

Financing the Real Sector in Nigeria

Introduction

A few weeks ago, Dangote Industries Limited, the Nigerian holding company for the businesses of Africa's most successful business person, announced the signing of a loan facility agreement for US\$3.15 Billion to part finance the construction of a crude oil refinery with a production capacity of 400,000 barrels of crude oil and 600,000 metric tonnes of polypropylene per day; and a fertilizer plant with a capacity of 2.8 metric tonnes of urea per annum. The announcement is remarkable for a number of reasons, not least the fact that it is not just the only major financing transaction in

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Nigeria's "nonstarter" private refining industry, but also the fact that never before has so much money been advanced to a single borrower in a single financing transaction in Nigeria.

One aspect of the story, which seldom featured in the news stories that trailed the announcement, is the significance of the transaction within the Nigerian corporate finance space.

About US\$2 Billion (two thirds) of the financing commitment was secured from Nigerian banks, the majority of the mandated lead arrangers were Nigerian banks and, alongside international counsel, Nigerian law firms guided the parties to a successful execution of the transaction. [Banwo & Ighodalo](#) advised the Dangote Group. The deal is a loud and clear testament to the continuing development of the framework for financing the real sector in Nigeria.

Since the beginning of 2013 there have been a number of other clear (but perhaps not so loud) testimonies. In the telecommunications industry, in April MTN Nigeria announced a N470 Billion medium term financing from a consortium of Nigerian and foreign banks with

Nigerian banks providing up to 70% of the financing. Subsequently in June, Emerging Markets Telecoms Service Limited (Etisalat Nigeria) announced the signing of agreements for a US\$1.2 Billion medium-term syndicated loan facility to be provided by a club of 13 banks.¹ Also, in the days running up to the August 21st deadline set for payment of balances for the assets recently sold by the Bureau of Public Enterprises (“BPE”) under the Nigerian Power Sector Privatisation program, thirteen (13) of the preferred bidders concluded financing transactions totaling about US\$1.734 Billion. The majority of this funding also came from Nigerian banks.²

¹ Both on this transaction and on an earlier US\$650 Million financing transaction in 2011, Banwo & Ighodalo acted as sole legal counsel to the Banks.

² Of total financing secured, Banwo & Ighodalo was involved, either as lenders’ counsel or borrower’s counsel on deals worth US\$664.7 Million.

However, all of these testimonies should not lead one to think that the Nigerian commercial and legal framework for financing the real sector has come of age. Although these tend not to be apparent in the grand signing ceremonies, the negotiations of these deals have seldom been smooth sailing. The framework is far from perfect and a great deal of development is still required particularly in the areas of perfection and costs of taking security. The focus of this piece is on perfection costs and their impact on financing transactions.

The Package...

As with other jurisdictions, the security packages typically required for Nigerian financing transactions tend to follow a relatively straightforward pattern. There will normally be at least one All Assets Debenture (sometimes constituted by a “security deed”), which creates a fixed and floating

charge over the assets of the borrower(s). In addition, subject to the specific nuances of the particular transaction, lenders will normally also require some form of charge over all (or a controlling percentage) of the shares of the borrower. This will normally be provided by the main sponsor(s) of the borrower who will also (in most cases) be guaranteeing the financing. In addition to the foregoing, where there are any special assets such as land or ships, for which separate public registries are maintained, the lenders will usually also require that specific mortgages be created and registered in respect of such assets. There may also be some assignment of offtake contracts and the charge of revenue streams therefrom or execution of direct agreements where these are relevant to the underlying transactions/projects being financed.

Perfection Costs

For most of the security described in the foregoing paragraph to be fully effective, admissible in court and enforceable against relevant security providers, all of the security documents will need to be stamped by the Stamp Duties Office of the Federal Inland Revenue Service.³ Further, where the security is registrable under the Companies and Allied Matters Act Cap C20 LFN 2004 ("**CAMA**"), it will also be registered at the Corporate Affairs Commission ("**CAC**").

In addition to the foregoing, subject to the specific nature of the security, other requirements which may need to be complied with include:

- (a) (in the case of real property) procurement of the relevant state governor's consent and registration in the relevant lands registry, and
- (b) (In the case of shares of a publicly quoted company) registration of a lien with the Central Securities Clearing System Plc. ("**CSCS**").

Stamping

Under the existing framework, in connection with the stamping of security documents, stamp duty is chargeable at an ad valorem rate of 0.375% of the amount secured subject to the particular type of security and the nature of the assets involved.⁴ The duty is

imposed by the Stamp Duties Act Cap S8 Laws of the Federation of Nigeria ("**LFN**") 2004 ("**SDA**") which was originally enacted in 1939 and which has not been amended since 1964. Under the SDA, relevant instruments are required to be stamped within thirty (30) days of execution or where executed outside Nigeria, within thirty (30) days of receipt of the instrument in Nigeria. The obligation to stamp is statutorily imposed on the obligee; although in practice, the burden for the payment of the duty is usually transferred to the obligor. Under the SDA, any instruments required to be stamped are precluded from being received in evidence by a Nigerian court without the required duty and applicable penalties,⁵ first being paid. Where several instruments

³ In relation to transactions between individuals (as opposed to corporate entities) the applicable authority for stamp duty purposes will be the relevant State Revenue Service Stamp Duties Office.

⁴ Certain categories of security documents such as documents creating a charge on the shares of a company are only subject to nominal stamp duties at the rate of ₦500 (Five Hundred Naira).

⁵ Late payment of stamp duty attracts a penalty of interest at the rate of ten percent (10%) per annum from the due date up to the time when the amount of interest is equal to the unpaid duty.

(security documents) are employed in securing the same debt, the SDA permits parties to determine for themselves the instrument, which shall be deemed the principal document and to pay the ad valorem duty thereon accordingly. The SDA stipulates rates for non-principal/auxiliary instruments however, in practice; the Stamp Duties Office often stamps the other instruments at a nominal duty rate (usually N500).

Registration

Section 197 (1) of the CAMA prescribes that certain charges created by a company with the intention that it provide security, shall be void against the liquidator and any creditor of the company unless it is registered with the Corporate Affairs Commission ("**CAC**") within ninety (90) days of its creation. The CAMA requires the registration of all floating

charges and specified categories of fixed charges including charges "**for the purpose of securing any issue of debentures.**"

The registration with the CAC is done after stamping of the security documents and attracts a fee of one percent (1%) of the amount secured.

Governor's Consent

Under the Nigerian land tenure system as enshrined in the Land Use Act, Cap L22 LFN 2004 ("**LUA**"), the consent of the state governor in the state where land is situate is required for any alienation of land. The Nigerian courts have interpreted the requirement of governor's consent to be applicable to the transfer of legal title to land, whether by way of a sale or mortgage. The process of creation of a mortgage entails an initial consent to the

mortgage instrument by the governor⁶ followed by a separate stamping of the document and a registration with the relevant state land registry. A fee of about 1% of the secured amount is chargeable as consent fee in most states in Nigeria.

CSCS Lien

For shares listed on the Nigerian Stock Exchange ("**NSE**"), in addition to a share charge, to restrict and guard against dealings with the relevant shares, lenders will normally require that a lien be registered with the CSCS such that the shares cannot be dealt with except with the consent of the lenders. This process entails the submission of a joint memorandum from the borrower and the security trustee/lenders, to the CSCS together with

⁶ In many instances this power will typically have been delegated to a commissioner/permanent secretary for lands.

payment of lien charges in the sum of 0.25% of the value of the security.

Compared to costs in the UK...

Assuming (as will typically be the case) that a single financing transaction involved the full bouquet of security discussed above, the total cost of perfection would be somewhere in the region of 2.625% of the secured amount. Putting this in a practical context, in the absence of any efficient but legal structuring (and assuming that the typical security package was adopted), the perfection costs for the Dangote financing described above could potentially have been in the region of US\$82,687,500 (Eighty Two Million, Six Hundred and Eighty Seven Thousand, Five Hundred US Dollars). These costs are clearly too high. To perfect a similar security package in the UK, costs would be in the region

of a lump sum fee of circa £1,000. Fees for registering a charge at the UK Companies House are currently set at between £10 and £13.⁷ There is no requirement for payment of stamp duties on a charge and no requirement similar to governor's consent for creation of mortgages. For registration of security interests in the UK Lands Registry, fees are currently set at up to £910, subject to the value of the property.⁸

The current level of perfection costs in Nigeria adds an extra layer of complexity to Nigerian financing transactions as parties and their counsel invariably have to spend substantial time structuring, evaluating and negotiating various valid forms of

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<http://www.companieshouse.gov.uk/infoAndGuide/faq/companyCM.shtml>

⁸ http://www.landregistry.gov.uk/_data/assets/pdf_file/0006/18627/registration-services-fees-october-2012.pdf

alternatives and tweaks to the traditional security package structures in order to reduce costs without diminishing the strength of the security. Inevitably, perfection cost issues have in the past scuttled what would have otherwise been a straight forward financing transaction and, on several occasions, borrowers have had to obtain additional financing in order to meet the huge perfection costs. Indeed the challenges occasioned by perfections cost cannot be fully divorced from the seemingly *laissez faire* attitude of many banks to the perfection of security interests prior to the Sanusi era at the Central Bank of Nigeria ("CBN"). At such high rates, the incentive to avoid the perfection costs will be significant.

However, in the face of these challenges, Nigerian law firms have risen to the task and have worked to develop various

mechanisms for minimizing costs. Security packages feature the deposit of original title documents and blank transfer forms in escrow to aid the process of enforcement should the need arise. In addition, building on the fact that stamp duty and CAC filing fees are only payable on the amount agreed by the parties as the sum to be covered by the security, that is, a “secured amount” (which may be different from the facility amount), the practice has developed of parties deciding to initially pay stamp duties and CAC filing fees based only on an agreed secured amount and subsequently, where the need arises (i.e. where the borrower defaults on his repayment obligations), upstamping i.e. increasing the secured amount to the full facility amount and paying the difference in stamp duty and CAC filing fees. This structure ensures that the parties only incur the full stamp

duty obligation where the need arises. In this regard, section 202 of the CAMA permits parties to a registrable charge to determine a figure as the maximum amount secured by the charge, particularly where the charge secures fluctuating or uncertain amounts. The proviso to section 202 of CAMA further states that the maximum sum deemed to be secured by a registrable charge can be increased at any time prior to the winding up of a company, provided additional stamp duty is “subsequently” paid on such increase.

The structure is however not without its risks which include the fact that the relevant security document will only be enforceable in respect of the balance of the facility amount, from the date of upstamping thereof and charges registered by third parties over the same asset during the intervening period may claim

priority over the balance.⁹ Also, even though section 202 of CAMA suggests that parties can upstamp at any time before the commencement of winding-up proceedings, the provisions of section 495(1) of CAMA are however to the effect that every payment made by an insolvent company in favour of any creditor, with a view to giving such creditor a preference over other creditors shall, if winding up proceedings are commenced in respect of the company making the payment, within three (3) months after the date of the payment, be deemed fraudulent and void as against the liquidator of the company. In view of this section, where the upstamping structure is adopted, lenders run the risk that an upstamping payment made within the three (3) months preceding winding up of the borrower

⁹ This can however be mitigated where the obligee holds the original title documents; thus curtailing the obligor’s ability to validly deal in the security.

company may be deemed a fraudulent preference and therefore voided.

Beyond any innovative structures or arrangements which lawyers may develop for getting around the issue, what is really required is some statutory reform to the framework for financing transactions to bring costs to more manageable levels. This will go a long way to encouraging debt capital raising by Nigerian companies and easing the process for structuring financing deals.

Conclusion

In spite of the significant cost challenges, current CBN aggregate statistics show that lending to the real sector is growing. What may be inferred from the volume and size of the transactions described above is that in the face of all the odds, Nigerian advisers have become ever more adept at structuring

transactions within the existing legal and commercial framework such that board credit committees of Nigerian banks are becoming increasingly comfortable with innovative security arrangements and are therefore able to increase lending to the real sector. Nonetheless it is hoped that beyond the periodic calls for increased lending to the real sector, the Federal Government will undertake a review of Nigerian perfection costs to bring them more in line with the objectives of growing lending to the real sector and thereby accelerating the attainment of the economic objectives of the Government's transformation agenda.