

Shares

Nature of Shares

Shares are rights of ownership in a company. Shareholders have a stake in the business and take the corresponding risks and rewards. Generally shares will have rights in relation to voting, to income upon declaration of a dividend by the directors and rights to return of capital on winding up. Within this framework, it is possible to create different types and categories of share which participate differently in the company's income and assets. The Companies Act 2006 does not make any substantial difference to this freedom.

Issuing shares can be a mechanism for raising finance. Shares in a private company may be issued to investors such as venture capitalists. Ultimately if a company is launched on the Stock Market, the shares may be publically traded. Shares are commonly issued to employees by way of incentive.

Types of Shares

UK Company law allows a great deal of flexibility in the types of rights which may attach to shares. Particular types of rights may be appropriate to particular types of investors.

Ordinary shares are shares with no special rights or restrictions. These would typically be entitled to dividends declared by the directors from the income of the business (if any), after payment of all other classes of shareholders, loan holders and other lenders have been paid.

The holders of ordinary shares are usually entitled to attend and vote at general meetings, to receive accounts and other information. They are also usually entitled to the assets of the company in a winding up after all debtors and other shareholders have been paid their entitlement.

Preference shares can be very useful in providing for medium term investment in business. Preference shares generally carry a preferential right for payment of income and/or capital to a specified extent, usually a percentage of the nominal value of the shares. Like other shares, preference shares will not usually carry a legal right to payment of their dividend. For example, there may be insufficient profits.

Preference shares will typically have cumulative rights to income, so that no income may be paid to the ordinary shareholders until the arrears of preference dividend have been paid. Preference shareholders carry less risk than the ordinary shareholder, but correspondingly have a limited and fixed return.

Redeemable shares allow the shares to be purchased back by the company, subject to certain conditions. Redeemable shares may be an attractive option as they allow the investor to exit the investment without requiring other shareholders to finance the repurchase. The repurchase must generally be financed from accumulated profits.

Investments in small companies are commonly engineered by creating classes of preference shares, redeemable shares and ordinary shares or a combination. Company Law provides great flexibility to provide an appropriate investment structure. It allows ownership rights in the company to be structured in any way desired.

Dividends

Dividends may be declared by the Board of Directors out of available profits. There is no general right to a dividend unless this is specifically provided in a shareholders agreement. The payment of dividends attracts income tax for the recipient. Dividends are paid without retention of tax. Individuals in receipt are entitled to a tax credit against their income tax to compensate for the fact that the company has paid tax on the profits concerned. See our separate chapter on dividends and the chapter on investment income in our tax guide.

Transfer of Shares

A company must maintain an internal register of shareholders. A company may not transfer certificated shares unless a proper instrument of transfer has been delivered upon which stamp duty has been duly paid. A transfer of certificated shares (those proved by the issue of a certificate) in a private company is not completed until the transferee has been registered as owner in the register of members.

Under the standard draft Articles for private companies, the company is allowed to have restrictions on shares. Restrictions are required in the case of private companies, which constitute the vast majority of companies. Only public companies may have freely transferable shares. The shares of listed companies must be freely transferrable.

Under the standard private company restrictions, the directors may refuse to register a transfer of shares. Registration must either be granted or refused within two months. The Companies Act, 2006 makes new provision requiring the company to give reasons for refusing to register a transfer.

See our notes on shareholders agreements and joint ventures in relation to the issues that arise in relation the transfer of shares. These agreements usually make specific tailored provision in relation to the transfer of shares, that are appropriate to the circumstances.

The transfer of shares carries stamp duty or stamp duty reserve tax at 0.5% of the value of the transfer. Stamp duty reserve tax or stamp duty is payable on share transfers at the rate of .5%. In a transfer through CREST, SDRT is collected by CREST on settlement of the trade Stamp Duty is payable on a paper transfer. Penalties arise if stamp duty is not paid within 30 day.

The transfer of shares is potentially subject to Capital Gains Tax. See our guides to UK taxation and to the Irish aspects of UK taxation.

CREST and Public Companies

Most shares on trading Stock Exchange are uncertificated shares i.e. dematerialised. Title is recorded and transferred through a computer based system known as the Central Security Depository (CSD). This is operated independently of the companies whose securities it records. Operators of CSDs must be approved by the FSA. The only operator is CREST Co. Ltd who run the system called the CREST. CREST is also used for Republic of Ireland, Isle of Man and Jersey.

Title to shares can be transmitted by means of CREST only if the issue of the shares permits them to be held in uncertificated form i.e. dematerialised form and if the issuer and CREST permit them to be transferred by means of CREST. This is a requirement for shares listed in the Stock Exchange. CREST provides settlement on the London Stock Exchange and the Irish Stock Exchange.

Where a UK company has uncertificated shares, its registered members are divided into two; the operator register and the issue register. The operator register is maintained in the CREST computer system and is used to register transfers of uncertificated shares. The issue register transfers shares.

This Guide is intended as an overview and broad outline of the matters covered in it. Its purpose is to inform and raise awareness. We are happy to offer specific legal advice on particular circumstances.

This Guide should not be relied on as a substitute for comprehensive legal advice with reference to the particular circumstances.

While we have taken due care in the preparation of this publication, we do not accept legal liability as a result of any reliance placed on anything in this Guide. The reader should rely only on specific legal or taxation advice.