

Newsletter on North Africa



Contents

Focus

Investment in North Africa: avoiding pitfalls.
pages 2-3

Interview

"Morocco is reaping the success of its reforms"
Christian Estève, Head of the Euro-Med region at Renault
pages 4-5

Challenges

Pan-Euro-Med region: the dismantling of the tariff system.
pages 6-7

Business

Slow and complicated regional integration.
page 8



Joint press conference following the Paris Summit for the Mediterranean.
From left to right:
José Manuel Barroso,
Hosni Mubarak,
Nicolas Sarkozy
and Ban Ki-moon.

Editorial

Special issue on the Mediterranean Union

In this new issue of the *Newsletter on North Africa*, we could not avoid covering the launch of the Mediterranean Union on 13 July 2008 in Paris. The newly formed Mediterranean Union has received much criticism but has also prompted enthusiasm by company leaders, more so in the southern Mediterranean¹. French entrepreneurs highlight tax harmonisation among their expectations.

Therefore, rather than providing you with specific articles on the countries in North Africa as usual, we have opted for a more transversal approach with the aim of assessing North African multilateral relations relating to the economic, political and social challenges of this global

region. In addition to articles by our experts on transfer pricing and customs, we also asked one of our clients, the car manufacturer Renault, and more precisely the Head of the Euro-Med region, Mr Christian Estève, to provide us with his point of view. We will cover the practical aspects of trade between North African countries in more detail in a future issue. CMS Bureau Francis Lefebvre's teams wish you all the best for autumn 2008. ■

¹ According to a survey by KPMG during the SME Planet trade fair on 3 June in Marseille.

شريعة
CHARI'Â

The term *chari'â* refers to the idea of rectitude. This term establishes elementary notions in the science of Islamic law: *Char'* (divine law), *Tachri'* (legal practice), *Chari'* or *Mucharri'* (legislator). The foundations of *Chari'â* are based on four Islamic legal principles: prohibition of usury (*Tiba*), sharing of profit and loss, prohibition of speculation (*Gharar*) and the principle of the tangibility of the asset being financed.

Cross-border taxation

Investment in North Africa: avoiding pitfalls

By Stéphane Gelin, Partner at CMS Bureau Francis Lefebvre, transfer pricing expert.



Setting up a subsidiary in North Africa enables advantageous tax relief to be obtained but also an increase in the company's tax burden in France. Some measures to be taken...

Many French companies set up subsidiaries in North Africa, particularly in Morocco and Tunisia in order to benefit from reduced labour costs or support a client which has just set up business there. These investments are encouraged by a number of dispensatory tax systems which enable newly formed subsidiaries to significantly reduce their local tax burden or put a stop to their taxes for a certain period of time. However, this preferential tax system is likely to create tax pressure in France in relation to transfer pricing (Article 57 of the General Tax Code) and the immediate taxation of subsidiaries' profits in France (Article 209B of the General Tax Code). Subsidiaries of French companies in North Africa carry on extremely varied activities. To illustrate the tax consequences in

France, we will use two typical examples: setting up a telephone call centre and building a subcontracting plant. These two activities may be directly invoiced to the end client or more often within the group. Intra-group invoicing obviously prompts the classic question relating to transfer pricing but it also has an impact on the application of Article 209B.

Transfer pricing

It will be tempting for a French group to locate a large margin at the level of its local subsidiary in order to benefit as far as possible from the preferential tax system. However, Article 57 of the General Tax Code requires transactions between companies in the same group to observe the arm's length prin-



KEY POINTS

→ **Combining operational savings and a reduction of the effective tax rate** by benefiting from tax relief in North African countries, an increase in dividends not subject to a withholding at source and taxation of dividends limited to 5% thereof.

→ **Going beyond the approach of a subcontractor** receiving income based on costs, insofar as the net result of the local company only represents a low fraction of these costs, which are already largely reduced compared to the costs incurred in France for the same activity.

→ **Encouraging a “profit-split” approach** by including a share of the group’s operational savings in the North African company’s income; identifying and documenting the savings made as a result of setting up this company.

→ **Ensuring that it is possible to provide proof** of an effective local activity.

→ **Developing a legal structure for North African operations in order** to prevent the local company simply becoming an internal service provider: favouring sales of finished products and avoiding manufacturing activities; invoices services directly to end clients.

For additional information

Transfer Pricing,
Editions Francis Lefebvre,
by CMS Bureau Francis Lefebvre’s International Department.

ciples, i.e., the prices applied must be comparable to those applied between two independent companies. It is often difficult to identify comparable prices applied by independent companies on the local market: the services or products are generally specific and the vertical integration of international groups reduces the number of independent players in a given industry.

Moreover, if comparable transactions actually exist, observing the prices applied continues to be problematic. For this reason, companies (and tax authorities) generally apply the cost price plus method to set the price for the provision of services or products manufactured by subcontractors. This method does not generally enable a large result to be located at the level of the service provider or subcontractor as the margin often ranges between 5% and 10%. This approach amounts to transferring the total savings to the French client or principal. An alternative approach involves sharing the savings between the service provider and the client using the profit sharing method. It is consequently necessary to identify these savings and share them between the two parties by using an economic technique deriving from “gambling theory”, which enables a negotiation process to be modelled. In general, this approach enables a larger share of the profit to be located in the subsidiary than the cost price plus method.

Implementation of Article 209B of the General Tax Code
In accordance with the provisions of this article, the profit generated by a subsidiary in a country with a preferential tax system (effective tax rate lower than 50% of the French rate) is immediately liable to taxation paid by the French parent company. This article applies provided that the French com-

pany has a direct or indirect holding of at least 50% in the company set up abroad. However, subsidiaries set up in North Africa may avoid this rule if they carry on industrial or commercial operations in this region, which is generally the case: Article 209B targets “mailbox” companies with no actual local substance. Nevertheless, even if the local company carries on operations, Article 209B will apply if more than 20% of the foreign company’s profit derives from certain management transactions relating to financial assets or intangible assets on its own behalf or on behalf of the group. The same applies even if this percentage reaches the 50% threshold, where these transactions and the provision of internal services are added.

Therefore, in practice, if the local company provides services to other companies in the group, its results which qualify for local relief are liable for French tax paid by the French parent company. This applies even if the services are actually provided to a client outside of the group (for example, a hotline service) if it is invoiced to the group company, which sold the services or products making the hotline for the client necessary. On the other hand if the local company directly invoices the group’s external client, its operations will not be considered to be an internal service.

In relation to industrial matters, it is consequently recommended that manufacturing activities are avoided and carried out by other companies in the group since a service is provided; on the other hand, if the local plant purchases raw materials and sells finished products to a group company, this activity is not considered to be an internal provision of services and the corresponding profits may accordingly avoid application of Article 209B. ■

Renault in North Africa

“Morocco is reaping the success of its reforms”



Christian Estève is the Head of the Euro-Med region at Renault (Eastern Europe, Russia, CIS, Turkey and North Africa). At a time when Renault is increasing projects in the region, he discusses the advantages and disadvantages of creating a North African market.

The North African market is still much dispersed.

What impact does this have on the car manufacturing industry?

Christian Estève : There are significant differences between the three countries in the region. Tunisia is somewhat different. It has a system of quotas which is reviewed on an annual basis. The Moroccan and Algerian markets are also very different although they are both developing. Algeria has completely lifted restrictions on its customs tariffs and duties. Its market is open to all four points of the compass with vehicles coming from the Far East, China, Iran, etc. One hundred thousand vehicles have been sold in Algeria this year. With Dacia and Renault, we are ranked in the two leading places. We are witnessing a war of imported vehicles with no local industrial fabric. Morocco offers a more skilled market, customs tariffs and duties are being dismantled and a local car industry is being created.

How does Renault's strategy form part of this complicated context?

C. E.: We have an importer in Tunisia. This importer enables us to have a drawing right of 8,800 vehicles per year. In Algeria, our commercial subsidiary should achieve between 35,000 and 40,000 sales this year. We have developed all of the Renault range in Algeria, mainly by relying on a sales network, a spare parts store and a training centre for technicians. We carry on three activities in Morocco. Firstly, trading activities with Renault Morocco (network, spare parts and training). We also have a plant in Casablanca, which manufactures 55,000 and 60,000 cars each year and whose production will double to reach 100,000 vehicles at the beginning of next year. Finally, we have just launched the construction of a plant in the Tan-



Christian Estève,
Director of the Euro-Med
region at Renault.

giers free zone. It will specialize in low-cost vehicles for the international market and will produce 300,000 vehicles per year as from 1 January 2011. This will be one of the largest production centres in the region. Several suppliers will support this project and enable a large-scale industrial fabric to be developed in Morocco.

MILESTONES

Present in North Africa for almost one century
Established in North Africa since the start of the 1920s, Renault is currently present through its subsidiaries Renault Algeria, Renault Morocco and the importer Artes in Tunisia. The group has an extensive distribution network for the Renault, Dacia and Nissan makes and is the leader on the Moroccan and Algerian markets. It also has a plant in Casablanca and will have a second unit in Tangiers as from 2011 with a production capacity of 400,000 vehicles per year, i.e., the largest site in the Mediterranean basin.

THREE QUESTIONS TO



Frédéric Elbar,
Partner, Head of North
Africa at CMS Bureau
Francis Lefebvre

Will the idea of the Mediterranean Union facilitate the establishment of a single market?

C. E.: We are interested if the idea of this Union is to create a large free trade zone like in continental Europe. At present, North Africa is entangled in constraints. Importing a Logan produced in Morocco into Algeria is extremely complicated. It will be worthwhile imposing discipline. However, the economic aspect of the Mediterranean Union is not currently highlighted. Since the Agadir Agreement signed by Egypt, Jordan, Morocco and Tunisia in 2004, a legal framework exists for a free trade zone but it is very difficult to apply.

How do you envisage the development of North Africa?

C. E.: Companies are increasingly required to manufacture in low-cost countries, such as China. However, it is simply necessary to look at a map: we have a French-speaking base at our doorstep in the southern Mediterranean offering many advantages. It is consequently for these countries in North Africa to become more attractive since companies create wealth where they find the most facilities. At present, our relations are completely inverted: competition is increasingly found at country level. Morocco has implemented many reforms, which have already been adopted by Eastern countries. Morocco is starting to reap the success of these reforms and serves as an example to be followed. ■

Renault's subsidiary in Casablanca, Morocco.
The car manufacturing group started doing business in this country at the start of the 1920s.



..... How are you structured to assist your clients in North African countries?

Our clients require assistance with understanding the legal and cultural environment in which they are developing. We provide them with such assistance through our local teams (through the intermediary of our offices in Casablanca and Algiers, which have 17 consultants or via our correspondents in Tunisia and Libya). They also need high quality expertise in these regions, which have seen major developments in corporate law. Our leading experts work closely with our local teams.

..... Renault's example perfectly illustrates these current developments. What is the effect of these developments?

These countries previously had limited tax laws and significant unofficial doctrine for the initiated. The tax authorities have gradually opened up to users and taxpayers and official doctrine has developed. Tax law tends to form part of a more accessible legislative framework. Morocco accordingly launched tax reforms during the period 2000 – 2001. Algeria has formed a department for large companies two or three years ago and Libya has taken measures to manage the influx of new investors.

..... In this ever-changing context, how do you provide follow-up for your clients?

Activities carried on by companies have legal, tax and customs consequences both in the country of investment and in France where their registered office is based. This is also true in relation to human resources. It is consequently necessary that they ascertain the consequences of their local operations on their registered office's compliance rules. To this end, coordination between our Paris and local teams is a guarantee of security. In sum, we manage investments on both sides.

Investment incentives

Pan-Euro-Med region: the dismantling of the tariff system

By Nathalie Pétrignet, Partner at CMS Bureau Francis Lefebvre,
expert in sales policy, distribution and customs law.



The entry into force of cumulation of origin – which is based on the bilateral free trade agreements extended to the Pan-Euro-Mediterranean region – and the related Eur-Med certificate will have an impact on trading in the Mediterranean region. Explanations.

The European Union in conjunction with a number of countries from the Mediterranean region and European countries have formed a Pan-Euro-Mediterranean free trade zone intended mainly to increase economic integration between the various partners. Its principle was defined in the Barcelona Declaration, which was adopted during the Euro-Mediterranean conference of 27 and 28 November 1995. The partners agreed on a strategy aimed at creating a region of shared peace, stability and prosperity by means of the gradual introduction of a free trade zone between the European Union and its Mediterranean partners and between the partners themselves, such as Israel, the West Bank, the Gaza Strip, Cyprus, Malta, Jordan, Egypt, Lebanon, Syria, Turkey, the Faroe Islands and North African countries (Algeria, Morocco and Tunisia) by 2010¹.

As a result, the Euro-Mediterranean association agreements were entered into between the European Union and its Mediterranean partners providing for the benefits of mutual trade relations, which replaced the bilateral trade agreements entered into previously.

In order to avoid delaying the process, it was accepted that the system could enter into force on a gradual basis between a certain number of countries without waiting for all of the relevant



The introduction of the Eur-Med certificate aimed to provide proof of origin - acquired in accordance with this extended cumulation of origin will drastically change Mediterranean trade.

countries to sign free trade agreements between them. A "diagonal" cumulation of origin was then implemented in the free trade zone.

However, in order for this cumulation of origin system to work, it is necessary for all of the countries in the zone to enter into free trade agreements between them and adopt a joint rule in these agreements, which determines the preferential origin.

Pan-Euro-Mediterranean cumulation of origin is accordingly based on a certain number of preferential agreements, which contain identical rules relating to origin.

Finally, the gradual entry into force of this Pan-Euro-Mediterranean cumulation of origin implies the creation and use of a new proof of origin: the Eur-Med certificate or Eur-Med invoice declarations.

KEY FIGURES

43

countries comprising the Pan-Euro-Mediterranean system: the 27 Member States of the European Union, the Member States of the European Free Trade Association (EFTA), four European States (Iceland, Lichtenstein, Norway and Switzerland), Turkey and the signatories of the Barcelona Agreement: Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Syria, Tunisia, the West Bank, the Gaza Strip and lastly the Faroe Islands.

Rules relating to cumulation of origin contained in the preferential agreements

The joint fundamental principle of any preferential system is based on the principal according to which products deemed to originate in a country are obtained in this country, either entirely or after sufficient transformation of products imported into this country. This is the case for products obtained from raw materials imported from third countries must have been sufficiently transformed to qualify for the preferential tariffs. The following

criteria laid down in the agreements entered into by the European Union are implemented to determine whether products have been sufficiently transformed:

- **change of tariff position** between the finished product and non-origin products used in the manufacturing process;
- **added value**: the value of imported products used in the finished product may benefit from preferential origin provided that it does not exceed a certain percentage of the value of this product;
- **specific processing**: specific processing must be carried out to imported goods in order to benefit from preferential origin. This rule is frequently applied for products in the textile industry.

Concept of multilateral cumulation of origin

If, in any preferential system, third products are subject to an obligation relating to the rule of sufficient transformation in order to qualify for origin status, the rules relating to cumulation of origin introduce flexibility to this rule since they enable use in a country of materials imported from other partner countries by not applying the obligation of sufficient transformation to imported materials originating from this country.

Partial multilateral cumulation of origin or Pan-Euro-Mediterranean cumulation of origin aim to establish a unique area for cumulation of origin enabling the use of materials originating from the European Union and the following third countries: Algeria, Bulgaria, Egypt, the Faroe Islands, Iceland, Israel, Jordan, Lebanon, Morocco, Norway, Romania, Switzerland, Lichtenstein, Syria, Tunisia, Turkey, the West Bank and the Gaza Strip.

The countries participating in the Euro-Med zone have implemented diagonal cumulation of origin rules: products that have origin status in one of the 43 countries in accordance with the rules of origin laid down in the Euro-Med Agreement may be added to products of origin of one of the other 43 countries without losing this origin status in the Pan-Euro-Med zone. However, cumulation of origin may only be applied if the countries of production and end destination have entered into free trade agreements providing for identical rules relating to origin with all of the countries implicated in the purchase of the origin status of the goods, i.e., with all countries which provide the

ECONOMIC STATISTICS

→ **EUR 12 billion**

Total of textile exports from the European Union to countries in the Euro-Med zone.

→ **EUR 23 billion**

Total of clothing imports from the European Union to countries in the Euro-Med zone, which places the textile industry for this zone in second place worldwide after China.

materials used. Materials originating from a country which has not entered into an agreement with the countries of production or end destination must be treated as non-origin (in accordance with the principle of "variable geometry"). Therefore, if a country in the Pan-Euro-Med zone is not bound to the other countries in the zone by a free trade agreement, it may not in practice benefit from cumulation of origin.

It is therefore necessary to regularly check the applicable provisions and the list of agreements and table setting forth the applicable agreements between the various partner countries published in the Official Journal of the European Union and updated regularly.

Certificates of origin

Finally, a new Eur-Med certificate of circulation has been introduced aimed at providing proof of the origin acquired in accordance with the application of the new extended cumulating of origin. It is also possible in order to provide proof of origin of the products in the Euro-Med zone to issue a Eur-Med origin invoice declaration with different descriptions than those used for the invoice declaration existing under other preferential systems. ■

1 This date may be deferred based on the effective date of each agreement.

KEY POINTS

→ **The Pan Euro-Mediterranean system of cumulation of origin** involves gradually extending the system of Pan-European cumulation of origin to other countries.

→ **The same rules of cumulation of origin** will gradually determine the origin of the products traded between partners in the Pan-Euro-Mediterranean zone.

→ **Materials originating from partner countries** are not subject to the "sufficient transformation" rule.

→ **The Pan-Euro-Mediterranean cumulation of origin can only apply** if a free trade agreement exists between the relevant countries, i.e., the country of production, the country supplying the materials and the country of destination provided that the agreement contains the same rules relating to preferential origin.

→ **The entry into force of the Pan-Euro-Mediterranean** cumulation of origin implies the creation and use of a new proof of origin: the Eur-Med certificate or Eur-Med invoice declaration.

North African market

Slow and complicated regional integration

By Jean-Jacques Lecat, Partner,
Joint Head of the Africa team
at CMS Bureau Francis Lefebvre.

Economic integration of countries in North Africa is only in the initial stages. However, the ground has been paved with regional, bilateral and now multilateral cooperation with the Mediterranean Union.

The regional integration project for countries in North Africa within the same organisation mainly resulted in the signature of the Treaty creating the North African Union between Algeria, Libya, Morocco, Mauritania and Tunisia in 1989. Around 30 agreements have been signed within the framework of this treaty, including seven which have currently been ratified (but not yet applied). The same also applies to the agreement relating to investment incentives and mutual investment protection, the double tax treaty or the creation of a North African Bank for Investment and External Trade. The provisions aimed at introducing a free trade zone and an economic union between these countries have remained a dead letter.

The association agreements entered into between the European Union and each of the countries in North Africa (with the exception of Libya) in the scope of the Euro-Mediterranean partnership introduced in Barcelona, although bilateral, also aim to create convergence between these economies and regulations in these countries: they set, beyond the creation of a free trade zone, joint objectives such as liberalisation of payments, introduction of competition protection rules based on those applying in the European Union, effective protection of intellectual and industrial property rights and investment. They



also aim to encourage measures with regional consequences: development of regional institutions and harmonised programmes. Financial support to implement these agreements, provided by the Meda programme and the BEI, amounted to almost €12 billion from 2000 to 2007. However, harmonising the rules and systems of the three countries is hampered by the entry into force of agreements with far away dates and diverging conceptions of their implementation.

The Mediterranean Union is intended to form a multilateral framework, which now falls in the scope of the Euro-Mediterranean agreements: all members of the Union are asked to participate. The relevant projects are proposed by the Commission. They cover specific aspects (pollution control in the Mediterranean, creation of East-West sea/road transport, solar plan, etc.). The implementation of these aspects will be a high political priority with financing sources coming from a broader base than European funds. ■

CONTACTS • À Paris Frédéric Elbar, associé, tél. : +33 (0)1 47 38 43 51 – frederic.elbar@cms-bfl.com & Jean-Jacques Lecat, associé, tél. : +33 (0)1 47 38 56 82 – jean-jacques.lecat@cms-bfl.com • À Alger Samir Sayah, avocat, tél. : +213 21 37 07 07 – samir.sayah@cms-bfl.com • À Casablanca Wilfried Le Bihan, avocat, tél. : +212 22 48 14 82 – wilfried.lebihan@cms-bfl.com

CMS Bureau Francis Lefebvre

1-3, villa Émile-Bergerat – 92522 Neuilly-sur-Seine Cedex, France – T +33 1 47 38 55 00 - F +33 1 47 38 55 55 - info@cms-bfl.com

CMS Bureau Francis Lefebvre is a member of CMS, the organisation of 9 major independent European law firms providing businesses with legal and tax services across Europe and beyond. Operating in 48 business centres around the world, CMS has over 595 partners, more than 2,200 legal and tax advisers and a total complement of over 4,600 staff.

CMS member firms' offices and associated offices:

Amsterdam, Berlin, Brussels, London, Madrid, Paris, Rome, Vienna, Zurich, Aberdeen, Abu Dhabi, Algiers, Antwerp, Arnhem, Beijing, Beirut, Belgrade, Bratislava, Bristol, Bucharest, Budapest, Buenos Aires, Casablanca, Cologne, Dresden, Dubai, Dusseldorf, Edinburgh, Frankfurt, Hamburg, Kuwait City, Kyiv, Leipzig, Ljubljana, Lyon, Marbella, Milan, Montevideo, Moscow, Munich, New York, Prague, São Paulo, Sarajevo, Seville, Shanghai, Sofia, Strasbourg, Stuttgart, Utrecht, Warsaw and Zagreb. www.cms-bfl.com

The members of CMS are in association with The Levant Lawyers with offices in Beirut, Abu Dhabi, Dubai and Kuwait.

Newsletter on North Africa • Newsletter published by CMS Bureau Francis Lefebvre • Editorial director: Florence Jouffroy • Editor-in-chief: Frédéric Elbar • Legal texts written by CMS Bureau Francis Lefebvre • Editorial design: entream.com – T +33 1 42 04 43 29 – www.entream.com • Photos: AFP, Getty, Jupiter • ISSN: 1770-0019.