

# Why you need a Shareholders Agreement

For privately owned companies, a shareholders agreement is absolutely essential. Even if you've started a business with friends or relatives, this formal legal document sets out ground rules for ownership of the business, including the roles, the responsibilities and the obligations of each shareholder.

Here are just 3 types of scenarios a shareholder agreement can cover:-

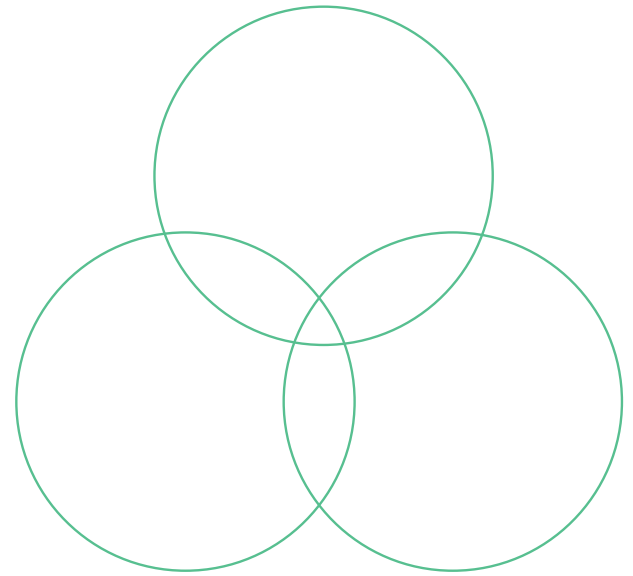
## 1. Drag and Tag Rights

With a drag-along provision, if the majority shareholder sells his stake, the minority shareholders must also join the sale, under the same terms, the same price and the same conditions. This protects the majority shareholder from losing out on a lucrative sale of a company, as prospective buyers may wish to purchase 100 per cent of a company's shares, whilst still ensuring that the minority shareholders receive the same purchase terms.

Alternatively, having a tag-along provision in your agreement means the minority shareholders have the right to join the majority shareholder's deal if he or she decides to sell, again with the same terms, the same price and the same conditions. This way, if the majority shareholder decides to jump ship, the minority shareholders won't be left behind.

## 2. Anti-Dilution Clauses

Whether you opt for a Weighted Average or Full-Ratchet anti-dilution clause, the provision can protect you from the risk of dilution later on if the company's valuation is reduced. In other words, it prevents the company from issuing shares at a lower price than that paid by preceding investors. Although tempting to



include in your shareholders agreement, anti-dilution clauses can backfire in certain circumstances. For example, if your company needs to raise new equity capital from existing shareholders in order to bolster its market position, lower issue prices will incentivise shareholders to buy, whereas an anti-dilution clause could mean that the issue price is higher than what it should be based on the company's actual underlying value, thus discouraging shareholders from re-investing.

## 3. Pre-emption Rights

By granting all shareholders pre-emption rights in the company bylaws, each shareholder has the first option to buy newly issued shares so that he or she can keep his percentage of total ownership. It can also give shareholders the first choice to buy an asset before it is offered to a third party. The primary benefits of this clause are that shareholders can maintain control of their venture and monitor wealth transfer in the company.

When founding a company, some shareholders may be hesitant to draft a shareholders agreement because of the mistaken belief that it will be available for public scrutiny. However, as a private law contract, the terms of a shareholders agreement are completely private and often confidential.

No matter how much you trust your fellow shareholders, circumstances can change along the

way, and the only means of protecting everyone's interests is with a carefully drafted shareholders agreement.

At Carter Bond, our expertise in business legal issues means we can draft a shareholders agreement to satisfy all of your concerns and requirements.

**For more information, or for expert advice on business or personal legal issues, call us on +44 (0)20 3475 6751 or via email at [info@carterbond.co.uk](mailto:info@carterbond.co.uk)**

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"I would highly recommend the services of Carter Bond for any type of corporate or commercial work."

Enis Rifat, MIYA Solicitors

#### HIGHLIGHTS

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We were awarded the 'Commercial Lawyers - London', in the prestigious 2020 UK Enterprise Awards

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