AVCA The African Private Capital Association

AVCA L&R

LEGAL & REGULATORY BULLETIN

ISSUE #9 | December 2023

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LETTER FROM THE CHAIRS

We are writing to you to introduce the 9th edition of AVCA's Legal and Regulatory Committee Bulletin. We start by thanking those who have contributed to this edition for their hard work and willingness to share insights on legal and regulatory developments across the African continent.

We are committed to monitoring and reporting changes that impact private capital raising and investment in Africa. We also advocate for favourable policies, educate our membership, and inform a wider audience interested in the development and impact of private capital markets in Africa. In this bulletin, we explore legal, regulatory, and tax changes impacting the fundraising and transactional private equity and credit landscape.

Our committee comprises senior legal practitioners at law firms, de-velopment finance institutions and institutional investors, whom we believe are well placed to provide insights and potentially influence change in environments where you, as African private capital market participants, operate. Full details of our members can be found within this bulletin.

In our last bulletin we emphasised that an area of future focus for us would be Africa's various merger control regimes and where changes might be sought to benefit investors and private capital allocators. After engaging with committee members, policy makers and regulators, we undertook a comprehensive merger control survey before preparing an article titled *"Optimising merger control regulation: A tool for increasing investment in Africa"* which draws insights from the study carried out earlier this year.

In this edition, we also cover private equity investment in **Uganda** and a newly proposed competition bill. In **Kenya**, we cover changes in the carbon trading regulatory regime and capital gains tax implications on offshore disposals of shares –topics of relevance to investors with exposure to Kenyan assets. We also travel to **Rwanda**, where we take a closer look at the country's market building efforts, including the growth of the Kigali International Financial Centre, and provide a regulatory update for private equity investors.

Some other key macro-trends addressed in this bulletin in-clude: (i) the implications of recent sectoral and fiscal devel-opments for investments in **Nigeria**, as well as an update on the country's legal framework in relation to the electricity in-dustry; (ii) the introduction of new financial products in **Mauritius** to boost the country's fund raising capabilities; (iii) how **South African** private equity firms are performing in times of economic uncertainty; and (iv) an overview on co-investing practices alongside African private equity fund managers.

We trust that you will find this bulletin enlightening. If you would like further information on anything in this bulletin or there are any topics that you would like to see covered in future, please let us know.

Yours,

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ABOUT AVCA | CHAMPIONING PRIVATE INVESTMENT IN AFRICA

As the pan-African industry body, AVCA plays a significant role as an effective change agent for the industry and acts as the trusted independent source of information, insight, and intelligence inspiring investor confidence; making the case for both commercial returns and impact of private capital in Africa.

AVCA represents a community of capital allocators, investors, fund managers, advisors, entrepreneurs and professional services committed to our shared vision of a prosperous Africa that is sustainable, inclusive, and innovative. AVCA – The African Private Capital Association is the nex-us of private capital in Africa, championing and enabling private capital investment in Africa.

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PRIVATE EQUITY INVESTMENT IN UGANDA AND THE PROPOSED COMPETITION BILL

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Uganda has historically had no national law on competition but rather sector specific competition laws for example in the banking, telecommunications, and energy sectors. In 2022, however, the Minister of Trade, Industry and Cooperatives (Minister) tabled before Parliament the Competition Bill, 2022, (the Bill), which bill seeks to promote and sustain fair competition across the various markets in Uganda, control anti-competitive behavior, enhance access for new investors and safeguard consumer interests. After undergoing several revisions, Parliament passed the Bill on 26 May 2023, but on 24 July 2023, the President requested for it to be sent back for further consideration. Whereas Parliament sat to reconsider the Bill on 31 August 2023, there have been no further updates on its passing.

Private equity investments on the other hand continue to grow in Uganda, with various business sectors looking lucrative and attracting more and more sophisticated investors, more recently in the financial services sector, data technology and traditional FMCG. In 2022 alone, Uganda's private equity deal value stood at USD 70 million according to Digest Africa. There are also efforts to enhance the regulatory regime applicable to the structuring of private equity funds in Uganda spearheaded by the East African Venture Capital Association and funded by the European Union, IFAD (International Fund for Agricultural Development), and other stakeholders including industry regulators.

This article analyses salient aspects of the Bill and their potential impact on private equity investments in Uganda.

Analysis of the Bill

Administration:

The Bill proposes that an independent body, the Competition and Consumer Protection Commission (Commission), be responsible for enforcing the Competition Act, meeting once every quarter with provision for special meetings at the request of three members to cater for any backlog resulting from only the quarterly meetings. This is contrasted against an earlier position in the same Bill that gave the oversight and enforcement function to the Ministry responsible for trade (Ministry), assisted by a technical committee to be established within the Ministry (Technical Committee).

Without doubt enforcement of the Competition Act by the Ministry would create challenges, considering potential political influence and inefficiencies with the Technical Committee whose members would not be fully dedicated to competition matters owing to pre-existing full time jobs. The independent autonomous office would likely instill more confidence in private equity investors vis a vis the Ministry, if one considers typical time lags in decision making at ministerial levels.

Anti-competitive behavior:

To achieve its objectives, the Bill prohibits (i) anti-competitive practices and agreements, (ii) abuse of dominant position by exploiting consumers and excluding competitors, and (iii) mergers, acquisitions, and joint ventures with an adverse effect on competition. While each of these restrictions is addressed in great detail by the Bill, this article focuses on item (iii) immediately above, being most pertinent to private equity investments.

Mergers, acquisitions, and joint ventures with an adverse effect on competition:

The Bill does not define what amounts to "adverse effect". However, it among others lists the following considerations for the Commission to consider when determining if a merger, acquisition of control or joint venture would have an adverse effect on competition in a given market:

- the level of mergers, acquisitions or joint ventures in the market;
- the market share of the parties involved in the merger, acquisition or joint venture;
- the likelihood that the merger, acquisition or joint venture may result in the removal from the market of a vigorous and effective competitor;
- the possibility of a rise in failing businesses;
- the nature and extent of innovation in the market; and
- whether the benefits of the merger, acquisition or joint venture outweigh the adverse impact of the merger, acquisition or joint venture, if any.

In our view, the considerations are numerous and widely worded making it easy for an equity investment to fall within the ambit of the restriction against anti-competitive behavior, particularly where such investment triggers multiple considerations. How these considerations will be applied remains to be seen. It is nonetheless hoped they will not be applied in a way that would suffocate the budding private equity sector.

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Merger, Acquisition and JV Notifications:

Private equity investors proposing to enter into mergers, acquisition of control or joint ventures will be required to give notice thereof to the Commission and also obtain its approval of the proposed merger, acquisition, and joint venture (as applicable). Failure to serve this notice would render such transaction void.

At this stage, the thresholds for notifiable mergers and joint ventures aren't prescribed but are awaited under regulations to be passed pursuant to the passing of the Bill into law. It is anticipated that the Bill will have transitional arrangements to cater for the applicability of approval requirements for the mergers and joint ventures caught midway completion.

In the case of acquisitions of control transactions, a private equity investor will be deemed to acquire control if (i) it has the ability to exercise 49% or more of the voting rights in another entity, (ii) can appoint more than half of the members of the board of directors or similar body in the other person; or (iii) where it can control the affairs of the other person. It is imperative to note that the 49% threshold is low compared to the 51% global practice threshold in equity investments. It is hoped that the 49% will be reconsidered, so less transactions are caught by the approval requirement.

Private equity investments on the other hand continue to grow in Uganda, with various business sectors looking lucrative and attracting more and more sophisticated investors.

Notification Timelines:

The timeline for giving notice to the Commission under the Bill varies depending on the transaction at hand. For instance, the notice for a proposed merger or amalgamation is proposed to be given after the board of directors or similar body of the respective parties have accepted the proposal to merge or amalgamate. For a proposed acquisition of control of another person, notice must be given after the conclusion of negotiations of the agreement of acquisition of control. Regarding joint ventures, notice must be given after the execution of the joint venture agreement by the relevant persons. These seem reasonable timelines and are indeed aligned with market practice for regulatory approvals being catered for as conditions precedent to the closing of an equity investment under private equity.

Approval process:

According to the Bill, once full notice of a merger, acquisition or joint venture is received from the party seeking approval, the Commission will be mandated to inquire into the merger, acquisition or joint venture within 120 days and will have power to direct the parties to the merger, acquisition, or joint venture to publish details of the relevant transaction in a prescribed manner. The Commission may also invite persons affected or likely to be affected by the merger, acquisition or joint venture to file their written comments or objections and shall thereafter proceed to consider the request to approve the merger, acquisition or joint venture.

If the Commission is of the opinion that a merger, acquisition or joint venture has no adverse effect on competition in the market, it shall approve the proposed transaction and where it holds a contrary opinion, it shall communicate the conditions subject to which it proposes to approve the merger, acquisition or joint venture. If the concerned parties agree to the Commission's conditions, they will be required to indicate their acceptance within 14 days and if they do not, they will apply to the Commission for further modification of the conditions.

Where the Commission agrees with the modifications to the conditions proposed by the parties, it will be required to approve the merger, acquisition or joint venture subject to the modifications and if it does not accept the proposed modifications, it will give the parties a further period of time within which to indicate their consent to the merger, acquisition or joint venture as proposed to be approved, subject to the conditions given earlier. If the parties fail to indicate their consent at the end of the prescribed time, then the merger, acquisition or joint venture will be taken to have been disapproved by the Commission.

The proposed approval process appears fairly straight forward, transparent and flexible to allow for conditional approvals and party engagement with the Commission. It is hoped that this will instill sufficient confidence in the private equity investors and encourage further investment in Uganda. It is also hoped that the proposed 120 days within which the Commission is obliged to respond can be reduced to 90 days to make the process more expeditious.

Interface with COMESA:

The Bill does not cater for interface with regional competition regimes such as the COMESA regime, thereby giving rise to dual notifications to both the Commission and regional competition regulators like the COMESA Competition Commission (CCC). Based on regional practice, it is recommended that at the point of setting the thresholds for notifiable mergers, acquisitions and joint ventures, consideration is also given to the COMESA thresholds, such that the Commission in Uganda would cede jurisdiction to regional competition regulators like the CCC or the East African Community competition regime (once operationalized), where CCC thresholds are triggered to avoid over regulation. For thresholds not caught by the CCC, the Uganda Commission would have jurisdiction and only be informed of notifications to the regional regulators to avoid duplicity of applications and facilitate private equity deal flow in Uganda and the region.

Exemptions:

The current version of the Bill provides for no exemptions to the notifications and approval requirements flagged above. This means that without exception private equity investments that trigger the restrictions and /or notification requirements, including those proposing to operate in priority sectors and/or sectors with specific competition provisions, will have to comply with the Competition Act. This is bound to raise red tape and questions around which regime takes priority over the other, whether the applications for approval under separate laws are made simultaneously. It is hoped that this will be resolved ahead of the passing of the Bill into law.

> **The Competition Bill is a sign of growth of the markets in Uganda and it is hoped that rather than stifle investment it will be a tool to further enhance and encourage investment.**

Conclusion

The Competition Bill is a generally welcome development in the private equity and mergers and acquisitions industry. It is a sign of growth of the markets in Uganda and it is hoped that rather than stifle investment it will be a tool to further enhance and encourage investment.

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OFFSHORE DISPOSAL OF SHARES IS NOW SUBJECT TO CAPITAL GAINS TAX IN KENYA

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The Finance Act, 2023 introduced changes to various tax laws with most changes having the effective date of 1 July 2023 while some have an effective date of 1 September 2023 and 1 January 2024.

Some of the key provisions introduced by the Finance Act relate to the capital gains tax (CGT) regime and seek to significantly expand the tax base. These changes are likely to have a tremendous effect on the structures adopted by international investors, especially the private equity investors, who make investments in Kenya through offshore entities. The new changes are not particularly straightforward as there have been various contrasting interpretations on their application.

Separately, the Kenya Revenue Authority (KRA) has become increasingly aggressive in its pursuit for revenue through increased audits and assessments, particularly, with respect to revenue and gains accrued abroad, and in particular, offshore disposals. With the introduction of the new CGT provisions, the KRA is expected to scrutinise offshore company structures with investments in Kenya more keenly.

This note highlights the key issues that should be noted by private equity investors with portfolio entities in Kenya relating to the new CGT provisions including a brief analysis of a recent decision from the Tax Appeals Tribunal relating to an offshore disposal.

New CGT provisions introduced by the Finance Act 2023

The Finance Act introduced two key provisions which are aimed at subjecting offshore disposals to CGT in Kenya. We have categorised the provisions into two tests as follows:

a the Immovable Property Test Provision; and

b the Residency Test Provision.

a The Immovable Property Test Provision

The Immovable Property Test Provision provides that CGT applies to any gains derived from the alienation of shares or comparable interests in a foreign company, including interests in a partnership or trust, if, at any time during the 365 days preceding the alienation, the shares or comparable interests derived more than 20% of their value directly or indirectly from immovable property situated in Kenya.

The key issues that an offshore seller will need to understand to determine if the provision applies to a disposal include:

a What constitutes immovable property situated in Kenya for purposes of the 20% value?

b Does CGT apply on the entire offshore gain or part of the offshore gain commensurate to the value of immovable property in Kenya?

c Does the gain need to be apportioned where the offshore disposal includes the value of portfolio assets not based in Kenya?

d How should sale transactions be structured to mitigate the impact of CGT, particularly where a sale involves both Kenyan and non-Kenyan assets?

The above are some of the key considerations which private equity investors would need to have in mind in respect of their investments in Kenyan portfolio companies, particularly, for purposes of understanding the potential tax implications on a future exit. Depending on the outcome of this analysis, an offshore sale of shares may attract Kenyan capital gains tax.

b Residency Test Provision

The Residency Test Provision provides that CGT applies on the gains derived from the alienation of shares of a company resident in Kenya if the alienator, at any time during the 365 days preceding such alienation, held directly or indirectly at least 20% of the capital of that company. The person alienating the shares is required to notify the Commissioner of Domestic Taxes in writing where there is a change of at least 20% in the underlying ownership of the shares.

The issues for consideration in respect of this provision include the following:

a What constitutes alienation of shares of a company resident in Kenya?

b What constitutes direct or indirect ownership and what threshold of disposal triggers CGT in Kenya?

c How does this provision apply to complex structures where it is difficult to identify the ultimate owners and their indirect ownership stakes?

d What measures should investors put in place to mitigate the risk of this provision applying to offshore disposal of shares?

The above issues would need to be analysed on a case-by-case basis as they require a factual analysis to be undertaken in respect of each foreign entity which holds Kenyan investments.

OFFSHORE DISPOSAL OF SHARES IS NOW SUBJECT TO CAPITAL GAINS TAX IN KENYA

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Recent decision from the Kenyan Tax Appeals Tribunal – appointment of a tax representative in Kenya of a foreign entity

In a recent judgment delivered by the Tax Appeals Tribunal (the Tribunal), the Tribunal held that gains derived from the sale of shares in a Mauritian company were subject to tax in Kenya. The Tribunal further upheld the appointment of an indirect Kenyan subsidiary of the Mauritian company in which shares were sold as a tax representative of the foreign entity in Kenya. The Kenyan subsidiary was therefore held liable for taxes in Kenya on behalf of its foreign indirect shareholder.

The Tribunal's judgment in the case was based on the fact that majority of the directors in the Mauritian company were tax resident in Kenya, and they had control over key aspects of the Mauritian company, including authorising bank transactions and other related matters. On this basis, the management and control of the foreign company was deemed to be exercised in Kenya and the Mauritian company was therefore deemed to be Kenyan tax resident. The Tribunal did not however fully address itself on some pertinent issues, such as whether the proceeds received by the Mauritian company from the sale of shares were in the nature of trading income or capital gains.

While we do not agree with the decision of the Tribunal as there are various key aspects of the tax legislation which were not addressed in the decision, the judgment forms a precedent which can only be reversed by the courts. We understand that the taxpayer has appealed the decision at the High Court.

This decision signifies the need for investors to scrutinise their structures and operations with respect to Kenyan investments to avoid potential tax disputes with the KRA, especially, with the enactment of the new CGT provisions.

Conclusion

The new CGT provisions and recent tax developments present potential tax risks to investors with investments in Kenya upon divestment. It is therefore important that private equity investors with investee companies in Kenya to undertake an analysis of their group structure and asset portfolio to determine whether there is a risk of an offshore divestment being subject to tax in Kenya. Where this is the case, various options may be employed to mitigate this risk.

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CHANGES TO CARBON TRADING IN KENYA

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On September 1, 2023, the Climate Change (Amendment) Act, 2023 (the Amendment Act) was signed into law by the President of Kenya. The Amendment Act amended the Climate Change Act, 2016, to provide a formal mechanism for the regulation of carbon markets in Kenya.

The Amendment Act provides for the participation in carbon markets through bilateral or multilateral trading agreements, engagement with private entities, or involvement in voluntary carbon markets and also provides a comprehensive approach to emissions mitigation through carbon reduction credits, removal or sequestration credits, technologies and projects on the whitelist, and emphasizes the significance of carbon removal and sequestration strategies for Kenya (including afforestation, reforestation, nature-based solutions, and advanced removal technologies).

The changes create a flexible and inclusive framework by offering diverse avenues for engaging in carbon trading to various industry players including the Government and private proponents, while addressing specific aspects of emissions reductions and carbon management. Entities may participate in Kenya's carbon markets through bilateral or multilateral trading agreements, trading with the Government, or in voluntary carbon markets.

The Amendment Act creates a distinction between land-based and non-land-based projects, although these specific types of projects are not defined in the Act. Land–based projects appear to be projects implemented through a community development agreement which governs the relationships and obligations of the stakeholders. With the amendments, the annual social contribution from proponents of land-based projects will need to be at least 40% of the aggregate earnings. For non-land-based projects, the annual social contribution from the project will need to be at least 25% of the aggregate earnings. The amendments are not clear on where mangrove or teal type projects will fall in terms of social contributions and set the thresholds higher than many other jurisdictions.

The Amendment Act establishes a National Carbon Registry (the Registry), which will be maintained by the Designated National Authority, being the National Environment Management Authority (NEMA). The Registry will serve three main purposes: (i) it will provide a centralized and authoritative platform for recording and tracking various aspects of carbon trading and emissions reduction efforts within Kenya; (ii) the Registry will maintain a register of Community Development Agreements, demonstrating Kenya's commitment to recognizing the rights and benefits of local communities impacted by carbon projects, and fostering transparency and fairness in benefit-sharing arrangements; and (iii) the Registry will record transfers, adjustments, and cancellations of carbon credits, thereby promoting integrity and preventing double-counting, which is essential for maintaining the environmental effectiveness of carbon trading and helping to avoid green-washing.

Every land-based project is expected to have a Community Development Agreement (CDA) in place. The CDA is intended to enable identification of the stakeholders of the project; the establishment of a framework for the involvement and engagement of communities in the carbon trading initiative; and to document the impacted communities' socio-economic development priorities. A "community" is defined under the Amendment Act as an organized group of individuals sharing common attributes such as Kenyan citizenship, ancestry, culture, livelihood, socio-economic interests, geographical and ecological location, and ethnicity. How a CDA would work where a project is on private land is not clear.

Every carbon trading project is required to obtain an Environmental and Social Impact Assessment ESIA). This requirement appears excessive, as not all carbon projects will meet the criteria under the Environmental Management Coordination Act (EMCA) for mandatory ESIAs. In our view, only those projects that would otherwise by their nature have been subject to EMCA should be required to obtain an ESIA. Projects that would not otherwise be subject to an ESIA under EMCA should not be subjected to such a process through the Amendment Act as doing so will only reduce the ability of the proposed carbon mechanism to effectively reduce, remove or avoid emissions across the targeted sectors in line with Kenya's Nationally Determined Contribution (NDC) targets.

Under the Amendment Act, any dispute in respect of a land-based project must be subject to the dispute resolution mechanisms set out in the CDA. Conversely any dispute that is not land-based must be settled through alternative dispute resolution in the first instance. Where a dispute is not resolved within 30 days, the dispute must be referred to the National Environmental Tribunal. While this may work for smaller projects, it is unlikely that larger investments or investors in projects that involve Government land, will be willing to subject their agreements to domestic dispute resolution, thereby effectively reducing the appetite for investment in such projects.

The Amendment Act establishes a framework for addressing a range of actions that undermine the integrity of carbon trading. Violations include: (i) unauthorized carbon trading or inadequate record-keeping, (ii) the dissemination of false information regarding environmental or financial benefits, (iii) involvement in money laundering through carbon projects, and (iv) the unauthorized sale of carbon credits. Individuals or entities found guilty of these offenses may incur significant penalties, with fines reaching a maximum of Kes. 500,000,000 and potential imprisonment for a period of up to 10 years.

In conclusion, the Amendment Act represents a significant step forward in Kenya's commitment to address climate change and develop a viable carbon market. This development is not only crucial from a climate impact perspective but also holds significant commercial prospects as the recognition of diverse stakeholders and establishment of a regulatory and implementation framework promotes transparency and accountability, which are aspects highly valued by investors and trading partners. However, there are certain gaps and shortcomings within the Amendment Act that require further refinement or clarification. Compliance markets, development of a local trading market, veracity of carbon credits prior to the Amendment Act, lack of clarity on carbon standards, mandatory referral to the National Environmental Tribunal, and community interests are some of the areas that need to be addressed. The commercial potential of Kenya's carbon market will only be maximized once these areas are fully addressed, and a failure to do so may result in reduced investor confidence in carbon reduction projects in Kenya creating a roadblock for the achievement of Kenya's NDC targets through voluntary cooperation.

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RWANDA – REGULATORY UPDATE FOR PRIVATE EQUITY INVESTORS

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L&R

Rwanda has been on a consistent path of transforming itself into an international financial destination attractive to investors seeking opportunities across the region and the African continent. This process has led to the country taking several steps to improve its regulatory landscape to attract investors and encourage private equity investments.

The setting up of the Kigali International Financial Centre (KIFC) has ensured the introduction of an investment oriented legal and regulatory framework that is fully compliant to international standards.

This article seeks to highlight the latest regulatory enactments that are likely to be of importance to private equity fund investors.

Tax regime

Several Laws[1] have been gazetted to implement comprehensive tax reforms following the Medium Term Revenue Strategy passed in May 2022. These laws included significant changes that will be of interest to private equity investors.

Focusing on corporate income tax, value added tax (VAT) and excise Duty, the tax reforms will reduce tax rates, broaden the tax base, seek to improve tax compliance and to curb tax evasion.

In determination of tax liability, corporate partners are subject to corporate income tax while individual partners are subject to personal income tax.

The Government of Rwanda has reduced the corporate income tax statutory rate from 30% to 28% with a special rate between 20 % and 25% for listed companies.

The law on income tax now excludes Partnerships from paying Corporate Income Tax by providing that income generated from general partnerships, limited partnerships and limited liability partnerships is taxable at the level of each individual partner. The partnership prepares its financial accounts, determines and declares the taxable share in profit of each partner, withholds and remits corresponding tax to the tax administration in accordance with the procedure prescribed by the tax administration. The partnership and the partners are jointly liable in case of a failure to meet these obligations. In determining the tax liability, corporate partners are subject to corporate income tax while individual partners are subject to personal income tax.

The law on income tax has also introduced a provision providing for the exemption from paying the withholding tax of 15% for newly registered taxpayers who are subject to withholding tax on payments, on goods imported for commercial use and on public tenders during the relevant annual tax period.

The Law nº 048/2023 of 05/09/2023 determining the sources of revenue and property of decentralized entities sets out new property tax and rates on land tax. The tax rate on immovable property has been set between zero to FRW 80 per square meter of the surface of land.

These rates are determined as follows; 0.5% of the market value of both the building and related plot of land for residential use; 0.3% of the market value of both building and related plot of land for commercial use; and 0.1% of the market value of both the building and related plot of land for industrial use, building and plot belonging to micro-enterprises and small business.

Tax on sale of immovable property is applied at 2% of the property value for registered taxpayers and 2.5% on non-registered tax payers. The first FRW 5,000,000 of sale of every immovable property will be tax exempt.

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[1] These Laws include Law nº 048/2023 of 05/09/2023 determining the sources of revenue and property of decentralized entities published in Official Gazette (O.G) n° Special of 14/09/2023, p.2; Law nº 049/2023 of 05/09/2023 establishing value added tax published in O.G n° Special of 14/09/2023, p.62; Law nº 050/2023 of 05/09/2023 establishing the excise duty published in OG n° Special of 14/09/2023, p.116; Law nº 027/2022 of 20/10/2022 establishing taxes on income published in Official Gazette nº Special of 28/10/2022; Law nº 051/2023 of 05/09/2023 amending Law nº 027/2022 of 20/10/2022 establishing taxes on income published in OG n° Special of 14/09/2023, p.141; Law n° 020/2023 of 31/03/2023 on tax procedures published in Official Gazette n° Special ter of 31/03/2023.

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Business Structures

(a) Collective investment Schemes

The law governing Collective Investment Schemes (CIS)[2] expands on the structures that may be utilized by private equity investors. A Collective investment scheme is defined as a type of scheme where there is an arrangement for collecting and pooling funds from investors or participants for the purpose of investment in the interest of each participant or investor represented by his or her proportional ownership in the scheme. The scope of this applies to Unit trust schemes, investment company schemes, partnership schemes and contractual schemes.

(b) Company structures

The Law n° 007/2021 of 05/02/2021 governing companies provides for private and public companies which are further categorized into five types namely: (i) a company limited by shares (ii) a company limited by guarantee; (iii) a company limited by shares and guarantee in which liabilities of the shareholders are limited to paid or unpaid amount on their shares but also may belimited by guarantee, where liabilities of members are limited to the amount that the members undertake to contribute to the assets of the company in case of winding up; (iv) an unlimited company where the legal liability of its members or shareholders is not limited, where all members or shareholders have total and joint liability to cover all contingent debts; and (v) a protected cell company in which a single legal entity consists of a core linked to several cells, each with separate assets and liabilities.

A company limited by shares and a company limited by shares and guarantee may be a private company or a public company. However, a company limited by guarantee and an unlimited company cannot be a public company. Any of these companies may be a limited life company. Individual cells of a protected cell company may also be established for a limited period of time. The ability to use of protected cell companies will be of interest to private equity and venture capital funds.

Rwanda, the Investment Law and Kigali International Finance Centre (KIFC) have provided tailor made incentives targeting different groups of investors including private equity investors.

Investment promotion and facilitation

In order to promote and facilitate investment in Rwanda, the Investment Law and Kigali International Finance Centre (KIFC) have provided tailor made incentives targeting different groups of investors including Private Equity Fund Investors.

(a) Pure holding company

An investor who establishes a pure holding company with total net assets consolidated in Rwanda being not less than USD1,000,000, annual expenditure in Rwanda of at least USD 15,000, a physical office of the company in Rwanda and with at 30% of the professional staff being Rwandan is entitled to tax incentives of 3% preferential corporate income tax rate and 0% preferential withholding tax on dividends, interest and royalty payments.

(b) A Special Purpose Vehicle (SPV) registered for investment purposes

An investor who registers a SPV for investment purposes who comply with the following conditions: in projects which are meant to last for more than two years, with total net assets consolidated in Rwanda being not less than USD 1,000,000,an annual expenditure in Rwanda of at least US D15,000,a physical office of the company in Rwanda, at least 30% of the professional staff are Rwandan is entitled to tax incentives that include 3% preferential corporate income tax rate and 0% preferential withholding tax on dividends, interest and royalty payments.

(c) Collective Investment Scheme

This is a type of scheme where there is an arrangement for collecting and pooling funds from investors or participants for the purpose of investment in the interest of each participant or investor represented by his or her proportional ownership in the pool.

An unlimited company which the legal liability of its members or shareholders is not limited, where all members or shareholders have total and joint liability to cover all contingent debts; and a protected cell company in which a single legal entity consists of a core linked to several cells, each with separate assets and liabilities.

[2] Law n° 062/2021 of 14/10/2021 governing Collective Investment Schemes published in Official Gazette nº Special of 02/11/2021

To qualify for tax incentives, the following are required: a minimum fund size of not less than USD 1,000,000 within the first three years, a minimum expenditure in Rwanda of USD50,000 per year, a CIS manager, custodian and operator established and registered in Rwanda with at least 30% of the professional staff being Rwandan citizens.

The tax incentives include a 3% preferential corporate income tax rate and 0% preferential withholding tax on dividends, interest and royalty payments.

(d) Global trading/Paper trading

This is a commercial entity making deposits in financial entities in Rwanda to finance its trading activities outside Rwanda and not authorized to import or export goods in Rwanda.

In order to qualify for tax incentives, it has to have the following: an annual turnover or trade volume of not less than USD10,000,000, an annual expenditure in Rwanda of at least USD50,000, at least 30% of the professional staff are Rwandan citizens and a physical office of the company in Rwanda.

The tax incentives are a 3% preferential corporate income tax rate and 0% preferential withholding tax on dividends, interest and royalty payments.

(e) Intellectual property company

This is a commercial entity that is established for the sole purpose of owning intellectual property rights.

In order to access the tax incentives, the company must haveannual expenditure in Rwanda of at least USD10,000, a physical office in Rwanda, to have a bank account in a bank operating in Rwanda, and at least thirty percent (30%) or three (3) of the staff are Rwandan citizens, whichever is higher.

The tax incentives are a 3% preferential corporate income tax rate and 0% preferential withholding tax on dividends, interest and royalty payments.

Tax incentives for other investment sectors

Tax incentives of 15% preferential corporate income tax rate and 0% preferential withholding tax on dividends, interest and royalty payments are now available for a range of investment companies and advisory firms operating in the financial services sector. These include a registered investor licensed to operate as a fund management entity, a collective investment scheme, a wealth management service provider, a financial advisory commercial entity, a family office services entity, a fund administrator, a financial technology commercial entity, a captive insurance scheme entity, a private bank, a mortgage fiance institution, fi ance lease commercial entity, Asset backed securities entity, reinsurance company, trust and corporate service providers.

Other than the tax incentives, the Investment Law also provides other incentives to registered investors which are of interest to a Private Equity investor.

(a) Immigration incentives

A registered investor who invests an equivalent of at least two hundred fifty thousand United States Dollars (USD 250,000) may recruit three foreign employees without necessarily demonstrating that their skills are lacking or insufficient in the labour market in Rwanda.

Under the new Income Tax Law, a resident taxpayer who was not resident in Rwanda in the five (5) years immediately prior to becoming resident and who works as an expert or a professional directly for an entity carrying out Kigali International Financial Centre licensed activities, is exempted from personal income tax on foreign sourced income during the first five (5) years following the date of becoming resident.

A non - resident taxpayer is only liable to personal income tax which has a source in Rwanda.

(b) Non – fiscal incentives

Upon fulfilling all tax obligations in Rwanda, an investor shall be allowed to repatriate the following;

- Capital profits derived from business activities; debt and interest on foreign loans; proceeds from the liquidation of investment
- Any other assets of an investor.

This is a commercial entity that is established for the sole purpose of owning intellectual property rights.

(c) Judicial incentives

Rwanda has entrenched the right to settle any dispute arising against a state organ or anyone through Alternative dispute resolution. An investor has a right to own private property, whether individually or collectively. Private property, whether individually or collectively owned, is inviolable. Any interest in or right over a property forming part of the investment cannot be seized or confiscated, except where provided for by relevant laws. Action to expropriate an investor's property deemed to be in the public interest can only be taken after the investor is given fair compensation in accordance with relevant laws. A foreign investor (creditor) can sell the debtor's movable or immovable property without going to court if such a clause is stipulated in an agreement.

Conclusion

These regulatory changes will ultimately enhance transparency, support entrepreneurship, attract institutional investments, facilitate cross-border investments, streamline processes, promote responsible investing, and create a favorable and conducive investment environment attractive to private equity and venture capital investors.

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MARKET BUILDING EFFORTS BEARING FRUIT

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Looking Backwards

In March 2022, we published an article (Rwanda – As A Financial Services Centre) highlighting the efforts of the Rwandan Government to develop an international financial centre, the Kigali International Financial Centre (KIFC), to catalyse Rwandan and African economic growth. In this article, we consider what has changed since then and identify areas which could benefit from new focus.

The previous article detailed the strategic and policy rationale for the KIFC and various organisations' work to turn rationale into reality. It summarised the legal, regulatory and tax framework typically required of a financial centre if it is to achieve market acceptance. The article concluded that Rwanda's efforts to implement a framework tailored to the needs of the private credit/equity and venture capital industry deserved the industry's support, noting the country's laudable aim to increase cross border and foreign direct investment in African businesses. The article also highlighted the long-term developmental need for a financial centre in the heart of Africa, what the building blocks for such a centre might be and whether those building blocks were in place in Rwanda.

This article explores the extent to which Rwanda's market building efforts are bearing fruit. We consider recent legal, regulatory and tax reform and current industry participation in the KIFC. We also consider what more the Rwandan Government might do to encourage the use of the KIFC as a conduit for investing in central, eastern, and southern Africa.

This article should be of greatest interest to fund managers and fund service providers, including administrators, bankers, custodians, fund formation lawyers and insurers. Based on long run growth projections, we believe that Africa's private capital fund industry will require more tailored financial centres to service its needs in future. Mauritius and Luxembourg will continue to play an important role. As will Morocco and, we anticipate, Rwanda.

Legal, Regulatory and Tax Changes

Much of the legal and regulatory heavy lifting has already been done in Rwanda with the promulgation of laws and regulations, which accommodate fund, holding company, special purpose vehicle, trust, foundation, and partnership structures familiar to the private equity and venture capital industry. However, the Rwandan Government continues to pass new laws and to fill gaps or improve the existing framework where it has been found wanting, for example:

1. Law N° 020/2023 of 31/03/2023 on tax procedures: streamlines tax administration procedures.
2. Law N° 018/2023 of 30/03/2023 amending Law N 008/2021 of 16/02/2021 governing partnerships: amends beneficial ownership requirements.
3. Law Nº 027/2022 of 20/10/2022: clarifies taxes on income.
4. Law No 017/2023 of 30/03/2023 amending Law No 13bis/2014 of 21/05/2014 governing the office of the notary: simplifies certification of foreign documents.
5. Law N° 021/2023 of 31/03/2023 governing the automatic exchange of information for tax purposes: enhances tax transparency in line with international best practice.
6. Law N° 019/2023 of 30/03/2023 amending Law N° 007/2021 of 05/02/2021 governing companies: amends beneficial ownership requirements.
7. Regulation N° 52/2022 of 01/09/2022 governing trust and company service providers: clarifies framework for operating in Rwanda.

There are also plans to amend other laws and regulations which are either unclear or no longer accord with evolving international best practice, to align with those of comparable jurisdictions. For example, under the Law governing Collective Investment Schemes (CIS), a "fund operator" is an entity licensed as an investment manager, which undertakes the dual function of managing and operating the CIS. The licence caters to both the management and the administration of the CIS. The investment manager can delegate some of its functions, although not those relating to its investment policy and asset allocation. Rwanda's Capital Markets Authority (CMA) is currently reviewing its legal framework to respond to market changes and create a specific fund administration licence next year.

In the meantime, service providers performing only fund administration services can apply to the CMA for a bespoke approval to carry out these limited services. Once the law has been changed, they will be able to apply for a licence.

Rwanda has also improved its tax practices and transparency having joined the multilateral Convention on Mutual Administrative Assistance in Tax Matters and the Eastern and Southern Africa Anti Money Laundering Group, which adopts and implements the recommendations of the inter-governmental Financial Action Task Force. It has also signed nine new tax treaties with, amongst others, China, France, Luxembourg, and Qatar with, we understand, at least 13 further tax treaties under negotiation.

From a commercial perspective, the tax regime remains competitive. Whilst the official withholding tax rate is 15% on interest, dividends and royalty and other payments to non-resident persons or entities, registered investors under the KIFC are exempted from withholding tax on interest, dividends, and royalties if they meet minimum economic substance requirements. The official capital gains tax rate is 5% but tax is exempted for the sale of shares and transfer of listed shares on the capital market, including other securities and sale of units of investment schemes. KIFC-registered investors are exempt from paying capital gains tax save for gains realised from the sale of immovable properties (i.e., real estate).

Market Participation

The KIFC has now licensed 12 private capital funds and eight trust and corporate service providers eligible to offer administration services to fund managers. We understand that several other licencing applications are under review presently.

For any new financial centre seeking to increase product awareness, information and transparency are key. We would recommend that Rwanda Finance Limited, the promoter of the KIFC, publishes a Q&A section on the KIFC's website to address the type of questions a cautious investment professional or fund formation lawyer might ask in relation to the KIFC as a possible fund domicile. For example, must a Rwanda-domiciled fund use the Kigali International Arbitration Centre as its dispute resolution forum? Answer, no. Or must a Rwanda-domiciled fund have significant numbers of Rwandan staff? Answer: yes, there must be Rwanda substance. Usually, 30%. Or is it correct, as a matter of Rwandan law, that no person can be forced to resign from a company? Answer, yes, but might there be workarounds using pre-signed resignation letters if, say, a fund manager is removed, and the investors and successor fund manager want to replace the incumbent manager's appointees on investee company boards with their own? This kind of additional guidance is likely to increase the market's confidence in using the KIFC.

KIFC Advantages

Rwanda's efforts to develop a fund management industry are assisted by limited foreign exchange control and ownership restrictions, the relative ease with which profits can be repatriated and a reputation for non-corruption (2nd highest score in Africa on the Transparency International Corruption Perceptions Index). Its technological connectivity is excellent, its education system produces bilingual speakers (English and French) and the number of direct flights to African, European (including my home, London) and Middle Eastern capitals is increasing.

KIFC Development Areas

Laws and regulations have changed fast. Very fast in some cases. In this context, some ministries appear to have overlapping responsibilities, which can cause confusion and slow down the review of licence applications and approvals. This should be addressed. The KIFC would also benefit from the deepening of the banking sector. The country has 10 commercial banks and a relatively light network of international correspondent banks (which, in fairness, does include Citibank, Deutsche Bank, Commerzbank, Standard Bank and First Rand amongst others). The country would also benefit from further double tax treaties, which benefit any country building a successful financial centre.

For any new financial centre seeking to increase product awareness, in formation and transparency are key. We would recommend that Rwanda Finance Limited, the promoter of the KIFC, publishes a Q&A section on the KIFC's website to address the type of questions a cautious invest ment professional or fund formation lawyer might ask in relation to the KIFC as a possible fund domicile. For example, must a Rwanda-domiciled fund use the Kigali International Arbitration Centre as its dispute resolution forum? Answer, no. Or must a Rwanda-domiciled fund have significant numbers of Rwandan staff? Answer: yes, there must be Rwanda substance.

Conclusion

Rwanda has a laser-like focus on the success of the KIFC with strong political support. The development of the KIFC is a key pillar of its vision to move to middle-income country status in 2035 and high-income country status in 2050.

Since our last article on the KIFC, fund managers and their advisers are increasingly considering the country as a fund domicile, some funds (often supported by African institutional capital) have domiciled there, and numerous fund administrators have opened in Kigali preparing for tomorrow. The hard and soft infrastructure required to support any financial services business, including connectivity (from broadband access to airports), accommodation (suitable office space and hotels), education and frankly, the "liveability" of Rwanda has improved.

As a development finance institution, we are delighted to see an African country developing a value-additive business in a methodical way. Hopefully, we will see more funds serving the African market domiciling there over time.

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RECENT SECTORAL AND FISCAL DEVELOPMENTS: IMPLICATIONS FOR NIGERIAN INVESTMENTS

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UDO UDOMA & BELO OSAGIE

Nigeria continues to evolve and to strengthen new and existing fiscal and monetary policies through business laws and regulations that aim to shore up revenue and to support the economy. There is a discernible increase in the sectoral regulation of investment and analogous transactions, and a widening of the capital gains tax net across various industries that have notable implications for investors and investment activity, including those in the private equity and venture capital space. This article explores some of the most recent key changes and their potential impact.

The Draft Nigerian Communications Commission Competition Practices Regulation, 2023

The Nigerian Communications Commission (NCC), the regulator of Nigeria's telecommunications sector, has proposed substantial amendments in the Draft Nigerian Communications Commission Competition Practices Regulation, 2023 (the "Draft Regulations"). These revisions build upon the 2007 NCC's Competition Practices Regulations ("2007 Regulations") and aim to enhance the criteria for transactions requiring prior NCC approval.

One critical correction is the adjustment of the threshold for NCC approval in cases of changes in shareholding. The 2007 Regulations mistakenly stated that approval was needed for transactions affecting "more than 100%" of a licensee's total shares. The Draft Regulations rectify this by setting the threshold at 10%, aligning with sections 27(a) of the 2007 Regulations and the Licensing Regulations, 2019.

Furthermore, any mergers and acquisitions (M&A) or investment resulting in a licensee transitioning from a private company to a public limited liability company will necessitate NCC approval. The effective date for the Draft Regulations remains pending confirmation.

The proposed amendments align the 2007 Regulations with existing practice. The requirement for NCC approval when transitioning from a private company to a public limited liability company may impact the structuring of M&A and investment deals in the telecommunications space. Private equity and venture capital investors considering investments in the Nigerian telecommunications sector should closely monitor the progress of the Draft Regulations in structuring investment strategies.

The National Insurance Commission's Revised Market Conduct Guidelines 2023

The National Insurance Commission (NAICOM) has issued the Revised Market Conduct Guidelines 2023 mandating prior NAICOM approval for transactions involving changes in ownership of Nigerian insurers that will entitle any person to either directly or indirectly control 10% or more of its equity. This provision aligns the guidelines with the Insurance Act, Cap I18 LFN, 2004.

The new guidelines, like regulations in other sectors, signify increased oversight and scrutiny in the insurance sector. Investors seeking to acquire qualifying ownership in Nigerian insurers should anticipate a more rigorous approval process and factor it into completion timelines and strategies.

Nigeria Civil Aviation Regulations 2023

The Nigeria Civil Aviation Authority (NCAA) has introduced the Nigeria Civil Aviation Regulations 2023 ("NCAR") following the Civil Aviation Act, 2022. Effective from July 10, 2023, the provisions of NCAR will replace an earlier 2015 version. The NCAR mandates the notification to the NCAA of all mergers, takeovers, joint ventures, or acquisitions of control in the aviation industry, including interlocking directorships.

These notifications apply when at least one involved company operates in Nigeria, the resultant market share is likely to create market power, and there is income generation in Nigeria relating to the sale or provision of civil aviation service, or where there is a use of a firm's assets in a manner that yields interest, royalties, and dividends.

As in other sectors, this NCAR broadens the scope of regulatory oversight in the aviation sector. Investors involved or proposing to be involved in mergers, takeovers, or joint ventures in the aviation industry need to prepare for increased scrutiny and regulatory reporting. Private equity and venture capital investors considering aviation-related investments will also need to account for the notification requirements and the potential impact on deal timelines and market power considerations.

Under the FA 2023, cryptocurrency and other digital assets are now considered to be chargeable assets under the Capital Gains Tax Act.

Fiscal developments

Capital gain tax (CGT) on digital Assets with effect from September 2023: The Finance Act, 2023 ("FA 2023") which was signed into law on 28th May 2023, and with effect from September 2023, imposes a 10% capital gains tax on the disposal of cryptocurrency and other digital assets. Under the FA 2023, cryptocurrency and other digital assets are now considered to be chargeable assets under the Capital Gains Tax Act. Given the spectrum of digital assets, the absence of a definition of the term "digital assets" creates a measure of uncertainty.

Extended loss relief period for capital gains: The amendments following the FA 2023 allow losses from the disposal of chargeable assets accruing to a person disposing of the asset or from other assets in the same class. Excess capital losses can now be carried forward for up to five years, starting from the year following their incurrence.

Eligibility for roll-over relief on disposals of stocks and shares: The FA 2023 introduces roll-over relief for the disposal of stocks and shares. Proceeds from qualifying disposals must be reinvested in shares, either within the same company or another Nigerian company, during the same assessment year.

The introduction of CGT on disposals of digital assets under the FA 2023 presents a new cost factor for investors in the cryptocurrency and digital asset space. Investors need to assess the tax implications of their digital asset holdings and disposals.

The extended loss relief period for capital gains may allow investors to offset losses against gains over a longer period, potentially reducing tax liabilities, a benefit that investors may consider in tax planning strategies. The introduction of roll-over relief for disposals of stocks and shares offers potential tax advantages for investors. Reinvesting proceeds in qualifying shares can defer CGT, which may also impact investment decisions and structuring.

Conclusion

These recent sectoral and fiscal developments in Nigeria carry both challenges and opportunities for investors. Nigeria's commitment to refining its regulatory environment underscores its potential as an attractive investment destination, including for private equity and venture capital, but careful consideration of these changes and their implications will be paramount to achieving successful and compliant investments.

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RECENT DEVELOPMENTS IN THE LEGAL FRAMEWORK OF THE ELECTRICITY INDUSTRY IN NIGERIA

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The regulatory framework for the Nigerian Electricity Supply Industry (NESI) experienced a seismic shift in the first half of the year 2023 as two legislative interventions, namely, the Constitution of the Federal Republic of Nigeria, 1999 (Fifth Alteration) (No. 17) Act, 2023 ("the Fifth Alteration Act") and the Electricity Act 2023, altered the status quo and effectively presented a new order for the NESI. Prior to these two enactments, there was a sole regulator[1] (and by extension, a single electricity market) for the NESI, controlled by the Federal Government. This was amidst concerns and arguments that the sector was by law, decentralised and ought to have been regulated jointly by the Federal and State governments. In this article, we will explore the status quo prior to the aforementioned enactments and also examine how they have laid to rest, various controversies surrounding the industry. The innovations in the new laws, as well as the opportunities created will also be explored.

THE LAW AS IT WAS

Prior to the enactment of the Fifth Alteration Act, Sections 13 and 14 of Part II of the Second Schedule to the Constitution of the Federal Republic of Nigeria 1999 ("the Constitution"), as amended, empowered the National Assembly as well as Houses of Assembly respectively, to make laws for the regulation of electricity. One cause for contention was Section 14 (b) which permitted Houses of Assembly to legislate on "the generation, transmission and distribution of electricity to areas not covered by a national grid system within that State". To start with, it was unclear as to which areas were covered by the national grid system and which areas, if any, were not. This was also not provided for under the now-repealed Electric Power Sector Reform Act (EPSRA) 2005. In addition, and to the detriment of the States, the EPSRA 2005 contained provisions which unified the electricity sector in Nigeria.

For instance, Section 62 (1) of EPSRA 2005 provided that no person shall, except under a license granted under the Act, engage in the business of electricity generation (except captive generation), electricity transmission, system operation, electricity distribution, or trading in electricity. This provision, among others, fuelled the view that the intention of the National Assembly was to exhaustively provide for the subject of the NESI. As a result, it was argued that State governments were stripped of the power to legislate on electricity for the following reasons:

1. any law of the Houses of Assembly which is inconsistent with EPSRA (an Act of the National Assembly) especially as it relates to regulatory authority, would therefore be void to the extent of its inconsistency and would give way to EPSRA, in respect of those areas already covered by EPSRA[2]; and

2. by virtue of the doctrine of "covering the field", any such law of a House of Assembly, (even if it is not inconsistent with EPSRA) would have been rendered inoperative to the extent covered by EPSRA. This is in consonance with the principles expressed in the Supreme Court's decision in AG Abia State & Ors v. AG Federation[3] where the court held as follows:

> "...the phrase 'covering the field' means precisely what it says. Where a matter legislated upon is in the concurrent list and the Federal Government has enacted a legislation in respect thereof, where the legislation enacted by the State is inconsistent with the legislation of the Federal Government it is indeed void and of no effect for inconsistency. Where however, the legislation enacted by the State is the same as the one enacted by the Federal Government, where the two legislations are in pari materia I respectfully take the view that the State Legislation is in abeyance and becomes inoperative for the period the Federal Legislation is in force. I will not say it is void. If for any reason the Federal Legislation is repealed, it is my humble view that the State legislation, which is in abeyance, is revived and becomes operative until there is another Federal legislation that covers the field."

In view of the above-mentioned position, there was a clamour for the decentralisation of the NESI. Lagos, Edo, and Kaduna States led the charge by setting up frameworks for the operation of the electricity sector within their respective States.

Lagos State, in 2021, through the Lagos State Ministry of Energy and Mineral Resources, issued the Lagos State Electricity Policy (the Electricity Policy)[4] which includes, among its objectives, the establishment of a regulatory framework for, and to license, all electricity market entities in Lagos State.

With the enactment of the Fifth Alteration Act and the Electricity Act 2023 (the Act), it is safe to say that all controversies and disputes regarding the decentralisation of the NESI have been laid to rest.

A NEW DAWN IN THE ELECTRICITY INDUSTRY

The Act introduces far-reaching innovations which, when effectively harnessed and implemented, can revamp the electricity industry and the power sector in general. These innovations are as detailed below:

1. **Consolidated Legal Framework**: The Electricity Act 2023 repeals and replaces the EPSRA 2005. It gives statutory backing to the National Power Training Institute of Nigeria (NAPTIN),[5] by formally establishing it while making provisions for its functions, powers, Governing Council and membership, among other things. The Act established the Hydroelectric Power Producing Areas Development Commission (N-HYPPADEC) to provide for the development of power-producing areas. The Act also re-established the Rural Electrification Agency and re-created the Nigerian Electricity Management Services Agency (NEMSA)[6] which was previously created vide the NEMSA Act of 2015. Curiously, the NEMSA Act was not expressly repealed. Given that it was almost entirely lifted into this new Act, it may be argued that the NEMSA Act 2015 is impliedly repealed or at the very least, rendered redundant. This is more so, because the preamble to the Act says that it consolidates the laws relating to the NESI (this includes the NEMSA Act 2015).

2. **Development of an Integrated National Electricity Policy and Strategic Implementation Plan**: The Act mandates the Federal Government through the Ministry responsible for Power to, within one year of the commencement of the Act, initiate the process for the preparation and publication of an Integrated National Electricity Policy and Strategic Implementation Plan (INEPSIP) in the Federal Government Gazette, in consultation with other stakeholders to guide the development of the electric power sector in Nigeria. The aspects which the INEPSIP should cover are listed in the Act. The INEPSIP is subject to review as required, but not later than every five (5) years. The initial INEPSIP or its revised versions are to be approved by the Federal Executive Council. This may serve as a guide to stakeholders on the projected outlook on the sector at the national level.

3. **Supervisory powers of the Minister and the functions of the Ministry:** Unlike the repealed Act, the extant Act has distinct provisions for the supervisory powers of the Minister, as well as the functions of the Ministry in charge of power. Among the Minister's supervisory powers are: issuing general policy directions to the NERC on matters pertaining to electricity, promoting the development of local content in the NESI, being responsible for the government's policy for the NESI, and advising the Federal Government on all matters pertaining to the NESI. The functions of the Ministry responsible for power include carrying out public-private partnership arrangements under the relevant statutory framework, coordinating the activities of the power sector, handling policy matters relating to research and development in the power sector, advising the Minister on all matters relating to conventional and renewable energy development and utilisation.

4. **Tariff Regulation:** The scope of the activities which are subject to tariff regulation, has been expanded to include electricity distribution franchising and any other activity that the NERC may deem fit to add. The methodology for fixing the prices of the activities which are subject to tariff regulation has also been expanded to include promoting co-generation and generation of electricity from renewable sources. The Act also requires the NERC to consider representations from licensees, license applicants, consumers, eligible customers, consumer associations, eligible customer associations, experts, and so on, while preparing a tariff methodology. This ensures that the interests and opinions of various stakeholders are taken into consideration. The Act also prevents the licensees from transferring the liabilities placed on them, as a result of fines, to their customers.[7]

5. **Establishment of the National Hydroelectric Power Producing Areas Development Commission (N-HYPPADEC):** Under this Act, the NERC is obligated to promote the generation of electricity using renewable sources. The Act establishes the National Hydroelectric Power Producing Areas Development Commission (N-HYPPADEC) with Power Producing States as members. Chairmanship of the N-HYPPADEC shall be rotated among the member states in alphabetical order and subsequently in the order in which new States become members. The composition of the N-HYPPADEC shall include a member from each of the remaining geopolitical zones. Its headquarters shall be in Minna, Niger State. The N-HYPPADEC shall have a Governing Council, the composition of which is provided for in the Act.

The overall goal of the N-HYPPADEC is to cater for the development of Hydroelectric Power Producing Areas.[8]

6. **Private Sector Involvement in Transmission Activities:** The Act also makes copious provisions for the involvement of the private sector in the transmission network, such as permitting private sector investment in the national grid.[9]

7. **Consumer Provisions:** Distribution Companies (DISCOs) are mandated to comply with the requirement to supply electricity through the installation of power meters from the date of commencement of the Act, except where the NERC extends the timeline of compliance with this requirement. This serves to check incidences of estimated billing, which consumers have complained about, over time. For accounting and audit purposes, the NERC can also direct licensees to install meters at the stages of generation, transmission, distribution, or trading, and at such places as may be deemed necessary. DISCOs are entitled to disconnect customers who are in default of their bills, after the prescribed notice period has been given. DISCOs are also entitled to recover the arrears owed but are barred from pursuing new tenants or landlords for the debt of the previous tenants or landlords.

8. **Decentralisation of the Electricity Sector:** Perhaps the most profound innovation in the Act is the provision that no person shall engage in the business of electricity generation, transmission, distribution, system operation, and supply of electricity without a license granted under State laws, save for those licensed by the NERC under the Act. [10] It is interesting that the Act did not provide for electricity trading as a business for which States can grant licenses. This implies that only the NERC can grant such a license. Nevertheless, other aspects such as electricity generation, transmission, distribution, and supply in Nigeria have been decentralised, as States can now fully regulate their own electricity networks and the various components of the electricity value chain within the various States.

9. **Private Sector Involvement in the Purchase and Resale of Electricity and Ancillary Services:** Preparatory to the medium and long-term electricity market stages, the NERC shall direct the Nigerian Bulk Electricity Trading Company (NBET) Plc to cease to enter into contracts for the purchase and resale of electricity and ancillary services and is expected to novate its existing contractual rights and obligations to other licensees [11] which have been licensed in accordance with Section 69 of the Act. These licensees are also empowered to enter contracts with generating companies, independent power producers, and other generators for the purchase and resale of electricity and ancillary services.[12]

10. **Cessation of System Operation Activities by the TCN:** The Act also mandates the Transmission Company of Nigeria (TCN) Plc to transfer the function of system operation to an Independent System Operator (ISO), which shall be incorporated by the TCN under the Companies and Allied Matters Act (CAMA) 2020 and with such subscribers as the NERC may determine, on such terms as the NERC may direct, where a substantially privatised market has been established. Consequently, the TCN shall cease to perform the function of system operation but shall retain its transmission function under its transmission license. The ISO shall have power to enter any arrangement with any entity or expert for the provision of technical support and expertise in the performance of its functions. The ISO shall be subject to the National Code of Corporate Governance.

It may be worthy of note that the State governments may also grant system operation licences within their territories to companies, and this is independent of whether or not the TCN continues to perform that function at the federal level.

11. **Promotion of Renewable Energy**: The Act adds new principal functions to the NERC, such as promoting the use of renewable energy services. As earlier mentioned, the methodology for fixing the prices of the activities which are subject to tariff regulation, has also been expanded to include promoting co-generation and generation of electricity from renewable sources. The Act also obligates the NERC to promote the distribution or supply of electricity from renewable sources.

12. **Penal Provisions:** Unlike the repealed law, the Act has created special provisions for offences. For instance, the Act criminalises the theft of electricity, electric lines and materials, receiving stolen electricity, interference with metres or works of licensees, among others. These provisions are perhaps in response to the trends of vandalism of electricity infrastructure and theft.

13. **Other Provisions:** The Act recognises as valid, the evolution and reform of the NESI from its vertically integrated service arrangement under the defunct National Electric Power Authority (NEPA) to the privatised stage implemented under the repealed Act, such as the unbundling of NEPA and the transfer of its assets, liabilities and staff to the initial holding company – the Power Holding Company of Nigeria (PHCN) – and the licensing of the 18 successor companies that emerged from the PHCN as distinct generation, transmission and distribution companies,

The Act focuses on the post-privatisation stage and tasks the NERC to ensure the development of the Nigerian electricity market from its current transitional electricity market stage to the medium and long-term electricity market stages or such other stages as the NERC may prescribe and, on such terms, preconditions or features that the NERC may approve. One of the main functions of the NERC is promoting gender mainstreaming and local content requirements within the NESI. When read in line with Section 227 of the Act, such local content requirements will include those contained in the **Regulations on National Content Development for the Power Sector, 2014,** such as procurements, employment and training, professional services, amongst others.[13]

OPPORTUNITIES ARISING FROM THE INNOVATIONS IN THE ACT

a) **Promoting Co-Generation and Generation of Electricity from Renewable Sources:** Ethical investors or other investors with interest and capacity in generating electricity from renewable sources are now encouraged to do so. This is more so as the NERC is obligated to promote co-generation and generation of electricity from renewable sources, via its methodology for fixing the prices of the activities which are subject to tariff regulation. An appropriate guide for investors through every stage of the process, from company formation [14] to licensing, amongst other regulatory requirements, would be necessary. Where the investors are foreigners, they will require a minimum share capital of N100,000,000:00 (One Hundred Million Naira) to qualify to obtain a business permit.[15] State governments may also want to partner with donor agencies for funding of electricity infrastructure. The African Development Bank (AfDB), for instance, has a portfolio of $12Billion of power projects, under which it manages the Sustainable Energy Fund for Africa (SEFA), which has focused on green mini-grids, energy efficiency initiatives and related areas. [16]

b) **Distribution or Supply of Electricity from Renewable Sources:** As it is with power generation from renewable sources, there is an opportunity for investors who may want to engage in the distribution or supply of electricity from renewable sources. The NERC is obligated to promote such businesses.

c) **Partnerships with the N-HYPPADEC:** The N-HYPPADEC was established with the clear mandate of bringing development to places that produce hydroelectric power. This offers opportunities for investors in many industries, such as construction, education, or even health, to collaborate with the N-HYPPADEC. Investors may be engaged by the N-HYPPADEC to construct roads and drainages, sink boreholes, build educational facilities, organise educational activities, supply books and other educational materials, provide medical supplies, and so on.

d) **Transfer of the Transmission Company of Nigeria (TCN) Plc's function of System Operation to an Independent System Operator (ISO) which is required to be incorporated by the TCN under the CAMA 2020 and with such subscribers as the NERC may determine**: In line with the Act, the NERC permits the TCN to set up an ISO and transfer its function of System Operation to the ISO. The TCN shall cease to perform the function of a System Operator, but shall retain its transmission function under its transmission license. This ISO is to be incorporated as a company under CAMA 2020 and shall have subscribers as may be determined by the NERC. This provides an avenue for foreign portfolio investors and domestic investors alike, to key into the ISO on such terms as the NERC may direct.

e) **Nigerian Bulk Electricity Trading Company (NBET) Plc's Cessation of Contracts for the Purchase and Resale of Electricity and Ancillary Services:** As earlier mentioned, preparatory to the medium and long-term electricity market stages, the NERC shall direct the Nigerian Bulk Electricity Trading Company (NBET) Plc to cease to enter into contracts for the purchase and resale of electricity and ancillary services and to novate its existing contractual rights and obligations to other licensees. This provides an avenue for investors to carry on the business of purchasing and reselling electricity. This decentralises the market and shifts it from having a sole participant (the NBET) to having multiple participants.

f) **Involvement of Private Sector in the Transmission Network:** The Act permits a non-licensee to make investments in the national grid in accordance with such Regulations as may be issued by the NERC. This gives room for non-licensees, subject to terms, to invest in the transmission owned, operated, and maintained by the TCN.

g) **The Creation of Distinct Electricity Markets for States:** The Act, coupled with the Fifth Alteration Act, creates unambiguously, a distinct electricity market in States, which they can fully regulate. Subject to the provisions of the Act, State governments can grant licenses for electricity generation, transmission, distribution, system operation, and supply of electricity within their respective States. This creates room for more investors to participate in the electricity markets at the State level, considering the fact that there is a large untapped energy market in the country.

The Energy Progress Report 2022 on Tracking SDG 7 has revealed that about 92 million Nigerians lack access to electricity.[17] In its 2023 report, Informa Markets, reports that less than a quarter of Nigerians in the rural areas have access to electricity.[18] These facts and figures can be exploited by investors, and this would in turn provide infrastructural development for the respective States and the country in general.

It is expected that States will take appropriate steps to putting the machinery in place, including legislation and infrastructure for generating, transmitting, and distributing electricity within their States. In this regard, it will be necessary for each State to engage stakeholders in the process of preparing such laws as needed for regulating the electricity industry in their respective States, to ensure consistency with the Electricity Act and the Constitution.

h) **Investment in the States' Electricity Infrastructure:** The implication of the powers granted to States to generate, transmit, distribute, and supply electricity, is that each State will have to put in place, the infrastructure necessary for these activities to take place. Power plants, power stations, transmission lines, distribution systems, and so on, will be required as infrastructure for the State's electricity industry and power sector. Putting these infrastructures in place could entail project financing, which is usually debt-based, but can make use of bonds and debt notes, or other traditional project finance structures. Equity financing, including the use of Islamic finance, can also be utilised in raising the needed funds.

Private participants may also require financing to set up the needed infrastructure for electricity distribution, amongst other things. Parties directly involved in the provision of electricity infrastructure, apart from financing, will also have to procure materials, assets, equipment, and other items for the projects. Creating the much-desired infrastructure will involve several industry players and service providers. To this end, State parties and businesses will normally enter various purchase and supply contracts with the relevant companies and private individuals.

CONCLUSION

A combination of the Fifth Alteration Act and the Electricity Act 2023 have revolutionised the electricity industry in Nigeria. Other innovations include the promotion of the use of renewable energy, the decentralisation of the electricity industry and the promotion of more private sector involvement, as well as investments.

These innovations, if properly exploited, will be of benefit to our overall development as a nation, particularly in aspects of capital project and infrastructure, while at the same time promoting a market-driven sector with potentially immense benefits to the consumers, investors and business owners, the States, and the economy at large in terms of reduction in production costs, increase in per capita income, improved living standards, employment opportunities, business growth and revenue generation for businesses as well as States. As with all other matters, it is always advisable for States, investors, business owners, and other industry players to consult experts and relevant stakeholders to assist or support them to achieve their regulatory goals and business objectives presented by the new electricity regime.

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[1] The Nigerian Electricity Regulatory Commission (NERC).
[2] See Section 4 (5) of the Constitution.
[3] (2002) LPELR-611(SC).
[4] See the Lagos State Electricity Policy, 2021.
[5] Part XIX of the Act.
[6] Part XVIII of the Act.
[7] Section 116 of the Act.
[8] Part VIII of the Act.
[9] Section 109 of the Act.
[10] Section 63 of the Act.
[11] Section 7 (2) (d) of the Act.
[12] Section 69 of the Act.
[13] Additionally, Section 164 (i) of the Act empowers the NERC to increase the contribution of renewable energy to Nigeria's energy mix by examining current National Content Development Regulations for the power sector to address local content requirements for local skill acquisition, local production, and assembly of solar photovoltaic (PV) components, deep cycle batteries, electro-mechanical components of SHP technology, wind power, boilers and turbines for cogeneration of less than 30 mw or other components as may be stipulated by the Commission for the development of renewable energy.
[14] Sections 863 and 78 of the Companies and Allied Matters Act 2020.
[15] Article 8.0 of the Revised Handbook on Expatriate Quota Administration 2022.
[16] See Informa Markets: West Africa Energy Outlook Report 2023.
[17] See Tracking SDG7: The Energy Progress Report, 2022.
[18] See Informa Markets, West Africa Energy Outlook Report, June 2023.

MAURITIUS: NEW PRODUCTS TO BOOST FUNDRAISING CAPABILITIES

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BOWMANS MAURITIUS

In the midst of a challenging fund-raising environment in the post-covid era, Mauritius has been pushing for greater recognition as a global funds jurisdiction by introducing novel structures and products in order to further expand its product offering and appeal to a wider audience of fund managers. The country has been very much reliant on its ties with the African and Asia continents and has developed a wide network of treaties to protect and promote cross-border investments and minimise double taxation, as well as creating a business-friendly local environment to facilitate cross-border transaction.

In the recent years, the securities and capital markets regulations have been relaxed in the context of securities being offered exclusively to sophisticated investors. The added formality of having resort to a locally licensed capital markets intermediary, or to have a foreign fund recognised by the Mauritius regulator, in order to market securities no longer applies where an offering is made to sophisticated investors only. However, the potential game-changer comes with a subtle amendment to the Mauritius Securities Act expressly allowing ''money market instruments' or 'debt instrument' as a permitted asset class in which Mauritius funds can invest.

Debt Funds

The status of a 'debt' fund by which we mean, a collective investment vehicle whose principal objective is to invest by way of loans, has been notoriously unclear in Mauritius regulations. This amendment puts Mauritius at par in terms of financial products offering with other domiciliation jurisdictions where debt as an investment instrument is quite common. The difficulty to raise a debt fund was long identified by commentators as a shortcoming in our product offering, particular for country which aspired to be a financial centre to the African continent at a time where lending interest rates are at an all-time high and there is a dire need for emerging business to access cheaper sources of finance. The difficulty was rooted in a two-pronged approach to financial services regulation, created by the divide between banking and non-banking financial services. Banking, which includes lending and money-market, is regulated by the Central Bank, while all other financial services are regulated by the Financial Services Commission. With a view to keep the two spheres of intervention by each regulator clear and distinct, investment funds, which are regulated by the Financial Services Commission, were prevented from investing via debt instruments which have been traditionally regarded as being the realm of the banks.

For many years Mauritius has been known as an ideal location for routing equity investments by both domestic and global funds while debt investments by funds have remained underutilised. Debt funds have traditionally preferred jurisdictions such as the Cayman Island or the British Virgin Island to operate from. With this development, there is a clear recognition that there is a portion of the debt market which is underserved by the banking industry and where funds can play a significant role as an alternative and more flexible source of debt financing given their experience with SMEs, startups and venture capital. It is also hoped that more debt funds will be set up using Mauritius as their domicile, but it is expected that local and international banks may set up their bespoke alternate funds to cater for previously underserved segments of the financial market.

Variable Capital Companies (VCCs)

Alongside these changes, the Variable Capital Company comes as a notable addition to the palette of fund vehicles consisting already of companies, trusts and partnerships. The Mauritius Variable Capital Company (VCC) was introduced through the enactment of the Variable Capital Companies Act 2022 (the Act) as an investment vehicle to provide an innovative and cost-effective vehicle for housing several funds under one legal entity, thus enabling various strategies under one roof.

A VCC is a body corporate which conducts its activities through its sub-funds and special purpose vehicles (SPVs). A sub-fund of a VCC fund may operate as a regulated fund, whether closed-end or open-end, and may elect to have a separate legal personality from that of the VCC fund. For many, it is considered as an upgrade to the Protected Cell Company (PCC) which provides for ring-fencing of assets and liabilities, but without the possibility of having cells with distinct legal personalities. This proved to be a drawback on exits in as much as the 'cell' housing an investment could not be detached from the main vehicle. Hence, fund managers frequently fell back on a fund owning multiple SPVs to ring-fence investments and facilitate exits.

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The main particularity of the VCC is that it allows for the existence of several legal persons within a structure. It challenges the age-old precept of a body corporate having a single legal personae and that personae's body of assets was readily available to meet the debt claims of that body corporate without possible recourse to the assets of the persons behind the body corporate.

The VCC goes further in ring-fencing protection, even at the risk of challenging the precept of legal persona of corporate bodies, such that where a sub-fund or SPV elects to have separate legal personality, such sub-fund or SPV is considered a separate "legal person", which means that the assets and liabilities of one sub-fund or SPV are legally completely separate from those of other sub-funds and SPVs within the same VCC. This faculty also enables a sub-fund to be transferred or migrated to another VCC or even exists as a stand-alone company. Another possibility is for one sub-fund to hold shares in another sub-fund or SPV within the same structure, potentially allowing a master-feeder structure to co-exist under one roof.

The cost saving will be significant in that the sub-funds are not required to have separate company secretaries, compliance officer or money-laundering officers. It has the option of having the same board or different board across its sub-funds, thus streamlining management and operations.

Local and international banks may set up their bespoke alternate funds to cater for previously underserved segments of the financial market.

Needless to say the segregation of assets and liabilities is a also huge advantage that allows for risk management and investor protection. If one sub-fund were to experience financial difficulties, the assets of other sub-funds would remain unaffected, providing a level of insulation. The assets of a sub-fund or SPV cannot be used to discharge any liability of the VCC or any of its other sub-funds or SPVs, including during winding up, administration or receivership of the sub-fund, SPV or VCC. Fund managers can set up different types of funds within the same structure and do simultaneous multi-offerings. They can also create funds targeting specific asset classes or investment strategies within the same vehicle, allowing them to tailor their fund structures to meet the unique needs and preferences of investors interested in those particular strategies.

End Note

Mauritius is the first country in Africa to have adopted VCC legislation, and in the region as of now, only Singapore boasts of a similar vehicle, which gives Mauritius an interesting value proposition added to the possibility of debt as an asset class. We expect to see VCC funds being set up to deploy both equity and debt financing in parallel, creating various kinds of mezzanine financial solutions. At the time of writing, 6 VCC funds that have been authorised by the Financial Services Commission and there are several other applications in the pipeline. While we do not expect the VCC to replace the limited partnership which has been tried and tested in the private equity space, we do expect that VCCs to gradually replace multi-class companies and PCCs as the vehicle of choice for open-ended funds, master-feeder structures and become a serious contender for PE funds which look to form multiple SPVs to manage risks and exits.

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SOUTH AFRICAN PRIVATE EQUITY FIRMS RISE ABOVE GLOBAL ECONOMIC STRESS

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New and amended legislation and economic pressures across Southern Africa are resulting in new opportunities as well as structural changes in the regions private equity (PE) industry in 2023.

PE is vital to the Southern African economy for a number of reasons. It drives job creation, acts as a catalyst for genuine economic transformation and attracts foreign investment. It introduces growth capital to a range of industries from infrastructure to technology, health care and venture capital. PE funds provide access to funding where more traditional sources of finance may not be available. PE continues to see activity from foreign investors, especially in the fund formation space, where international development finance institutions and other offshore institutional investors continue to target Africa for capital deployment. In South Africa for example, black-managed PE firms are increasingly participating more meaningfully in lucrative PE deals which is having the effect of, increasing the diversity of the PE sector and assisting with directing more investment towards black-owned businesses.

Here are some of the key trends that we have identified for 2023 and beyond.

Get ready for changes to the regulatory landscape

- The Conduct of Financial Institutions (COFI) Bill, once enacted, will further license and regulate new and established managers of alternative investment funds.
- Recently, amendments to Regulation 28 of the Pension Funds Act raised the limits on a retirement fund's infrastructure investments that have to be reported to the Financial Sector Conduct Authority. Now, direct infrastructure exposure across all asset categories cannot exceed 45% of a retirement fund's total assets (previously 30%), while PE asset allocation is now permitted at 15% (previously 10%).
- Merger clearance for private equity deals in Africa is becoming more rigorous, with regulators scrutinising PE firms acquiring extensive investments and intentionally structuring deals to avoid clearance obligations. Public interest considerations, such as job preservation and participation of historically disadvantaged persons, are now formally analysed, adding complexity. Developing a commercially feasible merger clearance strategy early on and finding creative solutions to address public interest challenges are crucial in navigating this evolving landscape.
- The "great resignation" has been felt in the PE sector, with portfolio companies continuing to experience high attrition, they remain at risk of losing valuable personnel and with them, confidential information to competitors. Carefully drafted employment agreements, which take cognizance of new issues in this regard, will become increasingly important in providing critical protections.
- Many share incentive schemes are under water and will need to be reset to align key personnel. It is becoming increasingly important to navigate the tax consequences of resetting incentive schemes, and as such, this should be carefully assessed.
- The Financial Intelligence Centre Act (FICA) now requires fund managers to "look behind the curtain" and conduct deeper due diligence on beneficial ownership, which could for example, include due diligence on the ultimate beneficial owners of the investors in a fund.
- Asset managers are accountable institutions and subject to new obligations to collect and retain certain records on the screening and monitoring of current and prospective employees. Managing these records needs to be done carefully to avoid breaching the Protection of Personal Information Act (POPIA).
- The Broad-based Black Economic Empowerment (B-BEEE) Commission is cracking down on fronting and in so doing, taking an increasingly restrictive interpretation of the law. It has been scrutinising the terms of transaction documents more closely, sometimes without referring to the provisions of the applicable B-BBEE legislation. Parties drafting a B-BBEE transaction have to ensure that they are compliant with the law.
- Public-private partnership procurement is on the rise, with changes to the electricity regulations allowing for an electricity trading platform, which will increase opportunities for PE firms to invest in the sector. Investments in public water and sanitation infrastructure are also opening up to the private sector, representing tangible opportunities for asset managers who are ready for them.

> Black-managed PE firms are increasingly participating more meaningfully in lucrative PE deals.

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Jurisdiction and domiciliation considerations

- Parties to cross-border acquisitions should be aware that the OECD's Pillar Two (under Base Erosion and Profit Shifting principles), which requires multinationals to pay a minimum of 15% tax in every jurisdiction, may be applicable. It is essential that PE fund structure and location allows the group of entities as a whole to be optimally assessed when determining whether the global minimum tax revenue threshold has been met.
- As ransom attacks become more frequent, reliable advice should be sought upfront to ensure that notification obligations, business continuity plans and ransom payments stay on the right side of the law, given recent legal developments on liability for fraudulent electronic transactions.
- International remote work can create compliance risks (including adverse tax and regulatory obligations) which are important to understand when considering a local presence in a foreign jurisdiction. Global mobility policies may be the solution to ensure key personnel can maintain flexible work arrangements.

> PE firms are increasingly undertaking more active portfolio management to ensure their assets are exit-ready.

- It's generally easier to enforce an arbitral award in a foreign jurisdiction than a court judgment - this is critical, particularly in a cross-border context. A well-crafted arbitration clause can help avoid significant procedural delays if a dispute arises. When drafting agreements, parties should take care in selecting the seat of arbitration and be aware of the location of the counterparty's assets because, in some jurisdictions, enforcement of awards can be difficult.

Still trending...

- We are seeing increased consolidation, especially of larger asset managers, as the most persistent trend into the future. One of the reasons is that fund raising has become more challenging as a result of continuing global events, including the Russia/Ukraine conflict, which has resulted in commodity price volatility; global inflation; the post-Brexit fallout and financial/ political instability in the UK; and the post-Covid decline in spending. Capital allocators are taking longer to conduct due diligence on PE firms, and it is becoming harder for PE firms to realise value on exits. Investors have become more circumspect, and a significant amount of capital remains unallocated. As a result, South African PE managers are partnering with offshore fund managers to try to attract capital.
- A second reason for consolidation is that PE firms are striving to distinguish themselves in an increasingly crowded market, whether through investment profile or targeted sector strategies/ return targets.
- Opportunities in Africa, especially in IT and fintech, are becoming more appealing than in more developed economies. Power and water supply challenges, which can be tackled using existing technological advancements in Europe and North America, are also opening up profitable opportunities.
- Other sectors attracting attention from PE firms are health care, energy, infrastructure, generative AI, data centres and consolidations of fibre networks. Many PE clients have invested in their own innovation labs and incubator programmes.
- ESG continues to remain an important consideration when structuring transactions.
- The acquisition of IP from South African-resident companies by companies in foreign jurisdictions is on the rise and requires sophisticated IP and exchange control structuring.
- Employee share ownership programs (ESOPs) and black private equity funds are increasingly being considered as viable B-BBEE partners.
- While market conditions make exits challenging and several disposal processes have been halted in their early stages, PE firms are increasingly undertaking more active portfolio management to ensure their assets are exit-ready.

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CO-INVESTING ALONG-SIDE AFRICAN PE FUND MANAGERS – AN OVERVIEW

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Co-investment transactions are on the rise globally, as tougher fund-raising conditions, higher-interest rates and increasingly sophisticated limited partners are leading fund managers to turn to co-investors to provide an additional source of funding. Already a useful tool for fund managers and limited partners investing in African companies, the use of co-investments in Africa is expected to grow as funds target larger investment opportunities.

In a typical fund investment, limited partners invest in a fund controlled by a fund manager, which in turn invests (directly or indirectly) in a blind pool of portfolio companies. In a co-investment transaction, a fund manager allows certain limited partners (the "co-investors") to make a "direct" equity contribution into one portfolio company alongside a fund: this can be achieved either through the fund manager setting up a new passive investment vehicle, or allowing the co-investor(s) to invest directly into the portfolio company.

Co-Investment Transactions

Benefits for a fund manager

The primary benefit of co-investment capital for a fund manager is that it increases the equity funding available for the target portfolio company. As fundraising has become more difficult, and high-interest rates prevent the gap in fund-raising being made up with debt, co-investments allow a fund manager to remain acquisitive.

Other benefits for a fund manager include:

Limited partner relationships. Limited partners want to be offered co-investment opportunities, as they increase their exposure to a portfolio company (discussed below). Fund managers will often offer co-investment opportunities as an incentive to "key" limited partners (early investors and/or larger limited partners), in order to build or retain a good relationship.

Portfolio diversification. Co-investment transactions free up liquidity for the fund to invest in additional portfolio companies, allowing the fund to diversify its portfolio. These transactions also allow the fund manager to gain additional exposure to a portfolio company if they are restricted from doing so through the main fund (i.e. as a result of investment or concentration restrictions).

Benefits for investors

- **Increased net returns.** Co-investments are typically on a reduced-fee reduced-carry arrangement, with co-investors benefiting from better net returns as a result.
- **Accelerated capital deployment.** Co-investment structures allow co-investors to commit additional capital and gain exposure to a portfolio company.
- **Fund manager insight and expertise.** Co-investment transactions allow co-investors to make direct investments with the benefit of the fund manager's investment team's analysis and negotiation. Some co-investors use these means to learn about an industry, an investment product or geography.

Key negotiated points

The principal investment documents for a co-investment transaction should be similar to the investment documents for the main fund. However, the fund manager will typically want additional flexibility to manage the co-investment vehicle, whereas a co-investor's main concern is ensuring alignment with the main fund in connection with any exit, follow on investment or other transaction, as well as any other specific oversight (for example, board or adviser roles) or information rights as desired.

The valuation of a late co-investor's interest in a portfolio company will be the key commercial consideration. The value of a co-investor's interest will directly affect the drag rights and other transfer restrictions.

A late co-investor should consider if the portfolio company is expected to have additional, subsequent equity fundraising rounds. If so, the co-investor's interest (direct or indirect) may be diluted at a later stage.

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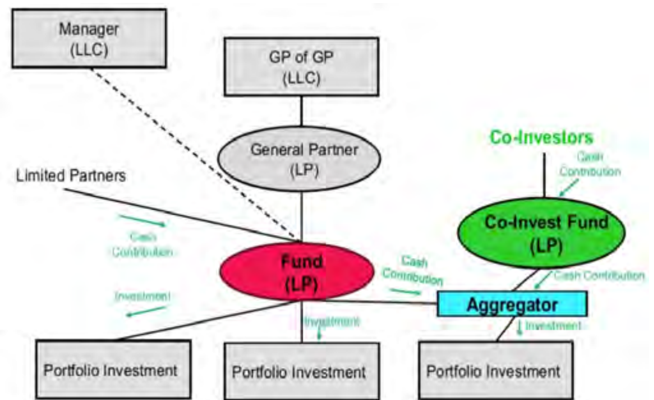
The negotiation of the co-investment documentation typically depends on:

- **Timing**. Whether the co-investor is investing prior to signing, prior to closing (but after signing) or as part of a post-closing syndication will change the documentation a co-investor will enter into and review, and will also affect the requests a co-investor will make and the protections it will require. This is discussed further below.
- **Relationship**. As above, co-investment opportunities are often offered to co-investors to develop or strengthen the relationship between the fund manager and a limited partner.
- **Co-investor's ticket**. The size of the co-investor's investment, in proportion to both the fund manager's investment and the overall transaction, will affect the co-investor's leverage and the rights it can obtain.
- **Target**. The jurisdiction of the target may affect negotiations. If the target is public, this will also affect a co-investor's requirements.
- **Co-investor requirements.** Prior to entering into co-investments, co-investors will need to ensure the investment doesn't breach any internal investment policies, including in relation to ESG, corporate governance or portfolio concentration restrictions. If any co-investor-specific issues arise, this will need to be considered in the structure of the transaction and the co-investment documents. The co-investor's side letter with the main fund will give guidance on how these requirements may play out in practice.
- Structure. The structure of the co-investment, including whether the investment is made directly, or through a limited partnership or private limited company, will affect the negotiation. This is discussed further below.
- Tax. Tax advice is key to any co-investment transaction, and any tax risk or assessment will drive the structure of the transaction.

Structuring Co-Investments

Co-investments are typically structured as either (i) an investment into a dedicated passive investment vehicle, which in turn invests (directly or indirectly) in a portfolio company on a side-by-side basis alongside the fund manager's main fund or (ii) a direct equity investment into the portfolio company by the co-investor.

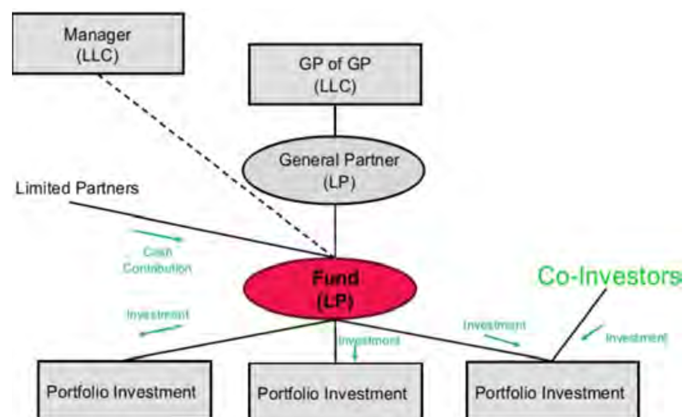
Side-by-side co-investment



A side-by-side co-investment vehicle can either be a limited partnership or a company. Typically, a partnership structure is used (as demonstrated in the above graphic), but a company may be used if required for tax or other reasons. Key features of a side-by-side investment structure include:

- **Passive investment.** A side-by-side vehicle should invest and exit on the same terms and at the same time as the main fund (pari passu), or alternatively, a co-investor should have look-through tag and drag rights. Co-investors would not generally have oversight (decision making or control) rights, other than pre-emptive rights; the fund manager will control the co-investment vehicle.
- **Fund manager's fiduciary duties**. The fund manager may owe fiduciary duties to a co-investor in such structures.

Direct co-invest



CO-INVESTING ALONG-SIDE AFRICAN PE FUND MANAGERS – AN OVERVIEW

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The main feature of a direct co-investment is that the co-investor, as a shareholder in the portfolio company, will be responsible for entering into corporate actions and taking any steps reserved for shareholders. To ensure alignment with the fund (and to prevent a co-investor being obstructive), the co-investor will typically enter into a shareholders' agreement with the fund. Other features of a direct investment include:

- **Exit rights**. Exit rights are typically structured as tag and drag rights (in respect of the fund, or any other majority investor, if applicable). As the fund manager is not involved once a direct investment has been made, the co-investor will be the party that elects to take up tag rights.
- **Fiduciary duties**. The fund manager will not owe any fiduciary duties to the co-investor in respect of the co-investment. The board of directors of the portfolio company is likely to owe fiduciary duties to the co-investor in the co-investor's capacity as a shareholder.

Timing Considerations

The co-investment documents, and a co-investor's key negotiation points, will be driven by whether the co-investment arrangement is entered into before or after the purchase agreement in respect of the relevant portfolio company is signed. The differences are considered below.

Pre-signing

- **Structuring**. As the purchase agreement hasn't been signed/the acquisition structuring not settled, a co-investor may, depending on their commitment size, be able to influence the structure of the underlying transaction and its terms. However, for the same reason, the fund (and the seller under the relevant purchase agreement) is likely to want the co-investor to enter into an equity commitment letter to ensure financing will be in place on closing.
- **Deal risk**. If the fund has agreed to pay (or receive) a broken deal fee, a co-investor who has entered into a co-investment arrangement pre-signing may participate alongside the fund.
- **Expenses**. The co-investor will have less visibility on the transaction expenses, and the fund manager will ask the co-investor to bear some portion of deal expenses, but may not be required to bear those expenses if the transaction does not close.
- **Diligence**. A co-investor will have more opportunity to review the fund manager's diligence of the transaction.
- **Suitability**. A fund manager will not want the co-investment documents to delay signing the transaction documents, and will require the co-investor to move quickly. Therefore, entering into a co-investment arrangement pre-signing may not be suitable for co-investors who cannot review documents and obtain appropriate internal sign-off/investment committee approval on short notice.

Post-signing

- **Structuring**. The co-investor will have less opportunity to influence the transaction or have specific requirements accommodated.
- **Deal risk**. The co-investor will have greater assurance on the likelihood of completion, and will be less exposed to any risk of broken deal fees becoming payable, or benefit of any such fees received from the seller.
- **Expenses**. Transaction expenses are more easily predictable.
- Diligence. Typically, a co-investor will be limited to "paper" diligence on a transaction.
- **Suitability**. A fund manager will be less dependent on the timing of a co-investor's entry into the co-investment documents post-signing.
- **Filings**. Post-signing co-investment transactions may implicate regulatory filings, especially in regulated industries and those with foreign direct investment or other regulatory scrutiny. Merger control should also be considered.

Late Co-Investors

In addition to the circumstances described above, where a co-investment transaction is entered into either before or shortly after a fund's investment into a portfolio company, a co-investment transaction can also be agreed at a much later stage of the fund's holding period of a portfolio company. These "late" co-investment transactions are considered below.

Circumstances leading to a late co-investment

- **Pre-IPO/exit**. A co-investment transaction prior to an IPO/exit allows the fund to demonstrate interest in the portfolio company, while the co-investor should benefit from the difference between the cost of their investment and the expected IPO/exit valuation.
- **Continuation fund**. A fund manager considering transferring a portfolio company to a continuation fund may view a late co-investment as providing useful evidence of such portfolio company's valuation.

- **New capital required.** A fund may have drawdown all its commitments, but intend to make further follow-on investments. Similarly, a portfolio company may require further capital, either into response to an acquisition opportunity or a market downturn pressuring its balance sheet.
- **Co-investor as a potential buyer.** A co-investor may take a minority position through a co-investment transaction with the intention to purchase the relevant portfolio company.

Difficulties arising in late co-investment transactions

The valuation of a late co-investor's interest in a portfolio company will be the key commercial consideration. The value of a co-investor's interest will directly affect the drag rights and other transfer restrictions.

A late co-investor should consider if the portfolio company is expected to have additional, subsequent equity fundraising rounds. If so, the co-investor's interest (direct or indirect) may be diluted at a later stage.

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OPTIMISING MERGER CONTROL REGULATION: A TOOL FOR INCREASING INVESTMENT IN AFRICA

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Deal certainty is a primordial consideration for financial investors. A crucial pillar that supports deal certainty is clear legislation that is enforced in a predictable manner. This is particularly important in the context of private equity transactions. Understanding the intricacies of merger control regulation is crucial when engaging in M&A activity across the continent.

Earlier this year, AVCA's Legal and Regulatory Committee conducted a comprehensive merger control survey to understand current merger control practices across the continent. This article offers suggestions on how some of the challenges identified in the survey and may be addressed to facilitate more capital flows to the continent.

Better clarity and harmonisation of laws

The survey identified a number of areas where better clarity is required on what transactions are notifiable. For example, South Africa and Tanzania were identified as not having clear legislation that would exclude internal restructurings from being classified as mergers and subsequently requiring antitrust approval. This ambiguity may lead to unnecessary delays when implementing such restructurings in these markets. However, in recent months the Fair Competition Commission in Tanzania has on occasion issues opinions to the effect that internal restructurings do not constitute a change of control and are therefore not notifiable.

The survey also identified a widespread use of public interest tests which in some jurisdictions (e.g., South Africa, Cameroon, Zambia and Zimbabwe) result in remedies frequently being imposed to require certain levels of employment, local sourcing, or presence to be maintained even in the absence of competition concerns. These public interest considerations lead to a higher proportion of notified mergers being subject to conditions. Such conditions can deter investment as they hinder buyers' abilities to make targets more efficient and competitive. It may be worth having such public interest considerations being outlined in legislation separate from competition law and as they often address concerns that are not of a competition law nature.

Additionally, improved congruence between national and supranational regulatory regimes would reduce the burden on various stakeholders having to comply with seemingly overlapping legislation. This sentiment was echoed in the results of the survey that showed that within economic communities, such as COMESA, it can be unclear whether the regional filing replaces the national one (in particular, in Egypt and Tunisia). Having to make filings at a national and supranational level that, on the face of it, appear to be duplicative ultimately increased the administrative burden and cost of doing deals. his also does not maximize the efficiency of either the national or regional authority's capacity as further discussed below.

Easy access to laws, regulations and guidance was also identified as a challenge in certain jurisdictions. Surveyed participants observed that in certain jurisdictions such as WAEMU, Tunisia or the DRC, the laws are only available in French, and in Egypt the law is only available in Arabic. Availing laws, regulations and guidance in a public portal, including English translations would improve access to and understanding of laws.

Clarity is often a result of an iterative process involving dialogue between the parties to which the laws apply and the regulator. Consequently, continued feedback and dialogue between all stakeholders is encouraged to build on existing regulatory frameworks to facilitate increased investment without compromising on competition concerns.

Reduced filing costs

As an example, the survey revealed that the filing fee of up to USD 200,000 for COMESA merger approvals is perceived as very high. In Nigeria, filing fees are calculated as a percentage of turnover/assets with no cap on the fee charged. Tanzania's filing fees (capped at TZS 100 million in the higher bracket, which is around USD 40,000 / EUR 37,000) are also perceived as very high and such fees are often higher where the target has several legal entities (as the regulator will often require filing fees to be paid in respect of each entity).

Whilst high filing fees may not in practice deter large transactions, they may disincentivise smaller businesses from pursuing acquisition strategies as a tool for growth. Certain countries are beginning to take measures to address this. For example, the Kenya Competition Authority announced that it shall exempt micro, small and medium sized enterprises from merger control requirements to stimulate the economy through start-ups and digital businesses. This is a welcome policy change that could be emulated by other countries across the continent.

> **Easy access to laws, regulations and guidance was also identified as a challenge in certain jurisdictions.**

Efficient resource allocation and collaboration amongst regulators

Due to the increase in transactional activity, many regulators are often capacity constrained. This results in delayed merger assessments (and consequently the overall deal timelines) from time to time.

One approach to reduce the strain on current resources of regulators across the continent would be to increase the filing thresholds. This would free up capacity to review the larger transactions and also decrease transaction costs for smaller business, which may in turn spur growth in the SME sector.

Additionally, fostering collaboration amongst antitrust regulators with overlapping jurisdictions could lead to better resource utilisation amongst such regulators by reducing the scope of overlap. This may be achieved by harmonising antitrust regimes and through knowledge and information sharing.

Moreover, with the ongoing implementation of the African Continental Free Trade Agreement to create to a singular free trade area in Africa, harmonisation of merger control regimes will be key to fostering growth in cross-border transactions and capital flows.

> **Improved congruence between national and supranational regulatory regimes would reduce the burden on various stakeholders having to comply with overlapping legislation.**

Conclusion

Merger control remains a pivotal aspect of deal making. Better access to and clarity of laws, harmonisation of merger control regimes, reduction in filing fees and bolstering capacity of regulators will go some way towards building a more robust competition regulatory framework.

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