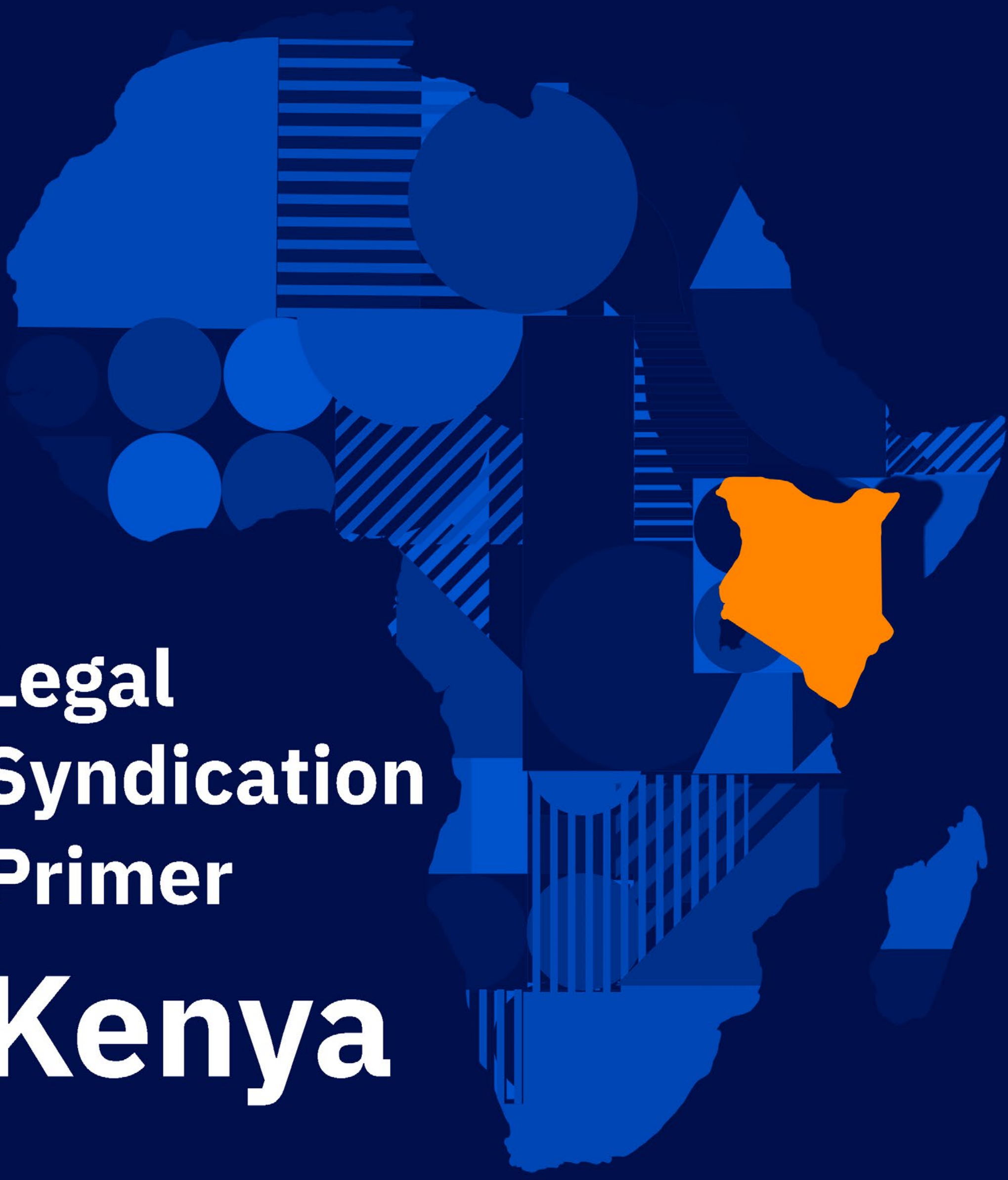

Legal Syndication Primer Kenya

Created by

BOWMANS

African Angel Academy

IN PARTNERSHIP WITH

International Tech Hub Network

Department for Digital, Culture, Media & Sport

Legal Syndication Primer

Kenya

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African Angel Academy

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Introduction

About the African Angel Academy

The African Angel Academy (AAA) is an online programme and knowledge community, which was established in 2020 by Viridian and ViKtoria Ventures, supported by the African Business Angel Network (ABAN), to grow the number of active angel investors on the continent. Drawing on the expertise of early-stage investors from across Africa, the Academy offers virtual learning and networking courses for those looking to start or grow their angel investing portfolio. As of 2022, AAA's alumni network comprises close to 400 (and counting) individuals representing more than 18 angel investing groups in 11 countries.

The AAA course is available for anyone to purchase and start learning at their own pace or to learn as part of cohort programmes AAA runs with partners throughout the year. In the cohort format, the online course is offered to selected participants along with live masterclasses, Q&As, networking and mentorship opportunities, and showcases spotlighting promising local startups.

To find out more about AAA's programme and course offerings, visit africanangelacademy.com/programmes.

The African Angel Academy is endorsed by the African Business Angel Network (ABAN).

About Viridian

Viridian is an impact agency that designs and delivers programmes for early-stage entrepreneurs, investors and entrepreneur support organisations across Africa's entrepreneurial ecosystem. Our programmes act as a catalyst for these key economic actors, ultimately growing shared prosperity across Sub-Saharan Africa.

www.viridian.africa

About ViKtoria Ventures

ViKtoria Ventures is a consulting and fund management firm with a focus on entrepreneurial finance in East Africa.

www.viktoria.co.ke

About the International Tech Hub Network

These guides were developed with support from the UK–South Africa Tech Hub, UK–Kenya Tech Hub, and UK–Nigeria Tech Hub. These hubs are part of the International Tech Hub network delivered by DCMS (Department for Digital, Culture, Media, and Sport), under a UK government initiative designed to promote inclusive growth of digital ecosystems in partner countries. Over the past two years, the Tech Hubs have partnered with the African Angel Academy to train, network, and mentor emerging angel investors and groups, connecting them to promising local startups and supporting them through an alumni network.

About the authors

Coulson Harney LLP (Bowmans Kenya) is a full corporate and commercial law firm providing legal advice and transaction services to a wide range of international and local clients in Kenya. The firm has 21 partners and directors and over 50 lawyers with qualifications and work experience drawn from private legal practice in the public and private sectors of Kenya, the United Kingdom, and Australia. Some of the lawyers are admitted as solicitors in England and Wales, allowing us to provide seamless advice on English-law-governed financing in the region. Our enhanced English law expertise helps us to effectively assist clients operating in Africa's increasingly sophisticated financial markets, especially those that involve cross-border projects in search of growth and funding from international financial institutions.

About the Kenya Syndication Legal Primer

This short guide was developed as a resource for a new supplementary AAA module, the AAA Active Angel Series Syndication Module. This module builds on the AAA foundational online course and aims to equip programme alumni with the knowledge and confidence to participate in syndicated deals, and to promote collaboration within the angel investing ecosystem. The guide outlines common syndication and angel deal structures available to angels in Kenya as of January 2023. For further detail on each structure and the suitability of using a specific structure for your deal or syndicate, please feel free to reach out to Bowmans Kenya on info-ke@bowmanslaw.com.

This guide comprises the following sections:

Part 1: Syndication structures

Part one of this guide provides an overview of the various syndication structures/vehicles available to angels making investments in Kenya. It explores the advantages and disadvantages of each structure, and any tax, legal or compliance requirements when using the structure.

According to research conducted by Briter and ABAN in 2021, there were more than 58 active angel syndicates on the African continent, and this number is expected to be higher in the new report which was released in November 2022 in partnership with the African Angel Academy.

AAA strongly encourages programme participants to either join or form a syndicate in their angel investing journey, depending on their experience level. Not only does syndication have significant benefits for the participating angels but it can have significant impact on startup success. For angels, syndicating is a great way to learn more about the investing process from more experienced leads, access more deal flow, access larger deals (by pooling capital) and, of course, to decrease their risk by building a diversified portfolio with access to a diversified pool of expertise. Startups may benefit from having a pool of angels with different backgrounds who are a great resource from a knowledge and networks perspective.

Part 2: Angel transaction structures

The second section of the guide looks at the available structures for angel investment deals in Kenya. It also outlines the advantages and disadvantages of each structure, and any tax or legal implications or compliance requirements.

The 2021 *Analysing Africa's Angel Investment Landscape* survey also discovered that 58% of investors were using multiple or mixed structures when making deals, although the use of SAFEs and convertible notes is growing in popularity.

The selection of transaction structure(s) will impact an investment's management and returns, and it is worth considering the implications.

Please note that the content of this guide cannot be considered to be legal advice, and AAA or Coulson Harney LLP (Bowmans Kenya) is not responsible for any consequences arising from the selection of any of the structures outlined in this guide.

These course notes serve as an introduction to the legal structures angel investors in Kenya can employ when making an investment and structuring a syndicate.

These notes have been developed by Bowmans Kenya for the African Angel Academy as part of the African Angel Academy's Syndication Module. The content developed for this module was funded by the UK Government's International Tech Hub Network via its UK–Kenya Tech Hub.

Part 1

Syndication legal structures

Overview of legal framework

There is no specific legal framework relating to angel investors and angel investments in Kenya. Angel investors and angel investments are thus subject to Kenyan laws ordinarily applicable to general investors and businesses. However, specific sectors may have certain requirements on the angel investors if the startup/investee operates in a regulated sector, e.g., insurance, telecommunications, and banking sectors. In addition, different laws may apply depending on the syndication structure adopted by the angel investors. Generally, the relationship between the corporate form of the syndication structure (if any, i.e. in the case of limited liability partnership, limited liability company), investee entities, and the angel investors would be subject to the general laws of contract, and the parties have autonomy in agreeing the contractual terms, subject to any mandatory legal requirements such as statutory voting thresholds to pass certain decisions.

Popular basic syndication structures

The most popular syndication structures in Kenya are the use of limited liability companies, limited liability partnerships, and direct/individual investing. Whereas in recent years we have seen the interposing of Delaware entities as holding companies for local startups, the syndication structures have remained the same, with the difference being that the investment is made at the Delaware level rather than at the local level.

If the startup/investee is incorporated in a different jurisdiction, the requirements of the syndication structure, the legal requirements relating to an investment by the syndication structure in such a startup/investee, and the tax implications on distributions of returns to the investors will depend on the laws of the startup/investee's country of incorporation. Below, we discuss the different types of syndication structures.

Limited liability companies

Overview

A limited liability company (LLC) is a form of company that is a body corporate with perpetual succession (continues to exist even after the death, bankruptcy, etc. of its members/shareholders). It is a separate legal person with the ability to own property in its own name and to sue and be sued in its own name. In an LLC, the liability of the members/shareholders is limited to the shares they hold in the capital of the company and, unless there are exceptional circumstances, the members/shareholders are not liable for the LLC's liabilities. An LLC in Kenya can have a single member but has a maximum limit of fifty (50) members/shareholders when it is private. There is no minimum capital requirement for a private LLC. In addition, the day-to-day management of an LLC is separate from its ownership; and a director or a board of directors, acting in accordance with their statutory and fiduciary duties, undertake the LLC's management. However, there is no restriction for a member to be a director of an LLC, and angel investors using an LLC as a syndication structure may also join its board of directors. Lastly, an LLC allows for flexible capitalisation as LLCs can be funded through equity, debt, or a mixed capital structure of equity and debt.

The compliance requirements, costs and timeline for setting up, and the advantages and disadvantages of using the LLC as a syndication structure, are outlined below.

Tax considerations

The LLC is required to obtain a personal identification number (PIN) from the Kenya Revenue Authority (KRA). Please note that for the LLC to get a PIN certificate, at least one director of the LLC must have a PIN certificate.

The taxable profits of an LLC are subject to income tax at the rate of 30%. The LLC is allowed to deduct allowable expenses incurred in the production of its income; however, generally, capital expenses are not deductible for tax purposes. Any dividend distributed by the LLC will be subject to withholding tax at the rate of 5% for resident shareholders and 15% for non-resident shareholders. Consequently, the effective tax rate for an LLC's local shareholders is 37% and 40.5% for non-resident shareholders. The withholding tax rates on dividends may be lower for foreign shareholders/investors if they are residents in jurisdictions with double tax treaties with Kenya. However, where the angel investor forming the LLC syndicate is a local Kenyan company and controls at least 12.5% of the LLC, dividend payments made to such a Kenyan company will not be subject to withholding tax. In addition, any transfer of shares in the LLC will attract a capital gains tax (CGT) at the rate of 5% of the chargeable gain.

Limited liability partnership

Overview

A limited liability partnership (LLP) is a type of entity that is a body corporate with perpetual succession (continues to exist even after the death, bankruptcy, etc. of its partners). It is a separate legal person with the ability to own property in its own name and to sue and be sued in its own name. In an LLP, the liability of the partners is limited to their contributions under the partnership agreement/deed, and the partners are not liable for the LLP's liabilities except under exceptional circumstances. An LLP is formed by a minimum of two partners, and a partner can either be a body corporate or a natural person. There is no separation of ownership and management in an LLP, and the limited liability partners participate in the LLP's management. However, an LLP is required to appoint a manager (who can also be a partner in the LLP) whose responsibility is to ensure the LLP complies with the LLP's various legal requirements. There are no minimum capital requirements for an LLP. An LLP does not have a share capital and can be funded through further contributions under the partnership agreement/deed or through debt.

Tax consideration

The LLP is required to obtain a personal identification number (PIN) from the Kenya Revenue Authority (KRA). An LLP is treated as a tax transparent entity; that is, an LLP's taxable profits are taxed in the hands of the individual partners rather than the LLP itself. The LLP itself is thus not subject to income tax in Kenya and the tax obligations flow through the LLP to the limited partners, who will be responsible for filing their returns and paying income tax on their share of profits.

Consequently, where a foreign angel investor is part of a syndication structure set up as an LLP, the LLP would create a taxable presence for that foreign angel investor as they would have to register and pay income tax in Kenya on their share of profits received from the LLP. Therefore, if a partner is a body corporate, they will be taxed at the corporate rate of 30%. If a partner is an individual, they will be taxed at a graduated scale, with the marginal tax rate being 30%.

From a tax perspective, it may thus be disadvantageous for a group of angel investors that comprise foreign persons to use an LLP as the syndication vehicle. It may be better to use a different syndication structure to avoid having to create a tax presence for foreign investors.

Capital gains due to the LLP members will attract a capital gains tax (CGT) at the rate of 5%.

Individual investing

Individual investing may be done in Kenya either through direct investing by an individual or by registering a sole proprietorship. A sole proprietorship in Kenya is established through registering a business name and using the business name to conduct business. When the angel(s) invest directly in their individual capacity or as a registered sole proprietorship, there is no separate legal personality between the angel investor(s) and the sole proprietorship. Consequently, the individual investor(s) are personally liable for any liabilities incurred during the investment or business, and their personal assets may be used to settle the liabilities. Individual investing thus exposes the angel investor(s) to limitless financial risks arising from their investment activities.

Tax consideration

Individuals are subject to income tax in Kenya at a graduated scale, with the highest tax rate being 30% of their taxable income. Since the individual angel investor is the taxable person, foreign angel investor(s) investing directly in their individual capacity or through a sole proprietorship will have a tax presence in Kenya and will thus be required to obtain a PIN certificate from the KRA, file annual tax returns, and remit their income taxes in Kenya.

Offshore syndication structures

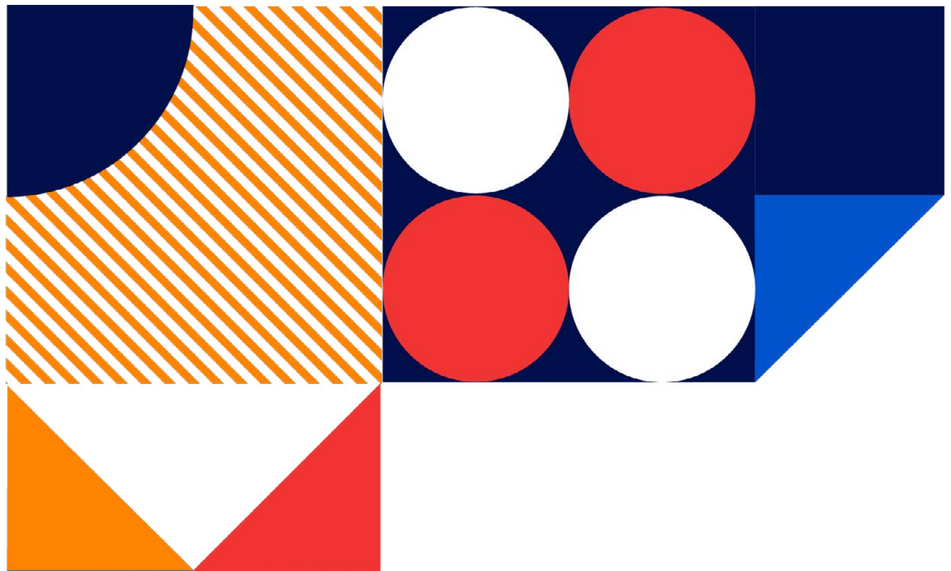
It is not uncommon for angel and early-stage investors to use offshore syndication structures to invest in startups/investees incorporated in Kenya. There is no specific legal framework that would apply to such offshore syndicates. The key consideration for angel and early-stage investors using offshore syndication structures is the tax implications of their flow of returns on their investment from the startups/investees. If the syndicate invests in a startup incorporated as a limited liability company, any dividends distributed by the startup will attract withholding tax at the rate of 15% and the effective rate (considering the corporate tax) will be 40.5%. If the syndicate comprises non-resident investors and the syndicate invests in a startup incorporated as a partnership or limited liability partnership, the syndicate may create a tax presence in Kenya and the syndicate will have certain tax obligations in Kenya. Other requirements and obligations would generally depend on the laws applicable in the jurisdiction of registration/incorporation or residency (in the case of individuals) of the investors or syndicate.

When the offshore syndication structure is used to invest in companies incorporated in offshore jurisdictions, there will be no taxes to the syndicate or indeed the Kenyan angels' part of the structure as the income (whether dividend or capital gains) are not derived from Kenya. Pursuant to the Kenyan Income Tax Act, income is only taxable in Kenya if it is accrued or derived from Kenya. Therefore, a Kenyan angel investor who is a member of a syndicate and who earns income from an offshore startup will not be subject to tax in Kenya. This will apply regardless of whether they have invested in the syndicate as individuals or through corporate entities. Further, no Kenyan taxes will apply on any capital gains arising from the offshore jurisdiction.

As such any taxes to be levied will depend on the jurisdiction where the startup is incorporated in and those of the syndicate structure set up.

A comparison

Corporate form	Compliance requirements	Costs and timeline	Advantages	Disadvantages
LLC	**Statutory books:** An LLC is required to maintain a register of members, directors, directors' residential address, charges, debentures, and beneficial owners. Accounting records to be kept for a period of seven years, the resolutions of the board of directors for a period of seven years, and the minutes/resolutions of members of the LLC for a period of 10 years. **Audited accounts:** An LLC is required to prepare and file audited financial accounts at the end of each financial year unless it is exempted under the small companies' regime. For an LLC to qualify for the small companies' regime, it must have fewer than 25 employees, net assets of less than KES 20,000,000, and an annual turnover of KES 50,000,000. **Annual returns:** An LLC is required to file annual returns every year with the Companies Registry. **Registered office:** An LLC is required to maintain a registered office address. **Company secretary:** An LLC with paid-up share capital of at least KES 5,000,000 is required to appoint a company secretary. **Change in particulars:** An LLC is required to file changes of its particulars within specified timelines with the Companies Registry. These include a change of name, change of members, change of directors, change of beneficial owners, change of registered office, and an amendment of its articles of association.	An LLC is easy to incorporate, and it may take less than a week to complete the incorporation process. The official costs of setting up an LLC is approximately USD 100 or KES 11,000, and the set-up is done through a self-registration process. However, these costs may be subject to any professional fees where the angel investors use the services of a lawyer or company secretary.	• The members/shareholders of an LLC have limited liability, and are thus able to limit their financial risks. • The LLC is a separate legal person from its members/shareholders. • An LLC allows for flexible capitalisation and can be funded through equity, debt, or a combined structure of equity and debt. • There are no local shareholding requirements for an LLC to be used as an investment vehicle. • An LLC is easy to incorporate, and it is inherently easy to conduct business using an LLC because of its characteristics.	• The compliance obligations of an LLC can be burdensome. • The process of liquidating or deregistering an LLC can be burdensome since an LLC has to go through an insolvency procedure before being dissolved/deregistered, which can be quite a lengthy and costly process. • It may be costly to repatriate the profits of an LLC to a foreign shareholder/angel investor as the effective tax rate would be 40.5%.



Corporate form	Compliance requirements	Costs and timeline	Advantages	Disadvantages
LLP	**Declaration of solvency/insolvency:** An LLP is required to lodge a declaration by its manager that, in their opinion, the LLP appears as at that date to be solvent or does not appear to be solvent as at that date. **LLP manager:** An LLP is required to appoint a manager(s) who is responsible for the LLP's compliance obligations. **Accounting records:** An LLP is required to retain its accounting records for not less than seven years after completion of the matters to which they relate. **Registered office:** An LLP is required to establish and maintain a registered office within Kenya to which all communication and notices to the LLP are to be addressed. **Change in particulars:** An LLP is required to file changes of its particulars within specified timelines with the Companies Registry, such as a change of name, change of partners, change of manager, and change of registered office.	An LLP is easy to incorporate, and it may take about two weeks to complete the registration process. The official costs of setting up an LLP is approximately USD 260 or KES 26,000, and the set-up is done through a self-registration process, subject to any professional fees where the services of a lawyer or company secretary are utilised.	• The compliance obligations of an LLP are minimal. • It is generally easy to set up and register an LLP. • An LLP can be advantageous because of its tax transparency. The tax obligations are on the LLP's individual partners, and thus each partner is responsible for their own tax obligation. • There are no local partner requirements. • The LLP can be funded either though contributions that represent an investor's interest in the LLP or via debt or a combination of both.	• Since an LLP is tax-transparent, it may create a tax presence in Kenya for foreign limited partners. • Because an LLP does not have share capital, it may offer less flexibility with respect to capitalising or funding the LLP.
Individual	There are no compliance requirements for an individual conducting investing activities in their individual capacity or via a sole proprietorship.	A sole proprietorship is seamless to set up and takes only a couple of days. The official costs of setting up a sole proprietorship is approximately USD 10 or KES 1,000 and is done through a self-registration process, subject to any professional fees where the services of a lawyer or company secretary are utilised.	• No ongoing compliance requirements. • Seamless and easy to start investing since no registration or incorporation process is required, and for sole proprietorship, the business name registration process is seamless. • Has efficient decision-making since the decisions are all made by the investors without the bureaucracy associated with a corporate structure.	• Need for direct registration with tax authorities: Individuals would need to register directly with the tax authorities • Limited Liability: Sole proprietors have unlimited personal liability for the debts and obligations of their business, meaning that their personal assets can be at risk in case of a lawsuit or financial trouble. • Unattractive for startups - Startups often prefer dealing with syndicates rather than with individual angels in their cap table. This may mean losing out on some deals for the angel.

Part 2

Angel Transaction Legal Structures

Overview of Legal Framework

There is no specific legal framework relating to angel investing and early-stage investing in Kenya. Angel investments and early-stage investments made within Kenya are thus subject to the laws ordinarily applicable to general investments. However, specific legal regimes may place certain requirements on the angel and early investors when the startup/investee operates in a regulated sector, e.g., the insurance, telecommunications, and banking sectors.

Generally, investments made by angel and early-stage investors are subject to general laws of contract, and the parties have autonomy in agreeing upon the specific contractual terms, subject to any mandatory legal requirements such as statutory voting thresholds to pass certain decisions.

Deal Structuring Mechanisms

The most popular deal structures used by angel and early-stage investors relating to investments in Kenyan startups/investees are straight up equity, convertible debt, and simple agreements for future equity (SAFEs). We set out further details of these structures below:

Equity/Shares

Overview

It is common for angel and early-stage investors to invest in startups/investees through equity and taking on the economic risk. An equity structure involves the angel investor(s) – acting in whatever form – subscribing for such number of shares in the startup/investee and receiving returns on their investments through profits. The investor takes on the economic risk of the business since they can only recoup their investment and receive returns if the startup/investee makes a profit. When an angel or early-stage investor takes up equity in a startup/investee, they would ordinarily be entitled to voting rights as shareholders and have certain minority protections under Kenya's corporate laws. Additionally, in the event of the startup/investee's winding up or liquidation, the investors as shareholders may be entitled to surplus assets in proportion to their shareholding after debtors have been paid. Since equity investments dilute the founders' shareholding, it is common for founders to prefer alternative deal structures to prevent being diluted early on.

Generally, founders and angel and early-stage investors have wide autonomy as to the commercial and legal terms of the investment, and any rights and obligations are usually the subject of negotiations.

Tax Considerations

The subscription of shares in a startup/investee in Kenya is not a taxable event for angel and early-stage investors. However, the startup/investee's taxable profits are subject to income tax at the rate of 30%. Any dividends distributed by the startup/investee will be subject to a withholding tax at the rate of 5% for resident shareholders and 15% for non-resident shareholders. Consequently, the effective tax rate for local shareholders/investors is 37% and 40.5%for non-resident shareholders/investors. The withholding tax rates on dividends may be lower for foreign shareholders/investors if they are residents in jurisdictions that have double tax treaties with Kenya.

Convertible Debt

Overview

Convertible debt is a form of deal structure where an angel and early-stage investor(s) lend funds to a startup/investee at interest, and the principal and interest amount is convertible into equity at the end of a particular period or upon a trigger event such as a change of control or a financing/priced round. The terms of a convertible debt structure are generally subject to negotiation between the parties, and the parties have wide autonomy.

Tax Considerations

The issue of convertible debt by a startup/investee to an angel or early-stage investor is not taxable. However, (a) interest payments made by the startup/investee to the investors is subject to withholding tax at the rate of 15% of the interest amount, and (b) the conversion of the interest amount into equity attracts withholding tax on the interest amount converted. Lower withholding tax rates may apply where the interest is paid or converted in favour of an angel or early-stage investor who is resident in a jurisdiction that has a double tax treaty with Kenya. It is thus advantageous from a tax perspective for angel and early-stage investors to make their investments using convertible debt structures as opposed to equity.

Simple Agreements for Future Equity (SAFEs)

SAFEs have become a common feature for angel and early-stage investors making investments in Kenyan-based startups/investees. However, since the common SAFEs are usually governed by the laws of the United States of America, they would generally be used where the investment is made by a Delaware or US-based holding company that subsequently owns a Kenyan-based operating entity. In this case, these SAFEs would not be subject to Kenyan laws, and we are yet to have a Kenyan-based SAFE or equivalent document. Therefore, any conflict or dispute relating to the SAFEs would generally be subject to the jurisdiction of the courts of Delaware or the respective state depending on the SAFE's terms.

In addition, legal/commercial questions and the tax implications of using SAFEs are yet to be tested in Kenyan courts or with the tax authority in Kenya.

A SAFE is an agreement between an investor and a company that provides rights to the investor to own equity in the company in the future.

The SAFE was created by the Silicon Valley startup accelerator Y-Combinator in 2013 for the purpose of having a standard set of terms and conditions that investors and startups can agree upon without prolonged negotiations. This allows investors to engage a company at an early stage of development, and for the company to receive funding from investors quickly.

Although the SAFE is similar to a convertible note, it is not debt but rather equity that will be issued at a future date – upon the occurrence of certain future events.

The future event could be one or a combination of:

- a future equity financing round;
- the sale of the company; or
- an IPO or a dissolution of the company.

In the SAFE, the investor and the company decide on key terms like investment amount and valuation cap. Upon mutually signing the SAFE, the investor can fund the company with the investment amount.

A SAFE usually has an unconverted status until the occurrence of one of the specific events described within. In the meantime, an unconverted SAFE will be referenced on the company's capitalisation table like any other convertible security.

Upon conversion to equity, the SAFE terminates as its aim is to turn SAFE holders into shareholders. The standard SAFE does not bear an interest rate as it is not a loan. It does not have a maturity date like a convertible note, which means the investors must wait for the occurrence of any of the future events before they can have access to any equity.

There are three versions of SAFEs, and any of them can be used by angel investors or syndicates.

- **SAFE – Valuation Cap, no Discount:** During a future financing round, SAFE holders will convert at a valuation no higher than the valuation cap, but there will be no discount applied on the price of shares as shares will be bought at the same price future investors are buying at.
- **SAFE – Discount, no Valuation Cap:** During a future financing, SAFE holders will convert at whatever valuation is agreed upon by future investors, but a discount will be applied to the share price, which means the SAFE holders will buy shares at a lower price than future investors.
- **SAFE – MFN, no Valuation Cap, no Discount:** No valuation cap or discount will be applied on the share price, but the SAFE will have a Most Favoured Nation clause. This clause means that, if the startup issues equity during a future financing round with more favourable terms than those agreed to with the SAFE holder, the SAFE holder can convert at these more favourable terms.

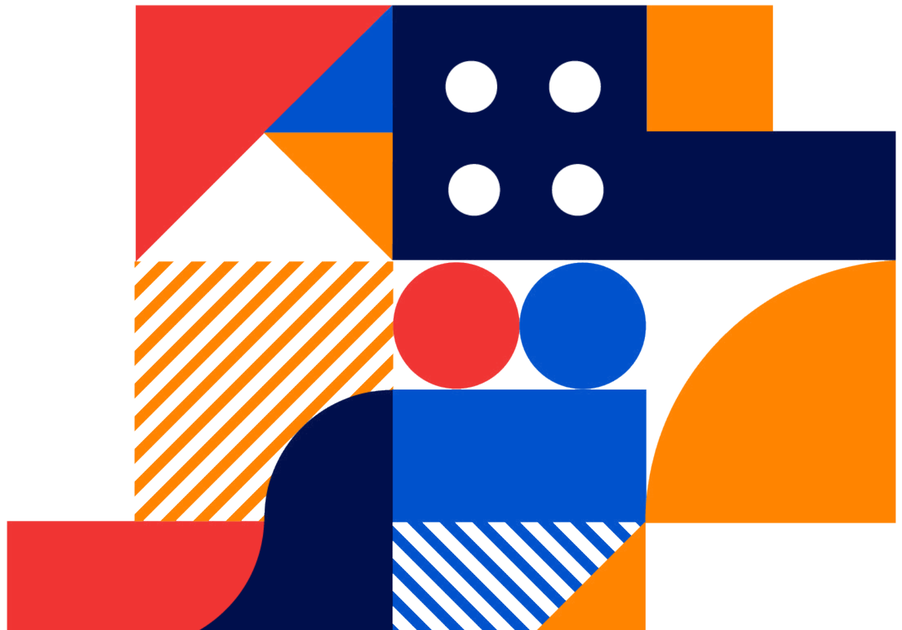
Before using any of the SAFEs provided by Y Combinator, a lawyer licensed in the country where the investee company was formed should be consulted so that the SAFEs are modified in accordance with the laws of that particular country.

Advantages of the SAFE

- It provides efficiency and expediency as only one document generally constitutes the substantive agreement.
- With fewer variables to understand and negotiate, investment terms can potentially be agreed upon faster.
- The SAFE does not require interest to be paid on the principal invested amount.
- In the event that the investee company is acquired or merges with another company, the SAFE holder is protected as the SAFE can be converted to shares or the investment can be returned to the SAFE holder.

Disadvantages of using a SAFE

- As a SAFE does not have a maturity date, there is a possibility that it never converts to equity if any of the future events do not occur.
- In the event of a company's insolvency, a SAFE holder may have no legal claim to the startup's assets because a SAFE holder is neither a creditor nor an equity holder.
- A SAFE may be transferred to affiliates of the investor only; i.e. it cannot be sold to third parties that are not owned by or do not share the same ownership as the investor.

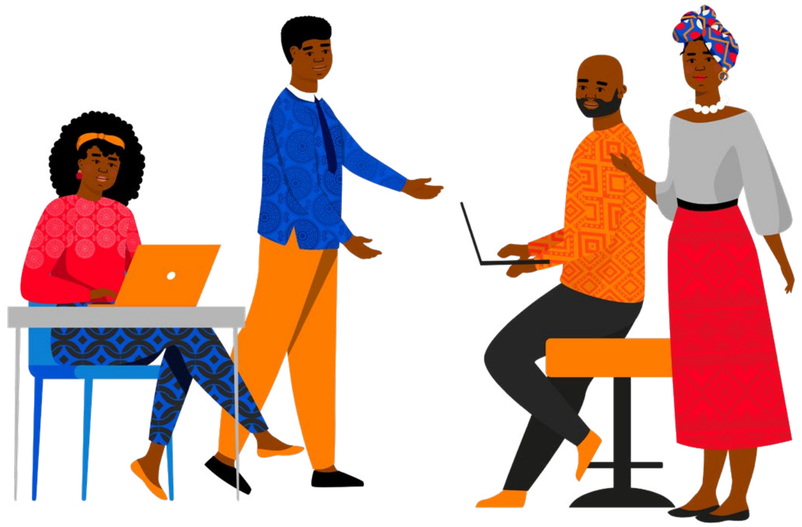


Deal Structuring Mechanisms in Summary

Deal Structure	Key Considerations	Advantages	Disadvantages
Equity/ Shares	**Priority of Payments:** Generally, in the event of the winding up of a startup/investee, lenders and preferred stockholders receive their investment back in priority to ordinary shareholders. Angel and early-stage investors are thus likely to be at the bottom of the pyramid hence likely to lose their investment **Economic Risk:** Taking up equity in an untested startup/investee creates a high economic risk as the startup/investee's failure is likely to wipe out the entire investment, and there is no guarantee of return as with debt structures. In addition, the investment can only be recouped if the startup/investee is profitable. However, there is an upside if the startup/investee is successful as compared to other alternative structures. **Valuation:** Considering that the startup/investee likely does not have sufficient track record to determine its valuation, and thus the valuation is mostly at the discretion of the founders, angel and early investors may not receive the full benefit of their investment. However, this may also play in their favour. **Control:** Equity investments generally come with voting rights and thus offer the investors an opportunity to participate in the management and control of the startup/investee. Angel and early-stage investors should therefore consider whether they want to participate in the decision-making of the startup/investee.	• An equity structure may result in huge economic benefits if the startup/investee becomes very successful. • An equity structure provides angel or early-stage investor(s) with the opportunity to participate in the management and control of the startup/investee, as well as providing them with visibility on the startup/ investee's performance. • An equity structure may provide an angel or early-stage investor(s) with an opportunity to make follow-on investments and avoid dilution through statutory pre-emption rights.	• **Time to Completion of Transaction:** In most jurisdictions, concluding equity transactions takes long due to the requirement to agree on valuation and to organize for the transfer of shares, which usually requires the registration of the shares in a government registry. • **Valuation Process Delays:** Compared to using convertibles or SAFEs, where the actual valuation may not need to be agreed on, equity transactions can have significant delays as negotiations must take place to establish the valuation and eventually close the transaction. • **Ranking of Angel Investors When They Receive Shares:** Unless the investors create different classes of shares (which might be complex), investors that end up with ordinary shares would rank at the same level as founders. This may not be favorable, especially if liquidation takes place or if they want to create investor rights.
Convertible Debt	**Conversion Event:** Angel and early-stage investors should consider the appropriate period or event that converts their debt into equity in the company. **Conversion Price:** Angel and early-stage investors should consider the appropriate formula or conversion price for their debt to obtain value for their money. **Interest:** Angel and early-stage investors should consider the appropriate interest rate for their debt investments to maximise the value of their investment without restraining the startup/investee's cash and working capital. **Protective Provisions:** Angel and early-stage investors should consider the appropriate protective provisions, such as consent requirements in favour of the investors on certain matters and information rights to provide the investors, with visibility on the performance of the startup/investee.	• **Economic Risk:** The economic risk of a convertible debt structure is lower than in the case of equity since the startup/investee has an obligation to pay back the debt; whereas in an equity structure, the startup/ investee does not have an obligation to return the investment. • **Priority in Payments:** Generally, debt holders are treated with priority to shareholders in the event of the winding up or liquidation of a startup/investee. • **Return on Investment:** Whereas shareholders only receive returns on investment once the startup/ investee becomes profitable, debt holders receive their interest and principal payments regardless of whether the startup/investee is profitable, provided it is revenue and cash generating. • **Tax Advantage:** Convertible debt structures offer a tax advantage as the effective tax rate on debt is lower than equity. This is because dividends are first subject to 30% income tax at the level of the startup/investee as profits and then withholding tax of 5% or 15% upon distribution; whereas interest payments are subject to a withholding tax of 15%.	• **Control:** Angel and early-stage investors that are debt holders have limited control over the startup/investee's operations and management, and thus investors have limited visibility on the startup/investee's activities. • **Economic Benefits:** In the event of a sale or liquidation of the startup/investee, and assuming such is not a conversion event, it is likely that debt holders may not maximise their returns compared to the shareholders. • **Lower Priority:** Whereas convertible debt holders have a higher priority than shareholders, they are generally lower in priority to other regular debt holders in the event of the startup/investee's liquidation.

Additional Resources

- ABAN African Investment Survey 2022
- Understanding SAFEs and Priced Equity Rounds: Fundraising + Investors, Legal, Safes | Y Combinator
- How to Invest in Startups with Angel Syndicates
- Syndication: Overview, Examples Reasons for Syndication
- Angel Networks in Emerging Markets
- How Venture Capitalists and Angel Investors Can Benefit from Investing in African Startups
- From Supa Strikas to Startups, Tomi Davies' Approach to Angel Investing



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