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Your Legal Questions

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Q. I am investing in a private company in return for a 40% shareholding. I have been advised to get a Shareholders' Agreement prepared to protect my investment. Do I really need one?

A. Whenever you have a shareholding which is less than 50% you are at risk that the remaining shareholder(s) will use their majority to vote through changes which you do not want and which may be detrimental to the company and consequently your investment.

A Shareholders' Agreement is essentially a contract made between the shareholders themselves containing mutual promises to do or not to do certain things. These promises will vary according to the circumstances of each case but some typical clauses include:

- A promise not to issue more shares without the consent of all parties. Otherwise a minority shareholding could be 'watered down' in value by the issue of additional shares to the majority shareholder(s).
- The right to nominate a specified number of directors
- An agreement regulating further borrowing by the company
- Agreements on the payment of dividends to shareholders and salary levels for employed directors
- Rights to sell or transfer shares. Some shareholders may want the first option to buy a fellow shareholder's shares before they are sold or transferred to anyone else. Others may want an unrestricted right to transfer shares to certain individuals such as family members. More controversially majority shareholders may want to be able to force minority shareholders to sell their shares if they get an attractive offer to buy the whole company from an outsider. These provisions are complicated and need careful drafting.

A Shareholders' Agreement is a vital document to protect your interest in the company and the advice of a solicitor should be sought before completing your investment.

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