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NOTIONAL SHARES IN THE POLISH SYSTEM AS A METHOD OF REMUNERATION OF EMPLOYEES

WHY NOTIONAL SHARE?

Running a business involves the expenses, most commonly in the form of employee salaries. Bearing in mind the increase of these costs and also increase in tax rates, entrepreneurs are undertaking various actions aimed at reducing costs.

However, fearing the loss of qualified staff or a decrease in the efficiency of their work, management boards of companies do not decide to lower wages.

Notional share could help to save some money and maintain employees.

WHY NOT TYPICAL SHARE?

Initially, the instrument, which was aimed at motivating employees, mainly the managerial staff, were typical shares. However, as demonstrated by the practice, rewarding executives with this type of instrument did not fulfil its primary purpose. New stockholders decided to sell their securities on the secondary market. It was then unfavourable from the standpoint of the company's dispersed shareholders.

NOTIONAL SHARE AS A WAY OF REMUNERATION



- ▶ The legal relationship between the company and the shareholder begins when the parties conclude an innominate contract in respect of this share
- ▶ The notional share does not vest the holder with any shareholding rights to the company.
- ▶ The beneficiary of this financial instrument is not seen as a shareholder (partner) of the issuer and has no voting right.

THE EXERCISE OF THE SHAREHOLDER'S RIGHT

- ▶ The exercise of the shareholder's right is based on receiving cash at a certain point in the future.
- ▶ The notional share can be set next to cash bonus because the beneficiary receives cash in both cases.
- ▶ The "bonus" received on the basis of notional share is usually much higher than the traditional cash bonus.
- ▶ Postponing payments (which may be short, medium or long term) is conducive to building a loyalty system among the most desirable employees.

SHAREHOLDER'S RIGHT IS A CONDITIONAL RIGHT

- ▶ The right to receive benefits provided on the basis of holding notional shares is a conditional right.
- ▶ Realization - the receipt of a benefit - can only take place if two conditions are met jointly.
- ▶ The first is the expiry of the period for which a notional share has been issued.
- ▶ The second is the achievement of a certain minimum contractual value of a given multiplier, e.g. EBITDA.

EXECUTION SHAREHOLDER'S RIGHT

Execution is nothing more than the redemption of these shares by the issuer company for the price that they reached at the time of the implementation.

CONSTRUCTION OF NOTIONAL SHARES

It meets all the basic criteria required for such qualification and this instrument is specified in the Regulation of the Minister of Finance of December 12, 2001 on detailed principles of recognition, methods of measuring the scope of disclosure and presentation of financial instruments.

- ▶ The value depends on the change in the value of the underlying instrument
- ▶ Purchase does not cause initial costs or is low
- ▶ Settlement will take place in the future

REASONS FOR NOTIONAL SHARES ISSUE

- ▶ An interesting way to reward and motivate employees
- ▶ Helps build loyalty for employees
- ▶ The company cannot reward employees in a conventional manner e.g. with typical shares) as a result of the restrictions resulting from the legal form of conducting its business activity (notional shares can be issued de facto by all entities)
- ▶ The company's authorities intend to divide the economic value of equity, but not the capital itself
- ▶ The company wants to provide the employees with additional opportunities and incentives to work
- ▶ Other incentive plans are too expensive

ADVANTAGES OF NOTIONAL SHARES

- ▶ Additional cash for employees
- ▶ The income earned from exercising notional shares is not subject to mandatory social security contribution and health insurance premiums
- ▶ Tax aspects:
 - the exercise of rights from notional shares should be regarded as income derived from cash capital
 - it will only be taxed at 19%
 - beneficial for taxpayers who exceed the second tax threshold

RISKS OF NOTIONAL SHARES

- ▶ The potential problems associated with the way disclosures of the financial consequences of the issuance and exercise of the rights under those instruments
- ▶ The company may also be exposed to criticism for paying employees cash awards
- ▶ The settlement of costs that result from the payment of notional shares may outweigh the profits
- ▶ Employees may not know how to use this type of incentive system
- ▶ The lack of knowledge of notional shares may raise concerns among employees whether the motivation program is fair
- ▶ A situation when a company may, despite financial difficulties, be obliged to redeem notional shares when the deadline expires.

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KG Legal, as a Polish law firm, renders legal assistance in investments in Poland. We provide specialist expertise for corporate and private clients. We advise in respect of setting up business in Poland, buying real property in Poland or investing in start-ups, including biotech and new tech start-ups or other commercial aspects.



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Investing in Special Economic Zones in Poland:

- ▶ Legal assistance in setting up and operating business by foreign investors in Polish Special Economic Zones;
- ▶ Legal support in obtaining tax exemption in Polish Special Economic Zones;
- ▶ Negotiating the conditions of investing in the Special Economic Zones with the administrator of SEZ;
- ▶ Legal assistance in purchasing and leasing real property in Polish Special Economic Zones.

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Representing international Clients before tax and administrative authorities in Poland:

- ▶ Legal assistance in obtaining relevant licences and permits, administrative decisions and certificates to conduct business in Poland;
- ▶ Representing international Clients in the Office of Competition and Consumer Protection;
- ▶ Representing foreign employers before employment law authorities and before administrative authorities in Poland (including Polish governors);
- ▶ Representing foreign companies before the Inspector General for Personal Data Protection.

Legal advice on cross border contracts:

- ▶ Legal support in negotiating investment contracts with Polish business partners;
- ▶ Drafting, reviewing and negotiating international contracts with Polish entrepreneurs;
- ▶ Securing contractual interests in such transactions as sales, distribution or licensing to Poland;
- ▶ Securing payment in Poland;
- ▶ Conducting local and cross border negotiations with the Clients' business partners in the Polish market;
- ▶ Advising on contractual penalties;
- ▶ Advising on security interests, mortgage, promissory notes, liens and registered pledges in Poland.



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Thank you for your attention

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