

DO I NEED A SHAREHOLDERS AGREEMENT?



This can be and should be, a common question for those going into business for the first time. A Shareholders Agreement is rarely a bad idea.

They should be considered in all situations where there are two or more shareholders or partners. To understand why, it is helpful to understand the concept of a Shareholders Agreement and the sort of things it can cover.

By outlining how the company is to be run from the outset, conflicts are more easily avoided down the track. When views diverge and circumstances change, resentment builds and this does happen.

WHAT IS A SHAREHOLDERS AGREEMENT?

In general terms, a Shareholders Agreement sets out how a company is to be run.

It details the rights and obligations of the shareholders. In some respects, it is similar to a Company Constitution. There can be some overlap between a Constitution and a Shareholders Agreement but they work in conjunction with each other.

The important difference is that a Constitution is a public document while a Shareholders Agreement is private and confidential between the parties. The details of a Shareholders Agreement are usually not matters that the parties want known to the public, including creditors, employees and competitors.

WHAT DOES A SHAREHOLDERS AGREEMENT COVER?

There is no model agreement but there are variations of the same theme. In the interest of keeping this article to a digestible length, here are a few things that a Shareholders Agreement can cover:

- **Decision Making**

Day to day decisions are generally made by the Board of Directors. The Shareholders Agreement can set out who has the right to appoint Directors. It could also set out how many votes each Director holds that could be proportionate to the number of shares of the appointing shareholders, rather than a single vote per Director. It can provide for a manager to make more decisions.

- **Minority Protection**

In a closely held company (with few shareholders), it can be easy for a single majority shareholder to dominate the decisions and management of the company. Without an agreement, majority shareholders may force issues that are not in the minority shareholders' interests. The minority shareholders will want protective provisions or to define the limit of the decisions that can be made by a single shareholder.



- **Pre-Emptive Rights**

If one shareholder wishes to sell shares, the other shareholders will usually want a first right to buy them to avoid shares going to a competitor. There is a range of ways to determine the sale price including by agreement, by valuation and by pre-determined formula.

- **Funding**

The agreement can set out how the company should raise working capital. If it is contemplated that the shareholders will make loans to the company, the basis of the loans can be set out, including whether interest is payable and whether the company should provide security.

- **Dispute Resolution**

With any luck, the Shareholders Agreement will minimise any potential for business disputes between owners but there can be matters for disagreement from time to time. It is helpful and cost efficient, to provide a clear framework and procedures for dispute resolution.

- **Exit Strategy**

The agreement should set out how a shareholder exits from the company. There are and will be, varying reasons and the agreement should provide for all scenarios.

In fact, I am of the opinion that perhaps the most important component of going into business with someone is knowing how to get out. Get it in writing!

Perriams has a “template” that we believe covers all aspects of the key to a “happy business marriage”.

If you would like to have a look over this, please do not hesitate to get in touch.



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