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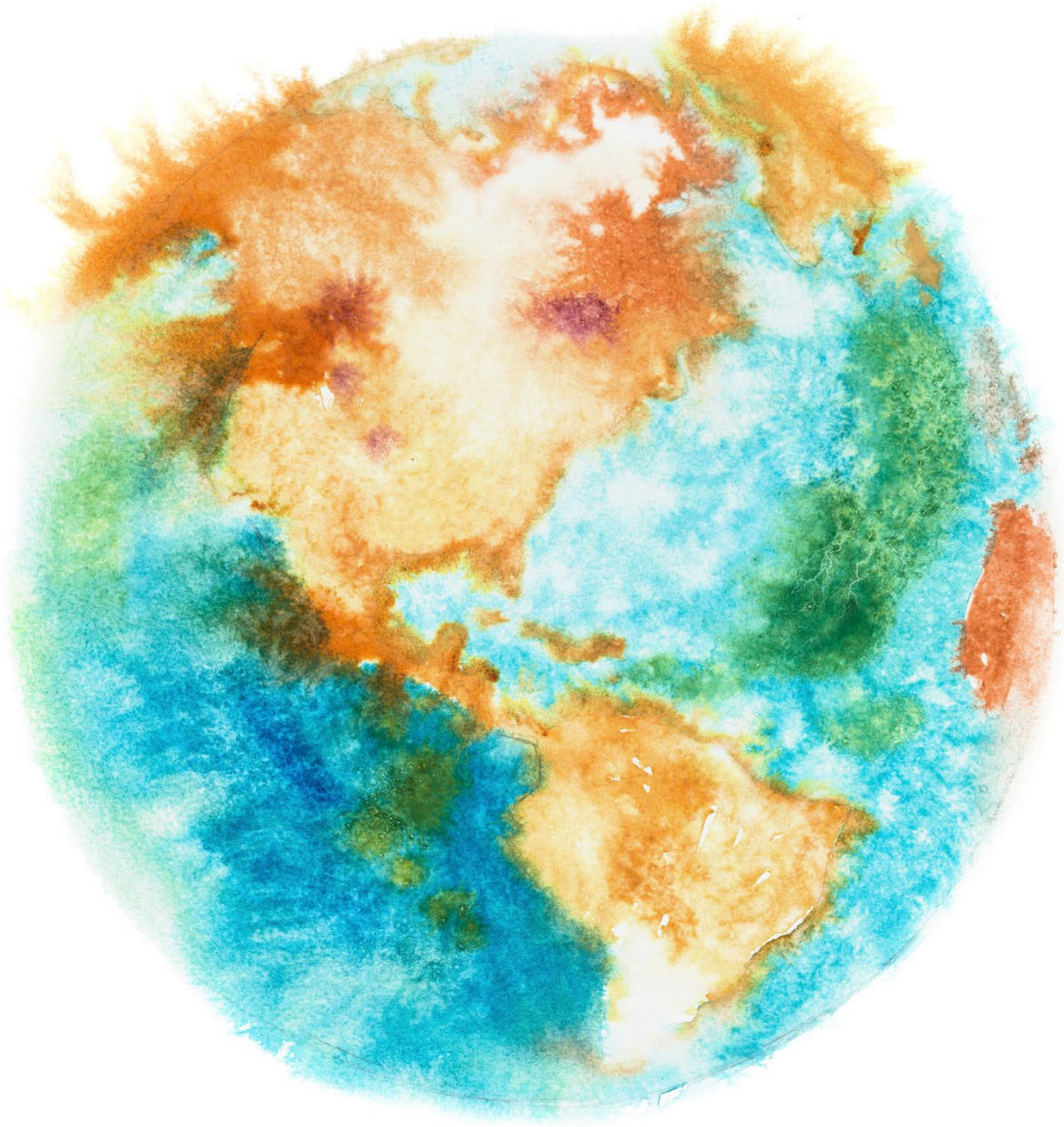

Tax Pitfalls to Avoid When Structuring a Financing in Francophone Africa

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Summary: Financial transactions taking place in Francophone Africa relating to investments, capital, or assets located there can be subject to certain taxes and formalities for the valid enforcement of the corresponding obligations locally. These can be costly for the foreign party to these agreements, hence some comments are offered below to better anticipate the relevant constraints.

Hundreds of millions of dollars flow into Western and Central African countries every year to finance the creation of new infrastructure and maintain existing water, transportation (roads, ports, airports, rails), and even costly electric infrastructure, in view of fueling growth.[1] Hundreds more will soon be needed to further develop infrastructure around the digital economy and adapt it to the effects of climate change. When advising on the structuring and financing of infrastructure projects or investments in Francophone Africa, a secured financing agreement and related guarantees are obviously necessary. However just as important is the ability to enforce these agreements if and when an event of default occurs. This article lists some critical tax points to take into consideration when developing similar projects in Francophone Africa in case no exemption or tax relief is available, whether it be through a double taxation treaty, multinational agreements, or otherwise.

Enforcing the provisions of a financing agreement and the guarantees securing it are subject to a tax formality which must be kept in mind from the outset. This is the case despite the fact that it will only be carried out after signing the agreements, hence at a time when there is generally less pressure on the parties. The formality is that of *registration*, inherited from French law and which consists in the recording of certain operations on a public registry in order to, among other reasons, give an official date to those operations (*ergo*, proving they existed at said date). This also ensures that the documents could not be tampered with since the tax administration keeps a copy of the original(s) in its records. Such a formality, dating as far back as the tenth century,[2] can seem obsolete today given the ever-increasing, sheer volume of electronic tools enabling quicker and safer online transactions. In reality registration has now become another means of collecting tax revenue on the transfer of assets from one party to another to some extent. Indeed, registration duties can apply either at a low fixed rate or at a proportional rate of the amount stated, or covered by the agreement at stake, which when it comes to the financing of sizeable projects, can quickly feel excessive, even more so if meant to cover a hypothetical need for the future enforcement of a security on the debtor's assets located in the relevant country. Even though in France excessive rates that were applicable to certain transactions have been reduced or repealed over time to increase the ease of doing business, most Francophone Central African countries still maintain proportional registration duties. For instance, while registration duties are not applicable to credit facility agreements in Senegal and Ivory Coast, they apply at a fixed rate in Gabon, and rise up to a proportional tax of one, two, or five percent in countries like the Republic of Congo, Cameroon, or Equatorial Guinea[3] respectively. Further, registration duties apply typically to all sorts of collaterals, which in effect decreases the ease of doing business.

There are some cases wherein this tax does not apply, but for the most part it can actually be preferable for the creditor that the registration formality be fulfilled. This is because the main consequence of not registering is that the corresponding documents would not be

[1] For further details, *see* Calderon,Cesar, Cantu Canales,Martha Catalina and Chuhan-Pole,Punam. *Infrastructure development in Sub-Saharan Africa: a scorecard*. World Bank Group. Policy Research working Paper no. WPS 8425. http://documents.worldbank.org/curated/en/866331525265592425/Infrastructure-development-in-Sub-Saharan-Africa-a-scorecard; *see also The World Bank Africa Annual Report 2021*, World Bank (October 1, 2021). https://www.worldbank.org/en/about/annual-report#anchor-annual.

[2] Daniel Gutmann. *Droit fiscal des affaires*, 12th Ed. (September 7, 2021).

[3] The legal system in Equatorial Guinea is based both on Spanish law as well as on regional legislation stemming from French law and contains a somewhat similar tax: the Asset Transfer Tax or, in Spanish, *Impuesto sobre Transmisiones Patrimoniales "Inter Vivos"*.

admissible in court or before any public authority. Therefore, in order for the relevant agreements to be enforceable and usable as evidence of the creditor's prerogative over the debtor's assets, they must first be registered. There is also typically no firm rule to identify the party which must bear the cost of registration duties (and penalties for late registration). The tax codes generally provide that the tax due can be sought from either party in the case of a bilateral agreement. However, at the time of an event of default of the debtor, the party that will need the agreements to be recognized as enforceable in court will be the creditor. At that point, the creditor will need to prepare the documentation for registration (including translating the relevant contracts to French or Spanish, as the case may be) and accept the accompanying fees. Even if typically, these charges are contractually subject to refund by the debtor, incurring further costs in order to ultimately be paid is less than ideal for the creditor.

However, it is also true that the creditor usually proposes the addition of gross-up clauses, stipulating that all amounts to be paid to said creditor shall be net of tax, i.e. without any withholdings (ranging from fourteen to twenty percent in Central African Francophone countries, for instance). Therefore, the effective sum is paid by the borrower and must be increased accordingly. The validity and enforceability of gross-up clauses have to be carefully and periodically verified since the grossing-up mechanism is not expressly regulated by law in the vast majority of Central African countries.

Finance documents entered into with foreign lenders may be governed according to foreign law and subject to foreign jurisdictional enforcement or international arbitration. However even in this case public policy rules and mandatory provisions of local law will still apply to such contracts. As a result, questions about the capacity of local parties will figure among the frequently raised issues when conducting a legal review of these transactions. Compliance with foreign exchange licensing requirements, each day more restrictive in CEMAC[4] and UEMOA[5] countries, as well as tax implications, are among the main items completing the legal checklist. Looking into the mechanisms of the tax registration formality, withholding tax and gross-up clauses, and ensuring that the necessary steps are properly anticipated and dealt with in a timely manner, are paramount to avoid unpleasant surprises further down the line from drafting project agreements with foreign entities.

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[4] The Central African Economic and Monetary Community, created in 1994, whose members are Cameroon, Central African Republic, Republic of Congo, Equatorial Guinea, Chad and Gabon.

[5] The West African Economic and Monetary Union, also created in 1994, today counting 8 members States (Benin, Burkina Faso, Ivory Coast, Mali, Niger, Senegal, Togo and Guinea-Bissau).