How to draft a shareholders’ agreement

Are you an entrepreneur? Maddyness has compiled a toolkit to help you create, grow, and even sell your own startup. From recruiting a team and protecting your brand to financing your innovation, you will find tips, tools and advice to help you navigate the entrepreneurship labyrinth. In this article: several recommendations to draft and finalise a shareholders' agreement efficiently.

At the time that their startup is created, many entrepreneurs forget that it is critically important to implement precautionary procedures in order to resolve complex situations that could arise.

Too long? Here's the key takeaways

- No matter the legal status of your business, you can finalise a shareholders’ agreement.

- A shareholders’ agreement should be put down in writing, and signed privately by each party or third party.

- An Associate’s Agreement can be modified and adapted easily, provided

that all signatories and their beneficiaries are in agreement.

In the case of one signatory not respecting the contract, they will be liable for the payment of damages.

Define the motives to finalise in the shareholders' agreement

A shareholders' agreement allows you to define and protect the legal structure of your startup and prevent certain situations that could put the growth of your startup at risk. Like all well-written agreements, a shareholders' agreement can clarify what each signatory wants from the beginning. If disagreements arise later on what was agreed upon and it seems that some stakeholders remember things differently, a well-written agreement will always help solve problems.

This is especially true when you are collaborating with friends. Even if you and your friend are on good terms now and you continue to get along well, things may evolve. There are some friends who, when they become business partners, realise later that they disagree on everything which can lead to conflict.

> *"Putting something in writing makes the shareholders face hypothetical scenarios that could become a reality."*

Choose a good time

A shareholders' agreement can be negotiated at any time, even if it is just about one project. Here we will identify three stages at which a shareholders' agreement is necessary and important for a startup.

Seed stage

In the "initial" stage, a shareholders' agreement will help form the first questions relative to the relationships of the founders, based on their financial

input, their obligations and their roles. This type of shareholders’ agreement can be negotiated and signed by all founders themselves even before the creation of the company.

Early stage

At this point, a shareholders’ agreement can have the same goals as the ones mentioned above, but it can also be used for new founders or investors joining the company. If the company already has a shareholders’ agreement, it can simply be modified to fit the new circumstances. If the company doesn’t have one, it will be necessary to regulate all the relationships between parties and to incorporate financial clauses for the investors.

Growth stage

At this point, the company has usually proven its business model and found a product and market but often needs supplementary funding in order to develop faster and grow its position. Investors will start negotiations with an investment agreement which will become the new shareholders’ agreement between all parties involved in the operation.

> *“It is possible to draft a shareholders’ agreement at the beginning but can be put into place at whatever time during the life of your business. It’s up to you to choose when is best for you!”*

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Appoint each signatory and clarify their role

First of all, a shareholders’ agreement can be established no matter which legal

status your business has: a private limited company or a public limited company. Secondly, not all the partners and shareholders may necessarily sign the agreement. You must appoint someone who will finalise the agreement with you.

Once all the signatories are gathered, you need to clarify the role of each one. This might seem obvious at first, but sometimes many people contribute in one way or another to the beginning of a project without ever being considered as a "founder" of the company. This step is very important and, when created at the beginning of the project, allows you to better distribute capital between founders down the line.

Stay as objective as you can, in order to avoid emotional decisions such as "I spent more time on it than you, I am more involved," etc. Write a list of target criteria on a piece of paper and evaluate the contribution of each person in the business, past or future. These criteria could be: starting concept, creation of concept, technical and non-technical roles, CEO's position, previous relevant experience, or even sector-specific relevant expertise.

> *"The shareholder agreement is a confidential legal document: only the signatories will know the contents."*

Decide what you want to include

The targets and contents of the agreement can vary. What is included in a shareholder agreement depends on its purpose. You can, for example, define who can be a shareholder or be part of the board of directors. Or what happens if one of the shareholders becomes disabled, passes away, resigns, retires, graduates, etc.

Here are some of the most common clauses to consider:

The duration of the agreement clause predicts the duration of validity. In the contrary case, the agreement can be broken at any moment by a party.

The non-competition clause, here, doesn't imply financial compensation if applied to shareholders or non-salaried directors. However, it should have a

time limit and should equally allow the concerned person to do their professional work.

The inalienability clause can prohibit a partner from selling their part of the company during a predetermined duration.

The pre-emptive and preference clause gives priority to partners to buy the shares of one of their partners if they would like to sell them to a third party. The first is applied when the seller has already found a buyer, and the second obliges the partner to offer their shares to their co-partners even before finding a buyer.

The consent cause allows the addition of a third party into the business capital through a consent procedure detailed in the agreement.

The forced handover clause can require the signatories of the agreement to buy the shares of a partner who wants to leave the company.

The forced buyout clause can require certain partners to sell their shares to other partners.

The exclusion clause allows the expulsion of a partner if they violate certain obligations.

The joint exit clause makes sure that partners who sell their shares must sell them to a single buyer, under the same conditions.

Many other clauses exist and are adaptable to each agreement, like:

Clauses predicting the arrival of a new partner or the rights of third-party inheritor.

Clauses destined to resolve conflicts.

Clauses dividing the power between partners.

Clauses of the agreement relative to the non-competition between partners.

Don’t forget that all shareholders’ agreements are voluntary and consensual. It should have reasonable terms and conditions. Finally, it should be interpreted accordingly to the general principles of the contracts’ rights and shouldn’t be used to swindle someone.

> *“All people who are part of the agreement should understand what they are accepting, so that there is no misunderstanding in the future.”*

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