How to Offer Shares to New Investors

Many owner managed businesses look to introduce new shareholders into their company to generate working capital and/or to enhance the skill sets to move the company forward to the next level. When offering shares to new investors business owners need to consider how best to protect the finance, time and effort they have invested into the company historically. If the introduction is structured in the right way then business owners can preserve the historic value of the company and simply allow the new shareholder to share in the success they help create going forwards enabling the new shareholder to demonstrate his/her worth to the company.

There are various situations which may lead a company to introduce a new shareholder. It may be that the existing shareholders are seeking to allot shares in the company to a new shareholder who has been a manager that has worked for the company for many years or alternatively an external investor, who is seeking to invest money into the business for a share in the profits going forward.

Regardless of who the shareholders are considering as an investor in the company they need to ensure that the existing value of the company at the point of the introduction is preserved. In order to achieve this the existing shareholder can create two or more classes of shares namely, "A" and "B" shares etc. The "A" shares can encapsulate the current value of the company which will then become the fixed value of the capital right of the "A" Shares. The "A" Shares would not have any voting or dividend rights and the shareholders would merely be entitled to a fixed sum on a return of assets being equal to the current value of the company. In contrast the "B" Shares would be held by all the shareholders both existing and new, and would have full voting and income rights. The capital rights of the "B" Shares would be subject to the "A" Shares. This would mean that any new shareholder would only be entitled to a share of the value of the company to the extent that he/she has contributed to the success of the company and where it is worth more than the initial valuation attributed to the "A" Shares. This would provide an incentive to the new shareholders to promote the success of the company whilst protecting the current shareholders' historical success. For example, if a Company is valued at £1,000,000 and the "A" Shares are attributed a fixed capital right of £750,000 then the "B" Shares would have a capital right to £250,000.

Of course the rights surrounding the different classes of shares may vary, for example if the current shareholders chose to introduce two new shareholders, one to work in the business and a second simply for investment, the income rights of those two new shareholders may need to be at different rates.

Introducing new shareholders into a company can be a risk as there is no guarantee that the relationship will work. If the current shareholders "ring fence" the investment they have already added into the business then the exposure is limited to future investment, the sensible advice is that the more uncertainty that can be taken out of the situation the better the chance of the company prospering.

If you would like any further advice in relation to the above, please contact Ruth Coleridge of Hawkins Hatton LLP, rcoleridge@hawkinshatton.co.uk or 01384 216840.