



Lancaster, Brooks & Welch LLP

BARRISTERS AND SOLICITORS

When Shareholders Don't Share

By Michael A. Mann

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Entering into any new business venture is fraught with challenges, risks and, hopefully, rewards; but when you start up that new business with a partner – whether it is a relative, a friend, or a former business colleague, this adds another dimension to the undertaking. Generally speaking, people who want to start up a business together are so eager to market their product or service that they neglect to put a proper legal framework for their business relationship in place.

Although incorporating a company to run the business is often a prudent course of action, when there is more than one owner of the business, incorporation alone is not enough. Shareholders Agreements, while not the “be-all and end-all”, are integral to a corporate business relationship. Sometimes referred to as “Buy-Sell” Agreements, a Shareholders’ Agreement for a corporation is analogous in many ways to a prenuptial agreement in that it can deal with the fall out of when “the marriage” breaks down. When properly drafted, a Shareholders Agreement will deal with situations such as first rights of refusal to buy shares, purchases on death and “shotgun buy-sell” clauses. These types of marketability clauses are meant to address the fact that shareholders do not want to be stuck in a business with someone that they may not get along with. While the mechanisms referred to in a Shareholders Agreement may not be perfect in all cases, it may at least keep the owners out of court to settle their disputes.

In addition to marketability provisions, a Shareholders’ Agreement often contains “Prohibited Acts” provisions. Regardless of the share ownership and regardless of who the directors and officers of a corporation may be, a Prohibited Acts section in the Agreement can define those matters of such importance that will require a unanimous decision of all of the shareholders (or some other majority decision as may be agreed upon) to take action or to refrain from doing something. For example, the decision to declare dividends to shareholders out of the profits of the corporation at the end of a business year is, by default, a decision made by the company’s board of directors; however, a Prohibited Acts section will often taken this out of the control of the directors and instead make that a decision of the shareholders. Other examples would include any capital expenditures in excess of a specified dollar amount or changes to the nature of the business that the company operates.

A Shareholders Agreement can also deal appropriately with non competition and confidentiality covenants in order to protect the business and the goodwill associated with it.

A Shareholders’ Agreement is not “written in stone” and, in fact, will need to be revisited regularly to ensure that it reflects the intentions of the company’s owners. Business owners should seek appropriate legal advice to put such an agreement in place.

*The foregoing information is provided to you for information purposes only.
We caution you to obtain legal advice specific to your situation in all circumstances*

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