

SETTING UP A BUSINESS IN MADAGASCAR

Company, regulatory and tax aspects

News Brief

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PricewaterhouseCoopers Tax & Legal

✕ SETTING UP A BUSINESS IN MADAGASCAR

Company, regulatory and tax aspects

Choice of the legal entity

Tax implication of the legal entity choice

What You need to know about the appointment of a foreign officer in Madagascar

Visa / Work permit

Specificity of the duty-free enterprise regime (*entreprise franche*)



**SETTING UP A BUSINESS IN MADAGASCAR,
IT IS POSSIBLE WITH PwC**

Legal update about the implementation of a business in Madagascar

Investing in Madagascar remains governed by a relative freedom to the extent that the new company is not subject to any specific condition, nationality, prior authorization or approval.

Like the options offered by OHADA or French law, foreign investors may choose between any of these two legal structures:

- a more permanent vision: a commercial company, a structure with its own autonomy (which may be a subsidiary, whose main legal forms are: the public limited liability Company (*Société Anonyme* – “SA”) or the private limited liability company (*Société à Responsabilité Limitée* « S.A.R.L »);
- a short-term vision: a structure without legal autonomy (it may be a branch, also referred in practice as a desk, liaison office, representative office, sales branch).

Note:

- In Madagascar, the branch with independent management can be kept as such for indefinite term.
- Pursuant to OHADA law, the activity of a branch of a foreign company shall be limited to two years as from the date of its registration with the commercial register. Once expired, and only for companies based outside of one of the sixteen States members of OHADA area, the Uniform Act requires that the branch shall be contributed to an existing company, unless otherwise stated by a Ministerial Decree. In practice, this exemption is granted and assimilated to a renewal of this period of two years (this usually happens with civil engineer and oil & gas companies).

Madagascar is not part of OHADA area: 1.The activity of a branch is not limited in time in Madagascar; 2.If a Malagasy company opens a branch in the OHADA area, this two-year rule shall be applicable to it.

Shareholder and tax aspects



Choice of the legal structure

In Madagascar, two types of legal entities are commonly used to set up a business:

- **the subsidiary**, which shall have an independent legal structure, as commercial company, usually Public Limited Liability Company (“SA”) or Private Limited Liability Company (“SARL”) ;
- **the branch**, which has no separate legal personality and cannot act on its behalf. In practice, it is often referred as *liaison office, resident representative or representative office, sales branch, office...*
So many different terms to address a same tax and legal concept: the branch.

We shall summarize below the main reasons that bring the investors (foreign or national) to choose one or the other of these options.

The choice of the legal entity to set up a business depends on the aim the investors want to reach together with the following criteria: development prospects, management method, employees’ status and visa constraints.

The below summary of the options shall enable the reader to assess the benefits of opting for one or the other of these structures.

Option between a subsidiary or a branch

What is a subsidiary?

The subsidiary is a Malagasy company, legally independent from the parent company and majority-owned by it.

Indeed, Articles 192 and 195 of law on commercial companies No. 2003-036 state that a subsidiary qualifies when the parent company holds at least 50% of its share capital.

When the parent company holds in the daughter more than 10% and less than 50% of its share capital, the parent is deemed to hold a simple participation in the daughter. The concept of subsidiary is therefore not applicable.

Advantages:

- ✓ The legal liability of the parent company with regards its subsidiary is limited as the subsidiary has its own legal personality. Save for direct guarantees granted by the parent on behalf of his daughter, the parent shall only be responsible for the commitments of its subsidiary up to the amount of share capital it subscribed (whether an SA or an S.A.R.L).
- ✓ In addition, not only the subsidiary shall be more integrated into the national market but shall also claim for public subsidies more easily (especially for big projects – Public Private Partnership “P.P.P”). We note that depending on the area, the subsidiary form may be required (for instance in order to obtain a mining license).

Disadvantages

- ✓ Some types of businesses are regulated and limit the freedom of setting up a subsidiary.

In these cases, a minimum Malagasy shareholding is often required by law. It is notably the case for insurance, real estate or telecommunication¹ sectors.
- ✓ The subsidiary supposes a medium/long term commitment, with a higher political or commercial risk.

What is a branch?

The branch is registered with the Register for Trade and Companies and offers management autonomy. A company directly sets up a commercial, industrial or services activities, without using a separate legal entity.

➔ It is a direct setting up in Madagascar of a foreign company.

Unlike the subsidiary, the branch does not have its own legal and tax personality. For example, it may not conclude contracts in its own name. Malagasy law provides that "rights and obligations arising from its activities

¹ For illustration purpose as regard telecommunication, regulation in force limits the participation of foreigner to 66% of the capital of the Malagasy company holding a licence.

or its existence shall be part of the assets of the company or the natural person who owns it. The company is validly notified at the head office of its branch. "

Usually, its purpose is to ensure representation of the foreign company with potential clients and local public authorities, to provide information on behalf of the parent company, to ensure, prospecting, advertising and commercial activity of the parent company.

Advantages:

Setting up a branch implies minimal formalities and costs of creation:

- ✓ no minimum share capital required,
- ✓ limited incorporation documentation (articles of association of the company, application for the registration of the branch, documents proving the right to use the premises where the branch is located, document appointing the representative of the branch)
- ✓ the company keeps control on its commercial policies,
- ✓ no need to hold shareholders or board of directors meetings,
- ✓ limited costs compared to the subsidiary...

The branch may be very useful to define the commercial policy:

- ✓ providing information,
- ✓ in its implementation (after sale service, storage, transport, facilities).

Companies : SA or SARL?

Development prospects

The Private Limited Liability Company (« SARL ») is a legal form usually used when the shareholders envisage close relationship between shareholders or restricted activity. Conversely, Public Limited Liability Company ("SA") offers anonymity to its shareholders and is a favorable option for equity opening.

Indeed, a company has three main sources of financing² :

- ✓ Equity: The share capital resulting from the shareholdings. A company can decide to increase its capital to finance its projects. Such decision entails the risk of dilution of shares but can also present an opportunity for one shareholder to increase its stake.
- ✓ Bank loan : Any such decision is dependent on a banking market that may not be consistent with the financial cycle of company needs.
- ✓ Bonds : flexible funding option, usually at a lower rate and not subject to any warranty, unlike bank loans. In addition, the issuer may have access to several investors.

While the SARL is limited to the first two sources of funding, the SA can use bonds as funding.

SA is often used when the company is expected to develop and requires significant investments. The share capital of the SA should only be paid up to 25% at the time of incorporation (the outstanding amount shall be paid within 3 years after registration with the trade and companies register).

The below summary describes the main attributes of the SA and SARL. However, it does not reflect specificities (e.g. oil or mining companies).

All amounts are in Ariary.

² The company is not limited to the bank and bond loans, company can also request from its partners a loan called "current account contribution". Let us note that such a current account – from a not resident partner – is subordinated to a prior authorization of Minister for Finance.

	SUBSIDIARY – Distinct entity		BRANCH
	Public Limited Company	Limited Liability Company	Liaison office or resident representative
Number of shareholders	1 and +	1 and +	NONE
Minimum share capital	10,000,000 : if several shareholders	Freely laid down in the Articles of Association	As it has no independent legal existence and depends on the parent company
	2,000,000 : if one shareholder		"(A) branch of the company (B) with a share capital of ..."
Management method	<p>1. Only if ≥ 4 shareholders: ✕ Board of Directors directed by a PDG, assisted by a PDGA or PCA & a DG (assisted by a DGA).</p> <p>OTHERWISE COMPULSORY IF ≤ 3 SHAREHOLDERS ✕ Chairman and Managing Director who can be assisted by one or several Chairman(s) and Managing Director(s) assistant(s).</p>	Manager	Except express appointment by the parent company, the legal representative is the Chairman and Managing Director or the Manager of the parent company.
Method of appointment and dismissal of the management entity		<p>(Art 343) Appointment: Double majority : 1. Majority of shareholders ; 2. Majority of shares</p> <p>Dismissal of a manager of a L.L.C: Decision of shareholders representing more than half of the company shares.</p>	In any case, it is essential that at least a legal representative is a " Malagasy Resident ".
	The terms of appointment and dismissal of management and supervisory bodies are more flexible in SA than in SARL ³ .		
Mandatory appointment of an auditor	YES	Optional except : ✕ annual turnover > 200,000,000 Or ✕ permanent staff > to 50 Or Share Capital > to 20 million ariary	NO
Nationality of the legal entity	Malagasy. However, the entity may not carry on activities reserved by the law to Malagasy people if the management is controlled by foreigners holding: - more than half the voting rights, - more than half the voting rights by virtue of an agreement concluded with other shareholders of the company (memorandum of understanding, shareholders agreement...), - a portion of the voting rights over 40% when no other Malagasy entity holds more shares than him.		
<p>Tax obligations</p> <p>1 → Income tax</p> <p>2 → Income tax on foreign services</p> <p>3 → Value Added Tax</p> <p>4 → VAT on foreign services</p>	<p>1 → YES : 20 % Exception : 01.01.05 Tax Code</p> <p>2 → YES : 10 %</p> <p>3 → YES : 20 % Exception : 06.01.06 Tax Code</p> <p>4 → YES : 20 %</p>	<p>1 → YES : 20 % Exception : 01.01.05 Only for activities carried out in Madagascar.</p> <p>2 → YES: 10 % but no tax if the operations are carried out between the parent company and the branch.</p> <p>3 → YES : 20 % Exception : 06.01.06 Tax Code</p> <p>4 → YES: 20 % but no tax if the operations are carried out between the parent company and the branch.</p>	

³ Appointment of a Manager in a L.L.C (Art 343): double majority: 1. Majority of shareholders; 2. Majority of shares. Dismissal of a Manager in a L.L.C (Art 343): Decision of shareholders representing more than half of the company shares. Appointment and dismissal of a Managing director in a P.L.C: Majority of the votes.

Visa – or – Authorization to practice in Madagascar

Foreigners staying in Madagascar may belong to one of these categories⁴ (1. non-immigrant; 2. immigrant; 3. stateless person and refugee).

- ✓ Non-immigrant can stay in Madagascar for less than 3 months (for each entry).
- ✓ Immigrant can stay in Madagascar for a period exceeding three months. Only this category of foreigner may be authorized to exercise an economic activity in Madagascar.

Any Malagasy company **requires** the appointment of a **resident corporate representative** (manager in a SARL, or other social mandate in a SA). Article 12 of Law No. 2007-036 of 14 January 2008 on investment requires that, within a maximum period of three months, the company shall appoint at least one resident corporate officer. Failing to do so, the company may not be able to acquire land, loose advantages resulting from the free zone regime, and / or winding up.

Once a resident corporate representative is appointed, Malagasy law does not impose any specific requirements with respect to other foreign corporate officer.

Attention shall be paid if these other corporate officer want to reside or not in Madagascar

The foreign corporate officer does not reside in Madagascar – Non Immigrant

In this case, when a corporate officer of the Malagasy company is a non-resident in Madagascar, a simple non-immigrant visa may be sufficient.

This might include what law calls "businessmen" whose activities require frequent travel to Madagascar. For those person, a "permanent entry and exit" visa is sufficient, valid for a maximum of 3 years and whose duration of stay for each entry must not exceed 3 months.

In this circumstance, the corporate officer is prohibited by Malagasy law to engage in any gainful activity.

The question thus arises of the remuneration that this non-resident corporate officer is likely to receive except acting allowance as administrator. To our knowledge, there is no case law on this subject.

⁴ **Regulations on immigration, entry and stay, work and investment in Madagascar:** **1.** Amended law no. 62-006 of 06/06/1962 establishing the organization and control of immigration. **2.** Decree No. 94-652 of 11/10/1994 establishing the modalities for implementation of the Law n° 62-006 of 06.06.1962. **3.** Ministerial Decree n°8421/97 of 19/09/1997 implementing Decree n° 94-652 du 11/10/1994, amended by the decree n° 97-1154 of 19/09/1997. **4.** Law n°2007-036 of 14/01/2008 on investments.

Immigrant performing economic activities in Madagascar – local representative officer

The case at hand is the foreign investor or foreign employee, or the legal representative.

If on the date of the establishment of the company in Madagascar, the foreigner has not yet obtained his resident visa, a transitional stage often starts. In practice, a temporary resident manager/director is appointed, during which the suitable formalities to obtain permanent resident visa are executed.

It is possible to appoint a non-resident corporate officer alongside a resident corporate officer (by-laws to be carefully drafted and/or drafting of a shareholders' agreement might be advisable in order to mitigate the managers/directors' liability).

To be noted that an investor visa may be granted for general managers or directors of SARL or SA or legal representative of a branch.

In practice, the foreign corporate representative is usually employed through an employment contract.

Practical formalities for obtaining the visa

In any case, the "Economic Development Board of Madagascar - EDBM" simplifies the process of obtaining the appropriate authorizations depending on the applicant's status. Several hypothesis:

First option: the "investor" is the legal representative of the company.

The Investor is the one who contributes in whole or in part to investments⁵.

This Investor Visa, (which is also a residence permit), is valid for three years and renewable. It is issued by EDBM on behalf of the Ministry of Interior.

⁵ Law n°2007-036: Investment is defined as « *all financial resources* » such as capital contributions, facilities and loans allocated to the implementation of any economic project. Law provides that « **Investor visa** » is « *granted to all foreign investors, whether linked to a Malagasy company by an employment contract or exercising within such company a social mandate as Manager, Managing Director, Deputy Managing Director, Chairman of the Board of Directors or Chairman Managing Director* ».

The holder of an investor visa is allowed to reside and work legally throughout the Malagasy territory without obtaining a work permit visa. The investor visa implicitly replaces the latter.

Second option: the manager/director cannot apply for an investor visa and must be employed through employment contract, duly authorized in Madagascar.

Before coming to Madagascar, the foreign employee must obtain an entry and stay visa, valid 1 month,

convertible and extendible. Then, once on site, EDBM shall grant a long stay visa.

The Professional Identity Card for self-employed foreigner

The activity carried out by a self-employed foreigner performing commercial, industrial, craft business or subject to patent must obtain a professional identity card for foreigners, in addition of the residence permit.

⇒ **Conclusion: The foreign investors in Madagascar shall be assisted upstream by a legal adviser when defining its project, in order to ensure that visa issues are not a barrier to set up a business in Madagascar.**

Tax implications according to the corporate form and the methodology

According to the corporate form

Whether the company is a SARL or a SA, the tax regime is the same (in 2013):

- ✓ Income tax at a rate of 20%,
- ✓ Tax on interest at a rate of 20%,
- ✓ Salary tax (withholding tax) with a maximum rate of 20%,
- ✓ VAT at a rate 20% on taxable income (financial interest are not taxable),
- ✓ Capital contribution of 0.5% on share capital increase,
- ✓ Registration fees at a rate of 2% to 6% on sales contract or acquisition property agreement.

According to the methodology

As a first step, whether the company is set up in the form of subsidiary or branch, the Malagasy accounting plan of 2005 and the GAAP are applicable.

On a tax rate point of view, whether the company is set up as subsidiary or branch, it will be subject to the same rate as mentioned above.

Finally, to be noted that Malagasy companies (branch or subsidiary) performing taxable operations with foreign companies shall generally be subject to specific reporting requirements (and payments of tax) when foreigners provide services⁶ (Cf. **PwC publication January 2013**)

Companies based in Madagascar, importing services from a foreign company must:

- ✓ **withhold** related Income Tax realized by the foreign provider company and **pay** back the said

tax to the tax revenue (cumulative obligation to declare and pay),

- ✓ **recover** with its provider the related VAT and **pay it back** to the treasure (cumulative obligation to **declare** and pay),

Finally, according to tax authorities interpretation of articles 20.06.12 et 20.06.14 of tax code, the company may be required to **declare** : 1. on behalf of the foreign company without permanent establishment in Madagascar, amounts (commission, discount...) paid to third-parties (understood as all companies based in Madagascar); 2. Disbursement advanced by foreign companies on behalf of the company based in Madagascar.

To be noted that only foreign company without a permanent establishment in Madagascar might be liable for such obligation.

Finally, if the foreign company has a permanent establishment in Madagascar, this latter becomes the fixed place of business of the foreign company and becomes legally obliged of the said obligations to declare on behalf of the foreign company. The same risk exists if instead of having a permanent establishment, the foreign company has a subsidiary in Madagascar with the same corporate name.

⁶ Art 01.01.14, Art 20.06.12, Art 20.06.14 of tax code

Specific case of a duty-free enterprise (zone franche)

Scheme:

It is an incentive system to attract foreign investors fully oriented to export activities.

This system offers tax incentives to accredited companies since these companies are only subject to the income tax and tax on interest.

In addition, accredited service providers companies are exempt from Income Tax for 2 years 5 years for intensive production companies (“entreprises de production intensive de base” or “EPIB”) and for industrial processing companies committed to activities falling under agribusiness sector, and at least 15 years for operating promotion companies that operate land arrangements.

At the end of the exemption period, accredited companies in duty-free zones are subject to Income Tax at a rate of 10 %. Companies are entitled to further reductions in the context of a reinvestment policy.

Companies eligible:

Eligible companies are defined by the law n° 2007-037 of 14 January 2008 on Duty Free Zone Companies in Madagascar and by the Decree N° 2005-087. These are export companies. They are of three categories:

- ✓ Industrial processing companies;
- ✓ Service providers companies; and
- ✓ Intensive production companies.

Eligible companies belong to the following areas:

- ✓ production of cinematographic film and video ;
- ✓ software design and development, data processing;
- ✓ technical testing and analysis, product certification;
- ✓ telemarketing and telecommunication; and
- ✓ offshore bank operations.

You want to set up business in Madagascar, You already set up, You plan to develop your activities and You are looking for strategic audit as to the corporate form, tax burden and your prospects development, PwC supports You throughout any step of your project.

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