Corporate Creditors Protection Rights Worldwide: Towards a Convergence of Strategies

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Abstract

Companies rely on creditors for funding to operate, making it crucial to have legislative and procedural frameworks that protect the interests of these creditors. This article engages in a comparative analysis of corporate creditors' protection rights on a global scale, emphasizing the Ethiopian case. The study contends that while countries may adopt distinct approaches to safeguard corporate creditors, and variations may exist in the strictness of rules across different strategies, nations have a universal commitment to implement strategies to ensure adequate protection for creditors' interests. Notably, the study underlines that, amid the surge in globalization and cross-border commerce, strategies for corporate creditor protection are progressively aligning and converging worldwide, signaling a positive trend in global business dynamics, and the Ethiopian case is not an exception. This convergence reflects a harmonized effort across nations to establish a consistent and practical framework for protecting corporate creditors' interests in the contemporary globalized economic landscape.

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Table of Contents

I. INTRODUCTION

Access to financing is essential for businesses to function. Companies with insufficient working capital cannot maintain daily operations.[1] When the subscribed capital is not sufficient to support the planned business activities of the company, as is often the case, companies must obtain additional working capital from various sources, with credit financing (loans) from creditors being the most common approach.[2] Corporate creditors are therefore crucial stakeholders with considerable control over the efficient and smooth operation of the company's day-to-day functions and the protection of its assets.[3] To promote lending and boost the inflow of funds into companies, it is essential to protect the interests of those who provide capital. This can be achieved by implementing laws, processes, and procedures that satisfy creditors' demands and safeguard corporate debtor assets.[4]

These measures act as a collective safeguard for creditors and are crucial for encouraging them to provide loans.[5] Failing to implement adequate protection measures can make creditors hesitant to lend money.[6] Nations worldwide have implemented various preventive and corrective measures to safeguard the rights of corporate creditors. While these nations share a common principle of protecting the interests of creditors,[7] each country has tailored its corporate credit regulations to suit its legal system's characteristics and economic advancement level.[8] Creditor protection laws have expanded beyond regional boundaries, driven by globalization, international trade, and easier access to other countries'

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1 *See generally* LEN SEALY ET AL.'S CASES AND MATERIALS IN COMPANY LAW: THE RAISING OF CAPITAL 488–511 (10th ed. 2013); RICHARD A. BREALEY ET AL., PRINCIPLES OF CORPORATE FINANCE 3–50 (13th ed. 2020).

2 *See generally* ANIL HARGOVAN ET AL., AUSTRALIAN CORPORATE LAW 272–308 (7th ed. 2021); STEPHEN A. ROSS ET AL., CORPORATE FINANCE 1–15 (11th ed. 2016).

3 *See generally* WILLIAM ALLEN ET AL., COMMENTARIES AND CASES ON THE LAW OF BUSINESS ORGANIZATIONS: DEBT, EQUITY, AND ECONOMIC VALUE 167–189 (6th ed. 2021).

4 *See generally* John Armour, *Share Capital and Creditor Protection: Efficient Rules for a Modern Company Law?*, 63 MODERN L. REV. 355 (2000); SUSAN MCLAUGHLIN, UNLOCKING COMPANY LAW 138–149 (2d ed. 2013).

5 LOUISE GULLIFER & JENNIFER PAYNE, CORPORATE FINANCE LAW, PRINCIPLES AND POLICY 389 (2d ed. 2015); Paul Gompers, Steven N. Kaplan & Vladimir Mukharlyamov, *What Do Private Equity Firms Say They Do?*, 121 J. FIN. ECON. 449 (2016); Paul Gompers et. Al., *How Do Venture Capitalists Make Decisions?*, 135 J. FIN. ECON. 169 (2020).

6 ALLEN ET AL., *supra* note 3, at 167–89.

7 *Id.* at 123–67.

8 Eilis Ferran, *Creditors' Interests and "Core" Company Law?*, 20 CO. LAW. 314 (1999); Eilis Ferran, *Corporate Transactions and Financial Assistance: Shifting Policy Perceptions but Static Law*, 225 CAMBRIDGE L. J. 240 (2004).

laws and best practices.[9] This underscores the need for a comparative analysis of legal frameworks to elucidate variations across nations. Nations must periodically assess their legal frameworks to meet the changing requirements of creditors, which leads to the ongoing revisions of laws and practices in both developed and developing countries. Recent revisions to legislation regarding creditors' rights in the United Kingdom and Ethiopia exemplify this obligation.[10]

This study compares Ethiopia's laws against the legal frameworks of leading industrial nations with strong legal and institutional structures that protect the interests of corporate creditors. This analysis uses the legal frameworks of United States, U.K., European Union, Australia, and India as reference points due to the substantial impact these jurisdictions' corporate creditor protection laws and practices have had on worldwide legislative patterns. The compared jurisdictions also represent the perspectives of developed nations regarding the safeguarding of corporate creditors' rights, whereas Ethiopia exemplifies the developing countries' perspective. As a Least Developed Country (LDC), Ethiopia and other countries benefit from the extensive experiences of developed nations in this area.

Moreover, this study provides an opportunity to compare the methods of protecting corporate creditors in jurisdictions that follow Common Law principles (such as the U.S., U.K., India, and Australia) with those that adhere to Civil Law traditions (such as Germany, France, and Ethiopia). This provides a complete inventory of the tactics employed to safeguard the interests of corporate creditors worldwide. The analysis reveals that Ethiopia currently offers one of the strongest safeguards for the rights of corporate creditors, in line with international norms, thanks to its implementation of a new Commercial Code in 2021 that incorporates modern rules and principles. This indicates that the protection of rights of corporate creditors in Ethiopia have aligned with the most advanced worldwide standards. It also suggests a pattern of harmonization of corporate creditors' rights locally and worldwide. This comparative study also helps to examine similarities and variations among nations, facilitating experience sharing in creditors protection. It also examines whether the relevant international regulations align or diverge.

To benchmark against the global landscape of creditor protection,[11] and to assess the adequacy of corporate creditor protection rights in Ethiopia, two Leximetric Corporate Creditor Protection Indexes were formulated. These

9 *See generally* ROY GOODE ET AL., TRANSNATIONAL COMMERCIAL LAW: TEXT, CASES, AND MATERIALS 49–73 (2d ed. 2015); MICHAEL BLOWFIELD & ALAN MURRAY, CORPORATE SOCIAL RESPONSIBILITY 1–50 (4th ed. 2019); Gary B. Born, *Planning for International Dispute Resolution*, 17 J. INT'L ARB. 61 (2000).

10 In this regard, the UK's Insolvency and Corporate Governance Code of 2020 and the Commercial Code of Ethiopia 2021 are typical. *See* Corporate Insolvency and Governance Act 2020 (UK); Commercial Code of Ethiopia (No. 1243/2021).

11 JOHN ARMOUR ET AL., CBR EXTENDED CREDITOR PROTECTION INDEX 1990–2013 (2016).

indexes cover the period from 1960-2020 and from 2021 onwards, relying on ten fundamental variables of creditors' protection identified on a merit basis.[12]

The article proceeds as follows. Part One explores the rationale for corporate creditor protection. Part Two discusses the worldwide types, nature, and comparative analysis of creditor protection strategies. Part Three examines the findings from the comparison of the strategies of corporate creditor protection. Part Four introduces and evaluates two novel Leximetric Creditor Protection Indexes for Ethiopia. These indexes specifically measure the adequacy of legal rights provided to corporate creditors. The final segment, Part Five, offers the conclusion.

II. Rationale for Corporate Creditor Protection

Creditors' rights refer to measures within a legal system that give corporate creditors the authority to recover debts from the corporate debtor. These laws might be mandatory or discretionary. It is imperative for states to protect the interests of corporate creditors for the reasons explored in this section.

A. The Risks Arising from Separate Legal Personality

Unlike partnerships, which do not exist separately from their members, and individuals who are personally responsible for their obligations, companies, as associations of capital, have a distinct legal personality recognized by the law, existing independently from their members.[13] Upon registration, the company establishes a separate corporate identity from its members, instantly attaining the status of an independent legally recognized entity.[14]

Upon the company's formal incorporation, it can engage in legal activities. Among the essential abilities of an incorporated business are the capacity to engage in contractual agreements, own and administer assets, and carry out all necessary activities associated with its legal status.[15] When the company is legally

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12 Refer to §§ 4.1–4.3 of the Leximetric Corporate Creditors' Protection Index for Ethiopia 1960–2020 and 2021 & beyond.

13 DEL. CODE ANN. tit. 8, §§ 101–09, 131–40, 241–45, 311–14 (West 2017) [hereinafter DGCL]; For Australia, see *Andar Transport Pty Ltd v Brambles Ltd* (2004) 206 ALR 387, 403–04; SEALY & WORTHINGTON, *supra* note 1, 1–80.

14 Henry Hansmann & Reinier Kraakman, *The Essential Role of Organizational Law*, 110 YALE L. J. 387 (2000); MCLAUGHLIN, *supra* note 4, at 62–82; AVTAR SINGH, COMPANY LAW 1–49 (17th ed. 2018); *Santa Clara County v. Southern Pacific Railroad Co.*, 118 U.S. 394 (1886); Companies Act 1985, c. 1, § 13(3) (UK); Companies Act 2006 §§ 7–16, 9(2)(b), 15(1), 112–21 (UK); Companies Act, 2013, §§ 3–22, 9 (India); DGCL, *supra* note 13, §§ 102(a)(3), 106, 108, 121–27; MODEL BUS. CORP. ACT §§ 2.01, 2.04–2.06 (2016) [hereinafter MBCA]; LE TALBOT, CRITICAL COMPANY LAW 23–62 (2008).

15 Corporations Act *2001* (Cth) § 124 (Austl.). For examples of Australian cases, see *Macaura v Northern Assurance Co Ltd* (1925) AC 619; *Consolo Ltd v. Bennet* (2012) FCAFC 120; *Sevilleja v Marex Financial*

established, no shareholder can claim exclusive ownership; they are all partial owners. The company operates independently and is solely responsible for its debts. Shareholders are not responsible for the company's conduct except for completely fulfilling their subscription shares.[16] Due to their independent legal identities, companies maintain separate assets that their shareholders do not own. This demarcation guarantees that the company's obligations are paid off utilizing its designated assets, separating its responsibilities from those of its proprietors.[17] The demands made by corporate creditors for company assets are prioritized over the demands made by the owners' personal creditors. The allocation of corporate assets is expressly designated to meet just the company's liabilities.[18] Corporate creditors are prohibited from making claims on the shareholders' personal assets. This exacerbates the risk for corporate creditors by limiting the assets available for them to pursue repayment. Additionally, it limits creditors' power to seek payment only from the company's assets, reducing their capacity to recover the whole amount if the company's assets are inadequate to repay the entire debt.[19] Due to the distinct legal identities, the restriction of creditors' ability to seek payment only from company assets threatens creditors' interests. Therefore, nations need to develop other methods to protect the interests of creditors.

1. Registration and legal personality in Ethiopia.

The Ethiopian company law places significant importance on legal personality and the process of registering and publishing traders and business organizations.[20] Hence, it established distinct and rigorous regulations outlining the registration obligations for traders and business organizations.[21]

Ltd (2020) UKSC 31; *Andar Transport Pty Ltd v Brambles Ltd* (2004) 206 ALR 387; *Lee v Lee's Air Farming Ltd* (1961) AC 12; Companies Act, 2013 §§ 9, 2(11) (India). For examples of Indian cases, see Bacha F Guzdarv v. Commissioner of Income-Tax, Bombay, AIR 1955 SC 74; Ashoka Mktg Ltd. v. Punjab National Bank (1990) 4 SCC 406, 423–24; New Horizons Ltd. v. Union of India, (1997) 89 Comp Cas 785, 802 (Del.); New Horizons Ltd v. Union of India, (1995) 1 SCC 478; (1997) 89 Comp Cas 849.

16 Salomon v. Salomon & Co Ltd. [1897] AC 22 (UK); Kondoli Tea Co Ltd., Re., (1886) ILR 13 Cal 43.

17 Commercial Code of Ethiopia art. 245 (No. 1243/2021) [hereinafter Commercial Code]; JOHN ARMOUR ET AL., FOUNDATIONS OF CORPORATE LAW, 1–37 (Eur. Corp. Governance Inst., Working Paper No. 902, 2017).

18 John Armour et al., *What is Corporate Law?*, *in* THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 1 (Reinier Kraakman et al. eds., 3rd ed. 2017).

19 CHARLES WILD & STUART WEINSTEIN, SMITH KEENAN'S COMPANY LAW 66–80 (14th ed. 2009); NICHOLAS BOURNE, ESSENTIAL COMPANY LAW 6–8 (3d ed. 2000).

20 The Commercial Code of Ethiopia addresses commercial registration. Commercial Code of Ethiopia arts. 70–104 (No. 1243/2021).

21 A trader is the sole person who operates activities of an economic nature, professionally and for a gain. There is no separation of legal personality between a trader and the business it is operating. Therefore, the trader is fully, jointly, and severally liable to creditors. *See id.* at arts. 5–15.

a) Registration and legal personality of traders.

While there are differences between companies and traders, it is essential to note that registration does not grant traders (i.e. sole business persons) and some partnerships a distinct legal identity.[22] However, all traders are required to apply to be listed in the Commercial Register.[23] As a result, all officially registered natural persons operating economic activities are automatically categorized as traders. They are prohibited from disproving their position as a trader and must accept all responsibilities connected with that categorization.[24] Failure to comply with the registration requirement is illegal, resulting in various restrictions on doing a particular business and civil and criminal fines.[25]

Despite being unable to market themselves as traders and receive the benefits that come with it, unregistered traders involved in commercial operations are nevertheless held accountable for any obligations towards third parties as if they were officially recognized as traders.[26] Traders must submit applications for registration and termination when there is a change in ownership resulting from a sale or lease or when the business ceases operations owing to various circumstances, such as bankruptcy or the death of the trader.[27] On the other hand, if a registered trader transfers ownership of their company or leases it out, they are both jointly and individually responsible for all obligations incurred by the assignee or lessee until the registration is officially revoked.[28]

b) Registration and legal personality of business organizations.

In Ethiopia, business organizations—with the exception of joint ventures—acquire legal personality following their official registration in the commercial register.[29] The formation of a commercial entity will not be legally recognized

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22 Per articles 183–244 of the New Code, Ethiopian law recognizes 4 types of partnerships. These are General Partnerships, Limited Partnerships, Limited Liability Partnerships, and Joint Ventures. Unlike companies that are associations of capital, partnerships in Ethiopia are an association of persons and the existence of the partnership depends on the personality of each partner. Partnerships are closed business and do not issue or offer shares. *See id.* at arts. 183–244.

23 *Id.* at arts. 82–89.

24 *Id.* at arts. 99, 102–05.

25 *Id.* at arts. 21–25, 97–05.

26 *Id.* at arts. 23(2), 97, 100, 103–05.

27 *Id.* at arts. 84(1–2), 93–96, 182.

28 *Id.* at art. 101.

29 *Id.* at arts. 175, 222, 234, 235, 254, 255, 499, 500. A business organization is an association established through a memorandum of association by persons (two or more) who bring together contributions for the purpose of undertaking an economic activity in cooperation and of participating in the profit made. *See id.* at arts. 172–812. Article 174 recognizes seven types of business organizations in Ethiopia. Of which, four are partnerships while the remaining three are companies namely Share Companies, Private Limited Companies, and One Member Private Limited Company. *See id.* at art. 174.

unless it is established through a memorandum of association.[30] This indicates that a business organization immediately acquires a separate legal identity upon registration.[31] This regulation applies to all officially acknowledged types of partnerships (except joint ventures) and companies in Ethiopia.[32] According to Ethiopian company law, a share company must register in the commercial register, regardless of how it was formed. The immediate result of this registration is granting the company an autonomous legal personality, allowing it to participate in juridical activities autonomously. One of the most important activities is the entitlement to own and administer property under one's own name.[33]

The legislation also requires that a company is granted legal status as soon as its name is entered into the commercial register, emphasizing the importance of registration. This status remains valid even if all other legal requirements for the company's establishment have not been met.[34] On the other hand, if there is a situation where the failure to register can harm the interests of creditors or shareholders, the court has the power to dissolve the company or take corrective actions at the request of a creditor or shareholder.[35] Similarly, the requirements for registration and creating separate legal identities apply to private limited companies and single-member private limited companies in Ethiopia.[36]

B. The Risks Arising from Limited Liability

It was in the 1897 landmark decision *Salomon v. A. Salomon & Co Ltd.* that companies' independent, juristic existence was established for the first time in the

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30 *Id.* at arts. 173, 177, 185, 214, 225. However, in Ethiopia, the requirement of registration and legal personality does not apply to a Joint Venture. A joint venture is a business organization established by an agreement among two or more persons. It has no legal personality, and its existence is unknown to third parties. Registration formalities required of other business organizations do not apply to a joint venture. *See id.* at arts. 234–44.

31 *Id.* at arts. 265 (1–3), 266. The duty of registration is a requirement of all business organizations in Ethiopia to acquire legal personality. Legal personality enables such organizations to operate juridical activities such as owning assets or operating economic activities for profit. In contrast, the cancellation of the register results in the termination of business organizations forcing them to cease their business activities.

32 Per the new code, these are general partnerships, limited partnerships, and limited liability partnerships. The three types of companies are share companies, private limited companies, and one-member private limited companies. *See id.* at arts. 174, 183–244.

33 *Id.* at art. 265 (1–3); Civil Code of Ethiopia arts. 1–50.

34 Commercial Code, *supra* note 17, at art. 266(1–2).

35 Commercial Code, *supra* note 17, at art. 266(2).

36 Articles 534–49 of the Commercial Code of Ethiopia address one member PLCs. Commercial Code, *supra* note 17, at arts. 534–49. Accordingly, a one-member private limited company is a business organization incorporated by the unilateral declaration of a single person. The company has its own legal personality separate and distinct from that of the member and the member shall not be personally liable for debts due by the company as far as he has fully made his contribution.

U.K.[37] Since this decision, the main advantage of conducting business for shareholders inside the corporate organizational framework is the granted privilege of limited liability for the company's obligations. Upon registration, the company, as a separate legal entity, acquires ownership of its assets and bears responsibility for its debts, relieving the shareholders from complete ownership and accountability for the company's financial obligations.[38] Unlike partnerships, where partners are fully liable for the partnership's obligations, incorporating a company with limited liability ensures that shareholders have limited exposure. Shareholders' liability is restricted to the amount they first subscribed.[39] When the company's assets are inadequate to cover its debts fully, shareholders are not legally obliged to contribute any amount beyond the outstanding portion of their initial subscription. This restraint limits creditors' right to exclusively pursue payment from the company's assets.[40]

The notion referred to as the doctrine of limited liability is highly praised by experts as one of the most important advancements of the 19th century. Limited liability confers several benefits, such as promoting investment in enterprises, facilitating the transfer of shares, improving transparency and certainty regarding the company's assets, and serving as a default norm to define the allocation of risks between creditors and shareholders.[41] It has also significantly improved the security of investors buying company shares, thereby promoting the worldwide growth of businesses.[42] Otherwise, acquiring a company's shares would expose shareholders to unrestricted personal liability in case of failure, discouraging investment.[43] However, introducing limited liability or "owner shielding" restrictions has increased the risk for creditors when doing business with companies.[44] The increased vulnerability for lenders arises from the concept of limited liability, wherein, after the formation of a company, the obligation to repay loans is restricted only to the assets owned by the company.[45] Creditors' claims

37 Salomon v. Salomon & Co Ltd. [1897] AC 22 (UK); *see also* Prest v. Petrodel [2013] UKSC 34 (UK); Limited Liability Act 1855 (UK); Joint Stock Companies Act 1856 (UK).

38 J H Rayner (Mincing Lane) Ltd v. Dept of Trade and Industry, [1990] 2 AC 418 (1989) 3 WLR 969 (HL) (UK); SEALY & WORTHINGTON, *supra* note 1, 81–177.

39 WILD & WEINSTEIN, *supra* note 19, at 1–42.

40 AVTAR SINGH, *supra* note 14, at 1–49.

41 Companies Act 2006 § 3(4) (UK); Limited Liability Act 1855 § 1 (UK); MCLAUGHLIN, *supra* note 4, 62–82.

42 Frank Easterbrook & Daniel Fischel, *Limited Liability and the Corporation*, 52 U. CHI. L. REV. 94–97 (1985); In re London & Globe Finance Corpn. Ltd., [1903] 728, 731 (UK); JANET DINE, COMPANY LAW 1–20 (4th ed. 2001).

43 SIMON GOULDING, COMPANY LAW 53 (2d ed. 1999); MCLAUGHLIN, *supra* note 4, 62–82.

44 Commercial Code, *supra* note 17, at art. 245; LE TALBOT, *supra* note 14, at 24. The 'owner shielding' rules refer to the rules that protect the assets of a firm's owners from the firm's creditors.

45 Commercial Code, *supra* note 17, at art. 245(2); NICHOLAS BOURNE, *supra* note 19, at 1–12.

are limited in accessing shareholders' assets, shifting some expenses and risks from the company's owners to creditors.[46] The shareholders have little or no accountability towards creditors for any losses incurred by creditors while conducting business with a company.[47] In contrast, the company is fully responsible for its debts to corporate creditors and must use all its assets to settle them.[48] Thus, nations should mitigate the dangers that creditors face from the non-personal responsibility of shareholders. This strategy aims to attain a harmonious and equitable alignment between the interests of the debtor and the corporate creditors.[49]

1. The doctrine of limited liability in Ethiopia.

a) Limited liability in Ethiopian companies.

As defined under Ethiopian company law, a share company has predetermined capital divided into shares, where its assets cover its liabilities.[50] Share companies can be formed either as closed companies, limited to just five members who are the founders, or as open (public) companies that issue shares to the general public.[51]

Similarly, a private limited company is a corporate entity in which the shareholders have completely paid their capital in advance and are not personally responsible for the company's debts, as long as they have fulfilled their financial obligations.[52] These companies typically have a membership size ranging from two to fifty individuals and cannot issue shares to the general public. They are privately held companies.[53] Both private limited and share companies must repay their commitments to creditors only by utilizing the company assets. Shareholders' obligation is restricted to fulfilling the contributions they pledged to contribute to

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46 Christopher J. Cowton, *Putting Creditors in their Rightful Place: Corporate Governance and Business Ethics in the Light of Limited Liability*, 10 J, BUS. ETHICS 21, 22 (2011).

47 Peter O. Mulbert, *Legal Capital—Is There a Case against the European Legal Capital Rules?*, 3 EURO. BUS. ORG. L. REV. 695, 710 (2002).

48 Article 289(1–7) of the Commercial Code of Ethiopia deals with the liability of shareholders to meet calls. Commercial Code, *supra* note 17, at art. 289(1–7). Eneless Nyoni & Tina Hart, *The Concept of Limited Liability and the Plight of Creditors within Corporate Governance and Company Law: A UK Perspective*, 5 INTEREULAWEAST 309, 312 (2018).

49 MARK STAMP, PRIVATE COMPANY LAW 14–16 (3d ed. 2001); §§ 691–92 of the UK Companies Act 2006 states that a limited company may not purchase its own shares. UK Companies Act 2006, *supra* note 14, §§ 691–92.

50 Commercial Code, *supra* note 17, at arts. 245–494 (Share Companies), arts. 495–533 (Private Limited Companies); art. 245(1); arts. 304(1–2), 342 (liability to meet calls).

51 *Id.* at arts. 245–53, 254–67.

52 *Id.* at arts. 495–533. Ethiopian PLCs are similar to close corporations in Delaware. DGCL, *supra* note 13, §§ 341–56.

53 Commercial Code, *supra* note 17, at art. 495(3–5).

the company, demonstrating the application of the theory of limited liability.[54] Because of limited liability, shareholders who have not fully paid for their shares are only responsible to the company's creditors. The liability alone applies to the unpaid portion of their shares, known as the "liability to meet calls." It is crucial to note that shareholders' personal assets are protected from these duties.[55]

Past transferees and subscribers in Ethiopia are collectively and individually responsible for any financial obligations related to calls on shares made by the company.[56] Paying interest at the legal rate is required if the call duty is not met by the designated date. After a written warning period of fifteen days, the company has the authority to either auction the shares that have not been paid for or cancel them, which would result in an adjustment of the company's capital.[57] In addition, shareholders who fail to pay for their shares by the due date will lose their voting privileges in shareholder meetings.[58] If the debtor declares bankruptcy, the law gives the trustee the authority to call for the surrender of shares and require owners and partners to pay their financial commitments, even if those commitments are not yet due on the day the bankruptcy judgment is made. Failure to fulfill these tasks results in legal proceedings against the shareholders or partners if the trustee requests it.[59] Moreover, shareholders are still required to fulfill their responsibility to the company by paying the outstanding sum on their subscribed shares, even in the event of the company's dissolution. If the company's residual assets are insufficient to meet its obligations, the law allows liquidators to call upon shareholders to pay any outstanding sums owed on their shares, if applicable.[60]

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54 *Id.* at art. 245(2).

55 *Id.* at art. 289.

56 *Id.* at art. 289(1).

57 *Id.* at art. 289(2–6).

58 *Id.* at art. 289(7).

59 *Id.* at art. 743(1–2).

60 *Id.* at art. 482(1–4).

Similar to the idea of piercing the corporate veil[61] in common law jurisdictions,[62] Ethiopian company law specifies certain situations that differ from the basic rule of limited liability. In certain cases, shareholders may bear joint and several liabilities with the company concerning creditors, fellow shareholders, the company, and other parties.[63] The liability of shareholders becomes unlimited when they deliberately participate in illegal activities that endanger the company's interests and those of shareholders or creditors. This encompasses mixing the company's assets with its own, deliberately obscuring the difference between the company's identity and its own, or using the company as a front to promote personal or third-party interests. Furthermore, responsibility also encompasses the intentional spreading of false information regarding the company's financial condition, the unauthorized use of corporate resources for personal or third-party gain, and the payment of dividends that exceed legal restrictions.[64]

The concept of limited liability also extends to one-member private limited companies in Ethiopia. These entities have separate legal identities that are not dependent on their sole member. Therefore, the member is exempt from personal liability for the company's debt if he or she has already contributed.[65] Under extraordinary situations, like those involving share companies, the safeguard of limited liability for a one-member private limited company member may be waived. In such instances, the member or any individual who has authority over the company, whether directly or indirectly, assumes joint and several liability alongside the company. Joint and several responsibilities are boundless, and it

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61 For U.K. cases, see VTB Capital Plc v. Nutritek International Corp [2013] UKSC 5; Prest v. Petrodel Resources Ltd [2013] UKSC 34; Wallersteiner v. Moir (No. 1) [1974] 3 All ER 217; Re Hellenic and General Trust Ltd [1975] 3 All ER 382; DHN Ltd v. Tower Hamlets LBC [1976] (CA); Littlewoods Mail Order Stores Limited v. Commissioner of Inland Revenue [1969] 1 WLR 1241; for U.S. decisions, see Krivo Industrial Supply Co. v. National Distillers & Chem. Corp., 483 F.2d 1098, 1106 (5th Cir. 1973); Van Dorn Co. v. Future Chemical and Oil Corp., 753 F.2d 565 (7th Cir. 1985); Sea–Land Services, Inc. v. the Pepper Source 941 F.2d 519 (7th Cir. 1991); Walkovszky v. Carlton 223 N.E.2d 6 (N.Y. 1966).

62 *Corporations Act 2021* (Cth) §§ 197, 267, 558G, 588V (Austl.). Australian courts pierced the corporate veil in certain exceptional circumstances, such as corporate misconduct. For Australian Cases, see *Atlas Maritime Co SA v Avlon Maritime Ltd (No. 1)* (1991) 4 All ER 769, 779; *Idoport Pty Ltd v National Australian Bank Ltd* (2004) NSWSC 695; Re Polly Peck International Plc [1996] 2 All ER 433, 447; *Green v Bestobell Industries Ltd* (1982) WAR 1; *Creasey v Breachwood Motors Ltd* (1982) BCLC 480; (1992) BCC 638; *Ballantyne Suits Pty Ltd v Ballantyne Chambers Pty Ltd* (2014) VSCA 223 at 34; *Dennis Willcox Pty Ltd* v *FCT* (1988) 79 ALR 267, 272; *Pioneer Concrete Services Ltd v Yelnah Pty Ltd* (1986) 5 NSWLR 254; *Adams v Cape Industries Plc* (1990) 433, 539; *Gilford Motor Co Ltd v Horne* (1933) Ch 935; *Jones v Lipman* [1962] 1 WLR 832; *Kensington International Ltd v Republic of Congo* (2006) 2 BCLC 296; (2005) EWHC 2648; *Artedomus v Del Casale* (2006) NSWSC 146; *Commissioner of Fair Trading v TLC Consulting Services Pty Ltd* [2011] QSC 233; Anil Hargovan, *Breach of Directors' Duties and the Piercing of Corporate Veil*, 34 AUS. BUS. L. REV. 302 (2006).

63 Commercial Code, *supra* note 17, at art. 295.

64 *Id.* at art. 295(1–6).

65 *Id.* at art. 534(1–3).

occurs when an individual deliberately partakes in illegal activities that endanger the company's or its creditors' interests. These actions encompass commingling the company's assets with personal property, neglecting to maintain a distinct separation between personal and corporate identities, intentionally spreading deceptive information about the company's financial condition, using company assets for personal or third-party gain without proper compensation, exceeding the legally allowed limit for receiving dividends or engaging in comparable misconduct.[66]

The aforementioned grounds are intended to prevent debtor opportunism arising from undue exploitation or misuse of the privilege of limited liability.

b) Limited liability in Ethiopian partnerships.

Unlike companies, the unique traits of each partner are essential to determine the nature of the partnership in Ethiopia. Each partner's personality is closely connected to the partnership venture.[67] All the partners have equal responsibility and are individually accountable to the partnership for its debts.[68] Consequently, separate legal identities and the resulting limited liability have no effect in most Ethiopian partnerships. This indicates that partners have unlimited liability, meaning that in cases where the partnership's assets are inadequate to settle obligations, creditors have the right to pursue compensation from each partner's assets.

In the context of a general partnership, every partner has joint and several liability for the obligations incurred by the partnership.[69] Individuals who have left a general partnership are nonetheless collectively and individually liable, together with the partnership, for the debts and obligations incurred by the partnership before their departure. Moreover, when a partner leaving the partnership still has unresolved responsibilities to the partnership, the duty might be passed to a replacement partner with the approval of the partnership's creditors.[70] Each partner must also promptly provide their financial commitment to the partnership.[71] The duties of a general partner in a Limited Liability Partnership endure, as they are entirely (unlimitedly) and collectively and individually

66 *Id.* at. art. 543(1–7).

67 *Id.* at. arts. 183, 184, 191, 205–11; Per articles 172–82 & 183–244, in general, partnerships are an association of two or more partners who agree to cooperate and share profit and losses together. The personality of each partner determines the existence of the partnership. The death or expulsion of a partner is a ground for dissolution of the partnership. The introduction of a new partner requires agreement of all partners, and they do not offer shares (interests) to third parties.

68 *Id.* at arts. 191, 192.

69 *Id.* at arts. 191(1(d, e)–2), 183–211 (addressing general partnerships in Ethiopia).

70 *Id.* at art. 196.

71 *Id.* at arts. 189, 190, 191(1).

responsible together with the partnership itself for the debts and responsibilities acquired by the partnership.[72]

Specific partnership kinds in Ethiopia may be subject to separate legal personality and limited liability regulations under extraordinary circumstances. In the case of a limited liability partnership, the responsibility of limited partners is limited to the amount of money they have already contributed to the partnership. This differs from general partners, who have unlimited liability for the partnership's commitments.[73] Consequently, creditors of limited partnerships have the exclusive right to demand payment of any unpaid contributions from limited partners, if applicable. This indicates that creditors cannot pursue limited partners' assets to satisfy the partnership's debts. Creditors are also prohibited from requesting repayment from limited partners for dividends received in good faith after the partnership's financial statement is endorsed.[74]

A limited liability partnership is characterized by the existence of a separate legal entity that is different from its participants.[75] This signifies that occurrences such as mortality, insolvency, withdrawal from the partnership, or any other situation impacting the partners do not impact the partnership's existence, entitlements, or responsibilities. Moreover, the notion of independent legal personality indicates that the partnership has specific assets put aside to cover its debts, and partners are only liable for the amount of their unpaid contributions.[76]

C. The Need to Curb Debtor's Opportunism

Notwithstanding the notion of separating management from ownership, companies are effectively governed by their management and shareholders to achieve commercial objectives, owing to their fictional nature.[77] Shareholders, the company's human constituents, play an active role in decision-making processes and influence the company's business activities. The control is exercised either directly through general meetings, via influential shareholders, or indirectly through the company's management.[78] Shareholders, as stakeholders, commonly

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72 *Id.* at arts. 212–20 addresses limited partnerships. Accordingly, a limited partnership comprises partners with different types of liability. General partners who are fully liable jointly and severally with the partnership itself for the obligations of the partnership and limited partners who are liable for the obligations of the partnership only to the extent of their pledged contributions.

73 *Id.* at arts. 212–18.

74 *Id.* at art. 218 (1–7).

75 *Id.* at arts. 221–34 addresses limited liability partnerships. Accordingly, a limited liability partnership is a business organization formed by two or more persons to render professional service and services complementary thereto in which the liability of partners is limited to the amount of their contributions.

76 *Id.* at arts. 222–33.

77 STEPHEN GRIFFIN, COMPANY LAW: FUNDAMENTAL PRINCIPLES 1–10 (4th ed. 2006).

78 HAL R. VARIAN, INTERMEDIATE MICROECONOMICS: A MODERN APPROACH 14 (8th ed. 2010).

create informal links to facilitate information sharing to monitor directors' performance informally and effectively.[79] Because of their favorable position and the benefit of limited liability, shareholders can pursue their economic interests even when conflicts of interest arise.[80] Shareholders who induce a company to behave in a way that harms creditors are not held personally accountable for their actions due to limited liability. Their personal assets are protected from being used to settle debts owed to creditors.[81] The difference in decision-making power and personal responsibility significantly alters the incentive system of companies compared to an individual who is personally liable to creditors.[82]

Shareholders risk losing their investment if there is an economic downturn. However, their lack of personal liability for decision-making motivates them to either make a last-ditch attempt to save the business or, in certain situations, take actions that could unfairly shift the business risk onto creditors.[83] Therefore, shareholders utilize their advantageous position and the safeguard of limited liability to divert value from the company's creditors using different strategies.[84] This may entail engaging in deceitful practices such as expediting the allocation of remaining net assets as dividends, intermingling shareholders' assets with the company's, engaging in risky business activities with uncertain results, or increasing the company's investment risk by substituting or diverting assets.[85]

These activities significantly reduce the value of the company's assets, resulting in insolvency, as reflected on the balance sheet. As a result, the certainty that the assets may be used as collateral for repaying debts is undermined.[86] Therefore, rules for safeguarding creditors, whether in a preventative or corrective manner, are crucial to reducing and resolving conflicts of interest by preventing or correcting the imprudent actions of shareholders.[87] This also pertains to

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79 THOMAS BACHNER, CREDITOR PROTECTION IN PRIVATE COMPANIES: ANGLO–GERMAN PERSPECTIVES FOR A EUROPEAN LEGAL DISCOURSE 20–27 (2009).

80 Francesco Denozza, *Different Policies for Corporate Creditor Protection*, *in* THE LAW AND ECONOMICS OF CREDITOR PROTECTION: A TRANSATLANTIC PERSPECTIVE 413–16 (Horst Eidenmüller & Wolfgang Schön eds. 2008). This is called the "shareholder–creditor agency problem."

81 Mulbert, *supra* note 47, at 695–732.

82 U.K. Companies Act 2006*, supra* note 14, at § 174; Cohen v. Selby (2001) 1BCLC 176 (Eng.); Peter O. Mulbert, *A Synthetic View of Different Concepts of Creditor Protection*, *or: A High-Level Framework for Corporate Creditor Protection*, (60 ECGI Working Paper, 2006).

83 Federico M. Mucciarelli, *General Principles of EU Corporate and Insolvency Law*, *in* RESEARCH HANDBOOK ON GENERAL PRINCIPLES OF EU LAW 1–20 (2019).

84 *See* Commercial Code, *supra* note 17, at art. 295 (1–6); Armour J., Gerard Hertig, & Hideki Kanda, *Transactions with Creditors*, *in* THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH, *supra* note 18, at 1–46.

85 John Armour, *Transactions at an Undervalue*, *in* VULNERABLE TRANSACTIONS IN CORPORATE INSOLVENCY 47 (John Armour & Howard Bennet eds., 2003).

86 ARMOUR, *supra* note 4, at 355–78.

87 GULLIFER & PAYNE, *supra* note 5, at 389.

directors responsible for making decisions on behalf of the company, serving as the company's representatives, and possessing the ability to enter into agreements with third parties on behalf of the company.[88] Directors possess significant power in management and can strategically utilize it to the disadvantage of creditors, whose interests depend on the company's financial health but may not necessarily align with the directors' objectives.[89] Directors may persist with a high-risk approach to navigate through a crisis. In the event of insolvency, this technique results in more financial losses for the creditors. Directors may misappropriate corporate funds by engaging in discounted transactions and disguised payouts, ultimately benefiting themselves or shareholders. This self-enrichment is detrimental to the company as it depletes its assets and puts the possibilities of debt recovery at risk.[90]

Directors can return a shareholder loan before the agreed-upon time or change the company's economic model to a more unpredictable and risky structure, which might increase the chances of default. They may divest current assets and allocate funds to more suspicious endeavors.[91] Directors may also deliberately continue the company's activities despite a substantial depletion of working capital or insolvency, even when commencing insolvency proceedings would be more advantageous for the creditors.[92] Continuing to operate a financially unstable company enables directors to take advantage of risky opportunities while still receiving salary payments and enjoying other benefits connected with their employment.[93] Directors can also deplete the company's assets by neglecting their obligation to exercise care, loyalty, and the required standard of a diligent and conscientious director in carrying out their responsibilities.[94]

Although companies are motivated to pursue more high-risk initiatives to potentially increase their profits, it is crucial to guarantee that creditors are not excessively exposed to avoidable contractual risks.[95] On the other hand, if a

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88 U.K. Companies Act 2006 *supra* note 14, at §§ 40–52 (powers of directors), 154–61 (appointment of directors), 170–77 (duties of directors); MICHAEL ADAMS, ESSENTIAL CORPORATE LAW 19–31 (Michael Adams & David Barker eds., 2002); ANDREW KEAY, COMPANY DIRECTORS' RESPONSIBILITIES TO CREDITORS 1–424 (1st ed. 2007).

89 John Armour et al., *Agency Problems and Legal Strategies*, *in* THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH, *supra* note 18, at 29–37.

90 Commercial Code, *supra* note 17, at arts. 462–67; THOMAS BACHINER, *supra* note 79, at 22.

91 U.K. Insolvency Act 1986, §§ 238–39, 242.

92 Commercial Code, *supra* note 17, at arts. 482(2), 424; ROY GOODE, PRINCIPLES OF CORPORATE INSOLVENCY LAW 519 (4th ed. 2011).

93 Commercial Code, *supra* note 17, at arts. 315 (6), 329 (1); Mülbert, *supra* note 47, at 1–10.

94 Commercial Code, *supra* note 17, at arts. 315–330; UK Companies Act 2006 *supra* note 14, at § 174; *Cohen v. Selby* (2001) 1BCLC 176.

95 Commercial Code, *supra* note 17, at arts. 315(6), 329(1); Mülbert, *supra* note 47, at 1–10.

company is on the brink of insolvency, the opportunistic behavior of its controllers becomes much more detrimental. Creditors are especially susceptible to harm during insolvency when the debtor company struggles with financial difficulties and there is a heightened likelihood that the debt may not be completely reimbursed. Insolvency law protects creditor's rights by removing the directors' authority from managing the financially troubled company. Because of this, directors are frequently motivated to take extreme actions when the company is on the verge of insolvency. This can result in a greater divergence of interests and changes to the allocation of risk. In such situations, directors may engage in actions such as making early or preferential payments of debts, dishonestly distributing assets, hiding, misusing, or destroying company property, and merging or transferring assets to related parties under favorable conditions, among other possible measures.[96]

If not monitored, all the operations carried out by the company's controllers result in unfair wealth transfers from creditors to shareholders, increasing the risk creditors face. This highlights the need to create regulations protecting creditors from potential adverse outcomes from abusing the limited liability principle.[97] Thus, it is necessary for either company[98] or insolvency law,[99] or the court (through the piercing of the corporate veil[100]) to employ either *ex-ante* or *ex-post* mechanisms of creditor protection. These mechanisms aim to mitigate the risks faced by creditors and ensure the necessary safeguards that minimize or eliminate the unfair exploitation of company assets and the interests of creditors by debtors.[101]

D. Creditor Protection Rights Enhance Economic Development

Creditor protection rights and strong judicial enforcement mechanisms encourage lenders to provide more credit to companies by reducing borrower risk and increasing the likelihood of loan recovery. This increases the likelihood of

96 *See* prohibitions imposed against the directors in Commercial Code, *supra* note 17, at arts. 315(6), 329(1), 424 (1), 671–77; Bachner, *supra* note 79, at 20–27.

97 Roy Goode, *The Avoidance of Transactions in Insolvency Proceedings and Restitutionary Defenses*, *in* MAPPING THE LAW: ESSAYS IN MEMORY OF PETER BIRKS 299 (Andrew Burrows & Alan Rodger eds., 2006).

98 U.K. Companies Act 2006, *supra* note 14, §§ 168, 178–87, 188–214, 215–22, 223–27, 369–70; The U.K. Company Directors Disqualification Act 1986 §§ 1–15.

99 MCLAUGHLIN, *supra* note 4, at 3–10; The U.K. Insolvency Act 1986 §§ 213–14, 217; The U.K. Insolvency Rules 1986; *Smith, Stone and Knight v. Birmingham Corp* (1939) 4 All ER 116 (Eng.).

100 WILD & WEINSTEIN, *supra* note 19, at 22–30; *see also Adams v. Cape Industries Plc* (1990) Ch 433, CA (Eng.); *Jones* v *Lipman* (1962) 1 All ER 442 (Eng.); *Wallersteiner* v *Moir* (1974) 3 All ER 217 (Eng.). Courts may remove the veil of incorporation.

101 Mulbert, *supra* note 82, at 1–10.

obtaining credit, which promotes economic growth.[102] Implementing stronger laws to safeguard creditors promotes the development of capital markets. Studies demonstrate that countries implementing more efficient creditor protection mechanisms tend to have better-developed credit markets.[103] Moreover, the presence of laws granting substantial rights to creditors promotes corporate financing by safeguarding corporate creditors from the negative consequences of corporate insolvency.[104]

III. COMPARISON OF THE STRATEGIES OF CREDITORS' PROTECTION GLOBALLY

The vast array of worldwide strategies aimed at protecting creditors is too complex to be fully discussed in this essay. Therefore, this Part specifically investigates and compares three widely utilized and efficient methods for safeguarding creditors. The mechanisms of debtor control rules, creditors' contracts-based (self-help) rules, and insolvency (bankruptcy) laws have proven effective in protecting the interests of creditors.[105]

A. Debtor Control Rules

These regulations include preventative measures (*ex-ante*) and remedial procedures (*ex-post*) as company law requires. They are implemented proactively to govern corporate debtors' actions while operating. The goal is to reduce the probability of default and alleviate the related risks.[106] Debtor control regulations primarily focus on supervising transactions and operations conducted by shareholders and directors. The objective is to proactively avoid any activities that may potentially subject the company to collapse, diminish its resources, and impede creditors' ability to obtain those resources.[107]

These laws aim to mitigate the possibility of creditors facing potential liabilities due to exploiting the limited liability privilege by the company's controllers. Therefore, adhering to regulations regarding debtor control imposes a burden on the company's controllers as a trade-off for the benefit of having

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102 THE WORLD BANK, PRINCIPLES FOR EFFECTIVE INSOLVENCY AND CREDITOR RIGHTS SYSTEMS, 1–8 (2021); Andrea Moro et al., *Creditor Protection, Judicial Enforcement and Credit Access*, 24 EUR. J. FIN. 250–81 (2018).

103 Stijn Claessens & Leora F. Klapper, *Bankruptcy Around the World: Explanations of its Relative Use,* WORLD BANK POLICY RESEARCH WORKING PAPER NO. 2865. 1–44 (2003).

104 Simon Deakin et al., *Varieties of Creditor Protection: Insolvency Law Reform and Credit Expansion in Developed Market Economies*, 15 SOCIOECON REV. 359–84 (2017).

105 ARMOUR ET AL., *supra* note 11, at 1–202.

106 John Armour et al., *How Do Legal Rules Evolve? Evidence from A Cross-Country Comparison of Shareholders, Creditor, and Worker Protection*, 57 AM. J. COMPAR. L. 579 (2009).

107 Deakin et al., s*upra* note 104, at 359–84.

limited liability.[108] If shareholders, directors, or the company violates these mandatory norms, creditors can take legal action against them under company law. In nations that adhere to common law principles, creditors can initiate legal action and perhaps request the court to disregard (pierce) the veil of limited liability. This would result in shareholders being held personally responsible in exceptional circumstances.[109] Debtor control regulations transfer authority from corporate controllers to creditors, altering the power dynamics in favor of creditors while the company continues its operations. On the other hand, although these mandatory precautionary measures are seen as efficient methods for safeguarding creditors, as opposed to relying on contract-based or insolvency rules,[110] they are not immune to criticism for several reasons.[111]

1. Comparison of debtor control mechanisms.

a) The minimum capital requirement.

(1) The minimum capital requirement in general.

The main goal of this requirement is to ensure that a company's assets, particularly the minimum equity, are adequate to sustain its operations. The objective is to hinder the creation of companies with insufficient capital, which are more prone to insolvency, thereby preventing an inequitable risk transfer to creditors.[112] The minimum capital of a company is fundamentally crucial since it directly affects the risk incurred by corporate creditors and enables creditors to assess the debtor's risk of default. Creditors are very interested in determining the extent of a company's capital before providing loans since it is a critical aspect that affects the amount of risk connected with the lending agreement.[113]

Therefore, when a company has limited initial capital, the creditor bears the responsibility for possible trading losses. In such cases, the risk for creditors is increased since even if they take legal action against the company to recover the debt, there is little probability that the company has the means to repay the amount appropriately owed.[114] Conversely, if a company has a significant share capital, the shareholders are responsible for the risk of incurring trading losses up to the amount of the share capital. This structure protects creditors' interests by

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108 Olga Petroseviciene, *Effective Protection of Creditors' Interests in Private Companies: Obligatory Minimum Capital Rules vs. Contractual and Other Ex Post Mechanisms*, 3 J. SOC. SCI. STUD. 213–28 (2010).

109 Cowton, *supra* note 46, at 22.

110 Petroseviciene, *supra* note 108, at 213.

111 *Id.*

112 EC II Directive on Company Law, art. 17 (1976); Armour, *supra* note 4, at 355–78.

113 MCLAUGHLIN, *supra* note 4, at 138–49.

114 *Id.* at 180–96.

stipulating that the company will bear losses only up to the limit of its share capital, while shareholders are responsible for covering any more losses.[115]

Nations that impose minimum capital requirements prohibit the reduction of a company's capital below the legally mandated minimum. These laws exist to protect the interests of creditors by requiring companies to keep a minimum amount of capital as a hedge against potential financial problems. Like Ethiopian law, Delaware law allows the reduction of company capital as a principle and provides guidelines for such reductions.[116] Nevertheless, it forbids companies from decreasing their capital unless the remaining assets of the company, after the reduction, are sufficient to satisfy all existing debts owed by the company.[117] This limitation is enforced to protect the monetary concerns of creditors. The duty of any shareholder who has not entirely paid for their shares shall not be absolved by any reduction in capital. Essentially, the responsibility of shareholders to fulfill their share payments remains unchanged by the capital reduction.[118] This also applies to the situation in Ethiopia.[119]

In Australia, until 1998, the law recognized the maintenance of capital rule to protect corporate creditors' interests from the adverse effects of the privilege of limited liability.[120] If a company could freely reduce its share capital, it may result in insufficient funds to meet the creditor's claims.[121] Moreover, until 1998, Australian companies were prohibited from issuing shares at a discount per value. However, in 1998, Australian law stopped relying on the share capital and the per-value rules, and the liability of shareholders became limited only to the extent of their unpaid share subscriptions.[122] As a principle, Australian law does not prohibit the reduction of share capital. Companies may reduce their share capital to protect various legitimate interests. However, following the reduction, the law aims to ascertain that such transactions do not result in the company's insolvency, are fair and reasonable to the company's shareholders, and are approved by the company's general meeting.[123]

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115 ALLEN ET AL., *supra* note 3, at 124.

116 DGCL §§ 154, 244 (a)(1–4).

117 *Id.* at § 244 (b).

118 *Id.* at § 244 (a)(1–4), (b).

119 Commercial Code, *supra* note 17, at arts. 442–61, 462–68.

120 *Beck v. Weinstock (*2013) 251 CLR 425; (2013) HCA 15; *Connective Services Pty Ltd v. Slea Pty Ltd* (2019) HCA 33.

121 *Re Exchange Banking Company* (1882) 21 Ch D 519; *Trevor v. Whitworth* (1887) 12 APP Cas 409.

122 Australian Company Law Review Act 1998 § 254C; *Commissioner of Taxation v. Consolidated Media Holdings Ltd* (2012) 293 ALR 257; (2012) HCA 55.

123 Australian Corporations Act 2001 §§ 256A, 256B(1)(2), 256C(1); *Re CSR Ltd* (2010) 265 ALR 703; (2010) FCAFC 34; *Re Molopo Energy; Molopo Energy Ltd v. Keybridge Capital Ltd* (2014) NSWSC 1864; *St George Bank Limited v. Commissioner of Taxation* (2009) 256 ALR 391; [2009] FCAFC; *Alcan (NT) Alumina Pty Ltd v. Commissioner of Territory Revenue* (2009) 239 CLR 27.

Suppose the companies do not undertake the reduction in the manner required by law. In that case, it results in severe sanctions such as civil penalties, directors' liability for insolvency trading, fines, or imprisonment, and interested parties can claim injunction and damages against the company.[124] Within the EU, a minimum capital requirement of €25,000 is enforced as the minimum barrier to establishing a public limited company.[125] However, the power to determine the minimum amount of capital private enterprises must have is assigned to individual member states.[126] Most EU nations establish a minimum threshold for minimum capital, which has little effect on the interests of creditors. The EU also undertakes periodic revisions to alleviate the capital requirements progressively.[127] Unlike the U.S., and more similar to Ethiopia, the EU mandates that companies adhere to a mandatory capital maintenance regulation. This regulation aims to protect creditor's rights by mandating companies to swiftly commence insolvency procedures in the case of a substantial decrease in their legal capital.[128]

The minimum capital requirements in the U.S. vary among states, ranging from insignificant sums (e.g., $1,000) to complete elimination of such requirements. Delaware does not have a specified minimum capital requirement to establish a company.[129] There is no minimum share capital requirement in Australia for Private Limited companies. The authorized capital or par value requirements for shares were eliminated in 1998. However, the law requires the fulfillment of additional requirements to register a company. It also requires that a company have at least one shareholder without stating the minimum paid-up amount.[130] In India, the formation of a company does not always require minimum capital. However, many companies opt to stipulate it. Nonetheless, the legislation grants companies the authority to set a minimum capital by specifying the minimum amount and the matching quantity of shares, which is allocated in

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124 Australian Corporations Act 2001 §§ 256D (1–4), 588G (1 (A)), 1324.

125 The EU II Capital Directive 1976, arts. 6–9; U.K. Companies Act 2006 §§ 761–65; Germany imposes 50,000 for public limited companies, Spain imposes 60,000 Euros; U.K. Companies Act 1985 § 118.

126 EU Second Company Law Directive, art. 17.

127 John Armour et al., *Transactions with Creditors*, *in* THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH, *supra* note 18; EUROPEAN CORPORATE GOVERNANCE INSTITUTE, MODERNISING COMPANY LAW AND ENHANCING CORPORATE GOVERNANCE IN THE EUROPEAN UNION – A PLAN TO MOVE FORWARD 18 (2003).

128 EU Second Company Law Directive art. 17; Commercial Code, *supra* note 17, at arts. 463, 466–67, 468(1); for Germany, refer to AktG (Stock Corporation Act) § 92 (2) & GmbHG (Act on limited liability company) § 64; for Switzerland, refer to Swiss Companies Act arts. 725, 817.

129 DGCL §§ 151–59, 154; Delaware Code 1953, Title 8, § 154; Del. Laws, c. 50, Title 56; Del. Laws, c. 106, § 2; Title 59, 74 Del. Laws, c. 326, § 4; 77 Del. Laws, c. 253, § 15; ALLEN ET AL., *supra* note 3, at 123–67.

130 Australian Corporations Act 2001 §§ 114, 117 (2(1)), 117(2(K)); Company Law Review Act 1998 § 254C.

the memorandum of association.[131] Japan made a notable advancement in 2006 by eliminating its comparatively high minimum capital requirement for establishing a company. This modification deviated from the prior strict capital requirements, indicating a shift towards more adaptable regulations in the company establishment process.[132]

Generally, capital requirement regulations are strongly criticized for being insufficiently large (and hence insignificant). Employing a predetermined sum is regarded as inadequate to capture the full extent of the possible risk that the company and creditors may encounter. These regulations are criticized for their tendency to provide false information to creditors and shareholders and unnecessarily delay the incorporation process.[133] Consequently, nations including the U.K.,[134] U.S., Australia, New Zealand, Spain, Lithuania, Estonia, Latvia, Malta, and Ethiopia implemented lenient requirements or eliminated the minimum capital requirement.[135]

Minimum capital requirements are mostly implemented in nations that follow civil law. Germany possesses a pervasive legal capital framework. The application of this principle has declined in common law jurisdictions, including the U.K., U.S., Australia, and New Zealand, where it was formerly utilized to protect creditors' rights.[136] Furthermore, EU states have more advanced regulations regarding minimum capital and capital maintenance requirements than the U.S.[137]

(2) The minimum capital requirement in Ethiopia.

Ethiopia's minimum capital requirement applies to share companies and private limited companies.[138] The Ethiopian company law defines a share

131 Indian Companies Act 2013 §§ 2(8), 2(15), 2(50), 2(64), 4(1(e)), 43–72; *SNDP Yogam, Quilon, re*, (1970) 40 Comp Cas 60; ILR 1969 Ker 516: (1970) 1 COMP. L. J. 85 (India), the minimum amount of capital stated in the memorandum becomes the authorized capital of the company.

132 Japanese Commercial Code, art. 168(4); Japanese Companies Act 2005, art. 9.

133 Petroseviciene, *supra* note 108, at 213–28.

134 U.K. Companies Act 2006 §§ 9(4), 10(2), 555(2), 555(2–4), 761, 767 (3). The Companies Act 2006 imposes a minimum share capital requirement on public companies; U.K. Companies Act 1985 § 121; WILD & WEINSTEIN, *supra* note 19, at 118–57.

135 *See* U.K. Companies Act 1985 §§ 111–18; Spanish Company Law (LSC), arts. 4, 5; Commercial Code *supra* note 17, at art. 247, 306; Luca Enriques & Martin Gelter, *Regulatory Competition in European Company Law and Creditor Protection*, 7 EUR. BUS. ORG. L. REV. 417 (2006); Hylda Boschma & et al., *The Reform of Dutch Private Company Law: New Rules for the Protection of Creditors*, (2007) 8 EUR. BUS. ORG. L. REV 567 (2006).

136 *See* John Armour, *Legal Capital: An Outdated Concept?*, 7 EUR. BUS. ORG. L. REV. 1 (2006).

137 ALLEN ET AL., *supra* note 3, at 123–67.

138 Commercial Code, *supra* note 17, at arts. 245–494 (Share Companies), 495–533 (Private Limited Companies, closed companies). However, this study mainly emphasizes Ethiopian Share Companies.

company and a private limited company.[139] In Ethiopia, the minimum capital requirement for creating a share company remained unaltered at 50,000 Birr (equivalent to 825 Euros), even though the New Code was introduced six decades after the Old Code. This enduring capital requirement remains unchanged despite the country's economic advancement.[140] Similarly, the New Code maintained the minimum capital required for establishing a private limited company at 15,000 Birr (248 Euros).[141] However, the New Code raised the minimum value of each share from 10 to 100 Ethiopian Birr and prevented the company from issuing shares below their par value.[142]

Private limited companies' minimum par value per share must be at least 100 Ethiopian Birr. Although it is required that all shares possess the same par value,[143] companies can issue shares at a price that is higher than their par value as long as it is in line with the company's interests, shareholders, and creditors. This might be specified in the company's memorandum or established via a resolution at an extraordinary general meeting of the shareholders.[144] The aforementioned rules suggest that whereas in the 1960s, the stipulated minimum capital was substantial, it is now insignificant for commencing corporate activities, thereby significantly diminishing the chances of creditors fully collecting their loan. But to increase the likelihood of creditors and shareholders being able to recoup their investments, the New Code prohibits the formation of a company unless the total capital is subscribed to and at least 25% of the nominal value of the shares sold is paid. The payment must be deposited in a designated bank account that is only accessible to the company being established.[145]

According to Ethiopian company law, the company has the right to adjust its capital for various reasons using different methods, subject to the approval of the extraordinary general meeting of shareholders.[146] The impact of changes in a company's capital on the interests of creditors is apparent. For example, a company can raise its capital by issuing new shares to the public or current owners, who may have preferential rights to buy these new shares. Another way to grow

139 *Id.* at arts. 245–53, 254–67, 495(1–5), 304(1, 2), 342 (liability to meet calls). Refer to the discussions in Section 1.2.1 of this study on the definition and requirements of Share Companies and Private Limited Companies.

140 *Id.* at art. 247(1), 306(1), 312. In 1960, the amount was considerable, but it has not been amended since then, making it a negligible amount to commence company activities.

141 *Id.* at art 496(1).

142 *Id.* at art. 247(2).

143 *Id.* at art. 496(2).

144 *Id.* at art. 268(1–2).

145 *Id.* at arts. 244(1–4), 281(1, 2), 282(1, 2).

146 *Id.* at arts. 442(1–4), 462.

capital is by raising the nominal value of the existing shares.[147] Similarly, a company may undergo a capital reduction due to financial losses, which can be done by decreasing the nominal value of shares or exchanging existing shares for a smaller amount.[148] Increasing a company's capital is not expected to harm the rights of its creditors and shareholders; instead, it is anticipated to benefit their interests. In contrast, decreasing a company's capital is likely to harm the interests of shareholders, especially the company's creditors.

Under the theory of limited liability, the company's obligations must be paid only from the remaining assets and capital. These assets jointly serve as pooled collateral, ensuring the repayment of obligations owed by the company. Hence, Ethiopian company law diligently protects the privileges of shareholders and, specifically, the rights of the company's creditors to challenge (and claim compensation for) the decrease in the company's capital if it harms their interests. For example, if a special meeting of shareholders approves a resolution allowing a decrease in the company's capital, the law requires the company to compensate shareholders for the decrease in the number or value of their shares. Before any earnings distribution, offering this compensation is imperative.[149] The law guarantees the rights of an unpaid creditor (who has rights before the adoption of a resolution to lower the company's capital) or a creditor who does not have enough guarantees to satisfy their claim to challenge the approval of a resolution to reduce the company's capital. This opposition by creditors is acceptable until the capital is restored to its original level when the claim was made.[150]

On the other hand, the law does not allow for decreasing a company's capital below the required legal minimum. Although the company can temporarily decrease its capital below the allowed minimum due to losses, restoring the capital to the minimum required by law is mandatory within one year from the publication date of the reduction in the company register.[151] The law explicitly forbids decreasing the company's initial capital, as doing so below the required minimum would indicate that the company does not have the necessary resources to carry out its regular business activities, let alone promptly fulfill its financial obligations to creditors. Per the aforementioned considerations, if a company's capital is reduced below the legally required minimum, it can harm the interests of its creditors. To protect creditors' rights, the law allows them to challenge the

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147 *Id.* at arts. 442–61.

148 *Id.* at arts. 462–66.

149 *Id.* at art. 466.

150 *Id.* at art. 467; Commercial Code of Ethiopia (1960) arts. 490–94 (Eth.) [hereinafter Commercial Code of Ethiopia 1960].

151 Commercial Code, *supra* note 17, at arts. 463, 468(1).

approval of a resolution to reduce capital until the capital is restored to the minimum amount required by law.[152]

If a company chooses to reduce its minimum initial capital and fails to either increase the capital to the required minimum within a year or convert the company into another type of business organization that is suitable for the reduced capital, such as transforming into a private limited company with an initial capital of only 15,000 Birr, the law implements further actions. This provision guarantees the entitlements of shareholders and, more specifically, creditors to request the court to issue an order to dissolve the company.[153] If the company's capital is reduced by more than 10%, every creditor who had rights against the company before the announcement of the capital reduction resolution has the right to challenge the reduction within three months after the publication.[154] Subsequently, the creditor can petition the court for payment or obtain adequate guarantees to resolve the debt.[155] Any decrease in the company's capital must not be carried out in a way that undermines the equal treatment of owners and creditors.[156] Ultimately, to protect the rights of creditors, the company itself, and the shareholders, Ethiopian company law considers the loss of 75% of a company's capital as a substantial reason for its dissolution.[157]

b) Dividend restrictions.

The dividend restriction regulation comprises several prohibitions regarding the payout of dividends, constraints on share repurchases, and restrictions on undervalued transactions. The following sections thoroughly analyze each of these features in a specific order.

(1) Prohibitions on distribution of dividends.

(a) Prohibitions on distribution of dividends in general.

This rule explicitly addresses the limitations imposed on distributing funds to shareholders, aiming to protect creditors from any potentially exploitative behavior by the borrower. To prevent capital depletion, issuing dividends to shareholders from the share capital that the company initially acquired from its

152 *Id.* at arts. 467, 468(2).

153 *Id.* at arts. 467, 468(3).

154 *Id.* at arts. 466, 468(2), 471(1–3).

155 *Id.* at art. 467.

156 *Id.* at art. 470.

157 *Id.* at art. 473(1(c)–5); per article 532 of the same code, in the case of a Private Limited Company, where three–quarters of the capital is lost, the board of directors (if any) or the manager will have the members decide whether to dissolve the company. However, if the members decide not to dissolve the company, they will need to make additional contributions to restore the capital.

shareholders is typically forbidden.[158] If distributions to shareholders are not provided from the company's earnings, they will decrease the company's net assets, which increases the likelihood of default.[159] Additionally, this reduces the anticipated value of claims held by creditors.[160] In the U.K., the law requires that dividend payments only come from net profits, and any transfer of company assets to shareholders is prohibited. There is an exception if the distribution value is less than the profits available.[161] This clause protects creditors and shareholders by forbidding any decrease in the company's capital.[162] Distributions made in violation of the law are considered illicit dividends that must be reimbursed.[163] While the U.K. has stringent regulations, these vary across countries, with Germany, for example, having some limitations and the U.S. having no enforced limits.[164]

Although there may be variations in the U.S. depending on the state, the general rule is that companies can distribute dividends from the excess funds in their capital accounts and retained profits. Companies are generally forbidden from distributing dividends in the event of insolvency or when their assets are lower than their liabilities.[165] For example, in Delaware, companies can distribute dividends using funds from their excess capital. However, with no excess, companies can only distribute dividends from their net earnings for the specific

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158 WILD & WEINSTEIN, *supra* note 19, at 160–72.

159 Armour, *supra* note 136, at 355–78; U.K. Insolvency Act 1986 § 238.

160 Laurence Booth & Jun Zhou, *Dividend Policy: A Selective Review of Results from Around the World*, 34 GLO. FIN. J. 1, 15 (2017).

161 U.K. Companies Act 2006, *supra* note 14, at §§ 641, 829, 830 (1, 2), 831, 832 (4), 829–853, 580; U.K. Companies Act 1985, *supra* note 125, at § 263; German Company Law §§ 30, 43 (1); Council Directive 77/91/EEC, 1976 O.J. (L 26/1) [hereinafter The EC Second Company Law Directive], arts. 15–16; SEALY & WORTHINGTON, *supra* note 1, at 512–555.

162 Any distribution in contravention of Part 23 of the U.K. Companies Act 2006 constitutes a Fraudulent Transfer and Breach of the Directors' Fiduciary Duty not to misapply company property; U.K. Companies Act 2006, *supra* note 14, at § 178 (2).

163 U.K. Insolvency Act 1986, *supra* note 91, at § 423; Wood v Odessa Waterworks Co (1889) 42 Ch D 636(U.K.); In re Exchange Banking Company (1882) 21 Ch D 519 (CA); In re Severn and Wye and Severn Bridge Railway Company (1896) 1 Ch 559; Aveling Barford Ltd v Perion Ltd (1989) BCLC 626; Re Halt Garage (1964) Ltd [1982] 3 All ER 1016; Precision Dippings Ltd v Precision Dippings Marketing Ltd (1986) Ch 447 (CA); Bairstow v Queens Moat Houses Plc (2001) 2 BCLC 531.

164 Irina Fox, *Protecting all Corporate Stakeholders: Fraudulent Transfer Law a Check on Corporate Distributions*, 44 DEL. J. CORP. L. 82–114 (2020).

165 8 Del. C. 1953, § 170; 56 Del. Laws, c. 50; 56 Del. Laws, c. 186, § 9; 59 Del. Laws, c. 106, § 5; 64 Del. Laws, c. 112, § 17; 67 Del. Laws, c. 376, § 5; 69 Del. Laws, c. 61, § 3; 72 Del. Laws, c. 123, § 3; 77 Del. Laws, c. 253, § 18; Model Bus. Corp. Act § 6.40 (Am. Bar Ass'n 2002).

fiscal year in which the dividend is announced.[166] According to Delaware law, a director is responsible for providing illegal dividends to stockholders.[167]

Before 2010, companies were allowed to pay dividends from their profits in Australia. However, since 2010, this requirement has been amended to better protect creditors' interests. Accordingly, a company must not pay a dividend unless: (1) the company's assets exceed its liabilities immediately before the dividend is declared and the excess is sufficient for the payment of the dividend; (2) the payment of the dividend is fair and reasonable to the company's shareholders as a whole; and (3) the payment of the dividend does not materially prejudice the company's ability to pay creditors. For example, the payment of dividends would materially prejudice the company's ability to pay its creditors if it became insolvent due to the payment. Failure to comply with this rule results in the liability of directors for insolvent trading.[168]

In India, companies are prohibited from declaring or distributing dividends for a financial year unless the funds originate from the company's profits for that particular year after accounting for depreciation, or from the company's earnings for any previous financial year(s) considering depreciation.[169] Japanese companies are prohibited from distributing profits unless they own assets worth a minimum of 3 million yen (equivalent to $19,400).[170] The U.K.[171], U.S.,[172] and Germany[173] have laws restricting distributions under fraudulent transfer regulations. Furthermore, the directors bear responsibility for the illegal dissemination of dividends.[174]

(b) Prohibitions on distribution of dividends in Ethiopia.

In Ethiopia, shareholders have the right to receive a share of the yearly net profits and a percentage of the net proceeds when the business is dissolved. The

166 8 Del. C. 1953, §§ 154, 170(a), 172–73, 244 (a)(4); 8 Del. C. 1953, § 173; 56 Del. Laws, c. 50; 59 Del. Laws, c. 437, § 10; 65 Del. Laws, c. 127, § 5.

167 8 Del. C. 1953, §§ 160, 171-74; 8 Del. C. 1953, § 174; 56 Del. Laws, c. 50; 59 Del. Laws, c. 106, § 6; 71 Del. Laws, c. 339, §§ 26, 27.

168 Australian Corporations Act 2001, *supra* note 15, at §§ 254 T(1(A, B, C)), 588G*; Corporations Amendment Act 2010* (Cth)s 254 T (Austl.).

169 Indian Companies Act 2013, *supra* note 131, at §§ 123–27.

170 Art. 168 (4) of the Japanese Commercial Code imposes about $100,000 for AGs (Open Joint Stock Companies); Art. 9 of the Japanese GmbHG (limited liability company) imposes about $30,000 for GmbHs (Closed Corporations). SHŌHŌ [SHŌHŌ] [COMM. C.] art. 168 (4) (Japan).

171 U.K. Insolvency Act 1986, *supra* note 91, at §§ 423–25.

172 11 U.S.C. § 548(a)(1)(A) (1978); Uniform Voidable Transactions Act (UVTA) (2014) §§ 4(a)(2), 5(a) & (b); U.S. Bank Nat. Ass'n v. Verizon Communications Inc*.*, 479 B.R. 405, 411 (Bankr. N.D. Tex. 2012); Lippi v. City Bank, 955 F.2d 599, 606 (9th Cir. 1992).

173 §§ 423–25 of the U.K. Insolvency Act 1986 prohibit Transaction Defrauding Creditors; The U.K. Fraudulent Conveyance Act 1571; 11 U.S.C. § 548(a)(1)(A) (1978).

174 U.K. Insolvency Act 1986, *supra* note 91, at §§ 423–25.

amount allocated to each shareholder is decided proportionally according to their ownership interest in the company's paid-up capital.[175] Shareholders can only receive dividends from the net profits indicated in the authorized balance sheet.[176] Ethiopian law explicitly forbids the distribution of dividends from total earnings unless the company's financial sheet is approved.[177] Any earnings disbursement conducted before the financial statement's endorsement or from the company's overall profits is considered a "fictitious dividend." Individuals involved in such unauthorized disbursements may face both criminal and civil liability for their actions.[178] The law guarantees the company's entitlement to recover any dividends disbursed to shareholders in cases where there is no balance sheet or if it does not comply with the authorized balance sheet.[179]

The legislation also ensures that creditors have the right to challenge any unlawful allocation of profits.[180] If a company is dissolved, the law mandates that the liquidators must not distribute any assets to shareholders until the company's creditors have been fully compensated or a payment provision has been deposited in the court. This ensures the safeguarding of creditor interests.[181] Hence, the rule applies to restrictions on distributing earnings and allocating the company's remaining assets.

In contrast to the principle of limited liability for shareholders, the law establishes that any shareholder who enables the distribution of dividends above the legal limitations will be held jointly and severally accountable with the

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175 Commercial Code, *supra* note 17, at arts. 291(1–2), 345(1–2). Similarly, arts. 279, 291, 448–57 of the New Code state that preferential shareholders can only exercise their right to purchase new cash shares issued by the company to increase its capital in proportion to their shareholding. Moreover, to the extent of their holding, the law recognizes shareholders' voting rights and the right of preferential shareholders having priority over profits, or in the case of liquidation of the assets of the company, priority right over repayment of contributions or distributions of a share of the surplus in the winding–up. For the rules prohibiting the distribution of profits in Partnerships, see arts. 191–98, 211.

176 *Id.* at art. 438(1); Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 452–56.

177 Commercial Code, *supra* note 17, at art. 438(2); Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 458–59; per article 211 of the New Code, even in the case of General Partnerships, the partners are entitled to participate in the distribution of profits, where there is a surplus after all claims have been settled and contributions returned. The surplus shall be distributed among the partners which implies that, where the assets are insufficient to repay contributions after payment of debts, expenses, and advances, the loss shall also be distributed among the partners.

178 *Id.* at arts. 438(3–5); per art. 529 of the same code, the same holds in case a Private Limited Company, where the distribution of fictitious dividends is prohibited.

179 *Id.* at art. 439; per art. 529 of the same code, in the case of a private limited company, members may be required to repay dividends which have been paid out of sums which are not actual profits. However, such claims for repayment of fictitious dividends shall be barred by a period of limitation after five years from the date the dividends were paid.

180 *Id.* at arts. 438–41, 467; Commercial Code of Ethiopia 1960, *supra* note 150, at art. 489.

181 Commercial Code, *supra* note 17, at art. 483.

company towards creditors and the company.[182] The law expressly specifies the grounds for establishing the legality of profit distribution by precisely identifying a business's net profit. According to this definition, a company's net profits include the whole amount received throughout the financial year after deducting general expenses, additional fees, amortization, and allowances.[183] The allocation of earnings to shareholders is limited to the net profit of a certain financial year after deducting prior losses but including extra income. Furthermore, obtaining authorization from the general meeting is necessary for any disbursement from reserve money.[184]

The law explicitly states that the distribution of earnings can only occur once a transfer has been made to the company's Legal Reserve Fund.[185] Once all expenses have been settled, the allocation of reserve money, from which profits might be distributed, is delegated to the general meeting's discretion.[186] Transfers to reserve funds are exclusively permitted from the net earnings indicated in the profit and loss statement.[187] Likewise, the company can only set aside cash from its revenues for legal purposes by transferring 5% of its net profits annually.[188] However, the company's obligation to distribute funds to the legal reserve ends when the net earnings transferred to the Legal Reserve Fund reach an amount equal to five percent of the company's capital.[189]

According to Ethiopian company law, directors are only eligible to receive a yearly salary, a predefined share of the company's net profits in a specific financial year. The compensation will be deducted from the overall expenditure.[190] Nonetheless, the director's portion of the net earnings can only be disbursed when a dividend is allocated to the shareholders during that particular year.[191] Ultimately, the prohibitions specified in Ethiopian company law regarding improper dividend payments are intended to minimize opportunistic actions by corporate insiders, including directors and shareholders. These rules aim to protect the interests of creditors by prioritizing the payment of company loans, legal reserves, and other costs such as salaries and allowances.

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182 *Id.* at art. 295(6).

183 *Id.* at art. 432(1).

184 Commercial Code, *supra* note 17, at art. 432(2).

185 *Id.* at art. 436(1); per art. 528, in the case of Private Limited Companies, not less than 5% of the profits shall be transferred each year to the legal reserve until such fund amounts to 10% of the capital. Profit can only be distributed after such transfer to the reserve fund.

186 *Id.* at art. 432(3).

187 *Id.* at art. 43(1).

188 *Id.* at art. 434 (1).

189 *Id.* at art. 434(2).

190 *Id.* at art. 304(1, 2).

191 *Id.* at art. 304(2–5).

(2) Prohibitions on share repurchases.

(a) Prohibition on share repurchases in general.

This regulation imposes limitations on the acquisition of company shares to protect creditors' rights and benefits.[192] In the U.K., a limited company cannot purchase its shares until fully paid. Acquiring shares requires an initial payment, and all future repurchases of the company's shares must be supported either from earnings that may be distributed or from the explicit proceeds of a newly issued batch of shares specifically meant to finance the repurchase.[193] Share buyback is widely allowed as a core concept in the U.S. Under Delaware law, directors are immune from liability when they use the company's publicly stated net profit or surplus to redeem company shares.[194] Directors are held responsible for engaging in an illegal acquisition or redemption of stocks that involves the company and its creditors, especially in situations of dissolution or insolvency. The liability includes the amount illegally paid for purchasing or redeeming the company's shares and the interest computed from when the obligation first arose.[195]

Australian law does not generally prohibit the buyback of shares by the company, and it also recognizes many legitimate reasons and forms for companies to repurchase their shares. However, to buy back its shares, a company must notify the Australian Securities and Investments Commission (ASIC) of its intentions. Moreover, as a rule, companies cannot buy back more than 10% of their shares within 12 months, and they shall cancel all bought-back shares, notify ASIC about the cancellation, and cannot reissue such shares.[196] Non-compliance with these rules results in severe sanctions such as civil penalties, directors' liability for insolvent trading, fines, or imprisonment, and interested parties can claim injunction and damages against the offenders.[197]

Furthermore, unlike in the U.S., the U.K. prohibits providing financial aid to companies to repurchase their shares.[198] Australian company law does not generally prohibit companies from offering financial assistance to purchase its shares. However, to protect creditors' interests, the law prohibits the misuse of a company's resources by giving various forms of financial assistance (loan, gift,

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192 J.B. Heaton, *The Social Costs of Dividends and Share Repurchases*, 12 J. BUS. ENTREPRENEURSHIP & L. 361 (2019).

193 U.K. Companies Act, *supra* note 14, at § 684, 691, 692; The EC Second Company Law Directive, arts. 18–19, & 22; UK Companies Act 1985, *supra* note 125, at §§ 159–70, 263(2)(b); *Trevor v. Whitworth* [1887] 12 App. Cas. 409 (U.K.).

194 8 Del. C. 1953, § 172; 56 Del. Laws, c. 50; 56 Del. Laws, c. 186, § 10; 66 Del. Laws, c. 136, § 5.

195 8 Del. C. 1953, § 174; 56 Del. Laws, c. 50; 59 Del. Laws, c. 106, § 6; 71 Del. Laws, c. 339, §§ 26, 27.

196 Australian Corporations Act 2001, *supra* note 15, at §§ 257 (B(4), F, H), 254Y.

197 *Id.* at §§ 259 F(1–3), 588G, 1324.

198 The EC Second Company Law Directive, art. 23; §§ 151–58; The U.K. Companies Act 1985, *supra* note 125.

security, or any other benefits) to purchase its shares. Generally, it is appropriate that persons or directors who acquire company shares should buy them using their own funds and without depleting company resources.[199] Accordingly, the law allows a company to financially assist a person or a holding company to purchase shares if and only if the assistance does not prejudice the interests of the company, shareholders, or creditors (company's ability to pay), and shareholders approve it.[200] Violating the above rules results in severe sanctions such as civil penalties, directors' liability for insolvent trading, fines, or imprisonment. Interested parties can also request an injunction and claim damages against the offenders.[201]

(b) Prohibition on share repurchases in Ethiopia.

In Ethiopia, the act of repurchasing shares is not explicitly forbidden. However, the requirements put on companies for conducting share repurchases are overly strict, making compliance practically impossible. This poses a substantial obstacle to such repurchases. Therefore, a company in Ethiopia can acquire its shares directly from shareholders or take shares as collateral from its owners if this purchase is approved through a shareholders' meeting. The cash used for the acquisition must originate only from the company's net earnings, and the company must pay off the shares in question.[202]

The imposition of stringent conditions, such as requiring full payment for the company's shares and funding purchases exclusively from the company's net profits, aims to safeguard the company's capital. This is because shareholders are unlikely to approve share repurchases that reduce the company's working capital. This safeguarding mechanism is used to protect and prioritize the best interests of both creditors and shareholders. If the specific standards are unmet, the company is prevented from buying back its shares. This limitation is implemented to prevent possible harm to the interests of creditors and shareholders, emphasizing the significance of preserving the financial integrity and stability of the company. The law also forbids the company from buying back its shares if the decision is made by a general meeting of shareholders to reduce its capital. This

199 HARGOVAN ET AL., *supra* note 2, at 342–57.

200 Australian Corporations Act 2001, *supra* note 15, at §§ 260A(2), B, C; *Connective Services Pty Ltd v. Slea Pty Ltd* [2019] HCA 33 (Austl.); *ASIC v. Adler* [2002] 41 ACSR 72 (Austl.); *Re VGM Holdings Ltd* [1942] Ch 235 (Can.); *Firminv. Gray & Co Pty Ltd* [1984] 8 ACLR 865 (Austl.); *E H Dey Pty Ltd (in liq) v. Dey* [1966] VR 464 (Austl.); *Independent Steels Pty Ltd v. Ryan* [1990] VR 247 (Austl.); *Coeur De Lion Investments Pty Ltd v. The President's Club Ltd* [2020] FCA 204 (Austl.).

201 Australian Corporations Act 2001, *supra* note 15, at §§ 256D(1–4), 588G(1 (A)), 1324.

202 Commercial Code, *supra* note 17, at art. 275(1, 4); Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 332(1, 5), 400.

ban directly protects the interests of corporate creditors, reinforcing the regulatory position against conduct that might harm the company's financial stability.[203]

The law also temporarily revokes the voting privileges connected to these redeemed shares to prevent any possible exploitative behavior by company insiders, particularly the management, who may take advantage of the rights and advantages associated with repurchased shares. In addition, it explicitly forbids directors from disposing of shares obtained by repurchasing from shareholders. This rule aims to protect the long-term benefits of both shareholders and creditors. The law also grants the company the authority to compensate (repay) the shareholders at the nominal value of their shares. However, the reimbursement should be carried out utilizing net earnings or reserve money, guaranteeing that it does not diminish the company's capital.[204] As previously said, if the company is dissolved, the shares the company redeems do not grant any right to claim refund of contributions.[205]

Unlike the U.S., the U.K. and Ethiopia have strict regulations prohibiting providing financial aid to a company to acquire its shares.[206] To summarize, buying back a company's shares harms the company's capital, resulting in decreased capital and increased risk for creditors.

(3) Prohibition on undervalued transactions.

(a) Prohibition on undervalued transactions in general.

This notion refers to trading economic value between the company and a shareholder at a reduced price or with very advantageous contractual conditions that the company would not have agreed to when dealing with an unconnected third party.[207] It is alternatively referred to as "disguised dividend" or "hidden asset distributions."[208] Following the Second EU Directive, Germany fully outlawed concealed distributions, setting it apart from the U.K. and other countries.[209] In

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203 Commercial Code, *supra* note 17, at art. 275(3); Commercial Code of Ethiopia 1960, *supra* note 150, at art. 332(3).

204 Commercial Code, *supra* note 17, at art. 280 1).

205 *Id.* at art. 280(2).

206 The EC Second Company Law Directive, art. 23; U.K. Companies Act 1985, *supra* note 125, at §§ 151–58; Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 334, 409.

207 Undervalued transactions refer to asset transfers at less than market value or the debtor's sale or transfer of assets to third parties shortly before their insolvency. Moreover, undervalue transactions may take the form of selling property for less than the asset's market value or purchasing something at a greater consideration than its value; VULNERABLE TRANSACTIONS IN CORPORATE INSOLVENCY 37–123 (John Armour & H.N. Bennett eds. 2003).

208 U.K. Insolvency Act 1986, *supra* note 91, at § 238, a liquidator could seek to recover the payments as a transaction at an undervalue in favor of connected persons if the company is in a state of factual insolvency; also refer to the decision in *Aveling Barford Ltd. v. Perion Ltd.* [1989] BCLC 626.

209 The EC Second Company Law Directive, arts. 15–16; Mulbert, *supra* note 82, at 357–408.

the U.S., such transactions are not intrinsically forbidden. For example, in Delaware, companies can provide loans, guarantee obligations, or aid any officer or employee of the company or its subsidiary, as long as it is deemed beneficial for the company. This includes those who hold positions as both officers or employees and directors of the company or its subsidiary. Companies in Delaware have the legal power to provide assurances or promises to other companies based on common law.[210]

In Australia, a company, as a separate legal entity, can enter into contractual relations with its members, thereby controlling shareholders or directors.[211] However, Australian law generally prohibits transactions (transfers) made by the debtor (*transferor*) who later becomes bankrupt with another person (*transferee*) if the transaction took place in the period beginning five years before the commencement of the insolvency and ending on the date of the insolvency and the transaction is made not for consideration or consideration less than the market value of the property.[212] Moreover, the law prohibits intentional transfers to defeat creditors and transfers where the consideration was paid to a third party.[213]

(b) Prohibition on undervalue transactions in Ethiopia.

Undervalue transactions are explicitly forbidden in Ethiopia as a fundamental principle. Therefore, a company cannot issue its shares before the specified payment, as mandated by the law and the memorandum of association. It is forbidden for a company to provide prepayments on its shares or provide loans to assist other parties in obtaining shares.[214] The law prohibits a company from giving a loan to a director or its holding company to provide a guarantee or security for a loan given by any individual to that director unless the transaction is approved in advance by a resolution of a general company meeting.[215] This approval must follow a mandatory review of a written report from an independent and impartial external auditor.[216] The report should provide details about the transaction, including the loan amount, its purpose, and the extent of the company's liability concerning any transaction connected to the loan.[217] The law also forbids any transactions between a company and persons or organizations

210 8 Del. C. 1953, §§ 143–46; 8 Del. C. 1953, § 143; 56 Del. Laws, c. 50.

211 Andar Transport Pty Ltd v. Brambles Ltd [2004] 206 ALR 387 (Austl.); Lee v. Lee's Air Farming Ltd [1961] AC 12.

212 Australian Bankruptcy Act of 1966 (Cth)s 120 (Austl.).

213 *Id.* § 121A.

214 Commercial Code*, supra* note 17, at art. 277; Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 334, 409.

215 Commercial Code*, supra* note 17, at art. 30(1).

216 *Id.* at art. 307(2).

217 *Id.* at arts. 307(1–3), 356, 357.

associated with the company unless these transactions are authorized by the board of directors and shareholders who possess at least 10% of the company's assets in a formal meeting.[218]

Any transactions that do not have prior permission from the board of directors and are not reported to the auditors, who are required to report to the general meeting for approval, will be considered invalid.[219] On top of this, shareholders are only permitted to reject transactions approved by the general meeting if they can demonstrate significant harm to the company or fraudulent activity.[220] The law also prohibits shareholders from engaging in criminal activities that have a similar effect to undervalued transactions. This encompasses deliberately participating in illegal activities that put the company's interests, shareholders, or creditors at risk. Prohibited activities include mixing the company's property with personal assets, blurring the line between the company's identity and their own, using the company as a cover to pursue personal interests or the interests of others, and taking company assets for personal or third-party gain without the approval of the appropriate management body.[221] The aforementioned rights bestowed upon corporate creditors regarding the prohibition of undervalued transactions are intended to safeguard their interests. This is accomplished by protecting the company's assets from depletion and reducing conflicts of interest and insider trading.

c) Directors' duties to creditors.

(1) Directors' duties to creditors in general.

Directors are legally obligated to act in the best interests of the company they work for and its shareholders. Directors of solvent companies in France,[222] the U.K.,[223] India,[224] and the U.S. are not obligated to fulfill fiduciary obligations towards creditors beyond what is specified in the appropriate contractual provisions.[225] In the aforementioned nations, the responsibility of enforcing fiduciary obligations usually lies with the board or the shareholders as long as the

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218 *Id.* at art. 306(1, 2). The law defines such affiliated persons.

219 *Id.* at arts. 306(4–6), 394, 395.

220 *Id.* at art. 306(3).

221 *Id.* at art. 295(1–6).

222 Code de commerce [C. Com.] [Commercial Code] arts. L. 223–252 (Fr.) [hereinafter French Commercial Code].

223 Companies Act 2006, *supra* note 14, §§ 170–82, 231 (setting out directors' duties); Percival v. Wright (1902) 2 Ch. 421 (U.K.); BTI 2014 LLC v Sequana SA and Others (2019) EWCA Civ 112 (Eng.).

224 Companies Act, 2013, *supra* note 14, §§ 149–95. The provisions set out the general duties and liabilities of directors towards the company and creditors.

225 DGCL, *supra* note 13, §§ 141–46, 365; Anil Hargovan & Timothy M. Todd, *Financial Twilight Re–Appraisal: Ending the Judicially Created Quagmire of Fiduciary Duties to Creditors*, 78 U. PITT. L. REV. 135–80 (2016).

company is financially stable. The persons mentioned possess the authority to commence derivative proceedings on behalf of the company. However, corporate creditors cannot make claims against directors for violating fiduciary responsibilities in these situations.[226]

Contractual agreements generally regulate the relationship between directors and creditors. Creditors have the authority to initiate legal proceedings against the organization in cases of violations of certain contractual, tort, and statutory responsibilities. Directors may face accountability towards creditors due to civil culpability for mishandling the company's assets.[227] In the U.K., directors are legally responsible to creditors when a company's assets are insufficient to repay its debts owing to insolvency. In times of insolvency, creditors' rights are given priority, which justifies their power to supervise and manage the company's assets through insolvency proceedings. These assets collectively serve as collateral for the recovery of debts.[228] The same holds for India.[229] In Delaware, if a company becomes insolvent and has not filed for federal bankruptcy, the directors must prioritize the interests of corporate creditors and shareholders as part of their fiduciary obligation.[230]

Australian law also imposes strict duties on company directors. Accordingly, directors must act with care and diligence, in good faith, in the company's best interest, and they should not allow the company to incur debts when it is insolvent. Directors also have the duty not to confer benefits to related parties or receive various benefits from the company. Directors must also be familiar with the company's business and continuously and independently manage and monitor the company.[231] The law holds directors strictly liable for the breach of their duties. Moreover, on the grounds of public policy and creditors' protection, directors can be personally liable for corporate debts incurred during trading while insolvent.[232] In Australia, directors' duties are enforced by the company and ASIC, and such

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226 DGCL, *supra* note 13, § 325(a, b); 56 Del. Laws, c. 50; 71 Del. Laws, c. 339, § 71; Alessandra Zanardo, *Fiduciary Duties of Directors of Insolvent Corporations: A Comparative Perspective*, 93 CHI.–KENT L. REV. 867–96 (2018).

227 DGCL, *supra* note 13, § 326; 56 Del. Laws, c. 50; 71 Del. Laws, c. 339, § 72; SEALY & WORTHINGTON, *supra* note 1, at 309–462; *see* HARGOVAN ET AL., *supra* note 2, at 417–558.

228 THE WORLD BANK, *supra* note 102, at 18–19 (2021); Companies Act 2006, *supra* note 14, § 172(3); MacPherson v. European Strategic Bureau (2000) 2 B.C.L.C. 683.

229 Companies Act, 2013, *supra* note 14, §§ 326–43.

230 Credit Lyonnais Bank Nederland v Pathe Comm. Corp., (Del. Ch. Dec. 30, 1991); DGCL, *supra* note 13, §§ 141–46, 291.

231 Corporations Act 2001, *supra* note 15, §§ 180–84, 588G; HARGOVAN ET AL., *supra* note 2, at 417–511.

232 Corporations Act 2001, *supra* note 15, §§ 197, 588G; *Daniels* v *Anderson* (1995) 37 NSWLR 438.

enforcement actions may result in extensive penalties against directors who are at fault, such as fines and disqualification from office.[233]

Essentially, the directors can be sued by the creditors for violating their fiduciary duties, but only in a derivative manner and only after the business has become insolvent.[234] This requirement is mandated to ensure that if the directors of the company neglect to take essential actions, creditors—who are often unaware of the company's unstable financial condition—are protected from potential harm caused by the company's continued operations. Conversely, when a company is close to insolvency, the probability of it regaining a stable financial position decreases rapidly.[235] Within this framework, the German responsibility for late submission of bankruptcy claims and the English responsibility for improper trading or violation of a fiduciary duty in prioritizing creditor interests can be seen as functionally identical, sharing a common dual goal. The primary objective of these initiatives is two-fold: firstly, to discourage directors by ensuring that they are held responsible for complying with the legally mandated requirements for protecting creditors, and secondly, to provide compensation to creditors who suffer losses as a result of non-compliance.[236] To summarize, the EU has more extensive laws that control the responsibilities of directors, with the specific goal of protecting the interests of creditors. This is in contrast to the U.S.[237]

(2) Directors' duties to creditors in Ethiopia.

(a) Directors' duties to creditors during insolvency in Ethiopia.

Explicit provisions in Ethiopian insolvency law outline the duties and liabilities of directors and other parties participating in insolvency procedures. These rules also address the consequences if these individuals fail to fulfill their duties during or near insolvency. Facing the possibility of insolvency, managers and directors have a primary responsibility to protect the interests of creditors and must take all necessary actions to prevent insolvency. Failure to comply with this requirement results in legal repercussions.[238] The law clearly defines the duties and liabilities of individuals or entities who are owed money by the bankrupt debtor,

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233 *ASIC* v. *Vizard* (2005) 23 ACLC 309; (2005) FCA 1037; *Gillfillan* v. *ASIC* (2012) 92 ACSR 460l; (2012) NSWCA 370; *ASIC* v *Macdonald* (No 11) (2009) 256 ALR 199; (2009) NSWSC 287; *ASIC* v. *Hellicar* (2012) 286 ALR 501; (2012) HCA 18.

234 Andrew Keay, *In Pursuit of the Rationale Behind the Avoidance of Pre–Liquidation Transaction*, 18 SYD. L. REV. 55–86 (1996).

235 *Id.*

236 BACHNER, *supra* note 79, at 247; In Re Horsely & Weight Ltd. (1982) Ch 442 (U.K.); Facia Footwear Ltd v. Hinchcliffe (1998) 1 BCLC 218 (UK); *Walker v Wimborne* (1975–1976) 137 CLR 1 (Austl.).

237 French Commercial Code, *supra* note 222, arts. L. 223–24, 225–51, 651–52; German Company Law (GmbHG) §§ 43–49 & AktG § 214(4); U.K. Insolvency Act of 1986 § 116.

238 Commercial Code, *supra* note 17, at arts. 699(1–2), 803(1–3).

individuals or entities who own shares in the debtor company, and individuals or entities who have made claims against the debtor, either during or close to the company's state of financial insolvency.[239]

Directors are accountable for the harm caused to creditors if they continue operating the company while being aware or reasonably expecting that the company cannot fulfil its financial commitments to creditors.[240] In the same way, directors are held fully responsible by law when the company's ability to meet financial obligations decreases or when the company decides to stop making debt payments while simultaneously seeking relief through preventive restructuring, reorganization, or bankruptcy proceedings, as deemed appropriate.[241] In all forms of insolvency procedures, the law protects the debtor's remaining assets and restricts strategic activities by corporate insiders against creditors, such as preferential treatment. The law also allows for the invalidation of many actions by debtors during the Suspect Period with the official request of the required organ to the court.[242]

To make it easier for creditors to exercise their rights and protect their interests, the law precisely defines the actions that can be invalidated, either as a requirement or as a choice. The law specifies the activities and payments that are not subject to being declared invalid, identifies the party responsible for submitting applications, establishes the deadline for submitting applications, and explains the consequences of retroactive invalidation.[243] The responsibility to safeguard creditors' interests also continues to exist even when a company is dissolved. Accordingly, the liquidators cannot participate in new business activities unless necessary to complete existing contracts or for the winding-up process's interests, as mandated by the law. Any departure from these limitations makes the liquidators responsible, both as a group and individually, to the company, creditors, or other parties for any business activities that go beyond the authorized limits of their authority.[244]

The Ethiopian company law also specifies the responsibilities of liquidators managing the liquidation process of a company undergoing dissolution. During

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239 *Id.* at arts. 804–06.

240 *Id.* at art. 329(1); Article 206(1) of the New Code during the dissolution of a General Partnership allows the managers to retain their powers until the appointment of a liquidator to dissolve the partnership. However, they are prohibited from commencing a new business after a decision to dissolve the partnership has been made.

241 *Id.* at art. 315(6–g); similarly, article 424 states that where the debtor company's ability to pay its debt diminishes or the company suspends payment, the agent of the debenture holders, if any, shall prove for all debenture holders in the preventive restructuring, reorganization, or bankruptcy proceedings. The agent shall receive on their behalf all notices of meetings.

242 *Id.* at arts. 671(1–5), 766.

243 *Id.* at arts. 671–77, 767.

244 *Id.* at art. 482(1–2).

company dissolution, the law guarantees that creditors have the right to demand compensation from liquidators if the incompetence of those liquidators causes non-payment.[245] Liquidators are also legally obligated to fulfill several rigorous duties throughout the company dissolution process to protect the creditors' interests from adverse outcomes.[246] Ethiopian insolvency law also deters illegal behavior during insolvency by implementing many prohibitions, limits, and criteria for incompatibility. These measures apply to individuals who violate the law or their responsibilities as creditors, managers, or directors. These measures restrict their ability to exercise particular rights, get benefits, or hold specified positions within insolvency procedures.[247]

(b) Directors' duties to creditors in normal times in Ethiopia.

The Ethiopian company law clearly outlines the authorities and responsibilities given to directors by the law, the memorandum of association, and the resolutions of the general meeting of shareholders. These duties are intended to maintain the company's resources and, consequently, protect the interests of corporate creditors.[248] Directors must supervise the company's financial management, ensuring enough capital and liquidity to meet its timely commitments. They are also tasked with establishing governance structures that facilitate proper monitoring of the company's financial statements and positions, implementing adequate procedures for risk management and internal control, establishing necessary reserve funds, and, when necessary, initiating the process of preventive restructuring, reorganization, or insolvency (bankruptcy) in the event of a debt payment suspension.[249]

The law also enumerates directors' duty of loyalty (towards the company, shareholders, and creditors),[250] the responsibility to exercise independent judgment, the duty of care and diligence,[251] and the obligation to avoid and

245 *Id.* at art. 490.

246 *Id.* at arts. 484–91.

247 *Id.* at arts. 803 (liability of managers), 807 (negligent bankruptcy), 809 (disqualification), 811 (granting benefit), 815 (personal bankruptcy).

248 *Id.* at arts. 315–30, 513(1–3); Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 362–67; For the duties of Managers in cases of Partnerships in Ethiopia, refer to articles 198–202 of the Commercial Code of Ethiopia 2021.

249 Commercial Code, *supra* note 17, at art. 315(1–6).

250 *Id.* at arts. 316(1–2), 355–62, 364–67. Directors' duty of loyalty requires the directors to act in the way that promotes the success of the company and to act for the benefit of shareholders of the company as a whole. Moreover, in discharge of their duties, directors shall regard the long-term interests of the company, the interests of the company's employees, the interest of the company's creditors, and the impact of the company's operations on the community and the environment.

251 *Id.* at arts. 318(1, 2). Accordingly, directors shall discharge their responsibility with care, skill, and diligence. Directors shall be liable for damages caused to the company and shareholders due to lack

disclose private dealing and conflict of interest.[252] Ethiopian company law also enumerates the directors' duties towards the company,[253] creditors,[254] shareholders, and third parties.[255] By contrast, France,[256] Germany,[257] the U.K.,[258] and Ethiopia[259] only impose the obligation of fiduciary duties on the directors of companies towards the company and its shareholders in the vicinity of insolvency. In Ethiopia, a strong duty is imposed on directors to consider the interest of creditors.[260] However, the U.S. imposes weak fiduciary duties on directors towards creditors.[261]

In summary, civil law nations, with a particular focus on Germany, France, and Ethiopia, often display comprehensive statutory legislation controlling the debtor aimed at defending the interests of creditors. Conversely, common law

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of care or diligence in discharging their duties. Moreover, the responsibility of the director shall be measured in terms of care and skill that they must exercise as well as diligence that may reasonably be expected of a person carrying out the functions of a director of the company.

252 *Id.* at arts. 319–22. Accordingly, unless authorized by a general meeting, directors may not be partners in rival business entities nor compete against the company either on their own behalf or on behalf of third parties. Besides, directors shall avoid activities entailing a direct or indirect conflict of interest with the interests of the company. For example, the directors should abstain from exploiting any property, information, or business opportunity regardless of whether the company could take advantage of the property, information, or opportunity. Crucially, directors shall inform (declare) the board of any situation that may involve a conflict of interest between their own and the company's interest. Directors must also abstain from accepting a gift or another type of benefit from a third party without approval from the board.

253 *Id.* at arts. 325(1, 2), 328(1–6). Accordingly, directors shall be jointly and severally liable to the company for damages caused by failure to carry out their duties. If not, the law guarantees the rights of the company to file a suit against such directors. Plus, directors shall bear the burden of proof for showing that they have exercised due care and diligence in discharge of their duties.

254 *Id.* at art. 329(1–3); arts. 346, 366(1, 4) of the Commercial Code of Ethiopia 1960, *supra* note 150. Directors are also liable for damage caused to creditors where the company continues its business after the time when the directors knew or ought to have concluded that there was no reasonable prospect of the company being able to pay its creditors. Plus, directors who fail to preserve intact the company's assets are also liable to the company's creditors to the extent of the reduction in the company's assets that they caused if the company's assets are not sufficient to pay creditors. In the case where creditors sustain damages, they have the right to sue the directors regardless of the company's decision not to institute proceedings against the directors.

255 *Id.* at art. 330. The law also guarantees the rights of shareholders or third parties to bring legal action for damages against the directors where they have been personally injured directly owing to the fault or fraud of the directors.

256 French Commercial Code, *supra* note 222, at arts. 223–52.

257 German Stock Corporation Act 1965 §§ 92–93; German Insolvency Code of 1994 §§ 15–17; German Civil Code (BGB) §§ 823, 832; BACHNER, s*upra* note 79, at 247.

258 Companies Act 2006, *supra* note 14, §§ 171–77; U.K. Insolvency Act 1986 § 214; BTI 2014 LLC v. Sequana SA and others (2019) EWCA Civ 112; *see also*, West Mercia Safety Wear Ltd v. Dodd (1988) BCLC 250.

259 Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 346, 362, 366(1, 4), 367.

260 Keay, *supra* note 234, at 55–86; Hargovan & Todd, *supra* note 225, 135–80.

261 Zanardo, *supra* note 226, at 867–96.

nations, like the U.K., U.S., Australia, and India, often have less severe regulations concerning debtor control. [262]

B. Contractual Creditor Protection Strategies

1. Perspectives on contractual strategies of creditor protection.

Contractual (self-help) mechanisms for creditor protection provide permissive, *ex-ante* (pre-emptive) actions accessible to voluntary contractual creditors. These strategies are meant to shield voluntary creditors who are both willing and competent in negotiating arrangements to lessen the risk of default by debtors, achieved through the instrumentality of a contract describing these protective measures.[263] Anchored in the idea of freedom of contracts and party autonomy, this technique permits creditors to provide appropriate protections for their loans by modifying credit conditions following their financing requirements. Additionally, the contractual strategies offer creditors the option to surveil debtors effectively.[264]

The contract-based strategy allows creditors to use self-help tools for creditor protection through varied approaches. This involves gathering information on the debtor, securing third-party credit insurance, disclosure requirements, integrating financial covenants into the contract, and getting security from the corporate debtor or its directors and shareholders.[265] However, the contractual strategy for creditors' protection is also criticized for its inherent costliness, primarily attributable to the transaction expenses needed in gathering information or executing the broad array of contracts essential for creditor protection.[266] These contracts may comprise security agreements, guarantees, and insurance covenants.[267] The contractual strategy is also blamed for failing to safeguard vulnerable (involuntary) creditors who are unwilling or unable to enter into such arrangements with the debtor. Furthermore, security contracts are criticized for their inability to offer comprehensive protection.[268]

2. Creditors' security-based rights in general.

The most potent form of creditor contract-based protection strategy involves securing assets through a proprietary claim from the corporate debtor or

262 Simon et al., *supra* note 104, at 359–84.

263 Petroseviciene, *supra* note 108, at 213–28.

264 Mulbert, *supra* note 82, at 375–77.

265 *Id.*

266 Petroseviciene, s*upra* note 108, at 213–28; Armour, *supra* note 136, at 1–18; Mulbert, s*upra* note 47, at 712–16.

267 Mulbert, s*upra* note 47, at 712–16.

268 Armour, *supra* note 85, at 355–78.

its controllers.[269] Security contracts pertain to the presence, diversity, practicability, and enforceability of security mechanisms and laws within a legal system. Creditors exploit these contracts to preserve their interests against depreciation and to limit their financial risk exposure.[270] For instance, creditors can shield themselves from the perils of default, insolvency, or pre-emptive opportunistic actions by the debtor through the execution of a robust possessory contract (pledge) or, preferably, a non-possessory contract (mortgage and floating charge) that provides adequate security.[271]

Security measures also curtail the borrower's latitude of action to mitigate the likelihood of transactions that could diminish the debtor's assets. In the event of a payment default by the debtor, the security holder is entitled to take possession of the assets and liquidate them to settle the outstanding debt.[272] By stipulating in the contract that the debtor refrains from incurring additional debt, creditors can also preserve their priority rights over the security.[273] Creditors can significantly mitigate risk by obtaining security directly from the company's controllers, holding them accountable, and dissuading them from engaging in opportunistic actions that could exacerbate the creditor's risks.[274] Secured creditors of corporate debtors benefit from various privileges that safeguard their claims from devaluation and mitigate financial exposure.[275] For instance, in insolvency proceedings, the holder of security holds precedence over unsecured creditors and other secured creditors with a lower ranking, affording the creditor the right to undertake measures to enforce the provided security.[276]

3. Comparison of security-based strategies of creditor protection.

a) Security-based strategies in other countries.

Generally, common law countries, including the U.K., U.S., Australia, and India, strongly prefer security-based protection mechanisms over mandatory protective rules. Conversely, with Germany as a notable example, civil law countries generally provide weaker protection by relying on contractual

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269 PAUL DAVIES & SARAH WORTHINGTON, PRINCIPLES OF MODERN COMPANY LAW 815 (9th ed. 2012).

270 THE WORLD BANK, *supra* note 102, at 15–17, (2021); ARMOUR ET AL., *supra* note 11, at 1–202.

271 THE WORLD BANK, *supra* note 102, at 5–7 (2021); Mulbert, *supra* note 82, at 357–77.

272 Deakin et al., *supra* note 104, at 359–84.

273 ARMOUR ET AL., *supra* note 11, at 1–4.

274 Petroseviciene, s*upra* note 108, at 213–28.

275 DAVIES & WORTHINGTON, *supra* note 269, at 818–22.

276 *Id.*; THE WORLD BANK, PRINCIPLES FOR EFFECTIVE INSOLVENCY AND CREDITOR/DEBTOR REGIMES 15–17 (2021).

mechanisms.[277] Regarding creditors' security contract protection, common law countries in general and the U.K.,[278] India,[279] U.S., and Australia, in particular, provide the most robust mechanism of creditor protection.[280] Civil Law countries, particularly Germany, with some exceptions such as France, Ethiopia, and Japan, generally offer the least robust security-based protection strategies.[281]

b) Security-based strategies in Ethiopia.

In contrast to the majority of civil law countries, Ethiopian securities law provides one of the most robust security-based protections for corporate creditors globally. This includes, among other measures:

i. Providing for and recognizing all types of securities in creditors' favor.[282] For example, security interests in Ethiopia can be formed over various properties: Immovable Assets (Mortgages[283] and Antichresis[284]), Movables (Pledges),[285] Business,[286] shares,[287] and receivables.[288]

ii. Imposing a strict requirement for registration of various securities, which protects creditors' interests.[289] For example, in Ethiopia, a mortgage on an immovable, however created, shall not produce any effect unless registered.[290] The

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277 BÜRGERLICHES GESETZBUCH [BGB] §§ 135, 381, 1113, 1191, 1228, 1234, 1247 (Gr.); ARMOUR ET AL., *supra* note 11, at 1–202.

278 Companies Act 2006, *supra* note 14, §§ 859–73; U.K. Law of Property Act, 1925 § 136; Dearle v. Hall 3 Russ. 1, 38 Eng. Rep. 475 (Ch. 1828); Re David Lloyd (1877) 6 Ch D 339.

279 Companies Act 2013, *supra* note 14, §§ 77–87 (discussing the Registration of Charges).

280 *See* ARMOUR ET AL., *supra* note 11, at 1–202; Petroseviciene, *supra* note 108, at 213–28.

281 Deakin et al., s*upra* note 104, at 368.

282 Commercial Code, *supra* note 17, at arts. 143–49; Civil Code of Ethiopia 1960 arts. 2863–74, 3041–116, 3117–30, 2825–74; Commercial Code of Ethiopia 1960, *supra* note 150, arts. 171–93, 329.

283 Civil Code of Ethiopia 1960 arts. 3041–116.

284 *Id.* at arts. 3117–30; Art. 3117 of the Civil Code defines an "antichresis" as a contract whereby the debtor undertakes to deliver the immovable to his creditor as a security for the performance of his obligations.

285 *Id.* at arts. 2825–74.

286 Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 171–93.

287 *Id.* at art. 329.

288 Civil Code of Ethiopia 1960 arts. 2863–74; Security interests are mainly governed by the Civil Code of Ethiopia 1960 and partly by the Commercial Code of 2021. Article 1 of the Commercial Code states that the provisions of the Civil Code shall apply to persons and business organizations carrying on a trade, unless expressly provided otherwise.

289 Commercial Code, *supra* note 17, at arts. 143–44, 122–42; Civil Code of Ethiopia 1960 arts. 3052–58, 3118, 1186, 1193, 2267(2); Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 171–75, 178–86, 1006, 1007.

290 Civil Code of Ethiopia 1960 arts. 3052–58.

mortgage of a business shall also be registered.[291] Antichresis shall be registered, or it shall not have any effect.[292] Given that a pledge is a possessory security, there is no requirement to register pledges in general.[293] However, pledges on special movables such as airplanes and ships must be registered.[294]

iii. Guaranteeing priority rights of secured creditors in asset enforcement and distribution.[295] For example, Ethiopian law guarantees the *mortgagee's* right to sell the mortgage by a public auction.[296] The same holds for the holder of the Antichresis.[297] A business *mortgagee* whose claim is not paid on becoming due can sell the business by a public auction.[298] The law also guarantees the *pledgee's* right to sell the pledge by a public auction or without a public auction if the thing is quoted in the market.[299]

C. Insolvency Rules of Creditor Protection

Insolvency rules are a last resort mechanism for protecting creditors by applying mandatory rules outlined in insolvency law.[300] While mandatory rules in company law aim to prevent potential risks for creditors, insolvency law ensures compensation for creditors if the debtor goes insolvent.[301] These rules minimize losses for creditors[302] through either the liquidation (straight bankruptcy) or reorganization or restructuring of a company's assets. The U.S., the U.K.,

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291 Commercial Code, *supra* note 17, at arts. 143–55; Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 171–75, 178–86, 1006–07.

292 Civil Code of Ethiopia art. 3118.

293 *Id.* at arts. 2832, 2845, 2852. Pledge produces effect from the day the *pledgee* takes possession of the pledge.

294 Civil Code of Ethiopia 1960 arts. 1186, 1193, 2267(2).

295 Commercial Code, *supra* note 17, at arts. 149–55; Civil Code of Ethiopia 1960, arts. 2853–54(1, 2), 3102(1), 3110(c), 3118, 3129; Commercial Code of Ethiopia 1960, *supra* note 150, at art. 189.

296 Civil Code of Ethiopia 1960 arts. 3102 (1), 3110 (c).

297 *Id.*, arts. 3118, 3129.

298 Commercial Code, *supra* note 17, at arts. 143–55.

299 Civil Code of Ethiopia 1960, art. 2853–54 (1, 2). The Pledgee can sell the pledge within eight days of giving default notice to the pledger.

300 UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW, LEGISLATIVE GUIDE ON INSOLVENCY LAW 10-20 (2021); THE WORLD BANK, *supra* note 102, at 21-32 (2021).

301 Piotr Staszkiewicz & Sylwia Morawska, *The Efficiency of Bankruptcy Law: Evidence of Creditor Protection in Poland*, 48 EUR. J. OF L. ECON. 365, 365–83 (2019).

302 Douglas Baird & Thomas Jackson, *Corporate Reorganizations and the Treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors in Bankruptcy*, 51 U. OF CHI. L. REV. 97, 97–130 (1984)

Australia, and Ethiopia have recognized both types of proceedings.[303] Insolvency law deals with all issues related to settling the affairs of the debtor, such as who manages the proceeding,[304] who starts the insolvency process, how the debtor's affairs are settled, the effects of the debtor's insolvency, how creditors can participate in the proceeding and enforce their rights,[305] how secured creditors' interests are protected, and so on.[306] However, compared to other strategies for creditor protection, insolvency proceedings are criticized for being complicated, lengthy, expensive, congested, and potentially harmful to a company's creditworthiness and goodwill.[307]

1. Comparison of insolvency rules protecting creditors.

a) Insolvency rules protecting creditors in general.

Most countries use insolvency procedures as a last resort to protect creditors. Insolvency rules are used in various nations, including the U.S., U.K., Australia, Germany, and Ethiopia.[308] For example, in the U.K., regulations governing the liquidation of solvent companies were stipulated in the Insolvency Act 1986 and the Insolvency Rules 1986 before the recent amendment in 2020. The primary purpose of insolvency laws in such jurisdictions is to reduce losses for creditors.[309] In insolvency, the interests of creditors are given priority over other stakeholders. In the U.K., directors' duties shift to prioritize the preservation of creditors' claims, and directors can be held liable for wrongful trading if they act against the best interests of the creditors.[310]

Initiating insolvency proceedings in the U.K. depends on considering creditors' best interests. Additionally, during insolvency, creditors have the authority to take possession of assets and implement necessary measures to

303 11 U.S.C. §§ 701–84; 11 U.S.C. §§ 1101–95; Commercial Code, *supra* note 17, at arts. 1119–53 (discussing Scheme of Arrangement); U.K. Companies Act 2006, §§ 895–901; Parts 5.1, 5.2, 5.3(A), 5.4(A)(B) of the Australian Corporations Act 2001.

304 Zanardo, *supra* note 226, at 867–96.

305 Simeon Djankov et al., *Debt Enforcement Around the World*, EUR. CORPORATE GOVERNANCE INST. Finance Working Paper No. 147, 1–69 (2006).

306 John Armour et. al., *CBR Extended Creditor Protection Index for the UK, the US, Germany, France, and India*, CENTRE FOR BUS. RSCH. Working Paper No. 382, 1–57 (2009)

307 David S. Stevenson, *Grab the Fire Extinguisher Comparing UK Schemes of Arrangement to U.S. Corporate Bankruptcy after Jevic*, 68 CLE. S. L. REV. 73, 73–84 (2019).

308 Sergei Davydenko & Julian Franks, *Do Bankruptcy Codes Matter? A Study of Defaults in France, Germany, and the UK*, EUR. CORPORATE GOVERNANCE INSTITUTE, Finance Working Paper No. 89 1–45 (2006).

309 The U.K. Corporate Insolvency and Governance Act, Chapter 12; The U.K. Insolvency Act 1986; The U.K. Insolvency Rules 1986; Oliver Hart, *Different Approaches to Bankruptcy,* HARV. INS. ECON. RSCH. Paper No. 1903, 1–21, (2000).

310 Claessens & Klapper, *supra* note 103, at 1–30.

recover their debts.[311] After the commencement of the insolvency procedure, creditors should have the right to obtain possession of assets or hold priority in asset distribution. They should also be able to determine the most suitable insolvency procedure or nominate the party responsible for overseeing the insolvency proceedings.[312] The level of protection afforded to creditors within a legal system is directly related to the extent to which these rights are conferred upon them. More rights enhance protection, while fewer rights diminish it.[313] During an insolvency proceeding, however, the U.K. provides robust protection to secured creditors. Upon default, secured creditors have significant control over the company, and there is no automatic stay against creditors' claims. Unsecured creditors have limited control rights and are excluded from participating in selling the company's assets. They do not receive any payouts unless the claims of secured creditors have been entirely settled.[314]

In Germany, the status of secured creditors holds an intermediate position, as a collective procedure is mandated, accompanied by a three-month automatic stay on creditors' claims. However, for any restructuring plan to be approved, the court requires the consent of most secured creditors, ensuring that creditors maintain substantial control over the restructuring process.[315] In France, the rights of secured creditors are particularly vulnerable. Approval from creditors is not required to sell collateral or convince for a reregistration plan. The court also holds complete control, and the state prioritizes its claims and those of employees when collateral is sold in insolvency, resulting in a high degree of subordination for other creditors.[316]

b) Insolvency rules protecting creditors in Ethiopia.

Ethiopian insolvency law provides critical rights to corporate creditors to protect their interests during insolvency.[317] The law states that the primary objective of restructuring, reorganization, and bankruptcy proceedings is to safeguard the legitimate interests of creditors.[318] This means that while other objectives may be considered, protecting creditors' interests take priority. As a result, the law prohibits any action that compromises creditors' interests or does

311 *Id.*

312 *See* N. Am. Catholic Educ. Programming Found., Inc. v. Gheewalla, 930 A.2d 92, 101–02 (2007).

313 ROY GOODE, *supra* note 92, at 58.

314 Davydenko & Franks, *supra* note 308, 1–45.

315 *Id.*

316 *Id.*

317 Insolvency (bankruptcy) in Ethiopia is governed by articles 588–825 in Book 3 of the Commercial Code of Ethiopia 2021. The law recognizes 3 types of procedures to deal with the affairs of a debtor who has or is about to suspended payment. These are Preventive Restructuring, Reorganization, and Liquidation proceedings.

318 Commercial Code, *supra* note 17, at art. 597(1).

not have the approval of the majority of creditors.[319] The law also specifies that maximizing the value of the debtor's assets is a crucial objective in preventive restructuring, reorganization, and bankruptcy proceedings. This is done to enhance the prospects of recovery for creditors.[320]

The law recognizes that the objective of insolvency proceedings is to organize the liquidation of the debtor's business in a timely, efficient, and effective manner.[321] This can be achieved by piecemeal liquidation or by selling the business as a going concern to maximize the value of assets available for recovery by creditors.[322] Therefore, the chosen liquidation strategy during insolvency proceedings should prioritize maximizing the debtor's assets, leading to increased recovery for creditors.[323] The law also allows the establishment and empowerment of the Creditors' Committee as one of the entities responsible for overseeing the proceedings.[324]

Ethiopian insolvency law ensures that creditors can approve various activities and acquire pertinent information during the proceedings, allowing them to protect their interests effectively.[325] The law guarantees that creditors have the right to equitable participation in distributing the net proceeds from realizing the debtor's assets.[326] It also acknowledges and prioritizes the rights or entitlements of existing (pre-insolvency) creditors and establishes explicit rules for determining the priority ranking of these claims.[327] The Ethiopian insolvency law ensures that secured creditors have preferential and exclusive rights to realize the proceeds from their security. This protects the interests of all creditors.[328] For instance, like in the U.K., secured creditors in Ethiopia are mostly unaffected by insolvency proceedings, including preventive restructuring and reorganization proceedings, as long as the creditor's security is established before the debtor's bankruptcy is declared.[329]

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319 *Id.* at art. 597(2–4).

320 *Id.* at art. 588(1–3).

321 *Id.* at art. 588(4).

322 Commercial Code, *supra* note 17, at arts. 617–34 (restructuring), 635–704 (reorganization), 705–825 (liquidation).

323 *Id.* at art. 588(4).

324 *Id.* at arts. 722–23.

325 *Id.* at arts. 593, 594, 597–99, 616, 619, 620, 627, 632, 635, 639, 640, 643, 645, 648, 649,650–51, 652, 678, 688–95, 697, 700, 704, 705, 709, 711–12, 719, 721, 748.

326 *Id.* at arts. 606(6), 628(1), 678, 679(2), 680, 683–95, 786, 789(1, 2).

327 *Id.* at arts. 592–96, 603, 606(1, 2), 654–57, 662, 664–67, 668–75, 761, 764–74.

328 *Id.* at arts. 595, 669, 680, 692, 751–54, 761(6), 763–65, 780–86.

329 *Id.* at arts. 592, 593–96, 597–99, 617, 625–27, 635–38, 654–58, 662–70, 675, 680–88, 692–95, 705, 707–14, 722–24, 747–50, 751–54, 761–65, 768–74, 780–84, 785–93; Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 1029–34.

When a debtor is declared bankrupt, the 'automatic stay' principle suspends individual lawsuits filed by unsecured creditors. However, it does not extend to lawsuits initiated by secured creditors against the debtor.[330] The legal entity known as the 'universality of creditors' established upon the declaration of bankruptcy does not encompass creditors whose claims are secured by a 'pledge' or 'mortgage.' Therefore, unsecured creditors whose claims are included in the 'universality' must suspend their legal actions, while secured creditors can enforce their security despite the commencement of a bankruptcy proceeding.[331]

To summarize, it is difficult to definitively conclude that common law countries generally provide stronger insolvency-based creditor protection compared to civil law countries and vice versa. However, countries like the U.K.[332] and Australia offer relatively stronger protection to creditors based on insolvency rules.[333] Among civil law countries, jurisdictions based on German law generally provide more protection to creditors than countries with a legal system rooted in French law.[334] However, the U.K. and U.S. also provide more robust protection regarding reorganization proceedings.[335] In Ethiopia, insolvency rules provide substantial protection to creditors by prohibiting the commencement of proceedings unless there is a court-proven suspension of payment,[336] giving creditors strong power to determine the outcome of the proceeding,[337] imposing a stay requirement on unsecured creditors,[338] and imposing no subordination rules on the rights of secured creditors.[339]

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330 Commercial Code, *supra* note 17, at arts. 625–26 (on suspension of suits (stay) during a preventive restructuring proceeding), 654–55 (stay during a re–organization proceeding), 761(1–6) (stay during insolvency proceeding); Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 977(1), 982, 1024–26, 1039, 1090 (suspension of the effects of bankruptcy), 1125.

331 Commercial Code, *supra* note 17, at arts. 662–70, 675, 680–88, 692–95, 705, 707–14, 722–24, 747–50, 751–54, 761–65, 768–74; Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 1025–26.

332 The U.K. Insolvency Act 1986; Claessens & Klapper, *supra* note 103, 1–30.

333 Commercial Code, *supra* note 17, at arts. 675, 692, 761–65, 768–74, 780–84, 785–93; Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 1058–64, 1065–72.

334 Lucian Arye Bebchuk, *A New Approach to Corporate Reorganizations*, 101 HARV. L. REV. 775, 804 (1988).

335 *Id.*

336 Commercial Code of Ethiopia 1960, *supra* note 150, arts. 968–73, 975–78.

337 *Id.* arts. 977 1(b), 982, 1002–03, 1039, 1119, 1142, 1140–44.

338 *Id.* arts. 1019–34.

339 Civil Code of Ethiopia 1960, arts. 1025–26, 1031–32, 1058–64, 3076–80, 2851–62; Commercial Code of Ethiopia 1960, *supra* note 150, arts. 187–93, 1065–71.

IV. Analysis of the Comparison of the Strategies of Creditors' Protection

This section analyses the findings of the study from the comparison of the strategies of corporate creditors' protection, as explored in the preceding sections. Accordingly, the following are the major findings:

A. No Single Strategy is Adequate

Designing a universal system for creditor protection worldwide is challenging due to the diverse interests of creditors that need protection and the various approaches to protecting creditors, each aiming to achieve different levels of security.[340] The complexity of this task is further heightened by the realization that no single method of creditor protection is universally effective, and the mechanism employed in one country may not be applicable or suitable to the circumstances of another country.[341]

B. Countries Use a Mix of Strategies

Countries have been trying to address the issue of creditor protection by using a combination of *ex-ante* and *ex-post* regulatory strategies suitable for their particular context. These strategies are drawn from various legal frameworks.[342] The strategies for creditor protection can vary based on factors like the economic level, policy considerations, judicial enforcement, and the development and origin of the legal system.[343] Although countries with similar legal systems may display similar tendencies in favoring certain mechanisms over others, they all agree on the essential requirement for adequate protection for corporate creditors.[344]

C. Full Protection is the Main Goal

When choosing creditor protection strategies, nations need to focus on the effectiveness of each strategy in safeguarding the interests of creditors. Instead of simply looking at whether a particular strategy is present, it is more important to evaluate whether the mechanisms used in a particular country can address the potential risks faced by creditors and ensure the required level of protection. This

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340 Armour et al., *Extended Creditor Protection Index*, *supra* note 306, at 1–57.

341 Mulbert, *supra* note 82, at 357–408.

342 Michelangelo Granato, *The Myth of the Optimal Capital Structure and the Dogma of Creditor Protection*, 18 EUR. BUS. ORG. L. REV. 617, 617–58 (2017).

343 Armour et al., *Legal Rules*, *supra* note 106, at 579–630.

344 *See generally* Granato, *supra* note 342.

approach is commonly referred to as a functional comparison of the strategies of creditor protection.[345]

D. Three Strategies are Predominant

Countries primarily employ one or a combination of the three major creditor protection strategies from the myriad of available creditor protection mechanisms.[346] These are mandatory debtor control rules, contract-based protections, and insolvency rules. While the ultimate objective remains consistent, these methods diverge in terms of their nature (source) and time of application.[347] Hence, it is plausible to infer that given the ubiquitous nature of creditors' risk across jurisdictions, all countries deploy at least one of the aforementioned methods for creditor protection.

E. Different Strategies for Different Problems (Eclectic Approach)

Nations often combine various strategies to mitigate the shortcomings of one approach with the strengths of another. This results in a more diverse and resilient mechanism for creditor protection. For example, contract-based strategies have limitations because they can be costly and may not adequately protect weaker (involuntary) creditors. In such cases, countries may use these mechanisms to safeguard strong creditors while implementing strategies to protect vulnerable creditors, such as insolvency or mandatory debtor control rules.[348] Similarly, the minimum capital requirement has faced criticism for being a costly, burdensome, and inefficient means of protecting creditors. As a result, some countries have either abolished the rule (such as U.K., U.S., Australia, and New Zealand, Japan, and India or adopted alternative methods to address the issue, such as piercing the corporate veil (as seen in the U.S., U.K., and Australia).[349]

F. Contextual Realities Determine the Use of Strategies

Countries tend to adopt different strategies for protecting creditors' interests based on their circumstances.[350] This is evident in their reliance on either debtor control rules or contract-based mechanisms. There is a clear distinction between these two strategies. Countries that use debtor control rules usually have a greater

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345 Mulbert, *supra* note 82.

346 ARMOUR ET AL., CBR 1990–2013, *supra* note 11, at 1–202.

347 Staszkiewicz & Morawska, *supra* note 301, at 365–83.

348 Mulbert, s*upra* note 82, at 359–74.

349 Mulbert, s*upra* note 47, at 695–732.

350 Armour et al., s*upra* note 106, at 579–630.

influence on government ownership and regulation in their legal systems. However, they often lack strong contract-based protection mechanisms.[351] These countries are typically categorized under the civil law legal system, with Germany and France being notable examples.

On the other hand, nations primarily employing contractual approaches exhibit minimal government intervention, facilitate private regulation, and possess more resilient judicial systems. These systems typically do not prioritize the use of debtor control mechanisms.[352] This pertains to jurisdictions following common law principles, such as the U.K., U.S., and Australia. In these nations, safeguarding creditors' interests is transitioning from the domain of company law to contract law.[353] It is important to note that combining strategies does not necessarily mean using debtor control rules and contract-based mechanisms simultaneously. This is because the simultaneous utilization of 'mandatory rules' and 'contract-based mechanisms' within a legal system may lead to an overprotection of creditors' interests. Instead, using distinct mechanisms that address various risks to creditors results in more robust protection.[354]

G. Insolvency Protection is the Common Denominator

Civil and common law nations demonstrate a significant inclination towards employing the insolvency rules mechanism as a last resort for safeguarding creditors' interests.[355] Therefore, employing a blend of creditor protection strategies involves utilizing insolvency rules as a *post facto* safeguard and *ex-ante* rules on debtor control in civil law countries or contract-based strategies in common law countries.[356] However, Ethiopia deviates from this dichotomy by employing a hybrid approach, concurrently utilizing mandatory rules and security contracts.[357]

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351 Paolo Santella & Riccardo Turrini, *Capital Maintenance in the EU: Is the Second Company Law Directive that Restrictive?* 9 EUR. BUS. ORG. L. REV. 427, 427–61 (2008).

352 DGCL §§ 160, 170; MARCUS LUTTER, LEGAL CAPITAL OF PUBLIC COMPANIES IN EUROPE 2 (De Gruyter, ECFR Special Volume, 2006).

353 For example, state corporation laws in the U.S. provide protection to creditors through 'contracts' and almost all states have abolished the minimum capital requirement including Delaware and California.

354 William W. Bratton, *Corporate Debt Relationships: Legal Theory in a Time of Restructuring*, 1989 DUKE L. J., 92, 95–170 (1989).

355 Sandra Frisby, *Cross–border Insolvency and Vulnerable Transactions*, *in* VULNERABLE TRANSACTIONS IN CORPORATE INSOLVENCY 427–77 (John Armour & H.N. Bennett eds., 2003).

356 Armour et al., s*upra* note 11, at 1–202.

357 *See supra* notes 340–44 and accompanying text.

H. Worldwide Harmonization of Creditors' Protection Strategies

Over the years, global creditor protection mechanisms have become increasingly harmonized in function and design.[358] Nations are working towards achieving this goal by removing regulatory mechanisms that are inefficient, costly, redundant, or cumbersome. Instead, they are adopting more efficient mechanisms that address all the risks creditors face and provide the necessary level of protection.[359] Several countries like the U.K., Australia, U.S. (Delaware), and India have moved away from the mandatory rule of having legal capital. Instead, they are shifting towards a contract-based approach through security contracts and updating their insolvency regulations. This convergence is aimed at enhancing and modernizing the legal framework of security devices and insolvency.[360]

For example, Australian law heavily emphasized the capital maintenance rule until the shift in legislative policy in 1998. After 1998, although maintaining capital rule remains an important principle, Australian law departed from the strict legislative application of the maintenance of capital rule to share capital transactions. Australian companies can undertake share capital transactions without court approval while protecting creditors' interests by ascertaining that the company remains solvent afterward. By so doing, the law has struck a balance between easier and streamlined procedures for share capital transactions and the need for creditor protection.[361]

Moreover, several countries are observed to judicially set aside limited liability by piercing the veil of incorporation to safeguard creditors' interests, with notable examples including the U.K., U.S., and Australia.[362] Nations also aim to standardize their frameworks for protecting creditors at a regional level by implementing harmonized standards of creditor protection. For example, the EU has initiated harmonizing the substantive insolvency regime and standardizing the legal capital requirement, demonstrating this effort.[363]

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358 Armour et al., *supra* note 11, at 1–202.

359 Armour et al., *supra* note 108, at 579–630. For example, a functional convergence in creditor protection strategies is evident as between the legal systems of the major industrial nations such as U.K., Germany, U.S., France, and India.

360 *See Bachner*, *supra* note 79, at 145–79.

361 Australian Corporations Act 2001, Chapter 2(J); HARGOVAN ET AL., *supra* note 2, at 342–57.

362 *Adams v. Cape Industries Plc* [1990] Ch 433, CA; *Jones v. Lipman* [1962] 1 All ER 442; *Wallersteiner* v *Moir* [1974] 3 All ER 217; Wild & Weinstein, *supra* note 19, at 22–30; Mulbert, *supra* note 47, at 695–732.

363 The EC Second Directive on Company Law (1976); Paul Krüger Andersen, *The European Model Company Act (EMCA)–a Tool for European Integration*, 19 ACAD. EUR. L. F. 77, 77 (2018); R. J. Deweijs, *Harmonization of European Insolvency Law: Preventing Insolvency Law from Turning Against Creditors by Upholding the Debt–Equity Divide*, 15 EUR. COMP. AND FIN. L. REV. 403, 403–44 (2018).

Standardizing methods for creditor protection through functional convergence is praiseworthy for two primary reasons. Firstly, having consistent regulations and streamlined enforcement mechanisms for creditors' rights ensures that creditor protection strategies are specific, adaptable, predictable, and cost-effective. Secondly, it addresses the long-standing issue of forum shopping and cross-border reincorporation by universally providing uniform treatment and standardized protection rules. This has historically posed significant practical challenges for debtors and creditors, requiring compliance with disparate rules and principles from two jurisdictions in pursuit of an equitable and level playing field.[364]

For example, in the U.K., there is no minimum capital rule. Additionally, the *Centros*[365] decision by the European Court of Justice (ECJ) allowed European private companies to choose their own regulations. As a result, many European businesses opted to incorporate under English law and conduct operations in other places. This caused significant regulatory challenges and inconveniences in practice.[366] Similar dynamics are observed in the U.S. where, owing to less stringent regulations, half of the companies in the country opt to incorporate under Delaware law.[367]

V. LEXIMETRIC EVALUATION OF CORPORATE CREDITORS' PROTECTION RIGHTS IN ETHIOPIA

A. Methodology

Applying the Leximetric Method of Legal Analysis, this section evaluates the adequacy of Corporate Creditors' Protection Rights in Ethiopia.[368] As Ethiopia recently revised its company law by replacing the 1960 Code with a New Code in 2021, two distinct creditor protection indexes have been formulated covering the period from 1960 to 2020 and 2021 onward. This approach facilitates readers in comparing and understanding how the New Code addresses the deficiencies of the former 1960 Code.[369] Per the Leximetric Rules, ten essential variables have been delineated for gauging the efficacy of creditor protection regulations in Ethiopia. Each variable undergoes analysis and is assigned a value of '0,' '1,' or a value in between, denoted as '0.5.' Here, '0' signifies inadequate or no protection,

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364 Carsten G. B. et al., *Cross–border Reincorporations in the European Union: the Case for Comprehensive Harmonization*, 18 J. CO. L. STU. 1, 1–42 (2018).

365 ECJ, Case No. C–208/00, Überseering BV v. Nordic Construction Company Baumanagement GmbH, 2002 E.C.R. I–9919.

366 ARMOUR ET AL., *Transactions*, *supra* note 127, at 1–18.

367 Enriques & Gelter, *supra* note 135, at 417–53.

368 ARMOUR ET AL., CBR 1990–2013, *supra* note 11, at 1–202.

369 *Compare* Commercial Code of Ethiopia 1960, *supra* note 150, *with* Commercial Code, *supra* note 17.

'1' signifies robust protection, and '0.5' denotes moderate protection concerning corporate creditors' interests for each variable.[370]

Given ten core variables, each variable is assigned a maximum value of '1' and a minimum value of '0.' The highest attainable sum for the aggregate values of all core variables is '10,' signifying robust protection. Conversely, the lowest conceivable sum for the total variable values is '0,' indicating weak protection.[371] In this study, the median score of '5' for the summation of values across all core variables serves as a benchmark. This benchmark assesses whether the creditor protection rules are deemed adequate.[372] If the cumulative score falls below '5' out of '10,' the rules are considered 'inadequate'; conversely, if the score surpasses '5,' the rules are deemed 'adequate.'

B. Corporate Creditors' Protection Rights Leximetric Index for Ethiopia 1960-2020 and Beyond[373]

Variable	**Template**	**1960-2020**	**2021 & FF.**	**Explanation**
1. Minimum Capital Requirement	It equals '1' if the minimum capital imposed equals 25,000 Euros; otherwise, it equals '0.'	**0**	**0**	In Ethiopia, the requirement applies to share companies and private limited companies.[374] A share company is a company whose capital is fixed in advance, divided into shares, and whose liabilities are met only by the company's assets.[375] A private limited company is a company whose capital is fully paid in advance, divided into shares, and whose members are not liable for the company's debts.[376] The minimum capital of share companies shall not be less than 50,000 Birr (825 Euros).[377] The minimum capital of PLCs shall not be less than

370 Refer to the table below.

371 Refer to the table below.

372 *See infra* Part VI.

373 ARMOUR ET AL., CBR 1990–2013, *supra* note 11, at 1–202; Armour et al., *Extended Creditor Protection Index*, *supra* note 306, at 1–34; compare the score of the other countries considered in this study with the score for Ethiopia.

374 Commercial Code of Ethiopia, arts. 245–494, 495–533.

375 *Id.* at art. 245(1).

376 *Id.* at art. 495(1–5), 533.

377 *Id.* at art. 247(1).

				15,000 Birr (248 Euros).[378] The law guarantees the rights of an unpaid creditor or a creditor who is not given adequate guarantees to oppose the reduction of the company's capital.[379] The capital shall be increased to the minimum required by law within one year from the publication date of the decrease in the commercial register.[380]
2. Dividend Restriction	Equals '0' if there is no "basic dividend restriction;" Equals '0.5' if there is a basic restriction" on dividend payments; Equals '1' if there is a basic dividend restriction, prohibition of repurchase of shares, and undervalue transaction.	**0.5**	**1**	(a) Every shareholder has the right to participate in the annual net profits and share the net proceeds on a winding-up. The share in the profits is calculated in proportion to capital holding.[381] Dividends can only be paid to shareholders from the net profits shown in the approved balance sheet.[382] Distribution of 'fictitious dividends' is prohibited, and persons making the distribution shall be criminally and civilly liable.[383] Creditors have full rights to oppose the illegal distribution of profits.[384] Every shareholder has the right to participate in the annual net profits.[385] (b) Share Repurchases: In principle, a company can acquire its shares exceptionally where (a) a meeting of the shareholders has authorized the acquisition, (b) the purchase price is made from the net profits of the company, and (c) the shares are fully paid.[386] Moreover, a company shall not purchase its share to reduce its capital.[387] (c) Disguised

378 *Id.* at art. 496(1).

379 *Id.* at arts. 467, 468(2).

380 *Id.* at arts. 463, 468(1); *see* Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 304(1, 2), 306(1), 312, 342, 490–94 (regarding minimum capital requirement in the old code).

381 Commercial Code, *supra* note 17, at art. 291(1–2).

382 *Id.* at art. 438(1).

383 *Id.* at art. 438(3–5), 529.

384 *Id.* at art. 438–41, 467.

385 *Id.* at arts. 438–41, 467.

386 *Id.* at art. 275(1, 4).

387 *Id.* at arts. 275(3), 280.

				Dividends: A company shall not grant advances on its shares nor make loans to enable third parties to acquire shares.[388] Any dealings made directly or indirectly between a company and a director shall receive the prior approval of the board of directors, and notice shall be given to the auditors. Directors may not contract a loan with the company.[389] Directors may not contract a loan with the company.[390]
3. Director Duty to Creditors	Equals '0' if there is no duty on directors to take creditors' interests into account; Equals '0.5' if there is a duty on directors to act in creditors' interests if the firm is commercially insolvent; Equals '1' if there is a duty on directors to act in creditors' interests if the firm is balance-sheet insolvent.	**0.5**	**1**	In the vicinity of insolvency, managers and directors have the fiduciary duties to protect the interests of the creditors.[391] Directors are liable for damage caused to creditors where the company continues its business and where there was no reasonable prospect of the company being able to pay its creditors.[392] Directors must apply for preventive restructuring, reorganization, or bankruptcy, where the company suspends debt payments.[393] Directors' duty: of loyalty,[394] to exercise independent judgment,[395] of care and diligence,[396] and to avoid and disclose private dealing and conflict of interest.[397] Directors also have duties towards the company,[398] creditors,[399] shareholders, and third parties.[400]
4. Security: Scope	Equals '0' if only mortgage of land is	**1**	**1**	Security interests in Ethiopia can be formed over various properties: Immovable Assets

388 *Id.* at art. 277.

389 *Id.* at arts. 295(1–6), 306(1–6), 307(1–3).

390 *Id.* at art. 277; *see* Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 332(1, 5), 334, 345(1, 2), 356, 357, 400, 409, 452–56, 458, 459, 489 (regarding dividend restriction in the old code).

391 Commercial Code of Ethiopia, arts. 699(1–2), 803(1–3).

392 *Id.* at art. 329(1).

393 *Id.* at arts. 315(6)(g), 424.

394 *Id.* at arts. 316(1–2), 355–62, 364–67.

395 *Id.* at art. 317(1–2).

396 *Id.* at art. 318(1–2).

397 *Id.* at arts. 319–22.

398 *Id.* at arts. 325(1–2), 328(1–6).

399 *Id.* at art. 329(1–3).

400 *Compare id.* at art. 330 *with* Commercial Code of Ethiopia, 1960 arts. 346, 355–62, 366(1, 4), 364–67.

	recognized; Equals '0.33' if land + 1 other form of security is recognized; Equals '0.66' if land + 2 other forms security are recognized; Equals '1' if land + 3 other forms of security are recognized.			(Mortgages[401] and Antichresis[402]), Movables (Pledges),[403] Business,[404] shares,[405] and receivables.[406]
5. Security: Registration	Equals '0' if only mortgage of land is registered; Equals '0.33' if land + 1 other security form is registered; Equals '0.5' if land + 2 other security forms are registered; Equals '1' if land + 3 other forms of security is to be registered.	**0.5**	**1**	A mortgage shall not produce any effect unless registered.[407] The mortgage of the business shall be registered.[408] Antichresis shall be registered.[409] In general, there is no requirement to register pledges[410]. However, pledges on special movables such as airplanes and ships must be registered.[411]
6. Security: Enforcement	Equals '0' if creditors cannot enforce security outside of court; Equals '1' if creditors can	**0.5**	**1**	A *mortgagee* can sell the mortgage by a public auction.[412] The same holds for the holder of the Antichresis.[413] A business *mortgagee* can sell the business by a public auction.[414] Besides, the law

401 Civil Code of Ethiopia 1960, arts. 3041–116.

402 *Id.* at arts. 3117–30.

403 *Id.* at arts. 2825–74.

404 Commercial Code of Ethiopia, arts. 143–55; *see* Commercial Code of Ethiopia 1960, *supra* note 150, arts. 171–93 (discussing mortgage of business).

405 Commercial Code of Ethiopia 1960, *supra* note 150, at art. 329.

406 *Id.* at arts. 2863–74.

407 *Id.* at arts. 3052–58.

408 Commercial Code of Ethiopia, arts. 143–55; Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 171–75, 178–86, 1006, 1007.

409 Civil Code of Ethiopia 1960, art. 3118.

410 *Id.* at arts. 2832, 2845, 2852.

411 *Id.* at arts. 1186, 1193, 2267(2).

412 *Id.* at arts. 3102(1), 3110(c).

413 *Id.* at arts. 3118, 3129.

414 Commercial Code of Ethiopia, arts. 143–55; *see* Commercial Code of Ethiopia 1960, *supra* note 150, at art. 189.

	enforce security privately or outside of courts.			also guarantees the *pledgee's* right to sell the pledge by a public auction or without a public auction if the thing is quoted in the market.[415]
7. Entry to Corporate Bankruptcy Proceeding	Equals '0' if debtors can commence bankruptcy unilaterally regardless of insolvency; Equals '0.5' if creditors can commence bankruptcy proceedings against a debtor; Equals '1' if debtors can commence bankruptcy proceedings upon proving balance sheet insolvency.	**0.5**	**1**	Insolvency proceedings in Ethiopia are governed by 'Book 3' of the Commercial Code.[416] A bankruptcy proceeding can be instituted through a petition by the debtor (voluntarily), one or more creditors, the public prosecutor, or the Court itself.[417] However, the petitioner shall prove the actual 'suspension of payment,' and the date of suspension of payment shall be ascertained and fixed by the Court at a First Hearing.[418] Therefore, the chance of threats by parties is zero.[419]
8. Stay of Secured Creditors	Equals '1' if secured creditors do not be stayed in liquidation proceedings where rehabilitation is not a realistic possibility; Otherwise, Equals '0.'	**1**	**1**	Secured creditors are unaffected by either a bankruptcy proceeding or scheme of arrangement so long as the security is constituted before adjudication[420] and the 'stay of proceeding' refers to only the unsecured creditors.[421] The immediate effect of the declaration of bankruptcy is the creation of a legal entity called 'universality of creditors,' which does not include creditors whose claims

415 Civil Code of Ethiopia 1960, arts. 2853, 2854(1–2).

416 Commercial Code of Ethiopia, arts. 588–825. This law recognizes three types of proceedings to deal with the affairs of a debtor who has or is about to suspended payment. These are Preventive Restructuring, Reorganization, and Liquidation proceedings.

417 *Id.* at art. 705(1–7).

418 *Id.* at arts. 706–14.

419 *See* Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 975, 968–73, 975–78, 968–1170 (regarding entry requirement of insolvency in the old code); *id.* at arts. 968–1080, 1081–118, 1119–53 (there were 3 types of insolvency proceedings: (1) Liquidation, (2) Composition, & (3) Scheme of Arrangement as per the old code).

420 Commercial Code, *supra* note 17, at arts. 595, 669, 680, 692, 751–54, 761(6), 763–65, 780–86.

421 *Id.* at arts. 625–26, 654–55, 761(1–6).

				are secured by a special pledge or mortgage.[422] Therefore, while unsecured creditors whose claims are included in the universality shall stay and suspend their suits, secured creditors can proceed against their security.[423]
9. The outcome of Bankruptcy Proceedings	Equals '0' if either court or debtor are decision-makers regarding whether the firm continues or is closed; Equals '0.5' if creditors are the primary decision-makers regarding whether the firm continues or is closed; Equals '1' if unsecured creditors or "residual claimants" are the decision-makers.	**0.5**	**0.5**	The Court, the Supervisory Judge, and the Trustee have all the power to control the bankruptcy proceeding.[424] However, the ultimate decision lies with the unsecured creditors. The reorganization plan shall be accepted provided that one or more creditors, representing at least two-thirds of the claims in each class of creditors, have voted in favor of the reorganization plan, including written agreements among the creditors.[425] However, where the two-thirds majority is not reached in each class of creditors' meetings, the reorganization plan is accepted, provided that the debtor and a majority of affected creditors have approved the plan. The court should also approve such a plan[426]. Similarly, the restructuring plan prepared by the debtor with the assistance of the expert in the field of restructuring shall be accepted by all affected creditors participating in the preventive restructuring proceedings, which also have the power to seek to amend the restructuring plan and make counterproposals. The court shall also approve the restructuring plan.[427]
10. Subordinati	Equals '0' if secured claimants are	**0.5**	**1**	Preventive restructuring, reorganization, and bankruptcy proceedings do not affect the rights

422 *Id.*

423 *Id.* at arts. 595, 669, 680, 692, 751–54, 761(6), 763–65, 780–86; Regarding the stay of secured creditors in the old code, *see* Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 977(1), 982, 1024–26, 1029–34, 1039, 1058–64, 1065–72, 1090, 1125.

424 Commercial Code, *supra* note 17, at arts. 705–15, 716–17, 718–21, 722–23.

425 *Id.* at art. 683.

426 *Id.* at arts. 684–88.

427 *Compare id.* at arts. 627–35 *with* Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 975–83, 977(1)(b), 982, 1002–03, 1039, 1119, 1142, 1081–85, 1170, 984–88, 989–90, 1087, 991–93, 1140–44.

on of Secured Claimants	subordinate to all other types of security; Equals '1' if secured claimants are not subordinate to all other types of security.			of secured claimants whose rights are constituted before the suspension of payment or adjudication.[428] Therefore, all secured claimants have the right to proceed against their security in priority to other creditors, and their interests are not subordinated with unsecured creditors.[429]

C. Comparison of the Two Creditors Protection Indexes for Ethiopia

Examining the two indices measuring corporate creditors' protection rights reveals a discernible shift. The Commercial Code of Ethiopia 2021 has instituted numerous contemporary rules and principles to safeguard corporate creditors' interests. This amendment is anticipated to positively influence corporate governance and creditors' protection in Ethiopia in the foreseeable future. This is apparent in the overall score for the 1960 Code, which scores 5.5 out of 10, indicating a moderate level of protection for creditors' interests. In contrast, the total score for the New Code is 8.5 out of 10, underscoring its provision of more robust protection for the interests of corporate creditors.

In a nuanced analysis, while debtor control rules feature prominently, the New Code provides heightened protection to creditors by implementing insolvency rules and security mechanisms. Moreover, in cross-country comparisons, the score of the New Code in ensuring the rights of corporate creditors stands among the highest by global standards. Nonetheless, it is advisable for the relevant government body to routinely assess and revise the provisions of the New Code, particularly in instances where the scores in the index indicate suboptimal levels of protection.

VI. Conclusion

Countries have sought to address the challenge of safeguarding creditors' concerns by deploying preventative and corrective regulatory measures customized to their unique contexts. The approaches to shielding corporate

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428 Commercial Code, *supra* note 17, at arts. 592–96, 603, 606(1–2), 654–57, 662, 664–67, 668–75, 761, 764–74.

429 *Id.* at arts. 595, 669, 680, 692, 751–54, 761(6), 763–65, 780–86; Regarding subordination of secured claims in the old code, *see* Commercial Code of Ethiopia 1960, *supra* note 150, at arts. 1024–26, 1029–34, 1058–64, 187–93, 1065–71.

creditors vary based on economic advancement, policy considerations, judicial enforcement, and the evolution and source of a legal system. Although nations with similar legal systems may demonstrate similar tendencies toward particular mechanisms, there is a unanimous agreement on the fundamental imperative of ensuring adequate protection for corporate creditors.

Nations also tend to utilize distinct methodologies influenced by their individualized circumstances in securing creditors' concerns. This is evident in their inclination towards either debtor control regulations or contractual mechanisms. A noticeable dichotomy prevails between these approaches, with most countries favouring one over the other in conjunction with insolvency regulations. Employing such distinct mechanisms to address diverse risks encountered by corporate creditors prevents unwarranted over-protection, thereby promoting a more robust safeguarding of creditors' interests.

Moreover, in selecting a creditor protection strategy, nations should prioritize the effectiveness of each approach in thoroughly addressing the potential risks faced by creditors, ensuring the provision of a comprehensive and necessary level of protection. Legal systems often integrate various strategies to guarantee the all-encompassing protection of creditors' interests, mitigating the limitations of one approach with the strengths of another. This amalgamation of strategies results in a more diversified and robust mechanism for safeguarding the interests of creditors.

On the other hand, mechanisms designed to protect creditors have undergone a process of harmonization, both in functionality and design, over time. Nations actively strive towards this goal by discarding regulatory measures that are deemed inefficient, costly, redundant, or cumbersome. Instead, they are adopting more streamlined and effective mechanisms to thoroughly address the risks encountered by creditors and ensure the necessary level of protection. Furthermore, countries aim to standardize their frameworks for creditor protection on a regional scale by embracing harmonized standards of creditor protection within their respective region.

The harmonization and convergence of creditor protection rights present a solution to ensuring consistent and efficient treatment for creditors, regardless of the jurisdiction in which the corporate debtor is incorporated or operates. Consequently, while identifying a universally accepted strategy for creditor protection is complex, different nations adopt specific strategies or a combination thereof based on their contextual circumstances. Significantly, corporate creditors' protection rights are undergoing harmonization regionally and globally. This applies to the three primary protection strategies for creditors examined in this study—Debtor Control, Security Mechanisms, and Insolvency Rules—and their implementation on a global scale. Therefore, given the universal nature of creditors' risk across jurisdictions, all countries employ at least one of the aforementioned methods for creditor protection.

Meanwhile, in 2021, Ethiopia implemented a New Code to align with international best practices in creditor protection. The previous Old Code had persistent deficiencies owing to delayed amendments. The introduction of the New Code seeks to rectify these shortcomings by integrating contemporary rules and terminology to safeguard the rights of corporate creditors. This initiative is a response to persistent demands from the commercial community and is consistent with Ethiopia's current stage of development.

The rules outlined in the New Code offer robust protection for creditors' interests, anticipating positive implications for future corporate governance. This alignment ensures that Ethiopia's protection rights for corporate creditors are in harmony with international best practices. However, to guarantee the comprehensive safeguarding of creditors' interest practical policies, procedures, and institutional frameworks must accompany the envisaged modern rules in the New Code, ensuring effective implementation.

In conclusion, corporate creditors across diverse regions encounter comparable challenges arising from information asymmetry and the opportunistic conduct of debtors. Such challenges are frequently attributed to the controllers of the corporate debtor exploiting the limited liability privilege. Despite distinct regulatory approaches among countries, the overarching goal remains the comprehensive protection of creditors by addressing all associated risks. Consequently, nations dismantle national barriers, acknowledging a shared objective of safeguarding creditors' interests. This commendable development signifies a progressive global convergence in strategies to enhance creditor protection.