidation schemes, it is not necessary to have two schemes for essentially the same end - adjustment of debts. What we need in stead of two simple adjustment schemes is a genuine reorganization scheme, which contemplates the restructuring of the bankrupt business beyond revision of debt payment provisions.

Finally, there is a need to reorient the outlook of Ethiopian bankruptcy system in ways that convey the message that priority is given to rehabilitation or rescuing of the troubled business and liquidation is the last option.[437]

[437] See our recommendations in this regard, in Tilahun and Taddese, supra note 3, at 111.