

## Exercising Stock Options

Exercising options is the process by which an investor can be buy specified number of shares at the predetermined price. The time frame is set out in the respective contract. Non -exercise within the referred time frame will trigger expiration of the share.

### Grant Price

Grant price of a stock option is usually inferior to its market price. Exercise of the option at the time of its purchase will, in this regard ensure an immediate profit.

Portuguese provisions governing stipulation of the purchase price, payment and completion provide that the parties are allowed to freely agree a purchase price with regard either to its amount or the chosen currency, provided that such stipulation does not go against the bona fide principle.

The price may be set in a specific foreign currency, either by indexing it to a specific amount in national currency at the exchange rate in force at the time of the agreement, or without such correlation.

However, exercising the options and holding them for more than a year can be advantageous from a tax perspective, however, upfront payment is warranted and the holder may suffer a loss on investment if the stock

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*Cameira Law*

*13-15 Craven Street | London  
/WC2N 5AD*

*Telephone: 44 (0)20 7930 1900*

*Facsimile: 44 (0)20 7930 2828*

*Rua Tierno Galvan, Torre 3, 17º  
Piso 1070-274 Lisboa*

*Telephone: 351 21 382 2500*

*Facsimile: 351 21 382 2509*



price drops on the market. This is particularly beneficial to investors who are prepared to tie up their investments for a period of one year.

**What are the parameters to prevent exercise, if there is a disparity between the price resulting from application of an agreed upon formula and fair market value.**

Portuguese provisions governing payment terms and consideration assessment conditions provide that if the parties to a contract freely agree upon a formula determining the future exercise price, such formula shall be enforceable, even if there are disparities in relation to the fair market value.

Therefore, considering that each party has

previously accepted to bear the risk of price fluctuations in accordance with future economic devaluation or inflation of the asset, the exercise of options may occur even if the price paid differs from the market price.

In most cases, exercise of options cannot be prevented as there is complete freedom for writers and holders to organize the sale of shares through the granting of options in the manner and on the conditions they deem appropriate, provided that they act fairly and in good faith and there is agreement on any

aspect of the transaction. In such cases the price may be indirectly set, through a predetermined formula, below its reasonably expected fair market value.

Nonetheless, in specific cases the exercise of options can be prevented as there are general principles laid down in the Portuguese Civil Code on pre-contractual and contractual duties and the bona fide principle which are applicable to contracts in general and to options contract holders specifically,



and that if breached may affect the validity of exercise.

According to these principles, the parties to an agreement are obliged to fully disclose all material facts and conditions upon which a deal is constructed, to not deliberately conceal defects and liabilities that may have an impact upon the price or value of the underlying, and to not exert unlawful pressures on the other party that may be construed as coercion or duress. In such cases, exercise of the option may be prevented. Additionally, agreements which only

benefit the buyer and are disadvantageous to the seller are null and void according to the Portuguese Civil Code's provisions on good faith and *bonos mores*, as well as provisions regulating consideration which must have some degree of adequacy and tend to go against disproportion. The manner in which the option was granted or acquired may also have some bearing on the assessment of whether a contract's completion is disproportionate or unbalanced and, if so, invalid, non exercisable and unenforceable. One such legal provision enshrined in the

Portuguese Civil Code is the *clausula rebus sic stantibus* – analysed below.

## **Legislation**

### **Streamlining procedures for the incorporation of private limited Companies – Decree-Law 33/2011.**

On December, 30, 2010, the Council of Ministers approved Decree-Law 33/2011 of 2 March that establishes a number of measures aimed to simplify the incorporation of private limited companies by quotas and sole quotaholder companies,



among which we highlight the following:

a) Removal of minimum mandatory share capital requirement, hence shareholders will be able to agree freely on its amount;

b) Shareholders or a single shareholder can make their capital contributions until the end of the first financial year.

These measures aim to reduce the administrative costs and expenses due with the company's incorporation, promoting the

competitiveness and encouraging employment, pursuant to the Government's commitment assumed under the XVIII Government's Program.

**Disclosure duties on long term positions on holdings – CMVM Regulation No. 5/2010**

Regulation No 5/2010 amends CMVM (*Comissão do Mercado de Valores Mobiliários*) Regulation No. 5/2008 of 15 October providing for the implementation of disclosure duties on the holding of the so called long term positions on shareholdings.

In summary, the new rules require that long term positions on holdings be disclosed at an initial threshold of 2%, 5%, 10%, 15%, 20%, 25%, one third, 40%, 45%, one half, 55%, 60%, two thirds, 70%, 75%, 80%, 85% and 90% of the share capital and also when such exposure is reduced below any of these thresholds, the investor is under a legal duty to disclose such holdings to the CMVM and to the invested company. Disclosure shall be made within four trading days of the occurring fact.



The process by which long term positions are hedged through physical shareholdings has caused concern to companies and regulators because of the perceived ability of the long term position holder to control access to the shares or exert influence over the shares indirectly through its counterparty, usually an investment bank. For example, on termination of the long term position, the investor may wish to acquire the shares underlying the long term position, at which point the investment bank would

be a natural seller of such shares.

The new rules significantly tighten the Portuguese disclosure regime and the building of significant economic stakes in Portuguese listed companies using cash-settled derivatives without disclosure, become increasingly difficult to achieve.

The concept of long term positions covers:

- A) Holdings with voting rights counted accordingly to the criteria set out by the provisions of the

Article 20 of the Securities Code;

- B) The agreements or financial instruments of similar economic effect to holding of shareholdings even if they do not generate the attribution of voting rights, held directly or by third parties who are holders of the following financial instruments:

- i) Contracts for Difference;
- ii) Cash-Settled Swaps;



- iii) Cash-Settled Options;
- iv) Cash-Settled Futures;

The new rules aim to enhance transparency of long term positions on holdings and give companies and investors

a clearer picture of who has significant economic control over listed shares.

**CASE LAW**

**Directors’ Liabilities in Insolvency and Company Recovery Procedure**

**Case: Decision from the Supreme Court from the 25<sup>th</sup> January.**

1. It was held that the court may take into account any other existing circumstances in addition to the list of criteria contained in paragraph 2 of Article 126-A of the Portuguese Insolvency and

Company Recovery Code, in determining joint liability by directors, that may have significantly contributed to insolvency of a company. The requirements under Article 126-A are *inter alia*, where directors:

- (a) hide or conceal equity ownership of the company;
- (b) dispose or dissipate, in whole or in part, the

- corporate assets of the company for their own benefit;
- (c) set up a parallel business to the detriment of the company; and
- (d) hold fictitious accounts, tamper with financial records or intentionally omit mandatory



accounting  
for their own  
benefit.

2. To ascertain whether a director contributed significantly to the insolvency of the company, it is essential that at least one (or more) of the requirements listed in paragraph 2 of Article 126-A are met.

3. The mechanism of reversal of legal burden is applicable. Therefore the legal burden of proof shifts to the director, who will have to prove that his action(s) did not contribute to a large

extent to the insolvency  
of the company.

4. Beyond the cases listed in paragraph 2 of Article 126 - A, the legal burden of proof rests with the applicant to demonstrate that the director contributed to the insolvency of the company, and that there is a causal link between the wrongfulness of his/her action(s) and the insolvency.

5. In addition, the applicant must prove that the action(s) was committed by the director, within the statutory limit of two years prior to filing for bankruptcy.

## CASE LAW

### Shareholders Agreements

#### **Case: Decision from the Supreme Court from the 26th January 2010.**

1. Shareholders agreements are expressly permitted and regulated by Article 17 of the Portuguese Companies Code.

These agreements are binding and enforceable amongst the parties, provided they do not contradict the law.

However, any such provisions will be deemed null and void if



they compromise a shareholder to vote in a certain direction, or indeed abstain from voting, at general meetings, whether in exchange for special benefits or in strict accordance with the instructions of the company or one of its corporate bodies.

2. Shareholders agreements are entirely independent of, and exterior to, the deed of incorporation and articles of association.

The effects of shareholders agreements bind only the parties to them, and are not enforceable

against either third parties or the company itself.

Therefore, in the event that one of the parties to the agreement does not vote at a general meeting, in accordance with the provisions therein, the resulting resolution may not be nullified on the basis that the clauses of the agreement were breached.

3. Shareholders agreements are subject to the general principles and rules concerning contracts. Therefore the general *bona fide* principle is applicable and may ultimately give

rise to damages resulting from pre- or extra-contractual liability.

**NEWS IN BRIEF**



**1. Ambassador Alexander Ellis – CPE (Centre of Portuguese Studies) 23th March.**

Cameira Law organized another CPE dinner on the 23th March 2011. The dinner was held at the IOD (Institute of Directors), London. The speaker was Ambassador

Alexander Ellis, Director for Strategy in the Foreign and Commonwealth Office and former British Ambassador to Portugal.

Ambassador João de Valleria, the new

Portuguese Ambassador in the United Kingdom was our distinguished guest on that day.

We are joined for the first two consecutive CPE dinners of this year, by the four major top level sponsors supporting the CPE: Banif Investment Bank, Millenium BCP, Caixa Geral de Depósitos and Bank Espirito Santo.

**2. Seminar on Investment Opportunities in the Federal State of**

**Piauí, Brazil rescheduled for March 2011.**

The Seminar on investment opportunities in the Federal State of Piauí is scheduled to March 2011 in Oporto. As a result of the recent appointment of the newly elected Government in Brazil, the Government officials of the Federal State of Piaui who had been invited to participate in the Seminar have requested a postponement of the Seminar to March 2011, to allow them to tackle key issues of immediate concerns in Brazil.

**3. Governor of Bank of Portugal, Carlos Costa – CPE (Centre of Portuguese Studies) July.**

Governor of Bank of Portugal, Carlos Costa will be keynote speaker at another dinner of the Centre of Portuguese Studies in London, again sponsored by the four major portuguese banks in the UK: Banif Investment Bank, Millenium BCP, Caixa Geral Depósitos and Bank Espirito Santo.

The materials of this Newsletter are not intended to constitute legal advice and should not be construed or otherwise relied upon as legal advice or as a legal opinion with respect to any of the subjects addressed.