Regulation of Private Equity in West Africa—Emerging Trends

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A survey of regulations in Nigeria, Ghana, the Gambia, Cameroun, Burkina Faso and Guinea suggests that the ease and the success with which private equity funds and fund managers exploit opportunities in these jurisdictions depends, to a considerable extent, on the adequacy of the framework within which their investments are made.

With democracy, improving political and economic stability and the growth of a middle class boosting the demand for goods and services, there is a discernible increase in the appetite for investment in Sub-Saharan Africa. The current regulatory environment is conducive to this shift in focus to the African frontier as most legislation is reasonably investor-friendly. Private equity (PE) investment is still largely regulated within the generic investment framework in almost all of the countries profiled; there is a dearth of evolved, discrete PE-specific legislation and policy in the countries surveyed.

The one exception is Nigeria, which is leading the vanguard of change. Its draft regulations for domestic PE funds demonstrate a growing recognition of the significance of the role of PE investment in the region and, hopefully, the benefits of appropriate regulation. It is early days as yet, and it remains difficult to discern whether and when this promising start will result in further PE-specific regulation in Anglophone or Francophone West Africa.

Overview of Laws Governing Fund Establishment and Operations

Currently, the activities of PE funds and managers operating in the countries surveyed are governed by company, investment and financial services legislation and regulations in Nigeria, Ghana and the Gambia, and primarily by OHADA[1] in Burkina Faso, Cameroun and Guinea.

Although foreign investment is on the rise in the countries surveyed, other than Nigeria, there is no specific enabling legislation that focuses on the development of local PE funds. The Nigerian Securities and Exchange Commission (SEC) produced draft regulations in 2011 which, if adopted, will regulate domestic private equity funds with minimum commitments of N1 billion (approximately US$6.5 million). This may have been in response to the investments already taking place in Nigeria in the energy, telecommunications, banking and finance, real estate, consumer goods and healthcare sectors.[2] This development could also have been predicated by interest from global firms, such as The Carlyle Group, considering a local presence in the country.

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Vehicles Typically Used by PE Funds in These Jurisdictions

The lack of a strong enabling framework may explain why several PE funds and managers have traditionally preferred to invest in West Africa through investment vehicles domiciled in offshore financial centres such as Mauritius, the Cayman Islands and the British Virgin Islands, which offer relative ease of establishment, fiscal and legal efficacy, and the relative flexibility of a centralised hub for investing across Africa.

Limited liability companies domiciled in offshore centres are the most common investment vehicle in the survey countries. In the case of domestic fund vehicles, partnership structures are available under the partnership legislation of Nigeria, Ghana and the Gambia. Nigerian law permits limited and limited liability partnerships but partnerships incorporated under Ghana's Incorporated Private Partnerships Act do not have limited liability.

Incorporation requirements vary by jurisdiction. If a PE fund's proposed activities could be construed as "doing business in Nigeria," it must incorporate a limited liability company in Nigeria to conduct such activities. Ghana has similar "doing business" rules although foreign entities including PE funds may register under its Companies Act as "external companies."

Where the activities of PE funds operating in Gambia fall outside the purview of its Banking Act, they are not subject to its targeted regulation. Domestic funds with commitments below N1 billion (approximately US$6.5 million) may not be specifically regulated if the Nigerian SEC's draft rules are adopted. Burkina Faso, Cameroun and Guinea do not appear to exempt any distinct investment structures from regulation.

[1] Organisation pour l'Harmonisation en Afrique du Droit des Affaires treaty.

[2] PE investors active in Nigeria today include Helios, Aureos, Emerging Capital Partners, Actis, DPI, Harith and African Capital Alliance.

Marketing and Financial Promotions

Each of the survey countries regulate the marketing and financial promotion of PE funds to potential investors.

The Investments and Securities Act (ISA) and SEC regulations regulate schemes inviting or permitting members of the public in Nigeria to invest money or other assets in a portfolio.[3] Offshore funds offered to members of the public in foreign jurisdictions may only solicit investments from investors in Nigeria with SEC approval. The SEC's draft rules, however, restrict the solicitation of funds by domestic funds from the general public, but permit solicitation from Qualified Institutional Investors.[4] No person (including fund managers) may operate in the Nigerian capital market as an expert or professional unless they are SEC-registered.

Regulations released last year by the Nigerian National Pension Commission (PenCom) prohibit pension fund administrators from investing pension fund assets in PE funds that are not SEC-registered or managed by SEC-licensed fund managers. The SEC extensively regulates promotional materials used by registered funds. Comprehensive information memoranda must be distributed to investors. The content of offer instruments is also strictly prescribed.

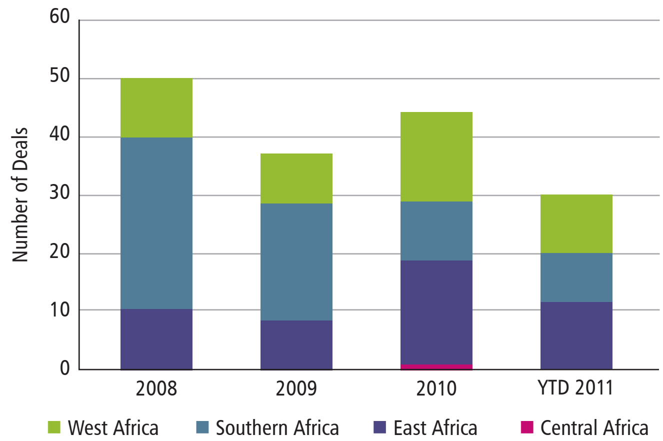
Gambian regulations permit marketing and promotions by licensed funds. Cameroun requires promotional activities to comply with laws on fair competition and publicity. Any practices designed to check, distort or significantly restrict competition on the domestic market are forbidden, and publicity must conform to rules of decency, morality and truth. To the extent that a fund is considered a "banking financial institution," Burkinabe laws restrict its promotional activities.

In Ghana, PE funds are not required to register with any regulators, unless the intention is to source investment funds from the Ghana Venture Capital Trust Fund, in which case fund managers must register as investment advisors with the local SEC. Ghanaian regulations permit marketing by PE funds if they do not constitute or relate to public offers of securities. In Guinea, no discrete marketing restrictions were highlighted.

[3] Section 69 of the ISA defines an invitation to the public as an offer that is (1) published, advertised or disseminated by newspaper, broadcasting, cinematography or any means whatsoever; (2) made to or circulated among any persons whether selected as members or as debenture holders of the company concerned or as clients of the persons making or circulating the invitation or in any other manner; (3) made to one or more persons upon the terms that the person or persons to whom it is made may renounce or assign the benefit of the offer or invitation or any of the securities in favour of any other person or persons; or, (4) made to one or more persons to acquire any securities dealt in by a securities exchange or capital trade point or in respect of which the invitation states that an application has been or shall be made for permission to deal in those securities on a securities or capital trade point.

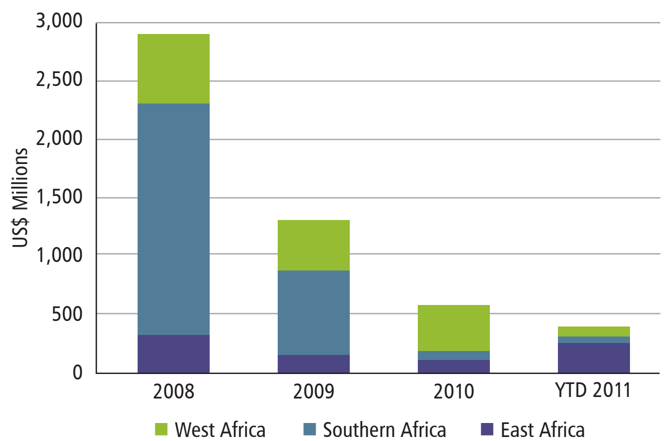
[4] The term 'Qualified Institutional Investor' is defined under the SEC Rules to mean a purchaser of securities that is financially sophisticated and legally recognised by the SEC, and includes fund managers, registered and/ or verifiable private equity funds, registered and/ or verifiable hedge funds and other operators determined by the SEC from time to time.

Figure 1: Sub-Saharan Africa PE Investment, Number Deals, 2008–2011Q3



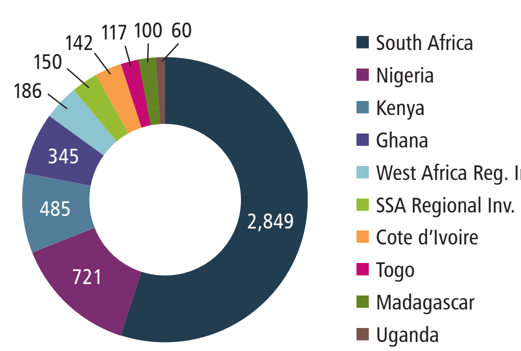
Source: EMPEA. Data as of 30 September 2011. Published 15 November 2011.

Figure 2: Sub-Saharan Africa PE Investment, Total Capital Invested (US$m), 2008–2011Q3



Source: EMPEA. Data as of 30 September 2011. Published 15 November 2011.

Figure 3: Sub-Saharan Africa PE Investment by Country, 2008–2011Q3 (US$m)



Source: EMPEA. Data as of 30 September 2011. Published 15 November 2011.

Reporting Obligations

Among the West African countries surveyed, Nigeria and Cameroun have the most detailed disclosure requirements.

Fund managers in Nigeria must file accounts and reports on fund activities with the SEC periodically. These accounts are not matters of public record, but may be made available to persons who make applications to review them. Where a fund is structured as a limited liability company or a limited liability partnership, audited accounts must be filed with the Corporate Affairs Commission or the Lagos State Partnerships Registry, as applicable, and is publicly available.

In Nigeria, the Money Laundering (Prohibition) Act which applies to financial institutions (including fund managers), requires such entities to report to the Economic and Financial Crimes Commission (EFCC) and the National Drug Law Enforcement Agency (NDLEA) any single transaction lodgement or transfer of funds in excess of N1 million (roughly US$6,500) or its equivalent in the case of individuals and N5 million (roughly US$32,000) or its equivalent in the case of a body corporate. "Suspicious transactions" must also be reported to the EFCC and the NDLEA.

Similarly, in Cameroun, anti-money laundering and anti-terrorism regulations require companies involved in launching and offering funds to report to the State Prosecutor (Procureur General) "all cases of funds received by from doubtful origin or suspected to originate from crime commission or tainted in the process of money laundering or the finance of terrorism." No other specific reporting obligations were indicated for Gambia and Burkina Faso.

Governance and Administration

Governance issues in PE-backed private companies are generally provided for under company laws in most surveyed jurisdictions.

Nigeria has, in addition, developed mandatory codes of corporate governance for public companies (SEC) and for banks and other financial institutions (the Central Bank). Governance issues in private companies with PE participation are typically addressed by contractual agreements and constitutional documents subject to the Companies and Allied Matters Act.

In both Ghana and Nigeria, incorporated companies must have at least two directors. There are no restrictions on foreign directorship in any country except Ghana, which requires even foreign directors to be Ghanaian residents. Only one-third of total board positions may be taken up by directors who are not shareholders in Guinean companies. Limited liability partnerships in Nigeria must have at least one designated partner who is responsible for administrative matters.

Investment Restrictions

In the case of domestic funds, investment prohibitions exist in Nigeria, Ghana, Cameroun and the Gambia. Nigeria prohibits investment in the production of arms and ammunition; military and paramilitary wear, immigration and prison services and the production of, and dealing in, narcotic drugs and psychotropic substances.

In Nigeria, sector-specific investment caps limit investment in banks, petroleum and telecommunications companies. Similarly, Ghana restricts investments in banking and mining. Foreigners (including companies with foreign shareholders) may not acquire more than a 50-year leasehold interest in land in Ghana. In the Gambia, the Central Bank prohibits certain investments or limits them to maximum percentage of capital assessed on a case by case basis.

Presently, compliance with investment restrictions and the implementation of environmental, social and governance ("ESG") systems are typically self-imposed by PE funds and their investors. Trading in toxic waste and products considered to be harmful to health, security and the environment is restricted in Cameroun. Given the importance that many PE funds and their investors place on ESG, more targeted legislation on these issues in a private equity context would be a positive and, no doubt, welcome development.

In addition to limiting or banning investment in certain sectors, some jurisdictions also impose requirements on domestic institutions to channel investment into domestic projects. The Pensions Commission of Nigeria Guidelines limit pension fund investments in PE to funds that will invest 75% or more of their assets in Nigerian companies or projects.

Exchange Control

Nigeria permits investors free capital inflow and remission of dividends and proceeds on disinvestment, subject to obtaining a certificate of capital importation from a Central Bank-authorised dealer at the time of investment. Gambian foreign exchange legislation was repealed over a decade ago. There are exchange control regulations in Guinea, Cameroun and Ghana that are comparatively weaker than South African mechanisms. Divestments from Cameroun (a CEMAC[5] state) must be declared to the Minister for Finance and the Central Bank for Central African States.

Country Risk Issues

Bribery, corruption and related offences are regulated by penal laws across the survey countries such as the Ghana Criminal Offences Act, the Gambian Criminal Code, and the Nigerian, Burkinabe, Guinean and Camerounian Penal Codes. Nigeria also has extensive regulations on bribery

[5] Economic Community of Central African States.

and corruption including the Economic and Financial Crimes Commission Act, the Independent Corrupt Practices Commission Act and the Criminal Code Act. Ghana has also enacted the Economic and Organised Crime Office Act. Cameroun has ratified the UN Convention Against Corruption.

The implications of the UK Bribery Act 2010 have been widely considered in Nigeria. Investors falling within its purview and that of the U.S. Foreign Corrupt Practices Act typically develop operational guidelines and provide targeted training within their local operations to ensure compliance. Extensive due diligence and effective local management continue to be useful tools for managing corruption risk.

Across the surveyed states existing investment laws appear to prioritise the creation of a secure investment environment. The risk of governments changing the rules and upending underlying assumptions for investment appears to be reduced or mitigated by the use of mechanisms such as government guarantees and political risk insurance from international agencies such as MIGA.[6]

Enforcement of Judgments

Foreign law judgments and arbitration awards are recognised and enforceable in each of the survey countries. OHADA provides reciprocity in enforcement of judgments. Nigeria, Burkina Faso, and Cameroun are signatories to the 1958 New York Convention on the Recognition and Enforcement of Arbitral Awards.

Conclusion

It is hoped that the issuance of PE-specific regulations in Nigeria heralds an increasingly focused approach to the regulation of private equity in West Africa.

While the existing regulatory environment in the surveyed countries is relatively investor-friendly, the operational and supervisory framework is also likely to become more tailored, in turn enabling more robust PE investment in the region. The next natural step in this evolutionary process is for the enactment of more discrete enabling legislation that addresses regulatory, tax and related issues that are PE-specific, to provide the much needed 'pull' for greater PE-participation and investment in West Africa.

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[6] Multilateral Investment Guarantee Agency.

