

COMMERCIAL LAW NEWSLETTER

The official company newsletter of Commercial Law Development Services

EQUITY AND DEBT FINANCING IN NIGERIA

Written by **Balarabe Akinwumi**
balaakinwumi@acuitas-legal.com

Navigating Capital Raising in Nigeria: Equity vs. Debt Financing

Introduction

Nigerian companies often face the critical decision of how best to raise capital. The primary options are equity financing and debt financing. Each approach offers distinct advantages and challenges, needing a thorough understanding of their implications. Navigating these options effectively is essential for companies looking to balance growth goals with regulatory compliance and long-term financial stability.



Equity Financing

Equity financing involves raising capital by selling shares of the company to investors. In exchange for their investment, these investors gain ownership stakes in the company, typically in the form of ordinary or preference shares or a combination of both. This method is particularly appealing for startups and businesses with high growth potential that may not have the cash flow to support regular debt repayments.

Legal Framework:

Under Nigerian law, equity financing is primarily governed by the Companies and Allied Matters Act (CAMA) 2020. CAMA sets out the legal requirements for share issuance, rights of shareholders, and the duties of directors in managing the company's affairs. For publicly listed companies, added regulations from the Investment and Securities Act, (ISA), CAP 124 LFN 2004, set up the Securities and

Exchange Commission (SEC). The Companies Regulations (CR), as amended, along with the SEC Rules and Regulations, 2013 (as amended, SEC Rules), offer essential guidelines for equity transactions in Nigeria. Foreign entities are allowed to make equity investments in Nigerian companies.

However, foreign direct investments (FDIs) (excluding portfolio investments) must follow the provisions of the Nigerian Investment Promotion Commission Act (NIPCA) Cap N117, Laws of the Federation of Nigeria (LFN) 2004, and the Foreign Exchange (Monitoring and Miscellaneous Provisions) Act (FEMMPA) Cap F34, LFN 2004.

The Procedure for Equity Investment in Nigeria

Introductory Meetings

A company that wants a fit-for-purpose equity investment starts with spotting prospective investors. The Companies always request that the identified investors sign a Confidentiality Agreement to protect itself before pitching its business and strategies to them to ensure that the details are not shown to third parties. This is followed by further



discussions on the key financial elements of the prospective investment.

The parties will then commence discussions on the financial issues which is limited to the commercial aspects of the business, until a more structured legal document is executed by parties.

Due Diligence

After signing a Confidentiality Agreement, the next step would be to conduct due diligence. The importance of conducting due diligence is pronounced to the extent that both parties actually conduct due diligence on themselves.

The conduct of due diligence could reveal that a company is not compliant with regulations and standards, it could also reveal the financial issues facing the company that could impact negatively on the business. The due diligence also help both parties negotiate and reach a compromise that is fair to the contract.

Signing an Agreement

The Equity Investment is not complete until both parties execute an Agreement that defines their rights and liabilities. For subscription of shares, the parties sign a Share Subscription Agreement but for Share purchase, the Parties sign a Share Purchase Agreement.



A Share Subscription Agreement stipulates the number of shares that will be issued to the Shareholder and the order and timing by which funds will be advanced. Subscription to fresh shares is what infuses the company with requisite funds, as proceeds from transfers goes to the selling shareholders. A Share Purchase Agreement is used to transfer ownership of shares, it also sets

out the terms and conditions relating to the said transfer in a company.

However, a subscription or transfer is not complete without an amendment of the Share Holders Agreement which defines the rights, obligations, and relationships of shareholders among themselves concerning the company and its management. For greater effectiveness, the company itself is often a party to the agreement.

This document serves as an added safeguard for both the investee company and the investors, as it outlines the key terms of the investment, the rights attached to the shares issued to the investor, governance provisions, protections available to investors, and specific exit-related rights.

Compliance with the Terms and Conditions

The agreements usually set out timelines for performing certain post execution acts like making payments, filings at the Corporate Affairs Commission to include the name of the new investors in the register of members, issuing new investors with Share Certificates and filing of Return of Allotment with the Corporate Affairs Commission.

Key Considerations:

a) **Dilution of Ownership:** One of the primary considerations in equity financing is the dilution of existing ownership. As more shares are issued, the percentage of ownership held by existing shareholders decreases, potentially impacting control over the company.

b) **Regulatory Compliance:** Companies must ensure compliance with the provisions of CAMA about share issuance, including obtaining necessary approvals and adhering to disclosure requirements. For public offerings, SEC regulations must be strictly followed to avoid penalties.

c) **Investor Rights:** Equity investors often seek specific rights and protections to safeguard their investments and influence the company's strategic direction.

Common rights include:

- **Board Representation:** Investors may request a seat on the company's board of directors, allowing them to take part directly in governance and oversight. This can provide them with a voice in major decisions and access to insider information, but it also means that the founders might need to share control of the company's strategic direction.
- **Veto Rights:** Investors may negotiate veto rights on key business decisions, such as mergers and acquisitions, issuance of new shares, or changes to the company's bylaws. These rights enable investors to block actions they believe could negatively affect their investment. However, granting veto rights can limit the founders' ability to make swift decisions, potentially leading to delays or conflicts in the company's growth strategy.
- **Information Rights:** Investors may seek regular updates on the company's financial performance, including access to financial statements and other relevant documents. This transparency helps investors watch their investment's performance and make informed decisions. However, it also means that the company must keep an important level of financial discipline and reporting standards.





- **Preemptive Rights:** These rights allow existing investors to keep their ownership percentage by giving them the opportunity to buy added shares before the company offers them to new investors. While this can help avoid dilution of their stake, it can also limit the founders' flexibility in raising added capital from new sources.
- **Exit Rights:** Investors may negotiate specific exit rights, such as drag-along or tag-along rights. The drag-along clause requires the minor shareholder to sell their shares. The tag-along clause requires the minor shareholder to be allowed to join in on a sale. Both clauses are designed to give the minor shareholder the rights to receive the same price, terms, and conditions as any other seller during an exit event like an acquisition or IPO. These rights ensure that investors can realize a return on their investment under favorable conditions, but they may also influence the timing and nature of the company's withdrawal plan.
- **Anti-Dilution Provisions:** To protect their ownership stake, investors might include anti-dilution clauses, which adjust the conversion ratio of their shares in case of a future financing round at a lower valuation (a down round). While this protects the investor's interests, it can significantly dilute the ownership of the founders and early investors.

While investor rights are crucial for safeguarding their interests, they can affect the control that founders, and early shareholders have over the company's operations and strategic direction. Therefore, it is essential for founders to carefully negotiate these terms to achieve a balance between securing the necessary funding and keeping sufficient control to guide the company's vision. The longterm implications of these rights should be a key consideration.

To manage this balance effectively, founders should adopt several negotiation strategies. Firstly, they should set up clear boundaries, defining specific areas where investor input is welcome while keeping full control in other areas. Secondly, the scope of veto rights should be limited to critical decisions, preventing

investors from having a say in a wide range of actions. Founders should build in flexibility by including clauses that allow for the renegotiation or modification of terms as the company evolves. Finally, it is important to be mindful of cumulative rights across multiple investors, as these could collectively erode the founders' control over time. By following these strategies, founders can secure the funding they need while preserving their ability to steer the company in line with their vision.



Debt Financing

Definition and Structure:

Debt financing involves borrowing money that must be repaid over time, usually with interest. This can take the form of bank loans, bonds, or other financial instruments. Unlike equity financing, debt does not require giving up ownership in the company, making it an attractive option for businesses looking to keep control.

Legal Framework:

The legal environment for debt financing in Nigeria is shaped by various statutes, including the Central Bank of Nigeria (CBN) regulations for banks and financial institutions, and the Investment and Securities Act 2007 for the issuance of bonds. The enforcement of debt obligations is typically governed by contractual agreements, which are enforceable under Nigerian contract law.

Key Considerations:

- **Repayment Obligations:** Debt financing imposes a fixed repayment obligation on the company, regardless of its financial performance. This can strain cash flow, particularly for companies in volatile industries.
- **Security and Guarantees:** Lenders often need collateral or guarantees to secure the loan, which can put company assets at risk. It is essential to carefully review the terms of any security agreements to ensure they are manageable.
- **Covenants and Restrictions:** Loan agreements often include covenants that restrict certain business activities, such as taking on added debt or making significant capital expenditures. These covenants can limit the company's operational flexibility and should be negotiated to align with business goals.

When considering debt financing, it is essential to carefully assess the associated obligations and risks to ensure the arrangement aligns with your business's needs. One of the primary concerns is the fixed repayment obligation, which can strain your company's cash flow, especially during periods of financial instability. To manage this risk, it is crucial to have a robust cash flow management plan and consider financing options with flexible repayment terms.

Another significant consideration is the security or collateral required by lenders. Offering company assets as collateral can be risky, as failure to meet repayment terms could lead to the loss of critical assets. It is advisable to negotiate terms that limit the exposure of essential operational assets and, where possible, spread collateral requirements across multiple assets to mitigate risk.

Furthermore, agreements often come with covenants that restrict certain business activities, such as taking on more debt or making significant capital expenditures. These restrictions can limit your operational flexibility.

Therefore, it is important to negotiate these covenants to ensure they align with your business goals and to actively watch compliance to avoid penalties.

Choosing Between Equity and Debt Financing

The decision between equity and debt financing is a strategic one, depending on several factors including the company's stage of growth, cash flow stability, and the industry in which it works. Companies must weigh the cost of capital, the impact on ownership and control, and the longterm financial implications of each option.

Conclusion

Equity and debt financing are vital tools for businesses looking to grow and expand in Nigeria. However, each comes with its legal and financial considerations that must be carefully navigated. By understanding the legal framework and key factors involved, Nigerian companies can make informed decisions that support their long-term growth goals.

For personalized advice on structuring your financing strategy in compliance with Nigerian law, please contact our firm. We offer comprehensive legal services tailored to meet your business needs.

CONTACT



Balarabe Akinwumi

balaakinwumi@acuitas-legal.com



COMMERCIAL LAW
DEVELOPMENT SERVICES

Call for Commercial Law Articles Now Open!

Share your expertise on legal matters today.

Submit your articles for publication to info@clds-ng.com
now!



+234 815 062 0054
+234 912 047 1457



CLDS-NG
WWW.CLDS-NG.COM

On behalf of the Editorial Board of the Journal of Commercial Law, I am pleased to invite you to contribute to our forthcoming edition.

As a respected platform for scholarly and practical engagement, the Journal of Commercial Law is dedicated to deepening the understanding and advancing the practice of commercial law in Nigeria and globally. We are currently accepting submissions that reflect original research, offer rigorous analysis, and present insightful commentary on contemporary legal developments.

We particularly welcome articles that address emerging trends, innovative practices, regulatory challenges, or evolving legal frameworks in commercial law. Whether your work highlights current issues, proposes forward-thinking solutions, or critiques existing structures, your voice can significantly enrich the ongoing discourse and help shape the future of the field.

Submission Guidelines:

- **Length:** Articles should be between 2,500- 10,000 words.
- **Topics:** Only Commercial Law topics
- **More Info:** <https://shorturl.at/2rKwB>

All submissions will undergo a rigorous peer-review process to ensure that they meet the high standards of our journal. Accepted papers will be published in our next issue, scheduled for **August 2025**.

Please send your submissions or any inquiries to info@clds-ng.com

We look forward to your valued contribution and to continuing the tradition of excellence that defines our publication.



COMMERCIAL LAW
DEVELOPMENT SERVICES

UPCOMING EVENTS.

JUL
10

Thursday, 11 am WAT/GMT+1

Virtual- N150,000

Risk Management and Compliance in the Maritime Industry: Navigating International Laws and Sanctions

JUL
24

Thursday, 11 am WAT/GMT+1

Virtual- N150,000

Litigation Management for CEOs: Minimising Legal Exposure and Costs

AUG
7

Thursday, 11 am WAT/GMT+1

Virtual- N150,000

Agreement Drafting Clauses in Contracts

AUG
21

Thursday, 11 am WAT/GMT+1

Virtual- N150,000

Introduction to Property Fraud and Money Laundering

SEPT
4

Thursday, 11 am WAT/GMT+1

Virtual- N150,000

Risks and Challenges of Artificial Intelligence in Legal Services

SEPT
18

Thursday, 11 am WAT/GMT+1

Virtual- N150,000

Conflict of Laws: International and Domestic Legal Issues

Email: info@clds-ng.com

Call: +234 912 047 1457

Kindly Note: VAT is applicable

Target Number of Participants: 20

Also, scholarship offer is applicable for the categories below:

- Early Bird (3 weeks before training date) – 10%
- Past participants – 10%
- Group (Minimum of 5 participants)- 15%

Contact us:

Email: info@clds-ng.com

Tel: 09120471457, 08037747968

Elevate Your Team with CLDS Training Programs!

Website

www.clds-ng



Phone

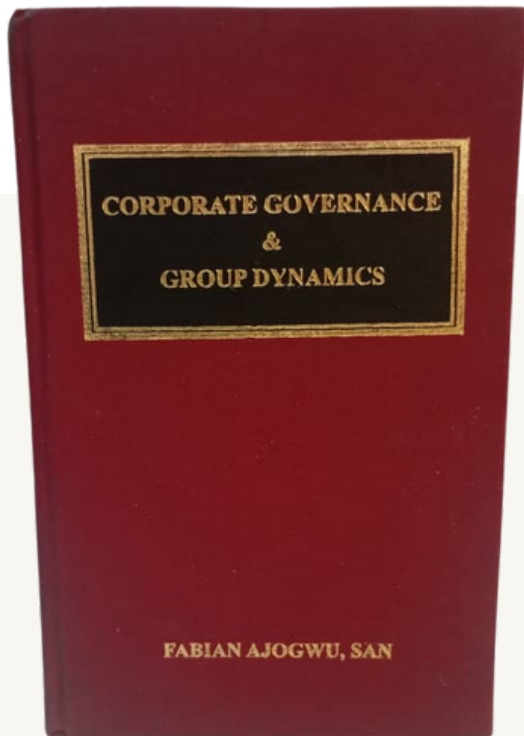
+234 815 062 0054



Email

info@clds-ng.com





HEY!

In this revised edition of 'Corporate Governance & Group Dynamics,' significant legal developments that have taken place since the book's initial publication in 2013, have necessitated an update to the laws and principles discussed within.

[BUY NOW](#)

TOP REC OF THE WEEK



This book argues that traditional corporate focus on power and profit is no longer sufficient, advocating instead for purpose-driven governance that prioritises ethics, sustainability, and stakeholder value. Through real-world case studies and the AFG Model, it offers a framework for businesses to achieve long-term success by balancing people, planet, purpose, and profit.

[**ORDER NOW**](#)

 +234 912 047 1457

 www.clds-ng.com



COMMERCIAL LAW
DEVELOPMENT SERVICES

**...development through research &
knowledge.**



www.clds-ng.com



[clds_ng](#)



[CLDSnigeria](#)



info@clds-ng.com