

AN ADVISORY BRIEF TO

HIS EXCELLENCY, THE PRESIDENT OF THE

REPUBLIC OF ZIMBABWE

CDE R. G. MUGABE

ON THE RECOMMENDED WAY FORWARD

ON THE SMM HOLDINGS (PRIVATE)

LIMITED (SMM) CASE

BY

DR G GONO

GOVERNOR

RESERVE BANK OF ZIMBABWE

14 MAY 2009

1. INTRODUCTION AND BACKGROUND

1.1 Your Excellency, this **Advisory Brief** seeks to highlight pertinent review points on the SMM case that are recommended to form the basis for **a resolute way forward** on this long outstanding matter.

1.2 The advice being proffered herein is based on the following imperatives:

(a) The Reserve Bank has meticulously reviewed the core basis upon which the charges against Mr. M Mawere were leveled by the State;

(b) We have thoroughly reviewed explicit documentary evidence and the extent to which it corroborates or diminish the charges and the application of the company **Reconstruction Law**;

- (c) Based on information available, the Bank has also tested the veracity of the declaration of SMM as **“an Insolvent State-Indebted Company”** upon which the Reconstruction Law was created and applied;
- (d) The Bank has also reviewed the various paper trails, covering court testimonial scripts, correspondence between parties and loan agreements relevant to the case; and
- (e) We have also sought to check if there are no conflicts of interest between Government’s overall objectives and the interests and activities of the current Administrators running the affairs of the company under the Reconstruction Programme.

1.3 Your Excellency, in the interest of brevity, I summarise below the main factors that merit Your consideration in shaping the way forward on this matter.

2. VALIDITY OF THE CLAIM THAT SMM WAS “AN INSOLVENT STATE INDEBTED” ENTITY AT THE TIME GOVERNMENT TOOK OVER ITS CONTROL

2.1 Your Excellency, having gone through the availed documentation, and the facts that prevailed on the ground at the time this matter arose, the Bank has come to the following conclusions on the various critical points:

WERE SMM LIABILITIES LEGALLY LOANS BY THE STATE?

2.2 Court records and proceedings of the matter indicate that the issuance of the Reconstruction Order on SMM was based on the following liabilities:

- a) A debt of Z\$396 million in respect of a commercial bond issued by the MMCZ whose proceeds were used by SMM;
- b) An RBZ PSF loan totaling Z\$30 billion, disbursed in two tranches, Z\$20 billion on 24 May 2004 and Z\$10 billion on 17 August 2004;
- c) A debt of Z\$8.2 billion owed to ZESA;
- d) A debt of Z\$252 million owed to the National Social Security Authority (NSSA); and
- e) A debt of Z\$39.9 billion that was due to ZIMRA.

2.3 Your Excellency, at law the above SMM liabilities at the time the **Reconstruction Order** was instituted did **not qualify as state loans to SMM.**

2.4 The RBZ's Productive Sector Facility (PSF) loans, MMCZ's loan, ZESA bills, NSSA bills and ZIMRA bills, whilst they could be linked to the State indirectly by extrapolation, were nevertheless still **debts between SMM as a legal entity and each one of these institutions in their own right as creatures of statutes,** and not directly the State.

2.5 In other words, the parastatals and the Reserve Bank are at law separate legal persons who can borrow, lend, sue and can be sued independent of the State.

2.6 Another pertinent point to note is that the law provides that before a creditor can degenerate the matter of outstanding liabilities of the debtor to liquidation or judicial management procedures, **first there must be documented proof of formal demands for settlement** by creditors who are owed the money.

2.7 In the SMM case **these were not done**, but rather the State spontaneously took over the matter and declared that it was owed money by SMM and had to apply Reconstruction procedures.

2.8 Your Excellency, it is fact that Government had as its main motivation the objective of ensuring that the companies under SMM did not collapse, which if allowed to happen could have led to adverse ripple effects in the economy, but the

manner in which the **“indebtedness to the State”** clause was deduced **did violate the law of contracts which recognizes the precise two or more parties to a specific contract** and not those of extrapolation.

2.9 In this case, the **creditor-debtor relationship** lied between SMM and the individual entities that were owed money, and not the State as erroneously advanced.

2.10A further complication that I see weakening the State’s **moral, constitutional and legal standing** is that the loans provided to SMM **were never triggered by any formal contract between the State and SMM.** The State has to this date **failed to produce** any such direct contract.

INSOLVENCY OF SMM

2.11 Your Excellency, at law, **insolvency declaration** is a **diagnostic conclusion** that has to be preceded by **minimum procedural steps** that do not only involve **notification** of shareholders, creditors, debtors and other related parties, but also impels the holding of actual **judicial hearings** to assess the material facts and financial data of the company, as to be able to **factually determine and conclude** the existence and degree of such insolvency.

2.12 In the case of SMM, it is fact that the verdict of insolvency was arrived at through a unilateral decree by the Hon. Minister of Justice, Legal and Parliamentary Affairs, **with neither notifications to the relevant parties nor the conduct of urgent judicial proceedings to**

collate the facts as to confirm and conclude that insolvency was indeed the status quo at that time.

2.13 The State's contention, therefore, that SMM was **"an insolvent State-indebted entity"**, in the Reserve Bank's opinion is **not correct**, implying that the application of the Reconstruction Laws was, **with the benefit of hind-sight, inappropriate.**

2.14 The issue here Your Excellency is not about opinions on what people saw as the allegedly weak financial status of SMM at that time, but rather materially that the procedures for insolvency declaration and the criteria for the determination of "loans by the State", were **grossly violated. This seriously weakens the State's standing in this matter.**

2.15 As things went, and as things stand, the State is, therefore, **exposed** to the risk that the investor community may conclude that **the letter and spirit of property rights, human rights and company law is not being followed** in so far as the rights of shareholders, debtors, creditors, employees and any other relevant parties are concerned. **This is not good for Government's and the country's image, Your Excellency.**

2.16 Your Excellency, the above findings and conclusions have far-reaching implications in that the State could very well have fallen victim to **emotions having reigned supreme** against the wisdom of following proper procedures in certifying debtor-creditor relationships in the SMM case and the manner in which insolvency was to be checked and certified.

ALLEGED EXCHANGE CONTROL VIOLATIONS

2.17 Your Excellency, in respect of Exchange Control matters, the State is making the following allegations against Mr Mawere:

2.18 Quite to the contrary, the Ministry of Justice, Legal and Parliamentary Affairs blazed ahead with the application of Reconstruction Laws where in essence they were not applicable.

(a) That in June 2003, Turnall Zimbabwe, an asbestos company exported merchandise worth US\$50,000.00 and ZAR22,000,000.00 whose amounts were not remitted to Zimbabwe at the time the case was under consideration;

- (b) That the asbestos was exported to Southern Asbestos Sales of South Africa (SAS) which in turn exported to Plex, United Kingdom;
- (c) That in December 2003, accused exported agricultural products worth US\$1,212,702.54 and this amount was not remitted to Zimbabwe at the time the matter was being considered. All products were exported through a South African company known as Southern Cotton Sales (Pty) Ltd;
- (d) That at the end of March 2004, accused had US\$18,464,595.27, CAD\$628,071.84 and ZAR4,515,367.48 in his accounts outside Zimbabwe which was supposed by then to have been repatriated to Zimbabwe;

- (e) That by establishing and running SAS, United Kingdom without authority from the Reserve Bank of Zimbabwe (“RBZ”), Mawere violated the Exchange Control Act, Chapter 22:05;
- (f) That on 20 February 2004, Mr Mawere transferred US\$150,000.00 from SAS South Africa to an account detached from SMM. It is further alleged that on 19 March 2004, he transferred US\$210,000.00 from the same account in South Africa to the same account in the United Kingdom; and
- (g) That had several places of abode in several countries which we are yet to identify.

2.19 Your Excellency, deliberations at the courts on these allegations have not been conclusive, as the State could not provide evidence **beyond**

reasonable doubt that the relevant amounts as alleged had been banked offshore with the express intention never to repatriate them back to Zimbabwe.

2.20 The defence's main thrust was that it was a common occurrence that export proceeds could be past due date in terms of repatriation to Zimbabwe, but it **did not and does not constitute willful externalization.**

2.21 For comparative reference, Your Excellency, on numerous occasions, the Reserve Bank of Zimbabwe published lists of companies and individual exporters who had long-overdue exports that had not been repatriated past the 90-day period, **but never were these companies or their shareholders brought before the courts for externalization.**

2.22 In the SMM case, the Reserve Bank is **happy to drop any Exchange Control related charges, in light of the evidence at hand.**

ASBESTOS AS A HARZADOUS MINERAL...

2.23 Another pertinent point to note is that the marketing arrangements between SMMZ and Southern Asbestos Sales (Pty) Limited (SAS) seem to also find a **legitimate legal defence justification** in that the buyers of the asbestos, itself a hazardous material, **prescribed explicit special packaging and handling standards**, which requirements could be met through technology economically available in South Africa. Legally, this valid argument **casts doubt**

on the State's case that SMM willfully sought to externalize funds through SAS.

2.24 SAS, was, therefore, logically created to establish an economic and effective platform for the requisite repackaging of the asbestos in line with the requirements of the few customers SMM faced.

NATURAL PERSON OF MR M MAWERE VS JURISTIC PERSONA IN THE FORM OF COMPANIES

2.25 Your Excellency, the State seems to have inadvertently made **an error of principle** by failing to distinguish the boundaries of rights and responsibilities for the person of Mr Mutumwa Mawere and those responsibilities for those who

were running with the day to day issues of the SMM group of companies.

2.26 Yes, at law, company directors are Liable to the circumstances of their companies, but in the matter at hand, the State's case seems to have hurriedly bundled all allegations on the lap of the person of Mr. M. Mawere, without documentary proof as to his direct involvement in the SMM day to day dealings, let alone the bulk of the charges leveled against him.

CONFLICT OF INTERESTS

2.27 Your Excellency, the Reserve Bank has also found the following **material grey areas** which seem to have **compromised the entire handling of the SMM case:**

a) Though there is reference to the Fifth Table of the Seventh Schedule of the Companies Act, which sets the payment levels for liquidators and administrators, the fact still remains that Mr Gwaradzimba, the Administrator is getting payments set at **6% of gross proceeds, of all SMM companies** which is even more lucrative than shareholders themselves, let alone revenues to Government. Your Excellency, there is **genuine need for the relevant sections of the Companies Act to be modified.** (see attached summary of relevant sections in the Companies Act). The Administrator's activities also seem to have entrenched interests of needlessly permanently dispossessing all Mr Mawere of his assets.

b) It has also been established that the **Administrator, Mr Gwaradzimba was a**

former auditor of SMM, making him **the least qualified** to vilify SMM financial systems and try to reconstruct the financial fortunes of the company. At best, knowing that he was a former auditor of SMM, **Mr Gwaradzimba ought to have honourably turned down the appointment** by the Minister of Justice, Legal and Parliamentary Affairs. Your Excellency, this **material fact** seems to have been grossly overlooked during the judicial proceedings against Mr Mawere.

- c) It has also been established that Mr Manikai, who presided as one of the legal minds on the SMM issue was **a former legal advisor to SMM**, again making him a less suitable candidate to preside over the SMM matter.

2.28 Your Excellency, **these anomalies do cast doubt and credibility deficits** on the transparency and

integrity of the subsisting control and management arrangements of SMM and how the whole matter was handled.

SELF-SERVING LAWSUITS

2.29 Your Excellency, as I write this Advisory Note to You, there is a matter that is before the High Court seeking to legally declare “culpability” of Mr Mawere, which would have the effect of empowering the Administrator to declare SMM assets to be legally and permanently owned and held by the Government of Zimbabwe. There are also unconfirmed indications that the current Administration team is actively making preparations to either directly or indirectly acquire stakes in SMM.

2.30 Without standing in the way of the competent courts, there is merit for Your Excellency to

allow confirmation and discussion around the various facts I have highlighted above before the decision to permanently transfer SMM assets to Government is taken.

2.31 Doing so would seriously dent Zimbabwe's commitment to the observance of legitimate statutes that sit in our books of law, particularly the constitution itself.

3. RECOMMENDATIONS

3.1 Your Excellency, based on the above pertinent factors, and discoveries, I humbly seek to submit the following decision points for Your consideration:

- a) In view of the fact that Government's bid to acquire SMM's UK Holding company did not go

through, it is recommended that the Reserve Bank of Zimbabwe **immediately recalls the US\$2 million that it had been directed by Government to pay as a deposit.**

b) Against the background of the anomalies and faulty premise upon which the Reconstruction procedures were administered by the Hon. Minister, it is recommended that a **moratorium be implemented to halt any further judicial proceedings that alienates Mr Mawere's assets from him.**

c) Also against the apparent irregularities surrounding the SMM issue, in terms of how due process and procedures were not followed, it is recommended that a **well qualified, independent Review Panel** be appointed to devise an **amicable** way of enabling

Government to **turn back the SMM assets over to Mr Mawere**, accompanied by audited sets of accounts to ascertain the state of affairs at the company.

- d) Also in view of the time now elapsed and the irregularities that have been detected, as well as in view of new information now at hand, it is recommended that **the Reserve Bank lifts and withdraws its earlier charges of externalization**, especially given that the South African entity SAS is under liquidation.
- e) It is also recommended that Your Excellency approve **the de-specification of Mr Mawere and his companies** so as to pave way for **a new beginning**, particularly in the context of investment promotion and empowerment in Zimbabwe.

f) There is need for an urgent realignment in the Companies Act in order to come up with realistic charges for liquidators and administrators. Where an administrator gets 6% of gross proceeds of a company under his/her insolvency salvage operations, as is the case with Mr Gwaradzimba in the SMM case, this creates **intractable conflicts of interest**, as well as further worsening of the struggling companies' financial standing.

3.2 Your Excellency, if one or more of the above recommendations find Your approval, it is also strongly recommended that an **Independent Transitional Board** be put in place, **represented by people other than the current Administrator** to exhaustively work through the

financials of SMM to pave way for an amicable settlement of this long outstanding matter.

3.3 Your Excellency, it is also important to note that bringing this matter to an amicable closure will not only be consistent with Your Excellency's **principled stance** on the need to allow the flourishing of rule of the law, but also will act as a very positive signal to the business community that Government **will best protect their investment interests.**

Thank You

DR G GONO
GOVERNOR

15 MAY, 2009