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Corporate Bankruptcy Requirements & Impacts “Under the Egyptian Law

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Corporate Bankruptcy Requirements & Impacts “Under the Egyptian Law

Cover Page Footnote

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Corporate Bankruptcy *Requirements & Impacts*

“Under the Egyptian Law”

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Introduction:

The Extension of Bankruptcy to the Commercial Companies

The term “Merchant” does not only make reference to a natural person, but can also mean a moral person and, more precisely, corporations. As firms acquire commercial capacity, they become subject to the same legal regulations governing individual merchants. They can then be declared bankrupt just at the moment that they stop paying their commercial debts.

While much emphasis has been placed on the provisions of bankruptcy generally in jurisprudence and legislation, the bankruptcy provisions of corporations are somehow overlooked, although such provisions are those which should have been given due attention, for two reasons:

First, the role of a trading corporation is far more significant than that performed by individual merchants in the business field. Trading corporations bring together all efforts and savings of individuals into one whole. They undertake large-scale economic projects that individuals alone can not complete, irrespective of their abilities and potentials, making them the perfect tool for economic advancement. And so, with the growth of such significance, these corporations, and particularly joint venture companies, gained power that only the power of the state prevails over. They are recognized as a social and economic power, which are held in great respect by their country that feels like it is its duty to watch over them so that they continue on the right path, in order not to become a tool for social exploitation or political control⁽¹⁾.

(1) Dr. Mohsen Shafiq, *Intermediate in Commercial Law*, Chapter I, 3rd Edition, 1957, page 329, Dr. Aktham Al Khawli, *Comparative Lebanese Commercial Law*, Chapter II, *Commercial Companies*, 1968, page 2, Clause 1, Dr. Mohamed Fareed Al Areeni, *Commercial Companies, Collective Commercial Project Between Unity of Legal Framework and Plurality of Forms*, Dar El Gamaa El Gadida, 2011, page 7.

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Second, corporation bankruptcy has the most dangerous effect on national economy and the greatest influence on trade credit. The capital of these firms is, in most cases, quite as huge as their debts. What is more, not only does the bankruptcy of a corporation influence the life of such corporation, but also affects the creditors, partners, administrative structure, and even the employees whose number could reach thousands in some cases. And this will unquestionably culminate in affecting the national economy system in general.

In light of the ancient commercial codification, texts only contained very few provisions concerning partnerships. These include: Article 198, which provides for the determination of the names of joint partners as well as their domicile in the “cessation of payment” report submitted by the company, and Article 241, which requires affixation of seals upon bankruptcy of partnerships or commandite companies on the “headquarters of the company and the other separate branches of each of the joint partners, as well as Article 341 that authorizes conciliation, upon bankruptcy of a partnership, with one or more joint partners, and Article 408 detailing the conditions for a joint partner to regain capacity (to be discharged of bankruptcy) upon bankruptcy. With respect to non-partnerships, such as joint venture companies, texts made no mention of such companies⁽²⁾.

The fifth and last chapters of the new commercial law are devoted to bankruptcy. The law also deals with corporate bankruptcy in the seventh section of this chapter. Article 698 of chapter 7 stipulated that the provisions set forth in this chapter and the following rules shall apply to corporate bankruptcy.

That is to say, the rules provided for in section 7 of chapter 5 shall first apply when it comes to corporate bankruptcy. Where such rules make no mention of corporate bankruptcy, the rules set out in the fifth chapter concerning bankruptcy generally shall apply, in consistency with the nature and confidentiality of the company, factors that distinguish it from individual merchants.

Study Subject and Plan

Within the framework of corporate privacy tackled in this study, it could be concluded that corporate bankruptcy rules are set apart from individual merchant bankruptcy. Such privacy leads to the initiation of a number of questions that this study responds to. Of these:

(2). Dr. Mohsen Shafiq, Egyptian Commercial Law, Chapter II, Dar Al Thaqa, 1949, page 1058.

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1. It is common knowledge that bankruptcy is a merchant-related system. Thus, in order for a company to be adjudicated bankrupt, it has to acquire a commercial capacity. When does a company acquire such capacity and when does it fail to do so? And what are the issues associated with this requirement?
2. For a company to be declared bankrupt, it has to possess legal personality. What are the companies that possess such personality and can they be adjudicated bankrupt and what is the status of joint venture companies, dissolved companies and companies under foundation?
3. For a company to be declared bankrupt, it has to stop paying its commercial debts. When can these debts be classified as commercial. Is there a chance a company can be declared bankrupt after its termination. Is a minimum capital required?
4. Which court has jurisdiction for adjudication of corporate bankruptcy? What are the procedural rules to be followed? Are they distinguished from the procedures pertaining to individual merchant bankruptcy or the same rules apply?
5. Where a company is adjudicated bankrupt, does it result in its termination?
6. Where a company is declared bankrupt, what impact does it have on its partners?

This is just part of numerous questions that could be raised regarding corporate bankruptcy, and which move forward this study, whereby we seek to emphasize the privacy of corporate bankruptcy rules under the Egyptian Law. To that end, we will not address the general rules; but will instead tackle the issue of corporate bankruptcy rules.

The study is divided into two chapters:

Chapter 1 : Requirements of Declaration of Corporate Bankruptcy

Chapter 2 : Impact of Corporate Bankruptcy

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Chapter 1

Requirements of Declaration of Corporate Bankruptcy

Corporate bankruptcy proceedings are initiated upon issuance of adjudication order. This provision requires certain conditions to be met. Some of them are objective and the others are formal.

Therefore, this chapter is divided into two sections.

Section 1 : The objective requirements for declaration of bankruptcy

Section 2 : The formal requirements for declaration of bankruptcy

Section 1

The objective Requirements of Declaration of Bankruptcy

Introduction

The legislator regulated corporate bankruptcy in section 7, chapter 5 of the new Commercial Law no. 17 of 1999.

The legislator initiated this chapter by Article 698, which requires that the provisions set forth in this chapter and the following rules apply to corporate bankruptcy, in addition to Article 699 which stipulated the following:

1. Except joint venture companies, every company of any of the forms set forth in the companies' law, shall be deemed bankrupt in case it stops paying its debts due to business disturbance. Such company should declare bankruptcy by virtue of a relevant order.
2. A company may be declared bankrupt even if the company has gone into liquidation.

As stated in these provisions, rules pertaining to declaration of bankruptcy of individual merchants apply to declaration of corporate bankruptcy, in consistency with chapter 5 concerning the corporate bankruptcy.

We will also examine the conditions for the declaration of bankruptcy in light of these provisions through the following subjects:

Subject 1 : The commercial capacity of a company

Subject 2 : The legal personality of a company

Subject 3 : Cessation of payment

Subject 4 : The issuance of adjudication order

Subject 5 : Capital requirement

Subject 1

The Commercial Capacity of a Company

Limitation of bankruptcy to non- civil commercial companies:

Pursuant to the Egyptian law, bankruptcy is recognized as a legal system pertaining to merchants, whether individuals or trade firms. In the new commercial law, the legislator should have disregarded such differentiation between civil and commercial persons. Instead, the legislator should have established regulations pertaining to the liquidation of troubled enterprises whether they acquired commercial or civil capacity⁽³⁾. Unfortunately, this part of the law was somehow disappointing.

In fact, the Roman law and the Islamic jurisprudence, and even the recent laws, do not differentiate between merchant and non-merchant when it comes to liquidation of funds. Numerous non-commercial enterprises and companies could engage in very serious speculations in the activities of commercial companies, especially that the *Paulian Action* (Revocatory Action) does not provide effective protection for creditors⁽⁴⁾.

In a brief review of recent laws, we found that they confirm this matter.

The French Law itself- a historical source for the Egyptian Commercial Law – extends the regulations pertaining to liquidation of funds, judicial reform, and protection system to all civil law persons without differentiation between civil and commercial activities, since the 1967 amendment, and laws issued in 1984 and 1985 and finally the law of 26 July 2005 on business protection⁽⁵⁾.

The same applies to Anglo-Saxon laws. The American Law⁽⁶⁾ did not distinguish between merchants and non merchants. Any person, company or institution can file for bankruptcy themselves, once they stop paying their debts

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- (3) Thus, some considered necessary to issue a civil bankruptcy law, Review Dr. Nabeel Ibrahim Saad, Towards a Civil Bankruptcy Law, Dar El Gamaa El Gadida, page 2004, page 5, for further details, review Prof. Dr. Mohsen Shafiq, Egyptian Commercial Law, Chapter II, Bankruptcy, Dar Al Thaqafa, 1951, page 39, Review his Doctorate thesis in French “Different Systems of Civil Bankruptcy”.
- (4) Dr. Mohamed Saleh, Bankruptcy and Preventive Composition, Al Nahda Al Masrya, 1948, page 15, Dr. Mahmood Mukhtar Berairy, Commercial Transactions Law, Chapter II, Bankruptcy and commercial documents, Dar Al Nahda Al Arabeya, 2005, page 30. To the contrary, Dr. Sharif Makram, Discontinuation of Payment and its Impact on the Rights of the Bankrupt’s Creditors, Dar Al Nahda Al Arabeya, 2005, page 76
- (5) This has extended to agricultural activity, which is originally recognized as a pure civil activity, and even a typical example of civil works.
- (6) Review the American Law: Charles. G. Howard, Principe of business law P. 182.

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at maturity date, save five types. These are: railway companies, banks, insurance companies, municipalities, housing and finance companies. Nevertheless, once they become insolvent, these excluded types can submit to the bankruptcy court a request for restructuring approved by the Interstate Commerce Commission.

Also, the English Law does not distinguish between merchants and non merchants with respect to bankruptcy. The Insolvency Act, passed in 1985 regulated the provisions of bankruptcy for natural persons and businesses, without differentiation between merchants and non merchants in this regard. This law had a tangible impact on the English Companies Act of 1985, in terms of amending numerous provisions and eliminating numerous chapters. Parts 19, 20 and 21 of the Companies Act and Insolvency Act were integrated into one law, i.e. the Insolvency Act of 1986, which aims at providing real alternatives for the liquidation of any troubled business which can survive⁽⁷⁾.

Therefore, it was desirable that the Egyptian legislator should intervene to change his concept of bankruptcy and put in place collective procedures driven by the desire of reform and assistance in the first place and punishment in the second place, in addition to waiving the capacity of merchant, especially with respect to moral persons⁽⁸⁾.

Following the enactment of the new commercial law, civil companies do not practically exist. The legislator identified the forms of trade firms and failed to identify those of civil companies. Hence, civil companies would not practically exist, unless in the form of a joint venture company. The latter cannot be declared bankrupt as it does not possess legal personality. And so, criticism would be resumed should the legislator consider establishing legislations for civil companies in the future.

Criterion for a Company to Acquire Commercial Capacity:

The old Commercial codification used to rely on objective criterion to identify the capacity of a corporation. Such corporation used to be deemed a trading corporation where it engages in trade activities and a civil corporation where it engages in civil activities. However, in light of the new commercial law, the legislator adopted the formal criterion. Thus, a company shall be

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- (7) Review the English Law: I.F. Fletcher, law of Bankruptcy, P. 28.
FRICMAN (GH), Hicks & Johnson Fridman, Bankruptcy , Law and practice London , Butterworth , 1970.
Also see, Dr. Husssein Fathi, Bankruptcy and Preventive Composition, 2010, page 19.
- (8) Dr. Mahmood Mukhtar Berairy, Commercial Transactions Law, page 30.

deemed as a commercial company if it takes a commercial form and as a civil company if it takes a civil form.

In addition to commercial companies, it is noted the companies governed by other laws such as holding companies and subsidiaries which are governed by the Law No. 203 of 1991 Regarding Public Work Sector Companies and Public Sector Companies governed by the Law No. 97 of 1983, and companies operating in the field of securities, which are regulated by the Capital Market Law No. 95 of 1992 and investment companies regulated by the Law No. 8 of 1997 on Investment Guarantees and Incentives and money pooling companies regulated by the Law No. 146 of 1988⁽⁹⁾, in addition to other commercial companies regulated by special laws⁽¹⁰⁾, such as exchange, tourism and land reclamation companies⁽¹¹⁾

Subject 2 The Legal Personality of a Company

A juristic person is a legal entity which consists of a group of entities such as associations, companies, or investment funds such as institutions⁽¹²⁾.

Pursuant to Article 52 of the Civil Code, a company shall acquire legal personality, whether civil or commercial, save joint venture companies⁽¹³⁾.

As a company acquires legal personality, it shall start to act as an independent entity. Thus, it can declare bankruptcy. Acquisition of legal personality is a requirement for declaration of bankruptcy⁽¹⁴⁾. However, the legal personality applies to all branches, so a branch is not a separate legal entity, and a plant does not acquire a legal personality⁽¹⁵⁾.

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- (9) Dr. Samiha Al Kalyoubi, Commercial Companies, Dar Al Nahra Al Arabeya, 2007, Page 11. For a detailed study concerning the formal criterion, review Dr. Ashour Abdel Jawad Abdel Hameed, Relation between the Company's form and its activity, Dar Al Nahda Al Arabeya, 2000.
- (10) Dr. Abdul Rahman Al Sayed Kurman, Intermediate in New Commercial Law, Dar Al Nahda Al Arabeya, 2000, page 477.
- (11) The opposite in light of the cancelled codification, Dr. Eid ali Shahata, The Legal System of Commercial Company Liquidation, 1992, page 391.
- (12) Examine the legal personality generally: Dr. Suleiman Morcos, Al Wafi In Civil Code, Introduction to Legal Sciences and Interpretation of the Introductory Chapter to Civil Codification, 1987, P. 672 onwards, and the moral personality of the company: Dr. Abdul Razzaq Al Sanhuri, intermediary in the interpretation of the civil code, 5th Section, Ownership Contracts, Volume 2, Donation, Company, Loan, Permanent Income and Composition, Dar Al Kalam, P. 288 onwards. Dr. Mohamed Kamel Moursey, Interpretation of the New Civil Code, Nominated Contracts, Part II, Arab Statement Committee, 1952, P. 495, Dr. Abu Zeid Radwan. Legal Personality Between Fact and Fiction, Journal of Legal and Economic Sciences, 1970, Issue 1, P. 193, Dr. Mahmoud Mokhtar Bariri, Moral Personality of Commercial Companies, and Conditions to Acquire it, Dar El Fikr El Arabi, 1985.
- (13) Civil Cassation, Hearing Dated 28/12/1981, List of Civil Cassation Judgments, Y. 32, P. 2447.
- (14) Civil Cassation, Hearing Dated 7/6/1993, List of Civil Cassation Judgments, Y. 44, P. 575
- (15) Civil Cassation, Hearing Dated 6/12/1978, List of Civil Cassation Judgments, Y. 29, P. 1847

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As firms acquire legal personality, they start to act independently of their partners⁽¹⁶⁾, as well as of their directors and representatives⁽¹⁷⁾. It is therefore logical to establish that once a company stops paying its debts, it shall be declared bankrupt. That is to say that claim in bankruptcy targets the company itself, and not its partners or representatives⁽¹⁸⁾.

This requirement generates the following questions:

When does a company acquire legal personality?

According to rule, a company exists as a legal personality when it is duly established (Article 507 of Civil Code). Partnerships shall be deemed to be legally established following the approval by contracting parties on their incorporation and on all the provisions set out in the memorandum of association. With respect to stock corporations, they shall be deemed to be legally established after completing the incorporation procedures provided for by law. The foundation of the limited liability Company will not be complete unless all the cost shares are distributed in the act of constitution of the company between the partners, and their amounts are paid in full (Article 29/1 of the Law No. 159 of 1981)⁽¹⁹⁾.

A company shall acquire legal personality, regardless of whether bankruptcy declaration procedures have been completed or not. In fact, these procedures are not necessary for a company to acquire legal personality but for pleading purposes. Should bankruptcy not be declared⁽²⁰⁾, no plead in relation to the company shall be made before third parties⁽²¹⁾.

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- (16) Civil Cassation, Hearing Dated 28/3/1977, List of Civil Cassation Judgments, Y. 28, P. 808
 Civil Cassation, Hearing Dated 15/5/1986, List of Civil Cassation Judgments, Y. 37, P. 561
 Civil Cassation, Hearing Dated 23/2/1987, List of Civil Cassation Judgments, Y. 38, P.294
 Civil Cassation, Hearing Dated 26/12/1988, List of Civil Cassation Judgments, Y. 39, P. 1414
- (17) Civil Cassation, Hearing Dated 14/4/1966, List of Civil Cassation Judgments, Y. 17, S 2, P. 862,
 Civil Cassation, Hearing Dated 25/6/1969, List of Civil Cassation Judgments, Y. 20, S2, P. 1062,
 Civil Cassation, Hearing Dated 26/1/1976, Y. 27, List of Civil Cassation Judgments Y.27, P. 301,
 Civil Cassation, Hearing Dated 27/1/1994, List of Civil Cassation Judgments, Y. 45, P. 269.
- (18) The Court of Cassation ruled as follows:
 “The court found that the company possesses a personality that is independent of that of the representative thereof. Pursuant to the appealed judgment records, the respondent pled against the appellant company, through the legal representative thereof and requested the declaration of bankruptcy thereof. The rendered judgment required the declaration of bankruptcy of the legal representative of the company, for his capacity and not his person. Therefore, the judgment is rendered against the company and the impact thereof shall be limited to the company alone, as the principal litigant in the lawsuit.
- (19) Mohamed Fareed Al Areeni, Commercial Companies, op cit, p. 54.
- (20) See Article 506/2 of the Civil Code. In implementation thereof, review: Civil Cassation, Hearing Dated 16/6/1979, List of Civil Cassation Judgments, Y.30. Issue 2, P. 636, and Civil cassation, Hearing dated 2/6/1991, List of Civil Cassation Judgments, Y.42, P. 414, Civil Cassation, Hearing Dated 28/4/1993, List of Civil Cassation Judgments, Y. 44, P.266.
- (21) Civil Cassation, Hearing dated 8/1/1979, List of Civil Cassation Judgments, Y. 30, Issue 1, P. 127.

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If this is the general rule, there are however some relevant exceptions⁽²²⁾:

First: the exception of joint-stock companies, companies limited by shares and limited liability companies. Such companies can only declare bankruptcy and acquire legal personality fifteen days after their registration in the commercial register, unless the competent authority shall settle upon the acquisition of legal personality prior to this period. Excluded from this provision are the companies and facilities which perform their activity in Sinai Peninsula, which shall not acquire legal personality, unless pursuant to a decision by the chairman of the General Authority for Investment & Free Zones (Article 17 of Law No. 159 of 1981 amended by law No. 94 of 2005).

Second: the provisions of Law No. 203 of 1991 on passing the law of Public Sector Enterprises, with respect to holding companies or their subsidiaries. Pursuant to the first paragraph of Article one of this law, a holding company shall be established pursuant to a decision by the prime minister, based on the proposal of the concerned minister. Its capital shall be fully owned by the state or public artificial persons. Its legal personality shall be confirmed from the date of recording it in the commercial register. Under paragraph 3 of Article 16 of the same law: a subsidiary shall take the form of a joint stock company and acquire legal personality from the date of recording it in the commercial register”.

Third: companies established according to the law of Investment Guarantees and Incentive No. 8 of 1997 shall acquire legal personality from the date of recording the same in the commercial register.

Declaration of bankruptcy of a company under foundation:

Does a company under foundation possess legal personality and can thus declare bankruptcy?

To answer this question, we must examine the legal position of the founders and the company under foundation. It is common knowledge that the procedures of foundation may take time before a company acquires legal personality. During this period, the founders perform some legal acts such as purchasing headquarters and entering into contracts with workers and experts, etc.

Hence the question arises whether such acts have impact upon the founders or the company?

(22) Samiha Al Kalyoubi, Commercial Companies, op cit, p.110.

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It's so simple. Should the company establishment project fail, the company shall not acquire legal personality. The acts thus remain binding upon the founders personally. Therefore, in case of cessation of payment, the founders shall be liable for the declaration of bankruptcy- should its conditions be met.

Nevertheless, in case of the success of the company project and the latter acquired legal personality, the question arises whether such acts shall be binding upon the partners or the company, given that the company was established prior to acquiring legal personality.

There are a number of different views concerning this matter.

Notwithstanding the controversial doctrinal dispute⁽²³⁾, it is fair to say that doctrine and jurisprudence settled upon the fact that a company possesses legal personality during its foundation period to the extent necessary for its incorporation, as it possesses legal personality during its liquidation period to the extent necessary for its liquidation. This personality is not absolute and is limited to the extent necessary for its establishment. During the foundation period, the founders engage in a contract as representatives of a company under foundation⁽²⁴⁾.

This opinion is confirmed in Egyptian legislation, which recognizes the rights of the future person (Article 156 of Civil Code).

It is also confirmed in the provisions of the Law No. 159 of 1981. Article 13 of this law stipulates that all contracts and disposals effected by the founders in the name of the company under foundation, become of the right of the company after its foundation where they are necessary for its functioning in all other cases,

These provisions contain a clear recognition that a company under foundation possesses the required personality to respect the founders' disposals during the foundation period.

This opinion culminates in granting the company the rights and obligations which arise during the foundation period directly, without having the founders themselves acting as creditors, debtors, or liable for transferring these legal relationships to the company following its foundation. While founders shall be

(23) Review the details of the views and criticism addressed thereto, Dr. Abu Zeid Radwan, op cit, p.51. Mustafa Kamal Taha , op cit, p.347. Mohamed Fareed Al Areeni, op cit, p.166. Mohamed Kamel Amin Malsh, Companies' Encyclopedia, page 315.

(24) Review court judgments: Civil Cassation 24/1/1963, List of Civil Cassation Judgments, Year 14, P. 180, and in jurisprudence: Samiha Al Kalyoubi, Commercial Companies, op cit, p. 568. Tharwat Abdel Raheem, New Egyptian Commercial Law Interpretation, page 566. Abu Zeid Radwan, op cit, p. 53. Mohamed Fareed Al Areeni, op cit, p. 168. Ali Al Baroudy, commercial law, Dar al- Matboat Al Gameah, 2012, page 272.

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first discharged of personal obligations, they however remain responsible for the foundation mistakes before the company and third parties.

Based on the recognition of the company's legal personality during the foundation period, once the founders stop paying their debts pertaining to the required disposals to establish the company, the company may be declared bankrupt due to such debts arising prior to its foundation. Also, the period of doubt, i.e. the period which runs from the date of cessation of payment through the date of issuance of adjudication order, starts from the date of cessation of payment should the remaining conditions required for the declaration of bankruptcy be met.

The legal personality of a company under foundation remains however limited to the extent necessary for its foundation. Therefore, contracts and disposals effected by the founders during the foundation period in the name of the company shall not become of the right of the company after its foundation, unless they are necessary for its foundation. Otherwise, such contracts and disposals shall not become of the right of company after its foundation⁽²⁵⁾.

Thus, when it comes to disposals which are not necessary for the foundation process in case of cessation of payment in this regard, a company may not be declared bankrupt even if the founders may declare bankruptcy where relevant conditions are met.

Declaration of bankruptcy of Joint Venture Companies:

A joint venture company is an implied company that does not have apparent presence before third parties. Its activities are performed by one of its partners in its own name, provided that profits and losses shall be distributed among all partners⁽²⁶⁾.

A joint venture does not possess a legal personality independent of the personality of its partners⁽²⁷⁾.

(25) While taking into account the exception of stock companies, as set out in articles 12 and 13 of the Law No. 159 of 1981, stipulating that a disposal shall only be applicable if such disposal is approved by the company's board if all the board members had nothing to do with this disposal of the founders or had no concern in it, or is approved by virtue of a decision of the general assembly of the company in a meeting in which the interested founders have only limited votes (art. 13). The same provision applies to any disposal taking place between the company under foundation and its founders, which will not be applicable to the founded company unless such disposal is approved by its board or the general assembly of the company, as laid down above. The interested founder shall not under the consideration of the authority which approves the disposal, all the data connected with the said disposal. (art. 12).

(26) Mohamed Kamel Amin Malsh, *Companies' Encyclopedia*, page 586.

(27) See Civil Cassation, Hearing Dated 21/3/1968, List of Civil Cassation Judgments, P. 588, and Civil Cassation, Hearing Dated 4/1/1996, in Appeal No. 352 of 59.

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It should be also noted that a joint venture may take the form of a commercial or civil company depending on its purpose.

There is no room for the formal criterion adopted by the Egyptian legislator in the New Commercial Law to apply thereto. Such law provides that commercial capacity may be only acquired by the companies that take one of the legal forms, irrespective of the purpose for which they were established. (Article 10, parag. 2). The implementation of this criterion is reduced to companies that possess legal personality and take one of the legal forms, while a joint venture is an implied company that does not possess legal personality or a legal form⁽²⁸⁾.

Provided that a joint venture does not possess legal personality, it may not be therefore declared bankrupt⁽²⁹⁾. Declaration of bankruptcy is only reduced to the partners or directors of such joint venture, should they perform a commercial activity.

Declaration of Bankruptcy of Invalid Companies

A memorandum of association serves as a legal tool for the incorporation of a company. For a memorandum of association to exist, two types of conditions shall be met: objective conditions (i.e. compromise, eligibility, willingness that is free of defects, object and cause) and formal conditions (i.e. drafting and publication).

Failure to meet one of the aforementioned conditions, the memorandum of association shall be null and void. According to the general rules, invalidation shall be retroactive. That is to say that the company shall be deemed to have never existed.

In point of fact, the enforcement of these general rules has bad consequences, as it must be acknowledged that despite the fact that the company exists pursuant to a memorandum of association, but such memorandum of association is different than other contracts for it grants the company a legal personality⁽³⁰⁾. Everything is fine as long as such legal person did not deal with third parties. Otherwise, the memorandum of association shall become null and void and the legal person shall retroactively cease to exist. However, the

(28) Mustafa Kamal Taha, op cit, p.325.

(29) Article 699/1 of the New Commercial Law stipulated the following, while it has excluded joint ventures from the right of declaration of bankruptcy.

(30) A moral person is different than a legal disposal. A moral person is a legal person similar to a living being. While it is impossible to eliminate the existence of a living being past, this confirms the company to be a legal entity. Dr. Aziz Abdul Ameer Al Akili, Legal Difficulties arising from the Bankruptcy of the companies, Kuwait, 2010 p. 26.

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problem arises when such legal person deals with bona fide third parties and fails to recognize the reasons that might lead to the invalidation of the contract.

Perhaps this culminated in shifting the position of judicial authorities in this regard. Judicial authorities used to require the retroactive invalidation of a memorandum of association, and thus such company may not declare bankruptcy. However, their position has shifted and they recognized the actual or factual existence of the invalid company during the period prior to the invalidation order. Thus, such company possesses legal personality during such period and can thus declare bankruptcy⁽³¹⁾.

The corporation *de facto* theory touches upon the protection of apparent status on the one hand and upon the fact that the invalidation of a memorandum of association shall not be retroactive.

But is it possible to enforce the corporation *de facto* theory in all cases?

Jurisprudence and judicial authorities distinguish between the different reasons for invalidation. There are specific invalidation reasons not resulting in corporation *de facto*. Thus, such company may not be declared bankrupt even though claiming its partners may be possible. These reasons are:

1. If invalidation is based on the illegitimacy of the purpose and if the company aims at trading in prohibited goods or running gambling houses. In such cases, recognizing the existence of the company is like implicitly recognizing the illegitimate purpose.
2. If invalidation is based on the non-satisfaction of one of the objective conditions pertaining to the company's contract, such as the agreement among that one of them is not required to provide a share of funds or works, or in case of absence of shares or a bogus company, or the agreement to distribute the profits and losses in a way that not all the partners will be entitled to the profits and responsible for the losses, or in case of the lack of basis or willingness of partnership among the partners.
3. Stock companies do not transform into corporation *de facto* in case of invalidation of their contracts, by reason of lack of procedures required by

(31) For details review Dr. Mufleh Awad, Doctorate thesis, 1985. Dr. Mohamed Fareed al Areeni, op cit, p.47. Dr. Samiha Al Kalyoubi, op cit, p.96. Civil Cassation 9/11/1965, List of Civil Cassation Judgments, Y. 16, page 986. Cassation 25/04/1977, list of cassation judgments. 28. Page 1032, Cassation 2/2/1961, list of cassation judgments. 12, page 106.

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the legislator, for, in such case, such companies do not acquire legal personality⁽³²⁾.

Cases where invalidation of the memorandum of association results in transforming such company into a corporation *de facto* are as follows:

1. If the memorandum of association become invalid, due to a consent defect or the ineligibility of one of the partners

If the company is established among two partners and one of such partners is ineligible to enter into contract, the company's contract shall become invalid. As a consequence, the company, then consisting of only one partner, shall cease to exist due to such invalidation. It is common knowledge that a memorandum of association can only be entered into by two or more partners (Article 505 of the Civil Code). In this case, the company's bankruptcy may not be declared as it has ceased to exist. Bankruptcy proceedings shall be then reduced to the eligible partner solely, should such partner act as a merchant. That is not the case when it comes to companies established among three or more partners. In case of ineligibility of one of such partners, which shall result in the invalidation of the memorandum of association, such invalidation shall only have impact upon the future person. The company shall be deemed to actually exist among the fully eligible partners during the period running from its foundation through the invalidation order. Thus, it cannot be declared bankrupt when it stops paying its debts.

2. If the memorandum of association becomes invalid due to the lack of formal elements, provided that such elements do not result in the company's acquisition of legal personality.

In such cases, the invalid company shall have actual presence and possess legal personality, which allows for the declaration of bankruptcy.

Declaration of Bankruptcy of *De Facto* Companies

De facto companies are established among two or more persons that deal with each other just like partners, without executing a partnership agreement and without following declaration of bankruptcy procedures, and such companies do not take the form of a company⁽³³⁾.

The personality of such companies is revealed in the event of bankruptcy of one of the partners, and the commercial books thereof show that such partner

(32) Dr. Ali Jamal El Deen Awad, op cit, p.702. Aziz Abdul Ameer Al Akili, op cit, p.39.

(33) Dr. Mohamed Fareed Al Areeni, op cit, p.32.

has other partners. Thus, the trustee in bankruptcy may either require such partners to pay the company's debts existing between them and the bankrupt or enforce the bankruptcy proceedings on the actual partners thereof directly. The trustee in bankruptcy may require the declaration of bankruptcy of the actual company as a independent legal person then such bankruptcy shall extend to such company's partners as an actual joint liability company⁽³⁴⁾.

This was taken into account by the Egyptian court of cassation when it ruled as follows: "when the existence of an actual joint-liability company with a clear address is confirmed and each of its partners engaged in trade activity, such company shall possess legal personality that justifies the adjudication order⁽³⁵⁾.

Subject 3

Cessation of Payment

A company shall be declared bankrupt once it stops paying its commercial debts upon business disturbance (Art. 699/1). Everything said about cessation of payment applies to both individual merchants and commercial companies. Companies have no privacy when it comes to cessation of payment, which shall be subject to the general rules. However, the problem lies in the identification of the extent to which the company's debts are commercial; especially that bankruptcy can only be declared when a debtor shall stop paying the commercial debts thereof, according to rule.

As such, we will examine here two matters:

Compliance with the general rules of cessation of payment, and the extent to which the company's debts are commercial,

First: Compliance with the General Rules of Cessation of Payment

This requirement is subject to all the jurisprudential decisions regarding the individual merchant's cessation of payment. We, therefore, recommend examination of general books in this regard⁽³⁶⁾, as there is no need, in the field

(34) Dr. Ali Jamal El Deen Awad, op cit, p.550.

(35) Civil Cassation, 18/12/1952, Published in the Lawyers' Journal, Y. 34, P. 1260.

(36) Dr. Mohsen Shafiq, op cit, p. 177. Dr. Mustafa Kamal Taha, op cit, p.33. Dr. Samiha Al Kalyoubi, op cit, p. 47. Dr. Ali Hassan Younes, Bankruptcy in the new Egyptian Commercial Law, Dr El Fikr al Arabi, 1957, page 39. Ali Al Baroudy and Mohamed Fareed Al Areeni, Commercial Papers and Bankruptcy, page 256. Dr. Mahmood Mukhtar Berairy, Commercial Transactions Law, page 31. Dr. Hussein Fathi, Bankruptcy and preventive composition, page 39. Dr. Abdul Rahman Kurman, Intermediate in the new commercial law, Bankruptcy and preventive composition, Dar Al Nahda Al Arabeya, 2000, page 70. Sharif Makram, Discontinuation of Payment and its Impact on the Rights of the Bankrupt's Creditors, page 87.

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of this specialized research, to reiterate the general rules in detail. This is notably because these companies enjoy no specific privacy. We will limit ourselves here to outlining the broad outlines of the general rules of cessation of payment as follows:

1. Material cessation of payment is not enough for a company to be declared bankrupt. Such cessation of payment should rather result from such company's deteriorating financial position

This is a subject upon which the court of cassation has already expressed its opinion, by saying that "cessation of payment...reflects a poor financial position affecting the merchant's credits and putting such merchant's creditor rights at risk or highly potential risk⁽³⁷⁾.

This was established in Articles 550/1 on individual merchants and 699/1 on commercial companies of the New Commercial Law.

2. The trader shall not be declared bankrupt because of discontinuing the payment of the criminal fines, taxes, duties, or social insurance due on him. (Article 555, Commercial Law).
- 2- Where a company shall resort to using unlawful means to settle such dues, with a view to delay the material cessation of payment, e.g. a company may not be declared bankrupt if it sells goods or assets at trifling prices, as long as such company has not materially stopped paying its debts. However, when it comes to calculating the period of doubt, the judge calculates it from the date of using such unlawful means for payment, and not from the date of material cessation of payment⁽³⁸⁾.
- 3- For a company to be declared bankrupt, if it stops paying its debts, the following conditions shall be satisfied with respect to such debts:
 - a- Such debt shall be due and payable, funded and undisputed⁽³⁹⁾ (Art. 554/1), regardless of the value of such debt. In addition, the plurality of

(37) Civil Cassation 29 March 1956 Y. 7, P. 435, Civil Cassation 24 February 1970 Y. 21 P. 318, Appeal No. 380 of 48 Hearing Dated 9/3/1981 Y. 32, P. 775- Appeal No. 1514 of 51 Hearing dated 31/1/1983 Y. 34 P. 361, Appeal No. 1457 of 50 Hearing Dated 17/3/1986, Appeal No. 174 of 51 Hearing Dated 31/3/1986- Appeal No. 361 of 59 Hearing Dated 26/2/1990, Appeal No. 358 of 59 Hearing Dated 7/5/1990, Appeal No. 21 of 60 Hearing Dated 25/2/1991, Appeal No. 912 of 54 Hearing Dated 20/5/1991, Appeal No. 50 of 67, Hearing Dated 20/11/1997, Appeal No. 9022 of 66 Hearing Dated 8/12/1997- Appeal No. 476, 559 of 68 Hearing Dated 15/4/1999, Appeal No. 897 of 69 Hearing Dated 3/7/2000, Appeal No. 942 of 69 Hearing Dated 20/6/2000.

(38) For the contrary, review Mustafa Kamal Taha op cit, p.38.

(39) Civil Cassation Hearing Dated 1/3/1966, List of Civil Cassation Judgments, Y. 17, P. 481, Cassation 4/4/1967, List of Judgments, S. 18, P. 760, Cassation 9/4/1964, List of Judgments, Y. 15, P. 531, Cassation 28/4/1962, Y.13, P. 528, Cassation 18/5/1961, Y. 12, P. 489, Cassation 2/2/1961, List of

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This significant question is provoked by the legislator's adoption of formal criterion to identify the nature of the companies, and whether they are civil or commercial. But does it mean that the legislator adopts the same criterion to identify the company's debts also, or does he rely on the general regulations?

During the foundation period, there is no issue with respect to the company's debts. All these debts are commercial, according to law. In Article 4, paragraph f, the legislator established that the foundation of commercial companies is recognized as a commercial act. Therefore, all acts necessary for the foundation shall be deemed to constitute commercial acts according to law. The resulting debts shall be regarded as commercial debts, from the date of filing for incorporation with the competent authorities until taking adjudication and measures and registration in the commercial register. Publishing company foundation in newspapers and publishing subscription, share promotion processes, in-kind share valuation, shareholder subscriptions, collection of share value, issuance of shares and publication in the official gazette or the companies' journal and the procedures of registration in the commercial register, in addition to other processes pertaining to the foundation of all commercial companies⁽⁴¹⁾.

Debts arising during the foundation period do not give rise to any issues. The real issue, however, lies in the debts resulting from the company's activity performed during the post-incorporation period.

Some jurisprudential texts provide that the debts of a company that performs civil activities shall be deemed civil debts and partners shall not acquire merchant capacity and both the company and partners shall not be subject to the bankruptcy regulations⁽⁴²⁾.

While others establish that the formal criterion⁽⁴³⁾ adopted to identify the capacity of a commercial company applies to the acts and activities of such company. Such company shall thus be recognized as a commercial company even though it was originally established as a civil company. As a result, such company may be declared bankrupt if it stops paying such debts.

(41) Dr. Samiha Al Kalyoubi, Intermediate in the interpretation of the Egyptian Commercial Law, chapter I, Dar Al Nahda Al Arabeya, 2005, page 129 – 130. Mustafa Kamal Taha, op cit, p.83.

(42) Dr. Tharwat Abdul Raheem, the new Egyptian Commercial Law, page 294.

(43) Dr. Ali Jamal El Deen Awad, Bankruptcy in the new commercial law, page 652. Dr. Abbas Mustafa Al Masry, legal restrictions of the business theory, Dar Al Gamaa El Gadida, 2005, page 175. Dr. Mahmood Mukhtar Berairy, Commercial Transactions Law, Chapter I, Dar Al Nahda Al Arabeya, 2000, page 69. Dr. Fayez Naim Radwan, Commercial Law Principles, Dar Al Nahda Al Arabeya, 2000, page 220. Dr. Ashour Abdel Jawad Abdel Hameed, Relation between the Company's form and its activity, page 105.

The assumption is made that all the debts of the company shall be connected to its activities. Such debts shall therefore be deemed to be commercial at all times, whether resulting from naturally or collaterally commercial acts. Hence, the legislator did not insist upon commercial debts as an essential condition (Art. 699 commercial), because this is how it's supposed to be. This is inconsistent with the provisions of Article 550/1 commercial which states the merchant's cessation of payment of commercial debts as a condition. This is logical, because an individual merchant leads an independent life that could result in civil debts. The life of a commercial company, however, is limited to the scope of its activities for which it was established⁽⁴⁴⁾.

The French judicial authorities took into consideration this last opinion. In its ruling rendered on 18/2/1975, the commercial chamber of the court of cassation confirmed the ruling rendered by the court of appeal of Paris, whereby it ruled that the commercial court has jurisdiction to examine the conflict pertaining to a joint –stock company that engaged in expert accountant professions (free profession). Its ruling was based on the fact that these companies are deemed to be commercial, due to its form, irrespective of their object. This form culminates in the acts performed by the company being recognized as commercial⁽⁴⁵⁾.

Subject 4

Declaration of bankruptcy of a Company after Termination

According to rule, a company loses legal personality upon its termination. Nevertheless, bankruptcy can, in some cases, be declared after termination. We will examine this matter below:

First: compliance of merchant death or retirement provisions

Article 551/1 of the New Commercial Law states that “A trader may be declared bankrupt after his death or after retiring from trade activities, if he died or retired from trade while in a state of discontinued payments. The request for declaration of bankruptcy shall be submitted during the year following the death

(44) Dr. Abdul Rahman Kurman, op cit, pp.478-479. Dr. Hani Sameer Abdul Razek, the liability of the board members of the joint company in case of bankruptcy, Doctorate thesis, Faculty of Law, University of Cairo, 2006, page 51.

(45) Bull. Civ. 1975. 4. no. 48. p. 39 Gaz. Pal. 1975. 1. somm. 89. Rev. Trim..Dr.com. 1976.P.124. obs. Houin.

Look into the dominance of commercial form:

Dr. Youssef Motlaq Mohamed Al Mutawtah, Civil company of commercial form and the impact of bankruptcy thereon in both the French and Kuwaiti laws, Comparative Legal Study, Ph.D. Thesis, Faculty of Law, Cairo University, 2008, P. 258-259.

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or retirement from trade business. This period shall not begin to apply, in case of retiring from trade, except from the date of deleting the name of the trader from the Commercial Register”.

This text can apply to companies, especially that Article 698 in the seventh section on corporate bankruptcy states that “the provisions prescribed in this part (“bankruptcy”), and the following rules shall apply to the bankruptcy of companies. Pursuant to Article 698, all bankruptcy-related provisions generally shall apply to corporate bankruptcy, while taking into account the privacy of such companies.

As such, pursuant to Article 551/1, a company may be declared bankrupt after termination, if the following two conditions were met:

First condition: such company shall stop payment prior to termination. In such case, it is not sufficient for a company to use unlawful means for payment. In the case of use of such means prior to termination, such company shall not be declared bankrupt after termination until cessation of material payment. Excluded are fraud cases. If it has been proven that the company termination is the result of escaping bankruptcy, such company may be declared bankrupt⁽⁴⁶⁾.

Second condition: filing for bankruptcy shall be made within one year from the date of termination. Such year starts from the date of striking off the company’s name from the commercial register, in accordance with Article 551/1 of the New Commercial Law, from the date of the end of liquidation of the company.

Pursuant to Article 551/1 of the New Commercial Law, a company may be declared bankrupt one year after liquidation and struck off from the commercial register. During liquidation phase, a company may be declared bankrupt, according to the legislator, as described below.

However, controversy arose over the declaration of bankruptcy of joint-liability companies one year after their dissolution by reason of death of a partner. To that end, some believed that such companies may not declare bankruptcy as the bankruptcy of such companies shall lead to the bankruptcy of partners. According to rules, the bankruptcy of a deceased partner may not be declared one year after the death thereof. While most believe the deceased person’s bankruptcy may not be declared immediately one year after the death thereof. However, the bankruptcy of the company itself may be declared as it

(46) Dr. Mustafa Taha op cit, p.42, concerning the death of the merchant.

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represents an entity that is independent of its partners. Also, the text linking the declaration of bankruptcy with the one-year term is exceptional and only tackles the bankruptcy of deceased persons without approaching the declaration of bankruptcy of the company itself⁽⁴⁷⁾.

Second: declaration of bankruptcy of a company during liquidation period

Article 699/2 stated that a company may be declared bankrupt even during the liquidation process.

During the liquidation, a company maintains legal personality to the extent necessary for the liquidation works. Therefore, such company may be declared bankrupt, so that the company's creditors shall be able to claim their debts and entitlements prior to the end of liquidation.

While the company maintains its legal personality during the liquidation process, the legislator established that such company may be declared bankrupt. Article 533 of the New Commercial Law and Article 138 of the Companies Act no. 159 of 1981 are devoted to this issue⁽⁴⁸⁾.

This rule is inconsistent with the principles of logic which provide that a company shall cease to enjoy legal personality upon its termination. The practical necessity however, required these principles to be overlooked⁽⁴⁹⁾.

If these principles of logic were applied and the company ceased to enjoy legal personality upon its dissolution, say, the company's properties would have become a shared property among partners, and the personal creditors of the partners would have been able to compete with the company's creditors over the collection of their debts. There can be no way that they would be deprived of this right upon dissolution of the company, i.e. when this right can be exercised the most, on the one hand. On the other, the company and its creditors can be compared in this case to legacy and the legator's creditors. Just as the legator's

(47) Dr. Ali Jamal El Deen Awad, op cit, p.708.

(48) Mohsen Shafiq, op cit, Chapter I, p. 694, Mustafa Taha op cit, p.301, Ali Al Zayni, principles of the commercial law, chapter I, Chapter I, General Theory and Companies page 507, Samiha Al Kalyoubi, commercial companies, page 105, Mohamed Fareed Al Areeni, op cit, p.80. Tharwat Abdul Raheem, the new Egyptian Commercial Law interpretation, page 412. Abu Zeid Radwan, op cit, p.182.

Cassation 25/3/1944, List of Legal rules, Clause 39, P. 693- Cassation 18/5/1944, List of Legal rules, Clause 38, P. 693, Cassation 11/12/1947, List of Legal Rules, Clause 37, P. 693, Cassation 10/6/1965, List of Cassation Judgments, Y. 16, P. 752, Cassation 26/1/1976, List of Cassation Judgments, Y. 27, P. 302, Cassation 26/1/1981, List of Cassation Judgments, P. 337.

(49) For a detailed study about the bankruptcy of the company under liquidation, review Dr. Eid Ali Shahata, The Legal System of Commercial Company Liquidation, 1992, page 383.

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personality continues to be valid, the personality of a dissolved company shall remain valid until the end of liquidation process. Moreover, this principle constitutes a significant motivating factor for companies. Creditors are aware that they are prioritized over the partners' creditors to collect their debts from the company's property, in case of dissolution. Therefore, the personality of a company can only remain valid for liquidation purposes only⁽⁵⁰⁾.

In sum, a company may be declared bankrupt during the liquidation process, whether it shall discontinue payment prior to its termination or during the liquidation process.

It may also be noted that the company's liquidator represents the company throughout the liquidation period and replaces the directors and board members. Thus, should the company stop paying its debts during liquidation, the liquidator shall decide upon cessation of payment and can request the declaration of bankruptcy of the company⁽⁵¹⁾.

To the extent that the company's liquidator shall act as its legal representative prior to declaration of bankruptcy and perform the required acts for its fair liquidation, the company shall be deemed to have been placed into liquidation unless declared bankrupt, and the liquidator shall continue to act as its representative and shall be entitled to defend its interests where such interests shall be in conflict with the interest of the body of creditors represented by the bankruptcy trustee. The liquidator may also assist the bankruptcy trustee where the presence of the bankrupt is crucial, e.g. reviewing the books of accounts, the budget and inventory. Even so, the right to company property management and disposal shall be transferred to the trustee in bankruptcy who shall be responsible for liquidating the company's property collectively and distribute the resulting amounts among the creditors. In the event that the company's assets shall exceed its debts, the bankruptcy trustee shall deliver such assets to the liquidator who shall distribute the same among the partners⁽⁵²⁾.

However, it must be noted that, during the liquidation process, the company may not request composition. Composition aims at assisting the merchant and assistants thereof in continuing to perform the commercial activity thereof and overcoming the crisis. This is inconsistent with the liquidation purposes that arise due to the existence of a legal reason for the company's termination⁽⁵³⁾.

(50) Dr. Ali Al Zayni, op cit, p.507-508.

(51) Dr. Mohsen Shafiq, Egyptian Commercial Law, page 1069. Eid Ali Shahata, op cit, p.419.

(52) Dr. Eid Ali Shahata, op cit, p.427-428.

(53) Dr. Aziz Abdul Ameer Al Akili, op cit, p.24.

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Hence, the question arises whether it is possible to declare the bankruptcy of the company after liquidation, in case of cessation of payment during liquidation, based on what is already contained in the previous clause with respect to the admissibility of declaration of bankruptcy of a company after its termination in case of cessation of payment before this happens.

While some provisions confirmed this, others prevented it, on the grounds that a company shall cease to exist upon dissolution and not from the date of end of liquidation. What is more, a company shall be deemed to have been dissolved upon quitting trading and not at the end of the liquidation, as such company is prevented from performing new acts during liquidation⁽⁵⁴⁾.

To conclude, it must be agreed that a company shall cease to enjoy legal personality at the end of the liquidation. Liquidation shall end by turning the company's assets into divisible funds among partners and collecting all the company's dues and settling all its debts. In the event that some company creditors shall fail to collect their dues, the company shall continue to exist and enjoy legal personality and shall be declared bankrupt even if the partners shall ratify its accounts and agree upon the end of liquidation, as long as the company's assets have not been distributed among the partners. Otherwise, the company shall be terminated, and the creditors shall be entitled to sue the partners personally. The creditors shall, in this case, have priority over the assets of the partners, to the extent that such assets are in kind and may request the declaration of bankruptcy of the partners if the relevant conditions are met⁽⁵⁵⁾.

Third: Declaration of bankruptcy of Transformed Companies

Transformation is the change of the legal form of a company, e.g. transformation of a joint-liability company into a commandite partnership or a limited liability company or the transformation of a company limited by shares or a limited liability company into a joint-stock company.

Here, the question arises whether such transformation does not culminate in terminating the transformed company or results in establishing a new company or, more specifically, a new legal personality.

The prevailing opinion distinguished between transformation authorized by law or in the company's memorandum of association, and that which is not stipulated by law or in the memorandum of association. Transformation

(54) Dr. Ali Jamal El deen Awad op cit, p.28.

(55) Dr. Ali Jamal El Deen Awad, Ibid p.29.

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authorized by law or in the memorandum of association does not result in the termination of the company and the loss of its personality, but such personality shall rather continue to be valid in the new form. However, the persistence of the original legal personality does not mean the company may be exempted from complying with the decided incorporation rules and procedures of the new form of the company, unless the legislator shall otherwise indicate. With respect to transformation that is not stipulated by law or in the company's memorandum of association, it shall result in the termination of the first company and the establishment of a new company⁽⁵⁶⁾.

Accordingly, in those instances where a company shall preserve its legal personality, it shall be held accountable for the debts it has stopped to pay in its previous form, and hence it may be declared bankrupt due to these debts. However, in cases where a company loses its legal personality, it shall be subject, in its previous form, to the already contained provisions of declaration of bankruptcy after termination.

With respect to the impact on partners, we will approach this issue in the second chapter of this research.

Capital Requirement

Pursuant to Article 550/1, a merchant may only be declared bankrupt if such merchant retains trade books. Accordingly, merchant not holding trade books may not be declared bankrupt.

A merchant who undertakes to hold trade books⁽⁵⁷⁾ is a merchant whose capital invested in trading activity exceeds twenty thousand Egyptian pounds.

In this requirement, the legislator sought not to subject small merchants to the stringent bankruptcy regulations. The legislator also aims to encourage small enterprises and not to intimidate them over declaration of bankruptcy in case they shall stop paying their debts.

This provision applies to both individual merchants and companies, even if practical necessity only exists with respect to small sized individual companies, as there can be no way that a stock company would be established with a capital less than twenty thousand Egyptian pounds.

(56) Dr. Mustafa Kamal Taha, op cit, p 235, for the contrary, review Dr. Ali Jamal El Deen Awad, op cit, p. 36.

(57) When a person becomes a merchant, he has to meet several obligations, among them is the obligation to maintain trade books, This obligation is basically imposed to let the merchant be able to know the exact state of his business and the result of his transactions.

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The estimation of the amount of capital invested in trading activities shall be subject to the authority of the ad hoc judge, especially that the determination of the amount invested in trade gives rise to several issues. That is to say, is the amount recognized in the commercial register and recorded in the trade activity publications just a capital, or does it represent the merchant's size of business and property. The project's stated capital does not represent the size of the merchant's business, e.g. real estate companies, commercial agencies and brokerage firms.

A small amount is usually recorded in the commercial register, although the size of funds invested in trade activity can reach up to hundreds of thousands and millions. Some⁽⁵⁸⁾ do not look at the amount stated in the commercial registers as a basis for filing bankruptcy claims against the debtor who discontinued payment. The creditor must be able to prove the size of funds invested by the debtor merchant and that such funds exceed the minimum amount referred to in Article (21) of the New Commercial Law.

This conclusion has been reached by the court of cassation, pursuant to a recent non-published ruling whereby the court has ruled that – even if the first paragraph of Article 550 of the New Commercial Law no. 17 of 1999 on declaration of bankruptcy of merchants required the retention of trade books and Article 21 of this Law required every merchant whose capital invested in trade exceeds twenty thousand Egyptian pounds to retain such books, the legislator, however, did not determine such amount, and but left the matter to the ad hoc judge to identify the amount invested in trading activities. Such amount is not necessarily reduced to the capital owned, whether recognized in the commercial register thereof or the amount actually used in trading activities. This shall also extend to the size of financial transactions conducted thereby to activate the business⁽⁵⁹⁾.

Any statement to the contrary shall in fact culminate in numerous commercial enterprises escaping bankruptcy regulations, especially after the

(58) Dr. Samiha Al Kalyoubi, op cit, p 42.

(59) See Judgment in Appeal No. 597 of 72, Hearing dated 10/4/2007 (non-published). The court stated: "if the appealed judgment touched upon the availability of capital invested in trade with the appellant, as specifically mentioned in the extract of the commercial register thereof, and the loan contract with a value of 265900 Egyptian pounds, as well as the data contained in the insurance policy valued at 525900 Egyptian pounds and the declaration whereby ?/ to obtain a loan to fund and operate the working capital thereof in trading activities, it was thus concluded that the appellant's capital invested in trades exceeds twenty thousand Egyptian pounds. Hence, the appellant may be declared bankrupt. Therefore, the judgment has valid grounds and is based on the facts shown in the papers.

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enactment of the New Commercial Law No. 17 of 1999, as some intentionally abstain from mentioning a capital exceeding the minimum required amount referred to in Article (21) of the New Commercial Law, with a view to avoid being governed by the bankruptcy provisions.

Section 2

Formal Requirements for Corporate Bankruptcy (Issuance of Adjudication Order)

A company shall not be deemed to have been gone into bankruptcy, unless a relevant order has been issued. Accordingly, cessation of payment shall not serve as the only cause of bankruptcy⁽⁶⁰⁾, as stipulated in the New Commercial Law no. 17 of 1999.

There is no privacy in corporate bankruptcy when it comes to the issuance, nature, implementation and challenge of the adjudication order. That being so, we will not approach these matters, but will rather discuss two matters only: the competent court for bankruptcy proceedings and how to request the declaration of bankruptcy of the company.

First: The Competent Court for the Declaration of Bankruptcy of the Company

1- Qualitative Jurisdiction

Prior to the enactment of the Law No. 120 of 2008 concerning the Establishment of Economic Courts, the qualitatively competent court that has jurisdiction to declare the bankruptcy of companies and bankruptcy generally was the Court of First Instance.

However, with the enactment of this law, economic courts became the only competent courts for declaration of bankruptcy and preventive composition. These courts also have jurisdiction over bankruptcy-related conflicts.

An economic court consists of a first instance circuit which has jurisdiction over cases with a value less than five million Egyptian pounds, as well as an appeal circuit for cases of undetermined values. Provided that bankruptcy claims have no defined values, the economic courts' appeal circuits shall have qualitative jurisdiction over the declaration of bankruptcy of companies.

(60) Doctorate thesis of Dr. Mustafa Taha in French entitled "analytical study of the theory of real bankruptcy", Paris 1948. Mustafa Taha, Bankruptcy principles, page 45.

2- Local Jurisdiction

The circuit court where the head office of a company is located shall have jurisdiction to declare the bankruptcy of a company⁽⁶¹⁾.

The head office of a company shall mean the place where such company performs its legal activities, i.e. Where decisions are made and the company's affairs are conducted and shall not mean the commercial center. This is consistent with the provisions of Article 53/3 of the Civil Code which reads as follows: a juristic person has its own domicile. This domicile is the place where its seat of management is situated. A corporation, whose seat of management is situated abroad but operates in Egypt, is deemed, in accordance with internal law, to have its seat of management at the place where its local seat of management is situated⁽⁶²⁾.

A company that has a branch in Egypt may thus be declared bankrupt, even if no adjudication order has been issued in a foreign country, without prejudice to the bilateral and multilateral international agreements enforceable in Egypt.

In the event that the foreign company's branch shall discontinue payment of its debts arising out of contracts and transactions executed in Egypt, the company may be declared bankrupt, provided that the bankruptcy impact shall be reduced to the company's property in Egypt only and shall not extend to the company abroad, according to the principle of territoriality of bankruptcy.

(61) The court of cassation ruled as follows: "Whereas the first respondent has, in his own capacity, filed for bankruptcy of the appellant company with North Cairo Court, even though the papers reveal that the head office of the company is located in Maidan Al Dhaher No. Bab el Shaariya district, which is subject to the local jurisdiction of South Cairo Court . If the appealed judgment overlooked this matter, it is therefore inconsistent with the law. (Appeal No. 428 of 72, Hearing Dated 26/5/2003 (non-published)).

(62) In a non-published judgment, the court of cassation ruled the following: "Paragraph 1 of article 559 of the commercial law no. 17 of 1999 indicates that the competent court that has jurisdiction over the declaration of bankruptcy of debtor merchant shall be the one within the circuit of which his ordinary domicile is located. Parag. 2 of Article 700 of the same law stipulated that the initiatory pleading referred to in article 553 of this law shall be submitted to the clerks office of the court within the circuit of which the company's head office is seated. If this head office is located within Egypt and shall be determined depending on the location where the company performs its legal activity and where its main offices are located and the director performs his tasks and the board and general assemblies hold their meetings in the headquarter if the company either the bankruptcy requestor is the debtor of the company or the persons stated in clause 1 of the article 700 of the new commercial law.

Based on the foregoing, and whereas the appealed judgment overlooked this requirement and the implementation of article 700/2 of the new commercial law was reduced to those mentioned in clause 1 of the last text only, despite the generality of and the inclusion thereof in the chapter of corporate bankruptcy, it is therefore flawed and made no mention of the head office of the company based on which the local jurisdiction shall apply. Appeal No. 722 S. 73, hearing of 27/06/2005 (non-published).

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Pursuant to such principle, the bankruptcy's impact shall be limited to the country where bankruptcy has been declared. The adjudication order issued in a foreign country shall have no impact on the bankrupt's property in Egypt. Accordingly, the declaration of bankruptcy of a foreign company abroad shall not serve as a substitute for filing bankruptcy with respect to the activity of its branch in Egypt. Therefore, upon the issuance of the adjudication order with respect to the company operating in Egypt, the two bankruptcy proceedings shall be separate with two different adjudication orders in two different countries⁽⁶³⁾.

As both bankruptcy cases are connected to one financial entity, hence the question arose: are the company's creditors whose debts arose abroad entitled to file for bankruptcy in Egypt and are the creditors whose debts arose in Egypt entitled to file for bankruptcy abroad?

To that end, the French Court of Cassation authorized foreign creditors to enter into bankruptcy proceedings in France, even if French creditors are prevented from entering into bankruptcy proceedings abroad. The bankruptcy regulations embody the fundamental principle of the "equality among creditors", irrespective of their nationalities.

For its part, the Egyptian judicial authorities seemed somehow reluctant in this regard. The Mixed Court of Appeal ruled as follows: if a company operating in the country where its head office is located is declared bankrupt and in Egypt where its branch is located, there shall be two separate bankruptcy cases. Creditors may enter into both bankruptcy proceedings. However, the Mixed Court of Appeals took back what it has previously stated in another ruling subsequent to the first one. In this ruling, the court ordered the allocation of property in Egypt to settle the creditors' debts arising in Egypt, whether such creditors were Egyptians or foreigners.

Creditors whose debts arose abroad may not take part in the Egyptian bankruptcy proceedings unless on the basis of reciprocate treatment.

For our part⁽⁶⁴⁾, we advocate the decision of the French judicial authorities and the first ruling of the Mixed Court of Appeals. Creditors in either bankruptcy case may seek their dues in the other bankruptcy case, for two reasons:

(63) Dr. Reda Al Sayed Abdul Hameed, *the Effect of the Company's Bankruptcy on the Partners*, Dar Al Nahda Al Arabey, 1998, page 12.

(64) Dr. Reda Al Sayed Abdul Hameed, *op cit*, p 14.

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First: despite the presence of two bankruptcy cases, but both cases are connected to the same financial entity. It would be inappropriate to say that the company's property in Egypt shall be allocated to settle the debts arising in Egypt. In the ruling referred to above, the Mixed Court of Appeals established that this allocation shall be founded on a provision of law.

Second: pursuant to Article 650 of the New Commercial Law, which applies also to companies, by cause of absence of special provisions in the chapter of corporate bankruptcy, all creditors, without differentiation between those whose debts arose in Egypt and those whose debts arose abroad, shall be entitled to provide the bankruptcy trustee with the documents of their debts, following the adjudication order, in order to collect the same.

Second: How to Request the Declaration of Bankruptcy of the Company

A company may be declared bankrupt upon the request of its representative, one of its creditors, the public prosecution or the court itself.

1- Declaration of Bankruptcy upon the request of the company's representative, in accordance with Article 700 of the New Commercial Law: "The legal representative of the company may not request declaring its bankruptcy except after obtaining permission for it from the majority of the partners or the General Assembly according to each case.

This Article, however, did not specify the type of required majority in the case of individual companies and whether such majority is simply a numerical majority or a certain capital majority and whether such majority is ordinary or extraordinary with respect to the companies governed by Law No. 159 of 1981 on Joint Stock Companies, Partnerships Limited By Shares & Limited liability Companies.

Pursuant to the provisions thereof, it is clear that the required majority for individual companies represents the numerical majority. This was subject to criticism as requesting declaration of bankruptcy by the legal representative of the company is of great significance, which should have required a numerical majority owning a certain percentage of the company's capital exceeding 50% of its capital. Requesting declaration of bankruptcy of a company is quite as important as requesting liquidation or dissolution of a company. Also, it is important to take into account whether the company's memorandum of association requires a percentage higher than the number of partners or the capital to request declaration of bankruptcy; as such percentage shall apply

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instead of the provisions of the aforementioned Article (700) of the New Commercial Law.

With respect to requesting declaration of bankruptcy of a company governed by the Law No. 159 of 1981, the legal representative may only request the same after obtaining the approval of the extraordinary General Assembly or the equivalent thereof, although the provisions of Article (700/2) of the New Commercial Law did not specify the type of assembly.

Pursuant to Article 70/2 of the referred to Companies Act, the legislator requires Shareholders representing at least one quarter of the capital to attend the extraordinary General Assembly meeting⁽⁶⁵⁾.

Pursuant to paragraph 2 of the same Article (700), the initiatory pleading shall be submitted to the clerk's office of the court within the circuit of which the company's head office is seated. If the head office is located outside Egypt, the initiatory pleading shall be submitted to the clerk's office of the court within the circuit of which the local administration office of the company's is Located.

This initiatory pleading shall contain data included in the statement of claim filed for the declaration of bankruptcy of the merchant. It shall include the reasons for cessation of payment. The Article added other information which shall be contained in the initiatory pleading, i.e. names of the existing joint partners, and those who quit after it discontinued the payments, together with an indication of the domicile of each joint partner, his nationality, the date/month in which he quit, in the commercial register⁽⁶⁶⁾.

(65) Dr. Samiha Al Kalyoubi, op cit, pp 290-291, Dr. Abdul Rahman Kurman, op cit, p 483.

(66) The court of cassation ruled that paragraph 1 of article 699 of this law stipulated "With the exception of joint ventures, each company assuming one of the forms prescribed in the Companies Law shall be considered in a state of bankruptcy if it discontinues paying its debt following confusion of its financial affairs. its bankruptcy shall be declared by virtue of a court ruling to be issued therefore. Parag. 2 of Article 701 of the same law provided that "If the creditor requests declaring the company bankrupt, all joint partners shall be litigated against. Also, article 703 of the same law established that
 "1- If the company is declared bankrupt, all joint partners thereof shall be declared bankrupt...., 2- The company shall pass a ruling in which it pronounces the company's declared bankruptcy together with the declaration of the bankruptcy of the joint partners even though it may not be concerned with declaring the bankruptcy of these partners....". this implies that even though the legislator has codified the court of cassation's decision that an adjudication order shall lead to the declaration of bankruptcy of all joint partners of such company, but he established that bankruptcy claims of joint – liability companies and limited partnerships became, according to this rule, among the claims in which law requires certain persons to be litigated against, i.e joint partners in order to push such partners to promptly settle the company's debts, for fear that they may be all declared bankrupt by virtue of the company's bankruptcy declaration order, which ensures the prompt settlement of its creditor's dues and helps reduce the declaration of bankruptcy of this type of companies and the resulting impact on the commercial and economic stimulation, in addition to reducing the opportunities of foreign investments (Appeal No. 982 of 73, Hearing dated 8/6/2004, Appeal No.

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Such information indicate that by ordering declaration of bankruptcy, the court passes a ruling in which it pronounces the company's declared bankruptcy together with the declaration of the bankruptcy of the joint partners even though it may not be concerned with declaring the bankruptcy of these partners.(Article 703/2) of the law.

Hence, in case of absence of joint partners in the company requested to be declared bankrupt, such as joint-stock companies, there can be no way that the initiatory pleading would include such information reduced to joint partners.

2- Declaration of Bankruptcy Upon the Request of the Company's Creditor

The company's creditor may make a request for declaration of bankruptcy of such company, even if such creditor shall be a partner thereof.

To that end, the request for declaration of bankruptcy shall result from a debt not linked to such creditor's capacity as a partner in the company, as though such partner lent the company money that the company failed to pay. He shall thus have interest in requesting the declaration of bankruptcy in his capacity as creditor. The same applies to the partner in a bank, who shall be able to request the declaration of bankruptcy of the bank if he deposited money with such bank and the bank discontinued payment upon request⁽⁶⁷⁾.

On the other hand, if the partner is not a creditor, such partner may not, in his individual capacity, request declaration of bankruptcy of the company, although a partner shall be regarded as a creditor with respect to part of the profits and the company's assets upon dissolution or liquidation.

In the event that the creditor shall request the declaration of bankruptcy of the company, the creditor shall solicit all joint partners, as the bankruptcy of the company results in the bankruptcy of the joint partners. It is thus necessary to declare their names in the statement of claim.

3- Declaration of Bankruptcy upon the Request of the Public Prosecution.

The public prosecution may request the declaration of bankruptcy of the debtor, whether an individual merchant or a commercial company. Companies

630 of 72, hearing dated 22/6/2004, Appeal No. 8 of 73, Hearing Dated 25/1/2005, Appeal No. 258 of 78, Hearing dated 9/2/2009, non-published judgments).
(67) Dr. Mohsen Dhafiq, Bankruptcy, page 1067. Dr. Ali Jamal El Deen Awad, op cit, p 649.

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enjoy no privacy in this respect. But, it is noteworthy that the public prosecution often uses its power in the field of companies, as companies are linked to the public economic system.

4- Declaration of Bankruptcy by the Court Itself.

The court itself may declare the bankruptcy of a company. The legislator, however, came up with another option for the court, as defined in Article 702.

Pursuant to this Article, the court may, as a matter of course/on its own, or upon the request of the company, postpone looking into the declaration of its bankruptcy for a period not exceeding three months, in two cases:

Case 1: To prop its financial status

Only one possibility to prop the company's financial status is enough. It is not required that this financial status shall be supported, and the source of support does not matter. The company may have funds owned by third parties with approaching maturity dates, or a partner may be joining the company with a large amount of money, or many partners.

Among the events that could arise at work, the cessation of payment by companies to which the government entrusts works, due to delayed payment of dues. Therefore, it would not be desirable to declare the bankruptcy of such companies, as long as their dues would be settled.

Case 2: if this is necessary for the good of national economy

When, for example, the object of the company is to mainly contribute in building the country's economy or the company is the only to import a basic commodity to the country, or the company's capital is so huge that the declaration of its bankruptcy would affect the financial market.

Should the court consider postponing the declaration of bankruptcy, it may order to take whatever measures are necessary to preserve the company's assets.

Should the company consider postponing looking into the declaration of bankruptcy of the company for a period not exceeding three months, if it is possible to prop its financial status, or if this is necessary for the good of national economy. The text authorized it to take the measures it deems appropriate to preserve the company's assets so that the company would not smuggle its money or execute disposals that may harm the creditors. It may appoint a controller over the company to control its acts. It may also request a

periodic report on the company's works and acts from the legal representative of the company.

Chapter 2 Corporate Bankruptcy Impact

The bankruptcy of a company produces the same effect as that produced by the bankruptcy of an individual merchant. But this does not change the fact that companies enjoy some privacy, which distinguishes them from individual merchants in terms of bankruptcy impact. This privacy appears to be the consequence of the company enjoying legal personality and the existence of partners in the company as well as the presence of an administrative structure for such company.

Such privacy lies mainly in the impact of the declaration of bankruptcy of the company on its partners, and on its directors and board members, in addition to some other aspects of privacy that we will look into in the first section of the chapter under the title: "The General Impact of a Corporate Bankruptcy".

Hence, we will divide this chapter into two sections:

Section 1: The General Impact of Corporate Bankruptcy

Section 2: the Impact of a Company's Bankruptcy on the Partners

Section 1

The General Impact of Corporate Bankruptcy

We will approach the general impact of corporate bankruptcy as follows:

Subject 1: the impact of declaration of bankruptcy on the company itself

Subject 2: the impact of declaration of bankruptcy on the creditors

Subject 3: Corporate Bankruptcy Management

Subject 1

The impact of declaration of bankruptcy on the company itself

Upon issuance of the adjudication order, such order shall have effects similar to those of the declaration of bankruptcy of individual merchants, as the company shall be prevented from disposing of its property. Throughout the period of doubt, the company's disposals shall be unenforceable. In this regard, the general rules of bankruptcy shall apply. Therefore, we do not see the need to

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reiterate these general rules. But, we will point out the particulars related to corporate bankruptcy and will not approach the general rules.

Therefore, we will be discussing the following four points:

First: Does Bankruptcy Lead to the Termination of the Company?

This issue gave rise to doctrinal conflict:

Some⁽⁶⁸⁾ believed that the company's bankruptcy shall result in its termination. According to them, this cause is one of the general causes of termination of all companies, irrespective of their nature, i.e. stock companies or individual companies. And the bankruptcy of the company shall be considered as a reason to terminate it, as it serves as a proof that such company is no more able to handle its commercial liabilities. Also, the bankruptcy of a company shall result in its liquidation and the distribution of liquidation-resulting amounts among the creditors. In addition, bankruptcy of individual companies necessarily leads to the bankruptcy of joint partners, and hence the individual company shall be deemed to be terminated for this reason.

However, most believed the opposite to be true. Most scholars believe bankruptcy does not culminate in terminating the company, because the company may request composition and resume its activity. So, if such company shall be deemed as dissolved by reason of bankruptcy, it will become impossible to request composition. It is impossible to execute a contract with an entity that does not exist. Articles 709 and 710 of the New Commercial Law require composition to be reached with the company, so that the company shall continue to exist despite its bankruptcy.

This opinion did not give rise to issues with respect to stock companies. The real problem, however, might be felt more in individual companies, it is common knowledge that the bankruptcy of the company definitely leads to the bankruptcy of joint partners and that the bankruptcy of a partner in this type of companies leads to the dissolution of the company (Article 528, Civil Code). But this objection is rejected, because the pretext based on which the law requires the dissolution of the individual company upon the bankruptcy of the partner is that a company is based on mutual trust among partners. When such trust shall cease to exist, the company may collapse and shall thus be dissolved. Affluent partners cannot be compelled to continue to be part of the contract with

(68) Dr. Samiha Al Kalyoubi, *Commercial Companies*, Dar Al Nahda Al Arabeya, 2008,p. 146.

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a bankrupt partner. This pretext becomes invalid in case of bankruptcy of the company and the joint partners thereof. Therefore, it must be established that the company shall continue to exist despite the bankruptcy of the company and its partners, as the company may reach composition and may thus resume its activity. In such a case, the company shall continue to exist until the end of bankruptcy proceedings. If bankruptcy shall end with composition, the company shall be able to resume its activity. However, the company whose bankruptcy ends with the Union shall not be dissolved. However, this company may be dissolved if it transpires that the remainder of its assets after liquidating the Union is inadequate to follow up its works in a useful way⁽⁶⁹⁾.

We advocate this opinion, especially because it is consistent with Article 711 of the New Commercial Law which states as follows: “The company whose bankruptcy ends with the Union shall not be dissolved. However, this company may be dissolved if it transpires that the remainder of its assets after liquidating the Union is inadequate to follow up its works in a useful way”⁽⁷⁰⁾.

Second: The Personal Effects of Bankruptcy

Bankruptcy produces personal effects on bankrupt merchants, such as keeping the name of the bankrupt secret or preventing the bankrupt from leaving the country, in addition to depriving the bankrupt of some of the civil and political rights thereof. A bankrupt is deprived of the right to vote and to become a member of the parliament or local councils, chambers of commerce or industry or trade unions.

The first idea which reasonably comes to mind is that these effects apply to individual merchants, and there can be no way that such effects can apply to companies upon bankruptcy, as such companies possess legal personality⁽⁷¹⁾. However, the following must be taken into account:

- 1- The declaration of bankruptcy of a company shall lead to the declaration of bankruptcy of joint partners and silent partners who intervened in management works, and every person who performed trade works to his own advantage in the name of the company. Thus, the personal effects referred to above affect the persons who were

(69) For details, review Dr. Mohsen Shafiq op cit, p 1077, Dr. Mohamed Kamel Malsh, Companies' Encyclopedia, page 754. Prof. Dr. Abdul Rahman Kurman, op cit, p 490. Dr. Hany Sameer Abdul Razek, The Liability of Board Members in case of Bankruptcy, Doctorate Thesis, 2008, page 112.

(70). Dr. Abdul Rahman Kurman, Loc.cit.

(71) Dr. Mohsen Shafiq, op cit, p 1067.

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declared bankrupt following the declaration of bankruptcy of the company although they do not apply to the company itself.

- 2- Parag. 2 and 3 of Article 704 stipulate the following: “If it transpires that the company’s assets are inadequate to settle at least 20% of its debts, the court, upon the request of the bankruptcy judge, may decree that all or some of the board members or directors, jointly among themselves or severally, shall pay all or part of the company’s debt, unless they establish that they exerted in running the company’s affairs, some the discretion the caution and careful person does”.
- 3- The court, *motu proprio* or upon the demand of the bankruptcy judge, may pass a ruling decreeing the forfeiture of the rights prescribed in Article 588 of this law, of the company’s board members or directors who have committed serious errors leading to confusion of the company’s works and discontinuation of its payments.

Therefore, the board members and directors may be affected by the personal effects of the declaration of bankruptcy, without being declared bankrupt.

Third: Invalidity of Disposals during the Period of Doubt

The period of doubt is the period that runs from the date of cessation of payment through the date of issuance of adjudication order. Over this period, the merchant shall expect the issuance of the order. Some disposals may be inconsistent with the creditors’ rights. Therefore, the legislator has decided to question these disposals⁽⁷²⁾.

The legislator decided that some disposals shall not be executed, in accordance with Article 598. These are:

1. Donations
2. Extraordinary settlement: Settling the debts before their maturity date and settling undue debts at maturity date.
3. The guarantees of the previous debt.

(72) Concerning the details of this matter, we refer to the following general references: Dr. Wajih Jamil Khater, Theory of the period of doubt in bankruptcy, Doctorate thesis, Faculty of Law, University of Damascus, 1971, published in Beirut in 1973. Dr. Mohsen Shafiq, op cit, p 472.. Prof. Dr. Ali Jamal El Deen Awad, op cit, p 357. Dr. Ali Al Baroody and Dr. Mohamed Fareed Al Areeni, op cit, p. 281. Prof. Dr. Hussein Fathi, op cit, p 135.

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Also, Article 599 provided for non execution of all disposals by the bankrupt, other than those mentioned, except for the settlement of the value of commercial paper⁽⁷³⁾.

This applies to the bankruptcy of companies. No privacy shall apply unless with respect to the determination of the period of doubt. In cases where the bankruptcy of the company shall lead to the bankruptcy of some individuals such as joint partners or directors, the bankruptcy becomes diverse leading to a period of doubt for the company different from the one for individuals. With respect to companies, the period of doubt shall run from the date of the company's cessation of payment. With respect to individuals, however, the period of doubt shall start from the date of each individual's cessation of payment of the debts thereof, whether such debts pertain to the company or not.

Subject 2

The Impact of a Company's Bankruptcy on the Creditors

The declaration of bankruptcy of a company has effects similar to those of the declaration of bankruptcy of individual merchants. Creditors gather together into a group called "body of creditors". Individual claims and proceedings cease and the maturity dates of debts and interest enforcement shall cease in addition to many other effects referred to in the general references⁽⁷⁴⁾ written about the bankruptcy. Here, we will only discuss the particulars of impacts in case of corporate bankruptcy, through the following points:

First: Body of Creditors

In case of declaration of bankruptcy of a company, the creditors gather together to constitute the body of creditors, represented by the bankruptcy trustee. The same goes for the company, as its creditors gather to constitute a body of creditors. There does not seem to be a problem with respect to both joint stock companies and limited liability companies, where there will be one body of creditors. However, with respect to partnerships and the two types of commandite companies, bodies of creditors are many. For these companies to be declared bankrupt, all joint partners shall consequently be declared bankrupt. Therefore, for each bankruptcy case, there will be a body of creditors. The company's bankruptcy shall consist of its creditors only without the partners'

(73). Dr. Mohsen Shafiq, op cit, p 573.

(74) General rules of the bankruptcy's effects on the creditors: Dr. Saeed Mohamed Al Hayajna, The effect of the declaration of bankruptcy on the creditors body, Dar Al Nahda Al Arabeya, 1992. Dr. Ali Jamal Al Deen Awad, , op cit, p 271. Prof. Dr. Ali Al Baroody and Dr. Mohamed Fareed Al Areeni, op cit, p 312. Prof. Dr. Hussein Fathi, , op cit, p 101. Dr. Sherif Makram, , op cit, p 311.

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creditors. Thus, the partners' creditors shall not take part in the company's bankruptcy and in its debt settlement procedures. They may not also take part in the reconciliation body. However, the bankruptcy of every partner includes the company's creditors and the concerned partner's creditors. Therefore, all these creditors may claim their debts and their voted are to be taken into consideration in the reconciliation process.

If the company's bankruptcy ends with the union or reconciliation, its property shall be distributed among its creditors only. The partners' personal creditors shall not take part in such distribution process. However, in case of the bankruptcy of a partner, sale returns shall be distributed among the company's creditors and the partner's personal creditors equally, without giving privilege to the personal creditors over the company's creditors. Our legislative references contain no provisions concerning such privilege⁽⁷⁵⁾.

Second: Lawsuit and Individual Proceedings Cancellation

In case of the declaration of bankruptcy of a company, its creditors shall be prevented from initiating any lawsuits or individual proceedings. Collective proceedings shall replace individual claims. The trustee in bankruptcy shall represent the company and the body of creditors in initialing these collective proceedings. However, some actions require research to accurately determine the prohibited lawsuits and individual proceedings.

- 1- **Nullity Lawsuits:** it is common knowledge that each partner and creditor shall be entitled to claim nullity of company, in the case of presence of one of the objective or formal nullity causes. Thus, the creditors shall be entitled to request the nullity of the company whether prior to or after their bankruptcy. In such a case, the nullity lawsuit shall not be deemed as an individual action that creditors are prevented from filing. Where nullity order is rendered, the company shall be dissolved and no composition may be reached⁽⁷⁶⁾. In case the nullity of the company resulted in a liability claim to face its founders, the creditor may not claim compensation, unless a personal damage occurred. In this case, the creditor may individually turn to these founders to claim damage. However, in case of general damage, only the company's trustee in bankruptcy may initiate such claim.

(75) Dr. Mohsen Shafiq , op cit, p. 1091.

(76) For the contrary, review Dr. Mohsen Shafiq, Ibid p 1081.

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- 2- Liability Claims- the director or the Board members may commit an error that may cause damage to the company and its creditors. In this case, each shareholder may, in the individual capacity thereof, claim for damage from such directors or board member. But do creditors enjoy this right even in case of the declaration of bankruptcy of the company, or shall the liability claim be deemed to be an individual claim that creditors are prevented to file.

In the New Commercial Law, the legislator established special regulations regarding the liability of directors and board members in paragraphs 2 and 3 of Article 704, which state as follows:

2. “If it transpires that the company’s assets are inadequate to settle at least 20% of its debts, the court, upon the request of the bankruptcy judge, may decree that all or some of the board members or directors, jointly among themselves or severally, shall pay all or part of the company’s debt, unless they establish that they exerted in running the company’s affairs, some the discretion the caution any careful person does”.

3. “The court, *motu proprio* or upon the demand of the bankruptcy judge, may pass a ruling decreeing the forfeiture of the rights prescribed in Article 588 of this Law, of the company’s board members or directors who have committed serious errors leading to confusion of the company’s works and discontinuation of its payments”.

This text shows that the legislator has established special regulations to hold the directors and board members accountable for their errors. However, the implementation of these regulations depends on whether the text requirements have been satisfied. If these requirements are met, the only person who request to file liability claim is the bankruptcy judge, as provided for in the text. Therefore, no creditors may file this claim, in accordance with the said Article.

However, in case the rule enforcement requirements are not met, the same question will keep coming up: who shall be entitled to file this claim?

For our part, we distinguish between claims based on personal damage and those based on general damage to the company.

If such claim is based on a personal damage, the creditor shall not be prevented from filing a liability claim. The jurisprudence⁽⁷⁷⁾ gives an example

(77) Dr. Mohsen Shafiq, op cit, p. 1080

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like when the directors distribute bogus profits and third parties would think the company enjoys a strong financial position and would thus buy some of its shares at an elevated price or borrow the same. In this case the company shall not be entitled to file the claim, but rather the shareholder or the creditor who incurred such damage shall enjoy such right. Therefore, the company's trustee in bankruptcy has nothing to do with this. The shareholder, in his individual capacity, or the creditor may file such claim against the directors, especially that they may not be declared bankrupt along with the company. This applies in case damage arises as a consequence of the breach of the company's Articles of association by the directors.

If the claim shall be filed for the sole purpose of exercising the company's right, the creditor shall not be entitled to file such claim, but the bankruptcy trustee⁽⁷⁸⁾ shall enjoy such right instead. This claim represents the use of the company's right, but in case of the declaration of bankruptcy of the company, the creditor may not exercise such right, as it is recognized as one of the collective proceedings initiated by the bankruptcy trustee.

3- Lawsuit to claim the rest of the shares: a company may continue to exist, even if the rest of the shares were not recovered from the partners. In this case, each creditor may exercise the company's right to claim the rest of the shares from the partners. However, in case of bankruptcy of the company, the creditors may not exercise such right, as the company has been declared bankrupt and no one shall be entitled to claim the rest of the shares, except for the bankruptcy trustee who shall do so on behalf of the company and its creditors. But in this case, the bankruptcy judge may restrict the claim to the extent necessary for the settlement of debts.

In this context, Article 706 reads as follows: "The bankruptcy trustee, after getting permission from the bankruptcy judge, may require the partners to pay the rest of their shares in the capital though its payment has not matured yet. The bankruptcy judge may order that this requirement shall be restricted to the measure necessary for settlement of the company's debts."

Nevertheless, may the partner plead a limitation period or set off?

No doubt, a partner may act in accordance with the standard limitation period while standing up to the bankruptcy trustee. However, the problem lies in acting in accordance with the five-year limitation period in confronting the bankruptcy trustee, as set out in Article 65 of the New Commercial Law? It is

(78) Dr. Ali Jamal El Deen Awad, op cit, p. 661

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assumed that the company's declaration of bankruptcy took place after its dissolution and the partner did not grant the total shares thereof and five years have passed since the company was dissolved before the trustee claimed the rest of the shares from the partner.

May the partner act in accordance with the five-year limitation period? Most believe that the partner may not act in accordance with such period, as it is based on the assumption that the debts are settled to the creditors, and this assumption is denied by the bankruptcy of the company⁽⁷⁹⁾.

With respect to claiming a right to set off, if the partner shall incur debts in the name of the company, may such partner claim a right to set off? It is a known fact that set off cannot take place after declaration of bankruptcy. Therefore, a partner may not claim such right, unless the relevant requirements were met prior to bankruptcy.

Third: Debt Maturity Lapse

The company's debt shall lapse as soon as declared bankrupt. While bonds represent debts, such bonds shall become payable whatever their remaining period to maturity. According to rule, all debts shall lapse upon declaration of bankruptcy, whether their term is specified or not.

If the company shall be declared bankrupt prior to the redemption of total shares, and it was not time to grant the remaining shares, will such maturity lapse and may the trustee be thus entitled to claim the remaining shares from the partners upon bankruptcy? With respect to joint partners in joint-liability companies, limited partnerships and partnerships limited by shares, the bankruptcy of such partners shall be declared upon the declaration of bankruptcy of the company. And so, the debts owed thereby, including the rest of the shares that they undertook to provide, shall fall due. With respect to secret partners and shareholders, that is not the case. The French judicial authorities believe such maturity shall lapse and the trustee may be entitled to claim the rest of the shares as soon as the declaration of bankruptcy shall take place. Saying the opposite would lead to the disruption and complication of the bankruptcy process⁽⁸⁰⁾. Most of the jurisprudential views propose that maturity shall not lapse with respect to such partners, as their bankruptcy shall be

(79) Appeal 3 March 1937, Bull. 49 page 131., Chapter III No. 1660, referred to by Dr. Mohsen Shafiq, Bankruptcy, page 1084.

(80) French Cassation 25 October 1897, Dalloz 1897, Chapter I, page 575, and another judgment 31 May 1902, Dalloz 1902, Chapter I, page 331.

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declared together with the declaration of bankruptcy of the company. It would then be impossible to cancel the maturity date. What is more, the bankruptcy leads to the cancellation of the maturity date of the debts owed by the company and the bankruptcy proceedings do not take into account the company's entitlements.

Fourth: Cancellation of Interests

Debt interests imposed on the company shall be cancelled from the date of adjudication order. With respect to the company's entitlements, the relevant interests shall continue to remain enforceable. While the company shall be deemed to be acting as a creditor with respect to the shares that the partners undertook to grant, their interests shall be enforced as soon as the partner shall abstain from paying on the agreed upon date, whether such date shall fall prior to or after the declaration of bankruptcy. Interests shall come into force from the date of maturity of the share without the need for judicial claims or excuses (Article 510 Civil Code). Based on the foregoing, if we consider the maturity date upon declaration of bankruptcy, interests shall be enforced from the date of adjudication order. According to a different view, interests shall only become enforceable upon judicial claim or excuses. However, this view is not consistent with the provisions of Article 510 of the Civil Code.

Subject 3

Corporate Bankruptcy Management

In the process of management of the company's bankruptcy, the general rules shall mainly apply. We will only discuss two matters relevant to the bankruptcy of companies.

Verification of Company's Debts

The verification of the bankrupt company's debts shall be governed by the general rules. The legislator established in Article 707 of the New Commercial Law the following: "The loan bond as issued by the company shall not be subject to procedures of verifying debts. These bonds shall be accepted with their nominal value after deducting the portion the company had paid therefore".

The legislator did not want to consider the market value of these bonds, but its nominal value.

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If the payment of a bonus on settlement is stipulated, the bond shall be accepted with its nominal value, in addition to the portion maturing of the bonus until the court ruling on declaring the bankruptcy is passed.

The reason why the loan bonds issued by the company are not verified is that they are recorded by writing in the bonds themselves and in the company's budgets.

Representation of a Bankrupt Company

The bankrupt take part in the bankruptcy processes. The presence of the bankrupt is required to assist the bankruptcy trustee in providing him with information on the books and correspondence thereof as well as on the bankrupt's budget and creditors and the verification of debts and composition proposals.

Therefore, Article 705 stipulated the following: "The Legal representative of the company which is declared bankrupt shall represent it in all matter for which the law requires taking the bankrupt's view or his attendance. He shall attend before the bankruptcy judge or its trustee whenever he is asked, and to give any required information or explanations".

A legal representative shall mean the company's director, whether a partner or not. It shall not mean each partner, the liquidator, the company's receiver, the Board chairman, or joint partners, unless bankrupt. In this case, their presence is required in bankruptcy proceedings.

Section 2

The Impact of A Company's Bankruptcy on the Partners

When it comes to the impact of a company's bankruptcy on the partners, we can distinguish between two types of partners:

Type 1: Joint Partners

All partners in a joint-liability company are recognized as joint partners. Also, there are joint partners in both limited partnerships and partnerships limited by shares.

Type 2: Dormant Partners; Dormant partners shall mean all the partners in joint-stock companies and limited liability companies and secret partners in limited partners and shareholders in partnerships limited by shares.

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According to rule, the declaration of bankruptcy of the company shall lead to the declaration of bankruptcy of joint partners only.

However, this rule required detailed study to identify its limits and the mechanisms to implement it, as well as the relevant procedures.

Therefore, we will divide our study into two subjects:

Subject 1: the impact of a company's bankruptcy on joint partners

Subject 2: the impact of a company's bankruptcy on dormant partners

Subject 1

The impact of a company's bankruptcy on joint partners

The legal position of a joint partner is represented in its merchant capacity, and in the fact that such partner is responsible absolutely and jointly for the company's debts. Also, the company's discontinuation of payment of its debts⁽⁸¹⁾ shall ensue that the partner stopped payment of his debts. This would unquestionably and reasonably lead to the declaration of bankruptcy of all joint partners⁽⁸²⁾ in case of declaration of bankruptcy of the company.

In this context, Article 703 of the New Commercial Law stipulated the following: “

- 1- If the company is declared bankrupt, all joint partners thereof shall be declared bankrupt. This shall comprise declaring the bankruptcy of the joint partner who quit after the company discontinued its payments, if the request to declare the bankruptcy of the company is submitted before the lapse of one year from the date the partner in the commercial register quit the company.
- 2- The company shall pass a ruling in which it pronounces the company's declared bankruptcy together with the declaration of the bankruptcy of the joint partners even though it may not be concerned with declaring the bankruptcy of these partners.

(81) The legal status of the joint partner: see, Mohsen Shafiq, *Intermediate in the commercial Law*, Chapter I, 1st edition, 1951, page 400. Mohamed Kamel Malash, *Companies' Encyclopedia*, page 85. Mustafa Kamal Taha, *op cit*, p.259. Dr. Aktham Al Khawli, *Lebanese Comparative Commercial Law*, Chapter II, *Commercial Companies*, Beirut 1968, page 166. Abu Zeid Radwan, *Commercial Companies in the Egyptian Comparative Law*, page 238. Dr. Samiha Al Kalyoubi, *Commercial Companies Dar Al Nahda Al Arabeya*, 2008, page 288.

(82) This rule was refused by few people in the French jurisprudence. Review Puc, *Companies' Bankruptcy*, oage 20. Roubin de Couder, *Commercial and Industrial Law*, Marmande Commercial Court, 29 June 1939, *Dalloz*, 1939, page 476. Dr. Ali Jamal el Deen Awad, *op cit*, p. 735, margin (1). For details review Dr. Aziz Abdul Ameer Al Akili, *op cit*, p. 64.

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3- The court shall appoint for the bankruptcy of the company and the bankruptcies of the joint partners one judge and one trustee or more. However, each bankruptcy shall be independent from the others in terms of its assets and liabilities, and its management, the verification of its debts, as well as its termination.

This text reflects what doctrine and judicial authorities settled upon prior to the enactment of the New Commercial Law No. 17 of 1999.

We will examine the rule decided by the text in terms of its scope of implementation, and the resulting impact (plurality and independence of bankruptcies), as well as the procedures of the extension of the corporate bankruptcy to partners, through the following requirements.

First Requirement Scope of Implementation of the Rule (joint partners that can be declared bankrupt)

This rule applies to all joint partners of the company, whether in joint-liability companies or commandite companies. Also, the rule applies and the joint partner shall be declared bankrupt even where the matter relates to *de facto* company. Bankruptcy extends to joint partners, whether in a legal or *de facto* company⁽⁸³⁾, as laid down below.

In individual companies, partners are supposed to be joint partners, unless otherwise proven⁽⁸⁴⁾. This provision shall apply to joint partners, even if their names were not recognized in the company's memorandum of association, inasmuch as such partners are joint partners according to their real will⁽⁸⁵⁾.

A joint partner shall be declared bankrupt following the declaration of bankruptcy of the company, whether such partner was a director engaged in management affairs or not. If, however, the company's director shall be a foreign non-partner who is not responsible for its debts generally, such director does not acquire the merchant capacity and may not thus be declared bankrupt following the declaration of bankruptcy of the company⁽⁸⁶⁾.

(83) Dr. Mohsen Shafiq, Bankruptcy, page 1071. Dr. Ali Jamal El Deen Awad, Bankruptcy in the new commercial law, page 587.

(84) The court of appeal's judgment (11 February 1931, Bulletin, Y. 43, page 227). Dr. Ali Jamal El Deen Awad, Bankruptcy in the new commercial law, page 587.

(85) Cassation 28/03/1974 in the appeal No. 438 for the year 37, list of the cassation judgments, page 606.

(86) Appeal No. 303, S. 48, hearing of 1/12/1980, list of the cassation judgments, S. 28, page 1957. Appeal No. 86, S. 46, hearing of 10/3/1983, list of the cassation judgments, S. 31, page 765.

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In this case, however, he might be held responsible for the company's debts in some cases and under certain conditions, if it was established he did not exert due diligence in running the company's affairs. But, even in this case, he may not be declared bankrupt but may only be held responsible for the debts, as will be discussed later in the part devoted to the impact of a company's bankruptcy on the directors and board members.

Joint partners are absolutely and jointly liable for the company's debts. Therefore, they must settle the company's debts, if the company shall fail to pay its debts. Failure to do so, and in case of declaration of bankruptcy of the company, such partners shall be declared bankrupt, as the company's discontinuation of payment shall ensue that such partners have in turn stopped payment⁽⁸⁷⁾.

While the company's bankruptcy leads to the declaration of bankruptcy of the joint partners, but the declaration of bankruptcy of a partner shall not lead to the declaration of bankruptcy of the company. In fact, partners may discontinue payments but the company may remain able to pay. However, the declaration of bankruptcy of the partner shall lead to the dissolution of the company, unless the company's memorandum of association shall establish that the company shall continue to exist despite the bankruptcy of one of the partners, in accordance with Article 528 of the Civil Code⁽⁸⁸⁾.

For a joint partner to be declared bankrupt following the bankruptcy of the company, he shall be a partner at the time when the company shall discontinue payments. However, if he ceases to be a partner prior to the company's discontinuation of payment, he shall not be declared bankrupt.

Some believe that if the company was dissolved while it was still financially able to settle its debts, and then discontinued payments during liquidation and upon declaration of bankruptcy, such bankruptcy shall not extend to joint partners, as they have lost their capacity as merchants since the dissolution of the company, whether such dissolution took place according to legal situations or not. However, if dissolution took place while the company has already discontinued payment and was then declared bankrupt, the existing partners

(87) The joint partner is responsible for all the company's debts. Appeal No. 1350, Y. 52, hearing of 25/1/1981, edition 748, Y. 59, hearing 1/7/1996, Appeal 660 S. 41 hearing of 7/6/1976, Y. 27, page 1285. Cassation 16/11/1981, Y. 32, page 2037. Appeal 1350, Y. 52, hearing of 25/11/1988, appeal 182, Y 41, hearing of 16/19881, Y. 32, page 953, appeal 704, Y. 50, hearing of 13/5/1985, Y. 35, page 751, appeal 660, S. 41, hearing of 7/6/1976, Y. 27, page 1285. Cassation, hearing of 8/1/1984, Y. 35, page 151, S. 47, appeal 176, Y. 26, hearing 26/4/1962.

(88) For details, review. Dr. Mohsen Shafiq, Intermediate in Commercial Law, Chapter I, page 687.. Dr. Abu Zeid Radwan, op cit, p. 239. Prof. Dr. Samiha Al Kalyoubi, op cit, p. 214

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until dissolution shall be declared bankrupt. If cessation of payment took place when they still enjoyed the merchant capacity, they shall be regarded as merchants who quit trade business⁽⁸⁹⁾.

However, others believe the declaration of bankruptcy shall extend to joint partners if the company shall discontinue payment of its debts during liquidation phase. As the company maintains its legal personality and commercial capacity during liquidation and is held accountable for its debts, partners also maintain their capacity as merchants during liquidation and shall thus be held accountable for the company's debts. Therefore, they shall be declared bankrupt upon the declaration of bankruptcy of the company, if the latter shall discontinue payment of its debts and they shall not proceed to settle such debts⁽⁹⁰⁾.

Time Scale of Declaration of Bankruptcy of Joint Partners

According to rule, it is resolved that, for a joint partner to be declared bankrupt following the declaration of bankruptcy of the company, such partner shall enjoy the capacity of joint partner on the date of adjudication order. Here, we must interrogate the status of the retiring partner, incoming partner, and transferor partner and whether they are responsible for the company's debts, and may be declared bankrupt following the declaration of bankruptcy of the company. We will approach this matter below: -

First: Liability of Retiring Partner

If a joint partner shall retire from the company⁽⁹¹⁾, he shall be liable for the debts incurred prior to the retirement thereof. with respect to debts incurred after his retirement, he shall not be held accountable for the same, on two conditions:

- 1- His name shall be deleted from the company's address
- 2- His retirement shall be recorded in the commercial register⁽⁹²⁾

Failure to meet any of these two conditions, the partner shall remain liable for all the company's debts, whether incurred prior to or after his retirement.

(89) Appeal 20 April 1927, Bull. 39, page 397. Dr. Mohsen Shafiq, Bankruptcy, page 1072. Prof. Dr. Mohamed Samy Madkour and. Dr. Ali Hassan Younes, Bankruptcy, page 573.

(90). Dr. Aziz Abdul Ameer Al Akili, Legal Difficulties arising from the Bankruptcy of the companies, page 62. Dr. Reda Al Sayed Abdul Hameed, the effect of the company's bankruptcy on the partners, page 65.

(91) For details concerning the withdrawal from the company and its effects, please review Prof. Dr. Mustafa Kamal Taha, op cit, p. 294. Prof. Dr. Tharwat Abdel Raheem, op cit, p. 407. Dr. Mohamed Fareed Al Areeni, op cit, p. 73.

(92) Prof. Dr. Mohamed Fareed Al Areeni, op cit, p. 109.

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With respect to the declaration of his bankruptcy following the declaration of bankruptcy of the company, an Article stipulated as follows: “If the company is declared bankrupt, all joint partners thereof shall be declared bankrupt. This shall comprise declaring the bankruptcy of the joint partner who quit after the company discontinued its payments, if the request to declare the bankruptcy of the company is submitted before the lapse of one year from the date the partner in the commercial register quit the company.

Therefore, in order to declare bankruptcy, two conditions shall be met: the company must have discontinued payment before the partner has quit the company and the bankruptcy of the company shall be declared within one year from the date the partner quit the company in the commercial register.

Failure to announce that the partner quit the company; he shall be considered responsible if it was requested to declare the bankruptcy of the company despite the fact that he quit it. However if it is recognized in the commercial register that he quit the company and one year passed since then, the partner may not be declared bankrupt following the declaration of bankruptcy of the company, even when it comes to debts arising when the partner was still in the company, and even if the company discontinued payments prior to the date he quit the company.

This shall not mean that the partner shall not be held responsible for these debts, but rather he will remain liable for such debts as long as the five year limitation period did not pass. However, such liability shall not result in the declaration of his bankruptcy as a consequence of the declaration of bankruptcy of the company, but the debts shall be collected from the same through seizure and execution. he may only be declared bankrupt if he possesses commercial capacity despite quitting the company. In this case, he shall be independently be declared bankrupt and not as a result of the declaration of bankruptcy of the company,

Second: Liability of Incoming Partner

According to jurisprudence⁽⁹³⁾, the incoming partner shall be liable for all the company’s debts whether incurred after or prior to joining the company, unless he shall resolve that he shall not be responsible for previous debts and announce the same upon joining the company. Accordingly, he may be declared bankrupt. This is so because upon joining the company, he shall be aware of its debts and

(93) Dr. Mohsen Shafiq, op cit, clause 408. Dr. Mustafa Kamal Taha, op cit, p. 265, Prof. Dr. Tharwat Abdul Raheem, op cit, p.430. Dr. Samiha Al Kalyoubi, op cit, p.287. Dr. Mohamed Fareed Al Areeni, op cit, p.109.

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as long as he accepted to join the company, he accepted his debts as well, unless he declared that he is not responsible for such debts, and this shall not affect the rights of the creditors, as they did not consider the presence of this partners in the first place.

Third: Liability of Transferor Partner

If a joint partner shall transfer the share thereof to another person and such transfer was authorized, the transferee shall be subject to the provisions pertaining to incoming partners.

With respect to the transferor, he shall not be held accountable for the debts incurred after such transfer occurred. As regarded to debts incurred prior to share transfer, he shall be governed by the provisions related to retiring partners.

That is to say that the transfer of a share shall not result, according to the prevailing jurisprudential view⁽⁹⁴⁾, in transferring the company's debts to the transferee, as creditors shall approve the transfer of debt to third parties.

Second Requirement Rule Implementation Impact (Plurality and Independence of Bankruptcies)

Article 703/3 of the New Commercial Law stipulates the following: "The court shall appoint for the bankruptcy of the company and the bankruptcies of the joint partners one judge and one trustee or more. However, each bankruptcy shall be independent from the others in terms of its assets and liabilities, and its management, the verification of its debts, as well as its termination

Pursuant to this Article, if the joint partners shall be declared bankrupt following the declaration of bankruptcy of the company, it shall be a matter of multiple bankruptcies and each bankruptcy case shall be independent of the other.

Thus, each bankruptcy shall be independent from the others in terms of its composition, the creditors' rights and its future. Such independence can be summed up as follows:

1. One judge and one trustee or more shall be appointed for each bankruptcy, at the sole discretion of the court

(94) Dr. Mohsen Shafiq, op cit, clause 313. Dr. Mohamed Fareed Al Areeni, op cit, p. 110.

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2. Each bankruptcy shall be independent from the others in terms of its assets and liabilities. The company's bankruptcy assets shall comprise its capital consisting of the total shares granted by the partners. With respect to the bankruptcy of partners, however, the assets shall comprise the partner's own property and exclude the share value thereof in the company, as the ownership thereof shall be transferred to the latter, unless such share was granted to the company as usufruct. The partner's bankruptcy liabilities shall comprise the personal creditors' debts and the debts of the company's creditors. They all take part in the bankruptcy equally. And so, the company's creditors shall be able to claim their debts in all bankruptcies⁽⁹⁵⁾. However, when it comes to the personal creditors of each partner, they shall only be entitled to participate in such partner's bankruptcy⁽⁹⁶⁾.
3. If the company bankruptcy comes to an end with Union, and composition was reached with one or more joint partners, the company's property may not be allocated to satisfy the conditions of such composition or to ensure the implementation thereof. The partner who reached composition shall be released from any liability (Article 710/1)
4. If composition is reached with the company and the joint partners' bankruptcies came to an end through Union, the company shall continue to exist, unless the subject involved in composition issues is for the company to forsake all the property (Article 710/2).

Third Requirement

Company Bankruptcy Extension to Joint Partners

In light of the cancelled codification, there were no detailed rules pertaining to corporate bankruptcy. The court of cassation settled upon a number of principles concerning the extension of a company bankruptcy to joint partners. The court ruled as follows: "the bankruptcy of the company shall definitely lead to the bankruptcy of the joint partner even if not engaged in the relevant lawsuit. A partner in a joint-liability company or a joint partner in a limited partnership shall be held accountable for the company's debts even if the debt, subject-matter of the claim, is considered a debt for the company solely⁽⁹⁷⁾."

(95) Dr. Mohamed Saleh, op cit, p.337.

(96) Dr. Reda Al Sayed Abdul Hameed, op cit, p. 73

(97) Cassation 16 December 1996, Appeal No. 3392 for the year 59, S. 84, page 1561. Cassation 6 February No. 471 for the year 46, S. 88, page 450.

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Here, the court of cassation does not require the joint partner to be a litigant in the company bankruptcy claim, but he shall be declared bankrupt following the declaration of its bankruptcy even if he were not engaged in the bankruptcy claim.

In this context, the court of cassation ruled that “if the ruling rendered for the company bankruptcy shall neglect the text of declaration of bankruptcy of joint partners or the announcement of their names, this shall not result in excluding them from bankruptcy. The company bankruptcy shall definitely lead to the declaration of their bankruptcy. Joint partners are responsible with respect to their own property for the company’s debts. If the company shall discontinue payment, this means that such joint partners have also discontinued payment⁽⁹⁸⁾.”

The principles decided upon by the court of cassation in light of the cancelled codification became void after the enactment of the New Commercial Law. This law established strict procedural regulations with respect to the extension of bankruptcy of a joint-liability company to joint partners.

These regulations represent three procedural rules:

- 1- The initiatory pleading shall comprise the names of current joint partners and those who quit after it discontinued the payments, together with an indication of the domicile of each joint partner, his nationality, the date/month in which he quit, in the commercial register. (Article 700/3).
- 2- If the creditor requests declaring the company bankrupt, all joint partners shall be litigated against (Article 701/2)

Some⁽⁹⁹⁾ note that this Article has reduced the liability of the partners to the bankruptcy declaration request through the creditor. Hence the question arises about the validity of this liability in case of a request by the public prosecution to declare the bankruptcy of the company, or if the court itself shall declare the bankruptcy of the company, or the company itself shall file for bankruptcy.

- 3- The court shall pass a ruling in which it pronounces the company’s declared bankruptcy together with the declaration of the bankruptcy of the joint partners even though it may not be concerned with declaring the bankruptcy of these partners (Article 703/2).

(98) Cassation 7 March 1972, list of the cassation judgments, year 23, Y. 49, page 311. Cassation 7/6/1976, appeal No. 66 for the year 41, S. 37, page 1285.

(99) Dr. Reda Al Sayed Abdul Hameed, op cit, p. 50

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Following the enactment of the New Commercial Law, the court of cassation expressed the change brought by this law, by stating: “ pursuant to Articles 699/1, 700/3, 701/2 and 703 of the New Commercial Law No. 17 of 1999, while the legislator, has established that all joint partners of a company shall be declared abrupt following the declaration of bankruptcy of the company, as settled upon by the court of cassation, but the legislator provided that bankruptcy claims pertaining to joint-liability companies and limited partnerships require, as prescribed by law, certain persons to be litigated against, i.e. the joint partners in all the phases of examination of the claim . this aims at pushing these partners to promptly proceed to settled the company’s debts for fear of declaring their bankruptcy by virtue of the company adjudication order. In doing so, this would ensure the settlement of the company creditors’ liabilities and limit such kind of bankruptcies and the resulting impact on the country’s economy and trade. It was thus required that the initiatory pleading shall comprise the names of such joint partners, i.e. the existing joint partners and those who quit the company after its discontinuation of payment, otherwise the court itself would have been authorized to order their engagement and render one ruling in which it pronounces the company’s declared bankruptcy together with the declaration of the bankruptcy of the joint partners. This shall comprise declaring the bankruptcy of the joint partner who quit after the company discontinued its payments, if the request to declare the bankruptcy of the company is submitted before the lapse of one year from the date the partner in the commercial register quit the company.

This principle requiring the engagement of the said partners in litigation applies throughout all phases of case examination, and all degrees of litigation, including the appeal phase. The ruling rendered in this case shall be indivisible, without taking into account that the failure of one of the convicted in bankruptcy to appeal the ruling shall be deemed as acceptance on his part. All partners shall be litigated against before the court of appeal until a final decision is reached. If the appellant shall fail to contest against any of them intentionally or by negligence, the court shall order such litigation to take place, so that the appeal shall be confirmed. If the contested judgment shall advocate the ruling of the court of first instance in which it pronounced the company’s declared bankruptcy together with the declaration of the bankruptcy of the joint partners, including the first three plaintiffs in their capacity as joint partners, such judgment shall be deemed to be inconsistent with the law, which requires its reversal without the need to examine the rest of appeal reasons⁽¹⁰⁰⁾.

(100) Appeal No. 258 for the year 78, hearing of 9/2/2009 .

Subject 2

The impact of a company's bankruptcy on dormant partners

Rule and Exception

Dormant partners shall mean secret partners in limited partnerships and partnerships limited by shares, and partners in limited liability companies and shareholders in joint-stock companies.

According to rule, the bankruptcy of the company shall not affect these partners; as such partners have limited liability and shall thus only be held accountable for the company's debts to the extent of the shares granted thereby. The company's discontinuation of payment shall not mean that such partners shall be deemed to have discontinued payment of these debts.

In order for limited liability partners not to be affected by the declaration of bankruptcy of the company, such partners shall comply with the legal provisions pertaining to such companies, especially the rules pertaining to informing others of the limited liability thereof, and that they are not liable for the company's debts exceeding the value of shares thereof in the company's capital. Failure to do so, such partners shall be declared bankrupt⁽¹⁰¹⁾. This bankruptcy shall affect their property and their person. The same goes for a secret partner who participates in the company management and whose name is recognized in the company's address, in addition to the person who performs trade activities to his own advantage in the name of the company and disposes of the company's properties, as though they were the own property thereof.

According to rule, dormant partners shall not be declared bankrupt following the declaration of bankruptcy of the partners. Exception thereto pertains to secret partners.

This rule is clear. The exception, however, shall be discussed as the following:

According to rule, the secret partner's liability shall be limited to the share granted thereby to the company. Such partner shall not acquire the merchant capacity upon joining the company and his liability does not extend to include his personal assets. Hence, such partner shall not be declared bankrupt if the company is declared bankrupt.

However, a secret partner may be declared bankrupt in two cases:

(101) Dr. Aziz Abdul Ameer Al Akili, op cit, p. 77

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First: If his name is recognized in the company's address

The legislator does not authorize the name of one of the secret partners to be included in the company's address. Such address shall rather comprise the names of the joint partners, or the name of one or more of them, together with the expression: "and the associates thereof". This aims at protecting third parties dealing with the company, so that third parties shall become aware of the status of the secret partner whose name is recognized in the company's address. in such a way as no one would confuse such partner for a joint partner⁽¹⁰²⁾.

If the secret partner shall fail to do so and accept that his name be included in the company's address or become aware of this and not object thereto, he shall become liable towards third parties for all the company's debts, as though he were a joint partner, when such third parties have good faith, i.e. they ignore he is a secret partner.

However, including the name of the secret partner in the company's address does not change the real legal status thereof with respect to the partners. In other words, he shall remain a secret partner to them. He shall be entitled to proceed to them if he shall be required to pay third parties the company's debts and such debts exceed the value of the share thereof in the company's capital.

If the name of the secret partner is included in the company's address without such partner's knowledge or despite his objection, the liability thereof towards third parties shall remain limited to the value of the share thereof. He shall be responsible for proving his ignorance of such occurrence or that he took the required measures to remove his name from the company's address, e.g. through publishing a statement in newspapers in which he corrected the address and submitting a petition to the commercial register to remove his name from the company's address. He may also claim damage incurred as a result of the misuse of his name, if it is established that the partners' intention was to create a bogus company credit and such act shall be recognized as a criminally punishable embezzlement⁽¹⁰³⁾.

Most believe that the secret partner who shall accept his name to be included in the company's address shall acquire the merchant capacity. He shall thus be recognized as a joint partner and may be declared bankrupt upon the declaration of bankruptcy of the company.

(102) Dr. Mustafa Kamal Taha, op cit, p. 312. Prof. Dr. Tharwat Abdel Raheem, op cit, p. 468. Dr. Mohamed Fareed Al Areeni, op cit, p. 134.

(103) Dr. Aziz Abdul Ameer Al Akili, op cit, p. 84

Second: Intervention of the Secret Partner in the External Management Works

The legislator established provisions pertaining to the management of limited partnerships and partnerships limited by shares in such a way as to adapt to the extent possible the interests of joint partners accountable for the company's debts and covenants and those of the secret partners who shall only be held accountable for company's debts to the extent of the value of their shares in the company. He thus authorized the joint partners to engage in the actual management of the company and granted the secret partners the right of control and supervision. That being so, a secret partner may not intervene in the management of the company, in order to protect the joint partners from the secret partners' eagerness to manage the company with a view to identify their liabilities from the company's debts. They thus enter into unstudied speculations that cause the company enormous losses. This also aims at protecting third parties dealing with the company, while believing that the persons who are responsible for the management are joint partners accountable for the company's debts. It later turns out that such person is a secret partner who shall not be held accountable for the company's debt except to the extent of the share thereof. For others to avoid such error, and in order to protect the joint partners, the legislator prohibited the secret partner from intervening in management works.

Failure to do so, such partner shall be personally and jointly liable along with the joint partners, for the debt arising out of the work performed in the name of the company. Given the work performed to the advantage of the company, such partner shall be regarded as similar to a joint partner. Therefore, if the joint-liability company shall be declared bankrupt by reason of cessation of payment of its debts and the court saw that the secret partner intervened in the external management works, the impact of the bankruptcy shall extend to such partner and such partner shall thus be compelled to settle the debts incurred as a result of such works performed jointly with the company and the joint partners, even though such debts may exceed the value of the share thereof in the company's capital.

However, such partner may not be regarded as a joint partner enjoying merchant capacity and may not be declared bankrupt upon the declaration of bankruptcy of the company.

If the secret partner intervened frequently in the external management works, such partner may be regarded as a joint partner. He shall thus be held

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jointly and absolutely accountable for all or part of the company's debts, depending on the occurrence of these works.

That is left to the discretion of the court. If the court shall consider that the works performed by the secret partner are of great significance or too dangerous that they may cause third parties to believe that such partner has an unlimited liability, the court may hold him responsible for all the company's debts, even though such debts may not result from the management works he performed.

If the secret partner shall be held personally and jointly responsible for all or part of the company's debts, he shall then acquire the merchant capacity, according to the prevailing opinion. He may not be declared bankrupt upon the declaration of bankruptcy of the company, if the works he performed are sufficiently enough to form the proficiency term required by legislator to acquire the merchant capacity.

Some believe that the secret partner acquires the merchant capacity, at the sole discretion of the court. This is so because the partner shall be deemed to have performed commercial works of sufficient significance to be recognized as a merchant by third parties.

While a secret partner shall be regarded as joint partner if he performed external management works, but this does not change the fact that he acts as a secret partner in his relationships with the rest of the partners. He may thus proceed to them to claim the amounts he paid in excess of the share thereof in the company as a result of performing the external management works, if he performed such works upon their request.

However, if he performed the management works without having received a request from the partners, his works shall not be binding upon the company and the rest of the partners shall not be liable for such works. Such partner shall be personally held accountable for his works. Nevertheless, the secret partner may claim the amounts paid in excess of the share value thereof from the joint partners, whenever such works shall inure to the benefit of the company, in accordance with the general rules. Such partners' claims shall be reduced to the extent of benefits to the company⁽¹⁰⁴⁾.

(104) Dr. Aziz Abdul Ameer Al Akili, op cit, p. 81

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Conclusion

In the light of the companies' role in the commercial life nowadays, no one can deny that corporate bankruptcy has become of a high importance. This is basically because of the role of a trading corporation which is far more significant than that performed by individual merchants in the business field; in addition to that, corporation bankruptcy has the most dangerous effect on national economy and the greatest influence on trade credit. In this study, we emphasize the privacy of corporate bankruptcy rules by showing the rules governing this subject under the Egyptian Law.

The study is divided into two chapters, the first chapter dealt with the requirements of declaration of corporate bankruptcy, while the second chapter dealt with the impact of corporate bankruptcy.

We presented in the first chapter the different requirements to declare the corporate bankruptcy, whether objective or formal, in particular, the commercial capacity of a company, the legal personality of a company, cessation of payment, the issuance of adjudication order, the capital requirement and issuance of adjudication order.

In the second chapter, we presented the impact of corporate bankruptcy, by studying in the first section the general impact of corporate bankruptcy on the company itself and on the creditors, and studying the impact of a company's bankruptcy on the partners in the second section.

Generally, we may conclude the following:

- Pursuant to the Egyptian Law, bankruptcy is recognized as a legal system pertaining to merchants, whether individuals or trade firms. In the New Commercial Law, the legislator should have disregarded such differentiation between civil and commercial persons. Instead, the legislator should have established regulations pertaining to the liquidation of troubled enterprises whether they acquired commercial or civil capacity.
- As firms acquire legal personality, they start to act independently of their partners, as well as of their directors and representatives. It is therefore logical to establish that once a company stops paying its debts, it shall be declared bankrupt. That is to say that claim in bankruptcy targets the company itself, and not its partners or representatives.

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- The actual or factual existence of the invalid company during the period prior to the invalidation order. Thus, such company possesses legal personality during such period and can thus declare bankruptcy.
- Material cessation of payment is not enough for a company to be declared bankrupt. Such cessation of payment should rather result from such company's deteriorating financial position. Where a company shall resort to using unlawful means to settle such dues, with a view to delay the material cessation of payment, e.g. a company may not be declared bankrupt if it sells goods or assets at trifling prices, as long as such company has not materially stopped paying its debts.
- A company may be declared bankrupt after termination, if the following two conditions are met, i.e. such company shall stop payment prior to termination, and filing for bankruptcy shall be made within one year from the date of termination.
- A company may be declared bankrupt during the liquidation process, whether it shall discontinue payment prior to its termination or during the liquidation process.
- Regarding transformed companies, in instances where a company shall preserve its legal personality, it shall be held accountable for the debts it has stopped to pay in its previous form, and hence it may be declared bankrupt due to these debts.
- Economic courts are the only competent courts for declaration of bankruptcy and preventive composition. These courts also have jurisdiction over bankruptcy-related conflicts. The circuit court where the head office of a company is located shall have jurisdiction to declare the bankruptcy of a company.
- A company may be declared bankrupt upon the request of its representative, one of its creditors, the public prosecution or the court itself.
- Bankruptcy does not culminate in terminating the company, because the company may request composition and resume its activity. So, if such company shall be deemed as dissolved by reason of bankruptcy, it will become impossible to request composition.

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- The declaration of bankruptcy of a company shall lead to the declaration of bankruptcy of joint partners and silent partners who intervened in management works, and every person who performed trade works to his own advantage in the name of the company.
- With respect to companies, the period of doubt shall run from the date of the company's cessation of payment. With respect to individuals, however, the period of doubt shall start from the date of each individual's cessation of payment of the debts thereof, whether such debts pertain to the company or not.
- If the company's bankruptcy ends with the Union or reconciliation, its property shall be distributed among its creditors only. The partners' personal creditors shall not take part in such distribution process.
- In general, in case of the declaration of bankruptcy of a company, its creditors shall be prevented from initiating any lawsuits or individual proceedings. Collective proceedings shall replace individual claims. The trustee in bankruptcy shall represent the company and the body of creditors in initialing these collective proceedings.
- Debt interests imposed on the company shall be cancelled from the date of adjudication order. With respect to the company's entitlements, the relevant interests shall continue to remain enforceable.
- A joint partner shall be declared bankrupt following the declaration of bankruptcy of the company, whether such partner was a director engaged in management affairs or not. However, the declaration of bankruptcy of a partner shall not lead to the declaration of bankruptcy of the company. In fact, partners may discontinue payments but the company may remain able to pay.
- If the joint partners shall be declared bankrupt following the declaration of bankruptcy of the company, it shall be a matter of multiple bankruptcies and each bankruptcy case shall be independent of the other.
- According to rule, dormant partners shall not be declared bankrupt following the declaration of bankruptcy of the partners, unless his name is recognized in the company's address or he intervened in the external management works.

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شروط وآثار افلاس الشركات في القانون المصري

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أستاذ القانون التجاري والبحري المشارك
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لما كانت الشركات التجارية تتمتع بالشخصية الاعتبارية، شأنها في ذلك شأن الأشخاص الطبيعية، فإنها تخضع لذات النظام القانوني الذي يخضع له التجار الأفراد، ومن ثم يجوز شهر إفلاسها إذا ما توقفت عن دفع ديونها التجارية.

ورغم أهمية أحكام الإفلاس بوجه عام، إلا أن موضوع افلاس الشركات لم يحظ مع ذلك بالاهتمام الذي كان يجب أن يناله، ومن هنا جاءت هذه الدراسة، والتي حاولنا من خلالها تسليط الضوء على بعض الأمور الهامة ذات الصلة بهذا الموضوع، حيث تناولنا على وجه الخصوص شروط شهر افلاس الشركات والآثار المترتبة على ذلك الإشهار، وذلك في إطار معالجة القانون المصري لهذا الموضوع.

وبناء على ذلك قسمنا الدراسة الى بايين، تعرضنا في أولهما الى شروط شهر افلاس الشركة، وقسمنا تلك الشروط الى شروط موضوعية وأخرى شكلية، وتناولنا كلاً منها تفصيلاً، كل في فصل مستقل.

بينما تناولنا في الباب الثاني آثار إفلاس الشركة، وذلك سواء الآثار العامة لشهر الافلاس أو أثر إفلاس الشركاء بالنسبة للشركاء، حيث خصصنا لكل من هذه الآثار فصلاً مستقلاً ضمن هذا الباب.