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Statutory Corporate Insolvency Procedures in Tanzania

Introduction

This paper reviews statutory corporate insolvency procedures in Tanzania. The paper discusses in-court procedures as opposed to out-of-court aka workout procedures. Tanzanian corporate insolvency law is mainly contained in the Companies Act that came into force on 01 March 2006. This Act is supplemented by Insolvency Regulations, 2005. Apart from the Companies Act, there are special procedures provided for banks and insurance companies under the Banking and Financial Institutions Act, 2006 and Insurance Act, 1996 respectively. Furthermore, there are special procedures for cooperatives, non-governmental organizations, trusts and societies. Since these are not companies, insolvency procedures are not governing these entities are not discussed in this paper. Statutory corporate insolvency procedures under the Tanzanian law include the process of appointing 'receiver and manager' and 'administrative receiver', 'company voluntary arrangement', 'schemes of arrangement; 'administration' and winding-up by the court'. The primary objective of administrative receiver, company voluntary arrangement, schemes of arrangement and administration is to restructure the business with a view to making it to survive as a going concern. The primary objective of liquidation and receiver and manager procedures is to collect debts. These procedures are reviewed below. In this paper, the word receiver refers to administrative receiver and non-administrative receiver (receiver and manager).

(i) Receiver and Manager (sections 405 to 415 of the Companies Act)

Receiver and manager can be appointed by a creditor under the terms of the debenture which normally contain a mixture of fixed and floating charges. A debenture is a contract that is entered into by a company or debtor and the creditor or debenture-holder. Under the debenture, the creditor is given proprietary interest over the company's assets by way of security. According to Lord Hoffman in English case of *Re Bank of Credit and Commerce International S.A. (No. 8)*, proprietary interests 'confer rights in rem which, subject to questions of registration and equitable doctrine of purchaser for value without notice, will be binding upon third parties and unaffected by the insolvency of the owner of the property charged'. Proprietary interest provided by way of security entitles the creditor to resort to company property for the purpose of satisfying liability due to him and the owner of the property retains an equity of redemption to have to have the property restored to him when liability has been discharged. Proprietary interest is created without any transfer of title or possession to the beneficiary. In the absence of a provision to the contrary, a debenture is freely assignable.

The debenture must be registered with the Registrar of Companies within forty two days (section 96 of the Companies Act) from the date of its creation. Apart from non-registration, a debenture may be invalid on other grounds such as lack of the capacity on the part of the company to enter into the charge, lack of authority on the part of the directors to execute the charge, abuse of power or conflict of interest by the directors in granting the charge, defect of form, etc. The debenture may enable the appointment of receivers to be made at any time, on the happening of a specified event or on occasion of the default by the company. The burden is upon the debenture-holder and receiver to prove that the power of appointment has become exercisable. An appointment for wrong reason will be invalid if a correct ground to justify non-appointment existed at the time of appointment. If the power to appoint a receiver and manager has become exercisable, the creditor owes no duty of care to the company or to its unsecured creditors or to any guarantor in deciding whether to exercise it, provided that creditor is acting in good faith. A receiver must be appointed in accordance with the terms of the debenture. An instrument of appointment may be executed in anticipation of a default and subsequent use.

A debenture in the ordinary case provides for the appointment by the creditor, on the occasion of any default by the debtor or the occurrence of specified events, of a receiver with power to carry on the company's business. The appointment takes the management of the company's property out of the hands of the directors and places it in the hands of the receiver. This power may be exercised either with a view to reviving the company or with a view to the beneficial sale of the undertaking as a going concern. The power to carry on the business of the company through an administrative receiver is deemed to be granted by the debenture except in so far as the existence of such power is inconsistent with any provision of the debenture. The power to present or defend a petition to wind up the company is likewise deemed to be granted, and if properly exercised must preclude any representation of the company at instance of the directors. A receiver and manager will only have such powers if conferred by the debenture and the appointment of a receiver in no way precludes other creditors petitioning for winding up, and, indeed unsecured creditors may be well advised to petition to protect their position in case a surplus exists after completion of the receivership. The appointment does not prevent time running purposes of limitations and the liquidator may exercise some supervision and restraining influence on the receiver. In the case of a floating charge, the creditor has the choice either to make the appointment. Once the appointment is made, it is for the receiver to decide whether to carry on the business with the objective of a rescue in the long term or of a beneficial sale as a going concern in the short term or to close the business and sell up. There is no general duty on the creditor or the receiver to carry on business on the mortgaged premises in order to safeguard the company's goodwill or to procure the most beneficial realization, If

the receiver does continue the company's business, five limitations on his freedom of action come into operation:

- First, the receiver will ordinarily be granted power and authority to carry on the company's business as agent of the company. But though the power to carry on the business survives liquidation, the agency does not.
- Secondly, the provisions of section 383 of the Companies Act will apply to the receiver in respect of the period of his carrying on business as agent for the company prior to liquidation, and accordingly if he is a party to fraudulent trading, he may be subject to a claim in a subsequent liquidation. The wrongful trading provisions of section 384 of the Companies Act may also apply to him if he exercises real influence over the trading affairs.
- Thirdly, in respect of certain aspects of his conduct, he owes duties to the company and may be held liable in negligence or for acts which damage the company.
- Fourthly, the directors' powers of management of the undertaking are placed in suspense during the period of his appointment in so far as their exercise would be inconsistent with the exercise by the receiver of powers conferred on the debenture-holder under his debenture. There is no kind of diarchy over the company's assets: the board of directors has no power over assets in the possession or control of the receiver. The directors remain in office and their powers remain exercisable so far as they are not incompatible with the right of the receiver to exercise the powers conferred on him.
- Fifthly, as soon as the debenture holder and preferential creditors and all receivership costs, liabilities and expenses are or can be paid off, the receiver must in the absence of any provision to the contrary in the debenture cease to act and hand back to the directors the powers of management.

(ii) Administrative Receiver (sections 416 to 423 of the Companies Act)

Administrative Receiver is described under section 405 (c) of the Companies Act (i) as a receiver and manager of the *whole or substantially the whole of a company's property* appointed by or on behalf of the holders of any debentures of the company secured by a charge which, as created, was a floating charge, or by such a charge and one or more other securities, or (ii) a person who would be such a receiver or manager but for the appointment of some other person as the receiver of part of the company's property. The concept of administrative receiver was created with a view to give special status to a receiver and manager appointed over the whole or substantially the whole of the company's property. Unlike

receiver and manager whose primary objective is to collect debts, the statutory objective of the administrative receiver is to enable the business to be sold as a going concern. Due to this reason, the administrative receiver is given broad powers to facilitate the objective of ensuring that a financially troubled company survives as a going concern.

Whether or not an appointee is administrative receiver is a question of law. The major distinctions between the administrative receiver and receiver and manager is that (i) the appointment of receiver and manager does not preclude the appointment of an administrator; (ii) receiver and manager does not enjoy privileges and investigatory powers given under the Companies Act to an administrative receiver; (iii) receiver and manager's powers are strictly limited to those conferred by the debenture and are not deemed to be extended unless the contrary intention appears; (iv) a person dealing with receiver and manager, even if acting in good faith and for value, must inquire whether the receiver and manager is acting within his powers and whether there has been any defect in his appointment, nomination or qualifications; (v) receiver and manager is strictly liable to third parties if he seizes or disposes of their property, notwithstanding the absence of negligence and the existence of reasonable grounds for believing (as well as actual belief) that he is entitled to seize or dispose of the property; (vi) there is no statutory bar on the removal and replacement of a receiver and manager by his appointor at any time; and (viii) receiver and manager does not need to act as an insolvency practitioner in relation to the company.

(iii) Company Voluntary Arrangements (sections 240 to 246 of the Companies Act)

A company voluntary arrangement is one of the new forms of insolvency procedures that were introduced in Tanzania in March 2006. The voluntary arrangements apply to any composition in satisfaction of debts or to a scheme of arrangement of company's affairs. The purpose of the arrangement is to enable a scheme to be effected with minimal involvement by the court. The principal feature of this procedure is that a voluntary arrangement must be voted upon by creditors must be reviewed, endorsed and administered by an insolvency practitioner. The voluntary arrangement cannot affect the rights of secured creditors without their consent. The voluntary arrangement may be proposed independently of, or pursuant to, an administration orders or in liquidation. A proposal can be formulated by the directors if the company is not in administration or liquidation or by the administrator or liquidator if it is, and is voted upon by meetings of the company and its creditors. If accepted at the respective meetings, the arrangement will become binding upon all persons who in accordance with the rules had notice of, and were entitled to vote at, the

meeting as if they were parties to the voluntary arrangement. This raises a statutory hypothesis that the creditor was a party to the arrangement as if he had consented to it. A person entitled to vote at the meeting is entitled to challenge a decision made at the creditors' meeting by application made to the court within 28 days of the outcome of the meetings being reported to the court, and the court has the power to revoke or suspend the approvals and/or give a direction for the summoning of further meetings.

If approved, the voluntary arrangement is thereafter administered by a supervisor who must be a qualified insolvency practitioner. The supervisor is not an officer of the company and has no power to act in the name of the company unless is given authority to do so pursuant to the terms of the voluntary arrangement. The supervisor is subject to the supervisory control of the court, and both he and creditors who are dissatisfied with any act, decision or omission can apply to the court for direction. The Companies Act contains no provision enabling a voluntary arrangement to be amended or varied, whether by vote of or on an application to the court for direction. It is therefore important to include a provision permitting amendments to be made in the scheme itself. The voluntary arrangement will end upon the making of a winding up order on a petition by the supervisor.

(iv) Schemes of Arrangement (sections 229 to 232)

As an alternative to a company voluntary arrangement, is possible for a scheme of arrangement to be promoted and sanctioned under sections 229 to 232 of the Companies Act. Section 229 provides that if a compromise or arrangement is proposed between a company and its members or creditors, or any class of them, is approved by a majority in number representing 75 per cent in value of those present in person or by proxy at meetings of each class of member or creditor, and is subsequently sanctioned by the court, it shall be binding upon all members or creditors, or upon the class of members or creditors, and upon the company. Where a scheme involves a reduction of capital, the statutory provisions in that regard must also be complied with. The concept of a compromise or arrangement is a subject to wide control by the court. Not only will the court decides whether the relevant class meetings have been held and the procedures properly followed but also will check if full and accurate information has been given to members and creditors it will also decide whether the proposal is such that an intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve. This is an obvious difference to the court's role in relation to a company voluntary arrangement, which, in the absence of challenge from dissident creditors, is far more administrative in nature.

(v) Administration Orders (sections 247 to 266)

This a new corporate insolvency procedure introduced for the first time in Tanzania in March 2006. It is a court sanctioned corporate restructuring procedure equivalent to Chapter 11 of United States Bankruptcy Code and administration procedure under the United Kingdom Insolvency Act, 1986. The Companies Act prescribes a number of purposes for which the order can be sought, and there must be an expectation that the order will achieve one or more of them. The purposes are (a) the survival of the debtor company (and the or any of any part of its undertaking) as a going concern; (b) the approval of a compromise or arrangement under sections 229 of the Companies Act or a scheme ; and (c) a more advantageous realization of the debtor's assets that would be effected on a winding up. The order will be granted if the court considers that it would be likely to achieve one or more of the purpose specified in the petition and that the debtor is or is likely to become unable to pay its debts. Insolvency for the purpose of administration orders means not merely inability to pay debts as they accrue due, but also a deficiency of assets in relation to liabilities. Administration is intended to be only an interim and temporary regime which is not to remain in force for a long time and which is designed to revive, and to seek the continued life of the company if at all possible.

If the applicant satisfies the court that there is a real prospects that one or more of the stated purposes may be achieved, the court has a discretion to order a period under the administrator to set the affairs of the company in order, to reorganize and repay its debts or dispose of its business or assets for the benefit of creditors. Though it is convenient to describe the breathing space afforded to the company as a moratorium, there is no authorization to the company to postpone payment of its debts or discharge of its liabilities, but merely a limited immunity granted to the company against the enforcement of a number of legal rights and remedies without the leave of the court or the consent of the administrator. If the court is satisfied that there is a real prospect of an administration order achieving one of the statutory purposes, it may make an administration order despite the opposition of more than half in value of the creditor. Whilst the appointment of a receiver (administrative or receiver and manager) can co-exist with that of a liquidator, the appointment of an administrator cannot co-exist with the appointment of an administrative receiver or liquidator. The court cannot appoint an administrator if there is an administrative receiver in office without the consent of his appointor, unless it is satisfied that the bases under which the receiver was appointed could be challenged on specified grounds. Once an administrator is appointed, no administrative receiver can be appointed throughout the administrator's period in office.

The administrator has extensive statutory powers and has power to continue the company's business as agent for the company. He is given power to appoint and dismiss the directors, and any powers of the directors which might interfere with the exercise by the administrator of his powers are exercisable only with his permission once the administrator has fulfilled his role, or his role ceases to be capable of fulfillment. His appointment will be terminated by order of the court, and either the board of directors (as reconstituted) will regain full power or the company will be wound up.

There are four substantial limitations on the effectiveness of the administration procedure. First, there is no power to appoint a provisional administrator although an interim manager may be appointed. Secondly, the administrator cannot be appointed against the wishes of a debenture holder if there is a floating charge under which the debenture-holder has appointed an administrative receiver. Thirdly, the jurisdiction is not exercisable in respect of a company which has already gone into liquidation. Fourthly, the moratorium is of a strictly limited character.

(vi) Liquidation (sections 274 to 404)

Liquidation is a process by which life of a company is brought to an end and its property administered for the benefit of its members and creditors. Liquidation or winding-up (the two terms mean the same) begins either by court order (compulsory liquidation) or by members passing a resolution to wind-up.

If a company is insolvent, either in the absolute ("balance sheet") sense, or in the sense of being unable to meet its liabilities as they fall due, the winding up procedure will in most cases be resorted to as the means of bringing about its orderly liquidation and dissolution. Where the company is experiencing a liquidity crisis which is demonstrably of a temporary nature, it may prove possible to avoid liquidation by means of a voluntary arrangement described. The law offers two separate modes of winding up procedure, namely voluntary or compulsory winding-up. The later form is known technically as "winding up by the court." In fact, the two forms of winding up are applicable to solvent as well as to insolvent companies. In most respects, the procedure to be followed is the same, irrespective of whether the company is solvent or not. However, in the case of a voluntary winding up of a solvent company, the reality of the members' ultimate interest is the return of their invested capital. In the first instance however the initiative and timing of the resort to a voluntary liquidation rests with the company, and in particular with those capable of controlling the official conduct of the company's affairs.

The voluntary winding-up procedure commences with the passing of a resolution at a duly convened company meeting, to the effect that the company be wound up voluntarily. If the company is insolvent it will not be possible for the directors to make a statutory declaration of the company's solvency, and in the absence of such a declaration the winding up will take the form of a creditors' voluntary winding up. The winding up will be conducted by a liquidator appointed from the private sector whose appointment is accomplished through resolutions passed at meetings of the company itself, and of the company's creditors. The dominant role in the appointment of the liquidator is accorded to the creditors, who may also resolve to establish a liquidation committee to act on their behalf in relation to the conduct of the liquidation. The principal differences between the voluntary and compulsory modes of winding up are ultimately attributable to the fact that a compulsory winding up is initiated by means of a court order, and is thus subject to more exacting, and more closely-applied, judicial and public administrative control. The first matters to be considered are the circumstances in which a compulsory winding up of an insolvent company can take place, and by whom, and in which court, a petition for a winding up order may be presented.

The appointment of the liquidator brings about the displacement of the directors from the exercise of their powers. Although the legal title to the company's property remains vested in the company itself, the liquidator assumes control of it and administers it for the benefit of the creditors, distributing the proceeds of realization in accordance with the statutory regime, which specifies the sequence in which the different categories of expenses and liabilities are to be paid. Creditors are required to prove their debts for the purpose of establishing their entitlement to receive dividend, and the same process is also employed as a means of determining creditors' eligibility to vote at meetings, and also the respective weight to be borne by the votes they cast. At the conclusion of the winding up process the company is dissolved and its legal personality extinguished, and the liquidator may obtain his release from office.

Conclusion

The Tanzanian corporate insolvency procedures generally resemble English insolvency procedures. Apart from the procedures, other principles that can be found under English Insolvency Act, 1986 such as principle of wrongful trading have also been adopted in Tanzania.

Before relying on anything contained in this paper, you are advised to seek legal advice. This paper has been prepared by Ngassa Dindi who is a partner at Lawcastles, Advocates. His email address is: ngassa.dindi@lawcastles.com