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Business Owners: The Importance of Shareholders' Agreements

Whether it's a family owned business or one owned by unrelated individuals, for private companies with multiple shareholders, a shareholders' agreement can be an important tool for maintaining a healthy relationship between the owners.

A shareholders' agreement outlines individuals' expectations, serves to minimize the potential for conflict and provides a mechanism to resolve disputes. Generally, it covers any or all of the following three areas:

Ownership – This can be one of the most important provisions of an agreement, especially if you don't want to end up in business with your business partner's spouse or kids. An agreement may restrict shareholders from encumbering or transferring shares without the consent of other shareholders and outline the procedures that must be followed on a third-party sale or a buyout of existing shareholders. The agreement may also discuss the procedures to follow upon the death, bankruptcy, disability, inactivity/retirement or marital breakdown of a shareholder.

Management – Particular business decisions such as the purchase or sale of certain assets or hiring/firing of key employees could be required to have unanimous or majority shareholder approval. Employment terms for the shareholders may also be documented, as well as restrictions imposed on their business activities outside of the company.

Financing – An agreement may address the method and terms by which the company can obtain additional funds and also how the retained earnings of the company will be used in situations such as repaying loans or declaring dividends.

Prior to implementing any shareholders' agreement, we recommend consulting with a legal and tax advisor.

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