Classes of Private Limited Company Shares

Business Information Factsheet

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Introduction

Most private limited companies only have one class of shares, called 'ordinary shares'. However it has become quite common for private companies to have more than one class of shares. A 'share' is a unit of ownership of a company, representing a fraction of the company's share capital.

Different classes of shares enable shareholders to be provided with differing rights depending on which sort of share they own. There are a variety of reasons why a company might choose to have more than one class of shares. For example, to create non-voting shares, to create shares with extra voting rights, or to create shares for their employees.

This factsheet provides an overview of different classes of shares and their purposes. It also explains the procedures that companies must use if they decide to vary the rights attached to different classes of shares.

The issuing of shares and the rights of shareholders are complex areas of company law and company directors should always seek guidance from a professional adviser before making any decisions.

Defining share classes when a new company is formed

Under the Companies Act 2006, shares are considered to be of different classes if they give shareholders different 'share rights'.

The Companies Act provides little guidance about what share rights are, so the term has been defined through case law. Examples of different share rights include the right to:

- Attend and vote at the company's general meetings (or vote in certain circumstances).
- Have more votes per share than another class of shareholder.
- Receive dividends (which may be fixed or variable).
- Receive dividends in priority to another class of shareholder.
- Have priority over another class of shareholder in repayment of capital if the company is wound up.
- Receive a share of surplus assets after capital has been repaid if the company is wound up.

A company may name different share classes in any way it chooses. It is common for companies to name share classes 'A' shares, 'B' shares, etc. Such shares are sometimes referred to as ABC or alphabet shares.

Common types of shares

Ordinary shares

Ordinary shares are the most common form of share issued by companies. Each ordinary share usually carries one vote. It also allows the shareholder to share in any dividends the company pays out and receive a share of surplus assets if the company is wound up.

If a company wants to make small variations in these rights, for example, different dividend rates, it can create different classes of ordinary shares, such as 'A' ordinary shares, 'B' ordinary shares, etc.

Companies can also create classes of ordinary shares with different nominal values - for example, 20p shares and £1 shares. If each ordinary share carries one vote, a shareholder buying 20p shares will receive five votes for every £1 they invest, while a shareholder investing in £1 shares will only receive one vote per £1 invested.

Voting and non-voting shares

Voting shares (including ordinary shares) give shareholders the right to attend and vote at the company's general meetings. Voting shares can also be drafted on the basis that their holders only have a right to vote if certain conditions are met.

Non-voting shares typically have the same rights attached to them as ordinary shares, except that the holder does not have the right to vote at the company's general meetings.

Preference shares

Preference shares are usually drafted to give the shareholder a 'preference', i.e. their shares will have priority over ordinary shares. This preference may include the right to receive a guaranteed or fixed amount of dividend or the right to receive capital (or both).

Preference shares with fixed or guaranteed dividends are usually drafted so that the shareholder is entitled to a percentage of the nominal value of the share. For example, if the company allots a £1, 5% preference share, the shareholder would be entitled to a dividend in respect of that share of 5p per year. (As with other dividends, the shareholder is only entitled to this payment if the company makes a profit.)

Some preference shares are drafted so that if the company cannot pay a dividend in one year it will carry it forward to future years. These are known as cumulative preference shares.

Deferred ordinary shares

Deferred shares rank lower than ordinary shares. This usually means that no dividend is paid to the shareholder until the holders of other classes of shares have received the minimum required dividend. If a company undergoes bankruptcy or liquidation, holders of deferred shares have no rights to company assets until all the other shareholders have been paid.

Redeemable shares

Redeemable shares are shares which give the company the option to buy them back in the future. The redemption date may be fixed or set at the discretion of the company directors. Such shares are often redeemed at the same price as the shareholder paid for the share, although this does not have to be the case.

Management shares

Management shares are often issued by a company to make sure that control of the company remains with certain individuals, such as the company's management team or original owners. Management shares are often drafted on the basis that each management share carries a multiple vote, for example 20 votes per management share. Alternatively, each share can have a smaller nominal value than other shares. This means that, for each £1 invested, there are more shares and consequently more votes.

Separate voting shares, dividend shares, capital shares

Some companies issue three classes of shares where class 'A' has all of the voting rights, class 'B' has all of the dividend rights and class 'C' has all of the capital rights. They do this so that shareholders can have different percentages of each different kind of right. For example, if there are only two shareholders then one shareholder may have 45% of the voting rights ('A' shares), 50% of the dividend rights ('B' shares) and 70% of the capital rights ('C' shares). The other shareholder then has 55% of the votes, 50% of the dividends and 30% of the capital.

Deadlock articles

Often a joint venture between two companies will result in the creation of a new company with two corporate shareholders, each with 50% ownership. Such a company (known as a deadlock joint venture company) may have two classes of shares which have the same rights attached to them, but which are intended to protect both shareholders in specific ways.

Changing class rights

If directors wish to change the rights attached to the classes of shares that were created when their company was formed, they must follow the procedures set out in the Companies Act.

If the company's articles of association specify a procedure for varying class rights, then the company must use this procedure. If the articles of association do not specify this, the company must gain the consent of the shareholders who own shares in that class. The Companies Act specifies that this consent must be given:

- Either in writing, from the holders of at least three quarters in nominal value of the issued shares of that class.
- Or by a special resolution passed at a separate general meeting of shareholders of that class approving the change.

The company must send a copy of the special resolution to Companies House within 15 days. It must also send a form (SH10) notifying Companies House of the variation within one month. Failure to do so is a criminal offence and carries a fine of up to £1,000. (Additional daily fines may apply if the company continues to delay providing the information.)

If holders of 15% or more of the shares in that class object to the change, they can petition the court to cancel the variation, provided they do so within 21 days.

The model articles of association, used by many private companies, do not include provisions for varying class rights. Companies that have adopted the model articles would need to use the statutory procedure under the Companies Act for gaining consent to any changes to class rights.

Further information

BIF 23 Duties of a Company Secretary
BIF 25 Duties of a Company Director
BIF 32 Choosing the Right Business Legal Structure
BIF 69 A Guide to Preparing and Submitting Company Accounts to Companies House
BIF 167 A Guide to Setting up a Private Company Limited by Shares
BIF 196 Glossary of Company Law Terminology

Useful contacts

Companies House is responsible for incorporating and dissolving limited companies in the UK, and for registering and publishing company information. It provides online access to UK company data, as well as guidance on starting, running and closing a company.
Tel: 0303 123 4500
Website: www.gov.uk/government/organisations/companies-house

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