Why shareholder agreements are vital

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Legal Matters

What would you feel like if you had no say in who you were in business with?

To make matters worse your new business partner is someone you do not have a good relationship with and knows nothing about your business or even the industry you are in.

This situation is not as uncommon as it sounds.

Business partners can die unexpectedly and leave their shares in their will or sell their shares in the company or business to whoever they like unless there is a shareholder agreement in place.

In a recent example, one of the six shareholders in an exporting business died unexpectedly in middle age.

This was, of course, a great shock to her family, and also to her business partners.

They had to quickly pick up all the tasks she had performed for the business and try to keep it on an even keel.

When you go into business with someone, you generally want to choose who that is.

If the shareholders had had a signed agreement in place they could have dealt with matters such as what happens to the shares when someone dies, becomes infirm or wants to sell.

Restrictions on leaving shares in a will could have been imposed, which would have avoided these problems.

Instead a process could have been agreed to value the shares and have them bought by the remaining shareholders.

The shareholders would then not be stuck with being in business with someone they did not get on with and who had no experience in their industry.

When you go into business with someone, you generally want to choose who that is.

Here they were left with no choice.

Shareholder agreements can cover who shares can be left to or sold to.

They can specify whether the company must buy the shares of a shareholder who dies or desires to leave.

When business partners are not moving in the same direction, things can get awkward. PHOTO: REUTERS

It is also possible to provide for the majority of shareholders, forcing the minority to sell (even if they do not want to) or the minority being able to require the buyer to buy their minority shares if the majority decide to sell.

Shareholder agreements can also cover other situations, like::

- How many directors will there be? Are all shareholders entitled to be a director?
- How are they appointed?
- How is the company managed?
- Are the directors directly involved day to day?
- How will directors be paid?
- Who can be a shareholder?
- Are there different classes of shares, with different voting rights?
- What decisions require unanimous shareholder support?
- What meetings are held? How often? What quorum required? What notices needed?
- Exiting the company and compulsory buy-outs.
- Valuation of shares. Who by and who pays?
- Resolving deadlocks.
- Restraints of trade. What terms, for how long and where?
- Non-solicitation of staff.
- Disputes resolution by mediation or arbitration.
- Distributions.
- Funding. Who will contribute what?
- Insurance. What kinds and for how much?
- Confidentiality. What does this apply to?
- Intellectual property. Who owns what?

A failure to have a signed written agreement can leave the company open to all sorts of problems if there are disputes or an unexpected change in circumstances.

Column courtesy of Rainey Collins Lawyers, phone 0800 733-484 or raineycollins.co.nz. If you have a legal inquiry email aknowsley@rainey collins.co.nz.