

The Brief

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Oil & Gas Update

Structuring of foreign investments in the hydrocarbons sector

A successful investment in the hydrocarbons sector in Africa does not only require ensuring the validity and the extent of hydrocarbons rights, it also requires careful structuring, especially for foreign companies holding rights in several assets in different jurisdictions. In this context, failure to implement the best structure for such an investment may entail certain difficulties in terms of management of the same and may especially have significantly adverse effect on the achieved/expected profitability.

Hereunder is a checklist of the main issues to be taken into account in the structuring process.

- Most petroleum laws in Africa consider petroleum activities as **commercial activities**. Therefore, the legal structure of a foreign investment should comply with the commercial company law in force in the investment country, which shall regulate *inter alia* the legal form, the incorporation, the management and the dissolution of commercial companies. Commercial company law in Africa often provides two main legal structures: i) **companies**, which are considered as legal persons and usually include several forms, and ii) **branches**, which are not considered as legal persons.
- Foreign investors tend to prefer to structure investment in the investment country through a branch for the following main reasons:

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- Legal requirements and administrative burdens pertaining to branches are usually mainly limited to the requirement to register in the investment country and file an annual tax return for corporate tax purposes, whereas companies, being legal persons, are often subject to additional legal requirements and administrative burdens, such as the requirement to constitute certain management bodies (general assembly of shareholders, board of directors and officers), to hold annual meetings, to file annual financial statements and to appoint statutory auditors.
- Proceeds shall automatically flow back to the foreign investor as and when the same are generated in the case of a branch, whereas allocation of proceeds back to the foreign investor will ultimately require a distribution of dividends in the case of a company. OHADA member countries however, often require financial year to close on 31 December and the OHADA Uniform Act relating to accounting rules does not allow the payment of interim dividends, then delaying allocation of proceeds to the foreign investor to the following financial year. In such a case, allocation of proceeds back to the foreign investor before the annual allocation of dividends may require implementing alternative mechanisms such as for instance a loan to the foreign investor from its local subsidiary and an agreement for technical assistance, subject to conditions.
- Although the investment could be implemented directly in the investment country, foreign investors tend however to prefer to structure investment in the investment country through one or several **special purpose vehicles**, to be incorporated in countries other than the investor and the investment countries. A branch of such special purpose vehicle is subsequently registered in the investment country for implementation of the investment. Determination of the place of incorporation of the special purpose vehicle shall depend on certain factors, including the nature of the investment, the investor country and the investment country. In addition to accounting and tax advantages, such an international structuring may be of interest for the following main reasons:
 - Since a branch does not constitute a legal person, potential responsibility claims shall not be handled in the investment country, where the legal environment may be relatively uncertain, but in the country where the special purpose vehicle is incorporated, where the legal environment is often clearer and the potential responsibility more predictable. It may also be easier to manage potential claims in the country where the special purpose vehicle is incorporated rather than in the investor country, where the political and social constraints may be relatively significant. In this context, environmental claims for instance, even eventually unsuccessful, may indeed be preferably handled in the country where the special purpose vehicle is incorporated.
 - A company, incorporated in the investment country, shall be subject to certain local laws, such as for instance bankruptcy laws. Certain countries in Africa, such as for instance Chad and Niger, have entered into the OHADA Treaty dated 17 October 1993, which harmonised business laws and regulations in the 17 member countries. Commercial companies operating in Chad and Niger are governed by the OHADA Uniform Act relating to bankruptcy proceedings. This Act may require the management of the company to be taken over or even the company to be liquidated in the event of a bankruptcy. Since a branch does not constitute a legal person, it shall not be subject to bankruptcy laws in the investment country. Bankruptcy shall therefore not be handled in the investment country but in the country where the special purpose vehicle is incorporated, where it may be easier to manage rather than in the investment country.
 - In addition, such a special purpose vehicle shall constitute a corporate veil to the direct responsibility of the foreign investor. In this context, special purpose vehicles may allow to effectively mitigate the responsibility of the foreign investor pertaining to operations in the investment country, the latter being ultimately liable to indirect responsibility only. It may also be easier to manage potential responsibility claims in the country where the special purpose vehicle is incorporated rather than in the investor country. In this context, environmental claims for instance, even eventually unsuccessful, may indeed be preferably handled in the country where the special purpose vehicle is incorporated, especially if the foreign investor is listed on a stock exchange in the investor country. Similarly, such a special vehicle shall constitute a corporate veil to the direct bankruptcy of the foreign investor and to the direct allocation of the related losses, if the investment were not successful.



- Finally, such a special purpose vehicle shall provide additional flexibility in terms of assignment, allowing the foreign investor to assign either the asset directly or the shares of the special purpose vehicles holding the asset. Such flexibility may also have an impact on the value, and therefore the consideration, for the shares/assets to be assigned.
- Hydrocarbons laws and regulations of the investment country however often require foreign investors to incorporate a **company** in the investment country:
 - Based on petroleum law dated 2 May 2007 for instance, the contractor to a petroleum contract is required to incorporate a local company for performance of exploration, exploitation and transportation activities in Chad. It seems however that this requirement only refers to the signatories of the petroleum contract and it could be argued that other companies holding participating interest in the related petroleum contract would not be subject to this requirement.
 - Similarly, based on petroleum law dated 31 January 2007 for instance, the foreign holder of an exclusive exploration authorisation is required to incorporate a local company for performance of exploration, exploitation and transportation activities in Niger. It seems however that this requirement only refers to the holder of an exclusive exploration authorisation and it could be argued that other companies holding participating interest in the related production sharing contract only would not be subject to this requirement.
- Certain countries in Africa, such as for instance Chad and Niger, have entered into the OHADA Treaty dated 17 October 1993, which harmonised business laws and regulations in the 17 member countries. Commercial companies operating in Chad and Niger are governed by the **OHADA Uniform Act relating to commercial companies and economic interest groupings dated 17 April 1997**, which was drafted mainly on the basis of the company law in force in France. This harmonisation facilitates the implementation of foreign investment and is therefore a significant incentive. We attach a presentation of OHADA in Chinese language for your information.
- The laws and regulations in force in the **investor country** may also provide specific legal and tax requirements and options for structuring an investment in a foreign country, which requirements and options should always be considered in the first place in order to consider the best way to structure an investment in a foreign country. The laws and regulations in force in the People's Republic of China for instance provide for certain requirements and options. We attach a presentation of the main mechanism in Chinese language for your information.
- Certain countries in Africa have entered into **tax, customs and/or exchange control treaties**, which harmonised tax, customs and/or exchange control laws and regulations in the member countries. This harmonisation facilitates the implementation of foreign investment and may also provide optimisation tools for foreign investors. We attach a presentation of such treaties in Chinese language for your information.

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