African Private Equity and Venture Capital Association

AVCA L&R LEGAL & REGULATORY BULLETIN

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LETTER FROM THE CHAIR

Dear Reader,

We were all hoping to re-enter a more "normal" business climate as the pandemic eases off. Yet the COVID tail is long, and now war in Europe threatens markets in unexpected ways.

Notwithstanding an unsettled macro environment, this edition of the LRC bulletin focuses back on the more mundane legal developments over the last several months that affect PE activity on the continent. AVCA is grateful for this edition's many contributors, who have addressed country-by-country changes in merger control, restructuring and venture capital funds, among other topics. The rise and early experience of the Kigali International Financial Centre is certainly one are for us all to watch; will Mauritius finally get a continental competitor?

On a personal note, this is the last bulletin to be published during my time as Chair of the Legal and Regulatory Committee. It has been an honour to work with such a fine group of committee members under the AVCA leadership, and alongside Cindy Valentine as my co-chair for most of my tenure. I wish best of luck to my successors!

Best,
Geoff Burgess

ABOUT AVCA | CHAMPIONING PRIVATE INVESTMENT IN AFRICA

The African Private Equity and Venture Capital Association (AVCA) plays an important role as a champion and effective change agent for the industry, educating, equipping and connecting members and stakeholders with independent industry research, best practice training programmes and exceptional networking opportunities.

With a global and growing member base, AVCA members span private equity and venture capital firms, institutional investors, foundations and endowments, pension funds, international development finance institutions, professional service firms, academia, and other associations.

This diverse membership is united by a common purpose: to be part of the Africa growth story.

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Senior Legal Counsel,
Bpifrance Investissement

Championing Private Investment in Africa

Contact AVCA

37 North Row, Third Floor
London W1K 6DH, UK
avca@avca-africa.org
www.avca-africa.org

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REGULATION OF INVESTMENTS BY PENSION FUNDS AND OTHER INVESTORS INTO PRIVATE EQUITY

Dominic Rebelo (Partner) & Maureen Chepkoech (Principal Associate)
ANJARWALLA & KHANNA

Private equity and venture capital funds ("PEVC funds") domiciled in Kenya, or that wish to raise funds in Kenya, are currently regulated by the Capital Markets Authority (the "CMA").

Recent amendments to the Capital Markets Act in 2020* expanded the remit of the CMA, enabling the CMA to licence, approve and regulate PEVC funds that indirectly have access to public funds in Kenya, with the aim of bringing PEVC funds that access public funds through public bodies and pension funds under the CMA's remit.

The CMA does not currently regulate the investments made by PEVC funds themselves (assuming that they are not made into listed companies or entities specifically licenced by the CMA); however, such investments may fall under other industry-specific regulators in line with their respective statutes and regulations.

As a general premise, investment funds or other entities that pool funds from the public are regulated as collective investment schemes under the Capital Markets Act, and their general partner or other management entity must be licenced by the CMA as a fund manager. General partners or the management entities of PEVC funds that do not fit within the definition of a collective investment scheme remain regulated as either investment advisers or fund managers, depending on the size of the funds under their management.

Pension funds are only allowed to invest in certain specific asset classes, with the proportions of such assets prescribed under the Retirement Benefits (Individual Retirement Benefit Schemes) Regulations, 2000 and the Retirement Benefits (Occupational Retirement Benefit Schemes) Regulations, 2000. Under these regulations, pension funds may invest a maximum of 10% of their assets under management in PEVC funds.

Beyond the restrictions on pension funds, PEVC funds offering securities to the public or a section of the public in Kenya would need to comply with the provisions of the Capital Markets Act and the Capital Markets (Securities) (Public Offers, Listing and Disclosures) Regulations, 2002 (the "Public Offers Regulations"), which require the PEVC fund to submit a prospectus for the CMA's approval prior to making any public offer. The law does not define the term "section of the public" and hence any offer to any section of the public by a PEVC fund for the purpose of procuring investors is caught. That said, the CMA has the power to exempt a public offer from the requirement to submit a prospectus; however, the procedure and requirements for such exemption are not defined, and there is no developed jurisprudence on this point.

In addition, the Capital Markets Act provides for restricted public offers, where a public offer of securities is restricted to sophisticated investors or directly communicated to a prescribed category and number of persons. Where a PEVC fund's offer falls under a restricted public offer, the PEVC fund would be required to submit a short form prospectus to the CMA for approval. While a short form prospectus is a simpler document, it is nevertheless a time-consuming and costly process to pull together.

For a PEVC fund's fundraising activities to be fully exempted from the application of the Public Offers Regulations, the PEVC fund would need to show that the subscription to the fund by Kenyan investors is made pursuant to a private offer. Private offers are not subject to any prior authorisation from the CMA, the disclosure requirements set out in the Public Offers Regulations will not apply and consequently no information memorandum or prospectus need be filed with the CMA. However, the PEVC fund will be required to file an approved information notice with the CMA.

In general, the CMA's mandate is to protect investments made by the wider public and specifically less knowledgeable or sophisticated investors who might invest in a collective investment scheme in reliance on a fund manager's expertise without necessarily having a full understanding of the associated risks.

While a short form prospectus is a simpler document, it is nevertheless a time-consuming and costly process to pull together.

*Act No. 8 of 2020

Drawing the line between investors who need protection and those who do not is inevitably more art than science, especially where offers often cut across corporates and individuals with different income and expertise, but a pension fund operating under its own pensions regulator should not be subject to the same regime. In seeking to define and draw the line between those investors who are sufficiently knowledgeable and those who require a regulator's protection, it is increasingly important for the CMA to work with stakeholders such as the East Africa Venture Capital Association and the African Venture Capital Association, as well as private sector groups to ensure that the development of the existing regulatory framework encourages investment while ensuring public protection when required.

THE AUTHORS:

Dominic Rebelo

Partner

ALN Kenya I Anjarwalla & Khanna

djr@africalegalnetwork.com

Maureen Chepkoech

Principal Associate

ALN Kenya | Anjarwalla & Khanna

mck@africalegalnetwork.com

UBO COMPLIANCE: EMERGING ISSUES FOR PRIVATE EQUITY AND VENTURE CAPITAL FUNDS IN KENYA

Wangui Kaniaru (Partner)
ANJARWALLA & KHANNA

The global wave of increased transparency and disclosure requirements of ultimate beneficial owners ("UBOs") has finally landed on East Africa's shores. In 2020 and 2021, Kenya and Tanzania adopted regulations mandating disclosure of UBOs for entities registered in both jurisdictions. The UBO regulations are far-reaching in their scope and have important operational and tax implications for portfolio companies and investments held by private equity and venture capital investors in the region.

The Kenya regulations came into effect in January 2021 and the compliance deadline was extended to 31 July 2021 due to make time allowance for compliance. The deadline for compliance in Tanzania was extended to 31 December 2021, again due to making time allowance for compliance. The Kenya regulations are at a more advanced stage of implementation and require companies incorporated in Kenya to disclose information on natural persons who are "beneficial owners" of shares. The definition of beneficial ownership is very broad and includes direct and indirect ownership or effective control of legal entities, as well as control arrangements created by off-shore trusts or voting rights agreements.

Beneficial ownership is disclosable in relation to persons directly or indirectly holding at least 10% of the issued shares or voting rights of a Kenyan company. Disclosure also applies if persons have a right to appoint or remove a director of a Kenyan company or if the person exercises "significant influence or control" over the company. Significant influence or control includes the ability to approve annual budgets or other financial or operational requirements of an entity in Kenya, such as strategic plans or borrowings. The broad definition of beneficial ownership means that disclosures are not restricted only to natural persons who are shareholders, but could also include directors and officers of investee companies or other entities within the ownership structure. At present, the Kenyan regulatory regime does not provide distinct rules for foundations, non-profits or partnership structures.

Many such rights exist in relation to reserved matters and pre-emption and governance rights that are standard in most private equity or venture capital shareholder agreements, joint venture agreements or other documentation that often sits offshore and is not immediately available to portfolio companies, which are now required to comply with the UBO disclosure requirements.

> Kenyan portfolio companies need to establish a process of compliance with the beneficial ownership requirements and identify relevant beneficial owners, and consider tax advice in relation to possible thin capitalisation or transfer pricing implications of existing arrangements.

The regulations do not include a carve-out for private equity funds or development finance institutions ("DFIs") and there is no procedure to seek an exemption from disclosures from the Registrar. Complications may therefore arise in cases of private equity funds as it likely to prove impractical or impossible to establish the natural persons who ultimately own or exercise effective control in a private equity fund or a venture capital fund structure.

In addition, the information disclosed to the Registrar is also accessible by the Kenya Revenue Authority ("KRA"), raising potential tax compliance risks where a Kenyan company is ultimately controlled by a non-Kenyan beneficial owner but is presented as being controlled by a Kenyan tax resident, and the Kenyan company has not recognised that it is thinly capitalised (by virtue of being foreign controlled). Furthermore, it will now be possible for the KRA to identify transactions involving a Kenyan entity and an offshore related party, especially bearing in mind that Kenya has recently ratified the Common Reporting Standards and is expected to start participating in the automatic exchange of information imminently.

A Kenyan company has responsibility to investigate and obtain particulars of its beneficial owners. Failure to comply would lead to potential criminal and financial penalties being imposed on the company and its officers. The regulations provide for stepped-up escalation for the company to identify its beneficial owners, and failure to respond to requests for information could ultimately lead to restrictions being imposed on the relevant shares, voting rights or appointment and removal rights of the affected person. As a practical matter, the digitization of company's statutory records in Kenya has meant that the system is configured in a way that restricts a company's ability to update any statutory records, unless its beneficial ownership register information is up to date.

Kenyan portfolio companies need to establish a process of compliance with the beneficial ownership requirements and identify relevant beneficial owners, and consider tax advice in relation to possible thin capitalisation or transfer pricing implications of existing arrangements.

THE AUTHOR:

Wangui Kaniaru

Partner

ALN Kenya I Anjarwalla & Khanna

wk@africalegalnetwork.com

TRENDS EMERGING FROM KENYA'S INSOLVENCY REGIME

Sonal Sejpal (Partner) & Wangui Kaniaru (Partner)
ANJARWALLA & KHANNA

The evolution of insolvency laws across the world has been aptly described as the "redefinition of insolvency from sin to risk, from moral failure to economic failure"[1] In the United Kingdom, for example, the treatment of debtors has significantly improved since medieval times, when failure to co-operate with bankruptcy commissioners would earn convicted bankrupts the death penalty. Kenya is no exception.

Until the enactment of the Insolvency Act, 2015 (the Insolvency Act), corporate insolvency in Kenya was instinctively regarded as the "kiss of death" for struggling businesses. With the 'once in a generation' overhaul of the insolvency landscape in 2015, Kenya has now adopted a pro-rescue culture, which embraces the possibility of a fresh start for businesses.

Despite the business rescue culture embedded in Kenya's current insolvency regime, the coronavirus pandemic has brought about profound economic challenges that have left many businesses teetering on the edge of failure. So far, this economic upheaval has not been reflected in the number of corporate insolvencies, which remain implausibly low across many jurisdictions, including Kenya. Regulators and other economic experts attribute this state of play to relief packages introduced by countries across the world to prevent mass business failure. It is feared that as the packages continue to be phased out, the artificially low corporate insolvencies may pave the way to a "tsunami of bankruptcies".[2]

Considering the potential spate of insolvencies and the typical economic downturn expected from the approaching electioneering season, private equity (PE) and venture capital (VC) funds with Kenyan investments should have a second look at their investee companies from an insolvency perspective. One of the main areas of concern for investors, especially regarding portfolio companies, is the issue of parent entity liability. There are also macro opportunities in relation to distressed debt or distressed assets, given the continuing economic weakness in the region that is likely to trigger insolvencies across companies and sectors.

PE and VC firms are often concerned about potential exposure to any financial or non-financial liability arising from investee insolvency. In general, Kenyan corporate insolvency is grounded in the concept of limited liability, a fundamental principle of corporate law that a company has separate and distinct legal personality from its directors and shareholders. Save for certain exceptions, shareholder liability in investee insolvency situations is remote, and creditors generally have no recourse to a company's shareholders or owners because of the concept of limited liability, which would also apply to directors in the parent entity.

Nevertheless, directors in the insolvent portfolio company itself should be concerned about potential liability under Kenyan insolvency and company laws. In an insolvency situation, the duty to promote the success of the company shifts to a duty to act in the best interests of the company's creditors. Therefore, directors must be cognizant of their fiduciary and statutory duties, including the duty to protect the investee's assets and minimise potential losses to creditors. Directors should also be aware that there are several offences that a director may potentially be liable for if the company goes into liquidation. These offences, which include wrongful and fraudulent trading, may attach significant liability on directors, including a court order making a director personally responsible to pay the company's debts or the possibility of criminal sanction.

> It is feared that as the packages continue to be phased out, the artificially low corporate insolvencies may pave the way to a "tsunami of bankruptcies".

Moving away from issues facing portfolio companies and their directors but keeping with the rescue culture at the core of the revamped insolvency regime, we have noted increased interest in the viability of pre-pack sales/ administrations in Kenya. The term 'pre-packaged sale' refers to an arrangement under which the sale of all or part of a company's business or assets is negotiated with a purchaser prior to the appointment of an administrator, and the administrator effects the sale immediately on, or shortly after, appointment.

[1] Bankruptcy in the Age of American Independence, Bruce H Mann, 2009, Harvard University Press.

[2] European Financial Supervisor Warns of 'Tsunami' of Insolvencies, Financial Times (28 April 2021). Available at: https://www.ft.com/content/c843dd94-91f7-444d-a3c7-5e0d7dd160d5 (last accessed 29 November 2021).

Pre-pack sales are not regulated under the Kenyan insolvency regime, and as far as we know, none have been successfully attempted in Kenya. The lack of defined guidance on the practice means that insolvency practitioners are unwilling to assume the risk that comes with a pre-pack sale. In addition, Kenya is a highly litigious jurisdiction, meaning that any disgruntled party (e.g., a single unsecured creditor) would be likely to initiate a potentially protracted legal dispute in respect of such a transaction. This would defeat the purpose of the entire process given that cases in Kenya can take up to three years to determine at first instance, with appeals taking much longer.

Another area getting increased attention in light of the COVID-19 economic crisis is distressed debt investing. The economic fallout from the COVID-19 pandemic has also presented a "generational opportunity in distressed debt investing"[3] outside of Africa, with investors in developed markets saying that this is "one of the great environments, possibly, to buy distressed debts that may have ever been in existence".[4] Distressed debt, also referred to as "impaired debt", "sub-performing debt" or "non-performing loans" (NPLs), is debt that "a borrower is unlikely to be able to repay in full to the lender on its maturity date because the borrower is in financial difficulty or in an insolvency process".[5] Distressed debt investing typically involves market participants buying debt for different reasons, including:

- making a quick profit by selling the debt;
- acquiring enough debt to influence the debt or company's insolvency or reorganisation process; or
- getting an advantageous position over other investors in the debtor company, for example, by using loan-to-own mechanisms where an investor purchases distressed debt with a view to converting the debt into an equity stake. The investor then hopes to benefit from any subsequent rise in value in the business.

> Participants in distressed debt markets are diverse and include PE funds, hedge funds and special situation funds.

Participants in distressed debt markets are diverse and include PE funds, hedge funds and special situation funds.

However, distressed assets continue to be largely overlooked as an asset class by investors in the African space. We believe that the limited investor appetite in distressed debt investments is due to a variety of reasons, including the lack of a developed legal and regulatory framework, political risks prevalent in many African countries and investor reluctance to deal with state- and family-owned businesses without strong collateral mitigants.

This has perhaps left the distressed market in Africa at a much more nascent stage compared to other regions.

That said, there is evidence of increased interest from various market participants looking to trade in distressed assets, particularly for businesses that have good business models but are facing significant financial difficulties for various reasons, including the COVID-19 cash crunch. On the continental scene, the International Finance Corporation (through its Distressed Asset Recovery Program (DARP)), partnered with Nimble Group, a South African distressed debt investor, to buy $90 million of unsecured retail NPL portfolios in South Africa, Namibia, Botswana, Lesotho and Eswatini (former Swaziland). There is also real opportunity for blended investment vehicles combining aspects of angel or VC investments with debt investments over a longer period of time than the typical five-year life cycle of investments in a conventional market environment. Hybrid investment vehicles would need a different investment funding structure and more customised time frames, depending on a sector or asset focus that addresses distressed opportunities.

[3] Paul Triggiani, Managing Director and Head of Distressed Credit at Invesco.

[4] Bruce Flatt, CEO of Brookfield Asset Management (see Private Debt Investor Publication: https://www.privatedebtinvestor.com/brookfield-sees-covid-19-creating-one-of-the-great-environments-for-distressed-debt/).

[5] Thompson Reuters, Practical Law, Distressed Debt (see https://ca.practicallaw.thomsonreuters.com/7-381-0310?transitionType=Default&contextData=(sc.Default)&firstPage=true).

Sonal Sejpal (Partner) & Wangui Kaniaru (Partner)
ANJARWALLA & KHANNA

This analysis of the market trends in the distress and recovery space ends on a hopeful note. Kenya's evolving insolvency regulatory framework continues to search for ways to support corporate rescue. For example, Parliament recently passed an amendment to the Insolvency Act to provide for a pre-insolvency moratorium that prevents creditors from taking enforcement actions while a company in financial distress considers its options for rescue. A wider effort to amend the existing Insolvency Act to address gaps and inconsistencies fell victim to the effects of the pandemic, but it is expected that the process to kick into high gear soon.

THE AUTHORS:

Sonal Sejpal
Partner
ALN Kenya I Anjarwalla & Khanna
ss@africalegalnetwork.com

Wangui Kaniaru
Partner
ALN Kenya I Anjarwalla & Khanna
wk@africalegalnetwork.com

RESTRUCTURING DISTRESSED PRIVATE EQUITY PORTFOLIO COMPANIES IN KENYA AND BEYOND – AN OVERVIEW

Vruti Shah (Partner), Kendall Evans (Director) &
Dominic Indokhomi (Partner)
BOWMANS

COVID-19 and other market factors, both local and global, have negatively impacted certain sectors, as well as operating businesses generally. Private equity funds may well have investments in portfolio companies, which may be experiencing near-term (and potentially long-term) declining revenues, liquidity constraints and potential challenges to servicing debt.

Where the business fundamentals of such distressed portfolio companies are sound, there may be a number of restructuring options available to a portfolio company and its fund and other shareholders. However, for a successful implementation of a restructuring option, action must be taken at the earliest stages of distress rather than at a point of no return.

There are three main stages a company goes through when it is in financial difficulty. The first is underperformance; this is where a cash generative business losses profitability. The signs here are subtle, but with close attention, it is in this phase that the company has its best chances to effect a restructuring. The next stage is the distress stage. This is where the business cannot fund any of the company's activity outside its immediate operations and it has difficulty meeting its commitments to its lenders or its trade creditors. Action taken in this period is still useful, though the options and the environment for a successful restructuring may be more limited. The final stage is the crisis stage where the company faces a critical shortage of cash, forcing it to use all of its cash generated by the business to service its debts. By this time, the company is either insolvent or on the brink of insolvency.

What Next if a Portfolio Company is in Distress?

Where the fund's portfolio company may be facing financial distress, as a first step, the fund should consider ensuring that the portfolio company undertakes an independent business review (IBR). The IBR would give the fund and other shareholders and the company itself an indication of the stability of the portfolio company at a given point in time and the financial viability in the short- to medium-term. It will also highlight areas of concern that need to be addressed for the portfolio company to operate successfully. If the results of the IBR reveal areas of concern, then the following options should be considered.

Operational Restructuring

Operational restructuring is the identification of the causes of operational underperformance and the development of a strategy to achieve improvement. Operational restructuring focuses on the profitability of operations. It does not address the capital structure or financing structure of a company.

With most turnarounds, operational restructuring and balance sheet restructuring (discussed below) should be considered together, not independently.

Balance Sheet Restructuring

A balance sheet restructuring refers to the restructuring of components of the business that form part of the reporting on the balance sheet. This is usually implemented by concessions made by debtholders and equity holders of a company in an effort to make the balance sheet stronger. Stronger in this context can mean a number of things but inevitably involves the company having less leverage than it did before.

One element of a balance sheet restructuring could be injection of additional capital to improve cash flow. Liquidity may be injected into a portfolio company by equity or debt.

General Corporate Considerations

Prior to injecting capital, the fund should consider: (i) whether the group/portfolio company can survive on its own resources; (ii) if not, what amount of additional funding should it provide and in what form; (iii) what are the fund's rights and obligations vis-à-vis the portfolio company in this situation, in particular, what do its own fund documents and the specific portfolio company's shareholders agreement (SHA) provide; and (iv) finally, is there a possibility of third-party financing (either a white knight or lender) and what will be the impact on the portfolio company as a result.

Even prior to the above, the fund can look at whether it has fully exercised its appointments at the board level and, if it has not it should ensure it is fully represented on the board in line with its rights in the SHA and consider carefully the composition (and expertise) of the management team. Particularly, a key question for shareholders is whether the management team is sufficient and efficient or should it be streamlined and specialist expertise be recruited.

Even prior to the above, the fund can look at whether it has fully exercised its appointments at the board level and, if it has not it should ensure it is fully represented on the board in line with its rights in the SHA and consider carefully the composition (and expertise) of the management team. Particularly, a key question for shareholders is whether the management team is sufficient and efficient or should it be streamlined and specialist expertise be recruited.

Debt Funding

Where a fund is looking at debt financing as a way to raise capital for its portfolio company, then there are several key considerations that it needs to take into account, including:

- the portfolio company's leverage ratios;
- what are the funding provisions in the SHA? Are there emergency funding provisions? Indeed, as a practice point, a private equity fund should consider including such provisions in the SHA upon its initial investment. The same question is applicable on an equity financing (see below);
- contractual obligations and/or restrictions on incurring additional debt;
- whether any structure of debt financing may be treated as a voidable transactions under insolvency laws; and
- attendant costs related to any proposed structure of the debt financing (and the restructuring of the current debt obligations, if necessary).

Equity Funding

For equity financing, the fund will wish to consider:

- what are the funding options and restrictions for the private equity fund at the fund level?
- are there any emergency funding provisions contained in the SHA (as indicated above, this is something a fund should consider including at the negotiation stage of the SHA and prior to its investment)?
- what are the consequences of dilution if the fund has no more capital to inject into the company or is otherwise restricted from doing so by its fund documents or investment committee?

Portfolio Company's Lenders

Another element of balance sheet restructuring is reducing leverage. This, amongst other options, may be done by way of covenant waivers and resets, debt waivers or haircuts, extended maturity dates, payment rescheduling combined with company led contributions such as non–cash capital contributions or debt for equity swaps for shareholder loans.

It is important that all stakeholders, the portfolio company and its shareholders (including the fund) begin negotiating and discussing the portfolio company's financial situation with its lenders early in the process to ensure that the lenders are part of the process from inception. In this way the lenders are more likely to give some of the concessions discussed above. Generally, financial institutions are reluctant to enforce security unless all avenues for rescuing a company have been explored and, as such, shareholders and the portfolio company itself should ensure early engagement with any lenders is undertaken to maximise lender buy in.

If no white knight can be found and the fund and other shareholders are unwilling to inject capital then some form of consensual or statutory restructuring is inevitable as set out below.

Consensual Restructuring Versus Statutory Process

Any restructuring may be implemented consensually or by using a statutory process. The path to be used would be determined on the facts of each scenario. Where there are fewer key stakeholders and creditors, it is possible to effect a restructuring by consensus of all affected stakeholders. This type of restructuring will require early, honest and open engagement with the company's lenders and other key parties.

However, where there are multitude of creditors, a formal restructuring process would be more of appropriate to effect any restructuring of the portfolio company.

> A key question for shareholders is whether the management team is sufficient and efficient.

RESTRUCTURING DISTRESSED PRIVATE EQUITY PORTFOLIO COMPANIES IN KENYA AND BEYOND – AN OVERVIEW

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What Are the Available Statutory Processes in Kenya?

If it is not possible to effect a restructuring in a consensual manner because the relationships with key stakeholders have broken down or there is a misalignment of stakeholder interests or for any other reason, then it is possible for the private equity fund to consider the following statutory processes to implement any restructuring. We have set out below the processes and options available in Kenya, however, the processes available in other African jurisdictions may vary.

Schemes of arrangement - it is an arrangement carried out between the company and a particular class of members or creditors. In order for a scheme to be effective, it needs the approval of a majority in number of the creditors or members (as applicable) representing 75% in value of those creditors or members. The scheme must be sanctioned by the court and a copy of the sanction order must be filed with the Registrar of Companies in Kenya. This is not an insolvency procedure and can be used by both solvent and insolvent companies.

Pre-insolvency moratorium - this is a procedure that can be used by the directors of eligible companies to obtain temporary protection from creditors, while the company considers a business rescue plan. There is no eligibility threshold for a company to qualify for the moratorium, provided that the applying company is in financial distress. The moratorium will be for a period of thirty (30) days but the court has discretion to extend the moratorium for further thirty (30) days. This process must be supervised by a "monitor" who must be a licensed insolvency practitioner.

Administration - this insolvency procedure allows for the reorganisation of an insolvent company or the realisation of its assets under the protection of an automatic 12-month statutory moratorium. It is conducted by an administrator who must be a licenced insolvency practitioner in Kenya.

Company voluntary arrangements - this is an insolvency procedure that is proposed by the directors of a company which allows a company to satisfy debts owed to creditors by paying only a proportion of the amount that it owes or coming to another arrangement with its creditors for paying back the debt. It is usually used to restructure unsecured creditors. It is supervised by a supervisor who must be a licenced insolvency practitioner in Kenya.

Liquidation - this is usually the last resort in most cases where numerous efforts to rescue a company have failed. It spells the death of a company and is conducted by a liquidator who must be a licensed insolvency practitioner in Kenya.

Other Considerations: Director's Duties in Kenya

Inevitably and as part of the control rights acquired by the fund, it will have appointed directors to the board of the portfolio company. These directors will have the same fiduciary duties as all the other directors of the company. The Kenyan Companies Act codified previous common law duties of directors in regard to their conduct and to possible liability if they fail in their duties. The duties owed by a director to a company are altered where that company is in or is facing the threat of insolvency. In those circumstances, directors have a duty to act in the interests of the company's creditors as a whole (i.e., to preserve the value in the company in order to maximise the return to creditors).

This is important because the Kenyan Insolvency Act provides for two statutory offences of wrongful and fraudulent trading which could result in the directors being personally liable if they are found culpable. Wrongful trading is usually a case of poor judgement or denial where the directors continue to trade when they know that there is no reasonable prospect of the company avoiding insolvency. Current and former directors can be found liable. Fraudulent trading is where the directors knowingly carried on trading with no intent to pay their debts.

Directors can mitigate the risk of liability by taking proactive measures such as holding regular board meetings which are fully minuted, closely monitoring the company's financial position, ensuring that directors who are nominees do not have conflicts of interest and seeking legal and financial advice early. The decision on whether to stop trading should be kept under review at all times.

Conclusion

Whilst a portfolio company in a distressed situation is not ideal for the fund or any other stakeholders in such company, in order to rescue and bring such portfolio company back to operating profitably, some of the key criteria to successful turn-arounds are:

- identifying issues early and acting quickly and decisively;
- to have a joined-up approach with buy-in from shareholders, the portfolio company (including its management), lenders and its other creditors; and
- for the fund to expect the unexpected and ensure provisions in the fund documents and the portfolio company's SHA to allow for expedited emergency funding.

THE AUTHORS

VRUTI SHAH

Partner

Bowmans, Nairobi, Kenya

vruti.shah@bowmanslaw.com

KENDALL EVANS

Director

Bowmans, Nairobi, Kenya

kendall.evans@bowmanslaw.com

DOMINIC INDOKHOMI

Partner

Bowmans, Nairobi, Kenya

dominic.indokhomi@bowmanslaw.com

PRIVATE EQUITY IN TANZANIA: HIGHLIGHT OF RECENT LEGISLATIVE CHANGES

Shemane Amin (Partner) & Daniel Ngumy (Partner)
ANJARWALLA & KHANNA

The Finance Act, 2020 which came into force on 1 July 2020, introduced a raft of changes to various legislations. Key among the changes relevant to Private Equity firms are (i) the amendment to the Companies Act, 2002 imposing a mandatory requirement for every registered company in Tanzania to disclose its beneficial owners to the Registrar of Companies and also for the Registrar of Companies to maintain a register of beneficial owners of all the companies registered in Tanzania and (ii) the amendments to the Income Tax Act which provide for certain triggers and compliance procedures for the payment of capital gains tax on the realisation of investment assets in Tanzania. We highlight below the salient features of the two key amendments.

1. Disclosure of ultimate beneficiaries' requirement under the Companies Act, 2002

Effective 1 July 2020, all persons seeking to register new companies (whether private or public companies) in Tanzania must identify the beneficial owners of such companies and submit the particulars of the beneficiaries to the Registrar of Companies at the time of registration. Pre-existing companies have until 31 December 2021 to submit particulars of their beneficiaries ownership (BO) to the Registrar.1

There is also an ongoing reporting requirement that any changes to the beneficial ownership of a company must be notified to the Registrar within thirty (30) days of such changes, and all companies registered in Tanzania will be expected to submit particulars of their BOs to the Registrar of Companies on an annual basis at the time of filing their annual returns.

The Government subsequently on 14 May 2021 issued the Companies (Beneficial Ownership) Regulations, 2021 (the Regulations) and the Companies (Forms) (Amendment) Rules, 2021, (the Rules) which set out further details on the forms, particulars and processes relating to the disclosure requirement.

Who is to be declared as a beneficial owner?

Pursuant to these amendments to the law, a beneficial owner is defined under the Companies Act, 2002 and the Regulations as a natural person (i) who directly or indirectly ultimately owns or exercises substantial control over an entity or an arrangement, or (ii) who has a substantial economic interest in or receives substantial economic benefit from an entity or an arrangement directly or indirectly, whether acting alone or together with other persons, or (iii) on whose behalf an arrangement is conducted or (iv) who exercises significant control or influence over a person or arrangement through a formal or informal agreement.

The Regulations do not contain a quantifiable threshold to determine if a natural person is a beneficial owner. This casts a wide net and may effectively mean disclosing every natural person who may have some interest in or rights in relation to a reportable legal entity in Tanzania. For comparative purposes, Kenya's beneficial ownership laws provide that among other things, beneficial owners are natural persons who own more than 10% of the issued share capital or exercise more than 10% of voting rights. In certain other countries, the threshold is 25% so as to exclude persons whose ownership or control or interests are not significant. This practically means that both the General Partner and the Investment Advisor must enter into written agreements with their respective shareholders such that at least 51% of the profits accrued by the Private Equity Fund Manager will accrue to their shareholders who are Black People and/or Black People who are not shareholders in the Private Equity Fund Manager.

The statutory forms require the following details to also be provided:

a) percentage of shareholding (with no minimum thresholds);

b) percentage of voting rights (with no minimum thresholds);

c) a right to appoint or remove a majority of the board of directors of the company (emphasis is ours); and

d) significant influence or control over the company.

This casts a wide net and may effectively mean disclosing every natural person who may have some interest in or rights in relation to a reportable legal entity in Tanzania.

Shemane Amin (Partner) & Daniel Ngumy (Partner)
ANJARWALLA & KHANNA

It is also the case that the important expression "significant influence or control" is not defined, and as such, careful consideration will have to be given to the meaning of this expression and thereby the natural persons who may be considered as having "significant influence or control". For example, in the case of a private equity investment, all the natural persons holding shares (whether directly or indirectly) in the limited partnership and general partnership of the private equity fund would potentially have to be disclosed. In order to overcome the practical challenges of implementing the Regulations, it is important that the Government offers clarity on these issues in due course.

What information is to be disclosed?

The particulars to be filed in the Company Registry concerning beneficial owners include: full name, date and place of birth; telephone number, nationality, national identity/passport number, residential, postal and email; place of work and position held; nature of interest including the details of the legal, financial, security, debenture or informal arrangement giving rise to the beneficial ownership; and oath or affirmation as to whether the beneficial owner is a politically exposed person or not.

Moreover, and key to note, is that pursuant to the amendments, the Registrar of Companies is required to establish and maintain a register of beneficial owners of all companies registered in Tanzania. The register will be accessible to government agencies/authorities with responsibilities for combating money laundering and terrorist financing, as well as the authorities that have the function of investigating or prosecuting offences related to money laundering and terrorist financing, such as the Financial Intelligence Unit and the Tanzania Revenue Authority (TRA), amongst others.

What are the implications on private equity firms and private companies of disclosing ultimate beneficial owners pursuant to the Regulations?

The requirement to disclose beneficial ownership can potentially have a significant impact on new and pre-existing companies in Tanzania, as there are various tax implications to consider, such as transfer pricing and thin capitalisation, amongst others, that may arise from the disclosure of relationships between various entities in Tanzania by virtue of a common ultimate beneficial owner.

As a result of the wide definitions and no thresholds, legal entities will face practical reporting challenges, some of which are explained below:

a) If a legal entity has private equity investment, it would be practically impossible to identify each natural person that has shareholding (direct or indirect) in the limited partner and general partner of the private equity fund.

b) A receiver or security holder is likely to be reportable by virtue of having significant influence or control.

c) If a legal entity has entered into a financing arrangement which gives to financiers broad covenants and rights to appoint board members, then the financier could be reportable by virtue of exercising significant influence over a company.

d) In the case of listed companies, ownership is likely to be diverse and shareholding may be held by pension funds and other similar entities, making it impossible to identify the ultimate shareholders.

e) Is a financial controller reportable by virtue of exercising significant influence over a company's financial affairs?

f) There may be a whole host of different legal entities that enjoy ownership or control rights in relation to which it may be practically impossible to identify all the natural persons. Examples are pension funds, unit trusts and collective investment schemes.

In this regard, there is need for companies to assess the impact of the beneficial owner disclosures on their shareholding structures and business operations, and if need be, take appropriate steps to mitigate exposure and begin gathering the requisite information in anticipation of fulfilling the filing requirements in the near future. Notably, the failure to keep a record of beneficial owners or to disclose to the Registrar the beneficial owners or changes in beneficial ownership is an offence and could result in the Company being liable to a fine not less than TZS 5,000,000 (approximately USD 2,155) and not more than TZS 10,000,000 (approximately USD 4,311).

> It is important that the Government offers clarity on these issues in due course.

2. Capital Gains Tax Triggers and Compliance Measures

Capital gains tax in Tanzania is due on realisation of interest in land, petroleum, mineral rights, buildings situated in Tanzania or shares or securities held in resident entities in Tanzania.

The Finance Act, 2020 amended section 90 of the Income Tax Act by introducing a definition of what amounts to the date of realisation for purposes of computing capital gains tax. In addition, the amendments also introduced compliance requirements for persons who derive a gain upon realisation of investment assets in Tanzania.

Specifically, effective 1 July 2020, the date of realisation of an interest in an investment is defined to mean: *"the date of execution of contract for sale; or the date of parting with possession, use or control of a realized asset; or the date of payment of part or whole of the consideration for the realized asset; whichever comes earlier"*** (emphasis is ours)..

In addition, the amendments further require a person who derives a gain from realisation of investment assets to notify the Commissioner General of TRA (the Commissioner) within fourteen (14) days of realisation of the asset*** and pay the instalment tax on the gain within thirty (30) days or such other period determined by the Commissioner from the date of the realisation of an interest. Further, the relevant authorities responsible for registration, transfer or approval of such transactions, such as the Tanzanian Investment Centre or the Fair Competition Commission (as applicable), shall not register the transfer of the interest or change the name of the Company without the production of a certificate by the Commissioner certifying that the instalment tax has been paid or that no instalment tax is payable.5

Whilst the above amendments bring clarity as to what amounts to the date of realisation, there are some practical challenges. Specifically, the requirement to pay the single instalment within thirty (30) days from the date of realisation of assets (as defined under the Tanzanian laws) does not take into account the fact that, from a legal perspective, the execution of a contract of sale or payment of part of the consideration does not guarantee the realisation of an asset, as various conditions precedent to completion of the transaction, such as the necessary approvals from the regulatory authorities and the transfer of legal ownership, are likely to still be pending at that time. Where a transaction may not close, it is important for sellers to carefully manage the practical challenge of seeking a refund for capital gains tax that has been paid.

Conclusion

It is important for private equity firms with investments in or contemplating investing in Tanzania to consider these amendments when evaluating their transactions and for general compliance purposes.

THE AUTHORS:

Shemane Amin

Partner

ALN Tanzania I Anjarwalla & Khanna

sda@tz.africalegalnetwork.com

Daniel Ngumy

Partner

ALN Kenya I Anjarwalla & Khanna

dng@africalegalnetwork.com

AMENDMENT OF THE COMMERCIAL CODE OF ETHIOPIA

Mesfin Tafesse (Principal Attorney), Deborah Haddis (Associate) & Natnael Aklog (Associate)
MESFIN TAFESSE & ASSOCIATES

Since the coming into power of Prime Minister Abiy Ahmed, Ethiopia has undertaken a number of significant reforms, changes and amendments to existing laws. This article highlights some of the major changes that have taken place that may be of interest to Private Equity firms that intend to invest in Ethiopia.

Among the many new reforms, the most notable ones include:

- Amendment of the Commercial Code of Ethiopia that has been in effect since 1960;
- Amendment of Ethiopia's investment laws;
- Various directives issued by the National Bank of Ethiopia with regards to regulation of foreign currency and payment systems; and
- A proclamation to introduce a capital market in Ethiopia.

Amendment of the Commercial Code of Ethiopia

Ethiopia has been using a commercial code that was originally issued in 1952. The previous Code contained provisions that were quite outdated and so an amendment was long overdue. A brand-new commercial code (New Code) was enacted by the House of People's Representatives in March 2021.[1] The work of reviewing the previous Code has been going on for over three decades and this testifies to the enormity of the challenge associated with the changes required from the previous regime.

The first new introduction is an expansion of regulated economic activities from 21 to 37. The expansion of the economic activities is in consideration of any new economic activities that may be introduced, among other things, due to advancement in technology, new discoveries in science or advancement of civilisation will be treated as a commercial activity.

The New Code also introduced new forms of business organisations. This included the introduction of a one-person company and a limited liability partnership (LLPs) as new forms of business organisations, as well as regulation on the structure of Holding companies, LLPs and one person companies. It also includes detailed provisions related to foreign investment in Ethiopia through a branch office. Moreover, the New Code has a new chapter that regulates wholly owned subsidiaries and group companies.

For firms that are incorporated abroad and have their head office or principal place of business in Ethiopia and for firms that are incorporated pursuant to Ethiopian laws and are operating abroad, the provisions of the New Code will apply. However, in the event that a company incorporated abroad has a business form that is not recognised by the New Code, the provisions regulating share companies will apply as appropriate.

The New Code introduces various options and procedures for bankruptcy, including preventive restructuring proceedings, reorganisation proceedings and a simplified reorganisation proceeding. It also includes a simplified special bankruptcy proceeding for small and medium enterprises.

The reforms included in the New Commercial Code bring various benefits to investors. As indicated above, this code includes a clear definition of how group companies and branches are to be regulated. In terms of the management structure of companies, the New Commercial Code permits a portion of the directors in the board to be non-shareholders. The New Code also allows for companies to utilise modern accounting technologies, making book-keeping easier. In terms of bringing clarity to some pre-existing grey areas as well as recognising new business forms, the New Code is to bring more stability and predictability as well as make doing business in Ethiopia easier.

Amendment of Ethiopia's investment laws[2]

A new legal regime for investment in Ethiopia was introduced through the enactment of Investment Proclamation No. 1180/2020 (the Investment Law). The primary change introduced by the Investment Law is a shift from the positive list approach to a negative listing approach of investment sectors that are permitted for foreign investment. The Investment Law provides an exhaustive list of business sectors that are reserved for domestic investors (mainly in small and medium businesses), leaving others open for foreign investment. The Investment Law has not, however, introduced any changes in opening up traditionally restricted sectors such as financial services, retail, import trade and legal services.

A new investment regulation has now been introduced and partially replaced the previous regulation enacted in 2012. This new regulation mainly deals with the sectors that are open to foreign investors, sectors that are reserved for domestic investment and sectors that are open to joint investment either with the government or local investors. The incentives provided to foreign investors are still governed by the previous Investment Regulation. However, an amendment to the incentives is also expected to be enacted in the near future.

[1] If you are interested in reading more about the changes introduced by the New Code, you can access a detailed legal update here.

[2] If you are interested in reading more about the changes introduced by the investment laws, you can access a detailed legal update here.

Mesfin Tafesse (Principal Attorney), Deborah Haddis (Associate) & Natnael Aklog (Associate)
MESFIN TAFESSE & ASSOCIATES

L&R

Notable directives issued by the National Bank of Ethiopia (the NBE) with regards to regulation of foreign currency

1. Directive Amending the Previous Directive on Retention and Utilisation of Export Earnings and Inward Remittances (Directive No. FXD/70/2021): This directive authorises banks to open foreign exchange retention accounts for eligible exporters of goods, services and inward remittances. Customers who are eligible are regular recipients of foreign exchange remittances from abroad or exporters of goods or services who have not been labelled as delinquent. Customers become delinquent when they do not settle their for-ex commitments with the NBE. This directive will apply to foreign investors who are interested in export business or those engaged in businesses that allow them to receive foreign exchange transfers from abroad.

Customers who are eligible can retain 45% of their account balances for an indefinite period after the deduction of 30% surrender requirement from the total earnings they made. The remaining 55% must be surrendered to the bank at the prevailing exchange rate immediately on the day of the receipt. Account holders can use the retained foreign currency to import goods and make payments for services without restriction provided that the account holder has the required business licence to undertake those activities.

> Customers who are eligible are regular recipients of foreign exchange remittances from abroad or exporters of goods or services who have not been labelled as delinquent. Customers become delinquent when they do not settle their for-ex commitments with the NBE.

2. NBE Issues New Payment System Directive (Directive No. ONPS/01/2020): Before this legislation came into effect, financial institutions (more specifically banks) were the only entities allowed to offer mobile money services. Cooperatives have only been providing financial services. The way they used to participate in the mobile-money services was through partnering with local private companies that provided a platform for mobile money services.

The Licence requirements for operating in this sector include:

- A minimum capital of 50 million ETB (US$1.5 million),
- Ownership by Ethiopian nationals or people of Ethiopian origin, and
- A minimum of ten shareholders are required.

The directive, effective on 1 April 2020, allows maximum account balances to users of ETB 30,000 (approx. US$634) and transaction limits of ETB 8,000 (approx.. US$1269) daily and ETB 60,000 monthly. Companies that receive the mobile-money permits can also provide saving, credit, insurance and pension products.

3. NBE Issues New Payment System Directive (Directive No. ONPS/02/2020: This allows non-financial institutions, i.e. fintech companies, to start offering payment processing and related services in the Ethiopian market by acquiring a payment system operator licence issued by the NBE.

This effectively brings new opportunities for new players in the market to start offering Payment Switch, ATM Operators, POS Operators and Online payment gateway operators' services. The directive allows companies that had been partnering with banks or microfinance institutions to provide retail services themselves. Minimum capital requirements have been introduced for each of these categories.

Recent trends of the market indicate that this sector may be liberalised to foreign investors as well. Should the sector be liberalised, it brings an untapped opportunity for foreign investors in the sector. The financial sector is one of the sectors that are still not fully liberalised for foreign participation.

Mesfin Tafesse (Principal Attorney), Deborah Haddis (Associate) & Natnael Aklog (Associate)
MESFIN TAFESSE & ASSOCIATES

L&R

A bill to introduce a capital market in Ethiopia

The Parliament approved the Capital Market Proclamation No. 1248/2021 establishing capital markets in July 2021.

This law establishes the Ethiopian Capital Market Authority (ECMA) as a Federal Government Regulatory Authority to protect investors, reduce systemic risk by ensuring the integrity of the capital market, promote the development of the capital market and generally oversee the objectives of the legislation.

The Capital Markets Proclamation aims to modernise the monetary policy of the country with alternative models. It also aims to establish a securities exchange in partnership between the Government and the private sector, including foreign investors. This provides that the total ownership of the Government may not exceed 25% of the capital of the securities exchange. However, if there is not sufficient interest from the private sector, the securities exchange may be established as a fully Government-owned enterprise that is to be regulated by the Council of Ministers. The ECMA may grant licenses to other securities exchanges or derivatives exchanges or over-the-counter trading platforms. However, detailed regulations on the requirements of acquiring such licenses are yet to be issued by the ECMA.

The Capital Markets Proclamation also has ambitions to support the national economy through capital mobilisation and financial innovation. Moreover, it contains provisions to ensure the integrity, fairness and efficiency of the capital market, as well as provisions on insider trading. It regulates investors who seek capital from the public, as well as prevents and/or mitigates systemic risks to the financial market of the country through effective monitoring and surveillance.

Some of the mechanisms introduced by the Capital Markets Proclamation in relation to the protection of the rights of parties who participate in the capital market is the establishment of the Capital Market Tribunal and the Compensation Fund. The tribunal is established to hear and determine appeals to the decisions of the ECMA. The compensation fund is established for the purpose of granting compensation to investors who suffer pecuniary loss resulting from the failure of a capital market service provider or securities exchange to meet his contractual obligations and paying beneficiaries from collected unclaimed dividends when they resurface.

The opening of a capital market brings with it opportunities for private equity investors to have an assessment of the Ethiopian market. Moreover, private equity firms will have the possibility of trading equity in an open market. The current trends of liberalisation are indicators that sectors like finance and telecom will be open to foreign investment. These trends coupled with the establishment of a capital market will bring many opportunities that may attract foreign investors.

THE AUTHORS:

Mesfin Tafesse
Principal Attorney
Mesfin Tafesse & Associates
mtafesse@mtalawoffice.com

Deborah Haddis
Associate
Mesfin Tafesse & Associates
dhaddis@mtalawoffice.com

Natnael Aklog
Associate
Mesfin Tafesse & Associates
naklog@mtalawoffice.com

PRIVATE EQUITY IN UGANDA

Fiona Nalwanga Magona (Partner) & Doreen Nawaali (Associate)
ALN UGANDA I MMAKS ADVOCATES

The COVID-19 pandemic has tested private equity firms in ways not seen before. In the first half of 2020, private equity activity took a sudden halt as COVID-19 took hold. This was not unlike sectors such as tourism, hospitality, education, real estate and retail, which were also hard hit by the pandemic.

Various mitigating measures were adopted by regulators of the different business sectors, all in a bid to stabilise their respective markets. In the financial services space, for instance, the Bank of Uganda issued a directive to financial institutions allowing for the restructuring of loans on a discretionary basis, which many financial institutions adopted, restructuring a significant portion of their loan portfolio indicating the devastating effect of COVID-19 on the economy. In the insurance sector, a moratorium on premium payment was also announced. Invariably, foreign direct investment (FDI) came to a minimum with a handful of restructurings and acquisitions of distressed assets.

As the rollout of the vaccines progresses, the economy is opening up again and businesses are beginning to stabilise, alongside private sector efforts and government policies targeted at improving access to finance to kickstart the economy. Cash flow constraints experienced by companies during COVID-19 may see many companies turn to private equity investment as a source of financing. This is because besides provision of capital, investments by private equity funds have considerable impact in terms of skills development through business development support, active management, exchange and transfer of know-how and access to a broader network. We anticipate that private equity funds will play a key role in supporting various entities across different sectors.

Regulatory Developments in the private equity and venture capital space

The enactment of new draft regulations on private equity and venture capital funds and the ongoing stakeholder engagement by the Capital Markets Authority demonstrate the growth of private equity and the efforts to create a more favourable regulatory environment for it. The draft Capital Markets Authority (Licensing and Approval) and Regulations 2021 (the ''Regulations'') seek to provide for regulation of venture capital funds established, incorporated and registered in Uganda. Applicants are required among others to fulfil both technical and financial requirements, including evidence of membership in a self-regulatory organisation with oversight over venture capital funds in Uganda as approved by the Capital Markets Authority.

The venture capital fund is required to have a board of directors with a minimum of five directors and at least a third of them independent directors. Additionally, the venture capital fund should have as its principal object the provision of risk capital to business enterprises in Uganda, and any changes to its shareholders, directors or fund manager are subject to no objection from the Capital Markets Authority.

The Capital Markets Authority (Accounting and Financial Requirements) Regulations, 2021 have also revised the net capital requirements and the minimum paid up share capital as below:

	Net Capital in UGX	Minimum Capital in UGX
Fund Manager	190,000,000 (approx. USD53,000)	375,000,000 (approx. USD105,000)
Venture Capital Fund	750,000,000 (approx. USD210,000)	1,500,000,000 (approx. USD420,000)

	Fees in UGX
Venture Capital Funds	Registration Fees – 750,000 (approx. USD210,000)
	Annual Registration Fees – 1,000,000 (approx. USD280,000)
Fund Manager License	Application Fees – 750,000 (approx. USD210,000)
	Annual Licensing and Renewal Fees – 3,700,000 (approx. USD1,000)

The Uganda Revenue Authority is also taking steps to create a more favourable tax regulatory regime for registered venture capital funds. The Income Tax Amendment Act 2021 seeks to amend Section 54 of the Income Tax Act. It provides that there will be no gain or loss if a registered venture capital fund reinvests at least 50% of the proceeds resulting from the sale/ disposal of investment interest within the year in which the sale took place. Notwithstanding the above, the registered venture capital fund shall be entitled to a loss or gain equivalent to the percentage of reinvested proceeds. From the reading of the amendment, this incentive is only available for registered venture capital funds that are provided for under the new draft Regulations, which are yet to be passed into law.

Emerging Trends and New Sectors of Interest

Whereas some sectors such as manufacturing, technology, media, telecommunications and healthcare were resilient during the pandemic, other sectors such as tourism, travel and hotel and logistics may need to rethink their business models. Private equity funds are shifting their focus to preserving the value of companies in their existing portfolios, and they are working to strengthen existing relations with their partners and lenders.

An area likely to see renewed interest is environmental, social and governance (ESG) investing. The rapidly growing list of signatories to the United Nations-supported Principles for Responsible Investment (PRI), the principal framework for investors who wish to integrate the consideration of ESG issues into their investment decision-making, is an indicator of increased awareness of ESG issues. Companies want to strike a balance between the moral values versus economic value. The Parliament of Uganda recently passed a National Climate Change Bill 2020, which gives force to the United Nations Framework Convention on Climate Change, the Kyoto Protocol and the Paris Agreement.

Another sector that has attracted investment is fintech, with financial inclusion being a key driver in this sector. This growth is being facilitated by efforts to build a more supportive regulatory framework for fintech following the gazetting of the National Payment Systems Act 2020 and the accompanying Regulations thereunder. The Central Bank of Uganda (BoU) has put in place a regulatory sandbox framework that allows innovative financial solutions, for example, fintech startups to be tested in live controlled environments with BoU's oversight and subject to the necessary safeguards.

The trend towards an increasing dependence on digital tools and IT-based working models has more companies moving services and products online and more employees working from home whilst using personal mobile devices to connect to home networks, which means there is an increased investment in online and technology-based solutions. Online mobile transport companies like SafeBoda partnered with United Nations Capital Development Fund to provide an e-commerce platform that connects market vendors to customers during the COVID-19 lockdown and beyond. This digitisation has also been adopted by the government to facilitate ease of doing business in Uganda. For instance, the Companies Registry, the Immigration Department, the Revenue Authority and the Investment Authority have all adopted an online platform to cut back on inperson traffic and improve efficiencies in their services to the public. An e-government procurement system is also underway. Renewable energy is one of the fastest growing sectors in Uganda.

Challenges

Uganda faced significant political upheaval in January 2021, with an internet shutdown for several days during the election period. The political and social unrest surrounding the election diminished investor appetite in the country. The Government's decision to shut down the internet in retaliation against Facebook closing the accounts of some pro-ruling party supporters left several companies counting billions of shillings in lost revenue.

Another challenge is that private equity funds do not have a special tax regime in Uganda and therefore income tax and/or dividend taxes will be assessed at the investee company level, at the fund level and again at the fund shareholder level. This creates an element of double taxation, making them tax inefficient and thereby creating a strong disincentive for investors to invest in Ugandan companies. Currently, a 30% corporate tax is payable by all corporate entities to the Uganda Revenue Authority. If a local private equity firm invests in another local firm and it is paid dividends by the company in which it invested, a withholding tax of 15% is payable on the dividends. If, however, the equity invested is in a magnitude of more than 25%, then the dividend is exempt. If a decision is made by the private equity firm to dispose of its investment in the local firm and it makes a gain on the disposal, the gain is taxed at 30%, which is a capital gains tax payable to the Uganda Revenue Authority. The 30% capital gains tax is high compared to other jurisdictions like Kenya and Mauritius, making Uganda a less favourable destination for private equity investment.

at 30%, which is a capital gains tax payable to the Uganda Revenue Authority. The 30% capital gains tax is high compared to other jurisdictions like Kenya and Mauritius, making Uganda a less favourable destination for private equity investment.

For fund managers to be able to successfully raise funds from investors, they need to demonstrate a track record of delivering good returns for their investors. The unfavourable tax regime significantly affects the rate of return to investors, making Uganda a less attractive investment destination for private equity.

Finally, while it is common place for private equity funds worldwide to set up as partnerships, in Uganda, the Capital Markets Authority Act only makes provision for private equity funds to be set up and registered as local companies. The new draft Regulations set out the criteria for registering venture capital funds as companies and not partnerships. The stakeholder recommendation to the Capital Markets Authority Act is to amend this provision to give private equity funds flexibility to set up as partnerships. Creating an option for funds to register as partnerships diversifies the structure under which private equity funds can be set up. It also limits investor liability to their fund investment.

Future Outlook

The deepening of the Ugandan capital market, coupled with economic growth, has the potential to support the development of the private equity space in Uganda.

Like all other collective investment vehicles that pool funds together, such as investment clubs, unit trusts and retirement benefits schemes, private equity and venture capital funds should not be taxed both on the investments that they make and the returns they receive and then for their existence as corporate entities. The recommendation is that the Capital Markets Authority should pronounce itself that private equity funds are a tool into which funds are individually placed, hence unifying the treatment of all similar collective investment vehicles. Understanding that they are pass-throughs, which solely pool funds to deploy into other companies, means that a more favourable tax environment is created.

Strengthening the regulatory environment will go a long way in building investor confidence in the market. This may require setting up a separate private equity and venture capital regulatory regime, providing a more favourable tax regime specifically for private equity and venture capital funds and making provisions for private equity funds to be set up as partnerships.

The lessons taught by the crisis could reshape the way funds pick their investments, manage their performance and work with portfolio companies and investors alike. There will be unprecedented scope and detail with due diligence assignments on a commercial and operational level to ascertain how the pandemic has changed businesses. Owing to the current economic environment, asset valuations have been affected, and hence there are potential opportunities for investors to purchase high-quality assets at attractive prices. The fundamental principles which drive private equity investment strategies, such as investing into high-quality assets, partnering with active and strong management teams and focused exit strategies, are expected to support private equity remaining a resilient asset class.

Strengthening the regulatory environment will go a long way in building investor confidence in the market.

This may require setting up a separate private equity and venture capital regulatory regime, providing a more favourable tax regime specifically for private equity and venture capital funds and making provisions for private equity funds to be set up as partnerships.

Funds will look for ways to preserve value, analysing strategies that worked and those that did not. Private equity funds should identify behaviours that generated high performance and apply those across their portfolios. Private equity funds can leverage their value-creating capabilities to support companies. The fundraising environment is likely to change with a continued focus on restructuring and supporting companies navigate the long-term effects of COVID-19.

The ongoing regulatory developments by the Capital Markets Authority and the increased stakeholder engagements are expected to increase access to capital for Ugandan businesses and create an environment that boosts investor confidence in the country.

THE AUTHORS:

Fiona Nalwanga Magona

Partner

ALN Uganda I MMAKS Advocates

magona@ug.africalegalnetwork.com

Shemane Amin

Associate

ALN Uganda I MMAKS Advocates

nawaali@ug.africalegalnetwork.com

RWANDA – AS A FINANCIAL SERVICES CENTRE

Mark Kenderdine-Davies (Chief Legal Officer)
CDC GROUP/BRITISH INTERNATIONAL INVESTMENT PLC

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In May 2018, on BBC Radio 4's Today programme, Clare Akamanzi, the Chief Executive Officer of Rwanda Development Board, gave a spirited defence of her company's decision to sponsor Arsenal F.C., an English Premier League team, to the tune of £30 million in order to promote Rwandan tourism, signalling a willingness on the country's part to show it was open for business, ready to market itself to the world.

More recently, Tidjane Thiam and Nick Barigye, Chairman and Chief Executive Officer respectively of Rwanda Finance Limited, have been promoting Kigali International Financial Centre (**KIFC**) to international investors as a conduit for financing businesses in countries in the East African Community (**EAC**), the Economic Community for Central African States (**ECCAS**) and the Common Market for Eastern and Southern Africa (**COMESA**). As with its Arsenal sponsorship, Rwanda is signalling its openness to business and foreign investors.

This article sets out why private capital investors, including members of the African Venture Capital and Private Equity Association (AVCA), should view the development of a new "onshore Africa" financial centre positively. It highlights the building blocks of a successful financial centre and then the legal, regulatory and taxation reform programme, which underpins the KIFC. It asserts that the Government of Rwanda **(GoR)** is providing the right enabling environment – the right framework in other words – for the KIFC to facilitate capital inflows into Eastern and Southern Africa.

Investment through financial centres

Institutional investment into African businesses (excluding South Africa) is typically channelled through corporate vehicles domiciled in other African financial centres (e.g. Mauritius and Morocco (Casablanca)), non-African financial centres (such as the UK, the U.S. (often Delaware), Luxembourg and the United Arab Emirates) or offshore financial centres (such as the Channel Islands, Cayman Islands or British Virgin Islands).

Non-governmental organisations and civil society occasionally criticise investor domiciliation choices. The criticisms vary but often allege lack of transparency, weak regulation, non-compliance with international standards, harmful tax practices and involvement in the facilitation of capital flight from developing countries. Indeed, some multilateral financial institutions no longer invest in certain corporate structures, which include vehicles domiciled in "blacklisted" or "greylisted" jurisdictions, leading to transactional uncertainty, workarounds and increased cost, unless identified and mitigated early. Whilst many of the impacted financial centres will address these concerns over time, various African governments have decided that it is strategically advantageous to create the right enabling environment for the development of credible financial centres of their own.

> The criticisms [of investor domiciliation choices] vary but often allege lack of transparency, weak regulation, non-compliance with international standards, harmful tax practices and involvement in the facilitation of capital flight from developing countries.

Pillars for a successful financial centre

So, what is the right enabling environment – the right framework - for a financial centre to flourish?

Pillar 1: *the government and legal system*

A country needs a government with the political stability, support and will to build a centre; a conducive business environment with an open, relatively stable economy; a robust commercial legal and judicial system; effective and flexible company and securities laws (with market participants able to negotiate rights in capital structures and enforce contracts locally); conformity with evolving international standards of business integrity and anti-corruption; a reliable and consistent approach to dispute resolution and enforcement; non-discriminatory treatment of cross-border investment; a transparent and fair regulatory environment with regulators committed to good corporate governance; and transparent and reliable rules for expropriation and protection against expropriation in other countries and a stable and fair framework for property rights.

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Pillar 2: *The infrastructure*

A centre also requires "hard" infrastructure (i.e., the technical (power, technology, connectivity, transport links etc.), financial (sufficient banking depth so payments can be processed via reputable global banks), people (bilingual language skills, flexible immigration policy, cost competitiveness etc.)) plus "softer" professional infrastructure where the sentiment of market participants coalesces positively around a particular country – is our capital in safe hands? Is this a good, trustworthy place to do business? Finally, even with the right framework in place, is the country saleable to international investors? Does it suffer from negative perceptions?

> Draft laws relating to the regulation of capital markets, the organisation of banks and the holding and circulation of securities are presently being considered by the Cabinet of the GoR. Kigali's skyline evidences how quickly the country's "hard" infrastructure is evolving.

Rwanda's approach to establishing a financial centre

After analysing the enabling environment of countries with successful financial services industries (particularly Singapore), the GoR has promulgated a slew of laws and regulations, which provide the framework for the KIFC to play an increasingly important role in the financing of African businesses. These new laws and regulations include those governing companies, partnerships (relevant for private capital investors), investment promotion and facilitation, collective investment schemes, negotiable instruments, insurance business, trusts, foundations, money laundering and the financing of terrorism, mutual legal assistance in criminal matters and data protection. Other laws established a Capital Markets Authority and a Financial Intelligence Centre. In addition, laws governing deposit-taking by microfinance institutions and insolvency and bankruptcy have been enacted and will likely be gazetted (i.e., become effective) in early 2022. Draft laws relating to the regulation of capital markets, the organisation of banks and the holding and circulation of securities are presently being considered by the Cabinet of the GoR.

Kigali's skyline evidences how quickly the country's "hard" infrastructure is evolving.

Investor engagement with the KIFC

Finally there's the incentive framework. Now the KIFC has been launched, what can be done to encourage investors to use it? The GoR has sought to provide a clear, consistent and internationally competitive taxation regime with no foreign exchange controls, no restrictions on the foreign ownership of assets, 100% repatriation of profits and other tax incentives, including a preferential corporate income tax rate and exemption from payment of withholding tax on dividends, interest and royalty payments. The GoR is also developing a network of double taxation avoidance agreements and investment promotion and protection agreements (known as bilateral investment treaties).

The GoR has expended considerable political and diplomatic capital on the KIFC as it seeks to persuade investment funds and holding companies to domicile in the country. It is also seeking to become a hub for fintech and green finance investment opportunities in the region. Its success, according to the Honourable Soraya Hakuziyaremye, the Deputy Governor of the Central Bank of Rwanda, is strategically important to the country.

Recent domiciliation announcements include launches of the $350 million Afreximbank-backed Fund for Export-Development in Africa, the $250 million Qatar Investment Authority and Rwanda Social Security Board-backed Virunga Africa Fund I, the Rwanda Innovation Fund and the Rwanda Green Fund.

The future of the KIFC and African financial centres

It is an exciting time for observers of African financial centres. In addition to Rwanda's efforts in Kigali, Casablanca is developing as a preferred financial centre for north and northwest African investment encouraged by recent listings on the Casablanca Stock Exchange. Cairo is prospering. Mauritius, historically a favoured option, is quickly regaining its mojo after a period of regulatory difficulty, now resolved. Kenya has ambitious plans to develop the Nairobi International Financial Centre as another conduit for capital whilst Johannesburg continues to play to its strengths in South Africa.

From a private equity and venture capital perspective, institutional investors and the managers they support should welcome the emergence of a new African financial centre providing a new domiciliation option and choice. Whilst it's difficult to know which financial centres will flourish over the coming decade, it is likely that the KIFC – a relatively new entrant - will be one of them given the environment the GoR has created for private capital investors. Those "Visit Rwanda" logos on the shirts of the Arsenal team signal not only the country's openness to tourism but also to financial services industry participants on the continent.

THE AUTHOR:

Mark Kenderdine-Davies

Chief Legal Officer

CDC Group plc / British International Investment plc

mkdavies@cdcgroup.com

THE CHANGING FACE OF MERGER CONTROL IN NIGERIA

Chinyerugo Ugoji (Partner), Chioma Olibie (Senior Associate) & Tobenna Nwosu (Associate)
AELEX

In December 2018, the Federal Competition and Consumer Protection Act (the "Act") was added to the list of laws governing M&A activity in Nigeria, which are divided along the lines of federal, sectoral, and subsidiary legislation. The Federal Competition and Consumer Protection Commission (the "Commission") established under the Act became Nigeria's foremost competition, antitrust and merger assessment body. Between November 2020 and August 2021, the Commission has exercised its rulemaking powers pursuant to Sections 17, 18, and 163 of the Act by publishing the Merger Review Guidelines, Merger Review Regulations and Merger Review (Amended) Regulations. New provisions for mergers in Nigeria, and important provisions in the Act, which have been clarified by the Merger Review Regulations and Guidelines, are considered below.

Relevant Merger Situation and Change of Control: Acquisition of shareholding or voting rights below 15% will generally not prompt the Commission's review, but acquiring shares or voting rights above 25% will confer upon the acquirer a rebuttable presumption that it has the power to materially influence policy in the seller. While the presumption of material influence is attached to shareholdings above 25%, the Commission may assess shareholdings below 25% but above 15% for potential material influence. In exceptional circumstances, shareholding of less than 15% will attract scrutiny for material influence. The ability to exercise material influence in the target's policy is the lowest level of control that may give rise to a merger situation. The Merger Review Regulations deem an internal restructuring to be notifiable only if it will cause a change in control of a company within the group. A change from joint control to sole control in a business is notifiable, as are acquisitions by which two or more firms gain control of a target. Control acquired over a series of transactions (not exceeding two years from the first transaction to the latest) shall be regarded by the Commission as having been acquired in one transaction effected on the date the latest transaction occurred.

Timeline for Notification, Review and Publication of Mergers: For small and large mergers, the Merger Review Regulations provide for a two-stage review. The Commission shall complete first phase review of a small merger (combined turnover below N1 billion) within 20 business days of satisfactory notification. This period is extendable by 15 business days if the merger raises competition concerns.

During first phase review for large mergers, the Commission will assess within 60 business days the merger's potential to prevent or significantly reduce competition in the affected market(s). Where it finds that the transaction has anticompetitive elements, it will extend its review by 30 business days and allow the parties to offer remedies for the competition issues. On completing its review, the Commission will approve the merger unconditionally or subject it to the remedies, or, if the merger still raises competition concerns, proceed to the second phase review lasting 60 business days, during which it will consider technological efficiencies, pro-competitive gains, or public interest grounds sufficient to offset the competition issues. If the Commission makes a positive determination on any of these grounds, it will approve the merger subject to conditions which it deems appropriate. In practice, where no material competition issue has surfaced, the Commission will seek to complete the first phase review within 45 business days.

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Chinyerugo Ugoji (Partner), Chioma Olibie (Senior Associate) & Tobenna Nwosu (Associate)
AELEX

Notification of a merger is done by way of a Form 1, but Form 1A is used to publish notice of the merger on the Commission's website within two business days of receipt of a satisfactory merger notification. The Form 1A is an executive summary of the merger. Before its publication, it should have been served on the trade unions for employees of the merger parties. As the Form 1A will appear on the Commission's publicly accessible website, it should be drafted to contain no confidential information or business secrets of the parties. A third party with an interest in the merger may alert the Commission of its interest within three business days of publication in the case of a small merger and within seven business days for large mergers.

Remedies and Appeals: With permission from the Commission, parties in a transaction that shows competition issues may propose remedies or restructure the transaction in a manner that resolves the issues. In assessing the effectiveness of a proposed remedy, the Commission will gauge the duration, competitive impact, and practicality of the remedy.

The Merger Review Regulations and Guidelines recognise three forms of remedies: (i) structural remedies, which entail changes in the market structure, e.g. by the merger parties committing to divest assets to an existing or new competitor, (ii) behavioural remedies, which involve constraints on the conduct of the merged entity, e.g. adherence to pro-competitive clauses, such as for relinquishing certain rights in the target or for resignation of board membership and (iii) a hybrid of both remedies, ideal when the merger spans markets - in some markets structural reliefs will best preserve competition, while in others behavioural reliefs will suffice.

A party against whom the Commission has ruled may appeal to the Competition and Consumer Protection Tribunal within 30 business days of being notified of the Commission's decision.

Standstill Obligations and Gun Jumping: Merger parties are forbidden to coordinate their activities or behave as though already merged until the Commission has approved the merger; they must remain competitors up to the point of approval. During due diligence and integration meetings, parties should be wary of taking actions that suggest coordination or integration of their businesses. The Commission can impose measures to instil or restore competition between parties; it can levy a penalty for gun jumping as prescribed in the Administrative Penalties Regulations.

Foreign to Foreign Mergers: The Foreign-to-Foreign Merger Guidelines 2019 have been withdrawn, and mergers between global parties with a presence in Nigeria are covered in Regulation 9 of the Merger Review Regulations. The Commission will review any transaction by which a Nigerian company comes within the control of a foreign entity if turnover requirements for notification are met, or such a merger is likely to prevent or lessen competition in Nigeria. For a transaction involving companies domiciled outside Nigeria but linked to Nigeria, for example, by having subsidiaries in Nigeria or turnover from Nigeria above the notification threshold, the Commission's review will be necessary. Parties outside Nigeria will appoint local counsel to notify the Commission on their behalf.

Anti-Competitive Effects of Minority Shareholding: The Commission will consider the following to be acquisition of minority shareholding with potentially anti-competitive effects: (a) an acquisition likely to cause less competition and more coordination between horizontal undertakings, i.e. business rivals, (b) an acquisition that could increase the acquirer's incentive to foreclose rival suppliers, in the case of vertical or conglomerate acquisitions, (c) an acquisition that initiates access to commercially sensitive information of competitors and (d) will block potentially pro-competitive mergers.

Expedited Procedure: The Commission may permit parties in eligible transactions (as outlined in para. 3.58 [i] to [iv] of the Merger Review Guidelines) to apply for expedited procedure, which could reduce the time for phase one review by up to 40%. This option is typically exercised by parties who can prove their transaction will likely not lessen or prevent competition in the market. The expedited procedure (Form 2) has an additional processing fee of N10M.

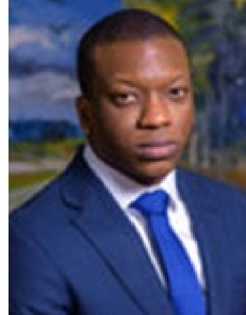
Negative Clearance: A party uncertain as to whether the transaction in which it is involved constitutes a notifiable merger may apply to the Commission for assessment under Regulation 10 of the Merger Review Regulations, subject to paying a fee of N2.5 million. It is unclear how long the assessment for negative clearance will take, but where the Commission finds that a transaction should not be notified, it will inform the parties and clear the transaction. If the Commission cannot make such a finding based on information provided by the party in Form 4, it will ask that the party proceed to phase one review.

Pre-Notification Consultation: Parties are now advised to seek consultation with the Commission, at least two weeks before contemplating submission of the merger notification. This consultation could be in person or by virtual means. The Commission will clarify parties' doubts on aspects of notification, such as whether to use the simplified or expedited procedure and which documents must accompany notification.

Conclusion/Outlook:

Nigeria, Africa's largest economy as of August 2021,1 presents significant opportunities and value for foreign investments and acquisitions. The country's M&A deal value for the first half of 2021 totalled USD1billion from 28 deals, nine of them inbound transactions in the technology sector. This reflects a deal value increase of 267% and a deal volume increase of 17% compared with the same period in 2020. Through the new Merger Review Regulations and Guidelines, the Commission has tried to reflect the scope and complexity of these transactions, and clarify procedural and substantive requirements for implementing mergers locally. It is hoped that these updates (and other regulations in the works) will increase transparency, efficiency and inter-agency cooperation in merger assessment.

THE AUTHORS:



Chinyerugo Ugoji
Partner
Aelex
cugoji@aelex.com

Chioma Olibie
Senior Associate
Aelex
colibie@aelex.com

Tobenna Nwosu
Associate
Aelex
tnwosu@aelex.com

ÆLEX

RECENT REGULATORY UPDATES IN SOUTH AFRICA AND THEIR IMPACT ON PRIVATE EQUITY

Jutami Augustyn (Partner, Private Equity) & Chibie Odimegwu (Candidate Attorney)
BOWMANS

The ever-growing reports of deals in South Africa continue to point to investor optimism in the region. However, legislators and regulators in South Africa have recognised that in order to continue this trend, they will need to consider, review and, where appropriate, amend, the existing legal framework. On this basis, this article sets out the recent developments in the South African private equity industry over the last year.

Loop Structures

The most notable development in South Africa over the last few months comes by way of the abolition of the prohibition against loop structures, which took effect from 1 January 2021. Under previous South African exchange control rules, a South African exchange control resident (individual or company) could not invest in a foreign structure that directly or indirectly owned assets in the Common Monetary Area (being South Africa, Eswatini, Lesotho, Namibia and South Africa) where such investments were subsequently invested back into the Common Monetary Area.

With this abolition in place, private equity funds that are tax resident in South Africa (i.e., a South African exchange control resident) may now make investments by way of the loop structure. However, an investment made this way prior to 1 January 2021 is still subject to approval by the Financial Surveillance Department of the South African Reserve Bank.

Private equity funds with authorised foreign assets may invest in South Africa, provided that where South African assets are acquired through a loop structure, the investment must be reported to an Authorised Dealer of the South African Reserve Bank as and when the transaction is finalised, and the private equity fund will be required to provide certain documents to the South African Reserve Bank on an annual basis through its Authorised Dealer.

All investors and funds that are either currently invested in loop structures or who have been unable to make investments as a result of the loop structure restrictions, should carefully consider the impact of the proposed relaxations on their current or future investments, particularly in relation to the potential tax impacts. Certain new tax laws that have been introduced are aimed specifically at these structures, which may result in an increased tax liability in certain scenarios. Further, the capital gains tax exemption that would apply on the disposal of shares in a foreign company will no longer apply to the disposal of shares in a controlled foreign company to the extent that such company's assets consist of South African assets.

Changes to the Pension Funds Act

Under Regulation 28 to the Pension Funds Act 24 of 1956, retirement funds are limited in respect of the percentages of their assets that they may invest in different asset classes. Various industry members, including the Southern African Venture Capital and Private Equity Association (SAVCA), have expressed the view that the current Regulation 28 constrains asset allocation decisions, which could then leave investors with potentially inefficient portfolios.

The proposed changes to Regulation 28, as outlined by the South African Minister of Finance during the national budget speech on 24 February 2021, seem like a welcome proposal to provide pension funds with a higher degree of diversification. The main proposed change includes allowing retirement funds to invest 45% of the funds in South African infrastructure and 10% in African infrastructure outside of South Africa, thereby increasing the maximum infrastructure investment exposure of retirement funds to 55%.

Another proposed change to Regulation 28 seeks to make private equity funds a standalone asset class that is separate to that of an investment in hedge funds. Furthermore, there are proposals to increase the limit of investments that pension funds can make in the private equity funds asset class from 10% to 15%, which of course will assist private equity funds in their various fundraising endeavours.

Certain new tax laws that have been introduced are aimed specifically at these structures, which may result in an increased tax liability in certain scenarios.

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Changes to the Income Tax Act

The South African Minister of Finance has also noted the abolition of the venture capital tax incentive present in section 12J of the Income Tax Act 58 of 1962 with effect from 30 June 2021; the rationale being that the incentive had not "sufficiently" achieved its objective of developing small, medium and micro-enterprises (SMMEs) "instead it provided a significant tax deduction to wealthy taxpayers".

Section 12J sought to encourage equity funding to SMMEs by allowing a taxpayer the benefit of a tax deduction in respect of 100% of any expenditure that the taxpayer actually incurred when acquiring shares of a venture capital company. The possible end of the section 12J tax break could have a material impact on the South African venture capital asset class and consequently lead to long-term impacts on certain sectors that depend on this type of funding.

COFI Bill

The Conduct of Financial Institutions (COFI) Bill is another regulatory development on the horizon. The COFI Bill intends to inter alia streamline the conduct requirements for financial institutions, which are currently regulated by a number of separate financial sector laws. The COFI Bill will inter alia replace the conduct provisions in various financial sector laws, with the aim to build a strong, effective and consistent market conduct legislative framework for all institutions that undertake financial activities – with the ultimate aim being putting the client/investor first. Traditional products such as collective investment schemes and private equity funds will also be licensed under the framework of the COFI Bill. This introduces a change to the current position of private equity funds in South Africa in that the unregulated investment class will now be subject to regulatory licensing and oversight by the Financial Sector Conduct Authority.

Compliance with the provisions of COFI – particularly in terms of licensing, application of conduct standards and treating of customers fairly – will become more of a focus point. Financial service providers will need to ensure that, amongst other things, governance practices are aligned with the COFI principles; the most important principle being treating customers fairly, which is an outcome based regulatory and supervisory approach that is aimed at ensuring that financial institutions deliver specific, clearly set out fairness outcomes for financial customers. These include outcomes such as providing customers with clear information before, during, and after the sale and providing products and services of an acceptable standard as expected by the customers.

The second round of comments on the COFI Bill closed on 30 October 2020 and the National Treasury is set to finalise the COFI Bill and thereafter submit it to Cabinet for approval and tabling this year. However, it is unclear at this point in time when exactly the COFI Bill will be enacted.

Broad Based Black Economic Empowerment (B-BBEE) Codes

The B-BBEE Codes, which seek to promote the participation of black people in the South African economy, have had a significant recent impact on the South African private equity industry. Under the B-BBEE Codes, shares held by private equity funds, which meet certain criteria, are deemed to be 100% black-owned. Therefore, a measured entity (such as a portfolio company) can treat any of its ownership arising from a private equity fund as being held by black people if, inter alia, (1) the fund manager is a black-owned company, (2) at least 51% of the private equity fund's executive management and senior management are black people and (3) at least 51% of the profits made by the fund manager post the realisation of any of its investments accrues to black people by written agreement.

When structuring a private equity investment that has B-BBEE ownership requirements, it is not uncommon to use employee share ownership schemes (ESOPs) as part of the investment in the underlying portfolio company in order to hold a percentage of the shares for the benefit of black employees. This might be part of or separate to any structuring considerations regarding the 'carry interest' applicable for the management of the fund manager and/or the general partner. A practice note published by the South African Minister of Trade, Industry and Competition on 18 May 2021 has clarified a few points on the interpretation of the B-BBEE Codes specific to ESOPs, including inter alia that ownership points can be derived from the shareholdings of broad-based vehicles such as ESOPs rather than from the beneficiaries of an ESOP.

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Jutami Augustyn (Partner, Private Equity) & Chibie Odimegwu (Candidate Attorney)
BOWMANS

A study conducted by SAVCA in 2020 indicated that private equity investments were effective in growing company revenue as the number of companies categorized as exempt microenterprises (i.e., businesses whose revenues are R10 million (or £500,000) or lower) after a private equity investment decreased from 26% to 13% while the number of companies categorised as generic microenterprises (i.e., businesses whose revenues exceed R50 million (or £2.5 million)) after a private equity investment increased from 51% to 66%.

Furthermore, private equity/venture capital investments played a role in improving the B-BBEE scores of companies with lower initial ratings, while also significantly improving the B-BBEE scores of companies with higher ratings. These results were effectively a strong showing of the advantages of private equity investments in the South African market.

The Impact of LPA Models

The Institutional Limited Partners Association (ILPA) has put together two Model Limited Partnership Agreements (the ILPA LPAs), being two Delaware-law based comprehensive limited partnership agreements (one dealing with deal-by-deal carry arrangements and one dealing with life of fund carry arrangements). The ILPA LPAs essentially set out ILPA's views as to what international limited partners should seek in the negotiations around the formation of funds. The ILPA LPAs were last updated in 2020.

The ILPA LPAs are predominately limited partner friendly and contain a whole host of provisions not appropriate in the South African and broader African market. For example, the inclusion of the option to impose a haircut on the general partner's carried interest upon the vote of a supermajority of limited partners. This brings forth an interesting dynamic when dealing with international investors that are more used to having certain of these provisions. Even though it leads to more intentional discussions around provisions historically considered 'market', it has not hindered fundraising in South Africa.

Similarly, there has been increased interest in the model limited partnership agreement (EDFI LPA) prepared by The European Development Finance Institutions (EDFI), which is anticipated to be used when establishing private equity funds targeting development finance institutions (DFI) is expected that the use of the EDFI LPA will appeal to DFI investors, which in turn could streamline the process of closing out DFI investments in South Africa.

Conclusion

The recent mixed bag of regulatory changes in South Africa have seemingly balanced out, if not led to improvements in, the overall effect to the private equity industry in South Africa. Looking towards a post-pandemic future, in an effort to increase investments in South Africa, one may expect to see further changes in the regulatory landscape, initiatives and approaches that would renew and/or strengthen the interest in the South African private equity industry.

THE AUTHORS

Jutami Augustyn
Partner, Private Equity
Bowmans

Chibie Odimegwu
Candidate Attorney
Bowmans

FCCPC AMENDS PROCESSING FEES APPLICABLE TO NOTIFIABLE TRANSACTIONS

Azeez Akande (Senior Associate)
JACKSON, ETTI & EDU

The Federal Competition and Consumer Protection Act, 2018 (the **Act**) vests the Federal Competition and Consumer Protection **Commission** (the Commission or the **FCCPC**) with powers to make regulations relating to imposition and collection of fees. Accordingly, the combined provisions of Regulation 15 and Schedule 1 to the Merger Review Regulations 2020 (the **2020 Regulations)** lay out different fees payable to the Commission for the transactions requiring its approval. The fees provided in Schedule 1 of the 2020 Regulations include Application, Expedited Procedure Service, Negative Clearance Procedure and Notification Fees.

On 6 August 2021, the Commission released the Merger Review (Amended) Regulations 2021 (the **2021 Regulations**), which amends Schedule 1 of the 2020 Regulations and effectively brings about significant changes to the manner of determining Notification Fees payable to the Commission in respect of notifiable transactions. The 2021 Regulations introduced a new table showing the manner of determining the applicable Notification Fee as shown below:

S/ N	Threshold	Fees (Consideration of Transaction)	Fees (Last Combined Annual Turnover)
1.	First N500 Million	0.45%	0.45%
2.	Next N500 Million	0.40%	0.40%
3.	Any sum thereafter	0.35%	0.35%

As with under the 2020 Regulations, the applicable Notification Fee is the higher of:

i) An amount being a percentage of the consideration of the transaction calculated using the table above; and

ii) An amount being a percentage of the last combined annual turnover calculated using the table above.

The 2021 Regulations take effect immediately and accordingly the changes to the Notification Fee payable to the Commission in respect of notifiable transactions are also effective immediately.

Value of Transaction (consideration or parties' combined annual turnover)	Notification Fee payable under 2020 Regulations	Notification Fee payable under 2021 Regulations	Percentage Reduction
N3,000,000,000 (approximately $7,290,000)	N17,625,000 (approximately $42,800)	N11,250,000 (approximately $27,300)	36.2%
N10,000,000,000 (approximately $24,300,000)	N70,125,000 (approximately $170,400)	N37,750,000 (approximately $86,880)	49%

Under the 2021 Regulations, the Application Fee – N50,000 (Fifty Thousand Naira (approximately $120)) per undertaking, Expedited Procedure Service Fee – N10,000,000 (Ten Million Naira (approximately $24,300)) and Negative Clearance Procedure Fee – N2,500,000 (Two Million Five Hundred Thousand Naira (approximately $6,075)) remain the same as they were under the 2020 Regulations without any change whatsoever.

The 2021 Regulations also formalise the practice that had been adopted by the Commission prior to the enactment of the 2021 Regulations, which is that the relevant turnover to be considered in determining Notification Fees payable in respect of notifiable transactions involving offshore undertakings with local component will be only the turnover attributable to the relevant local entity.

Azeez Akande (Senior Associate)
JACKSON, ETTI & EDU

A novel provision introduced by the 2021 Regulations is Regulation 6 which provides as follows:

> "The relevant turnover for the purpose of calculating the applicable fees[1] for transactions involving Private Investment Entities is the combined turnover of the relevant fund (subject to applicable conditions set out by the Commission) and the target."

However, the distinction between "Private Investment Entities" and other foreign investors is unclear and neither the Act nor the 2021 Regulations provide any clarification in this regard. It is also unclear what "relevant fund" referred to in the provision entails – the private equity fund from which the private equity firm is making investment from, the private equity firm itself or all the funds being managed or advised by the private equity firm? The "applicable conditions set out by the Commission" referred to in the provision is also not clear and the 2021 Regulations do not contain indications of such conditions.

One thing that seems to be clear however is that the provisions will most likely impact transactions involving private equity investors and other private investment undertakings in the market, as well as their potential investee companies. It is therefore expected that the Commission provides clarification on these issues so that there will be certainty in this aspect of the Commission's regulatory purview.

It is our advice that private equity investors and other private investment undertakings, their advisers, and their potential investee entities should consider this novel provision in structuring transactions that are notifiable to the FCCPC.

The Commission's decision to amend the provisions relating to quantum of the Notification Fee with a view to reducing the same appears to be in response to the views of stakeholders that the former applicable Notification Fee was too high. Whilst we expect the Commission to provide clarifications to the issues raised in respect of the new provision in the 2021 Regulations, we note that the reduction to the Notification Fee effected by the 2021 Regulations is a welcome development.

THE AUTHOR:

Azeez Akande

Senior Associate

Jackson, Etti & Edu

[1] This provision, though referring to "applicable fees", only relates to calculatioan of the applicable application fee as all other kinds of fees are already dealt with by separate provisions of the 2021 Regulations.

AVCA BOARD

'Tokunboh Ishmael
Chair
Co-Founder and Managing Director
Alitheia Identity

Ziad Oueslati
Vice-Chair
Managing Director and co-Founding Partner
AfricInvest Group

Paul Botha
Chief Executive Officer
Metier

Antoine Delaporte
Founder and Managing Director
Adenia Partners

Paul Kavuma
Chief Executive Officer
Catalyst Principal Partners

Olusola Lawson
Co-Managing Director
African Infrastructure Investment Managers

Abi Mustapha-Maduakor
Chief Executive Officer
African Private Equity and Venture Capital Association

Papa Madiaw Ndiaye
Founder and Chief Executive Officer
AFIG Funds

Henry Obi
Partner, Public & Regulatory Affairs
Helios Investment Partners

Jerry Parkes
Managing Principal
Injaro Investments

Luc Rigouzzo
Managing Partner
Amethis

Genevieve Sangudi
Managing Director
The Carlyle Group

Danladi Verheijen
Managing Director
Verod Capital Management

African Private Equity and Venture Capital Association

Championing Private Investment in Africa

Contact AVCA

37 North Row, Third Floor
London W1K 6DH, UK
avca@avca-africa.org
www.avca-africa.org

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