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# CORPORATE & COMMERCIAL ALERT

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### So, you want a loan? Does this mean you need section 44 financial assistance?

Section 44 of the Companies Act 71 of 2008 (Companies Act) regulates financial assistance by a company in the form of a loan, a guarantee or the provision of security to any person for the purpose of, or in connection with, *inter alia*, the subscription or purchase of any securities, issued or to be issued by the company or a related or inter-related company.

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## So, you want a loan? Does this mean you need section 44 financial assistance?

It has long been debated whether or not a conventional loan falls within the definition of a 'debt security' or 'security' so as to trigger section 44 when a company provides a loan, a guarantee or security for the purpose of a person subscribing or purchasing securities.

Section 44 of the Companies Act 71 of 2008 (Companies Act) regulates financial assistance by a company in the form of a loan, a guarantee or the provision of security to any person for the purpose of, or in connection with, *inter alia*, the subscription or purchase of any securities, issued or to be issued by the company or a related or inter-related company.

When section 44 is triggered, the company providing the financial assistance to a person who is subscribing for or purchasing the securities, must have passed a special resolution of the shareholders approving the financial assistance and the board of the company must prove that it is satisfied that (i) immediately after providing the financial assistance, the company would satisfy the solvency and liquidity test; and (ii) the terms under which the financial assistance is proposed to be given are fair and reasonable to the company.

It has long been debated whether or not a conventional loan falls within the definition of a 'debt security' or 'security' so as to trigger section 44 when a company

provides a loan, a guarantee or security for the purpose of a person subscribing for or purchasing securities. More plainly, the question has been whether a loan qualifies as 'security' for the purposes of section 44.

In the matter of *Consol Glass (Pty) Ltd v The Commissioner for the South African Revenue Service*, the Supreme Court of Appeal considered a Value Added Tax (VAT) dispute, and in doing so also provided clarity on the question of whether or not a conventional loan is to be considered a 'debt security' as defined in the Value-Added Tax Act 89 of 1991 (VAT Act), which in turn, answers the question of whether a loan constitutes 'security' for the purposes of section 44 of the Companies Act.

In the *Consol* case, Consol acquired the businesses of Consol Limited and two of its subsidiaries, which acquisitions were financed by Consol through debt financing in the form of Eurobonds. The debt, as well as Consol's obligations to pay interest and redeem the bonds, were denominated in Euros whilst Consol's revenue was denominated in Rand. To cover the risk of Rand volatility against the Euro,

## 2020 CONSISTENT LEADERS IN M&A LEGAL DEALMAKERS

### 2020

1<sup>st</sup> by M&A Deal Flow.  
1<sup>st</sup> by BEE Deal Flow.  
1<sup>st</sup> by BEE Deal Value.  
2<sup>nd</sup> by General Corporate Finance Deal Flow.  
2<sup>nd</sup> by General Corporate Finance Deal Value.  
3<sup>rd</sup> by M&A Deal Value.  
Catalyst Private Equity Deal of the Year.

### 2019

**M&A Legal DealMakers of the Decade by Deal Flow: 2010-2019.**  
1<sup>st</sup> by BEE M&A Deal Flow.  
1<sup>st</sup> by General Corporate Finance Deal Flow.  
2<sup>nd</sup> by M&A Deal Value.  
2<sup>nd</sup> by M&A Deal Flow.

### 2018

1<sup>st</sup> by M&A Deal Flow.  
1<sup>st</sup> by M&A Deal Value.  
2<sup>nd</sup> by General Corporate Finance Deal Flow.  
1<sup>st</sup> by BEE M&A Deal Value.  
2<sup>nd</sup> by BEE M&A Deal Flow.  
Lead legal advisers on the Private Equity Deal of the Year.

### 2017

2<sup>nd</sup> by M&A Deal Value.  
1<sup>st</sup> by General Corporate Finance Deal Flow for the 6th time in 7 years.  
1<sup>st</sup> by General Corporate Finance Deal Value.  
2<sup>nd</sup> by M&A Deal Flow and Deal Value (Africa, excluding South Africa).  
2<sup>nd</sup> by BEE Deal Flow and Deal Value.



## So, you want a loan? Does this mean you need section 44 financial assistance?...*continued*

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The court's analysis on the definition of a debt security and whether a loan could qualify as one in the context of a tax dispute has certainly provided some clarity on the status of a loan in the context of securities and section 44 of the Companies Act.

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Consol entered into collateral hedging agreements to cover its Euro exposure, which became increasingly expensive. The increasing expense resulted in Consol seeking funding in the South African market, denominated in Rand, to replace its Eurobond debt and to unwind the hedging positions.

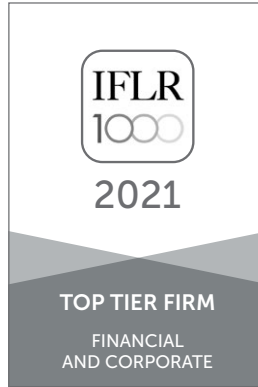
In substituting its foreign debt with local debt, Consol entered into various refinancing transactions which included a conventional loan agreement of some R5 billion from a consortium of South African banks. To secure the domestic loans, Consol procured various local and foreign services which required fees to be paid by Consol. Consol's liability for VAT arising from these fees incurred by it, gave rise to the appeal.

In deciding whether these services were acquired by Consol to make an exempt supply in the form of a financial service (which includes, as a variant, the issue of debt security), the court acknowledged that a conventional loan agreement does not readily fall within the concept of a 'debt security' as defined in the VAT Act. The court then went on to state that what is contemplated in the definition of a 'debt security' in the VAT Act is "... a document that may be issued, allotted, drawn, accepted, endorsed or the ownership of which may be transferred... of which a loan agreement is not one."

The court's analysis on the definition of a debt security and whether a loan could qualify as one in the context of a tax dispute has certainly provided some clarity on the status of a loan in the context of securities and section 44 of the Companies Act. The *Consol* case makes a clear case for stating that in the context of company law, section 44 would not be triggered when a company provides financial assistance for the purpose of, or in connection with a loan, as a conventional loan is not to be regarded as a security. However, in such a scenario, section 45 of the Companies Act, which regulates the provision of financial assistance to a director of the company or to a related or inter-related company (such as group companies) will apply and subsequently, the board of the company will still have to obtain shareholder approval and resolve that it is satisfied that immediately after providing the financial assistance, the company would satisfy the solvency and liquidity test; and the terms under which the financial assistance is proposed to be given are fair and reasonable to the company.

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*Jenni Darling and Kirstin Swanepoel*



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### BBBEE STATUS: LEVEL TWO CONTRIBUTOR

Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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