

Shareholders' Agreement

For companies with more than one shareholder, a shareholders' agreement is vital. Without a shareholders' agreement, the following scenarios could prove to be disastrous for a private corporation:

A shareholders' agreement defines the duties and obligations of shareholders in a private corporation. This agreement should be thought of as a set of ground rules which govern shareholders' behavior.

- Deteriorating relationship between shareholders;
- Shareholders wishing to sell their shares;
- A shareholder suffering a life threatening illness or dying; or
- A major disagreement on how the business is managed.

These scenarios illustrate the importance of establishing a set of ground rules to help deal with acrimonious situations.

Although shareholders' agreements will vary based on the various complexities that each business faces, the following is a list of provisions which may be included in a typical shareholders' agreement:

Significant Decisions

This provision will stipulate that significant decisions require shareholders' approval. Significant decisions may include a major change in company direction, the sale of the company etc.

Future purchase/sale/transfer of shares

- This provision provides for the future sale of shares (i.e. consent of the shareholders/directors is required for future issue of shares). It might also restrict who can become a shareholder in the company.
- A "right of first refusal" provision stipulates that a shareholder wishing to sell their shares must first offer the shares to existing shareholders before selling them externally.

A "shotgun clause" is an escape mechanism that shareholders can use in the event they cannot resolve a serious dispute. In a "shotgun" arrangement one shareholder may offer to buy the shares of the other shareholder for a stipulated price. The shareholder receiving the offer may either sell their shares at that price, or buy the offering shareholder's shares at that same price. This process aims to protect both parties and encourages the shareholders to determine a fair price.

Shareholders' Agreement

The agreement may also include the rules regarding the transfer of shares which may be triggered by the following events:

- death of a shareholder;
- marriage breakdown of a shareholder;
- bankruptcy/insolvency of a shareholder;
- disability of a shareholder; and
- retirement of a shareholder.

Finally, shareholders' agreements often address the following:

- how shareholder/employee are to be compensated;
- how disputes are to be resolved (i.e. arbitration, mediation);
- how the business is to be valued; and
- how a buyout is to be implemented.

Although a shareholders' agreement is a voluntary agreement, it is an essential tool in laying ground rules for matters of significant impact to corporations. Please note that this article deals strictly with privately held corporations. Public companies are regulated by the various securities regulations.

You should always consult a professional advisor before implementing a shareholder agreement.



The information contained herein has been provided by TD Wealth and is for information purposes only. The information has been drawn from sources believed to be reliable. Where such statements are based in whole or in part on information provided by third parties, they are not guaranteed to be accurate or complete. Graphs and charts are used for illustrative purposes only and do not reflect future values or future performance of any investment. The information does not provide financial, legal, tax or investment advice. Particular investment, trading or tax strategies should be evaluated relative to each individual's objectives and risk tolerance. TD Wealth, The Toronto-Dominion Bank and its affiliates and related entities are not liable for any errors or omissions in the information or for any loss or damage suffered.

TD Wealth represents the products and services offered by TD Waterhouse Canada Inc. (Member – Canadian Investor Protection Fund), TD Waterhouse Private Investment Counsel Inc., TD Wealth Private Banking (offered by The Toronto-Dominion Bank) and TD Wealth Private Trust (offered by The Canada Trust Company).

©/ The TD logo and other trade-marks are the property of The Toronto-Dominion Bank.

Revised 27/10/2011