

Pursuant to the Gibraltar Companies Act, there are numerous mechanisms through which the shareholders of a private company can extract cash from the company's balance sheet other than by way of dividend without having to resort to the Gibraltar courts.

There are several provisions in place which exist to protect a private company from reducing its share capital. The reasons for this can be clearly understood. Investopedia describes a company's share capital as "funds raised by issuing shares in return for cash or other considerations". Legislation is therefore in place to prevent these funds being distributed by the directors of the Company without having to go to a third party (e.g. the court) for consent.

However, in Gibraltar there are certain circumstances, when, with the consent of the shareholders of the company, a private company may be able to reduce either its paid up share capital or its share premium account. This can be done through the use of two mechanisms:

- a. the issue of redeemable preference shares; or
- b. effecting a buy-back of the company's shares.

The mechanism used in each individual case will depend on the circumstances of each particular private company. The use of the redeemable preference share route does not constitute a "reduction of capital", but it should be noted that what is being achieved is the reduction of the company's share premium account.

### Redeemable Preference Shares

Redeemable preference shares are often used in two situations:

- a. when there is to be a clear exit of shareholders in a determinable period of time (such as a structured exit of a private equity fund); or
- b. when (for whatever reason) there is a significant amount of money in the share premium account which the directors of a company may be looking to distribute to some or all of its shareholders.

These are not the only circumstances where redeemable preference shares may be useful. However, they are commonly used in these scenarios.

Redeemable preference shares can be created by the shareholders of a company at an extraordinary general meeting of the company (as long as they are permitted to do so by the articles of the company), and the articles of the company must clearly state how the redemption of the redeemable shares is to be effected. This will usually mean that the articles of association of the company have to be amended to include provisions for redemption. The flexibility of this route, however, is that you can tailor your redeemable preference shares (and/or the redemption of the same) to suit the circumstances of the particular company.

The shares must be redeemed either out of the distributable profits of the company or out of a fresh issue of shares, but any premium payable upon redemption of these shares can be provided out of the funds held in the company's share premium account.

## The Buy-Back Route

Alternatively, a private company which is not listed on any recognised investment exchange may buy-back its own shares (so long as it is permitted to do so by its articles), as long as it complies with several provisions of the Companies Act. This may be done either out of the distributable profits of the company or out of capital.

The one fact which needs to be borne in mind when effecting a buy back (either with distributable profits or capital) is that a company *must* have more than one shareholder, since the shareholder whose shares are to be bought back is unable to vote on any of the resolutions of the company which are to be passed for these purposes.

The buy-back of shares out of distributable profits is a less cumbersome route than a buy-back out of capital. Similar to the manner in which the mechanism is used in the United Kingdom, this mechanism is extremely useful when a company is looking to buy out a shareholder and terminate the shareholders relationship with the company. It can also be used to reduce a shareholder's stake in the company, without necessarily buying out that shareholder. This method uses a company's distributable profits to "pay-back" that shareholder and cancel those shares.

If a company is to buy-back its own shares out of distributable profits, it must approve the buy-back in advance by way of a special resolution of the company. This is done by the company approving a contract to be entered into for the purposes of purchasing its own shares. The contract is to be available for viewing at the company's premises for a period of 28 days prior to the contract being executed (once it has been approved at the special meeting). Any payment to be made by the company for its own shares is to be made out of the distributable profits of the company. Numerous other conditions also have to be fulfilled, including but not limited to the notification of the registrar.

A company (which is not listed on a recognised investment exchange) looking to buy-back its shares out of capital must also approve the buy-back by way of special resolution of the company. The company's directors must also issue a statutory declaration confirming (amongst other items) that the company is solvent. What a company is effectively doing by going through this avenue, is that it is buying back shares out of profits which would not necessarily be available for distribution.

This should be accompanied by an auditor's report. The company must ensure that the statutory declaration and the auditor's report remain available for inspection at the company's premises for the period of five weeks after the resolution has been passed.

Numerous other provisions have to be fulfilled.

It should be borne in mind that during the five week period, any member of the company may apply to the court to request the court to cancel the resolution. On such an application, the court may adjourn the proceedings in order that an arrangement be made to the court's satisfaction for the purchase of the interests of the dissentient member. The court may also make an order either cancelling or confirming the special resolution of the company.

It should be quite clear that this route may take several months and may become as cumbersome as a reduction of capital (where the company must apply to court) if there is a dissenting shareholder.

## Conclusion

The methods outlined above are all mechanisms by which to extract cash out of a company without the directors necessarily having to declare a dividend. It should be clear that the route to be followed by each company will very much depend on the facts of each particular case (and how the company is structured) as well as the results sought. The ease with which a company can alter its articles in a bespoke manner to cater for redeemable preference shares can be contrasted to the more convoluted process for buying back shares out of capital. It should also be clear from the brief summaries provided above that the buy-back of shares out of capital should really only be followed if the company is quite certain that it will not have any dissentient members (or it has no distributable profits).

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