

Paying in Equity: Shares for Services and Reverse Vesting

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For growing companies, issuing shares for services can preserve scarce cash and align incentives. Reverse vesting pushes that logic further: it allows a company to grant shares upfront while retaining a mechanism to claw them back if expectations are not met.

But equity is not a shortcut; it is simply a different currency. It comes with its own set of legal, tax, and practical constraints. Missteps at the outset have a habit of resurfacing later – often as tax liabilities, regulatory issues, or unexpected shareholders whose interests no longer align with the business.

Several constraints shape how these arrangements work in practice.

Tax: Start Here

Before discussing equity with a would-be recipient, obtain tax advice. Expectations can form quickly; unwinding them is harder.

From the recipient's perspective, that equity may not be "free": it can give rise to taxable income or a "[taxable benefit](#)", depending on the structure. See our blogs about [Issuing and Receiving Options](#) and [Forgotten Shareholders](#) for more information.

Corporate Law: Fair Value Matters

Issuing shares for services is not a matter of guesswork. Directors must determine the cash value of the shares and ensure the services received by the company are worth at least as much. In practice, that means more than rubber-stamping an invoice. Boards should consider what services were actually delivered – and whether the price reflects market reality.

For instance, section 23(4) of the *Business Corporations Act* (Ontario) provides:

Value determined by directors

The directors shall, in connection with the issue of any share not issued for money, determine,

- (a) the amount of money the corporation would have received if the share had been issued for money; and
- (b) either,
 - the fair value of the property or past service in consideration of which the share is issued, or
 - that such property or past service has a fair value that is not less than the amount of money referred to in clause (a).

The board must therefore determine the cash value of the shares, confirm the value of services actually received (and not otherwise paid for), and compare the two values to ensure that the cash value of the shares is at least covered by the fair value of those services.

A board will often refer to the relevant invoices in making these determinations, but should also confirm the services actually received by the company (rather than relying on what an invoice says was done). It may also be helpful to have a sense of the market value of the services, to evaluate whether the pricing used by the service provider is fair.

Securities Law: Who Qualifies?

Every issuance of securities needs a prospectus or an exemption. The commonly used exemption for compensatory issuances (section 2.24 of National Instrument 45-106 – Prospectus Exemptions) covers directors, executive officers, employees, and certain consultants.

In most cases, it is clear who qualifies as a director, executive officer, or employee, but “consultant” is narrower than it sounds. It requires a written contract and the expenditure of “a significant amount of time and attention” on the business. Handshake arrangements will not do.

Public companies issuing securities for services will have to comply with additional stock exchange rules. For example, each of the TSX Venture Exchange (TSXV) and the Canadian Securities Exchange (CSE) has issued guidance confirming that payment for investor relations, promotional and market-making activities must be on a cash basis, with security-based compensation arrangements limited to stock options only and subject to certain other requirements, including that it be reasonable and in proportion to the company’s scale.

In addition, each of the TSXV and the CSE provide that it is not acceptable for a person providing those services to receive cash compensation from an issuer and to also participate in a financing by subscribing for securities of the issuer in close proximity to receiving such cash compensation.

Paperwork Matters

Equity arrangements should be clearly documented from the outset.

Service agreements should specify that compensation will be paid in shares, along with the number of shares, pricing, and any timing considerations. Board approval is required for such arrangements, and a subscription agreement will be needed to complete the issuance. Consider whether there are any other documents the subscriber should execute, for example a unanimous shareholders’ agreement or a voting trust agreement.

Clarity at this stage reduces disputes later, particularly around valuation, timing, the scope of services provided, and tax planning.

Future Services and Timing

A company can agree in advance to pay for services in shares. However, it cannot issue those shares until services of equivalent value have been performed.

This creates a practical tension: the parties may want equity to change hands upfront, but corporate law requires value to be received first.

Two common approaches address this constraint.

Shares for Cash Up Front

For privately held companies, one option is for the corporation to issue shares for cash up front. The corporation will then have cash proceeds from the issuance which can help it pay for services over time.

This approach provides a clear record of value and avoids disputes about adjusting compensation for partial performance if the working relationship is terminated earlier than planned. There is no need for the board to assess the fair value of the services or ensure that they were actually received by the company. It also allows the service provider to become a shareholder from the outset, locking in their share price at that time.

Note however that this solution may not be available for publicly listed companies – see “Securities Law: Who Qualifies?” above.

Reverse Vesting

In a reverse vesting scenario, shares are issued upfront for cash consideration (typically at fair value) – but the company retains a right to repurchase them if defined expectations are not met. The repurchase price is often the original subscription price.

This structure works particularly well for founders and key contributors in early-stage companies where the share price is nominal or relatively low. It sets the relationship up for success by providing immediate ownership, while preserving a mechanism to unwind that ownership if the relationship breaks down.

However, its effectiveness depends on clear drafting. The conditions that trigger repurchase must be precise, objective, and easy to administer. Ambiguity here can turn a solution into a new source of dispute.

Not Just Shares: Options and Warrants

Shares are not the only way to compensate with equity.

Options and warrants provide a right to acquire shares in the future, typically for a cash exercise price. They can be issued at the outset of a relationship and structured with vesting conditions tied to performance or continued involvement.

The key distinction is timing. Options and warrants defer ownership until exercise, while reverse vesting grants ownership immediately (subject to clawback), which can help recipients feel more invested over the full course of the working relationship.

Each approach has different tax, legal, and practical implications. Some corporations put in place an option plan, which can help filter potential recipients of options to meet the requirements of Section 2.24 of NI 45-106. See our blog about [Issuing and Receiving Options](#) for more information.

Key Takeaways

- Equity can be a powerful tool – but only when treated with the same discipline as cash.
- Shares for services require a clear determination of fair value and proper board approval.
- Prospectus exemptions, particularly for consultants, depend on formal, documented relationships.
- Shares can only be issued once services are performed, creating a timing problem that must be addressed upfront.
- Reverse vesting can be an effective way to grant equity early while preserving downside protection.
- Clear documentation at the outset reduces the risk of disputes, tax surprises, and “forgotten” stakeholders later on.