legal matters | BUSINESS LAW

Workable, innovative, cost effective solutions for clients.

Hussein A. Hamdani

Hussein Hamdani is a partner in the Business Law and Real Estate Groups at SimpsonWigle LAW with an emphasis on assisting owner/operators of businesses with all aspects of their business needs.

Q

I am in a business with others, should we sign a shareholders' agreement?

A

Yes! The term "shareholders' agreement" is used to describe a formal agreement between the shareholders of a private company and the company. It is considered the most important agreement that business owners neglect to sign.

Most business people starting up new companies agree that a shareholders' agreement is important. Two reasons are put forward frequently for not putting the agreement in place at the beginning: "We are too busy getting the business up and running (and anyway, we all get along really well)"; and "We don't have the cash yet."

The first reason really doesn't hold water. Running a small business means you are always busy. So, if you don't have time to get around to a shareholders' agreement at the beginning, face it: you won't later on. As far as getting along really well, that is the way almost all businesses start. Yet, like marriages, a significant number of small companies encounter disputes between shareholders. By then, the goodwill between shareholders has evaporated, and it is not possible to sign a shareholders' agreement. Instead, the parties have to sue each other in court.

The second explanation for not getting an agreement in place, is the exact reason why a shareholders' agreement is important – the main point of an agreement is to save everyone legal fees in case there is a dispute in the future.

Some topics that a good agreement will cover includes the following:

Dispute Resolution. When a bitter dispute arises between shareholders, and it is agreed that they cannot both continue in the business together, decisions as to who should leave and the price of their departure, may be very difficult, costly and time-consuming. A shareholders' agreement can minimize both the timeframe and the costs involved, dealing with dispute resolution by adopting one of several possible methods of enforced share sales and answering in advance the questions of who buys and who sells, what is the price, and when the sale takes effect.

Management. Particularly where there are more than two shareholders, or where there is a minority shareholder, provisions restricting management may be important protection for those who can be out-voted. Typically, the agreement will provide that certain decisions require unanimous approval and others a specified percentage in excess of 50%.

Restrictions on Share Transfers. It would be a major problem if a shareholder could sell his/her shares to anyone, at any time and for any price. This would not be fair to the remaining shareholders. A properly drafted agreement sets out the rules and an agreed to process on how a shareholder can tranfer their shares.

Death. The death of a shareholder actively involved in a business creates problems on two fronts. The surviving shareholder(s) no longer have the benefit of the deceased's contribution to the business, and may need to replace that person with a new shareholder. The family of the deceased wants compensation for the deceased's interest in the business. The obvious solution is to provide a mechanism for the shares of the deceased to be sold to the company, the other shareholder(s) or a new shareholder. An agreement would deal with the mechanism on how the deceased's shares would be valued and how the family would be compensated. In the absence of such an agreement, the deceased's shares could be bequeathed in the will to an annoying nephew or someone the surviving shareholders have an issue with.

There are many other provisions a well-drafted shareholders' agreement will contain. It is important to speak to your business lawyer to assist you in preparing such an agreement.

HAMILTON
1 Hunter St. E.,
Suite 200
905-528-8411

SimpsonWigle LAW LLP

BURLINGTON
390 Brant St.,
Suite 501
905-639-1052

www.simpsonwigle.com

The advice offered in this advertorial column is intended for informational purposes only. Use of this column is not intended to replace or substitute any professional, financial, medical, legal, or other professional advice.

R0023298 4234