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Creditor Protection via Insolvency Law Perspectives from Ethiopia: A Critical Analysis

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This study, for the first time, critically examines whether the new Ethiopian insolvency regime protects creditors' interests using six variables identified through a reflexive thematic analysis of interview data. As evident from global best practices and the results of the qualitative analysis, the identified variables used as benchmarks in this study are typical tools to protect creditors' interests in the vicinity of or during insolvency. After a critical doctrinal analysis of the identified variables in Ethiopia in relation to global best practices and a thematic analysis of the interview data, the study found that the new Ethiopian insolvency regime is creditor-friendly. It is well equipped with the tools needed to protect creditors' interests in the vicinity of or during insolvency, with few areas for further improvement. The new law has substantially addressed and improved the deficiencies of the old law, aligning creditor protection rights with relevant global guidelines and best practices. The study further emphasizes that safeguarding creditors' interests is broader than good law, highlighting long-standing deficiencies in the existing insolvency practice and institutional framework. The study concludes that comprehensive protection of creditors' interests during insolvency requires a robust legal framework and an effective institutional framework for its practical implementation, suggesting substantial legislative and institutional reform.

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I. INTRODUCTION

Credit makes the world go round. Individuals and businesses need finance (capital) to operate their daily businesses. Creditors provide capital to businesses, making them a major stakeholder in businesses and the assets of their debtors. While extending a loan, creditors bear a tangible risk of non-payment due to various reasons.[1]

To mitigate or avert such risk and encourage them to continue extending credit, creditors' interests should be protected through various legal mechanisms before or after their debtors face financial difficulties.[2] Such mechanisms aim to control and strengthen the debtors' financial standing to ensure debt repayment. However, these preventive strategies may still fail due to financial distress. In such cases, the law permits the liquidation and distribution of the debtor's assets in favor of creditors as a curative measure.[3]

On the contrary, without such *ex-ante* or *ex-post* protective measures, added to the overwhelming risk of non-payment of their debts,

1. Simon Deakin et al., *Varieties of Creditor Protection: Insolvency Law Reform and Credit Expansion in Developed Market Economies*, 15(2) SOCIO-ECON. REV. 359, 363 (2017).

2. Rainer Haselmann et al., *How Law Affects Lending*, 23(2) REV. FIN. STUD. 549 *passim* (2009).

3. Piotr Staszkiewicz & Sylvia Morawska, *The Efficiency of Bankruptcy Law: Evidence of Creditor Protection in Poland*, 48 EUR. L.J. ECON. 365, 369 (2019).

creditors would abstain from extending loans, which in turn would cripple businesses.[4] Insolvency law is one of the main legal tools used to protect creditors' interests. Unlike other *ex-ante* protective measures applied while the debtor is in good financial status, insolvency is an *ex-post* mechanism used as a last resort to protect creditors' interests once the debtor is unable to pay his debts as they mature.[5]

When the debtor is insolvent or near insolvent, a creditor's risk increases due to both a shift in the debtor's risk-taking and decision-making and debtors' opportunistic behavior to divert value away from creditors through various tactics, leaving creditors exposed as residual risk bearers. Hence, during financial distress, with an increase in creditors' risk, insolvency law must provide direct access and accord stronger protection to creditors to ensure that the debtor's remaining assets are protected and their claims are recovered.[6]

Ethiopia has undertaken nearly a century of insolvency reform since 1933. For over six decades, insolvency in Ethiopia was governed by Book Five of the Commercial Code of 1960. It is evident from the scant existing literature that, over the years, due to long-standing and entrenched problems, the insolvency provisions of the Old Code have remained inadequate, unknown, impractical, outdated, and neglected.[7]

There were very few court cases based upon the Old Code, indicating that it was not adequately used to resolve insolvency disputes. The old law also failed to provide modern rules and principles for effectively regulating insolvency procedures.[8] The deficiencies of the old law have, for many years, devastated the interests of all insolvency stakeholders, including creditors.

To alleviate the entrenched problems, in 2021, following substantial recommendations, the Ethiopian Federal Government amended the insolvency provisions in Book Five of the Old Code, and replaced them

4. Peter O. Mülbert & Max Birke, *Legal Capital—Is There a Case Against the European Legal Capital Rules?*, 3 EUR. BUS. ORG. L. REV. 695, 710 (2002); Peter O. Mülbert, *A Synthetic View of Different Concepts of Creditor Protection—Or: A High-Level Framework for Corporate Creditor Protection* 42 (ECGI Working Paper, Paper No. 60, 2006).

5. Robert A. Haugen & Lemma W. Senbet, *Bankruptcy and Agency Costs: Their Significance to the Theory of Optimal Capital Structure*, 23(1) J. FIN. & QUANT. ANALYSIS 27, 32 (1988).

6. Stijn Claessens & Leora F. Klapper, *Bankruptcy Around the World: Explanations of Its Relative Use*, 7(1) AM. L. ECON. REV. 253, 254 (2005).

7. Tadesse Lencho, *Ethiopian Bankruptcy Law: A Commentary (Part I)*, 22(2) J. ETH. L. 57, 60 (2008).

8. *Commercial Code of Ethiopia*, Articles 968-1170, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

with Book Three of the Commercial Code of Ethiopia 2021.[9] It has been almost five years since the new law came into effect. Therefore, it is pertinent to study the impact of the new law in general and upon creditor protection rights in particular.

Moreover, in Ethiopia, there have been only a handful of studies on insolvency matters in general examining the provisions of the old law.[10] However, the issue of creditor protection remained unexplored, even under the old law. The new insolvency law also remained unstudied.[11] By examining, for the first time, creditor protection under insolvency law in Ethiopia, this Article fills a significant gap in the literature. The study is also the first of its kind to critically examine the new insolvency law in general and creditor protection rights in particular, contributing original value to the existing literature.

Building on adequate empirical and doctrinal legal research demonstrating that insolvency law is a standard mechanism for protecting creditors' interests, this study critically examines whether the new Ethiopian insolvency law effectively protects creditors' interests during insolvency. It also examines whether the new law addresses the deficiencies of the old law in protecting creditor rights and assesses the alignment of these rights with global best practices. By studying the Ethiopian case and comparing it with international best practices, the study offers lessons to be learned and experiences to be shared, thereby contributing to future insolvency legislative reform.

This study contains five parts. Part I introduces the study's research design. Part II reviews the related literature and justifies the need for creditors' protection under insolvency law. It critically reviews the relevant existing empirical and doctrinal legal research. Part III justifies the nexus between the identified variables and creditors' protection during insolvency. Using a qualitative analysis method, Part IV examines whether the new Ethiopian insolvency regime protects creditors' interests. Finally, Part V provides the conclusion and recommendations.

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9. POSITION OF THE BUSINESS COMMUNITY ON THE REVISION OF THE COMMERCIAL CODE OF ETHIOPIA 1-110 (Tilahun Teshome & Taddese Lencho eds., Addis Abba Chamber of Com. and Sectoral Ass'n 2008).

10. Lencho, *supra* note 7, at 59; BACKGROUND DOCUMENTS OF THE ETHIOPIAN COMMERCIAL CODE OF 1960 45-54 (Peter Winship (ed.), Haile Sellassie I University 1974).

11. Samuel M. Biresaw & Mia M. Rahim, *Ethiopia: Insolvency Law: A New Regulatory Regime for Corporate Insolvency*, 35(8) INT'L CO. COM. L. REV. 61, 65 (2024); Samuel Biresaw & Mia Rahim, *The Goals and Theories of the New Ethiopian Insolvency Regime Against Global Benchmarks*, 34(1) INT'L INSOLVENCY REV. 1, 3 (2025).

II. RELEVANT LITERATURE

It is evident from previous empirical research that strong and efficient insolvency laws and practices in a country are a typical tool to protect creditors' interests and stimulate economic development. Various studies throughout the late twentieth century have shown that failure to protect creditors' interests exacerbates agency problems (information asymmetry and conflict of interest by insiders) and discourages creditors from lending, thereby restricting capital markets.[12] Certain studies have also shown that weak creditor rights protection in insolvency is a key source of financial barriers.[13] Similarly, other studies have shown that legal protection of creditors limits the extent of expropriation by corporate insiders.[14] Others demonstrated that during financial distress, insolvency law is a typical tool to protect creditors' interests, which helps reduce the agency costs of debt and increase the size of capital and debt markets.[15]

Studies also showed that during financial distress, insolvency law serves as a useful tool to address the *ex-ante* and *ex-post* inefficient competition between creditors over the debtor's assets by penalizing those at fault.[16] To reduce the agency costs of debt, many countries have enacted

12. Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3(4) J. FIN. ECON. 305, 334-338, 342 (1976); Hayne E. Leland & David H. Pyle, *Informational Asymmetries, Financial Structure, and Financial Intermediation*, 32(2) J. FIN. 371, 371 (1977); Stewart C. Myers & Nicholas S. Majluf, *Corporate Financing and Investment Decisions when Firms Have Information that Investors do not Have*, 13(2) J. FIN. ECON. 187, 196, 207-209 (1984); Elazar Berkovitch & Ronen Israel, *Optimal Bankruptcy Laws Across Different Economic Systems*, 12(2) REV. FIN. STUD. 347, 348, 352-359 (1999).

13. Asli Demirgüç-Kunt & Vojislav Maksimovic, *Law, Finance, and Firm Growth*, 53(6) J. FIN. 2107, 2107 (2002); Jacopo Ponticelli & Leonardo S. Alencar, *Court Enforcement, Bank Loans, and Firm Investment: Evidence from a Bankruptcy Reform in Brazil*, 131(3) Q. J. ECON. 1365, 1366 (2016).

14. ROBERT CHARLES CLARK, CORPORATE LAW 1-50 (Francis A. Allen et al. eds., Wolters Kluwer 1986); Andrei Shleifer & Robert W. Vishny, *A Survey of Corporate Governance*, 52(2) J. FIN. 737, 738 (1997); Frédéric Closset & Daniel Urban, *The Balance of Power Between Creditors and the Firm: Evidence from German Insolvency Law*, 58 J. CORP. FIN. 454, 469 (2019).

15. RAFAEL LA PORTA ET AL., LAW AND FINANCE 27 (Harvard Institute for International Development (HIID), Development Discussion Paper No. 576, 1997); Rafael La Porta et al., *Law and Finance*, 106(6) J. POL. ECON. 1113, 1152 (1998); Rafael La Porta et al., *The Economic Consequences of Legal Origins*, 46(2) J. ECON. LITERATURE 285, 286 (2008); Ross Levine, *The Legal Environment, Banks, and Long-Run Economic Growth*, 30(3) J. MONEY, CREDIT & BANKING 596, 599 (1998); Ross Levine, *Law, Finance, and Economic Growth*, 8 J. FIN. INTERMEDIATION 8, 18 (1999).

16. Philippe Aghion et al., *Improving Bankruptcy Procedure*, 72(3) WASH. U. L. REV. 849, 869 (1994); OLIVER HART, FIRMS, CONTRACTS, AND FINANCIAL STRUCTURE 158-160 (Oxford

laws to better protect creditors, particularly during financial distress. In cases of crisis, regulators utilize insolvency law to shift power from shareholders to creditors, thereby increasing the size of capital and private debt markets.[17] Studies also found that strong creditor protection laws shield creditors from the debtor's opportunistic activities emanating from the abuse of limited liability.[18]

Numerous studies demonstrate that robust and effective creditor protection laws foster the flow of capital, stimulate lending, and promote economic development. One found that stronger creditor protection is associated with higher ratios of private credit to gross domestic product (GDP).[19] Others showed that protecting the property rights of creditors ascertains the flow of capital to firms or stimulates lending.[20] Several studies have also demonstrated that robust and effective laws are crucial for fostering effective capitalist development. Nations with strong laws protecting property rights and enforcing contracts tend to be more developed.[21] Some have found that countries with stronger laws and efficient enforcement mechanisms provide superior protection for creditors. Legal creditor protection is a strong predictor of financial

Univ. Press 1995); OLIVER HART, DIFFERENT APPROACHES TO BANKRUPTCY 1-50 (Nat'l Bureau of Econ. Rsch., Working Paper No. 7921, 2000).

17. Closset & Urban, *supra* note 14, at 454.

18. Samuel Biresaw et al., *Corporate Creditors Protection Rights Worldwide: Towards a Convergence of Strategies*, 25(1) CHI. J. INT'L L. 5, 22 (2024); Mülbert & Birke, *supra* note 4, at 727; Mülbert, *supra* note 4, at 23; THOMAS BACHNER, CREDITOR PROTECTION IN PRIVATE COMPANIES: ANGLO-GERMAN PERSPECTIVES FOR A EUROPEAN LEGAL DISCOURSE 20-27 (Cambridge Univ. Press 2009); WILLIAM T. ALLEN ET AL., COMMENTARIES AND CASES ON THE LAW OF BUSINESS ORGANIZATION 123-167 (Aspen Publ'g, 6th ed. 2021).

19. Simeon Djankov et al., *Private Credit in 129 Countries*, 84(2) J. FIN. ECON. 299, 301 (2007).

20. Sanford J. Grossman & Oliver D. Hart, *One Share-One Vote and the Market for Corporate Control*, 20 J. FIN. ECON. 175, 178 (1988); HART, FIRMS, CONTRACTS, AND FINANCIAL STRUCTURE, *supra* note 16, at 160.

21. CURTIS J. MILHAUPT & KATHARINA PISTOR, LAW & CAPITALISM: WHAT CORPORATE CRISES REVEAL ABOUT LEGAL SYSTEMS AND ECONOMIC DEVELOPMENT AROUND THE WORLD 1-22 (Univ. of Chi. Press 2008); DOUGLASS C. NORTH, INSTITUTIONS, INSTITUTIONAL CHANGE AND ECONOMIC PERFORMANCE 1-70 (James Alt & Douglass North eds., Cambridge Univ. Press 1990); Juan C. Botero et al., *The Regulation of Labor*, 119(4) Q. J. ECON. 1339, 1342-1343 (2004); MAX WEBER, ECONOMY AND SOCIETY 1-50 (Guenther Roth & Claus Wittich eds., Univ. of Cal. Press, 1st ed. 2013); CORPORATE BANKRUPTCY LAW IN CHINA: PRINCIPLES, LIMITATIONS AND OPTIONS FOR REFORM 83-86 (Natalie Mrockova ed., Bloomsbury Publ'g, 1st ed. 2021).

development, as it increases the flow of investments and the availability of external finance to firms.[22]

One such study found that common law countries with stronger and more efficient laws and a judiciary provide stronger creditor protection through insolvency law.[23] Others have shown that financial development promotes economic growth, and legal origin matters for economic development.[24] Previous doctrinal research also confirms that insolvency laws can be used to protect creditors' interests. For instance, one study found that creditor protection rights are converging worldwide, and insolvency law is a common protection strategy employed uniformly in both civil and common law countries.[25] Another found that the effectiveness of creditor protection mostly depends on the design of insolvency systems.[26] Certain scholars have argued that insolvency law provides a compulsory collective system of debt collection destined to protect the collective pre-insolvency property rights and interests of dispersed creditors.[27] Others have argued that the primary goal of insolvency law is to safeguard creditors' collective interests.[28]

The relevant international law-making bodies (such as the United Nations Commission on International Trade Law (UNCITRAL), the

22. Rafael La Porta et al., *Law and Finance*, 106(6) J. POL. ECON. 1113, 1145 (1998); Simeon Djankov et al., *The New Comparative Economics*, 31(4) J. COMPAR. ECON. 595, 597, 610 (2003); Djankov et al., *supra* note 19, at 325.

23. Prabirjit Sarkar & Simon Deakin, *Does Creditor Protection Matter? Legal and Financial Development in Four OECD Countries, 1970-2005* (June 3, 2015), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2613879.

24. Daniel M. Klerman et al., *Legal Origin or Colonial History?*, 3(2) J. LEGAL ANALYSIS 379, 404-405 (2011); Paul G. Mahoney, *The Common Law and Economic Growth: Hayek Might Be Right*, 30(2) J. LEGAL STUD. 503, 516 (2001); Ross Levine, *Financial Development and Economic Growth: Views and Agenda*, 35(2) J. ECON. LITERATURE 688, 691 (1997).

25. Biresaw et al., *supra* note 18, at 55-56; Samuel Biresaw & Mia Rahim, *Theories and Goals of Insolvency in Common Law—A Critical Review*, 25(1) J. BUS. L. 24, 39-42 (2025).

26. Régis Blazy & Nirjhar Nigam, *Corporate Insolvency Procedures in England: The Uneasy Case for Liquidations*, 47 EUR. J. L. ECON. 89, 90 (2019).

27. Thomas H. Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain*, 91(5) YALE L. J. 857, 861-62 (1982); THOMAS H. JACKSON, THE LOGIC AND THE LIMITS OF BANKRUPTCY LAW 1-30 (Harv. Univ. Press 1986); Donald R. Korobkin, *Rehabilitating Values: A Jurisprudence of Bankruptcy*, 91(4) COLUM. L. REV. 717, 718 (1991); Donald R. Korobkin, *The Role of Normative Theory in Bankruptcy Debates*, 82 IOWA L. REV. 75, 113 (1996).

28. Douglas G. Baird & Thomas H. Jackson, *Corporate Reorganizations and the Treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors in Bankruptcy*, 51(1) U. CHI. L. REV. 97, 101, 129 (1984); Douglas G. Baird, *Loss Distribution, Forum Shopping, and Bankruptcy: A Reply to Warren*, 54 U. CHI. L. REV. 815, 822 (1987); Alan Schwartz, *Bankruptcy Workouts and Debt Contracts*, 36(1) J. L. ECON. 595, 613-614 (1993).

International Bank for Reconstruction and Development (IBRD), the European Bank for Reconstruction and Development (EBRD), the International Monetary Fund (IMF), and INSOL) and national task forces (such as the Cork and Harmer Committees in the UK and Australia, respectively) have also recognized and endorsed the importance and application of insolvency law in protecting creditors' interests and promoting a country's economic development.[29]

III. JUSTIFYING THE NEXUS BETWEEN THE VARIABLES AND CREDITOR PROTECTION

In the previous Part, based on existing empirical and doctrinal research, this Article has introduced how insolvency law can be used as a tool to protect creditors' interests.[30] Based on qualitative analysis of interview data and the requirements of relevant international guidelines and best practices, this Article has identified six main variables (themes), and used them to evaluate whether the new Ethiopian insolvency law provides adequate protection for creditors' interests during insolvency or in the vicinity of insolvency.

In this subpart, drawing on international guidelines and best practices, this Article explains why the six identified variables are crucial tools for protecting creditors' interests in the vicinity of or during insolvency, and explains the relevance of each variable to creditors' protection.

29. U.N. COMM'N ON INT'L TRADE L. [UNCITRAL], LEGISLATIVE GUIDE ON INSOLVENCY LAW, at 18, U.N. Sales No. E.05.V.10 (2005); World Bank Group [WBG], *Principles for Effective Insolvency and Creditor/Debtor Regimes*, at 2, (2021), https://openknowledge.worldbank.org/server/api/core/bitstreams/3824fe8e-edb3-5f9b-aa28-f5afc759e562/content; IMF, *Orderly & Effective Insolvency Procedures: Key Issues*, 13 (1999); World Bank Group [WBG], *Principles for Effective Insolvency and Creditor Rights Systems*, at 2, (Dec. 21, 2005), https://documents1.worldbank.org/curated/en/191201468315535668/pdf/481660WP0FINAL10Box338887B01PUBLIC1.pdf; European Bank of Reconstruction and Development [EBRD], *EBRD Core Principles of an Effective Insolvency System*, at 4 (2021); INSOL Int'l, *Statement of Principles for a Global Approach to Multi-Creditor Workouts*, (Oct. 2000), https://www.iiiglobal.org/file.cfm/159/docs/insol_principles.pdf; INSOLVENCY LAW REVIEW COMMITTEE & DEPARTMENT OF TRADE, INSOLVENCY LAW AND PRACTICE: REPORT OF THE REVIEW COMMITTEE, 1982, Cm. 8558, at 54 (UK); Australian Law Reform Commission, *General Insolvency Inquiry*, at 2 (Report No 45, 1988).

30. *See* discussion *supra* Part I.

A. Directors' Duties During Insolvency

Corporate governance frameworks mainly regulate the relationships between a company's management and its owners. These frameworks ensure that directors and management pursue objectives beneficial to the company and its creditors.[31] According to international best practices, the insolvency provisions addressing directors' duties are crucial legal strategies to protect the legitimate interests of creditors, to ensure that those responsible for making decisions concerning the management of a company are informed of their roles and responsibilities in those circumstances, and to provide appropriate remedies for breach of those obligations, which may be enforced after insolvency procedures have commenced.[32]

Directors' duties become more critical when a company faces insolvency, as their responsibilities shift from prioritizing shareholders to protecting creditors' interests. The imposition of specific duties on directors during or in the likelihood of insolvency plays a crucial role in preventing reckless mismanagement, protecting creditor rights, and ensuring fair distribution of assets.[33] The existence of imminent insolvency or actual insolvency incentivizes corporate insiders (e.g. shareholders and directors) to engage in various forms of opportunistic behavior aimed at shifting or diluting value away from creditors or transferring risk to them.[34]

Hence, the imposition of special duties on directors towards creditors in the zone of insolvency is one of the strategies used by nations to curb the opportunistic behaviors of debtors which led to the abuse of the privilege of limited liability, thereby protecting the interests of capital providers (lenders) and stimulating lending.[35] Unlike solvency, where

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31. U.N. COMM'N ON INT'L TRADE L. [UNCITRAL], LEGISLATIVE GUIDE ON PUBLIC-PRIVATE PARTNERSHIPS, at 135, U.N. Sales No. E.20.V.2 (2020); CHARLES WILD & STUART WEINSTEIN, SMITH & KEENAN'S COMPANY LAW 286-312 (Pearson Educ. Ltd., 14th ed. 2009); UNCITRAL, *supra* note 29, at 163.

32. WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 19; EBRD, *supra* note 29, at 10; UNCITRAL, *supra* note 31, at 135-142.

33. Salomon v. A Salomon & Co. Ltd. [1896] UKHL 1, [1897] 4 AC 446, 448 (UK); MICHAEL MURRAY & JASON HARRIS, KEAY'S INSOLVENCY: PERSONAL AND CORPORATE LAW AND PRACTICE 626-56 (Thomson Reuters, 10th ed. 2018); ROBERT P. AUSTIN & IAN M. RAMSAY, FORD, AUSTIN AND RAMSAY'S PRINCIPLES OF CORPORATIONS LAW 240, 246 (LexisNexis, 17th ed. 2018).

34. SUSAN MCLAUGHLIN, UNLOCKING COMPANY LAW 269 (Routledge, 2d ed. 2013); Biresaw et al., *supra* note 18, at 20.

35. BACHNER, *supra* note 18, at 235; ALLEN ET AL., *supra* note 18, at 123-67; Tourprint International Pty Ltd (in liq.) v. Bott (1999) 32 ACSR 201, 215 (Austl.); Woodgate v Davis (2002) 42 ACSR 286, 294 (Austl.).

shareholders are the residual risk bearers (claimants) of the company's decisions, the directors owe fiduciary duties only to shareholders and the company, not to creditors. During insolvency, more protection (powers) should be accorded to creditors because, in addition to limited liability, the insufficiency of the debtor's assets to pay its obligations shifts the risk of bearing the residual risks of the debtor's business emanating from insiders' managerial decisions from the shareholders to creditors. This encourages the debtor to abuse the situation by making illicit corporate decisions, thereby forcing the creditor to bear the economic risks (losses) from those decisions due to the misalignment of incentives between decision-making and liability.[36]

Only during formal insolvency do the creditors exercise power and participate in decision-making regarding the debtor's assets. Due to the shift in risk-taking, the law removes the debtor or directors from administering the insolvent assets, reinstating the alignment between risk-taking and decision-making.[37] However, in the vicinity of insolvency, adequate protections should be given to creditors to protect them from the debtor's opportunistic behaviors by imposing various special duties on directors to initiate insolvency procedures, to recapitalize or liquidate the company, to consider creditors' interests, to prevent the company from incurring new debts, and to maximize the value of the firm.[38]

When a company is solvent, directors primarily focus on maximizing shareholder value. As a company approaches insolvency, its

36. Woodgate v. Davis (2002) 42 ACSR 286, 293 (Austl.); Bilta (UK) Ltd (in liq.) v. Nazir (No. 2) [2015] UKSC 23, [2016] AC 1, 8; Liquidator of West Mercia Safetywear Ltd v. Dodd [1988] 4 BCC 30, 31 (UK); Yukong Lines Ltd of Korea v. Rendsburg Investments Corporation [1998] 2 BCLC 485, 485 (UK); Stone & Rolls Ltd (In Liquidation) v. Moore Stephens (A Firm) [2009] UKHL 39, 67.

37. VANESSA FINCH, CORPORATE INSOLVENCY LAW: PERSPECTIVES AND PRINCIPLES 80-90 (2d ed. 2009); DAONING ZHANG, INSOLVENCY LAW AND MULTINATIONAL GROUPS: THEORIES, SOLUTIONS AND RECOMMENDATIONS FOR BUSINESS FAILURE 165, 166-67 (Routledge, 1st ed. 2021).

38. INSOLVENCY LAW REVIEW COMMITTEE & DEPARTMENT OF TRADE, *supra* note 29, at 400; Directive 2019/1023 of the European Parliament and of the Council of 20 June 2019 on Preventive Restructuring Frameworks, on Discharge of Debt and Disqualifications, and on Measures to Increase the Efficiency of Procedures Concerning Restructuring, Insolvency and Discharge of Debt, and Amending Directive (EU) 2017/1132 (Directive on Restructuring and Insolvency), art. 19, 2019 O.J. (L 172) 18, 37; *Corporations Act 2001* (Cth) s 588G (Austl.); Elliott v. Austl Sec's & Inv's Comm'n (2004) 205 ALR 594 (Austl.); James v. Andrews [2001] NSWSC 1149 (Austl.); In the matter of Swan Services Pty Ltd (in liq.) [2016] NSWSC 1724 (Austl.); Austl. Sec's & Inv's Comm'n v. Plymin (2003) 46 ACSR 126, 243 (Austl.); UNIF. VOIDABLE TRANSACTIONS ACT §§ 4(a)(1)-(2), 5(a)-(b) (2014); UNIF. FRAUDULENT TRANSFER ACT § 4(a)(1) (1984); 11 U.S.C. § 548 (2018).

financial stability deteriorates, and the risk of creditor losses increases. Consequently, corporate governance frameworks worldwide impose duties on directors to act in a manner which minimizes harm to creditors.[39] In many jurisdictions, insolvency laws recognize that directors' obligations shift once insolvency is imminent. These laws aim to prevent mismanagement, fraud, and the unfair disposal of assets that could worsen the financial situation. By prioritizing creditor protection, directors are deterred from taking excessive risks that may benefit shareholders at the expense of creditors. Imposing these duties fosters a structured and predictable approach to managing financial distress, ensuring transparency and accountability in decision-making.[40]

According to UNCITRAL, imposing duties on directors when insolvency is imminent or unavoidable is a typical tool to protect the legitimate interests of creditors and other stakeholders. This ensures that those responsible for making decisions concerning the management of a company are informed of their roles and responsibilities in those circumstances and provides appropriate remedies for breach of those obligations, which may be enforced after insolvency procedures have commenced.[41]

B. Creditors' Participation and Information Rights During Insolvency

Insolvency procedures are crucial legal mechanisms that ensure the orderly resolution of financial distress for businesses and individuals. At the core of these procedures are creditors, who include companies or individuals to whom the insolvent debtor owes money. The participation of creditors in insolvency procedures is fundamental not only to ensuring that their financial interests are safeguarded but also to promoting transparency, efficiency, and fairness within the legal framework governing insolvency.[42]

According to international best practices, the provisions on participation and information rights of creditors in insolvency procedures

39. Philip Gavin, *A Rejection of Absolutist Duties as a Barrier to Creditor Protection: Facilitating Directorial Decisiveness Surrounding Insolvency Through the Business Judgment Rule*, 15(2) BROOK. J. CORP. FIN. & COM. L. 313, 325 (2021).

40. Aurelio Gurrea-Martínez, *Towards an Optimal Model of Directors' Duties in the Zone of Insolvency: An Economic and Comparative Approach*, 21(2) J. CORP. L. STUD. 365, 386 (2021).

41. UNCITRAL, *supra* note 31, at 70; Andrew Keay, Company Directors' Responsibilities to Creditors 8-12, 221-25 (Routledge, 1st ed. 2007).

42. IMF, *supra* note 29, at 6.

are crucial legal mechanisms to facilitate the involvement of creditors, to provide a mechanism for the appointment of a creditor committee or other creditor representative where to do so would encourage the participation of creditors in the insolvency procedures, to ensure the right of creditors to access information on the insolvency procedures, and to specify the functions and responsibilities of the creditor committee or other representative.[43]

Moreover, the insolvency provisions that recognize creditors' rights to be heard, to review, and to appeal decisions are crucial to ensure that creditors have a right to be heard and to seek relief from the court when their rights, interests in assets, or duties under the insolvency law are affected. Further, it establishes procedures for providing relief and for appellate review.[44] Creditors play a pivotal role in insolvency procedures because they are the primary financial stakeholders affected by the outcome. Their participation is justified based on several interrelated reasons.[45]

A robust insolvency framework must be transparent and predictable to promote confidence among lenders and investors. Predictability allows creditors to assess their risks and make informed decisions before lending. Unpredictability in the application of insolvency laws can deter lending and investment, as creditors may fear that their rights will not be upheld fairly. A transparent system ensures that creditors understand their position and can take proactive measures to protect their interests.[46]

The participation of creditors ensures that their interests are considered in decision-making processes, particularly during liquidation or rehabilitation. Unsecured creditors, who have no collateral backing their claims, are especially vulnerable and may have limited recourse if excluded from insolvency procedures. Active participation enables creditors to advocate for solutions that maximize asset recovery and ensure the equitable treatment of all parties involved.[47]

Insolvency law should include incentives to gather and disseminate information, ensuring a transparent and predictable system.[48] Transparency is closely related to the objectives of predictability and

43. *Id.* at 88; UNCITRAL, *supra* note 29, at 16-19; WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 24.

44. UNCITRAL, *supra* note 29, at 206.

45. *Id.* at 171.

46. *Id.* at 59.

47. *Id.* at 203.

48. *Id.* at 14.

equity. During insolvency procedures, creditors must be provided with sufficient information to exercise and defend their rights under the law, thereby avoiding information asymmetry and enabling them to make informed decisions.[49] In the absence of transparency or disclosure, creditors will be constrained from meaningfully participating in insolvency proceedings to claim their rights and to approve or oppose essential activities that affect their interests.

Unsecured creditors often face challenges coordinating their actions due to the dispersion of claims and the associated participation costs. If each creditor expects others to act, then none may, leading to the collective action problem and unrepresented creditor interests. Formal mechanisms, such as creditor committees, help resolve these collective action problems by providing a unified voice for creditors.[50] Creditors serve as a check on the insolvency representatives, administrators, or trustees who manage insolvency procedures. Their participation helps prevent mismanagement, fraud, and conflicts of interest. By monitoring insolvency practitioners' actions, creditors can ensure that procedures are conducted fairly and efficiently.[51]

As discussed above, given the merits of creditors' participation, insolvency laws across jurisdictions recognize creditors' participation rights in insolvency procedures. In many countries, insolvency laws recognize creditors' committees as a key mechanism for representation, particularly in insolvency cases involving many creditors.[52] For example, creditors' committees play a crucial role in ensuring creditors' participation in insolvency procedures and in enabling them to exercise their rights to information. They provide advisory roles, facilitate decision-making, and negotiate on behalf of creditors with other stakeholders.[53]

In many nations, insolvency laws often grant creditors' committees the authority to approve key decisions, such as asset sales and

49. IMF, *supra* note 29, at 6.

50. UNCITRAL, *supra* note 29, at 136.

51. Susan Block-Lieb et al., *Representing the Interests of Unsecured Creditors: A Comparative Look at UNCITRAL's Legislative Guide on Insolvency Law, in* INTERNATIONAL INSOLVENCY LAW: REFORMS AND CHALLENGES 3-4 (P.J. Omar ed., 2009).

52. Kenneth N. Klee & K. J. Shaffer, *Creditors' Committees Under Chapter 11 of the Bankruptcy Code*, 44(4) S. C. L. REV. 995, 1011 (1993).

53. Carl A. Eklund & Lynn W. Roberts, *The Problem with Creditors' Committees in Chapter 11: How to Manage the Inherent Conflicts Without Loss of Function*, 5 AM. BANKR. INST. L. REV. 129, 138-43 (1997); Greg M. Zipes & Lisa L. Lambert, *Creditors' Committee Formation Dynamics: Issues in the Real World*, 77 AM. BANKR. L.J. 229, 244 (2003).

restructuring and reorganization plans, to recommend or request action from the court, and to oversee the conduct of insolvency representatives to prevent abuse or high administrative costs.[54] The relevant international lawmaking bodies, such as UNCITRAL and the World Bank, have emphasized the importance of creditor participation during insolvency by recommending national insolvency laws to recognize and enforce creditor committees to enhance participation; to clarify the appointment, role, and responsibilities of these committees and the organs responsible for administering the insolvency; and to ensure that creditors can vote on major decisions affecting their interests.[55]

On the other hand, guaranteeing creditors' information rights during insolvency also has many advantages. For example, effective participation in insolvency procedures depends on the timely and accurate availability of information. Protecting creditors' rights to information is crucial for maintaining confidence in the insolvency process and ensuring informed decision-making.[56]

C. The Protection of the Debtor's Assets During Insolvency

Preserving and maximizing the debtor's assets are central to the efficacy of insolvency procedures.[57] The rationale behind preserving a debtor's assets during insolvency is rooted in economic efficiency, fairness, and the legal principle of maximizing value for creditors.[58] Without proper mechanisms to safeguard the debtor's assets, creditors risk receiving minimal or no compensation for their claims, leading to financial losses and systemic instability.[59] According to international best practices, the insolvency provisions on the protection and preservation of the estate are crucial legal strategies for establishing measures to ensure that the value of the estate is not diminished by the actions of the debtor, creditors, or third parties, to determine the scope of those measures and the actions and parties to which they apply; to establish the method, time,

54. Roman Tomasic, *Creditor Participation in Insolvency Proceedings*, *in* ASIAN INSOLVENCY SYSTEMS: CLOSING THE IMPLEMENTATION GAP 209, 215 (OECD, 2007).

55. IMF, *supra* note 29, at 76-77.

56. WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 11.

57. Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain*, *supra* note 27, at 864; Tomasic, *supra* note 54.

58. UNCITRAL, *supra* note 29, at 11.

59. Elizabeth Warren, *Bankruptcy Policy*, 54(3) U. CHI. L. REV. 775, 788 (1987).

and duration of application of those measures; and to establish the grounds for relief from those measures.[60]

Preserving debtors' assets impacts creditors' interests during insolvency in various ways. One of the primary motivations for protecting a debtor's assets is to ensure that creditors receive the highest possible return on their claims. The value of a debtor's assets also significantly influences the type of insolvency procedures applied. If the assets are preserved effectively, the debtor's business may continue as a going concern rather than be subjected to piecemeal liquidation. A going concern sale often yields a higher recovery for creditors than a sale of individual assets in distress. This approach aligns with the principle that assets should be deployed to maximize value for the holders of rights in them.[61]

Similarly, in the absence of measures to preserve the debtor's assets, individual creditors may rush to enforce their claims, leading to a chaotic and inefficient process. This fragmented approach often results in the rapid depletion of the debtor's estate, reducing the overall value available for distribution.[62] A collective insolvency procedure mitigates these risks by consolidating creditor claims into a single process, thereby preserving asset value and ensuring an orderly distribution. Additionally, it reduces the strategic costs of litigation and enforcement actions, ultimately benefiting creditors collectively.[63]

Insolvency laws seek to prevent fraudulent or opportunistic behavior by debtors and creditors. Without adequate asset preservation measures, debtors may dissipate assets before insolvency proceedings commence, reducing the value available to creditors.[64] Some creditors might attempt to gain an unfair advantage over others by securing claims through preferential transactions. In this regard, as experience shows, the

60. IMF, *supra* note 29, at 70; EBRD, *supra* note 29, at 9; WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 23; WBG, *Principles for Effective Insolvency and Creditor Rights Systems*, *supra* note 29, at 15-17; UNCITRAL, *supra* note 29, at 99.

61. BOB WESSELS ET AL., INTERNATIONAL COOPERATION IN BANKRUPTCY AND INSOLVENCY MATTERS 1-20 (Oxford Univ. Press 2009); Mathias M. Siems et al., *The Protection of Creditors of a European Private Company (SPE)*, 12 EUR. BUS. ORG. L. REV. 147, 154 (2011).

62. Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain*, *supra* note 27, at 865.

63. Baird & Jackson, *supra* note 28, at 101.

64. JINGCHEN XU, MARITIME CROSS-BORDER INSOLVENCY UNDER THE UNCITRAL MODEL LAW REGIME: COMMONWEALTH AND US PERSPECTIVES 9-15 (Hart Publ'g 2020); Lee Suet Lin Joyce, *Is Singapore's Insolvency Regime Excessively Pro-Creditor?*, 12(1) INT'L INSOLVENCY REV. 37, 52 (2003).

imposition of a stay on creditor actions (claims) and the appointment of an independent liquidator prevent such actions, ensuring a fair process for all stakeholders.[65]

An effective insolvency system also ensures impartiality and efficiency in maximizing value by appointing independent and professional representatives to oversee the debtor's asset management. The insolvency administrators assume control over the debtor's estate, preventing mismanagement and unauthorized transfers. Centralizing control under a neutral and professional authority fosters confidence among creditors, preserves value, and enhances the potential for asset recovery.[66]

Removing the debtor's control over the estate and appointing a neutral administrator helps prevent asset dissipation, value dilution, and the debtor's misbehavior. This measure safeguards creditor interests by ensuring that professionals administer the estate and that assets are used solely for lawful insolvency purposes.[67] As discussed above, having considered the advantages of preserving or maximizing the debtor's assets during insolvency in protecting the interests of creditors and other stakeholders, nations have recognized and applied various strategies in their insolvency laws.

For example, a typical strategy in insolvency law to preserve the debtor's assets is the imposition of an automatic stay on creditor actions. This stay of claims prevents creditors from unilaterally seizing or liquidating the debtor's assets, which could disrupt business operations and diminish the value of the insolvent estate. The stay also grants the insolvency representative sufficient time to assess the debtor's financial status, explore reorganization options, and implement strategies to maximize asset value. Additionally, creditor actions against the estate are stayed, reinforcing the collective nature of insolvency proceedings.[68]

In cases where the debtor's insolvency is imminent or during the suspect period, to preserve the debtor's assets and further protect creditors' interests, nations often include claw-back provisions in their insolvency laws, which allow the liquidator to recover assets that were wrongfully transferred before the commencement of procedures. These provisions target transactions that unfairly deplete the debtor's estate, such as fraudulent conveyances and preferential payments made to select

65. UNCITRAL, *supra* note 29, at 90, 145.
66. *Id.* at 31.
67. *Id.* at 136.
68. *Id.* at 83.

creditors. The law maximizes the debtor's assets by recapturing these assets, resulting in a more equitable distribution among all creditors.[69]

D. Secured Creditors' Protection During Insolvency

One of the fundamental concerns of insolvency law is to determine how secured creditors are treated when a debtor fails to meet its obligations.[70] Compared to other creditors, secured creditors hold a distinct position due to their security interests in collateral.[71] Insolvency law often prioritizes secured creditors over unsecured creditors—a practice with profound economic, legal, and financial implications.[72]

Based on international best practice, the rights of secured creditors and the priorities of claims established before insolvency procedures under commercial or other applicable rules should be protected. The differing rights that creditors have concerning the debtor's assets before the commencement of the proceedings should be protected. In particular, the rights and priorities of secured creditors, as well as transparent rules for ranking the priorities of existing and post-commencement creditor claims, should be outlined.[73]

Similarly, according to international best practice, the insolvency provisions regarding the treatment of pre-insolvency and ongoing contracts during insolvency are typical legal strategies to protect the interests of secured and other creditors.[74] Accordingly, by using the provisions on the treatment of pre-insolvency rights and ongoing contracts, insolvency law administers ongoing contracts under which both the debtor and its counterparty have not yet fully performed their respective obligations, including the relationship between the insolvency law and other applicable laws. This serves to maximize the value and reduce the liabilities of the estate, define the scope of the powers to deal

69. IMF, *supra* note 29, at 27; JANIS SARRA, CREDITOR RIGHTS AND THE PUBLIC INTEREST: RESTRUCTURING INSOLVENT CORPORATIONS 252-53 (Univ. of Toronto Press 2003).

70. MURRAY & HARRIS, *supra* note 33, at 1-44.

71. Rizwaan Jameel Mokal, *What Liquidation Does for Secured Creditors, and What It Does for You*, 71(5) MOD. L. REV. 699, 732 (2008).

72. WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 26.

73. *Id.* at 6; WBG, *Principles for Effective Insolvency and Creditor Rights Systems*, *supra* note 29, at 19; EBRD, *supra* note 29, at 4; IMF, *supra* note 29, at 78; UNCITRAL, *supra* note 29, at 13-14.

74. UNCITRAL, *supra* note 29, at 87, 120; WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 25; WBG, *Principles for Effective Insolvency and Creditor Rights Systems*, *supra* note 29, at 17-18; IMF, *supra* note 29, at 88.

with these contracts and the situations in which and by whom these powers may be exercised, identify the types of contracts that should be excepted from the exercise of these powers, and identify the kinds of protection that will be available to counterparties to continuing contracts.[75]

The rationale for prioritizing and protecting secured creditors stems from the necessity to uphold commercial predictability, encourage credit provision, and maintain economic stability.[76] Insolvency law generally upholds the rights of secured creditors, ensuring that their claims take precedence over those of unsecured creditors during insolvency proceedings. This protection is grounded in several key legal principles.[77] Some argue that corporate insolvency law must recognize rights accrued under general law before liquidation. Security interests and real rights created before insolvency should remain unaffected by liquidation procedures. This principle ensures that legal agreements between debtors and creditors are honored, maintaining the integrity of commercial transactions.[78]

The creditor bargain theory, as developed by Thomas Jackson, advocates that insolvency law should respect the priority rights of secured creditors. These creditors enter into agreements based on the expectation that their claims will be prioritized in case of insolvency. Upholding these agreements preserves the legitimate expectations of creditors and fosters confidence in lending relationships.[79] While insolvency law operates on the principle of *pari passu* (equitable treatment of creditors), secured creditors are often exempt from this rule because they hold a legal claim over specific assets. Courts generally recognize that secured creditors should have a superior claim over encumbered assets, as the assets were pledged to them before insolvency.[80]

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75. WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 35; WBG, *Principles for Effective Insolvency and Creditor Rights Systems*, *supra* note 29, at 19; IMF, *supra* note 39, at 88; UNCITRAL, *supra* note 29, at 132.

76. Lucian Arye Bebchuk & Jesse M. Fried, *The Uneasy Case for the Priority of Secured Claims in Bankruptcy*, 105 YALE L.J. 857, 861 (1996).

77. Baird & Jackson, *supra* note 28, at 129-30.

78. ROY M. GOODE, PRINCIPLES OF CORPORATE INSOLVENCY LAW 1-10 (Robert Stevens ed., Sweet & Maxwell, 4th ed. 2011); Anto Kasak, *Is Full Preference for a Secured Claim in Insolvency Proceedings Justified?*, 28 JURIDICA INT'L 112, 116-17 (2019).

79. Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain*, *supra* note 27, at 871, 899; JACKSON, THE LOGIC AND LIMITS OF BANKRUPTCY LAW, *supra* note 27, at 1-50.

80. Randal C. Picker, *Security Interests, Misbehavior, and Common Pools*, 59 U. CHI. L. REV. 645, 670 (1992).

On the other hand, prioritizing secured creditors is not just a legal necessity but also an economic imperative. The economic rationale for this priority includes promoting credit availability, mitigating lending risks, and enhancing financial stability.[81] Credit is the lifeblood of modern economies, and secured lending plays a crucial role in facilitating economic growth.[82] The World Bank asserts that capital and credit are fundamental to a well-functioning market economy.[83] Secured lending enables businesses to access financing at lower interest rates because lenders are assured of collateral as recourse in the event of default.[84] Otherwise, financial institutions would be reluctant to extend credit without strong protections for secured creditors, constraining credit provision and economic development.[85]

The availability of secured credit helps mitigate lending risks.[86] Security interests reduce the likelihood of borrower misbehavior, such as asset dilution or excessive risk-taking.[87] Secured transactions lower the cost of credit by providing lenders with a form of protection against default.[88] When secured creditors are assured of their rights, they can offer more favorable loan terms, which benefits both businesses and consumers.[89]

E. The Use of Optional Insolvency Procedures

Insolvency occurs when a debtor is unable to meet their financial obligations. International best practices indicate that handling a debtor's insolvency involves two central legal mechanisms: rehabilitation

81. REINHARD BORK, PRINCIPLES OF CROSS-BORDER INSOLVENCY LAW 170-75 (Intersentia Ltd. 2017).

82. INSOLVENCY LAW REVIEW COMMITTEE & DEPARTMENT OF TRADE, *supra* note 29, at 10; Axel Krohn, *Rethinking Priority: The Dawn of the Relative Priority Rule and the New "Best Interests of Creditors" Test in the European Union*, 30(1) INT'L INSOLVENCY REV. 75, 86 (2020).

83. PHILIP R. WOOD, PRINCIPLES OF INTERNATIONAL INSOLVENCY 356 (Sweet & Maxwell, 2nd ed. 2007).

84. IAN FLETCHER, THE LAW OF INSOLVENCY 1-15 (Sweet & Maxwell, 4th ed. 2009).

85. ROY GOODE, GOODE ON LEGAL PROBLEMS OF CREDIT AND SECURITY 1-10 (Louise Gullifer ed., Sweet and Maxwell, 5th ed. 2013).

86. FINCH, *supra* note 37, at 725; Saul Levmore & Hideki Kanda, *Explaining Creditor Priorities*, 80 VA. L. REV. 2103, 2104 (1994).

87. SECURITY RIGHTS AND THE EUROPEAN INSOLVENCY REGULATION 10-29 (Gerard Mccormack & Reinhard Bork eds., Intersentia Ltd. 2017).

88. FINCH, *supra* note 37, at 105; E.A. Webber, *The Tension Between Bankruptcy and Secured Credit: A High-Level Overview of a Long-Standing Debate*, *in* THE CHALLENGES OF INSOLVENCY LAW REFORM IN THE 21ST CENTURY 83-97 (H. Peter et al. eds., 2006).

89. ELIZABETH WARREN, CHAPTER 11: REORGANIZING AMERICAN BUSINESS 40-50 (Wolters Kluwer 2008).

(reorganization) and liquidation procedures. Based on international best practices, depending on the circumstances, providing creditors (involved parties) with the option to settle their affairs with the debtor through reorganization and liquidation procedures within a legal system is a typical legal strategy to protect creditors' interests during insolvency.[90]

The combined use of the above strategies, tailored to the debtor's business situation, provides creditors and other involved parties with options to resolve the debtor's insolvency efficiently, promptly, and in an orderly and equitable manner. The combined use of different procedures also ensures the holistic protection of creditors' interests before, during, or after the debtor's insolvency through the instruments of preventive restructuring, reorganization, and liquidation, respectively.[91]

Both procedures are designed to ensure an orderly resolution of debts while balancing the rights of creditors and debtors. Recognizing and enforcing rehabilitation and liquidation procedures in a country provides essential protection for creditors, ensuring that their financial interests are safeguarded during insolvency procedures.[92] This subpart examines international best practices, the justification for these mechanisms, and their role in securing creditors' interests. It discusses the roles of rehabilitation and liquidation in safeguarding creditors' interests. It also generally compares the benefits of using both procedures in a legal system to protect creditors' interests during insolvency.

In accordance with international best practices, rehabilitation or reorganization procedures are designed to enable insolvent entities to continue operating while restructuring their debts. The following are the key roles of rehabilitation procedures in protecting creditors' interests during insolvency.[93] As their name indicates, rehabilitation procedures are a typical tool to maximize or preserve the value of the debtor's assets.

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90. *See* EBRD, *supra* note 29, at 6; WBG, *Principles for Effective Insolvency and Creditor Rights Systems*, *supra* note 29, at 6; WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 21; INSOL International, *supra* note 29, at 8, 32; WORLD BANK, A TOOLKIT FOR CORPORATE WORKOUTS 68 (2022); IMF, *supra* note 29, at 64; UNCITRAL, *supra* note 29, at 18.

91. *See* EBRD, *supra* note 29, at 6; WBG, *Principles for Effective Insolvency and Creditor Rights Systems*, *supra* note 29, at 13; WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 8; UNCITRAL, *supra* note 29, at 9-10.

92. EBRD, *supra* note 29, at 8; IMF, *supra* note 29, at 58; Helen Anderson et al., *Shareholder and Creditor Protection in Australia: A Leximetric Analysis*, 30 CO. & SEC. L. J. 366, 376-77 (2012).

93. WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 8; WBG, *Principles for Effective Insolvency and Creditor Rights Systems*, *supra* note 29, at 6; Baird & Jackson, *supra* note 28, at 99-100.

When an insolvent company undergoes rehabilitation, it retains operational control under a court-approved plan, ensuring that its assets are not liquidated at distressed values. Instead, assets are used productively, maintaining their value and revenue-generating potential, thereby benefiting creditors by increasing the likelihood of repayment.[94] Rehabilitation procedures also enable a structured repayment plan to settle the debtor's debt, ensuring the equitable treatment of creditors. The process typically involves debt restructuring, extended payment schedules, or reductions in outstanding liabilities, offering creditors a more predictable and fair recovery of their claims than immediate (piecemeal) liquidation.

By keeping a distressed company operational, reorganization procedures ensure that existing business relationships between creditors and debtors remain intact. This is particularly important for suppliers, lenders, and service providers, who may continue to benefit from future transactions with the insolvent debtor under a rehabilitation scheme. Moreover, the fact that rehabilitation procedures are conducted with judicial oversight ensures transparency and fairness in debt restructuring. Because creditors have a voice in approving restructuring or reorganization plans, rehabilitation procedures allow them to negotiate favorable terms.[95]

Finally, sudden insolvencies and liquidations can cause significant market disruptions. In such cases, allowing a company to reorganize its financial affairs rather than being immediately liquidated enables the economy to avoid adverse ripple effects, thereby preserving creditor confidence and financial stability.[96] As is evident from international best practices, rehabilitation focuses on restructuring an entity to enable it to continue its operations. On the other hand, liquidation procedures, as a last resort remedy, ensure that a fair and orderly dissolution of the debtor's assets takes place when recovery or rehabilitation is not viable. The following are the significant roles of liquidation procedures as a tool to protect creditors' interests during insolvency.[97]

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94. UNCITRAL, *supra* note 29, at 209; XU, *supra* note 64, at 9-15.

95. WBG, *Principles for Effective Insolvency and Creditor Rights Systems*, *supra* note 29, at 6; WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 8; Steve J. Arsenault, *Westernization of Chinese Bankruptcy: An Examination of China's New Corporate Bankruptcy Law Through the Lens of the UNCITRAL Legislative Guide to Insolvency Law*, 27 PENN. ST. INT'L L. REV. 45, 50 (2008).

96. UNCITRAL, *supra* note 29, at 165-66.

97. *Id.* at 31; SARRA, *supra* note 69, at 30-55.

Primarily, liquidation procedures provide for a prompt, orderly, and equitable protection of creditors' interests by defining and enforcing creditors' priority rights and ranking them during the final distribution of the debtor's remaining assets. Liquidation follows a structured legal framework that prioritizes creditor claims by classification as secured, privileged, or unsecured. This structured distribution ensures that creditors receive payments in accordance with legal provisions, thereby preventing arbitrary or unfair asset allocations.[98]

Liquidation procedures also provide strict legal oversight by imposing penalties for violations of insolvency law. This is a typical tool to prevent debtors and other involved parties from engaging in fraudulent transfers or asset concealment that could harm creditors by diluting their value. This oversight ensures that the debtor's assets remain intact and creditors receive their fair share of the remaining assets.[99]

Compared to prolonged and uncertain rehabilitation efforts, liquidation provides creditors with a definitive and quick resolution of the debtor's assets and recovery of their claims. While the recovery may not be complete, liquidation allows creditors to close accounts and move forward without prolonged financial uncertainty.[100] Liquidation procedures are also typical tools that encourage market discipline. Liquidation procedures enforce market discipline by discouraging irresponsible financial behavior among businesses. When debtors or businesses are aware that liquidation is a potential consequence of insolvency, they are more likely to adopt responsible financial practices to preserve the value of their assets, thereby indirectly benefiting creditors.[101]

Finally, the fact that liquidation procedures establish the legal rights of creditors to participate (to vote, approve, or oppose) in the liquidation process of the debtor's assets ensures that creditors can present their claims and receive fair treatment under the law. This legal recourse is a fundamental protection mechanism that allows creditors to enforce their

98. WBG, *Principles for Effective Insolvency and Creditor Rights Systems*, *supra* note 29, at 18; WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 26.

99. WBG, *Principles for Effective Insolvency and Creditor Rights Systems*, *supra* note 29, at 15; WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 15.

100. WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 7.

101. UNCITRAL, *supra* note 29, at 95.

rights effectively.[102] Recognizing and enforcing rehabilitation and liquidation procedures ensures that creditors are protected under all insolvency scenarios. While rehabilitation offers a path for businesses to recover and fulfill their obligations over time, liquidation provides an essential safety net for creditors when recovery of their claims is not feasible.[103]

It is evident from international best practices that the combined presence of these procedures ensures that creditors have multiple avenues to recover their claims, that businesses with viable futures are allowed to restructure their affairs, and that creditors retain confidence in the financial and legal system, thereby promoting investment and lending activities.[104]

F. The Fair Treatment of Creditors During Insolvency

The principle of fair treatment of creditors is a foundational concept in insolvency law, ensuring fairness and order in the resolution of financial distress. Rooted in the doctrine of *pari passu*, which mandates equitable treatment of similarly ranked creditors, this principle maintains the integrity of collective procedures by distributing debtor assets in a structured manner.[105] According to the international best practice, the provisions on equitable treatment of creditors in insolvency procedures are crucial legal mechanisms to establish the order in which claims should be satisfied from the estate, ensure that similarly ranked creditors are satisfied proportionately out of the assets of the estate, and specify limited circumstances in which priority in distribution is permitted.[106]

Equitable treatment of creditors in insolvency procedures is based on the principle that creditors with similar legal rights should be treated fairly, receiving distributions in proportion to their relative ranking and

102. *Id.* at 83; MURRAY & HARRIS, *supra* note 33, at 1-44.

103. WBG, *Principles for Effective Insolvency and Creditor Rights Systems*, *supra* note 29, at 6.

104. WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 6; Douglas G. Baird, *A World Without Bankruptcy*, 50 LAW & CONTEMP. PROBS. 173, 189 (1987).

105. UNCITRAL, *supra* note 29, at 6; GOODE, *supra* note 78, at 99-100; RIZWAAN JAMEEL MOKAL, CORPORATE INSOLVENCY LAW: THEORY AND APPLICATION 127-128 (Oxford Univ. Press 2005).

106. EBRD, *supra* note 29, at 7; WBG, *Principles for Effective Insolvency and Creditor Rights Systems*, *supra* note 29, at 15; WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 21; IMF, *supra* note 29, at 47; UNCITRAL, *supra* note 29, at 275.

interests. This approach does not necessarily mean identical treatment but rather a framework that respects the different contractual arrangements creditors have made with the debtor. For example, secured creditors, whose claims are backed by collateral, are treated differently from unsecured creditors. The guiding philosophy of equitable treatment ensures that no creditor is unduly disadvantaged by fraud, favoritism, or systemic bias.[107]

One of the main justifications for equitable treatment is to create predictability and stability in financial markets. When creditors know insolvency laws will be applied fairly and consistently, they are more likely to lend and invest. This predictability fosters economic growth by reducing the risks associated with financial transactions. In the case of cross-border lending, equitable treatment ensures that international creditors' claims are not arbitrarily subordinated, a crucial consideration in an era of global financial integration.[108]

The *pari passu* principle is central to corporate insolvency law. It dictates that unsecured creditors share the insolvent company's available assets ratably according to their pre-insolvency claims. There are two interpretations of *pari passu*: the stronger interpretation, which mandates a *pro rata* distribution of assets among unsecured creditors, and the weaker interpretation, which allows for differentiation based on statutory ranking among unsecured creditors.[109] The justification for *pari passu* lies in its efficiency and fairness. A mandatory, collective regime reduces legal costs and delays, eliminating the need for courts to engage in complex adjudication over the distribution of the debtor's assets. *Pari passu* ensures that insolvency is managed in an orderly manner, maximizing the collective benefit of all stakeholders by preventing a chaotic race among creditors to seize assets individually.[110]

However, the *pari passu* principle has exceptions, particularly in cases involving secured creditors, preferential debts, and statutory claims. While preferential debts, such as employee wages and certain tax

107. IMF, *supra* note 29, at 6; Eugenio Vaccari, *Creditor Treatment in Corporate Insolvency Law*, 30 INT'L INSOLVENCY REV. 316, 317 (2021).

108. GOODE, *supra* note 78, at 1-100; David A. Skeel Jr., *The Empty Idea of "Equality of Creditors,"* 166 U. PA. L. REV. 699, 731 (2018).

109. Mari Schihalejev, *Restrictions on the Participation of Debtor-Related Creditors in Bankruptcy Proceedings: Is There Need for New Approach in Estonian Law?*, 4 INT'L COMP. JURIS. 52, 54 (2018).

110. FINCH, *supra* note 37, at 599-674; Frédéric Closset et al., *Corporate Restructuring and Creditor Power: Evidence from European Insolvency Law Reforms*, 149 J. BANKING & FIN. 1, 1-2 (2023).

obligations, are given statutory precedence, secured creditors have priority over specific assets. Despite these exceptions, *pari passu* remains a cornerstone of insolvency law, reinforcing the broader goal of equitable treatment.[111]

Equitable treatment enhances the efficiency of insolvency procedures by streamlining asset distribution and reducing strategic behavior among creditors. By adhering to a standardized process, insolvency laws ensure that creditor claims are adjudicated systematically, reducing litigation and administrative costs. This efficiency benefits not only creditors but also the legal and financial systems.[112]

Fairness is another fundamental rationale for equitable treatment. Insolvency laws uphold justice and procedural integrity by ensuring that similarly situated creditors receive equal treatment. If certain creditors were unfairly prioritized without a legal basis, confidence in financial institutions and the insolvency framework would erode. Ensuring fairness prevents the concentration of losses on weaker creditors while discouraging opportunistic behavior by more powerful financial entities.[113] Insolvency procedures must guard against fraudulent transfers and preferential treatment that may distort the equitable distribution of assets. Fraudulent conveyance laws prevent debtors from transferring assets to favored parties before they become insolvent, thereby preserving the integrity of the insolvency estate. Similarly, avoidance provisions enable the claw-back of transactions that undermine the equal treatment of creditors.

By prohibiting preferential treatment, insolvency laws ensure creditors do not exploit their relationships with the debtor to gain an unfair advantage. For example, debtor-related persons, such as corporate insiders or shareholders, are often disadvantaged in insolvency procedures to prevent conflicts of interest. These safeguards uphold the collective nature of insolvency and reinforce public trust in financial

111. Elizabeth Warren, *A Principled Approach to Consumer Bankruptcy*, 71 AM. BANKR. L. J. 483, 501 (1997); Closset & Urban, *supra* note 14, at 456-58.

112. Rizwaan Jameel Mokal, *Priority as Pathology: The Pari Passu Myth*, 620(3) CAMB. L.J. 581, 616-17 (2001); R.J. de Weijs et al., *The Imminent Distortion of European Insolvency Law: How the European Union Erodes the Basic Fabric of Private Law by Allowing 'Relative Priority' (RPR)*, 125 TIJDSCHRIFT VOOR BELGISCH HANDELSRECHT. 477 (2019).

113. Philip R. Wood, *The Law of International Insolvencies and Debt Restructurings*, *in* THE LAW OF INTERNATIONAL INSOLVENCIES AND DEBT RESTRUCTURINGS 1-50 (James R. Silkenat & Charles D. Schmerler eds., 2006); Michelangelo Granato, *The Myth of the Optimal Capital Structure and the Dogma of Creditor Protection*, 18 EUR. BUS. ORG. L. REV. 617, 619 (2017).

systems.[114] On the other hand, while equitable treatment is a fundamental principle, it must be balanced with other policy considerations, such as protecting employees, ensuring the continuity of viable businesses, and promoting economic stability. In some cases, deviations from strict equality are justified.[115]

For instance, preferential claims for employees ensure that vulnerable workers receive priority compensation in the event of liquidation. Similarly, restructuring laws may allow for differential treatment of creditors if it increases the likelihood of corporate survival, ultimately benefiting all stakeholders.[116] Despite these necessary deviations, the overarching objective remains the fair and orderly distribution of assets. Striking a balance between creditor rights and broader social and economic goals is essential for maintaining the legitimacy and effectiveness of insolvency law.[117]

The principle of equitable treatment is widely recognized in international insolvency frameworks. Many jurisdictions adopt variations of the *pari passu* rule while incorporating local priorities and policy considerations. UNCITRAL and the World Bank have developed guidelines emphasizing creditor equality as a fundamental principle of effective insolvency systems.[118] Multiple international approaches have since emerged along these lines.

For example, in the United States, the Bankruptcy Code enshrines the principle of equality among creditors as a primary objective. The trustee in bankruptcy procedures ensures that unsecured creditors share proportionately in the available assets unless a creditor demonstrates a legally justified priority.[119] Additionally, the European Union's insolvency regulations emphasize fairness and transparency in cross-border insolvency cases.[120] Different jurisdictions have developed distinct approaches to creditor ranking and priority, reflecting diverse legal

114. MURRAY & HARRIS, *supra* note 33, at 1-44; Jay Lawrence Westbrook et al., *Introduction*, *in* A GLOBAL VIEW OF BUSINESS INSOLVENCY SYSTEMS 1-40 (Martinus Nijhoff Publishers 2010).

115. Skeel, *supra* note 108; Barry E. Adler, *The Creditors' Bargain Revisited*, 166 U. PA. L. REV. 1853, 1860-61 (2018).

116. WESSELS ET AL., *supra* note 61, at 1-20; Daniela Maresch et al., *Creditor Protection, Judicial Enforcement and Credit Access* 1 (EUR. CENT. BANK, Working Paper No. 1829, 2015).

117. XU, *supra* note 64, at 1-50.

118. UNCITRAL, *supra* note 29, at 290; WBG, *Principles for Effective Insolvency and Creditor/Debtor Regimes*, *supra* note 29, at 2.

119. 11 U.S.C. §§ 701-784 (2018); 11 U.S.C. §§ 1101-1195 (2018).

120. COUNCIL REGULATION 2015/848, 2015 O.J. (L 141) 19 (EU); Council Directive 2017/1132, 2017 O.J. (L 169) 46 (EU); INSOLVENCY ACT 1986, c. 45, sch. 6 (UK).

traditions and economic policies. However, the universal commitment to equitable treatment underscores its fundamental importance in maintaining confidence in insolvency systems worldwide.[121]

IV. MATERIALS AND METHODS

This qualitative study examines whether the new Ethiopian insolvency law effectively protects creditors' interests during insolvency proceedings. Additionally, by comparing it with the requirements of relevant international guidelines, the study explores the alignment of creditors' protection rights in Ethiopia with global best practices.

To explore whether Ethiopian insolvency law provides adequate protection to creditors' interests during or in the vicinity of insolvency, the authors of this Article conducted interviews with nine expert respondents, selected using purposive sampling.[122] Of the nine respondents, three are senior judges, three are insolvency lawyers (practitioners), and the remaining three are law professors. Then, an inductive thematic analysis of the qualitative interview data was conducted using the reflexive thematic analysis (RTA) method, as developed by Braun and Clarke (2006, 2019).[123]

The RTA method is a step-by-step approach for conducting a thematic analysis of qualitative interview data. It is a method for extracting "themes" and patterns from qualitative data. This Article has followed the six steps of the RTA method to analyze the qualitative data and identify the final themes: data familiarization, code and theme generation, theme review, theme naming and definition, theme definition, and report generation.[124]

The themes discussed below are developed from the interviewees' responses to the follow-up question, which was asked after they replied positively to the main research question, "Do you believe the new

121. IMF, *supra* note 29, at 5; LOUISE GULLIFER, GOODE AND GULLIFER ON LEGAL PROBLEMS OF CREDIT AND SECURITY Para. 4.09 (Sweet and Maxwell, 6th ed. 2017).

122. Lawrence A. Palinkas et al., *Purposeful Sampling for Qualitative Data Collection and Analysis in Mixed Method Implementation Research*, 42 ADMIN. POL'Y MENTAL HEALTH 533 (2015).

123. Virginia Braun & Victoria Clarke, *Using Thematic Analysis in Psychology*, 3 QUAL. RSCH. PSYCH. 77, 79, 87 (2006); Virginia Braun & Victoria Clarke, *Reflecting on Reflexive Thematic Analysis*, 11 QUAL. RSCH. SPORT, EXERCISE & HEALTH 589, 590 (2019).

124. Braun & Clarke, *Using Thematic Analysis in Psychology*, *supra* note 123; Braun & Clarke, *Reflecting on Reflexive Thematic Analysis*, *supra* note 123; David Byrne, *A Worked Example of Braun and Clarke's Approach to Reflexive Thematic Analysis*, 56 QUAL. & QUANT. 1391, 1398 (2021).

Ethiopian insolvency regime protects creditors' interests?" Based on the positive reply, respondents were then asked: "What justifications can you provide to substantiate that the law protects creditors' interests during insolvency?" The respondents, to justify how Ethiopian insolvency law protects creditors' interests during insolvency, among others, then mentioned that Ethiopian insolvency law "imposes various duties on directors to consider creditors' interests during insolvency," "protects creditors' participation and information rights," "protects the debtor's asset," "protects secured creditors' interests," "provides fair treatment of creditors' interests," and "provides optional insolvency procedures to resolve the debtor's insolvency."

As the discussions in Part I and II of the study demonstrate, these themes are essential, as they are standard tools for protecting creditors' interests during insolvency. The more these themes are recognized and enforced in a legal system, the greater the protection is for creditors' interests. Then, based on the different justifications provided by each respondent, respondents were asked follow-up questions to clarify how Ethiopian insolvency law uses each justification (theme) as a tool to protect creditors' interests. The respondents provided detailed answers, which were then developed into "codes." Based on these codes, the six themes (variables) used in this study were then developed as a tool to evaluate whether the new Ethiopian insolvency law effectively protects creditors' interests. Additionally, the themes derived from the interviewees' responses were compared with international benchmarks to address the study's subsidiary goals.

V. QUALITATIVE ANALYSIS OF CREDITORS' PROTECTION RIGHTS DURING INSOLVENCY IN ETHIOPIA

This Part presents the findings of the qualitative analysis of the interview data, organized by variable in a theme-driven format. Accordingly, the following are the significant findings in each of the themes identified in this study based on the codes developed from the interview transcripts:

A. Directors' Duties During Insolvency in Ethiopia

As evident from the interviewees' responses and in line with international best practices, Ethiopian insolvency law is well-equipped with the following legal strategies that impose various duties on directors. The first legal strategy utilized to protect creditors' interests is to define to

whom the directors owe their duties and whose interests they should consider when insolvency is imminent. One of the law's primary objectives is to safeguard the legitimate interests of creditors by penalizing irregularities in insolvency procedures, imposing duties on directors, and prohibiting any activity or transaction that violates creditors' interests.[125]

Unlike in normal periods, during the suspect period, Ethiopian law expressly imposes fiduciary duties on the company's directors to protect the interests of creditors and take all necessary steps to prevent insolvency.[126] For example, in the case of groups of companies where a subsidiary company has no reasonable prospect of avoiding dissolution, the law imposes a duty on the directors of the parent company to effect, without delay, a fundamental restructuring of the subsidiary or initiate its winding-up (insolvency) procedure.[127] Otherwise, if management allows the subsidiary company to continue operating to its detriment, when initiating insolvency procedures would have been the correct remedy, they shall be held liable for wrongful trading and for any unpaid debts of the subsidiary.[128]

An additional legal strategy to protect creditors' interests is to stipulate the party and its powers to bring actions against wrongful directors during insolvency, as well as during the limitation period within which such an application must be made.[129] In an action against directors or other persons concerning liability arising during the suspect period, in cases of a reorganization procedure, or against the supervisor in a reorganization, or, upon their default against a controller or a creditor acting on behalf of the estate, the plaintiff shall institute legal proceedings for invalidation.[130] During a liquidation procedure, the trustee in bankruptcy shall have the same powers as the supervisor in

125. Commercial Code of Ethiopia, Articles 588-825, 597(1-4), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

126. *Id.* at Articles 699(1, 2), 480-491; Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court, in Addis Ababa, 05-06/06/2023.

127. Commercial Code of Ethiopia, Article 564(1, 2), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

128. *Id.* at Articles 563(1-3), 564(3, 4).

129. Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court, in Addis Ababa, 05-06/06/2023.

130. Commercial Code of Ethiopia, Articles 673(1, 2), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

reorganization, and the creditors' committee shall have the same powers as the controllers to apply for invalidation.[131]

Civil actions against responsible directors during insolvency may only be brought before the court by the trustee in bankruptcy or, in his default, by a creditor acting on behalf of the estate.[132] Criminal actions against directors or other persons concerning liability arising during the suspect period, as well as in all cases of bankruptcy-related offenses, are investigated by the public prosecutor or the trustee in bankruptcy.[133] However, unlike insolvency, during solvency, the power to sue a director is vested in the company via the instrumentality of its board of directors, also known as derivative suits.[134]

At any time, when directors violate their duties to creditors by continuing the company's business after such time as when the directors knew or ought to have concluded that there was no reasonable prospect of the company's being able to pay its creditors or by failing to preserve intact the company's assets, creditors have the right to directly sue such directors regardless of the company's decision not to institute proceedings against the directors.[135] Another legal strategy utilized to impose duties on directors during insolvency is to define the period before formal insolvency, during which directors' duties towards creditors commence.[136] Initially, to declare the debtor insolvent (bankrupt) at the first hearing opening the proceedings, the court must prove the cessation of payment and set the date of suspension of payments.[137]

Under Ethiopian insolvency law, the period from the date of cessation of payments, as fixed by the court, until the date of the opening of proceedings (i.e., the first hearing) shall be considered the suspect period. The duration of the suspect period may not exceed eighteen months.[138] Due to that, the date of suspension is usually before the date of opening of the proceeding, which implies that the effects of the debtor's insolvency retroactively commence not from the day of the first hearing but from the presumed date of payment cessation. An additional legal

131. *Id.* at Articles 766, 767.

132. *Id.* at Articles 806(1-4).

133. *Id.* at Articles 814(1-3).

134. *Id.* at Articles 328(1-6), 306 (1-6).

135. *Id.* at Articles 329(1-3), 330.

136. Interview with Respondent Judge 3 (RJ3), Senior Judge, Ethiopian Federal High Court in Addis Ababa, 12-13/07/2023.

137. Commercial Code of Ethiopia, Articles 590(3, 4), 591(1-4), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

138. *Id.* at Article 591(5).

strategy employed to protect creditors' interests is to define actions that potentially give rise to the director's liability and prohibit them.[139] The law provides for specific acts during the suspect period that could give rise to directors' liability or adverse consequences for a director or the debtor. The law treats these acts of the debtor or directors differently based on their nature and the gravity of the consequences of the acts on creditors' interests.

The first group of acts refers to those that lead to mandatory invalidation, and the law has exhaustively enumerated them. These acts shall be mandatorily invalidated because they directly affect creditors' interests by diverting, degrading, or reducing the value of the debtor's assets, resulting in unfair preferential treatment among creditors, which is contrary to the principle of equality among creditors and the priority ranking rules of distribution in insolvency.

During a reorganization procedure, at the request of the supervisor in reorganization, the court shall invalidate the following acts performed by the debtor (directors) during the suspect period: assets or rights transferred to other persons through gratuitous assignments, donation, cancellation, or waiver of rights; assets or rights transferred to other persons for a price that is manifestly undervalued; payments of debts that are not due, whether in cash, by assignment, set-off or otherwise; payments of debts otherwise owing than in cash, or by set-off, or by negotiable instrument or by transfer to a bank; and creation of mortgages, pledges or other *in rem* security interest, over the assets of the debtor, in respect of debts contracted before the creation of such rights *in rem*.[140] As the name indicates, once these acts are performed, the court should presume they are detrimental to creditors' interests and must invalidate them upon complaint. No acts other than those in the above list may lead to mandatory invalidation.

The second group of acts comprises those acts that lead to optional invalidation, and the law has enumerated them by exclusion from mandatory acts. These acts are believed to have minor effects on creditors' interests and are subject to case-by-case treatment by the court to be invalidated. Hence, the court can assess their impact and proceed with the invalidation, as the law does not enumerate such acts but instead stipulates them in general terms. Technically, based on the court's discretion and the

139. Interview with Respondent Judge 3 (RJ3), Senior Judge, Ethiopian Federal High Court in Addis Ababa, 12-13/07/2023.

140. Commercial Code of Ethiopia, Articles 671(1-5), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

situation's need, all the remaining acts of the debtor may result in optional invalidation.

At the request of the supervisor in a reorganization, the court may invalidate all other acts performed by the debtor during the suspect period, provided that the creditor knew or should have known that the debtor was already in a situation of cessation of payments and the act was detrimental to the estate or the payment was made in preference to other creditors.[141]

The third group of acts contains those acts and payments that are excluded from invalidation except in cases where they are done by the directors fraudulently. The law enumerates such acts exhaustively. The court may not invalidate these acts because the law presumes they are not wrong. Because they are performed in the ordinary course of events, they are necessary to undergo insolvency procedures, help administrators do their work, preserve or maximize the value of the debtor's assets, and be more productive. Therefore, except in cases of fraud, these acts are presumed not to prejudice creditors' interests; instead, they are tools to protect creditors' interests.

The following acts and payments made by the debtor during the suspect period may not be subject to invalidation, except in the case of fraud: new financing, the creation of security interests, the sale of assets, the payment of debts, as well as any other legal acts and payments made by the debtor under the restructuring plan, which the court has confirmed; the realization of mortgages, pledges and other *in rem* security interests; acquisition of assets necessary for carrying out the ordinary course of business; and acquisition of goods by and rendering of services to third parties in good faith provided fair price paid for the goods or services.[142] It should be noted that whether the acts are subject to optional or mandatory invalidation, the court will invalidate them upon complaint by the authorized persons discussed above. If not, the acts will remain valid and continue to devastate creditors' interests.[143]

The other strategy the law uses to protect creditors' interests is defining the effect of the court's invalidation of these invalid acts on the parties' interests.[144] It is evident from the law that the decision to invalidate a payment or an act has a retroactive effect. To restore the parties to the position before the invalid acts are performed, the things exchanged

141. *Id.* at Articles 672(1, 2).

142. *Id.* at Articles 674(1-4), 675.

143. *Id.* at Articles 673(1, 2).

144. Interview with Respondent Judge 2 (RJ2), Senior Judge, Ethiopian Federal First Instance Court in Addis Ababa, 19-20/06/2023.

should be restored in kind, or else the property's market value shall be returned to the benefit of the estate.[145] The right of interested parties to invalidate the specific acts of the debtor or directors stated above is restricted by a period of limitation. However, in exceptional cases, any invalidation proceedings filed more than two years after the date of the judgment opening reorganization proceedings shall be barred.[146] It should be noted that all the above rules, during a reorganization procedure, are also applicable to a bankruptcy (liquidation) procedure.[147]

The other essential tool the law uses to protect creditors' interests is to impose civil and criminal liability on directors for breaches of duty during the insolvency process.[148] In the event of a likelihood of insolvency, directors shall have a fiduciary duty to protect the interests of creditors and take all necessary steps to prevent insolvency.[149] Consequently, failure to discharge their duties entails civil and criminal liabilities against directors. Regarding civil liabilities, the court may, in the course of insolvency procedures, order that one or more directors bear all or part of the debts of the entity where the director is at fault and has contributed to the insufficiency of assets of the company, corresponding to the aggregate of the decrease in the value of the assets and the increase in the value of the liabilities.[150]

If the directors perform the following acts, they are presumed to be at fault and to have contributed to the insufficiency (decrease) of the debtor's assets or increase of the liabilities: grossly negligently failing to file for bankruptcy within forty-five days after the cessation of payments, grossly negligently continuing money-losing activities, carrying out commercial operations on their behalf, and disposing of company assets as though they were their own and concealing their personal affairs under cover of the company.[151]

145. Commercial Code of Ethiopia, Articles 677(1-4), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Civil Code of Ethiopia, Articles 1808-1818, Proclamation No. 165, Negarit Gazette, Year 1960, No. 2.

146. Commercial Code of Ethiopia, Articles 676(1, 2), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

147. *Id.* at Articles 766, 767.

148. Interview with Respondent Judge 2 (RJ2), Senior Judge, Ethiopian Federal First Instance Court in Addis Ababa, 19-20/06/2023.

149. Commercial Code of Ethiopia, Articles 699(1, 2), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

150. *Id.* at Article 803.

151. *Id.* at Article 803(1).

Where several directors have committed management failures contributing to the insufficiency of the debtor's assets, the court may hold these managers liable jointly and severally.[152] The law states that, as a result of the civil action, sums recovered under such action against the responsible director(s) shall be used to pay the bankrupt entity's creditors, in accordance with the creditors' priorities of ranking during distribution.[153] Civil actions against responsible directors may only be brought before the court by the trustee in bankruptcy or, in his default, by a creditor acting on behalf of the estate.[154]

In addition to criminal liability under criminal law, Ethiopian insolvency law imposes detailed criminal sanctions on responsible directors for offenses related to negligent bankruptcy, fraudulent bankruptcy, disqualification due to bankruptcy, the granting of benefits, and personal bankruptcy.[155] Insolvency law, in the course of bankruptcy proceedings, also empowers the court to order that one or more directors of a company be declared bankrupt personally and bear all or part of the debts of the entity when they have committed one of the acts stated under article 815.[156] Finally, in addition to the criminal sanctions under insolvency law, Ethiopian criminal law also imposes detailed liabilities on directors for bankruptcy-related crimes, such as fraudulent bankruptcy, irregular bankruptcy, fraud in execution, unjustifiable preferences, and misappropriation or destruction of property.[157]

B. Creditors' Participation and Information Rights During Insolvency in Ethiopia

As evident from the interviewees' responses and in line with international best practice, to ensure creditors' participation and information rights are adequately protected during insolvency, Ethiopian insolvency law is well equipped with the several legal strategies that are destined to guarantee creditors' participation and information rights:

Primarily, to ascertain creditors' participation and information rights, Ethiopian insolvency law recognizes that one of the main objectives of all

152. *Id.* at Article 803(2).

153. *Id.* at Articles 786, 803(3).

154. *Id.* at Articles 806(1-4).

155. *Id.* at Articles 653, 655(5), 656, 673(1, 2), 687, 328(1), 699(1, 2), 803(1, 2), 804(1-3), 805(1, 2), 806-814, 766, 767.

156. *Id.* at Articles 815((1,2), 786.

157. Criminal Code of Ethiopia, Articles 34, 90, 716(1-3), 725-733, Proclamation No. 414, Year 2005.

insolvency procedures is to ensure legal certainty and transparency through efficient, orderly, and timely procedures.[158] Additionally, to guarantee creditors' information rights, creditors are notified of, or have access to, material information regarding essential activities during the procedures, and are allowed to be heard and to present their opinions.[159] For example, in all insolvency procedures, creditors have the right to demand all relevant information regarding the debtor's affairs from the insolvency administrators in writing or otherwise.[160]

Another legal strategy employed to protect creditors' participation and information rights is the establishment of a creditors' committee.[161] The law accords the creditors' committee with the necessary advisory powers and responsibilities to advise, consult with, and supervise the insolvency representatives in the performance of their administrative duties.[162] The other legal strategy used to ensure creditors' participation and information rights is to impose duties on the debtor, creditors, and insolvency representatives to cooperate with appropriate organs, to submit financial documents and relevant information, to give notice, to deposit and publicize insolvency court decisions, and to report to the required organs.[163]

For example, during all types of procedures, the law imposes a duty on the petitioning debtor to provide the court with all its relevant and latest financial documents. Additionally, the court can collect relevant information on the debtor's finances from third parties, such as banks or tax authorities.[164] Similarly, in all procedures, the law imposes a duty on

158. Commercial Code of Ethiopia, Article 588(1), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court in Addis Ababa, 05-06/06/2023.

159. Commercial Code of Ethiopia, Article 598, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Judge 2 (RJ2), Senior Judge, Federal First Instance Court in Addis Ababa, 19-20/06/2023; Interview with Respondent Lawyer 3 (RL3), a Senior Lawyer Practicing in Ethiopian Federal Courts in Addis Ababa, 10-11/10/2023.

160. Commercial Code of Ethiopia, Articles 599(1-3), 593(5), 649(1-3), 650, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

161. Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court in Addis Ababa, 05-06/06/2023.

162. Commercial Code of Ethiopia, Articles 722, 723, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

163. *Id.* at Articles 591(3), 601(3, 4), 607, 617(2), 621(2), 636, 637, 644, 648-650, 653(5), 662(3), 664, 665(3), 667(1-2), 681(7), 682(2), 685(1), 700, 705(1-2), 710, 720, 726(4), 728, 732, 733, 736, 755, 802(1-4); Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court in Addis Ababa, 05-06/06/2023.

164. Commercial Code of Ethiopia, Articles 617(2), 636, 637(1-3), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

petitioning creditors to submit an affidavit, documentary evidence showing their legitimate and matured claims that have not been paid, and proof of the debtor's insolvency.[165]

Another legal mechanism used to protect creditors' participation rights is a guarantee of creditors' rights to approve essential activities during insolvency procedures.[166] For example, during restructuring and reorganization procedures, creditors, in their capacity as creditors, have the right to request amendments to the plans and to offer a counterproposal. The plans should also be unanimously approved by all creditors participating in the procedure or a qualified majority of them.[167] Similarly, the required majority of creditors also has the right to approve the business sale as a going concern under the ambit of the reorganization procedure.[168]

To fully ensure creditors' participation, the law requires that both the restructuring and reorganization plans, in all cases, comply with the "best interest of creditors" test, ensuring that the plan better suits creditors' interests than whatever they would have received in liquidation.[169] Otherwise, noncompliant plans shall be rejected by the court.[170] On the other hand, during a restructuring procedure, the law guarantees creditors the right to request that the court replace the expert, ensuring they can appoint an expert who has considered their interests. Unless creditors representing two-thirds of the total amount of claims support the appointment, the court cannot appoint the debtor's proposed restructuring expert.[171] Similarly, the law protects various approval rights of creditors to ensure their participation and information rights and defend their interests.[172]

Another strategy utilized to ensure creditors' participation rights is a guarantee of creditors' rights to apply for or propose changes during the procedures.[173] For example, the law guarantees creditors' rights to

165. *Id.* at Articles 637(4), 658, 751-754, 705(6, 7), 755.

166. Interview with Respondent Judge 2 (RJ2), a Senior Judge, Ethiopian Federal First Instance Court in Addis Ababa, 19-20/06/2023.

167. Commercial Code of Ethiopia, Articles 627(1, 2), 678(1-2), 680-687, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

168. *Id.* at Articles 597(1-4), 689-695.

169. *Id.* at Article 678(5).

170. *Id.* at Articles 697(6), 700-704(1-3).

171. *Id.* at Articles 619-620.

172. *Id.* at Articles 643(1-3), 645(1), 719(1-4), 748(3), 593(4(c)).

173. Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court, 05-06/06/2023.

commence or initiate a reorganization procedure.[174] In a reorganization proceeding, for justifiable reasons, the law also allows creditors to apply to the court to extend the initial four-month observation period or to restart it anew.[175] The law guarantees the rights of creditors with matured claims against the debtor to initiate liquidation proceedings.[176]

The other legal tool utilized to ascertain creditors' participation rights is a granting of the right to disapprove, oppose, or appeal activities that encroach on or are likely to infringe upon their interests.[177] For example, creditors have the right to oppose, within seven consecutive days of the insolvency representative's decision, the decision to continue or terminate an ongoing contract.[178] Creditors have the right to appeal the judgment rejecting the opening of a liquidation procedure.[179] The law also guarantees creditors' rights to seek the rejection of the judgment, thereby opening a liquidation procedure.[180]

C. The Protection of the Debtor's Assets During Insolvency in Ethiopia

Additionally, as evidenced by the interviewees' responses and in line with international best practices for preserving or maximizing the remaining debtor's assets during insolvency, Ethiopian insolvency law is well-equipped with various following legal strategies to maximize such assets.

First, the law stipulates that maximizing the value of the debtor's property (estate) is one of the primary goals of all recognized insolvency procedures in Ethiopia, which increases creditors' chances of recovery.[181] Second, the law serves to divest the debtor of control over the insolvent

174. Commercial Code of Ethiopia, Articles 635(1(b)), 648(4), 651(1(b)), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

175. *Id.* at Article 651(2).

176. *Id.* at Articles 705(4 (b), 709, 648(1-4), 710, 748(1, 2); Interview with Respondent Lawyer 1 (RL2), Senior Lawyer, Practicing in Ethiopian Federal Courts in Addis Ababa, 25-26/09/2023.

177. Commercial Code of Ethiopia, Articles 632(1-4), 639(1,2), 640(1-3), 652(1), 688, 692(1-4), 719(1), 697(1-8), 721, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Judge 2 (RJ2), Senior Judge, Ethiopian Federal First Instance Court in Addis Ababa, 19-20/06/2023.

178. Commercial Code of Ethiopia, Articles 594(1-3), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

179. *Id.* at Article 711.

180. *Id.* at Articles 616(1-5), 712(1-3).

181. *Id.* at Article 588(1); Interview with Respondent Professor 2 (RP2), Professor, at Addis Ababa University, in Addis Ababa, 03-04/08/2023.

estate's management and appoint professional management to supervise and administer the procedures and the debtor's assets.[182] During the ensuing procedures, the law appoints insolvency representatives (the supervisor, the trustee, the experts, and the controllers) to administer the debtor's assets.[183]

To ensure proper administration, the law also strictly outlines their powers, duties, and liabilities, resulting in an effective division of labor, transparency, and accountability in the discharge of duties.[184] Additionally, the law imposes a duty on insolvency representatives to take conservatory measures to preserve the debtor's rights and assets.[185] This increases productivity, maximizes the asset's value, benefits creditors, and ensures the efficient administration of the debtor's remaining assets, thereby ending the misuse of capital.[186]

A third strategy the law utilizes to preserve the debtor's assets during a restructuring procedure is to guarantee the debtor's right to apply to the court for a single stay of action against a creditor who has requested payment of its claim or has instituted enforcement actions.[187] Similarly, during a reorganization proceeding, the law imposes an automatic stay of all claims against the debtor by all types of creditors during the observation period.[188] The judgment awarding the stay of proceedings in favor of the debtor temporarily suspends the enforcement of all types of claims (secured or preferential) by creditors against the debtor, thereby relieving the debtor, for the duration of the stay, from the demand or harassment of creditors demanding to be paid and gives the debtor more time to readjust their affairs. It also preserves the debtor's remaining assets

182. Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court in Addis Ababa, 05-06/06/2023.

183. Commercial Code of Ethiopia, Articles 604-616, 619-622, 642-647, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Professor 3 (RP3), Professor, Addis Ababa University in Addis Ababa, 22-23/08/2023.

184. Commercial Code of Ethiopia, Articles 715-725, 742-754, 760, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

185. *Id.* at Articles 725-750, 604-616.

186. Interview with Respondent Professor 3 (RP3), Professor, Addis Ababa University, in Addis Ababa, 22-23/08/2023.

187. Commercial Code of Ethiopia, Articles 625(1, 2), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court in Addis Ababa, 05-06/06/2023.

188. Commercial Code of Ethiopia, Articles 654(1-5), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

from depletion by protecting them from piecemeal sale by individual creditors, thereby increasing the value of the assets in a going concern.[189]

Another strategy the law utilizes to preserve the debtor's assets is to provide precise and objective legal procedures or requirements for identifying, collecting, preserving, and recovering the debtor's assets and rights duly and in a cost-effective manner, which are known as conservatory measures.[190] In this regard, the law has implemented many strategies to protect and realize the debtor's assets and rights, such as procedures constituting the bankrupt estate, conservatory measures, affixing seals of the bankrupt estate, inventory, administration of the debtor's estate, recovery from the estate, invalidation of suspect acts, and submission and verification of pre-insolvency claims. [191]

Additionally, the law grants the debtor the exceptional right to possess their assets (debtor-in-possession) and make decisions that fall within the ordinary course of business.[192] Similarly, during the observation period of a reorganization procedure, the law authorizes the debtor to remain in control of their assets and affairs and to conduct all day-to-day operations of its business without prior approval from the insolvency representative.[193] As the person with detailed knowledge of their business, the debtor can guarantee their own rights to remain in possession of their assets and to make decisions in the ordinary course of business, enabling them to stay active and cooperative during the procedure. It augments the efficiency and productivity of the insolvency process.

An additional strategy utilized to preserve the debtor's assets and rights during a reorganization procedure is the institution of an "observation period" of four months, which gives the debtor a cooling time that enables them to reorganize their affairs better, reevaluate their options, and prepare a productive reorganization plan with the assistance

189. *Id.* at Articles 625(3), 655(1-5); Interview with Respondent Professor 3 (RP3), Professor, Addis Ababa University, in Addis Ababa, 22-23/08/2023.

190. Commercial Code of Ethiopia, Articles 726-728, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court in Addis Ababa, 05-06/06/2023; Interview with Respondent Professor 2 (RP2), Professor, Addis Ababa University, in Addis Ababa, 03-04/08/2023.

191. Commercial Code of Ethiopia, Articles 659-677, 725-746, 751-760, 766-774, 803, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

192. *Id.* at Article 624; Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court in Addis Ababa, 05-06/2023.

193. Commercial Code of Ethiopia, Articles 653(1-4), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

of the insolvency representatives.[194] Additionally, the law prohibits suspect acts and the invalidation of transactions entered during the suspect period, thereby recovering and restoring assets that the parties illegally transferred or siphoned from the insolvent estate.[195]

Yet another legal strategy the law used is to obligate the petitioning debtor, creditors, and relevant third parties to provide the court with all relevant and up-to-date financial statements and other relevant documents.[196] The obligations imposed on the petitioning debtors, creditors, and other relevant third parties to produce the necessary documents immensely assist the insolvency representatives with efficiently preserving and realizing the remaining assets of the debtor, identifying the claimants from the estate, collecting debts from third parties, and recovering the debtor's assets controlled by third parties.[197]

The final strategy the law uses to preserve the value of the debtor's assets is to impose obligations on the insolvency representatives to take crucial steps for continuing the debtor's business operations or fulfilling ongoing contracts and prohibiting unproductive or unviable procedures.[198] In both reorganization and liquidation procedures, the law imposes duties on insolvency representatives to take all necessary measures to preserve the debtor's assets, continue the business, and decide whether to continue or terminate ongoing contracts.[199]

194. *Id.* at Articles 651(1-4), 655-657; Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court in Addis Ababa, 05-06/06/2023; Interview with Respondent Professor 2 (RP2), Professor, Addis Ababa University, in Addis Ababa, 03-04/08/2023.

195. Commercial Code of Ethiopia, Articles 671-677, 766-767, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court in Addis Ababa, 05-06/06/2023.

196. Commercial Code of Ethiopia, Articles 617(2), 636, 637(1-4), 705(6, 7), 755, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court in Addis Ababa, 05-06/2023.

197. Commercial Code of Ethiopia, Articles 658, 751-754, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

198. Interview with Respondent Judge 1 (RJ1), Senior Judge, Lideta Branch of the Ethiopian Federal High Court in Addis Ababa, 05-06/06/2023.

199. Commercial Code of Ethiopia, Articles 593(4(a)), 606(1-6), 629(1, 2), 672(1, 2), 674(3), 689(3-6), 690, 699, 713(1(e)), 716-717, 727, 731, 742(1), 744(1-4), 745, 747-750; Interview with Respondent Lawyer 3 (RL3), Senior Lawyer, Practicing in Ethiopian Federal Courts in Addis Ababa, 10-11/10/2023.

D. Secured Creditors' Protection During Insolvency in Ethiopia

As evident from the interviewees' responses and in line with international best practices, Ethiopian insolvency law is well-equipped to protect the interests of secured creditors during insolvency proceedings, employing the following legal strategies. First, the new Ethiopian insolvency law addressed the long-standing problem of private enforcement by banks as secured creditors. Previously, Proclamation No. 97/1998 allowed banks that lend with collateral to take over and sell the secured property via a public auction when the debtor defaults on the debt, even in cases of an insolvency procedure.[200]

By doing so, the foreclosure law allowed banks to take complete control of the property, which would otherwise be subject to an insolvency procedure that would significantly affect the interests of other secured and unsecured creditors.[201] Due to this, banks, as private parties enforcing their rights, were granted absolute power of foreclosure and priority over the encumbered assets, privately following informal procedures.[202]

The new Ethiopian insolvency law has addressed this issue during insolvency procedures by imposing the stay (upon complaint or automatically) principle, which is also applicable to banks' claims against the debtor.[203] However, after the opening of insolvency proceedings, the new law gives the insolvency representative six months to retain the collateral with the insolvent estate and decide whether to sell the encumbered asset, pay the bank the amount secured by the claim, or retain the property.[204]

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200. *Property Mortgaged or Pledged with Banks*, Articles 1-7, Proclamation No. 97/1998, (Eth.); *A Proclamation to Amend the Property Mortgaged or Pledged with Banks*, Proclamation No. 216/2000, (Eth.); Interview with Respondent Professor 1 (RP1), Professor, Senior Member, Amendment Committee of the Commercial Code of Ethiopia 2021 in Addis Ababa, 27-28/07/2023.

201. *Property Mortgaged of Pledged with Banks*, *supra* note 200; *A Proclamation to Amend the Property Mortgaged or Pledged with Banks*, *supra* note 200.

202. Interview with Respondent Professor 1 (RP1), Professor, Senior Member, Amendment Committee of the Commercial Code of Ethiopia 2021 in Addis Ababa, 27-28/07/2023. (PhD dissertation data, University of New England Austl.) (stored in a secure digital repository; available at https://rune.une.edu.au/).

203. Article 625(1-3) of the Commercial Code of Ethiopia (2021) imposes a complaint on a stay of claims. In addition, per articles 654-657 & 761(1-6), during a reorganization and liquidation procedure, the law imposes automatic stays on secured creditors' claims for a period of up to four months.

204. Commercial Code of Ethiopia, Articles 761(1-6), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

By doing so, the new law strikes a balance between private and public enforcement. It also resolved the entrenched problem of unilateralism in debt enforcement by replacing it with a collectively enforced insolvency procedure.[205] The law also guarantees that creditors' priority rights are paid ahead of other preferred and unsecured creditors during the final distribution of the debtor's assets.[206] It establishes the general priority ranking for the payment of other creditors. It excludes secured creditors from this ranking, as they are to be paid even before the ranking indicates that secured creditors are not subject to the *pari passu* principle.[207]

Additionally, the law preserves creditors' rights to claim interest on their secured claims until the date of the judgment opening the liquidation procedure.[208] The law also requires the insolvency representative, given their legal priority to liquidate the security, to obtain the consent of secured creditors before encumbered assets are sold as part of the sale of the business as a going concern. If the encumbered assets are sold, an equivalent amount shall be paid to such secured creditors.[209]

During a liquidation procedure, the law protects the rights of secured creditors in possession of the security to liquidate their security interest either directly or through the insolvency representative. Moreover, after the sale of their security, if the value of the sold property is insufficient to cover the entirety of their claims, the law also guarantees their rights to

205. Interview by Samuel Biresaw & Mia Rahim with Senior Judge, Ethiopian Federal High Court Insolvency Bench (May 25, 2023 - June 1, 2024) (PhD dissertation data, University of New England Austl.) (stored in a secure digital repository; available at https://rune.une.edu.au/).

206. Interview with Respondent Professor 1 (RP1), Professor, Senior Member, Amendment Committee of the Commercial Code of Ethiopia 2021 in Addis Ababa, 27-28/08/2023; Interview with Respondent Judge 2 (RJ2), Senior Judge, Ethiopian Federal First Instance Court in Addis Ababa, 19-20/06/2023.

207. Commercial Code of Ethiopia, Articles 785(1-2), 786(1-11), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Professor 3 (RP3), Professor, Addis Ababa University, in Addis Ababa, 22-23/08/2023.

208. Commercial Code of Ethiopia, Articles 763(1, 2), 764(1, 2), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Judge 2 (RJ2), Senior Judge, Ethiopian Federal First Instance Court in Addis Ababa, 19-20/06/2023; Interview with Respondent Professor 3 (RP3), Professor, Addis Ababa University, in Addis Ababa, 22-23/08/2023.

209. Commercial Code of Ethiopia, Articles 692(1-4), 761(3), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Judge 2 (RJ2), Senior Judge, Ethiopian Federal First Instance Court in Addis Ababa, 19-20/06/2023.

claim the unpaid amount to the extent of the insolvency estate as unsecured creditors.[210]

Given the very purpose of a liquidation procedure, the law guarantees the rights of all types of secured creditors to realize their security if the insolvency representative cannot sell such encumbered assets within six months after the judgment opening a liquidation procedure.[211] The law also recognizes the rank and priority of secured creditors in receiving payment.[212] When the insolvency representative distributes the proceeds from the sale of encumbered assets, the law obliges the insolvency representative, after deducting costs and expenses for realizing such encumbered assets, to prioritize paying creditors with security interests over these encumbered assets over other creditors. The law also guarantees the rights of secured creditors who have not been paid in full from the proceeds of the sold-encumbered assets to participate as unsecured creditors for the remaining unpaid amount.[213]

Where the security held by a creditor or his preferential rights against the debtor are contested by the insolvency representative, the law ascertains the rights of such secured creditor to participate in the proceeding as an unsecured creditor.[214] Similarly, when establishing classes of creditors, in all cases where secured creditors are not fully paid from the proceeds of the sale of encumbered assets to the extent of their unpaid amount, the law also guarantees the rights of secured creditors to join and participate in the class of unsecured creditors.[215]

Where the insolvency representative decides to sell and distribute the proceeds of unencumbered assets before those of encumbered assets, the law also guarantees the rights of verified and admitted secured creditors to participate as unsecured creditors to the extent of the total

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210. Commercial Code of Ethiopia, Article 761(4), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Professor 3 (RP3), Professor, Addis Ababa University in Addis Ababa, 22-23/08/2023.

211. Commercial Code of Ethiopia, Articles 751-754, 761(5-6), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Professor 1 (RP1, Professor, Senior Member, Amendment Committee of the Commercial Code of Ethiopia 2021, in Addis Ababa, 27-28/08/2023.

212. Commercial Code of Ethiopia, Articles 780(1-3), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Judge 2 (RJ2), Senior Judge, Ethiopian Federal First Instance Court, in Addis Ababa, 19-20/06/2023.

213. Commercial Code of Ethiopia, Articles 781(1, 2), 784(1, 2), 785(1, 2), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

214. *Id.* at Articles 669(1, 2).

215. *Id.* at Article 680(3).

amount of their claims.[216] Furthermore, the law recognizes and prioritizes existing (pre-insolvency) creditors' rights or entitlements before the commencement of insolvency procedures.[217]

Accordingly, the law defines and provides a well-structured method for submitting pre-insolvency claims, such as who can submit the claims, how and when to submit, the details of the claim, security or guarantee details, the rights of set-off attached to the claim, documents evidencing the claim, the consequences of failure to submit the claims within the stipulated time limit, exceptions to such claims, and the verification and admission of such claims.[218] Finally, the law recognizes and enforces the treatment of ongoing contracts during the debtor's insolvency.[219] Ongoing contracts are the primary source of pre-insolvency claims, and their treatment directly impacts creditors.

During the opening of insolvency procedures, the law ascertains the continuation of ongoing contracts. The law also provides detailed rules governing ongoing contracts, including the definition of ongoing contracts, opposition to ongoing contracts, termination of ongoing contracts, and the effects and exceptions of ongoing contracts.[220]

E. The Use of Optional Insolvency Procedures in Ethiopia

Ethiopian insolvency law is also well-equipped with the following legal strategies designed to balance and provide options for both rehabilitation and liquidation procedures to resolve the debtor's affairs efficiently. Primarily, the law recognizes three modern procedures as options for administering the debtor's insolvency.[221] These procedures are

216. *Id.* at Articles 782, 783(1, 2).

217. Interview with Respondent Judge 2 (RJ2), Senior Judge, Ethiopian Federal First Instance Court in Addis Ababa, 19-20/06/2023; Interview with Respondent Lawyer 1 (RL1), Senior Lawyer, Practicing in Ethiopian Federal Courts in Addis Ababa, 11-12/09/2023.

218. Commercial Code of Ethiopia, Articles 592(1, 3), 603(1, 2), 606(1, 2), 654(1-3), 655(1-5), 656(1, 2), 657(1-3), 662(1-5), 664-675, 761(1-6), 764-774, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Lawyer 2 (RL2), Senior Lawyer, Practicing in Ethiopian Federal Courts in Addis Ababa, 25-26/09/ 2023.

219. Interview with Respondent Judge 2 (RJ2), Senior Judge, Ethiopian Federal First Instance Court in Addis Ababa, 19-20/06/2023; Interview with Respondent Lawyer 1 (RL1), Senior Lawyer, Practicing in Ethiopian Federal Courts, in Addis Ababa, 11-12/09/2023.

220. Commercial Code of Ethiopia, Articles 593(1-7), 592(2-3), 594-596, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Professor 3 (RP3), Professor, Addis Ababa University, in Addis Ababa, 22-23/08/2023.

221. Interview with Respondent Lawyer 1 (RL1), Senior Lawyer, Practicing in Ethiopian Federal Courts, 11-12/09/2023.

preventive restructuring, reorganization, and liquidation.[222] By using three different types of procedures that use various strategies and have different aims in resolving the debtor's affairs, the law provides the parties a comprehensive option to follow a procedure that is destined to either rehabilitate or liquidate the debtor's affairs, which, depending on the circumstances of the case and given their interests, empowers the parties to adopt the most productive insolvency procedure to deal with the debtor's affairs.[223]

The law also clearly stipulates the general goals of all procedures and the specific goals of each, designed to protect the interests of the involved parties.[224] Out of the three recognized insolvency procedures dealing with the affairs of an insolvent debtor, two of them (preventive restructuring and reorganization) have the general objective of restructuring or rehabilitating the debtor's assets and preventing the liquidation of a viable business, which indicates that two-thirds of the provisions of Ethiopian insolvency law are dedicated to rehabilitating the affairs of the debtor's business. In contrast, only one-third of the provisions address liquidation procedures.[225]

The overarching objectives of restructuring and reorganization procedures in Ethiopia are to restructure the debts of the debtor or to reorganize viable businesses by using various strategies, including the sale of the business as a going concern, to assure the continuation of the business, to maximize the productivity or value of the debtor's assets, and to liquidate unviable businesses only.[226] In contrast, the primary objective of a liquidation procedure is to efficiently liquidate and distribute the debtor's remaining assets to creditors.[227]

In addition to the main procedures discussed above, to encourage efficiency and productivity in the interests of the parties, provided that the associated requirements are met, the law recognizes and enforces the

222. Commercial Code of Ethiopia, Articles 588(1-4), 591(1-5), 617, 635, 705(1, 2), 618(1, 2), 630(1, 2), 628, 631, 638(1, 2), 639 (1, 2), 640(1-3), 651 (1-4), 659 (1), 697(1-8), 700-704, 816-825, 820-821, 706(1), 711(1-3), 712 (1), 722(1,2), 629(2-b), 685(3), 700 (1, 2), 617-634, 680-688, 635-704, 705, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

223. *Id.* at Articles 588-616, 617-704, and 705-825 of the Commercial Code of Ethiopia 2021; Interview with Respondent Professor 2 (RP2), Senior Professor, Addis Ababa University, in Addis Ababa, 03-04/08/2023.

224. Commercial Code of Ethiopia, Articles 588(1-4), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

225. *Id.* at Articles 617-634 (Preventive Restructuring), 635-704 (Reorganization), 705-825 (Liquidation).

226. *Id.* at Articles 617-704.

227. *Id.* at Articles 705-825.

opening of expedited procedures for dealing with the affairs of an insolvent debtor.[228] The court can initiate expedited reorganization and liquidation procedures under specific circumstances.[229]

Another critical strategy is the prohibition of the parallel opening of any recognized procedures.[230] This is because each procedure has different goals when dealing with the debtor's insolvency. The simultaneous pursuit of these opposing goals renders insolvency procedures futile and unproductive. For example, the debtor cannot rehabilitate his business if his assets are simultaneously liquidated (sold) under a liquidation procedure. Hence, the law prohibits the simultaneous opening of any two procedures.[231]

Additionally, the law empowers the court to prohibit or reject any activity or scheme under any of the recognized insolvency procedures (such as the restructuring plan, the reorganization plan, sale of the business as a going concern, new financing, the takeover plan, compromise or settlement, stay of proceedings, affixing of seals, or observation period) whose continuity or operation does not contribute to the rehabilitation of the debtor's business or maximize his assets or prevent liquidation of the debtor's business.[232]

Another strategy employed by the law is to balance rehabilitation with liquidation is allowing for the conversion of unsuccessful procedures (such as restructuring, reorganization, simplified reorganization procedures, procedures to sell the business as a going concern, or simplified liquidation and reorganization procedures) into more productive and suitable procedures designed to rehabilitate the debtor's assets and increase productivity.[233] The law also mandates the rescue of

228. Interview with Respondent Lawyer 1 (RL1), Senior Lawyer, Practicing in Ethiopian Federal Courts in Addis Ababa, 11-12/09/2023.

229. Commercial Code of Ethiopia, Articles 673, 700-704 (simplified reorganization procedure), 816-825 (simplified liquidation procedure) Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Civil Procedure Code of Ethiopia 1965, Articles 284-292 (summary procedure), 300-314 (accelerated procedure) Decree No. 52/1965, Year 1965.

230. Interview with Respondent Lawyer 1 (RL1), Senior Lawyer Practicing in Ethiopian Federal Courts in Addis Ababa, 11-12/09/2023; Interview with Respondent Professor 2 (RP2), Senior Professor, Addis Ababa University, in Addis Ababa, 03-04/08/2023.

231. Commercial Code of Ethiopia, Articles 635(1(b)), 618(3), 632(2), 705(2), 744, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

232. *Id.* at Articles 617, 627-633, 678-695, 735, 742, 744-750; Interview with Respondent Lawyer 1 (RL1), Senior Lawyer, Practicing in Ethiopian Federal Courts in Addis Ababa, 11-12/09/2023.

233. Commercial Code of Ethiopia, Articles 632(1-4), 634(1-3), 698, 704(1-3), 705, 794-798, 821-825, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with

only efficient and potentially viable businesses through restructuring or reorganization procedures while liquidating non-viable and inefficient businesses. This approach also involves resolving the debtor's affairs in a timely and orderly manner with minimal disruption.[234]

Furthemore, the law also establishes a clear priority and order of importance among the three recognized procedures, as is evident from the structural arrangement of the provisions in Ethiopian insolvency law.[235] Accordingly, the law prioritizes a restructuring procedure when the debtor is still solvent or on the verge of suspending payment. In agreement with creditors, the restructuring procedure aims to restructure the debtor's debts to prevent the debtor from becoming insolvent.[236] The law provides involved parties the chance to prevent the debtor's insolvency and the associated risks via the instrumentality of a preventive restructuring procedure, which, based on the principles of freedom of contract and party autonomy, provides a contractual mechanism for the parties to renegotiate a debt repayment plan without the need to pass through the cumbersome, lengthy, and costly insolvency procedures.[237] Accordingly, the first title (Title Two) of Book Three of the law deals with a restructuring procedure.[238]

However, when a restructuring procedure is not feasible or unsuccessful for various reasons, the law gives second priority to a reorganization procedure. A reorganization procedure aims to rehabilitate the debtor's affairs in agreement with creditors on the verge of insolvency or who have already been insolvent for less than forty-five days.[239] The second title (Title Three) of Book Three of the law deals with a reorganization procedure.[240] Where a reorganization procedure is infeasible or unsuccessful, the law authorizes the court to resolve the debtor's affairs through the instrumentality of a liquidation procedure,

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Respondent Lawyer 1 (RL1), Senior Lawyer, Practicing in Ethiopian Federal Courts in Addis Ababa, 11-12/09/2023; Interview with Respondent Lawyer 3 (RL3), Senior Lawyer, Practicing in Ethiopian Federal Courts in Addis Ababa, 10-11/10/2023.

234. Commercial Code of Ethiopia, Articles 629(2-b), 685(3), 700(1, 2), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Lawyer 1 (RL1), Senior Lawyer, Practicing in Ethiopian Federal Courts in Addis Ababa, 11-12/10/2023.

235. Book 3 of the Commercial Code of Ethiopia 2021; Interview with Respondent Lawyer 1 (RL1), Senior Lawyer, Practicing in Ethiopian Federal Courts in Addis Ababa, 11-12/09/2023.

236. Commercial Code of Ethiopia, Article 617, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

237. *Id.* at Articles 588-616.

238. *Id.* at Articles 617-634.

239. *Id.* at Articles 680-688.

240. *Id.* at Articles 635-704.

which targets the liquidation and distribution of the debtor's remaining assets to creditors.[241] The last title (Title Four) of Book Three of the law deals with a liquidation procedure as a last-resort mechanism to resolve the debtor's insolvency.[242]

The final strategy the law utilizes to guarantee the optional use of the procedures involves the various requirements stipulated to trigger each procedure. Interested parties can initiate restructuring and reorganization procedures if they are still solvent or have been insolvent for less than forty-five days, facing a foreseeable financial difficulty.[243]

On the contrary, if the debtor is already insolvent (i.e., in suspension of payments) or has been insolvent for at least forty-five days, the law presumes that the business is unlikely to survive through restructuring or reorganization procedures. Instead, the law encourages such debtors to initiate a liquidation procedure, which is a testament to the law's commitment to liquidating non-viable or inefficient businesses.[244]

F. The Fair Treatment of Creditors' Interests During Insolvency in Ethiopia

Ethiopian insolvency law is also well-equipped with various legal strategies designed to accord equitable treatment to creditors. Primarily, the law equitably guarantees various procedural rights of creditors, such as initiating procedures, voting or approving plans, and submitting and verifying their claims.[245] Accordingly, the law guarantees the rights of various parties (such as the debtor, creditors, and public prosecutor) to initiate various insolvency procedures. It encourages them to use insolvency law to resolve the debtor's financial difficulties. Although the law does not permit creditors to initiate a preventive restructuring procedure, it guarantees creditors' rights to initiate both reorganization and liquidation procedures.[246] The law also guarantees creditors' rights,

241. *Id.* at Articles 680-688, 705.

242. *Id.* at Articles 705-825.

243. *Id.* at Articles 617, 635; Interview with Respondent Lawyer 1 (RL1), Senior Lawyer, Practicing in the Ethiopian Federal High Court, in Addis Ababa, 11-12/09/2023.

244. Commercial Code of Ethiopia, Articles 705, 627-633, 638-640, 680-688, 697-698, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

245. Interview with Respondent Judge 3 (RJ3), Senior Judge, Ethiopian Federal High Court in Addis Ababa, 12-13/07/2023; Interview with Respondent Professor 2 (RP2), Professor, Addis Ababa University, in Addis Ababa, 03-04/08/2023.

246. Commercial Code of Ethiopia, Articles 635, 617-619, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

whose claims against the debtor are due and payable, to initiate a liquidation procedure.[247]

The fact that the law does not stipulate additional qualification requirements for creditors to take advantage of their rights to initiate the procedures, such as the amount of claim or minimum number of creditors to apply for commencement and so on, encourages all creditors who have claims against the debtor, regardless of the claim's amount or the number of creditors, to apply for the commencement of the relevant procedures.[248] The right to initiate procedures empowers creditors to protect their interests by immediately applying for the most suitable insolvency procedure against the debtor, considering the debtor's circumstances. It also encourages them to discourage hostile or recalcitrant debtors from depleting the remaining assets or diverting or transferring value away from the estate by engaging in fraudulent or preferential transactions in bad faith.

Additionally, the law imposes a duty on creditors to submit their claims and security interests and ensure their claims' verification by the insolvency representative, which enables them to legally substantiate their claim and participate in the distribution of the proceeds of sale as lawful claimants.[249] The law also guarantees creditors the right to participate in the preparation of restructuring and reorganization plans (either directly or indirectly), to approve or accept the plan (or to reject or propose their own plan), and to appeal or oppose the plan after the court confirms it.[250] This enables creditors to defend their mutual interests by supporting and encouraging schemes that protect them and oppose and avoid activities detrimental to their interests.[251]

Once creditors approve the plan, the law requires the court to approve the reorganization plan, among others, after verifying that the necessary majority of the creditors has approved the plan, that there is a reasonable prospect of preventing the debtor's insolvency, assuring the

247. *Id.* at Articles 635(1(b, c)), 705(4(b)).

248. *Id.* at Articles 635, 637(4(a-d)),705 (1-7) 636-637, 635(1,2), 705(4(d)).

249. *Id.* at Articles 662-670; Interview with Respondent Judge 3 (RJ3), Senior Judge, Lideta Branch of the Ethiopian Federal High Court in Addis Ababa, 12-13/08/2023.

250. Interview with Respondent Professor 1 (RP1), Professor, Senior Member, Amendment Committee of the Commercial Code of Ethiopia 2021 in Addis Ababa, 27-28/07/2023.

251. Commercial Code of Ethiopia, Articles 627-633, 639-640, 678(1, 2), 772-774, 768-770, 680-682, 684, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23; Interview with Respondent Professor 2 (RP2), Senior Professor, Addis Ababa University, in Addis Ababa, 03-04/08/2023.

debtor's business, that creditors with the same rank receive the same satisfaction of their claims, and that the plan complies with the "best-interest-of-creditors test."[252]

The law also gives creditors the right to approve the sale of the business as a going concern. To protect creditors' interests, ensure business continuity and productivity, and maximize the value of the business, in cases where the sale of the business is a going concern, the law obliges the court to verify that creditors have not adopted a reorganization plan and the winning bidder's business plan has a reasonable prospect of assuring the viability of the business.[253]

The law guarantees the equitable rights of creditors of the same class to participate in and vote at their class meeting or the creditors' general meeting.[254] For example, during a reorganization, to ensure equitable representation, participation, and voting by creditors, the law requires the insolvency representative to ensure that the voting rights of creditors in classes and at general creditors' meetings correspond to the principal amount of their pre-insolvency claims.[255]

Additionally, the law recognizes different classes of creditors that reflect a sufficient commonality of interest based on objectively verifiable criteria, and to ensure equal treatment for the members of each class under the *pari passu* principle.[256] Moreover, the law requires the insolvency representative to assign creditors with different types of claims or interests to separate classes, ensuring equitable treatment. For example, principal, secured, privileged, and unsecured creditors shall be treated in separate classes.[257]

Moreover, the law also outlines the principle of payment distribution.[258] It stipulates that creditors shall be paid on a *pro rata* or *pari passu* basis, based on the admitted claims, where the total amount to be

252. Commercial Code of Ethiopia, Articles 685(1-5), 686-688, Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

253. *Id.* at Articles 683, 689(1-6), 690-695.

254. *Id.* at Articles 683-695; Interview with Respondent Judge 3 (RJ3), Senior Judge, Ethiopian Federal High Court in Addis Ababa, 12-13/07/2023.

255. Commercial Code of Ethiopia, Article 681(2), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

256. *Id.* at Articles 606(6), 678(4, 5), 680(1-9), 685(1-5); Interview with Respondent Judge 3 (RJ3), Senior Judge, Ethiopian Federal High Court in Addis Ababa, 12-13/07/2023.

257. Commercial Code of Ethiopia, Articles 680(2-6), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

258. Interview with Respondent Professor 1 (RP1), Professor, Senior Member, Amendment Committee of the Commercial Code of Ethiopia 2021, in Addis Ababa, 27-28/07/2023.

paid is insufficient to fully satisfy the claims of creditors belonging to the same class of rank. By doing so, the law protects the interests of creditors by guaranteeing their rights to equitably participate in the distribution of the debtor's net assets. It ensures equitable treatment of creditors of the same class.[259] For example, during a reorganization procedure, once the reorganization plan has been accepted by the required majority of each class of creditors, the court shall approve the plan. However, in due course, the law requires the court to verify that under the plan, classes of creditors with the same rank shall receive the same or equivalent satisfaction of their claims.[260]

In addition to defining the distribution rules among creditors of the same class based on the outlined ranking criteria, the law also sets out the general distribution rule and the priority of payment among different classes of creditors. It states that where the total amount of money subject to the final distribution among creditors is insufficient to fully satisfy their claims, lower-ranking creditors shall not be paid until all higher-ranking creditors are fully paid.[261]

Subsequently, the law defines the general creditors' ranking priorities during the distribution of payments.[262] After encumbered assets are fully realized by secured creditors and their claims are fully paid, the law requires insolvency representatives to follow a predetermined priority ranking system to distribute the remaining proceeds of the realization among the remaining creditors, including both preferred and unsecured creditors.[263]

Other creditors shall be paid based on the following ranking of priorities: costs and expenses of the proceedings; new financing in the context of preventive restructuring; new financing in the context of reorganization; new financing authorized in the context of bankruptcy; post-bankruptcy creditors, including creditors of new and ongoing contracts; employee claims and claims of social security authorities; taxes and duties owed to federal, regional, and local government authorities, other than those which can be claimed from the debtor holding taxes and

259. Commercial Code of Ethiopia, Article 789(1), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

260. *Id.* at Articles 685(3(f)), 680-688.

261. *Id.* at Article 789(2).

262. *Id.* at Article 786; Interview with Respondent Professor 1 (RP1), Professor, Senior Member, Amendment Committee of the Commercial Code of Ethiopia 2021, in Addis Ababa, 27-28/07/2023.

263. . Commercial Code of Ethiopia, Article 786(1-11), Proclamation No. 1243, Negarit Gazette, Year 2021, No. 23.

duties on behalf of the government (but excluding interest and penalties); amounts ordered for the maintenance of the bankrupt debtor and his family; other preferred creditors; unsecured creditors; and penalties and fines imposed upon the debtor.[264]

In all cases where the remaining assets of the debtor are insufficient to pay the claims of all creditors, the use of a predetermined ranking of creditors' claims enables the insolvency representatives to distribute the remaining proceeds amicably, orderly, efficiently, and fairly, which is still highly beneficial for creditors to recover at least parts of their claims. Based on the ranking system, the law requires that, during insolvency proceedings, where the court has approved post-commencement financing, the claims of post-commencement creditors who extended the new financing shall have priority over the claims of existing unsecured creditors in the event of the subsequent opening of bankruptcy proceedings.[265]

Considering the importance of new finance for the continuation of the debtor's business, the law encourages creditors to extend finance to the debtor even after they are aware of the insolvency, by ensuring that post-commencement creditors are paid ahead of ordinary creditors.

VI. CONCLUSION

The relevant literature is adequate in showing that insolvency law is one of the mechanisms to protect creditors' interests as a last resort. Building on the existing doctrinal and empirical studies, this study examines whether the new Ethiopian insolvency regime effectively protects creditors' interests during insolvency, utilizing six variables (themes) identified in accordance with international best practices and a reflexive thematic analysis of interview data.

The study reveals that Ethiopia's new insolvency regime is creditor-friendly. The doctrinal analysis of the law in relation to global benchmarks, along with the RTA of the qualitative data, reveals that the law adequately guarantees creditors' protection rights. It is well-equipped with tools and strategies to protect creditors' interests holistically during insolvency. The law also adequately guarantees various creditor rights to protect their interests during insolvency. Not only does the law contain adequate rules for all the variables used in this study as benchmarks, but it also provides detailed guidelines for their effective implementation.

264. *Id.*

265. *Id.* at Articles 628(1), 679(2).

Among others, in line with the international benchmarks and the results of the thematic analysis, to ensure the protection of creditors' rights during insolvency or when insolvency is imminent, the law imposes duties on directors to consider creditors' interests; prohibits avoidance transactions; punishes illegalities during the procedures; ensures the preservation of the debtor's assets, ensures creditors' participation and information rights; accords equitable treatment to unsecured creditors; ensures the procedural rights of creditors; protects secured creditors' interests; protects the pre-insolvency rights of creditors; recognizes ongoing contracts; provides rehabilitation, liquidation, and summary procedures as optional procedures to resolve the debtor's affairs; and adopted the creditors' best interests test as one of its pillar principles.

As evident from international best practices and the thematic analysis results, the identified variables are typical tools for comprehensively protecting creditors' interests during insolvency or when insolvency is imminent. Additionally, the study shows that the new law has significantly improved and addressed the deficiencies of the old Ethiopian insolvency law in providing adequate protection for creditors' interests. Unlike the old law, the new law also includes modern rules, principles, and procedures for insolvency, which are crucial for protecting creditors' interests.

It is also evident that the new law, in detail, addresses the general and specific aims of insolvency procedures in Ethiopia, with the overarching aim of protecting creditors' interests. The new law is also well-equipped with the necessary tools to achieve its objectives. Most importantly, this study also demonstrates that creditors' protection rights in Ethiopian insolvency law align with the relevant international guidelines and global best practices. However, to protect creditors' interests, the parties should use the law and the procedures outlined in it, and the courts should apply these as tools to resolve the debtor's insolvency. The law is not self-enforcing. No matter how well a law may be crafted, it will not achieve its intended goals or resolve practical problems unless it is meaningfully applied, rendering it ineffective otherwise.

Although the new Ethiopian insolvency regime is modern and well-equipped with the needed tools to protect creditors' interests, creditors' interests can only be protected if the law is applied correctly. It is evident from the collected data that Ethiopia has a long-standing, entrenched problem with the deficient application of insolvency law. A problem that remained unabated after a century of insolvency legal reform. Collected data indicate that, although there are several justifications for the lack of

practice, the primary reason is the deficiency of the existing institutional framework for insolvency enforcement.

To effectively protect creditors' interests, based on the comprehensive creditor protection rights outlined in the law, a necessary institutional framework should be established and periodic reforms implemented to ensure ongoing protection. Moreover, the government, courts, insolvency practitioners, commercial community, and other insolvency stakeholders in Ethiopia are required to encourage parties and practitioners to utilize the law as a tool to resolve the affairs of financially distressed debtors. To alleviate this problem, the current situation of the practical application of Ethiopia's new insolvency regime and its impact on creditors' interests needs to be studied.

Finally, it is recommended that the government continue to reform the law to further improve the country's insolvency legal framework and sign the relevant international conventions on domestic or cross-border insolvency law, which have substantial implications for the protection of the domestic and cross-border interests of Ethiopian and foreign creditors.