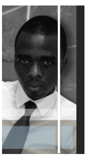

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Pooling of assets in Rwanda: what message does the new Insolvency Law send to corporate groups?

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It has been long-established by the classic fundamental principles of corporate law that companies are separate and distinct persons from their shareholders, directors and officers. From this flows the general principle that it is the company, and the company alone, that can be liable for its obligations. This holds even in cases of companies linked by direct and indirect share participation and which are, in their entirety, dominated by a parent company, often a mere holding company without any business activity. These are referred to in corporate jargon as “corporate groups”.

The existence of distinct legal personalities of companies under the same group of companies presupposes that it is conceivable that one of the companies under the parent company’s control may become insolvent and liquidated while other companies are doing well. As a consequence of limited liability of companies, if the assets of the insolvent entity cannot satisfy the claims of its creditors, they can presumably go unpaid without any single possibility to access the assets of other companies in the group. However, with the enactment of Law N° 23/2018 of 29 April 2018 relating to insolvency and bankruptcy (the “**Insolvency Law**”), creditors of companies (members of a corporate group) can now access the deep pockets of the parent company or other members of the groups that are doing well, thanks to the introduction of pooling of assets by the same law.

The pooling of assets is enshrined under article 121 of the Insolvency Law and provides as follows:

“On application of the liquidator, creditor or shareholder, the court may order that: (1) any company that is or has been a related company of the company in liquidation must pay to the liquidator the whole or part of any or all of the claims made in the liquidation; or (2) where two or more related companies are in liquidation, the liquidations in respect of each company must proceed together, as if they were one company, to the extent the court so orders and subject to such terms and conditions as the court may impose.”

The same law goes further in article 122, which provides factors that courts must take into consideration when deciding whether assets of the group can be pooled/consolidated, and those are “(1) the extent to which the related company took part in the management of the company in liquidation or any of the other company, (2) the conduct of the related company towards the creditors of the company in liquidation or any of the other company (3) the extent to which the circumstances that gave rise to the liquidation of the company are attributable to the actions of the related company, (4) the extent to which the businesses of the companies have been combined, (5) such other matters as the court considers appropriate.”

The Insolvency Law, however, provides that because creditors of a company in liquidation rely on another company that is or was related to it, this is not a ground for making an order of pooling of assets of related companies.

Indeed, each of the above factors needs to be given their concrete sense by courts, and it is one’s point of view that the first challenge courts will be faced with is to define the concept of “related companies” and whether the pooling of assets can extend to assets held by members of the group registered and operating offshore.

For instance, if one considers the first factor under article 122 of the Insolvency Law – the extent to which the related company took part in the management of the company in liquidation or any of the other company – it is the right of a parent company, as shareholder, to exert control over its subsidiaries by adopting decisions within the shareholders’ jurisdiction in accordance with the applicable laws and the subsidiaries’ constitutional documents. The parent company can also appoint members of the boards of its subsidiaries and, in some instances, directors of the parent company can change hats and sit on the subsidiaries’ boards. Whether this may be sufficient, or whether a greater degree of involvement is required in order to trigger the pooling of assets, is not clear from the law as it stands and is yet to be answered.

In any case, although each of the factors under the Insolvency Law will be elucidated down the road via case laws, it is at least clear for now that related companies may be viewed as one entity for the purpose of the consolidation of assets in the event of insolvency of one or more companies members of the group, and factors that may give rise to such consolidation are, for the first time, provided for by the law.

It is also uplifting to recognise that Rwandan law finally acknowledges the reality (and possible rise) of cross-jurisdictional corporate insolvencies that may impact on its jurisdiction. This suggests that corporate groups (which do not actually exist in law, but rather as an economic reality) need to revisit their way of directing the affairs of their members by adhering to proper corporate governance setting clear demarcation among powers of shareholders and management as well as avoiding parent/sister companies’ involvement in relationships between their subsidiaries/sister companies and third parties such as negotiating contracts and other similar acts. The introduction of the pooling of assets, especially the third and fourth factors (the extent to which the businesses of the companies have been combined and the extent to which the circumstances that gave rise to the liquidation of the company are attributable to the actions of the related company) may also affect cash pooling arrangements, which are a common practice in group of companies and most (if not all) multinationals.

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