Mr Moyo/fs

5 July 2006

The Coordinator
Governor's Appeals Panel
Reserve Bank of Zimbabwe
Samora Machel Avenue
**HARARE**

**ATTENTION: MR A J MANASE**

Dear Sir

**SUGGESTIONS FOR IMPROVEMENT OF BANKING LEGISLATION IN ZIMBABWE**

You requested me to make recommendations for improvement of banking laws.

Unfortunately, I have not had an opportunity of making appropriate consultations. I returned from West Africa nine days ago. My programme has been very congested. Accordingly, the views expressed in this letter must be treated as my personal views. They are not the views of any organization I may be associated with. Although I would have liked to have consulted widely within the Sadc region and to have been in a position to express the views of the Sadc Lawyers Association, time does not allow me to do so. You will, however, be pleased to know that from the 23rd to the 26th of November this year, Sadc Lawyers Association shall be hosting a conference during

which issues such as the rightful role of central banks, harmonization of financial laws, obstacles to the creation of a single currency, financial laws and human rights are likely to be debated during one of the main sessions. Obviously, the views of practitioners in banking law and regulation are likely to be expressed during that session. An invitation is likely to be extended to the Governor of the Reserve Bank and legal officers such as yourself.

Furthermore, during the period 17th to 22nd September this year over 3000 lawyers, many of them experts in corporate and banking law will meet in Chicago under the auspices of the International Bar Association to discuss, among other things, matters relevant to banking law and regulation. The views to be expressed during that important Conference may be relevant to the work you are doing. Early this month, I sent brochures for that Conference to your colleagues Fortune Chasi and Jean Maguranyanga.

All things considered, I think the time allowed for collection of views in this important matter is too short. I would, therefore, recommend that the time be extended. An extension will allow for wider consultations.

It is important to emphasize that recommendations made are not at all meant to reflect on the conduct of any person. In common with any law reform recommendations, they are aimed at trying to achieve pre-determined future guarantees. Obviously, they have in mind future players whose conduct may turn out to be less predictable than the players we know.

I understand that an opportunity will be given to us to raise in greater detail and clarify some of the representations during the course of next month. I propose to take full advantage of that occasion. In the meantime, regarding the Banking Act, the Reserve Bank of Zimbabwe Act, the Bank Use Promotion and Suppression of Money Laundering Act and the main Exchange Control Regulations, I make the following observations:

**FUNDAMENTAL RIGHTS**

1. Banking legislation should be made consistent with the Declaration of Rights contained in the Constitution of Zimbabwe. As is provided for in Section 3 of the Constitution if any other law is inconsistent with the Constitution, that law shall, to the extent of the inconsistency, be void.

2. Under Section 16 of the Constitution, no property may be compulsorily acquired except where:

   2.1 a law is put in place which authorizes the compulsory acquisition; and

   2.2 the acquisition is necessary in the interests of interests enumerated in the Constitution; and

   2.3 the law authorizing acquisition requires the acquiring authority to give reasonable notice of an intention to acquire the property or interest or right in the property to any person owning the property or having an interest or right in the property; and

   2.4 the law authorizing the acquisition of property provides for fair compensation before or within a reasonable time after the acquisition of the property or interest or right in property; and

2.5 the law requires the acquiring authority to apply to the High Court for a confirming order not later than 30 days after the acquisition where the acquisition is contested; and

2.6 the law authorizing the acquisition enables any person whose property has been acquired to apply to the High Court for a prompt return of the property if the Court does not confirm the acquisition; and

2.7 the law enables the claimant for compensation to apply to Court for determination of any question relating to compensation.

3.1 Except for situations where specific exclusions are made in it, such as exclusions dealing with agricultural land, section 16 covers all seizures of property or all forms of compulsory possession of another's property as will be evident from the fact that some forms of possession of another's property, falling short of acquisition of ownership, meant to be exempted from the ambit of Section 16, are specifically provided for in Section 16 as exceptions. It would not have been necessary to provide for such exceptions if Section 16 did not cover the compulsory taking of the possession of another's property.

3.2 It is, furthermore, apparent from the fact that administrators of deceased estates, those who administer property in the interests of public order, those who take possession in terms of schemes of arrangement are specifically catered for in Section 16 that even the taking of compulsory possession of another's property is covered by Section 16.

4. Accordingly, seizures necessitated by the placing of a financial institution under the control of an administrator and the placing of a financial institution under curatorship ought to be done in terms of a law that complies with the requirements of Section 16. The provisions relating to the seizure of a financial institution and placing same under curatorship do not comply with the requirements of Section 16 particularly in that:

4.1 the Banking Act deals with purposes which go beyond the interests enumerated in Section 16;

4.2 the Banking Act does not make it mandatory, in all cases, to give reasonable notice of an intention to take possession the institution;

4.3 the Banking Act does not require the acquiring authority to apply to the High Court for a conformation order;

5. Consequently, the Banking Act requires amendment to ensure that the Reserve Bank of Zimbabwe is obliged to apply to the High Court for a confirming order within 30 days of the seizure or curatorship of a financial institution.

6. No reconstruction or reorganization or rearrangement of a financial institution under curatorship should take place without the consent and approval of at least 50% of the shareholders and where the reorganization or reconstruction or rearrangement is done by shareholders it should not take place without the approval of at least 75% of the creditors.

7. As was correctly observed by the Supreme Court, a curator's powers are akin to those of a judicial manager. He has no authority to dispose of the assets of an institution under curatorship except in the ordinary course of the institution's business. The Supreme Court's interpretation of the law is consistent with Section 16 and the law governing disposal, by a judicial manager of assets under judicial management. To give effect to Section 16, the Banking Act requires a prohibition against disposal, by a curator, of the assets of an institution under curatorship without the consent of its shareholders and creditors. This will have the added advantage of bringing the concept of curatorship closer to the tried and tested concept of judicial management.

8. Comparative Assessment

8.1 The Gambian legislation provides for judicial supervision of the process of curatorship which they refer to as possession of the financial institution by the Central Bank and ensures involvement of interested parties such as creditors and shareholders and directors through the Registrar of the High Court at critical stages of the process.

8.2 Where the Central Bank decides to embark on a reorganization, referred to in our jurisdiction as a reconstruction, the Central Bank is required to give all interested parties a reasonable opportunity of being heard and there is provision for creditors and depositors constituting a third in value of deposits and claims rejecting the reorganization. The organization can,

furthermore, be defeated by depositors and other creditors on the basis that it is inequitable or that its execution is undesirable.

8.3 Under Mauritian legislation, it is significant that a curator is treated and referred to as a "conservator" to emphasize the duty to conserve rather than dispose of the assets of the institution. Furthermore, a reconstruction or rearrangement cannot take place without the participation of interested parties. The conservator is required, to afford a hearing to all interested parties and propose a plan of reorganization. The approval of a conservator's plan of reorganization is subject to it being equitable to depositors, creditors and shareholders among other factors.

8.4 Under the South African legislation, a curator is subjected to the normal requirements of the Companies Act regarding his conduct. A scheme of arrangement or reorganization under the South African Companies Act requires the active involvement and consent of a significant percentage in value of interested parties as is the case under our Companies Act. Furthermore, even with the consent of interested parties, a curator cannot dispose of the assets of the institution under curatorship except in the ordinary course of the conduct of its business.

9. Furthermore, the powers of a curator require regulation to ensure that:

9.1 an institution, which cannot be run without a minimum of 5 directors is not placed under the control of one person.

9.2 the ability of shareholders and directors to challenge actions of the curator is not made dependant on authorization by the curator.

10. The ideal situation is one whereby the curator is imposed as an advisor or supervisor of the board of directors of the institution under curatorship.

11. There should be a requirement for qualifications of a curator. In particular, a curator should have experience, knowledge and qualifications relevant to the predominant business of the financial institution under curatorship. Most jurisdictions appear to impose this requirement.

## 12. APPEALS AND FUNDAMENTAL RIGHTS

The provisions relating to hearing of appeals against decisions of curators by the Reserve Bank contravene Section 18 subsection 9 of the constitution which requires that every person be afforded, in the determination of the existence or extent of his rights, a hearing by an independent and impartial court or other adjudicating authority established by law. The requirement of an appeal to the Reserve Bank requires removal from the Banking Act in order to ensure compliance with Section 18 subsection 9 of the Constitution. Alternatively, it may be necessary to establish a review board similar to that established by the South African Banking Act to deal with situations where a party is aggrieved by a decision by the Registrar of Banks in that country, such as a decision to decline to issue a banking licence. In that situation, the South African Act provides at Section 9 subsection 2 for a permanent review board appointed by the Minister and chaired by a lawyer. The board has two other members. One of the two members has to be an accountant and

auditor registered in terms of the South African Public Accountants and Auditors Act.

## 13. ANTI MONEY LAUNDERING AND FUNDAMENTAL RIGHTS

13.1 At the outset, it must be observed that the worldwide drive against money laundering is a welcome initiative as it is rooted in the fight against terrorism, drug trafficking, and corruption, evils which no society can afford to tolerate.

13.2 However, the recording, disclosure and reporting obligations contained in Sections 24, 25, 26, 27, 28 and 29 of the Act have given rise to difficulties. The general view is that those provisions, insofar as they seek to impose, on legal practitioners, the obligations referred to above, are inconsistent with the Declaration of Rights and are, consequently, unconstitutional. In America, similar legislation, in deference to attorney and client privilege and confidentiality, exempts lawyers from recording, disclosure and reporting obligations. In Canada, after an initial attempt to include lawyers and which attempt triggered litigation in various parts of the federation of Canada the government agreed to exempt lawyers from the ambit of the legislation. In France, the legislation is applied to lawyers in consultation with the Law Society. However, in France, as in other parts of Europe such as Belgium, Poland and Germany, the legislation is currently being challenged insofar as it seeks to impose recording, disclosure and reporting obligations on lawyers.

13.3 The following issues have arisen from the arguments raised in various jurisdictions including Zimbabwe.

13.3.1 In a democratic society, lawyers should not be placed under any obligation to disclose anything communicated to them by their clients in their professional capacity. Attorney and client confidentiality is one of the pillars of an effective administration of justice. Both attorney and client privilege and attorney and client confidentiality are critical, the observance of the requirements for a fair trial. Our legislation seeks to protect attorney and client privilege only in limited circumstances. It does not at all protect attorney and client confidentiality. Accordingly, it interferes with the right to a fair trial.

13.3.2 In imposing disclosure and reporting obligations on lawyers in relation to information in respect of which they are under a duty to observe confidentiality, the legislation imposes the consequence of searches on lawyers. Instead of an officer undertaking a positive obligation of searching, the law enforcer merely takes the passive role of ordering the lawyer to disclose information and report information given to him by his client. Consequently, the legislation imposes the consequences of a search without any judicial supervision. It interferes with the right to privacy.

13.3.3 By compelling lawyers to record information not necessarily for the benefit of their clients but for reporting to authorities, at the expense of their clients, the legislation compulsorily conscripts lawyers into law enforcement. In a democratic society, the separation between law enforcement and defence is critical for

the observance of the cornerstones of criminal justice and fair trial.

13.3.4 By turning lawyers into spies against their clients, the legislations undermines the legal profession. It makes lawyers untrustworthy in the eyes of their clients. This discourages full disclosure. Full disclosure to lawyers is traditionally accepted to be something in the interests of an effective administration of justice and a fair trial.

13.3.5 The Supreme Court has already held that interception of communications between lawyers and their clients which discourages full disclosure by clients to their lawyers violates the right to freedom of expression in a manner which cannot be justified in a democratic society. The recording, disclosure and reporting obligations contained in the Bank Use Promotion and Suppression of Money Laundering legislation, insofar as they relate to lawyers, have exactly the same effect.

13.4 I may state that America and Canada, which have agreed to exempt lawyers, may be more attractive destinations for dirty money than Zimbabwe. No drug dealer will find it attractive to bring money into Zimbabwe taking into account our strict exchange control restrictions. Our problem is that of money leaving Zimbabwe or money not coming to Zimbabwe. We have no evil of dirty money being laundered in Zimbabwe. Our emphasis should be on trying to access our looted resources which are currently being held outside the country and bringing them back into our country. Zimbabwe does not appear to be under any

visible threat of a terrorist attack. Consequently, there is no justification for us having legislation that goes beyond the legislation of countries that are under a real danger of a terrorist attack.

13.5 I therefore recommend that:

13.5.1 Paragraph 3 to the third schedule to the Bank Use Promotion and Suppression of Money Laundering Act be repealed.

13.5.2 The Legal Practitioners Act Chapter 27:7 be amended so that money laundering by any legal practitioner may be classified as dishonorable and unworthy conduct by a legal practitioner to discourage any abuse of trust accounts by legal practitioners.

## 14. IN DUPLUM

Although I do not agree with the Justice Smith's Panel's conclusion that the *in duplum* rule did not apply to loans by the Central Bank, I do agree that a hyperinflationary environment reduces the application of the *in duplum* rule to any loan, whether by the Central Bank, a commercial bank or any other lender to something of an absurdity. The situation requires legislative intervention. The rule should be repealed for all, not just the Central Bank. It being a common law rule, it should be repealed by an act of Parliament. Where inflation levels are as high as 1 200% per annum, the *in duplum* rule is breached within one month. That effectively kills all lending business as no institution can lend if the effect will be to lose its capital. Furthermore, to say that the *in duplum* rule does not apply to the loans by the Central Bank but

applies to other financial institutions is to ignore the fact that one cannot control the price charged by the retailer without controlling the price charged by the wholesaler. The opinion by he panel ignores the fact that Central Bank, being the formulator of monetary policy, is able to influence the operating environment and levels of interest rates. Other players do not have a similar advantage and power. The *in duplum* rule should be repealed without exception by legislative intervention. In Zimbabwe, there is no evidence of its consistent application between 1890 and the now famous Gillespie judgment in **CBZ LIMITED and M M BUILDERS AND SUPPLIERS (PRIVATE) LIMITED** of 1996 Vol. 2 Z.L.R. page 420. That case relied heavily on ancient authorities. Few will require persuasion to appreciate that in the abnormal environment obtaining in Zimbabwe today, there is need for legislative intervention to repeal the rule. Indeed, when the Money Lending and Rates of Interest Act was enacted in this country, the legislature did not see it fit to include the *in duplum* rule. It was introduced by judicial activism and the need to restate Roman Dutch Law as it existed in Roman times taking into account modifications which took place in the Netherlands during times far removed from the situation obtaining in present day Zimbabwe.

The need for legislative intervention to repeal the *in duplum* rule was recognized by the South African Law Reform Commission as way back as 1974 and in 1991, the South African Appellate Division observed that it was not the court's function to abolish the rule. It observed that it was for the legislature to do so [See **LTA CONSTRUCTION BPK v ADMINISTRATUER, TRANSVAAL**. Although the judgment is in Afrikaans, the head note is sufficiently instructive. Furthermore, in **SANLAM LIFE INSURANCE**

**LIMITED v SOUTH AFRICAN BREWERIES LIMITED** 2000 (2) SA 647, Mr Justice Blieden aptly observed that: "**Bearing in mind the commercial and economic exigencies which apply in a modern business world, it seems to me that the effect of the *in duplum* rule should be confined rather than extended. The opprobrium which attaches to money-lending transactions in Roman law and Roman-Dutch law to a large measure no longer applies. In modern commerce the moneylender is now normally a bank or similar financial institution whose honesty and integrity is not in question. Money lending as a means of affording financial assistance constitutes the very lifeblood of modern commerce, enabling parties with initially insufficient capital to build up profitable and successful business ventures which they would not have been able to do without the assistance of the loans granted to them. In modern societies, as opposed to the societies which prevailed in ancient and medieval times, maximum interest rates are normally controlled by central banks established by the State. In the business world of today the rate of interest charged on any transaction depends on principles of supply and demand rather than the so-called 'moral' considerations which applied in times past. It could be argued with some force that the effect of the *in duplum* rule in modern commerce is to provide a legal means for the dishonest debtor to escape his obligations to comply with what he has agreed to pay rather than to alleviate the plight of overburdened debtors**."

Zimra recently obtained a statutory exemption from the *in duplum rule*.

15. **THE RIGHT TO MAKE REPRESENTATIONS**

15.1 The current Governor has been good at consulting Chief Executive Officers of financial institutions. Furthermore, the idea of an advisory committee is good. A good law should, however, be designed with the possibility of undesirable people taking control. In Mauritius, the first transparency duty of the Central Bank is, in the conduct of its operations, to promote open discussion and comment on its monetary and financial stability policies. [See Section 33 subsection (1) of the Bank of Mauritius Act of 2004]. As a statutory body, the Reserve Bank of Zimbabwe has an obligation to consult and give an opportunity to make representations, all persons who may be adversely affected by any measure it proposes to take and all persons who have a legitimate expectation of being consulted. That rule of natural justice has been given statutory recognition in Zimbabwe. [See Administrative Justice Act].

15.2 The worldwide trend towards democratic institutions and reduction of concentration of power has caught up with financial regulators as well. Monetary policy can produce far reaching consequences for financial institutions, business entities and indeed the public in general. In recognition of the power vested in those whose duty it is to formulate monetary policy, other statutes (in Southern Africa the Bank of Mauritius Act) provide for a statutory Monetary Policy Committee chaired by the Governor of the Central Bank but providing for other apolitical persons with recognized experience in the field of economics, banking or finance who are appointed by the Minister. The formulation of monetary policy

begins with such committee and its recommendations to the Board of the Central Bank. The committee provides such underlying research papers as may assist in the better understanding of its recommendations and findings. The Board of the Central Bank is responsible for publication of the recommendations submitted to it by the Monetary Policy Committee and the Monetary Policy determined by the Board following recommendations by the Committee. The current Governor must be commended for establishing some advisory body. It does not, however, have any statutory recognition or authority. Furthermore, there is no opportunity to critique its findings, research and recommendations.

## 16. ENTRENCH INDEPENDENCE OF MONETARY AUTHORITIES

15.1 The modern trend with respect to regulatory agencies is to ensure their independence and impartiality by proscribing a number of activities. Direct participation in the market is one such activity. As a result, one finds that Central Bank statutes:

16.1.1 limit the depositors the Central Bank may accept deposits from;

16.1.2 limit the entities it may make advances to;

16.1.3 limit its ability to acquire any interest in any commercial, agricultural, industrial or other undertaking.

16.2 Indeed, there is an incongruity in that whereas our act limits the Central Bank's underwriting activities, it does not impose any limitation on its lending and other activities.

## 17. SILENT PARTNERS AND HOLDING COMPANIES

17.1 The Banking Act requires a prohibition prohibiting allotment or issue or transfer of shares to or registration of shares in the name of any person other than the intended beneficial shareholder. Obviously, an exception for unit trust trustees, executors, administrators of insolvent estates, liquidators, central securities depository and, on a short term basis, stockbrokers, will be necessary if this recommendation is adopted. The South African law is a useful example in this regard.

17.2 A holding company is not a banking institution and therefore not governed by the Banking Act. In theory therefore a holding company can have as subsidiaries a banking institution and non-banking company, that is, a non-banking company can be a sister company to a banking institution. This defeats the spirit and objective of Section 34.

## 18. FURTHER RESTRICTION ON DIVIDENDS

The issue of bonus shares out of profit should be treated as a payment of a dividend for the purposes of restrictions on payment of a dividend. This is now a standard supervisory requirement in developed jurisdictions.

## 19. CUSTOMER'S DUTY TO REPORT UNAUTHORISED CONDUCT

The Banking Act requires a section dealing with customers' duties to report unauthorized conduct in relation to operation of his account particularly unauthorized signature or alternation. Where the customer fails to make such a report, he should be prevented from asserting, as against the bank, the unauthorized signature or alteration on any cheque or other instrument paid in good faith by the bank.

## 20. ABANDONED FUNDS

There is a surprising absence of provisions dealing with abandoned funds in the Banking Act.

## 21. OMBUDSPERSON

There is a need therefore for an ombudsperson for the banks including the Reserve Bank of Zimbabwe. (See South African, Botswana and Mauritius).

## 22. COMPOUNDING

Mauritian banking laws authorize, with the concurrence of the director of public prosecutions, the compounding of any offence with the Reserve Bank in respect of an offence committed under the Mauritian Banking Act as long as the offence is prescribed as compoundable where the offender agrees in

writing to pay such amount not exceeding the maximum penalty specified for the offence, as is acceptable to the Central Bank. An agreement to compound is final and conclusive on payment of the amount. No further proceedings in regard to the offence may be taken against the person who will have agreed to compounding. A similar provision in our Banking Act would held resolve matters expeditiously and furthermore facilitate resolution of matters involving bakers who left the country.

## 23. BEARER CHEQUES

Something ought to be done about the fact that bearer cheques are neither bank notes nor negotiable instruments as defined by law. Already persons caught trying to smuggle them out of Zimbabwe have been acquitted by the Courts on this basis.

## 24. EXCHANGE CONTROLS

Exchange Controls of 1977 as revised in 1996 are out of date. Liberalizing exchange markets in general appears to me to have obvious benefits. Clearly, exchange controls are not producing the desired effect. Foreign exchange shortages continue. The Zimbabwean dollar has three different values depending on the market. Huge distortions and potential for corruption have emerged as a consequence of the different exchange rates. Liberalization will bring to an end the black market. It will allow the Zimbabwe dollar to find its true value. Currently, it has been heavily devalued by, among other things, its unavailability on the official markets. It will

decriminalize ordinary commercial activities, create an incentive for people to bring money into the country and encourage investments. No normal investor will invest money without being certain that he will be able to receive his return in his usual country of residence.

25. There is a need for provisions requiring that a reasonable notice be given to the Bank in the event of adverse changes in conditions of banking such as statutory reserve amounts, capital levels and accommodation rates.

## 26. INSOLVENT TRADING

There is a need for a provision to the effect that a director, officer or employee of a financial institution who knows of the insolvency of an institution and who receives or authorizes the acceptance of a deposit from any person without first advising such person of the insolvency of the institution shall be criminally liable. (See Gambian and Section 47 of Botswana's legislation).

## 27. ELECTRONIC BANKING

There is a need for provisions regulating electronic banking with a view to ensuring that measures are put in place to protect customers and other financial institutions from criminal activities and from violation of their rights to privacy. [Mauritian legislation has elaborate electronic banking provisions].

## 28. STANDARDS OF GOOD ADMINISTRATION

I believe that a section in the Reserve Bank of Zimbabwe Act similar to Section 62 of the Bank of Mauritius Act of 2004 would complement the Reserve Bank of Zimbabwe's efforts to promote investor confidence. That section provides that:

28.1 "(1) That Bank shall –

(a) use the powers given to it under the banking laws equitably and uniformly and in accordance with sound administrative practices; and

(b) refrain from using any such power to serve an objective for which the power was not given or in excess of what shall be required to achieve the objective for which the power was given.

(2) Every decision of the Bank taken pursuant to banking laws shall be -

(a) impartial;

(b) motivated only by objective and rational considerations; and

(c) executed with fairness and restraint.

I look forward to hearing from you regarding the suggestion that there be a time extension and the collection of oral representations.

Yours faithfully

**STERNFORD MOYO**