the sponsor's credit standing and payment obligations under the lease and the sponsor would obtain benefits such as avoiding the debt on its balance sheet and circumventing debt restrictions.

I have circulated a model of a project financing package involving a number of the foregoing aspects. While the overall project may be reasonably complicated, the individual techniques for spreading risk are relatively straightforward and can be used in relation to other transactions and, I suggest, could be used by most of you to assist your clients to raise funds or to obtain some of the benefits referred to previously. These techniques are valuable tools but the list is by no means exhaustive - there is still plenty of scope for an innovative approach to financing to meet the needs of the various parties involved. The practice in New Zealand has too often been for financing to be considered on the balance sheet of the borrower and with the lender automatically taking standard mortgage or debenture security. The time is coming when a bit more sophistication will be necessary as there are other benefits to borrowers in the arranging of a finance proposal than merely obtaining the funds required. Borrower should be aware of the additional price they are paying by granting excessive security - the cost is a restriction on future financing flexibility. Lenders can also benefit from the foregoing techniques as they provide means whereby their credit risk may be reduced.

Major projects have by their very size demanded a better appraisal of the objectives of the parties and risk allocation. The new techniques of project financing evolved as conventional financing did not meet the parties requirements. Project financing is a further example of what can be achieved by an innovative approach to solving legal and commercial problems.
FINANCING THROUGH THE USE OF TAXATION PLANNING

by David J. Ross, BCom, ACA, CMA

A brief summary of matters covered in a paper presented to the Legal Research Foundation - May 1982

1. We are living in turbulent times, partially due to the effect of inflation and the uncertain world situation.

2. Disclosed corporate profits require major adjustments to compensate for inflation, and major profit increases by leading companies are having very little effect on share market prices. Share market prices on average are less than three-quarters of the disclosed asset backing of the companies concerned.

3. Liquidity and cash flow are becoming more important than earnings as a positive cash flow means survival, whereas profitability without cash flow can mean disaster.

4. Taxation could be regarded as a 'business expense' or as a distribution from profits that have been earned - should taxation be regarded as a cost of operating a business?

5. An emotional area of taxation planning - tax avoidance and tax evasion.

6. Lease or purchase decisions - taxation advantages and non balance sheet disclosure.


8. Corporate restructuring - particular emphasis on the family group of companies or the private company.


deficiency guarantee may be reduced as the loan is amortised. The limitation on the liability under the guarantee may be beneficial to the guarantor both in relation to balance sheet footnotes and to its creditworthiness in respect of other transactions.

(b) Semi-guarantees

There are a number of ways in which the financier may obtain some support from the sponsor without a direct guarantee. These range from a mere comfort letter and cross-default clauses under other obligations through to deposits under which there will be a set-off to various forms of undertaking which will ensure that there is a cash flow to enable the financier to be paid.

7. Third party guarantees

There may be other persons who have a strong interest in the project proceeding and who are prepared to assume part of the risk. These would include either Governments or Governmental agencies who require the project to be completed as either part of national development or to provide employment opportunities or to ensure availability of the products or services deriving from the project. These guarantees may be either general unconditional guarantees or may relate to specific risks.

8. Lease of project

The sponsor could set up a company which was not a subsidiary to be the owner of the facility and to lease the facility to the sponsor. The lease would be of a "hell of high water" nature and would provide sufficient funds to service the debt and to meet expenses. The owner would raise the funds required on the strength of
The risk of construction is particularly significant as the project is exceptionally poor security if it is never completed or doesn't work upon completion.

A completion guarantee may be given either by the sponsor or by third parties. An obvious third party is the supplier or constructor of the plant. The project entity may purchase the plant under a "turnkey contract" pursuant to which the supplier has a total responsibility for ensuring that the plant is completed and operating satisfactorily before it becomes entitled to payment. As there may have been progress payments required to fund the construction, there may need to be a refund clause requiring repayment by the supplier or, where the supplier is not sufficiently substantial, bank performance guarantees or guarantees from other parties.

The contract could be a fixed price contract with liquidated damages or indemnity provisions to cover lost revenue because of delays.

6. **Sponsor support**

The sponsor may provide support which is less than a full guarantee by such means as:

(a) **Deficiency guarantees**

A deficiency guarantee is a guarantee limited to the shortfall suffered by the financier in the event of a default resulting in a realisation of security by the financier. It is common for the deficiency guarantee to be subject to a limit expressed either as a monetary amount or as a percentage of the amount financed. A limited