



VPro Lawyers Newsletter
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FINANCIAL ASSISTANCE

Is there a problem?

Having recently survived a last minute “financial assistance” panic by the lenders in an otherwise straightforward transaction for the acquisition of shares in a company, it occurred to me that this so called “problem” of financial assistance is probably a real mystery to most business people. The threat of financial assistance sometimes carries with it the potential to seriously delay, and even derail otherwise straight forward business dealings.

So what does it mean, to “financially assist” an acquisition of shares? Quite simply, it refers to a purchaser of a company’s shares using the target company’s own resources to facilitate the purchase of its shares.

The theory, from a legal point of view, is that this benefits the buyer of the shares, but does not benefit the company itself or its creditors, or other shareholders. It potentially harms their financial interests.

Many years ago, financial assistance was outlawed in the United Kingdom. A similar approach was followed in the “colonies”, including Australia.

Changing the Law

Otherwise innocent transactions were threatened with invalidity because of a technical breach of the financial assistance prohibition which frequently operated as an unwelcome trap. In the 1980s complex legislation was introduced to alleviate the problem but it was only as late as 1998 that simplified legislation made it clear that financial assistance, could after all, lawfully be given by a company provided that it does not “materially prejudice” the interests of the company and its shareholders, or the company’s ability to pay its creditors.

Material Prejudice

If there is no “material prejudice”, then that should be the end of the enquiry! This involves assessing the impact of the transaction on the company’s balance sheet, profits and cash flow. If this is not quantitatively material, then there is, and should be no problem. People in business, accustomed to making business judgments, should have little difficulty in reaching a conclusion one way or the other, in most situations.

Exceptions and Approach

Even if there is material prejudice, that is not the end of the matter. There are a number of specific exemptions (most typically to facilitate the issue of shares to employees). As well as that, the legislation permits financial assistance to be authorized by the shareholders themselves, provided that the prescribed procedure is carried out.

In other words, the question of financial assistance should not be a problem at all or, if it is, in most cases, it should be relatively easily dealt with. This should not be an excuse for delay, excessive cost or increased complexity.

Directors

One word of caution. Even if financial assistance is permitted, or approved by shareholders, that does not relieve the directors from their responsibility. But there is nothing special about that, because the directors always have a duty to act for a proper purpose, in good faith and in the best interests of the company.

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