SQUIRE SANDERS

INTERESTS AND SHARES IN A COMPLETE DIFFERENT WAY – NEW POSSIBILITIES FOR BUSINESS OWNERS

Introduction

Are you considering inviting a financial investor to contribute to your business but are afraid of loss of control over company management? Do you want to motivate your employees through some form of integration with company profits? Do the rights of your co-shareholders, initially created when founding the company many years ago, no longer correspond with the business reality of today? Are you planning other changes to your company, business or among the partners? If so, forget everything that you have ever heard about shares in a limited liability company or a joint-stock company: there are totally new possibilities available! Here, we consider new options in light of joint-stock company shares only; however, all the information provided is also applicable to shares in a limited liability company.

Voting Rights

One of the most interesting developments within the new legal regulation is the departure from the rule where only one vote can be attached to a share. While in the US the option to issue shares with various numbers of votes is quite usual, European legal regulations are more reserved in this respect and, often, issuing shares with various voting rights is restricted (France) or completely excluded (Germany). The new Czech law stipulates that shares can be attached with various voting weights and thus the Articles of Association may provide that the shares owned by a shareholder liable for the daily management of the company will bear a higher number of votes compared to a shareholder whose participation in the company represents a financial investment.

Share in Profit

It is now possible to agree on distributing the share in profit among the owners of the individual classes of shares – for example, issuing shares with a fixed share in the company's profit which could be established as a fixed amount of profit or a percentage from the invested amount. This option may be a solution for investors who want to achieve a fixed minimal return on their investment. However, in this instance it is necessary to pay attention to the fact that even under the new regulation it will not be possible to attach to shares the right to a certain interest regardless of whether the company's economic results are reached.

Alternatively, it will also be possible to issue shares with a subordinated share in profit or liquidation balance. The dividend with respect to shares with a subordinated share in profit would be payable after the shareholders holding all other types of shares receive their dividends. This would enable the preferential return of capital to the financial investor with the distribution of profit as agreed among all the shareholders afterwards. For shares with a deferred creation of title to dividend, the new class of shares could contribute to decreased fluctuation of the key employees.

Division Shares

The new regulations also make it possible to issue so-called division shares, where the dividend will be derived from the performance of a given part of the company (division) or subsidiary, provided that the company itself has generated a profit. In the case of application of these division shares, the company will save work by dividing its business through a corporate transformation. This regulation is based on the shares known in the US as "tracking stock". In Europe, similar shares were used for restructuring ABN AMRO Bank (today RBS). Issuing these shares could be useful in the attempt to find financial investors for growth or a new business segment without having to separate it. Recently, we have just recommended this option to a significant Czech-based IT company that developed a certain patent outside its main business activity. This way, the company may issue division shares for the employees who participated in the patent invention as well as to new financial and strategic investors the company is trying to find for this new sphere.

No-par Value Shares

Furthermore, it will be possible to issue so-called "no-par value shares" that have no nominal value. The share in the registered capital will be determined pro rata to the total number of shares issued. No-par value shares are suitable for companies having in plan frequent entries of new investors, as it will be easier to change registered capital. The no-par value shares cannot be issued along with shares with a nominal value.

Creativity First

The above possibilities must not be abused. The general principles of the new legal regulation are to protect investors against disadvantages. The flexibility offered by these alternatives could become an excellent basis for creative structuring of private investments, altering shareholders' relations and acquiring a new capital for business development. Small and medium-sized businesses are the core of every economy and the possibilities of acquiring capital for further growth is seen as an important step in restarting economic growth.