



THE RIGHT TO ACQUIRE A SHARE IN A COMPANY

Rewarding employees by assigning shares in the Company

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In this text, we are analyzing newly adopted regulation regarding a financial instrument called “The Right to Acquire a Share” (ownership) in a company, as a new financial instrument in Serbia.

This financial instrument was introduced by amendments to the Companies Act, which entered into force on April 1st 2020.

Basic idea

The basic idea that led to the definition and introduction of this financial institute in our legal system is to enable a new way of rewarding (and attracting) employees who can potentially significantly contribute to the business success of the employer (e.g., managers, executives, directors, etc.).

However, this right is not limited to employees, and its application can be much wider - it can be used like any other value (although it is harder to imagine paying for goods or services this way, even this is legally possible).

Procedure

The procedure by which this financial instrument can be used is relatively simple.

The first step for the implementation of the financial institute is the **separation / reservation of the company's own share**. The reserved own share the company (either owned by single or multiple shareholders) acquires for free from its members (from their entered/paid share capital), **for the purpose of establishing a financial instrument – The right to acquire a share in a company**.

The Decision on acquiring the reserved own share is made by the General Assembly of the company by a two-thirds majority of all members, provided that the share of the member who did not vote for the adoption of the Decision cannot be reduced.

The right to acquire a share in a company can be given to a third party for free. On the other hand, the share itself, if the option is used, must have a certain price. The current legal solution is unclear as to whether the price for the share must be paid in cash or can be paid in goods, services, and rights. We are of the opinion that this is also possible, if the price, i.e., the value of the share is clearly monetarily expressed.

The second step is the issuance of a financial instrument - The right to acquire a share in a company. The Company is obliged to submit the Decision on issuing financial instrument to the Central Registry within five working days from the day of issuance, for the purpose of registration of the financial instrument. At this moment it is also registered due date for settling the price for financial instrument – paying for share.

The third step is the realization of right, i.e., acquisition of a share in the company. The right to acquire a share may be: (1) realized by acquiring a share or (2) cancelled.

The right to acquire a share in a company is realized by paying a defined share price, within a certain period which cannot be shorter than 15 or longer than 30 days from the due date and afterwards by registering the acquired share in the company at the Business Registers Agency.

The right is cancelled if the holder does not pay the price for acquiring the share within the deadline determined by the Decision on issuing financial instrument - The right to acquire a share in a company. By same Decision can also be defined other cases in which the right can be canceled.

Additional specifics

Financial instrument the right to acquire a share in a company cannot be the subject of a pledge, nor the subject of inheritance.

On the other hand, heirs of the holder of this financial instrument have the right to demand from the company the payment of compensation in the amount of the market value of the share that the holder would be entitled to acquire on the due date of the financial instrument.

Tax treatment

Acquisition of a share by employees in the company is exempt from salary tax if the employee does not sell his share within two years of acquisition.

If the employee disposes of his share before the expiration of the period of two years, he will be obliged to pay taxes and contributions on the difference between the market value of the acquired share and the compensation paid. In this situation, determining the market value of the share is complicated by the fact that it is a non-transferable and non-inheritable right. It is expected that the Tax Administration will use the book value of the share in process of determination of the amount of due taxes and contributions.

The obligation to pay taxes and contributions also occurs in the case that employee voluntarily terminates his employment relationship before the expiration of the period of two years since acquiring shares.

Acquisition of a share by a person who is not employed in a company is subject to personal income tax on other incomes, at a rate of 20%, as well as contributions for pension and disability insurance at a rate of 25.5%. The tax base is the market value of the acquired share, reduced by 20% of standard costs. The issue of determining the market value of the acquired share also remains controversial here.

It should be mentioned that the sale of the acquired share may be subject to capital gains tax, at a rate of 15%. Capital gain is the difference between the purchase and sale price, i.e., the market value of the share when buying and selling the share.

Open issue

One of the most controversial issues related to the application of this new legal institute is related to the procedure of cancellation of the reserved own share.

Namely, if the company decides to cancel the reserved own share, the company is obliged to carry out the procedure of reducing the share capital. However, as the reserved own share will be acquired only from the share of members who voted for the decision to acquire the reserved own share, if there is a reduction of share capital, the same would be done exclusively to the detriment of the member who agreed to allocate the reserved own share from his share in the company. In the final solution, if the financial instrument is not realized, the respective member would end up with a smaller total share in the company.

We consider such a solution disputable and certainly discouraging for the use of this institute in any case in which the decision was not made by an absolute majority and at the expense of all members in proportion to the size of their shares.

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