FIFTH
PUBLIC
CONSULTATION
PAPER

5. COMPANY LAW AND ONLINE REGISTRY REFORM: CLOSING A BUSINESS

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GOVERNMENT OF THE KINGDOM OF ESWATINI.

NEW ZEALAND COMPANIES OFFICE

The Government of New Zealand, through the New Zealand Companies Office, is assisting with these reforms.

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Executive Summary

This is the fifth in a series of consultation papers prepared by the Ministry of Commerce, Industry and Trade (Ministry) regarding reforming the Eswatini Companies Act 2009 and subsequently implementing an electronic, online company registry. The first consultation paper provided a roadmap on how the reform would move forward; the second paper focused on issues around the initial incorporation of a company; the third paper discussed issues that affect the ongoing maintenance of a company, such as director duties and instituting a solvency test; and the fourth examined how companies raise capital and associated capital rules. This fifth paper examines the closure of a company—specifically how to close a company while protecting both shareholders and creditors. This paper will look at the following specific issues:

1. Are there interim steps that can help troubled companies keep them in business?
2. How can creditors best be protected?
3. What specific forms of insolvency procedure will be appropriate for Eswatini and
4. Should some form of cross-border insolvency be included?

The Ministry welcomes all stakeholder feedback. Comments should be directed to the following email address: ________________________.

1.0 Closing a company

Proper economic policy dictates that there should be an orderly procedure for winding down and ultimately closing a company. This procedure should balance various interests, including those of the shareholders, secured creditors, government, and other third parties that may have a claim over company assets. When a company's assets are liquidated, they should be distributed fairly. To promote lending, secured creditors should be at the top of the list. When a company becomes insolvent, and there is no realistic prospect of re-organization or rescue, it should go into some form of external administration. This approach—which policymakers should take—balances the various interests and aims to return the maximum amount to the various stakeholders of the company.

Under the existing Companies Act, the more traditional and historical types of winding up exist.[1] These are: winding up (both voluntary and by the court); liquidation; and a form of judicial management, which gives the court powers to deal with companies when they are unable to repay debts, but there is a reasonable probability that with appropriate management they would be able to remain a going concern.[2]

1 See Chapter XIV Companies Act 2009, Winding up of Companies.

2 Chapter XV Judicial Management

This paper considers some of the alternative options currently being supported by countries with modern company insolvency procedures. These options attempt to balance stakeholders' interests and maximize their returns while utilizing realistic time frames. Whatever insolvency framework is adopted, it must be appropriate for the types of business and business practices prevalent in Eswatini. The context is crucial and can only be determined by conducting extensive consultation with business and insolvency professionals.

The options to consider are (i) compromises with creditors, (ii) receivership, (iii) voluntary administration, and (iv) liquidation. In addition, cross-border insolvency is discussed for possible inclusion in the new company law framework.

1.1. Compromises with creditors

When companies enter financial difficulty, it serves society to try to help the company continue rather than immediately force it into liquidation. A provision in the law that recognizes compromises between a company and its creditors can be a powerful tool for achieving this. A compromise is usually a revision of the company's debt based on a proposal put forward by a party with an interest in avoiding the company's liquidation. If approved, it binds all creditors, including any individual creditor who may oppose the compromise.

The current Companies Act contains provisions related to compromises that generally appear satisfactory. However, they require the court to oversee and approve any compromise. Modern laws lessen court oversight, recognizing that a compromise is essentially a private agreement between a creditor(s) and the company. Further, there can be significant time delays waiting for court action, which can work to the detriment of both the company and its creditors. The Ministry believes that updating the provisions in Chapter XII to remove most judicial interventions will improve this process for both companies and creditors.

1.2. Receivership

Receivership is designed to maximize returns for secured creditors. In modern company law, a secured creditor can directly appoint a receiver if the company is in default. This immediate appointment is critical to protecting a secured party's position in collateral as delays can—and often do—end up lessening the value of the collateral or the business.

Chapter XV of the Companies Act contains provisions related to "judicial management," the older version of receivership. Overall, the provisions of Chapter XV seem appropriate, but it requires a court appointment of a judicial manager to oversee the company's affairs. The need for court intervention at this stage can cause significant financial hardship to secured creditors if the court cannot respond with haste to the application. Many countries allow for the direct appointment of a receiver if the underlying loan documents permit this step, and the Ministry believes this would be a good development for Eswatini creditors. Typically, in common law countries, the right to appoint a receiver has been a contractual matter, often included in the

loan documents and therefore regulated by the common law of contract. Some countries adopt a stand-alone statute to make the rules clearer for all. For Eswatini, it is recommended that receivership be provided for in the new Companies Act. The advantage of providing for receivership in the proposed Act is to provide a statutory code that outlines the rules and places clear statutory obligations on the parties and, most importantly, the receiver.[3]

The receiver will normally have the power to manage the company's business and, for example, sell assets. The term 'manager' is often used to describe a receiver, which highlights the function of the position.

1.3. Voluntary administration

Some countries have recently adopted provisions that provide for a voluntary administration process intended to help try to resuscitate companies under financial stress.[4] Voluntary administration is intended to be a relatively short-term measure that freezes a company's financial position while the administrator determines the company's future. The goal of voluntary administration is to give an insolvent company (or a company that, in the opinion of the directors, may become insolvent) two options. It can either reorganize and continue its business or, if the business cannot continue, develop a plan to dispose of the business that provides creditors and shareholders with a better result than immediate liquidation. It is often used when a short-term cash-flow issue threatens an otherwise viable business.

The process begins when the company's directors appoint an independent administrator. The administrator must then investigate the company's affairs and form an opinion as to whether it would be best for the company to: (i) enter into a "deed of company arrangement," setting out a new path forward for the company and its creditors; (ii) be put into liquidation; or(iii) end the administration and return to business as normal, as the company is still viable. Voluntary administration:

- creates a temporary pause for a company to address and remedy its problems as creditors are unable to take enforcement action against the company during a brief debt moratorium period;
- preserves the overall enterprise/goodwill value of the company, including employment and supplier relationships, during the pause;
- does not require a court application;
- provides for an orderly, transparent process under the direction of an independent administrator; and
- sees that creditors are paid their debt, in part or full, over a newly defined period, with any unpaid amount usually written off. Creditors are often willing to accept this new period as they will realize

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3 In its Corporate Insolvency Act 2017, Zambia provided a clear statement of duties and obligations of both receivers and liquidators.

4 See, for example, Part 15A of the New Zealand Companies Act.

more on their debt than if the company was put into liquidation.

If used in the right circumstances and the right way, voluntary administration is a powerful tool to restructure and rehabilitate a business. This serves all of society, as liquidation is usually a disastrous event for shareholders, creditors, and employees alike. The Ministry believes that including some form of voluntary administration provisions in the Companies Act could well serve Eswatini.[5] Any form of voluntary administration must balance the interests of secured creditors against the interests of the company owners very carefully.[6]

1.4. Liquidation

The existing Companies Act provides for the winding up and closing of businesses, including liquidation procedures. Just as with receivership, the current approach to liquidation seems generally satisfactory. However, one change could be significant. Under modern law, a liquidator can be appointed by the court, upon request from a shareholder or director, or if the creditors vote to move to liquidation. However, Section 310 of the Act only allows the Master of the High Court to appoint a liquidator. As with receivership, the need for court intervention at this stage can cause significant financial hardship to creditors if the court cannot respond with haste to the application. The Ministry believes that allowing the direct appointment of a liquidator will make the entire process more efficient.

1.5. Cross-border insolvency

The reform of the existing Companies Act provides an excellent opportunity to consider cross-border insolvency, the term given to describe circumstances where an insolvent entity has assets, creditors, or both in more than one country. As business is very much an international endeavor conducted across boundaries, it is more important than ever to ensure that rules regarding the rights to property across jurisdictions are perfectly transparent. This paper has already outlined approaches to dealing with a company and its assets in an insolvency.

The position becomes much more complicated where assets are located outside of Eswatini.

Questions arise as to whether the company assets outside Eswatini are available to creditors. The questions of priority and recognition of Eswatini creditors become a fundamental point of law, yet are not easily resolved. The additional complexities surrounding cross-border insolvencies result in significant risk, uncertainty, and costs to business. A possible solution is to adopt some form of the United Nations

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5 Indeed, Zambia's Corporate Insolvency Act 2017 included a form known as "business rescue proceedings" which introduced a statutory outline for the rehabilitation of a financially distressed company. Zambia's Act sets out a relatively straightforward rule framework to implement this protection for companies.

6 New Zealand introduced Voluntary Administration in 2007.

Commission on International Trade Law (UNCITRAL) Model Law on Cross-Border Insolvency. Like any other UNCITRAL text, it provides a uniform approach to dealing with the issues, and a country ratifies the law and makes it part of its domestic laws. This creates certainty around cross-border insolvencies and removes time delays and excessive costs. The Ministry suggests that Eswatini consider the adoption of this Model Law text to improve the overall insolvency laws.[7]

2.0. Conclusion

This paper has outlined the options available to Eswatini in reforming its approach to company insolvency. There are now newer and more streamlined methods of dealing with the various stages of insolvency. Although there are common approaches taken when designing each method, the most appropriate methods must be adopted for the economy and institutions that exist in the country. There is little point in introducing complex procedures if there is little institutional support, such as experienced insolvency practitioners. Context is fundamental to delivering the best framework for dealing with company financial stress and maximizing the outcome for both company owners and other stakeholders with a vested interest.

7 New Zealand enacted its Cross-Border Insolvency Act is 2006. Several African states have adopted this model law, most recently Zimbabwe in 2018.

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