

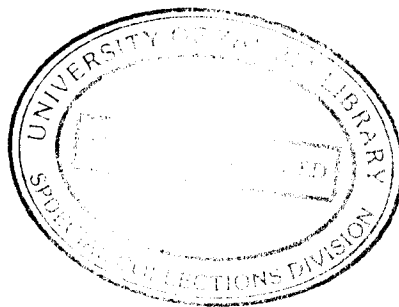
**THE PLACE OF MINISTERIAL STATEMENTS AND DIRECTIVES IN THE
MANAGEMENT OF STATE OWNED ENTREPRISES**

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Being a Directed Research essay submitted to the University of Zambia Law Faculty in Partial
fulfillment of the requirements for the Award of the Bachelor of Laws (LLB) Degree.

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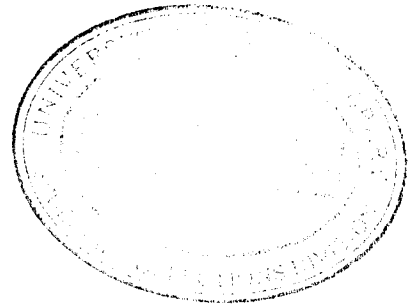
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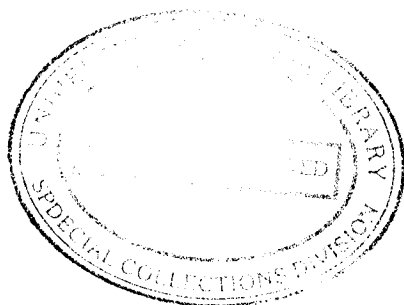
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ABSTRACT

In the governance of the affairs of the nation, Governments of the world pursue different economic policies with regards to sustaining the development of their respective countries. One such economic policy is establishment of SOEs. This paper has established that in Zambia SOEs are a feature of the post independence period and are incorporated under the Companies Act, Chapter 388 of the Laws of Zambia. As such the expectation is that they should run in accordance with the provisions of the Companies Act and the general principles of company law. However, the Government has in some instances issued various Ministerial statements and directives in the management of these SOEs. The purpose of this research is to ascertain the place of these Ministerial statements and directives in the management of SOEs. The first chapter introduces the concept of SOEs and briefly explains the historical background to the creation of SOEs bringing the problem into perspective. The next chapter highlights the issue of separate corporate personality in SOEs. It also addresses the issue of corporate governance in SOEs and argues that the interference by the State in the management of SOEs in the form of directives and statements is largely due to lack of good corporate governance in these enterprises. The Third Chapter explains the legal validity of these Ministerial statements and directives in the management of SOEs. In this regard, the case of *Edgar Hamuwele and Another v. Ngenda Sipalo and Another* is analysed to discuss the effects of a Ministerial statement purporting to dissolve a State Owned Company incorporated under the Companies Act. The last chapter sums up the findings of the place of Ministerial statements and directives in the management of SOEs. It goes further to outline some recommendations which can minimise the interference by the State in the management of parastatals. These include the incorporation of the OECD Guidelines on corporate governance in parastatals among others.

V

DEDICATION

To the memory of my late mother and father. I wish you were both here to see how far I have come. Even in death, you will always be in my heart and I will always love you.

ACKNOWLEDGEMENTS

First and foremost, I thank the Almighty God for the mercy and love that he has shown to me in my life.

To my Supervisor Mr Malila SC, I wish to express my sincerest gratitude for the patience and the guidance that you showed to me while doing this paper. You took time from your busy schedule and ensured that my writings had some direction. I thank you for that.

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Auntie Maureen, thank you for being there for me always. In the many hurdles that I have faced in life, you have always taught me to trust in God, believe in myself and be strong. You have been both a mother and a father to me and you have given me all the love, care and support that a parent will ever give to a child. You are the rock of my life and I will always love you.

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Yenda Shamabobo, thank you for loving me and always being there for me. You have supported me tirelessly and helped a lot in undertaking this research. You taught me not to give up even when I felt like giving. I thank God for giving me you in my life.

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CHAPTER ONE

STATE OWNED ENTERPRISES

1.1 Introduction

In the governance of the affairs of the nation, Governments of the world pursue different economic policies with regards to sustaining the development of their respective countries. One such economic policy is establishment of State owned enterprises or corporations. A State owned enterprise is synonymous with terms such as Government-owned corporation, State-owned entity, State owned company, publicly-owned corporation, Government business enterprise, or parastatal.¹

For purposes of this work, a State owned enterprise is a legal entity created by a Government to undertake commercial activities on behalf of an owner Government. Their legal status varies from being a part of Government to stock companies with a State as a regular stockholder. There is no standard definition of a Government-owned corporation (GOC) or State-owned enterprise (SOE), although the two terms can be used interchangeably. The defining characteristics are that they have a distinct legal form and they are established to operate in commercial affairs. While they may also have public policy objectives, GOCs should be differentiated from other forms of Government agencies or State entities established to pursue purely non-financial objectives that have no need or goal of satisfying the shareholders with return on their investment through price increase or dividends.²

¹ Anonymous, "Corporate Law," www.wikipedia.com(accessed October 11, 2011)

² Anonymous, "Corporate Law," www.wikipedia.com(accessed October 11, 2011)

The various forms of SOEs are made up of purely commercial companies set up under the Companies Act³ and entities set up under statute also known as parastatal boards, or corporations. A statutory corporation or organisation is defined as an artificial legal personality created under the statute of a particular country and whose objectives, structure, appointment of the board, dissolution or winding up are found in the enabling statute. The law applicable to statutory corporations in Zambia is specifically the enabling legislation and not the Companies Act as with other firms or corporations. Examples of statutory organisations in Zambia include the Zambia Revenue Authority (ZRA) created under the Zambia Revenue Authority Act⁴ and the Energy Regulation Board created under the Energy Regulation Act⁵. The rationale for development of statutory corporations has been advanced as being the need for Government to decentralize and ease the task of service delivery by creating bodies that are not entangled in the huge and bureaucratic government machinery. In addition these bodies may also be created for the regulation of certain critical sectors of the economy such as energy and revenue collection.⁶

The other forms of State enterprises in Zambia are SOEs incorporated under the Companies Act. The State owned companies are a feature of the immediate post independence economic reforms and they were introduced as a means of promoting Zambian entrepreneurship and extend to the Government of Zambia active participation in the economic sector, as well as give it control over industries which provided essential commodities, and which would be too risky for the country and for the poor if left in private hands. It is for the same reason that the British Government

³Chapter 388 of the Laws of Zambia.

⁴Chapter 321 of the Laws of Zambia.

⁵Chapter 436 of the Laws of Zambia as amended in 2003.

⁶E Kaunga, "Privatisation: The Zambian Experience" (July 1986) : 1-3

showed social responsibility by monopolizing British Rail, Gas Corporation, British Steel, and Posts and Telecommunications. In the case of gas for instance, almost everyone in England uses it for heating and cooking. It would be dangerous to leave it in the hands of private entrepreneurs, one of the dangers being that the commodity could be pegged at a price beyond which an average person can afford. This could result in many people dying from the cold.⁷

However, the creation of these parastatals has not been free from confusion and disregard of the law governing them. Successive Governments have at large interfered with the management of SOEs by not adhering to the law that regulates companies in the country, that is, the Companies Act, Chapter 388 of the Laws of Zambia. This interference has been in the form of Ministerial statements and directives. For instance during Kenneth Kaunda's tenure, the Government could make any pronouncements over the management of SOEs which were effected without due regard to the fact that a State owned company is incorporated under the Companies Act and as such should be regulated in accordance with the provisions of the Act. An illustration of this confusion was seen in the case of *NAMBORD v. National Milling Company Ltd*⁸ where judgment on a debt was given in favour of National Milling Corporation against NAMBORD. In the process of execution of a writ of *fifa* by National Milling Company, Kaunda then President issued a directive that the execution should be aborted because SOEs cannot sue each other.

Similarly in the case of *Edgar Hamuwele and Another v Ngenda Sipalo and Another*,⁹ the learned trial judge misdirected himself when he held that the Ministerial statement given in Parliament to place Lima Bank, an SOE, incorporated under the Companies Act in receivership was legally valid as to invalidate the subsequent resolve by its shareholders to place it in

⁷ E Kaunga, "Privitisation: The Zambian Experience" (July 1986) : 1-3

⁸ High Court of Zambia, Ndola [1979] Unreported.

⁹ SCZ Judgment No 4 of 2010.

liquidation. The Supreme Court held otherwise and stated that a Ministerial statement was not effective as to legally place the company in receivership. Notwithstanding the fact that Lima Bank was an SOE, its affairs had to be regulated in accordance with the provisions of the Companies Act.

Examples of companies incorporated under the Companies Act in Zambia which are Government owned include Indo-Zambia Bank in which the Government has shares worth 40%¹⁰ and the Zambia Consolidated Copper Mines Investment Holding (ZCCM-IH) with 85% shares¹¹.

The Government further has a 100% shareholding in the Zambia Electricity Supply Company Limited (ZESCO).¹² ZESCO is a parastatal incorporated under the Companies Act. It was established in 1970, and its governance has evolved over time to one that defines an arms-length relationship with Government. This relationship is defined in the Performance Contract that was signed between the Government and ZESCO in 1996. The contract defines the commercialization issues and other operational benchmarks for ZESCO over the contract period of three (3) years.¹³ In terms of management, ZESCO is governed by a board of directors which is appointed by Government with wide consultations and participation of the private sector. To

¹⁰Indo-Zambia Bank 2010 Annual Report.

¹¹www.luse.co.zm (accessed, November 7th 2011).

¹²www.zesco.co.zm (accessed, November 8th 2011).

¹³www.zesco.co.zm (accessed, November 8th 2011).

support the board in the running of ZESCO is the Management Executive Board headed by the Managing Director and assisted by Directors.¹⁴

In addition, the Zambian Government has a 100% shareholding in the Zambia Daily Mail Limited. Zambia Daily Mail is a limited company whose equity is wholly subscribed by the Government of the Republic of Zambia and it is incorporated under the Companies Act. It is one of the leading publishers of daily newspapers in Zambia. The history of Zambia Daily Mail Limited dates back to the 1950s when it used to be called African Mail, the forerunner to the Central African Mail. The name later changed to Zambia Mail after independence in 1964. It was later bought by the Zambian Government from private owners. It became a daily newspaper in 1970 and the name changed to Zambia Daily Mail.¹⁵

This essay will therefore concentrate on State owned or controlled companies incorporated under the Companies Act and show how there has been interference by successive Governments in their management in form of Ministerial statements and directives. It will also discuss the legal status of SOEs as companies incorporated under the Companies Act. Furthermore, the essay will discuss the legal status of Ministerial statements and directives in the management of SOEs with emphasis on a Ministerial statement or directive purporting to dissolve an SOE incorporated under the Companies Act¹⁶.

The problem that has necessitated the undertaking of this research is that there is need to have a clear cut position on the status of SOEs in terms of management of their operations. The

¹⁴ Jane Kabaki, "Corporate Governance at ZESCO, Zambia." Paper presented at the Second Network on Corporate Governance on SOEs in Southern Africa, Maputo, Mozambique, June 2009.

¹⁵ Anonymous, "The Zambia Daily Mail," www.wikipedia.com (accessed, November 8th 2011).

¹⁶ Chapter 388 of the Laws of Zambia.

confusion to be resolved always borders on whether an SOE is to be regulated by the Government in its operations or whether it has to adhere to the law as laid down in the Companies Act. This confusion was reflected in the case of *Edgar Hamuwele and Another v. Ngenda Sipalo and Another* where the learned trial judge took the misconceived view that a Ministerial statement to place an SOE incorporated under the Companies Act in receivership was valid without following the procedure laid down in the aforementioned Act.

Another instance in which Government interference was exhibited in the operations of a State owned company was the recent appointment by the Minister of Information, Broadcasting and Tourism Given Lubinda of a new media head to run the Zambia Daily Mail Limited. Mr Lubinda, during a press briefing at his Ministry on October 21st 2011, appointed Zambia Daily Mail acting news editor Isaac Chipampe to the position of Managing Director.¹⁷

As far as the legal requirements in the Companies Act are concerned, every registered company ought to be run by a board of directors. To this end, section 203 of the Companies Act provides for the appointment of such directors. The aforementioned Act further vests certain powers in the board of directors unless the Articles provide otherwise. One such power vested in the directors is that they may from time to time appoint one or more Managing Director for such period and on such terms, and subject to the terms of the contract may revoke any such appointment as per section 214(2) of the Companies Act.¹⁸

The appointments made by the Minister as illustrated above indicate a pure disregard of the provisions of the Companies Act. The board of directors is the one which is mandated to appoint

¹⁷ Anonymous, "Lubinda Announces Dismissal of Zambia Daily Mail and Times of Zambia Managing Directors," www.lusakatimes.com (accessed, November 8th 2011).

¹⁸ The Companies Act, Chapter 388 of the Laws of Zambia.

the Managing Directors and not the Minister. He is not part of the board of directors and he is not authorised to make such appointments. This clearly shows that there is Government interference in the operations of SOEs.

Furthermore, Government interference in SOEs registered under the Companies Act has been seen in the case of ZESCO Limited. However the Government is quick to dispel such allegations of Government interference and they claim that ZESCO operates freely. For instance, in 2004, the then Energy Permanent Secretary (PS) Mr. Geoffrey Mukala in his appearance before Parliamentary Committee on Energy chaired by then United Party for National Development(UPND) Mwinilunga Member of Parliament stated that there was no interference by the Government in the operations of ZESCO.¹⁹

The above proposition by the then Energy PS Mr. Mukala that there is no Government interference in the operations of ZESCO is hard to reconcile with the recent happenings. For example, on October 12, 2011 after the swearing in ceremony, President Sata announced that he had suspended a contract between ZESCO and a named Egyptian Company that was hired by the Movement for Multi-Party Democracy (MMD) government to pave way for investigations. Mr. Sata stated:

“It has come to my attention that the Egyptian company was milking us money, so I have decided to suspend this contract to pave way for investigations.”²⁰

¹⁹ Anonymous,” Mukala refutes interference by the State in operations of ZESCO,” Times of Zambia, 28th April 2004.

²⁰ Anonymous,” ZAF Commanders fired, ZRA Bosses Suspended,”www.zambianwatchdog.com(accessed, November 18th 2011).

The Companies Act which provides for the appointment of directors in section 203 goes an extra mile and enumerates some of the duties of the directors. Section 215(1) of the Companies Act provides:

“subject to the provisions of this Act, the business of a company shall be managed by directors who may pay all expenses incurred in promoting and forming the company and may exercise all such powers of the company as are not by this Act or Articles required to be exercised by resolution”.²¹

On the basis of the foregoing provision in the Companies Act, the board of directors is mandated to carry out the business of the company and this includes the entering into contracts and rescission of the contracts if need arises. As such, the cancellation of the contract between ZESCO and a named Egyptian company by the President is unlawful and is a pure disregard of the law and reflects Government interference in the operations SOEs registered under the Companies Act.

Arising from the above problems identified in the operations of SOEs, which is Government interference in their operations in form of Ministerial statements and directives, this essay will undertake an investigation as to the pure legal status of SOEs. It will further analyse the place of Ministerial statements and directives in the management of SOEs incorporated under the Companies Act. In discussing the foregoing, an analysis of the *Edgar Hamuwele Case* will be made.

The Companies Act in its preamble states that its mandate is to provide for the formation, management, administration and winding-up of companies; to provide for the registration of charges over the undertakings or properties of companies; to provide for the registration of foreign companies doing business in Zambia; and to provide for matters connected with or

²¹ The Companies Act, Chapter 388 of the Laws of Zambia.

incidental to the foregoing. Section 2 of the aforementioned Act further provides that a company is one that is incorporated under the Act.²² As parastatals are companies incorporated under the Companies Act, the expectation is that they should run as such.

The purpose of this study is to highlight the irregularities that face SOEs despite the fact that they are incorporated under the Companies Act. Special emphasis will be placed on the legal effect of a Ministerial statement on SOEs with regards to it being dissolved. This study will further discuss the case of *Edgar Hamuwele and Christopher Mulenga v. Ngenda Sipalo and Brenda Sipalo* to underline the contribution it has made in the autonomy of SOEs as companies to be regulated under the Companies Act disregarding any Executive interference.

The specific objectives of the study will be to:

(b) understand the nature of a parastatal as a company

(c) address the issue of corporate governance in parastatals

(c) ascertain the legal framework under which the operations of SOEs can be regulated with special emphasis on the legal validity of a Ministerial statement made in Parliament to dissolve a state owned company incorporated under the Companies Act.

(d) understand the contribution that the case of *Edgar Hamuwele and Another v Ngenda Sipalo and Another* has made to the objectives in (a) and (b).

This study is justified on basis that it is important to evaluate the control that a Government can exercise over a State owned company. In Zambia, successive Governments have a tendency of

²² The Companies Act, Chapter 388 of the Laws of Zambia

interfering with the operations of State owned companies incorporated under the Companies Act. There is total disregard by the Governments of the fact that though wholly owned by the State, SOEs cannot be regulated by merely making pronouncements that the Government so desires. There is need to understand that SOEs are companies like any other company and they have to be regulated in accordance with the provisions of the Companies Act. The only difference between SOEs and a mere company is that the shareholder of SOEs is the Government unlike a mere company whose shareholders consists of individuals or corporate persons.

This research will be centered on the qualitative aspect rather than quantitative one. Therefore this paper will be restricted to desk research. No form of field research will be undertaken and no research questions will be formulated. The scope of sources of information to be used will include among others law reports, law journals, texts books, articles both within and outside the Zambian jurisdiction, dissertations under obligatory essays and those awarded to master's and doctorate program. The internet will also be used as a source in the research to be undertaken.

1.2 Historical Background to the Creation of State Owned Enterprises in Zambia

At independence, the then President, Kenneth Kaunda, received a country with an economy that was completely under the control of foreigners. For example, the British South Africa Company (BSAC, originally setup by the British imperialist Cecil Rhodes) retained commercial assets and mineral rights that it claimed it acquired from a concession signed with the Litunga of Bulozhi in 1890 (the Lochner Concession). Only by threatening to expropriate it, on the eve of

independence, did Kaunda manage to get the BSAC to assign its mineral rights to the incoming
Zambian Government.²³

Following in the steps of the Soviet Union, Zambia instituted a program of national
development plans, under the direction of the National Commission for Development Planning.
The first plan was the Transitional Development Plan. It was then followed by the First National
Development Plan (1966–71). These two plans, which provided for major investment in
infrastructure and manufacturing, were largely implemented and were generally successful.²⁴

A major switch in the structure of Zambia's economy came on the 19th of April 1968 when the
President of Zambia then, Kenneth Kaunda, announced that the State would intervene in the
Zambian economy and nationalise all private retail, transport, and manufacturing firms in the
country, through what came to be known as the Mulungushi Reforms. Kenneth Kaunda,
announced the Government's declared intention to acquire equity holdings (usually 51% or
more) in a number of key foreign-owned firms, to be controlled by a parastatal conglomerate
named the Industrial Development Corporation (INDECO).²⁵ The then President in his
Watershed speech at Mulungushi said:

“This shall be a land of equal opportunity for all. Since our emphasis is
people and all activities are centered on serving the people, there is no
better alternative under our present circumstances, in the light of bitter
experience, and in view of the people's desire for economic self
determination, than to control the resources of the country and the means
of production and distribution ... A newly independent country with a

²³ Anonymous, “Creation of Parastatals in Zambia,” www.wikipedia.com (accessed November 18th 2011).

²⁴ Anonymous, “Creation of Parastatals in Zambia,” www.wikipedia.com (accessed November 18th 2011).

²⁵ NdangwaNoyoo, “Nationalisation: A Case Study of Zambia.” Paper Presented at the Rhodes University Summer
School, September 2011.

responsible government cannot stand by and let its resources be exploited for the benefit of foreigners alone. We object to have a nation of foreigners on one hand and capitalist masters on the other hand..... Several times before, I have declared in very clear terms that political independence without matching economic independence is meaningless. It is economic independence that brings in its wake social, cultural and scientific progress of man. No doubt political independence is the key, but only the key to the house we must build.....If we are true humanists then whatever institutions we create must be geared towards fulfilling our commitments to the common man. Basically this means providing adequate food, adequate clothing and adequate shelter for all our people in Zambia and not just a few of them.....Today our society is being exploited very badly indeed by some unscrupulous men and women who are driven to the extreme right by the 'profit motive'. A good number bring very little capital into Zambia, but because of their know-how they are able to build something locally on borrowed Zambian money and send out of the country excessive profits after a very short time.”²⁶

A year later, on 11th August 1969, the Matero Reforms were announced, and these resulted in the Government purchasing 51 per cent shares from the existing mining companies: Anglo American Corporation and Roan Selection Trust, leading to partial nationalisation of the copper industry. Eighty per cent of the economy was now under state control after this second phase of nationalisation which now encompassed mining, energy, transport, tourism, finance, agriculture, services, and commerce, trade, and manufacturing and construction sectors. Further reforms were carried out on 10th November 1970. These were extended to the financial sector including the insurance companies and building societies. However, foreign-owned banks such as Barclays, Standard Chartered and Grindlays successfully resisted takeover.²⁷

By January 1970, Zambia had acquired majority holding in the Zambian operations of the two major foreign mining corporations, the Anglo American Corporation and the Rhodesia Selection Trust (RST). Subsequently, the two changed their corporate names and became the Nchanga

²⁶ Kenneth Kaunda, "Towards Complete independence." Watershed Speech, Published by ZIS (Lusaka 1968).

²⁷ Ndongwa Noyoo, "Nationalisation: A Case Study of Zambia." Paper Presented at the Rhodes University Summer School, September 2011.

Consolidated Copper Mines (NCCM) and Roan Consolidated Mines (RCM), respectively. The
Zambian Government then created a new parastatal body, the Mining Development Corporation
(MINDECO). The Finance and Development Corporation (FINDECO) allowed the Zambian
Government to gain control of insurance companies and building societies.²⁸

In 1971, INDECO, MINDECO, and FINDECO were brought together under an omnibus
parastatal, the Zambia Industrial and Mining Corporation (ZIMCO), to create one of the largest
companies in sub-Saharan Africa, with the country's President, Kenneth Kaunda as Chairman of
the board. The management contracts under which day-to-day operations of the mines had been
carried out by Anglo American and RST were ended in 1973. In 1982 NCCM and RCM were
merged into the giant ZCCM.²⁹

1.3 Conclusion

The creation of SOEs was a feature of the immediate post independence period when Kaunda
undertook a major restructuring of the economy in the 1968 Mulungushi and 1970 Matero
reforms. The rationale behind this economic policy was to distribute wealth to the Zambian
people which was largely prior to independence in the hands of the white minority. These
companies were set up and incorporated under the companies Act. The expectation was that, they
would run as companies incorporated under the Companies Act. To the contrary, there have been
a lot of Ministerial statements and directives in the management of State owned companies. This
has created a lot of confusion as to the legal status of these SOEs as well as the legal validity of

²⁸ NdangwaNoyoo, "Nationalisation: A Case Study of Zambia." Paper Presented at the Rhodes University Summer
School, September 2011.

²⁹ E Kaunga, "Privitisation: The Zambian Experience" (July 1986) : 1-3

these Ministerial statements and directives and the answer to the foregoing problems is what this paper seeks to achieve.

The next chapter will briefly discuss what the term company entails. It will also discuss the corporate personality of a company and its consequences. Furthermore, the discussion will focus on the issue of corporate governance in SOEs.

CHAPTER TWO

NATURE OF A COMPANY AND CORPORATE GOVERNANCE IN PARASTATALS

2.1. Introduction

Although company law is a well recognized subject in the legal curriculum and the title of a voluminous literature, its exact scope is vague since the word company has no strictly legal meaning. In legal theory, the term company implies an association of a number of people for some common object or objects. The purposes for which men and women may wish to associate are multifarious, including those as fundamental as marriage and mutual protection. In common parlance, the word company is normally reserved for those associated for economic purposes, that is, to carry on a business for gain.¹

The Companies Act² attempts to define a company. Section 2 of the Companies Act defines a “company” as “A company incorporated under this Act or an existing company³” which is not a very useful definition. In *Tennant v Stanley*⁴ Buckley J. defined the word “company” as follows: “The word “company” has no strict technical meaning. It involves two ideas namely, first that the association is of persons so numerous as not to be aptly described as a firm and secondly that the consent of all the other members is not required for the transfer of a member’s interest. Furthermore in *Darmouth v Warword*⁵, Marshall C.J. defined a company as “A person, artificial, invisible, intangible and existing only in the contemplation of the law as being a mere creature of

¹ L. Gower, *The Principles of Modern Company Law* (London: Steven & Sons Limited, 1957), 3.

² Chapter 388 of the Laws of Zambia

³ Chapter 388 of the Laws of Zambia.

⁴ [1906] 1 CHD 131

⁵ 4 Wheat [US] 518

the law. It possesses only those properties which the charter of its creation confers upon it, either expressly or incidental to its existence.”

It is important to understand the definition of the term company in the legal sense because as it has been discussed above, the word company implies an association and the purpose for which people may associate are many. In company law, the purpose for which people associate is strictly for economic purposes with exceptions.

2.2 Formation of a Company

In terms of formation of a company under the Companies Act, Section 6(1) provides that any two or more persons associated for any purpose may form an incorporated company by subscribing their names to an application for incorporation in the prescribed manner and form upon payment of the prescribed fee.⁶ Where an application for incorporation has been lodged, the Registrar shall subject to the Act issue a certificate in the prescribed form stating that the company is, on and from the date specified in the certificate incorporated and that the company is the type of specified in the application for incorporation.⁷

The above procedure lays down the legal requirements that have to be fulfilled by anyone who wishes to incorporate a company under the Companies Act. The significance of the process of incorporation is that it determines the point at which the company comes into being, the point at which a company can be regarded as separate corporate personality bequeathed with all attributes of corporate personality.

⁶ Companies (Amendment) Act No. 24 of 2011.

⁷ Chapter 388 of the Laws of Zambia

2.3 The Doctrine of Separate Corporate Personality

The consequence of registering a business as a company is to transform the business into an entity in its own right, with legal rights and responsibilities that are distinct from those of its members. In modern company law registration as an incorporated company bequeaths a company with a separate legal personality; the business becomes a legal entity. This outcome is referred to as the doctrine of separate corporate personality.⁸

The principle of separate corporate personality was confirmed in the leading case of *Salomon v. Salomon & Co*⁹. Salomon owned a boot and shoe business. His two sons worked in the business and they were anxious to have a stake in it so Salomon formed a registered company with himself as managing director, in which his wife, daughter and each son held a share. The company's nominal capital was £40,000 consisting of 40,000 £1 shares. The company resolved to purchase the business at a price of £39,000. Salomon had arrived at this figure himself. It was an honest but optimistic valuation of its real worth. The company paid him by allotting him £20,000 £1 shares treated as fully paid, £10,000 worth of debentures (a secured loan repayable before unsecured loans) and the balance in cash. Within a year of trading, the company went into insolvent liquidation owing £8,000 to ordinary creditors and having only £6,000 worth of assets. The plaintiff, Mr. Salomon, claimed that as a debenture holder with £10,000 worth of debentures he was a secured creditor and entitled to repayment before the ordinary unsecured creditors. The unsecured creditors did not agree. The House of Lords held that despite the fact that following the company's formation, Salomon had continued to run the business in the same manner and with the same control as he had done when it was unincorporated, the company formed was a

⁸L Talbot, *Critical Company Law* (New York: Routledge- Cavendish,2008) 23.

⁹ [1897] AC 22

separate person from Mr. Salomon himself. When the company was liquidated therefore, and in the absence of any fraud on the creditors and shareholders, Salomon, like any other debenture holder, was a secured creditor and entitled to repayment before ordinary creditors. The Court thus upheld the principle that a company has a separate legal existence from its membership even where one individual holds the majority of shares and effectively runs the company as his own. In his leading judgment, Lord Macnaghten stated,

“The company is at law a different person altogether from the subscribers to the memorandum; and, though it may be that after incorporation the business is precisely the same as it was before, and the same persons are managers, and the same hands receive the profits, the company is not at law the agent of the subscribers or trustees for them. Nor are the subscribers as members liable, in any shape or form. Except to the extent and in the manner provided by the Act.”

The legal consequence of the doctrine of incorporation, namely that a company is a separate legal entity from its members is represented by the veil of incorporation. This veil is a curtain drawn between the company and its members or owners.¹⁰ This legal separation creates a number of attributes and these attributes will be discussed below.

2.4. Attributes of Separate Corporate Personality

One of the attributes of separate corporate personality is that members that make up the company have limited liability. This means that the liability of shareholders for the company's debts is limited to the amount that they have not paid to the company for its shares. The shareholders are as a general principle not liable for the debts of the company. They are under no obligation to the company or its creditors beyond their obligations based on the value of their shares.¹¹

¹⁰F Cassim, *Contemporary Company Law* (New York: Juta and Co Ltd, 2011) 17.

¹¹Cassim, 18.

Another attribute of separate corporate personality is the fact that shares in a company are transferable in a manner provided for in the company's articles. Those persons who are originally involved in setting up and running the business may wish to leave the business or to leave their 'share' of it to their beneficiaries on their death but, usually, all parties, particularly those remaining involved in the business, will want to affect the company as little as possible.¹²

The ability of the company to own property is another attribute of separate corporate personality. The corporate property belongs to the company and members have no direct proprietary rights to it but merely to their shares in the undertaking.¹³ A company does not hold its property as an agent or trustee of the shareholders. All the property purchased by the company belongs to the company and not to its shareholders. Even a shareholder holding all the shares in a private company does not have a proprietary interest in the company's assets.¹⁴

The company as a separate corporate personality can enter into contracts, enforce its rights, sue and be sued for breach of its legal obligations. If a company sustains a loss for which it has a right of action, a shareholder of the company does not have a direct right of action for the loss. The company's loss is not in law the shareholder's loss, even though the company's loss could reduce the value of the shareholder's shares. Thus a shareholder of a company cannot institute legal proceedings to obtain redress to injuries done to the company, or institute an action to enforce contracts entered into by the company. The company itself must institute the action, as it is in law capable of suing and being sued in its own name.¹⁵

¹²Simon Goulding, *Company Law* (London: Cavendish Publishing Ltd, 1999) 8.

¹³Gower, 69

¹⁴P Davis, *Principles of Modern Company Law* (London: Sweet and Maxwell, 2008) 120.

¹⁵Cassim, 20.

Another attribute of separate corporate personality is that a company is embodied with perpetual succession. This entails that a company enjoys a potentially perpetual existence, which means that, notwithstanding changes in its membership, through a transfer of shares, by death or any other cause, the company retains its legal identity and continues to survive.¹⁶

The principle of separate corporate personality is important in that it recognizes the company as having a legal personality distinct from the shareholders. Therefore, all the parastatals that are incorporated pursuant to the Companies Act are bequeathed with distinct legal personality from the Government who are the shareholders. The parastatal as a distinct legal person has the capability to enter into contracts, enforce these contracts, sue and be sued and own property among other consequences of corporate personality.

There is a tendency by the Government to completely disregard the separate corporate personality of parastatals. One classic example of such an act was illustrated in the case of *Mwanza v. National Transport Corporation (NTC)*¹⁷. In this case, Mr. Mwanza sued NTC for wrongful dismissal. He contended that NTC had no right to dismiss him as general manager for its wholly owned subsidiary United Bus Company of Zambia Limited (UBZ). Mr. Mwanza alleged that since he was appointed by President Kaunda, only Kaunda could fire him. According to Mr Mwanza, when the post of UBZ General Manager fell vacant, the President had written to him in the following terms:

“I have the pleasure to appoint you as general manager of UBZ with immediate effect.”

Mr. Mulenga who gave evidence for NTC and was at the material time the chairman of NTC and Minister of Power, Transport and Works said that the letter from the President did not constitute

¹⁶ Maasdorp v Haddow [1959]3 SA 861 C 866

¹⁷ 1978/ HPC/0124

automatic appointment since the UBZ manager were not legally appointed by the President. He rightly argued that the power to appoint a UBZ General Manager lay with the UBZ board of directors which was chaired by the Managing Director of NTC. He however added that the President could nominate somebody for the post but it was up to the UBZ board of directors to appoint or reject the President's nominee. Likewise the General Manager could only be dismissed by the UBZ board of directors.

However, Mr. Mulenga contradicted himself when he said that Mr. Mwanza was in fact dismissed on the instructions as opposed to the advice of the President. He said since UBZ as part of the NTC group companies fell under the responsibility of his Ministry, and he was chairman of NTC by virtue of his Ministerial post, unfavourable reports pertaining to conduct and performance of Mwanza as UBZ General Manager had come to his attention. He reported the matter to the President who issued instructions that Mwanza be relieved of his post. The letter terminating Mwanza's appointment was then written by the Managing Director of NTC presumably acting as chairman of UBZ. Mulenga did not say whether the chairman wrote the letter of Mwanza's dismissal on instructions from the UBZ board of directors.

Another instance in which corporate personality of parastatals has been disregarded is the suspension of the contract between ZESCO and a named Egyptian Company by the President¹⁸ which was discussed in chapter one. ZESCO as a separate legal entity acting through the board of directors is legally capable of rescinding a contract. The interference by the President is unjustified and a total disregard of the separate corporate personality of parastatals. It merely

¹⁸Anonymous," ZAF Commanders fired, ZRA Bosses Suspended," www.zambianwatchdog.com (accessed, November 18th 2011).

reflects the yearning need of the Government to exert political interference in the management of SOEs.

2.6. Types of Companies

There are two types of companies that can be incorporated under the Companies Act¹⁹, being a private company and a public company. By section 13, a company incorporated under the Companies Act may either be a public company or a private company.

The Companies Act²⁰ under section 14 defines a public company as a company which has a share capital; the articles will state the rights and privileges of the different classes of shares, all the shares are to rank equally, members liability is limited to the unpaid amount on the shares and articles are not to impose any restriction on the right to transfer the with three exceptions, unpaid shares, where there are shares issued to directors or other officers of the company and in the case of pre-emption rights.

The second type of company that may be incorporated under the Companies Act is a private company. A private company according to section 13 of the Companies Act is in three forms; a private company limited by shares, a company limited by guarantee and an unlimited company.²¹ In terms of membership of a private company, Section 16(1) of the Companies Act provides that the articles of a private company shall limit the number of its members to a specified number, being a number not more than fifty. However, as per section 16(2) of the aforementioned Act,

¹⁹ Chapter 388 of the Laws of Zambia

²⁰ Chapter 388 of the Laws of Zambia

²¹ Chapter 388 of the Laws of Zambia

regulations may provide that the articles of an unlimited company may, subject to any specified conditions, limit the number of its members to a number larger than fifty.²²

A company limited by shares is one where the members' liability to contribute towards the company's debts is limited to the nominal value of the shares for which they have subscribed, and once the shares have been fully paid up, there is no further liability.²³ A company limited by guarantee is one which shall not carry on business for the purpose of making profits for its members or for anyone concerned in its promotion or management as per section 19(5). The liability of the members in such a company is limited to the amount that he undertakes to contribute to the assets of the company in the event of its being wound-up.²⁴ An unlimited company is one in which members in case of such a company being wound up have unlimited liability.²⁵

The foregoing enumerates the types of companies that can be incorporated under the Companies Act. This in essence entails that all the parastatals that are incorporated pursuant to the Companies Act fall within the above discussed classes. In most cases, parastatals are in the form of public companies, for example ZESCO is a public company limited by shares in order to enable the corporation to declare profit.²⁶ Indeni petroleum Refinery Company is a parastatal and it is private company limited by shares. Lukanga Water and Sewerage Company was established

²² Chapter 388 of the Laws of Zambia

²³ Gower, 12.

²⁴ Chapter 388 of the Laws of Zambia

²⁵ Chapter 388 of the Laws of Zambia

²⁶ Jane Kabaki, "Corporate Governance at ZESCO, Zambia." Paper presented at the Second Network on Corporate Governance on SOEs in Southern Africa, Maputo, Mozambique, June 2009.

under the Water Supply and Sanitation Act No. 28 of 1997. The Company was later incorporated as a private company limited by shares.²⁷

2.7. Corporate Governance in Parastatals

Corporate governance arrangements define the responsibilities, authorities and accountabilities of owners, board of directors and executive managers of a company²⁸ or the system or process by which companies; partnerships, close corporations and trusts are directed and controlled. Directors of the board, members of a close corporation and trustees of a trust are all responsible for the governance of their enterprise.²⁹

The concept of corporate governance has grown in prominence in recent times. In the wake of Enron, WorldCom, Adelphia Communications and an ever-lengthening litany of corporate malpractice scandals, finding new ways to protect average investors has become an international priority. It is, therefore, not surprising that corporate governance reform is gaining importance as a crucial mechanism for addressing the erosion of investor confidence.³⁰ It goes without saying that there is no single, universally appropriate, model of corporate governance. This principle is recognised in the Kings Report on Corporate Governance for South Africa and it states:

"Companies are governed within the framework of the laws and regulations of the country in which they operate. Communities and

²⁷ Fourth Report of the Public Accounts Committee on the Report of the Auditor-General for 2007 on the Accounts of Parastatal Bodies for the Fourth Session of the Tenth National Assembly appointed by the Resolution of the House on 25 September 2009

²⁸ Jane Kabaki, "Corporate Governance at ZESCO, Zambia." Paper presented at the Second Network on Corporate Governance on SOEs in Southern Africa, Maputo, Mozambique, June 2009.

²⁹ Cheryl James, "Corporate Governance", November 2002

³⁰ Cheryl James, "Corporate Governance", November 2002

countries differ in their culture, regulation, law and generally the way business is done. In consequence, as the World Bank has pointed out, there can be no single generally applicable corporate governance model. Yet there are international standards that no country can escape in the era of the global investor. Thus, international guidelines have been developed by the Organisation for Economic Development Principles of Corporate Governance (OECD), the International Corporate Governance Network and the Commonwealth Association for Corporate Governance. The four primary pillars of fairness, accountability, responsibility and transparency are fundamental to all the international guidelines of corporate governance."³¹

However, this essay will restrict itself to corporate governance in terms how parastatals are controlled and directed in Zambia. This is because the issues of control vis à vis the Government as shareholder and the board of directors is a major concern in SOEs. There is a tag of war between these two entities as to who has the powers to govern the affairs of the company. This tag of war has in effect led to confusion as to the role that the Government should play as shareholder and on the other hand, the role that the board of directors should play as agents appointed to act on behalf of the company.

In the 1970s through to the 1990s, privatization of SOEs or parastatals was the general trend around the world including Zambia. Later, there was a realisation that the State could still play a vital role in the growth of the economy by maintaining a stake in parastatals. In order to maintain a stake in such parastatals, States realized that corporate governance was critical and a key component in ensuring that the enterprises made a positive contribution to the country's overall efficiency and competitiveness. In 2005, the OECD came up with guidelines on corporate governance in SOEs.³²

³¹ Paragraph 23 on page 15 of the Kings Report in South Africa on Corporate Governance.

³² Eugene Chandi," Article on Corporate Governance in Parastatals" Maravi Blog. <http://maravi.blogspot.com> (accessed, November 18th, 2008).

The OECD guidelines on SOEs is an international benchmark that helps governments assess and improve the way they exercise ownership of these entities which often constitute a significant share of the economy. These guidelines aim at striking a balance between the State's responsibilities for actively exercising its ownership functions such as the nomination in the management of the company. The guidelines are based on six principles namely; ensuring an effective legal and regulatory framework for SOEs, the State acting as owner, equitable treatment of shareholders, relations with stakeholders, transparency and disclosure and the responsibility of the board of directors.³³ This discussion will only limit itself to the principle of State acting as owner and responsibility of board of directors because these principles are the ones which outline the role of the Government in the management of SOEs and the responsibilities of the board of directors which the Government usually usurps.

Under the principle of State acting as owner, the State should act as an informed and active owner and establish a clear and consistent ownership policy, ensuring that the governance of SOEs is carried out in a transparent and accountable manner with the necessary degree of professionalism and effectiveness. Specifically, the Government should not be involved in the day to day management of SOEs and allow them full operational autonomy to achieve their defined objectives. The State should let SOE boards exercise their responsibilities and respect their independence. The State as owner should also exercise its ownership rights according to the legal structure of the company.³⁴

In terms of the principle of responsibility of the board of directors, the boards of SOEs should have the necessary authority, competences and objectivity to carry out their function of strategic

³³ OECD Guidelines on Corporate Governance in SOEs, 2005.

³⁴ OECD Guidelines on Corporate Governance in SOEs, 2005.

guidance and monitoring of management subject to the objectives set by the company. The boards should act with integrity and be held accountable for their actions. The SOE boards should also have the power to appoint and remove the CEO. In addition, the boards of SOEs should be composed in such a way that they can exercise objective and independent judgment.³⁵

A board of directors is a body of elected or appointed members who jointly oversee the activities of a company. A board's activities are determined by the powers, duties and responsibilities delegated to it or conferred on it by an authority outside itself. These matters are typically detailed in the organisation's by-laws. Typical duties of board of directors include; governing the organisation by establishing broad principles and objectives; selecting, appointing and reviewing the performance of CEOs; ensuring the availability of adequate financial resources; accounting to the stakeholders for the organisation's performance and selecting the salary and compensation of company management.³⁶

This essay will now discuss the corporate governance in parastatals by using ZESCO as an example against the governance framework generally and the OECD principles in particular. ZESCO's governance structure is composed of the Ministry of Finance and National Planning as shareholder with the Ministry of Energy and Water Development as the executing authority. The ZESCO board of directors is appointed by the Minister of Energy and Water Development. The ZESCO Articles stipulate the composition, appointment, term and removal of the board members. Appointment has to be made from the following bodies; the Zambia National Farmers Union, the Zambia Institute of Chartered Accountants, the Engineering Institute of Zambia, the Law Association of Zambia, the Zambia Association of Chambers of Commerce and Industry,

³⁵ OECD Guidelines on Corporate Governance in SOEs, 2005.

³⁶ Anonymous, "Board of Directors," www.wikipedia.com (accessed, March 6th 2012).

the Permanent Secretary in the Ministry of Finance and National Planning and the Permanent Secretary in the Ministry of Energy and Water Development. The mentioned organisations have to submit nominees to the Minister of Energy who takes them through the Government vetoing process and then announce the new board members. The new board members choose a chairperson from their ranks but may not select either of the two Government representatives as chairperson.³⁷

An important characteristic of the ZESCO board of directors is that only the board of directors has the power to appoint and remove the Managing Director. In many SOEs, the State or the Government appoints the Managing Director which can lead to external (political) interference. This principle of ensuring that board of directors appoints the Managing Director is that such a person is protected from Government and other external interference.³⁸ However, the foregoing mandate of the board of directors is not in some cases what happens. For example, just after assuming power, Mr. Sata retired ZESCO Managing Director Mr. Ernest Mupwaya and replaced him with the former Chief Executive Officer, Cyprian Chitundu.³⁹

The above composition of the ZESCO board of directors and their jurisdiction seems to be the general trend of the composition of board of directors in other parastatals. This composition seems to reflect the OECD corporate governance principles in parastatals in that the board of directors appears to be independent and appear to be appointed from persons who seem to be competent hence lessening the control that the Minister has over such parastatals. In reality, this

³⁷ Jane Kabaki, "Corporate Governance at ZESCO, Zambia." Paper presented at the Second Network on Corporate Governance on SOEs in Southern Africa, Maputo, Mozambique, June 2009.

³⁸ Jane Kabaki, "Corporate Governance at ZESCO, Zambia." Paper presented at the Second Network on Corporate Governance on SOEs in Southern Africa, Maputo, Mozambique, June 2009.

³⁹ Anonymous, "ZAF Commanders Fired, ZRA Bosses Suspended," www.lusakatimes.com (accessed, 2nd March 2012.)

is not the case. The mere fact that that the Minister and his Government have to approve the nominees ensures that the Government is able to control the composition of the board and hence ultimately control the affairs of the board. The Government will only approve the nominees they think are loyal to the Government regardless of their competence and credibility.

In Zambia, it is clear that that the guidelines on corporate governance in SOEs are infringed. The Government almost takes part in the day to day management of SOEs. The autonomy of the company as a separate entity is not recognized and the independence of the board is not respected. The board is not allowed to perform the functions that it is legally mandated to perform such as the appointment of Managing Directors or CEOs. For example, Mr Given Lubinda, then Minister of Information, Broadcasting and Tourism appointed Mr Chipampe as the new media head to run the Zambia Daily Mail Limited during a press briefing at his Ministry on October 21st 2011.⁴⁰ This appointment was purely a preserve of the board of directors.

Mwaura in his paper argues that the poor performance of the board of directors of parastatals has been attributed to the existence of multiple agents. Unlike in a private company which has a single principle (shareholders) and agents (managers), a parastatal is governed by multiple agents namely, the manager and the State or public officials. Voters who elect the agents (public officials) are considered to be the principles of both the board of directors and the State.

Mwaura further argues that in Kenya for example, the President is empowered to determine the composition of the board of directors. Due to the political nature of appointments, parastatal boards are composed of many directors who are ex-civil servants with little or no private

⁴⁰ Anonymous, "Lubinda Announces Dismissal of Zambia Daily Mail and Times of Zambia Managing Directors," www.lusakatimes.com (accessed, November 8th 2011).

business experience. The appointment of directors by the President politicizes directorship. Directors are appointed to the position that carries with it all the liabilities but are not given the power to carry out the roles that the law imposes.⁴¹

The observations made by Mwaura are also typical to the management of parastatals in Zambia. The management of a parastatal is by the chairman and the members of the board of directors, all appointed by the relevant Minister. The chairman and the board of directors are responsible for implementation of aims and objectives of the parastatals. The board of directors is drawn from the Government and prominent persons from the private sector. The chairman of the board of directors reports to the Government through the Minister.⁴² The people who are appointed to serve on the SOE boards are appointed on party lines and not on basis of their credibility. And if a director is appointed on political lines, his or her autonomy in performing the functions he is mandated to perform is highly compromised. His performance will in most cases be in favour of the appointing authority that feed him. In any case, Ministers end up making directives and statements in the management of SOEs without having regard to the function of the board of directors.

The foregoing sentiments were also echoed in *The Post* newspaper editorial comment⁴³ where the editor observed that politically affiliated persons are often appointed to boards and management of SOEs at the expense of professionalism. These politically appointed boards lack independence that is the ability to make impartial decisions without fear or favour. The

⁴¹ Kiarie Mwaura, "The Failure of Corporate Governance in State Owned Enterprises and the Need for Restructured Governance in Fully and Partially Privatised Companies: A Case Study of Kenya" *Fordharm International Law Journal*, no.31 (2007): 34-75

⁴² <http://www.shvoong.com/business-management/management/2052603-parastatals> (accessed, 6th March 2012).

⁴³ The Editorial Comment, "Cronyism in Parastatal Appointments," *The Post Newspaper*, Saturday, 26th June 2010.

appointment of directors of SOEs should not be aimed at influencing pursuit of political policies at the expense of interests of the entity. Directors and senior managers who are appointed on basis of political patronage usually exert direct and undue political interference in the way the entity is run.⁴⁴

If directors of parastatals try to adhere to their professional ethics and do what is right for the company, they are threatened with loss of their jobs and in some cases they do actually lose their jobs. For instance, the then Managing Director of ZESCO Mr. Chitundu was massively intimidated and made to compromise his professionalism by signing an Indefeasible Right of Use Agreement (IRU). Under the IRU revenue sharing was 80% for ZAMTEL and 20% ZESCO. The agreement also stated that provisions of the IRU would apply to all existing and future optical fibre networks to be rolled out by ZESCO.⁴⁵

The above terms of the IRU were clearly not beneficial to ZESCO and as such the director did not see it fit to sign the agreement immediately without proper procedure. Because of his reluctance in signing the IRU, the director was summoned to State House where he met with Dr. Richard Chembe - Economic Advisor to the President and Mr. Joseph Jalasi - Legal Advisor to the President. He was subjected to immense pressure by Dr. Chembe who said that he was delaying the process and would not be confirmed in his position. On the 17th of December 2009, while he was in Egypt, The ZESCO Managing Director was instructed to sign the signature page of the IRU which was faxed to him and which he signed and faxed back. The ZESCO Board passed a retrospective board resolution at a Board Meeting held on the 28th January 2010

⁴⁵ Report to H.E the President of the Republic of Zambia, Mr. Michael Chilufya Sata of the Commission of Inquiry into the sale of Zamtel Chaired by Hon. Sebastian Zulu S.C. Minister of Justice, 42

authorizing ZESCO to sign the IRU Agreement which had, in fact, already been signed by ZESCO on the 17th December 2009 and the ZESCO Managing Director's contract of employment was terminated.⁴⁶ The foregoing act leaves much to be desired. It confirms the fact that the Government does in fact exert pressure on directors of parastatals leading them to make shocking decisions. Any reasonable person would have realized that the IRU was not beneficial to ZESCO.

In Zambia today, the appointment and dismissal of CEOs and other key Executives of SOEs are at the prerogative of a Minister. But the power to hire and fire CEOs is a key board competence. It is therefore contradictory to charge the board with responsibility with no power to hire and fire CEOs. This political interference amounts to usurpation of board powers by politicians running the Government.

2.8. Conclusion

All parastatals that are formed under the Companies Act are mandated to follow the provisions laid down in the Companies Act. By virtue of their incorporation, parastatals are bequeathed with a separate corporate personality. This means that they are distinct from the Government which is the shareholder. Therefore, parastatals as corporate persons can sue and be sued, enter into contracts, possess potential perpetual existence and they can own property among other attributes. However, Government has disregarded the corporate personality of these parastatals. Government has continued to interfere in the management of these parastatals through Ministers responsible for the parastatals issuing various statements and directives in their management.

⁴⁶ Report to H.E the President of the Republic of Zambia, Mr. Michael Chilufya Sata of the Commission of Inquiry into the sale of Zamtel Chaired by Hon. Sebastian Zulu S.C. Minister of Justice, 42

Due to the problems of interference in the management of SOEs, corporate governance is important in trying to assess the role that should be played by the government in the management of SOEs. The OECD principles on corporate governance in parastatals are an important benchmark in governance of parastatals. This is because they outline the role that the Government as owner of the enterprise and the role that board parastatals as agents of the company should perform.

The next chapter will look at the legal validity of Ministerial statements and directives in the management of SOEs. It will then narrow down to the legal validity of a Ministerial statement purporting to dissolve a State Owned Company. In this regard, the *Edgar Hamuwele case* will be examined.

CHAPTER 3

MINISTERIAL STATEMENTS AND DIRECTIVES IN MANAGEMENT OF PARASTATALS

3.1 Introduction

As it was established in Chapter two, Government interferes in the management of SOEs by disregarding the fact that parastatals are corporate entities bequeathed with corporate personality as was established in the *Salomon case*. This control that is exerted on these parastatals is usually in the form of Ministerial directives and statements including presidential directives. These directives in some cases purport to dissolve SOEs which are incorporated under the Companies Act. Therefore, this chapter will discuss instances of Ministerial statements and directives in the management of parastatals and the legality of these actions within the law that governs companies in Zambia, that is, the Companies Act and other principles of company law. Emphasis will be laid on a Ministerial statement purporting to dissolve a parastatal incorporated under the Companies Act. In this regard, the Case of *Edgar Hamuwele* will be discussed.

3.2 Examples of Ministerial Directives and Statements and their Legal Validity

The issuance of Ministerial directives and statements in the management of parastatals is very prevalent. It is very common to hear members of the Executive, be it the Ministers, Permanent Secretaries or even the President issuing directives to parastatals. For example, while on a campaign tour in the Copperbelt Province, President Banda directed the Minister of Mines, Maxwell Mwale, to direct the Board of Zambia Consolidated Copper Mines Investment Holding ZCCM (IH) to immediately write off outstanding balances which sitting tenants of 3,386 houses

in the Copperbelt Province owed to the company. The President also directed ZCCM-IH to immediately stop recoveries of all outstanding balances and harassment of sitting tenants. President Banda said he had decided to issue directives because of complaints and petitions which sitting tenants presented to him. He said the directive referred only to residential properties.¹

Another instance in which Ministerial directives were issued to a parastatal was in the Zambia Telecommunications Company (ZAMTEL) versus ZESCO optic fibre saga. In this matter, a Joint Technical Committee comprising ZAMTEL and ZESCO staff was set up under the auspices of the Communications Authority in July 2008 on the understanding that the two parties would seek to rationalize and harmonise their optical fibre network roll-out and expansion plans, based on mutually beneficial and agreed commercial terms. Contrary to the above, on the 28th of October 2009, the ZESCO board were informed by the board Chairman that the Ministry of Finance, as principal shareholder, was directing ZESCO to cede their optical fibre network to ZAMTEL and to cease all commercial operations on their optical fibre networks.² The minutes stated:

“The Chairman informed the members that he had received a letter from the Ministry of Finance and National Planning explaining that there were new developments on the issue of how to manage the ZESCO Optic Fibre. The letter was a directive from the principal shareholder and it directed among other things that ZESCO should lease the existing Fibre Optic to ZAMTEL on a lease whose duration would be determined by Government and that ZESCO should only use the Optic Fibre for its operations and the Commercial aspect would cease hence forth. The Board discussed the matter extensively and **AGREED** that this was Government Policy which the Board could not change and therefore it

¹Anonymous, “Cancel all debts of Sitting Tenants, RB directs ZCCM-IH” www.lusakatimes.com (accessed, 17th March 2012).

² Report to H.E the President of the Republic of Zambia, Mr. Michael Chilufya Sata of the Commission of Inquiry into the sale of ZAMTEL Chaired by Hon. Sebastian Zulu S.C. Minister of Justice

was decided that the earlier resolution to merge the assets of ZESCO and ZAMTEL and the creation of a new entity should be varied to conform with the Shareholder's directive.”³

In light of the above directives, the question that now arises is the legal validity of these directives towards parastatals bearing in mind that parastatals are companies incorporated under the companies Act. In the case of *Salomon v. Salomon*⁴ which was discussed in the preceding chapter, it was established as a principle in company law that a company is on its own a separate artificial person. The principle established applies with full vigour in Zambian company law. For instance, Section 22(1) of the Companies Act⁵ provides that a company shall have, subject to this Act and to such limitations as are inherent in its corporate nature, the capacity, rights, powers and privileges of an individual.

However, since the company is an artificial person, it has to perform its acts through the use of natural persons. The foregoing was emphasised in the case of *Associated Chemical Limited v. Hill and Delamain Zambia Limited and Another*.⁶ In this case, the Supreme Court of Zambia stated that as a metaphysical entity or fiction of law which only has legal but not physical existence, a company though being a separate and distinct legal person from its members can only act through humans charged with its management and the conduct of affairs. These natural persons that are appointed by the company to act on its behalf are known as the board of directors. The duties of the board of directors have already been discussed in the preceding

³ Minutes of a Special Meeting of the Board of Directors held on 28th October, 2009, at Head Office Corporate Board Room at Stand 6949 Great East Road, Lusaka, Starting at 10: 00hrs.

⁴ [1897] AC 22 HL

⁵ Chapter 388 of the Laws of Zambia

⁶ SCZ Judgment No. 2 of 1998

chapter. In addition, Section 203 of the Companies Act states that a director is any person who is appointed by the members of a company to direct and administer the business of the company.⁷

As discussed in the preceding chapter, corporate governance tends to be a tag of war between the board of directors and the Government as to who has the power to control the company. The answer to this question determines how the company's affairs are to be conducted. There are two primary decision making bodies within a company, the general meetings of shareholders and the board of directors. Directors derive their powers and functions from the Articles of the company or the Companies Act. Therefore, if a dispute arises between directors and shareholders as to a particular course of action the company should take, whether the former or the later should be able to assert supremacy is determined primarily by the construction of the Articles.⁸

In the case of *Kasengele and Others v. Zambia National Commercial Bank*⁹, the Supreme Court held that shareholders as a matter of right enjoy overriding authority over company affairs even over the wishes of the board of directors. The above view in case law treats the directors ultimately as agents of the company who although are entrusted with the day to day management of the company can still be given instructions by the shareholders and have their powers limited. However, the power of the shareholders in exercising their powers has been limited by statute which has clearly outlined the role that the board of directors is to play. To this end, section 215 of the Companies Act provides that subject to the Companies Act, the business of the company shall be managed by the directors, who may, pay all expenses incurred in promoting and forming the company, and may exercise all such powers of the company as are not, by the Companies Act, required to be exercised by the company by resolution.

⁷ Chapter 388 of the Laws of Zambia

⁸ Simon Goulding, *Company Law* (London: Cavendish Publishing Limited, 1999) 144

⁹ SCZ Judgment No 11 of 2000.

However, Section 215 does not mean that the shareholders cannot have a say in the affairs of the company. Section 216 of the Companies Act provides the shareholder with an opportunity to have the final say in the most important issues in any company by limiting the powers of the board of directors in relation to certain acts. Section 216(1) provides that the directors of a company shall not without the approval in accordance with the aforementioned section of an ordinary resolution of the company sell, lease or otherwise dispose of the whole, or substantially the whole, of the undertaking or of the assets of the company¹⁰; issue any new or unissued shares in the company¹¹; or create or grant any rights or options entitling the holders thereof to acquire shares of any class in the company.¹² Specifically, the approval for a transaction referred to in paragraph (a) of subsection (1) shall be an approval of the specific transaction proposed by the directors.¹³

The import of the above provisions is that although the Government is the shareholder in a parastatal, the parastatal is a corporate personality distinct from its shareholder, the Government in this case, endowed with the capacity to perform acts that a natural person can perform. But as it has been established, it will perform these acts through the board of directors. The board of directors is mandated to exercise all powers that a company has the right to exercise as long as those acts are not contrary to the provision of the Companies Act and the Articles. The Articles of a company are rules and regulations that govern the conduct of the company. It has also been seen that shareholders do have a right in certain transactions to have the final say. Therefore, the Minister or any other person has no power to issue directives in the management of parastatals. The board of directors is the only body legally mandated to determine how the affairs of the

¹⁰ Section 216(1)(a) of the Companies Act, Chapter 388 of the Laws of Zambia

¹¹ Section 216(1)(b) of the Companies Act, Chapter 388 of the Laws of Zambia

¹² Section 216(1)(c) of the Companies Act, Chapter 388 of the Laws of Zambia

¹³ Chapter 388 of the Laws of Zambia

parastatal should be conducted subject of course to the provisions of the Companies Act and the Article of a company.

On the basis of the foregoing position of the law, it is submitted that the directive issued by former President Banda to former Mines Minister, Mr. Mwale to direct ZCCM to cancel the debts and stop the recovery of the balances from the sitting tenants of ZCCM's houses was a clear political move. President Banda had no place at all in issuing directives at ZCCM, a company bequeathed with corporate personality. Such an act would only have been legally done by ZCCM acting through its board of directors as provided for under the Companies Act. Therefore, the directive issued by former President Banda is illegal and violates the principles of company law and the Companies Act.

Similarly, the directive issued at ZESCO to lease their optic fibre to ZAMTEL is clearly contrary to what the law provides. In section 216 of the Companies Act, it has been discussed that the directors' powers in a company is limited when it comes to leasing the assets of the company. They can only do so if the company approves by ordinary resolution. The approval of the company will only be to the specific transaction proposed by the directors. This means that the ZESCO board was the one which was mandated to propose to the company the lease of the optic fibre to ZAMTEL. The Government's role as shareholder was merely to decide whether to approve the proposed transaction or not. But in this case, the Government did propose and approve the lease of the ZESCO optic fibre to ZAMTEL. The board's role was merely to sign the lease without question. This act by the Government is clearly illegal as it is in contravention of Section 216 of the Companies Act.

Another area in which the Government is fond of issuing Ministerial statements is in the dissolution of parastatals which habit can be traced back to the 1970s. The first wave of purported company dissolutions by Ministerial action took place on 10th November, 1970 when President Kaunda forced foreign minority holders of UBZ in which the Government had 51% shareholding, who were all limited companies to go into liquidation. The reason he gave for such an act was that he had received definite information that the 49% shareholders were involved in a major contract in the Cabora Bassa scheme.¹⁴

Another incident of purported presidential dissolution of a parastatal was on 23rd September 1977 when President Kaunda, in an early morning national broadcast, announced the dissolution of a wholly owned subsidiary of ZIMCO called Medical and Pharmaceutical Corporation Ltd (MEPCO). The President did not expressly state the reason why he ordered the dissolution of this company which was the sole buyer and distribution company of medical drugs throughout the country. But in the capital city of Lusaka, news had leaked that MEPCO had started refusing to supply drugs to Government hospitals because the Government was in serious arrears in debts owing to the company. The shortage of drugs soon led to operational difficulties at the hospitals and the issue finally made news in the dailies to the embarrassment of the Government.¹⁵

Additionally, in 1976-77, the Minister of Finance, Mr. John Mwanakatwe, directed that a liquidator be appointed to manage the dissolution of a wholly-owned subsidiary of FINDECO,

¹⁴Remmy Kabanga Mushota, "The legal validity of a ministerial directive purporting to dissolve limited liability companies in Zambia," *Comparative and International Law Journal of South Africa*, no.12 (July 1979):140-164.

¹⁵Remmy Kabanga Mushota, "The legal validity of a ministerial directive purporting to dissolve limited liability companies in Zambia," *Comparative and International Law Journal of South Africa*, no. 12 (July 1979):140-164.

the Industrial Finance Company (IFC) Ltd, which provided finance to Zambian businessmen in terms of loans and hire purchase facilities. Accordingly, the company was wound up.¹⁶

Again, the validity of the above directives purporting to dissolve parastatals incorporated under the Companies Act comes into question. It seems the only reason Kaunda issued the directives political reasons as he could not give a concrete reason as to why the companies were being dissolved. The Zambian Companies Act in its preamble among other things states that it is an Act to provide for the winding up of companies.¹⁷ This means that if any company that is incorporated under the companies Act is wound up, it has to be done in accordance with the Companies Act.

The Companies Act in section 263 provides for two modes of winding up. The first mode of winding up that is prescribed in the Companies Act is winding up by the court.¹⁸ The court may order the winding up of a company on the petition of a person other than the Registrar if¹⁹; the Company has by special resolution resolved that it be wound up by the court²⁰; the company does not commence its business within twelve months after its incorporation or suspends its business for twelve months²¹; the company is unable to pay its debts²²; the period if any fixed for the duration of the company by the articles expires of the event, if any, occurs on the occurrence of which the articles provide that the company is to be dissolved²³; the number of

¹⁶ Remmy Kabanga Mushota, "The legal validity of a ministerial directive purporting to dissolve limited liability companies in Zambia," *Comparative and International Law Journal of South Africa*, no.12 (July 1979):140-164.

¹⁷ Companies Act, Chapter 388 of the Laws of Zambia

¹⁸ Section 263(a) of the companies Act, Chapter 388 of the Laws of Zambia

¹⁹ Section 272(1) of the Companies Act, Chapter 388 of the Laws of Zambia

²⁰ Section 272(1)(a) of the Companies Act, Chapter 388 of the Laws of Zambia

²¹ Section 272(1)(b) of the Companies Act, Chapter 388 of the Laws of Zambia

²² Section 272(1)(c) of the Companies Act, Chapter 388 of the Laws of Zambia

²³ Section 272(1)(d) of the Companies Act, Chapter 388 of the Laws of Zambia

members is reduced below two²⁴; or if in the opinion of the court, it is just and equitable that the company should be wound-up.²⁵

The second mode in which a company can be wound up provided for in section 263 is through voluntary winding up which can either be a members' voluntary winding up or a creditor's voluntary winding up. A company may be wound up voluntarily if the company so resolves the resolution being a special resolution.²⁶

On the basis of the foregoing, a company in Zambia incorporated under the Companies Act can only be lawfully dissolved in accordance with part XIII of the Companies Act. Therefore, Ministerial statements purporting to dissolve parastatals are void for all intent and purposes. As long as the legal requirements provided for in the Companies Act with regards to winding up are not complied with, then no effective winding takes effect. The company will continue to legally exist as it can only be brought to an end legally by complying with part XIII of the Companies Act.

3.3 Analysis of the Case of Edgar Hamuwele and Christopher Mulenga v. Ngenda Sipalo and Brend Sipalo, SCZ Judgment No. 4 of 2010

The facts of the case were that the 1st respondent was the Managing Director of Lima Bank Limited (in liquidation). The appellants were appointed as joint liquidators of Lima Bank. As liquidators of Lima Bank, the appellants offered for purchase to the 1st respondent premises at 14B, Chila Road, Lusaka. The letter offer specified certain conditions that the purchaser should comply with failure to which the offer would be revoked. The 1st appellant did not fulfill the

²⁴ Section 272(1)(e) of the Companies Act, Chapter 388 of the Laws of Zambia

²⁵ Section 272(1) (f) of the Companies Act, Chapter 388 of the Laws of Zambia.

²⁶ Section 305 of the Companies Act, Chapter 388 of the Laws of Zambia.

conditions leading the appellants to cancel the offer. After the revocation of the letter, the first respondent placed a caveat on the premises which action was challenged in the High Court and upon hearing the parties, the High Court ordered that the caveat be removed. The 1st respondent appealed to the Supreme Court against the High Court Order and his appeal was unsuccessful. The 1st respondent refused to vacate the premises even after losing the appeal hence the originating summons to seek vacant possession of the premises.

In opposing the originating summons, the 1st respondent questioned the validity of the appointment of the appellants as liquidators of Lima Bank. The background leading to this doubt was that on the 19th of March, 1997, the then Minister of Agriculture issued a Ministerial Statement in the National Assembly to the effect that the bank had been put in receivership and that a debt collector would be appointed. On other hand, after the Ministerial statement, there was a resolution by members of the bank to place it in voluntary liquidation by an extra ordinary meeting held on 25th March 1997 at which it was resolved to wind up the affairs of the Bank and to appoint joint liquidators. It was at that meeting that the appellants were appointed as joint liquidators.

At the close of trial, the trial judge opined that since Lima Bank was dissolved by the Minister's pronouncement on 19th March 1997, it follows that the bank ceased to operate from that day. He agreed with the first appellant's contention that the resolution to appoint the appellants as liquidators was made after the bank was dissolved by the Minister and placed under receivership. He also agreed with the respondents that since the resolution to appoint the appellants as liquidators was made after the Minister's decision then that resolution was null and void.

The appellants appealed to the Supreme Court and one of the grounds they advanced was that the learned trial judge erred in law and in fact when he failed to find and hold that only a liquidation process or exercise was validly and legally effected or set in motion in respect of the bank in question. They contended that the learned trial judge misdirected himself when he took the view that Lima Bank had been placed in receivership pursuant to Ministerial statement.

The Supreme Court held that the Ministerial statement remained as an intention to appoint a receiver or a policy declaration, which intention or declaration never crystallized. The Supreme Court stated that they did pronounce themselves in the case of *Manil Patel and Ketankumar Patel* ²⁷ that a policy has no force of law and cannot therefore prevail against an enactment. Therefore, Lima Bank was never placed in receivership. In terms of the law, only a valid process of liquidation commenced at the time of passing the extra ordinary resolution. On basis of the foregoing, it follows that the appointment of the appellants as joint liquidators by members of Lima Bank.

The *case of Edgar Hamuwele* is a remarkable judgment in that it clearly gives the status of a Ministerial statement. The Supreme Court rightly held by stating that a ministerial statement is a mere declaration of intent with no force of law. A distinction should always be made between an executive act and the legal requirements or steps that may be required to carry out the Executive act into effect. The Ministerial directives and statements can only have effect in the management of parastatals if they are done within the ambit of the law or if the necessary steps legally required are taken. Failure to comply with the legal requirements renders the directives and statements null and void.

²⁷ SCZ Appeal No. 63 of 1996.

3.4 Conclusion

It has been established that the Executive makes various Ministerial statements and directives in the management of parastatals. However, these statements have no force of law as long as they do not comply with the legal requirements. The *case of Edgar Hamuwele* has been a landmark decision in establishing the legal status of Ministerial statements in the management of parastatals. The case established that Ministerial statements and directives have no effect in the management of parastatals and cannot prevail over the legal requirements.

The next chapter will make a conclusion of the findings of the discussion. It will further outline some recommendations that can minimize the interference by the State in the management of parastatals.

CHAPTER FOUR

CONCLUSION AND RECOMMENDATIONS

4.1 Conclusion

It has been established that the creation of SOEs was a feature of the immediate post independence period when Kaunda undertook a major restructuring of the economy in the 1968 Mulungushi and 1970 Matero reforms. The rationale behind this economic policy was to distribute wealth to the Zambian people which was largely prior to independence in the hands of the white minority. These companies were set up and incorporated under the Companies Act and the expectation was that, they would run as companies incorporated under the Companies Act. Hence, parastatals are like any other company incorporated under the Companies Act. The only difference with the other companies incorporated under the Companies Act is in terms of shareholding is that the majority shareholding in parastatals is the Government.

It has also been established that by virtue of their incorporation, parastatals are bequeathed with a separate corporate personality. The principle of separate corporate personality as was propounded in the leading case of *Salomon v Salomon*¹ entails that at law parastatals are distinct from the Government which is the shareholder. Therefore, parastatals as corporate persons enjoy all the attributes that come with a company being a separate corporate personality. These include the fact that a parastatal can sue and be sued, enter into contracts, possesses potential perpetual existence; its members in this case the Government have limited liability among other attributes.

¹ (1897) AC 22 HL

However, Government has in many instances disregarded the corporate personality of these parastatals by interfering in the management of these parastatals. To illustrate the disregard of the separate corporate personality of parastatals, the case of *Mwanza v. National Transport Corporation*² was discussed where President Kaunda appointed Mr Mwanza as UBZ general manager and also dismissed him which act was purely one to be done by the company acting through its board of directors. Another instance that was discussed in which the Government completely disregarded the corporate personality of a parastatal was the suspension by President Sata just after assuming power of a contract between ZESCO and a named Egyptian company on the basis that the Egyptian company was milking ZESCO a lot of money.³

Furthermore, it has been established that corporate governance is critical and key in trying to minimize the interference of the Government in the management of SOEs. This interference as was discussed mainly stems from lack of a clear cut borderline on when the State as the majority or sole shareholder should respect the corporate personality of these parastatals. Corporate governance is the process by which companies are controlled and directed.⁴ It is important in trying to assess the role that should be played by the Government in the management of SOEs.

It has been observed that in 2005, the OECD came up with guidelines on corporate governance in SOEs which guidelines helps Governments assess and improve the way they exercise ownership of these entities. These guidelines are based on six principles. Of primary importance to this discussion were the principles of State acting as owner and the responsibility of the board of directors. This is because interference in the management of parastatals by the Government is

² The High Court of Zambia, 1978 before High Court Commissioner Mr. John Jeary at Lusaka(unreported)

³ Anonymous," ZAF Commanders fired, ZRA Bosses Suspended," www.zambianwatchdog.com (accessed, November 18th 2011).

⁴ Cheryl James,' Corporate Governance' November, 2002.

usually usurpation of the powers of the board by the Government and these two principles clearly outline the role that the Government as owner of the enterprise and the role that board parastatals as agents of the company should perform.

Under the principle of State acting as owner, it was established that the State should act as an informed and active owner and establish a clear and consistent ownership policy ensuring that the governance of SOES is carried out in a transparent and accountable manner with the necessary degree of professionalism. The State should also not be involved in the day to day management of SOEs and allow these entities achieve their defined objectives. The State should also let the board of directors exercise their responsibilities and respect their independence.

On the other hand, under the principle of responsibility of board of directors, it was established that boards shall have the necessary competences and objectivity to carry out their function of strategic guidance and monitoring of management subject to the objectives set by the company. The boards should act with integrity and be held responsible for their actions. Most importantly, the SOE boards should have the power to appoint and remove Managing Directors and be composed in such a way that they can exercise independent and objective judgment.

However, it has been established that in Zambian parastatals, the principles of corporate governance are not adhered to especially with respect to the composition and powers of the board. It was argued in the paper that in most cases, politically affiliated persons are often appointed to the positions of board of directors. For instance, even though the ZESCO Articles outline the bodies from which the ZESCO board is to be drawn, the mere fact that the nominees have to be approved by cabinet ensures indirectly for the board to be composed of persons who support the Government. This often leads to the boards lacking objective and independent

judgment. Such boards are compromised in that they fail to adhere to professionalism. If they try to adhere to their professionalism, they are threatened with loss of their jobs as was seen when Mr Chitundu, then ZESCO Managing Director was threatened by the Government and made to compromise his professionalism by signing an IRU which was clearly disadvantageous to ZESCO. It has been equally established that the Government usually usurps the powers of the board when it comes to appointment and removal of Managing Directors.

Furthermore, it has been established that the interference in management of parastatals is sometimes done by various responsible Ministers issuing directives and statements to these parastatal. The legality of these directives is of great concern. The legal position is that these statements have no force of law as long as they do not comply with the legal requirements. The *case of Edgar Hamuwele*⁵ has been a landmark decision in establishing the legal status of Ministerial statements in the management of parastatals. The case established that Ministerial statements and directives have no effect whatsoever and cannot prevail over the legal requirements.

In light of the above conclusion, the author makes the following recommendations.

4.2 Recommendations

The State should provide legal machinery through which the OECD guidelines on corporate governance in parastatals can be incorporated. These guidelines should be made binding on parastatals. This recommendation can minimize the unnecessary interference of the State in the management of SOES.

⁵ SCZ Judgment No 4 of 2010

In addition, in furtherance of one of the OECD guidelines on corporate governance in parastatals which is that the board of directors should be composed in such a way that they exercise independent and objective judgment, the appointment of parastatal boards should not be left to the State. The appointment of these directors should not be subject to approval by cabinet to minimize the composition of the board being politically affiliated. Instead the persons nominated by the various bodies that are required to nominate persons for appointment to the respective parastatal boards should not pass through the cabinet vetoing process. The names should be automatically accepted by the Government. If the foregoing mechanism of appointing the boards is not used, then the nominees should be subjected to approval by Parliament. This however can also lead to appointment to boards of politically affiliated persons if the ruling party forms the majority in Parliament.

Another recommendation that would be useful in minimising the interference by the State in the management of parastatals would be to have an impartial body composed of experts approved by Parliament whose mandate should be, on behalf of the people of Zambia, to review the governance of parastatals periodically and see if there has been unnecessary interference from the State which is prejudicial to the parastatal. If there is any unreasonable irregularity discovered as a result of the interference, the state should be made liable for the loss incurred by the parastatal.

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