

## Playing Chess When Creating Share Classes



**Gisèle Rosselle**

Partner  
giselle.rosselle@strelia.com



**Cédéric Devroey**

Associate  
cederic.devroey@strelia.com

Creating share classes allows a company to distinguish the rights of its shareholders. This is common in Belgian Corporate Law. The new Belgian Code of Companies and Associations (BCCA) defines a share class as a series of shares whereby the rights that are attached to them are different to the rights that are attached to other series of shares issued by the same company. Some examples are: shares with multiple voting rights, shares with varying rights to dividends or liquidation proceeds, shares with varying transfer modalities attached to them, shares with different rights as regards nominating candidates for the board. The differences in the rights attached to share classes can affect corporate strategies. This means the strategy considered by shareholders in various stages of a company's decision-making can significantly impact the decision's outcome, which in turn can affect the short- or long-term plans and goals of the company. In this Strelia M&A Series, we will be drawing an analogy between the creation of share classes and the game of chess. We see share classes as chess game pieces, the rights attached to them as their movement, and the restrictions to their movement (as a result of the change of rights attached to the share classes) as tactics that can be deployed to achieve a certain goal. We will give a recap of certain rules of law in relation to share classes and share our insight into how to navigate towards checkmate.

### *Game Rules – A Brief Recap*

Chess strategy is all about evaluating chess positions and setting up goals and long-term plans for the future play. Share-creation strategy is the same: evaluating shareholders' positions and making plans to steer the company towards reaching its goals. In chess, the most basic way to evaluate the shareholders' position is to count the total pieces on both sides. In share creation, this is looking at the number of share classes and considering the rights attached to each share class. For example, a share class could have multiple voting rights. This must be borne in mind as it can impact the power balance at future share issuance because the preferential subscription right is exercised per class; this means some of the shareholders will be able to increase their voting power.

After share classes have been created, the general meeting may decide to change the rights attached to any of the classes, for example, restricting the voting rights attached to certain share classes. But what constitutes a change to the rights attached to share classes is very broadly outlined in the BCCA. It defines this concept as any decision, such as the creation of one or more new share classes, that creates an unequal impact on the share classes. To ensure that the principle of equality between the share classes is observed, the BCCA lays down mandatory law rules that must be followed if a company wishes to change the rights attached to share classes. These rules include: (i) the contemplated change must be approved at the general meeting by a 75% majority in each class, (ii) the board must draw up and submit to the general meeting a special report on how the contemplated change would impact the rights of the other shareholders, and (iii) the statutory auditor (or external auditor) must report on the financial and economic elements of the board's report.

### *Navigating the Chessboard towards Checkmate*

Throughout the life of a company, events and circumstances will require shareholders' decisions to steer, and sometimes even to save, the company. Just like the chess game, tactics will therefore have to be deployed in different stages to achieve the desired decision-making outcome. Let's apply the above rules to a sample scenario in which a company is in need of cash, and shareholders are called to decide on a capital increase. If this capital increase results in inequality between existing share classes, then it constitutes a change of rights attached to a share class. This triggers the requirement of 75% of the votes in each class, representing 50% of the total shares, to be fulfilled. But if a shareholder holding 25%+1 in the company vetoes this, the decision will be blocked. A new shareholders' meeting will have to be called (second call), and the 50% quorum will no longer be required. The decision will be adopted if 75% vote yes. However, if this is not attained, then there is a deadlock. Parties could try to resolve this out of court through negotiations, and if they cannot reach a consensus, the dispute could be brought to court. The court could conclude that the minority shareholders' exercise of their voting right constitutes an abuse and order them to pay damages. And if the dispute concerns a repeated abuse of voting right by the minority shareholders, the court could, under certain conditions, order their exclusion or order the judicial dissolution of the company.

To avoid such a scenario from going to that extent, or, in other words, to anticipate such situation from the very beginning, shareholders could try to assign a share class to potentially difficult minority shareholders in which they do not have 25%+1 (i.e., they cannot veto) at the time of share class creation. This is analogous to the opening phase of the chess game, i.e., evaluating everyone's positions. Alternatively, voting restrictions could be imposed on minority shareholders so that none of them will have 25%+1 in a share class. But the BCCA is unclear on this, whereas the old Companies Code provided explicitly for the lifting of voting restrictions if there is a change of rights attached to share classes. Shareholders could also enter into voting arrangements. This is a tactic that can be used to pave the way to checkmate. These arrangements can require all shareholders concerned to exercise their voting right in a certain way in general or with regard to specific transactions or types of decisions. If voting arrangements are desired, they must be restricted in time, be in the interest of the company, and not amount to an obligation to vote according to the instructions of the board of the company or its subsidiary. In addition, voting rights of shareholders (and the voting arrangements) may not be exercised in such a way that it constitutes an abuse by the majority or minority shareholders. If a court concludes that there is abuse, it can nullify the general meeting's decision in question.

Creating share classes thus requires strategic thinking from the start, just like chess strategy, which makes it much more fruitful at the end of the day than simply following somewhat burdensome legal procedures.