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WHY DO YOU CREATE SEPARATE CLASSES IN THE COMPANY?

When structuring a syndication, it is important to determine ways in which the lead sponsor (manager) and guarantors can be compensated additionally for their “sweat equity.” What some know as an override is a common means of accomplishing this.

The legal mechanics behind structuring an override involve the creation of two separate classes of members of the company with differing compensation and voting rights. Typically, Class A is where the entirety of the capital goes. Under this structure, anyone who puts money into the deal (including the lead sponsor) is thus a Class A member. Class B is then typically reserved for sweat equity with the lead sponsor doing as they see fit with them.

The classic example is a 90-10 split between Class A and Class B. This would reflect what some know as a 10% override. If the capital raise is \$1,000,000.00, and I contribute all \$1,000,000.00 I will own 90% of the company’s voting and distribution rights. The manager at their discretion would then allocate the remaining 10%. The creation of Class B is not only a good way to provide additional compensation to the manager, but also provides them additional voting rights beyond their capital contribution.

REMEMBER, ALL COMPANY AGREEMENTS CAN BE STRUCTURED DIFFERENTLY. ALWAYS CONSULT AN ATTORNEY BEFORE ENTERING INTO ANY BINDING LEGAL DOCUMENT.

-Written By Greg Ehrlich, Associate Attorney, Kaliser & Associates PC.

**Please note the information provided here is not legal advice and all information provided is merely for discussion purposes.*