

Taking Security in Africa

A Comparative Guide for Investors

Ethiopia

May 2024



About This Guide

In light of Africa's sustained economic growth over the last two decades, the continent has become an increasingly attractive destination for investment.

However, to a foreign investor, assessing legal risk requires an understanding of the laws and legal systems particular to the jurisdictions in which the investment is being made. The many different legal systems of the continent's 54 countries and regional blocs can be challenging to navigate. Africa's complex legal systems and the limited information about how those systems apply to foreign investments are often seen as obstacles to investment.

This guide provides an overview of the types of assets over which security can be taken, the different types of security, as well as the related procedures for the perfection and enforcement of such security in Africa. With contributions from leading local law firms, we focus on eight of the most active jurisdictions for foreign direct investment: Egypt, Ethiopia, Ghana, Kenya, Mauritius, Nigeria, South Africa, and Uganda.

This Ethiopia chapter was prepared with the help of Ethiopian firm Habesha Legal Advocates LLP.

Clement N. Fondufe, *Co-Chair, Africa Practice*
Kem Ihenacho, *Co-Chair, Africa Practice*

Contents

04	Types of Security Interests
06	Perfecting Security Interests and Priority
08	Enforcement of Security
10	Contacts

Types of Security Interests

What categories of assets are typically provided as security to lenders in Ethiopian financings?

Shares

Security over shares can be taken by way of a share pledge agreement.

Bank Accounts

Security over the proceeds of a bank account can be taken by way of agreement between creditor and pledgor (subject to the prior approval of the account bank — which is generally a purely administrative process). The pledgor will typically transfer a sum of money equal to the value of the security interest into a blocked account.

Land

In general, security cannot be granted over land because there is no private ownership of land in Ethiopia. However, security can be granted over the right to use land by way of pledge. An investor can also provide security over a leasehold land interest by way of a mortgage, provided that any such mortgage in respect of urban land is limited to the extent of the lease amount already paid.

Contractual Rights

There is no explicit legislative provision that allows security to be taken over contractual rights in general, except for security taken over public contracts from a contractor or subcontractor approved by the administrative authorities. It is also possible that security over contractual rights can be granted by way of an assignment unless such assignment is forbidden by law, the contract, or the very nature of the transaction. The pledgor must provide consent in order for the creditor (also in its capacity as assignee) to take possession of the asset received in pledge.

Insurance Proceeds

Security over a life insurance policy at surrender value can be taken by way of a pledge agreement or endorsement at the back of the insurance policy. Furthermore, security over insurance proceeds can be taken as an extension of a pledged asset.

Authorisations and Licences

There is no law regarding the creation of security interests over rights arising under authorisations or licences.

Intellectual Property

Security can be taken over patents, copyrights, and other intellectual properties. However, unless and otherwise agreed, a security interest in a tangible asset incorporating intellectual property does not cover the intellectual property itself, and a security interest in the intellectual property does not cover the tangible asset. Movable Property Security Right Proclamation 1147/2019 includes provisions about the security of intellectual property.

Personal Property and Tangible Assets

Security can be taken over personal property and tangible assets.

Types of Security Interests

Can security be taken over future assets?

Yes.

Can security be taken generally over all of a person's/entity's assets, or is it necessary to take security over each individual asset, or each class of assets, separately?

Security can be taken over all or part of a group of assets depending on the terms agreed by the parties. Pledges can be used for movable assets. Mortgages can be used for fixed assets (and may cover multiple fixed assets under a single mortgage).

Are there any restrictions on who can legally grant/hold a security interest?

As a general rule, any person who has the capacity to dispose of an asset or right can grant a security interest in that asset or right. However, there are some restrictions on the issuance of security depending on the issuer and the security instrument. For example, debentures cannot be issued by individuals, companies with capital that is not fully paid, or companies that have not issued a balance sheet in respect of their first financial year. Private limited companies cannot issue transferable securities in any form. Farmers and pastoralists cannot use their land as security when taking a mortgage, subject to regional nuances.

Are security trustees or security agencies recognised under Ethiopian law? If so, do any steps need to be taken to ensure the enforceability of a security trustee's or a security agent's right in the secured property?

Although the concepts of a "security trust" or "security agency" are not expressly provided for under Ethiopian law, pursuant to the law of contracts and agency, the relevant parties are free to agree and enter into a private contract in which one or more individuals or entities are identified or nominated as security agents to hold security for lenders. Further, the parties to the security agreement can agree to allow the third-party security agent to handle possession of the pledged property.

What about third-party security?

Under Ethiopian law, a person can grant security over their assets to secure the existing, future, or conditional obligations of a third party through an agreement of suretyship, pledge, or mortgage. However, a person can secure a third party's debt by way of mortgage only in cases where he or she is entitled to dispose of the immovable asset gratuitously at the time of such mortgage agreement.

Other Securities

Security can be granted over warehouse receipts, treasury bills, and government bonds in the form of pledges. Security over businesses can be granted either by contracts or by law in the form of a mortgage.

Perfecting Security Interests and Priority

Are there any asset-specific perfection requirements?

Bank Account

To perfect a security interest in a bank account, a notice of the security must be given to the account bank, which then provides its approval to validate the security. Moreover, the account bank can issue a letter of guarantee on behalf of the pledgor to the creditor. For example, the bank may provide a letter on behalf of the bank account holder to secure the appropriate discharge of security. The pledgor typically deposits a sum of money equal to the value of the secured amount to a blocked account, which cannot be accessed until the security is discharged. During such time, the account bank will continue to pay interest on the blocked account.

Shares

To take security over shares, an entry should be made in the register kept at the head office of the company. The shareholders themselves (i.e., not the pledgee) must represent the pledged shares at the annual general meeting of the company.

Contractual Rights and Life Insurance

Security over any instrument bearing a contractual claim can be taken in a similar fashion to the assignment of rights by analogy in the Civil Code through a separate agreement. Life insurance must be delivered to the pledgee or the third party named in the contract of pledge if the claim or right pledged is established by such instruments.

Land and Other Immovable Properties

Under Ethiopian law, mortgages over a lease (periodical usufruct), or any other immovable asset such as real estate must be registered at the applicable lands or immovable properties registry. Security over land use shall be registered by the secured creditor in the movable collateral registry which is under the National Bank of Ethiopia. There is no applicable time limit, although mortgages are only effective upon registration, and the date of registration determines the order of priority between the mortgages. Notably, the registry authorities are obliged to register the mortgage immediately when all legal formalities are satisfied.

Personal Property

Pledge: Under Ethiopian law, a pledge requires the transfer of actual or constructive possession of existing movable property.

Mortgage: Any mortgage agreement should be in written form and should specify, in Ethiopian currency, the amount secured by the mortgage agreement. A special power of attorney is necessary in instances in which the agent is required to sign on the client's behalf. The registration of a mortgage is effective for 10 years from the day the entry was made.

Business Mortgage: Businesses consisting mainly of goodwill, incorporeal elements such as copyright and patents, and corporeal elements such as goods, should be registered by the appropriate federal or regional authority and given a business licence in order to be eligible for mortgage.

Any business mortgage should be registered upon the request of an interested party by filing the two copies of the registration application form that are prepared by the registration authority. The applicant should also attach the contract and any other evidence that forms the basis of the registration request.

Perfecting Security Interests and Priority

What are the fees, costs, and expenses associated with creating and perfecting security in Ethiopia?

Stamp Duty

- Stamp duty is payable on all security deeds at the rate of 1% on the value secured by the security document. The stamp duty is payable before or on the date of signing of the security deed. The debtor bears the stamp duty cost unless otherwise agreed. In exceptional circumstances, an exemption from paying stamp duty may be obtained from the Minister of Finance upon application.
- Stamp duty should also be payable on notarial acts, contracts, agreements, and memoranda thereof, at the nominal flat rate of ETB 5. Separately, power of attorney stamp duty is charged at the nominal flat rate of ETB 35, bonds at the rate of 1%, and documents of title to properties at the rate of 2% (as applicable).
- The amount of stamp duty is calculated using an applicable average value of the stock or security at such time as the instrument is created if an instrument is chargeable with stamp duty on an *ad valorem* basis in respect of any stock or of any marketable security.
- Any person executing or signing (excluding witnesses) a stamp duty chargeable document who does not pay or fraudulently seeks to avoid paying stamp duty may face criminal punishment in the form of: (i) a fine of an amount between ETB 25,000 and ETB 35,000; and (ii) a term of imprisonment between 10 and 15 years. Further, the security document may not be validly registered and will be deemed inadmissible in the Ethiopian courts.
- Fees for the registration of a mortgage and related services, which can be determined by the appropriate authority, are payable based on the Commercial Code.
- Fees vary from ETB 30 to ETB 200 for the security registration-related services provided by the Movable Collateral Registry office located at the National Bank of Ethiopia.

Enforcement of Security

Outside the context of bankruptcy or insolvency proceedings, what steps should a secured party take to enforce its security interest?

Bankruptcy in Ethiopia is governed by the third book of the new commercial code of Ethiopia enacted in 2021 with Proclamation No. 1243, which replaced the fifth book of the 1960s Commercial Code.

- The scope of application of the bankruptcy legal regime covers all traders and business organisations, excluding joint ventures having no legal personality, as well as craftsmen and natural persons exercising independent professional activities.
- Bankruptcy can be instituted by way of a petition made by the debtor, one or more creditors, the public prosecutor, or the court itself.
- The competent court may declare bankruptcy of a company if there is suspension of payment or if the company is no longer able to meet its commitments relating to its commercial activities. The factual declaration of bankruptcy without court judgment has no legal effect in Ethiopia.
- There is no provision for a discharge in Ethiopian bankruptcy law. A bankruptcy proceeding cannot be closed, and the debtor is not restored to their full rights, unless the debtor proves that either: (i) all the creditors who have proved claims have been paid; or (ii) the trustees have been deposited with a sufficient amount to pay all creditors.

Are “company rescue” or reorganisation procedures available?

Yes, such procedures are available under the New Commercial Code of Proclamation No. 1243/2021 in the form of a preventive restructuring or a reorganisation. Preventive restructuring aims to enable financially distressed but viable debtors to efficiently restructure their debts with unanimous creditor consent, ensuring

continued operation or facilitating a business sale. Reorganisation proceedings aim to restructure debts and operations efficiently with the consent of a qualified majority of creditors, benefiting them through a reorganisation plan or business sale.

Are there any entities excluded by law from bankruptcy proceedings?

Non-commercial business organisations, i.e., ordinary partnerships and joint ventures with no legal personality, are excluded from Ethiopian bankruptcy law.

Are any governmental or other consents required in connection with an out-of-court enforcement of security?

No governmental or other consents are required for an out-of-court enforcement of security.

Are there any restrictions on who can enforce a security interest over assets located in, or governed by the laws of, Ethiopia?

No.

Will the commencement of insolvency proceedings against a grantor of security affect the ability of a secured party/creditor to enforce the security interests granted to it by that company?

No, a secured creditor will still be able to enforce its security. In the case of a pledge, the trustees may at any time pay for and redeem the property pledged for the benefit of the estate. However, the enforcement of the foreclosure right of a secured creditor can be suspended for a period of up to six months from the date of declaration of bankruptcy.

Enforcement of Security

Are there any preference periods, clawback rights, or preferential creditors' rights that creditors should be aware of?

There is a specific period of time, to be determined by a supervisory judge, in which to submit pre-insolvency claims. In fact, all proceedings for proving debts must be concluded no later than six months from the date of the judgment in bankruptcy. Clawback rights depend on the nature of the transaction and the good faith of the parties. For instance, the rights of creditors of a bankrupt party cannot be affected by the following transactions if such transactions are performed during a certain period (where such transactions can be questioned) or before the date of suspension of payments (factual bankruptcy) and the date of adjudication of bankruptcy (real bankruptcy):

- gratuitous assignments;
- payments of debts not due, whether in cash or by assignment, sale, set-off, or otherwise;
- payments of debts due otherwise than in cash, by negotiable instrument, or by transfer to a bank; and
- securities set up on the property of the debtor in respect of debts contracted before the setting up of such securities. Moreover, the trustees might request the invalidation and raise a clawback right of payments made by the debtor for all acts of consideration entered into by the debtor after the date of factual bankruptcy, if the counterparties receiving payment or dealing with the debtor had prior knowledge of the factual bankruptcy.

Can debt a company owes a creditor be contractually subordinated to debt that company owes another creditor? Are contractual subordination provisions that are agreed among creditors legally recognised on the insolvency or bankruptcy of the company?

No, there is no contractual subordination in Ethiopian law.

How is priority among secured parities determined on the insolvency of the debtor?

Secured creditors have priority over the encumbered asset to enforce their security. However, where there are amounts that are not secured by the security package, a secured creditor is treated as an unsecured party. The order of preference among the debtor's creditors is as follows:

1. costs and expenses of the proceedings;
2. costs of the new financing in the context of preventive restructuring;
3. costs of the new financing in the context of reorganisation;
4. costs of the new financing authorised in the context of bankruptcy;
5. post-bankruptcy creditors, including creditors of new and ongoing contracts;
6. employee claims and claims of social security authorities;
7. taxes and duties owed to federal, regional and local government authorities, other than those which can be claimed from the debtor holding taxes and duties on behalf of the government (but excluding interest and penalties);
8. amounts ordered for the maintenance of the bankrupt debtor and family;
9. other preferred creditors;
10. unsecured creditors; and
11. penalties and fines imposed upon the debtor.

Contacts

Latham & Watkins



Clement N. Fondufe

Co-Chair, Africa Practice
clement.fondufe@lw.com
+44.207.710.4685



Kem Ihenacho

Co-Chair, Africa Practice
kem.ihenacho@lw.com
+44.20.7710.4560



JP Sweny

Partner
john-patrick.sweny@lw.com
+44.20.7710.1870



David J. Ziyambi

Partner
david.ziyambi@lw.com
+44.20.7710.5807



Chidi Onyeche

Associate
chidi.onyeche@lw.com
+44.20.7710.1006

This guide was authored by Latham & Watkins in collaboration with:

Habesha Legal Advocates LLP
Taos Tower 3rd Floor Room #3, 19
Addis Ababa, Ethiopia

+251.115.581070
<https://habeshadvocates.com/Home>

Habesha Legal Advocates LLP



Yonas Girma Adimassu

Partner

LATHAM & WATKINS^{LLP}

Austin	Milan
Beijing	Munich
Boston	New York
Brussels	Orange County
Century City	Paris
Chicago	Riyadh
Dubai	San Diego
Düsseldorf	San Francisco
Frankfurt	Seoul
Hamburg	Silicon Valley
Hong Kong	Singapore
Houston	Tel Aviv
London	Tokyo
Los Angeles	Washington, D.C.
Madrid	

LW.com

Taking Security in Africa: A Comparative Guide for Investors is published by Latham & Watkins as a news reporting service to clients and other friends. The information contained in this publication should not be construed as legal advice. Should further analysis or explanation of the subject matter be required, please contact the lawyer with whom you normally consult. The invitation to contact is not a solicitation for legal work under the laws of any jurisdiction in which Latham lawyers are not authorized to practice. A complete list of Latham's thought leadership can be found at www.lw.com.

Latham & Watkins operates worldwide as a limited liability partnership organized under the laws of the State of Delaware (USA) with affiliated limited liability partnerships conducting the practice in France, Hong Kong, Italy, Singapore, and the United Kingdom and as an affiliated partnership conducting the practice in Japan. Latham & Watkins operates in Israel through a limited liability company, in South Korea as a Foreign Legal Consultant Office, and in Saudi Arabia through a limited liability company. © Copyright 2024 Latham & Watkins. All Rights Reserved.