

Legal News



What is the purpose of a shareholders' agreement?

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Dear clients and business friends

If a corporation ("Aktiengesellschaft") is held by a single shareholder or if all the shares of a stock exchange listed company are distributed among the general public, there is no need to draw up a shareholders' agreement. If, on the other hand, the shares are held by a limited number of people who feel the need to regulate their rights and obligations with regard to the corporation above and beyond what is possible under corporation law, the shareholders' agreement becomes an indispensable element of legal structuring.

Shareholders' agreements are, for example, concluded in family-owned corporations in order to structure the rights of the shareholders in accordance with their needs or when capital is invested in a start-up and the later exit of one or more shareholders needs to be regulated.

The aim of this edition of Legal News is to remind the reader of a few basic elements and considerations in connection with shareholders' agreements and to provide ideas for the structuring of those agreements.

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1. Benefits of shareholders' agreements

Shareholders' agreements are suitable for all corporations, from small and medium-sized operations all the way to the stock exchange listed company. There are various titles in use: syndicate, shareholder pool, pool agreement, shareholder consortium, pact or shareholders' agreement, etc. The Swiss Code of Obligations defines the applicable rules for all corporations, from small to large. Nevertheless, the law does not regulate all the details. Shareholders have the opportunity to supplement the structural framework for the future of their company in accordance with their own needs and their common aims because, in this field, there is contractual freedom.

With a few exceptions, the articles of incorporation cannot burden shareholders with any obligations. There is no legal relationship between the shareholders and they have no obligation of loyalty to the company in which they have invested. The articles of incorporation of a corporation therefore cannot include any terms bound to the person of the shareholder. The requirements that are not covered by the articles of incorporation can be covered by the shareholders' agreement.

The possibility of tailor-made stipulations is particularly appreciated in small companies and those owned by families. In this way, the interests of minority shareholders can be protected, for example in that they are granted a position on the Board of Directors if they hold a certain minimum number of shares. If no shareholders' agreement has been

concluded and if, therefore, corporate law is exclusively applied, the majority shareholder alone could appoint all the members of the Board. In addition, a shareholders' agreement can also define qualified majorities for certain important resolutions, such as sale of the company.

The agreement can be concluded with all the shareholders of a company or, more frequently, with some of them. The agreement is, however, only effective for those who sign it. If a shareholder has not signed the agreement, it does not apply for him or her.

2. Vote binding

Shareholders' agreements often include vote binding arrangements which oblige the parties to exercise their voting rights in accordance with the resolutions of the syndicate of shareholders. Arrangements of this kind deviate indirectly from the principle of "one share one vote" in that for resolutions of the syndicate, not every shareholder is granted voting rights in proportion to his or her financial investment (for example if every member of the syndicate has one single vote). If there is any infringement of a vote binding arrangement, the disadvantaged parties cannot dispute the resolutions of the General Meeting. In this case, they can merely claim compensation of damages from the shareholder who has breached the agreement.

3. Possible special clauses

Shareholders' agreements can also serve to provide financial benefits in the

case of liquidation or rights to acquire (purchase or pre-emptive purchasing rights) or for the sale of shares. As an example, a "put option" includes the right of a shareholder to sell his or shares to another shareholder. In the so-called "Tag Along", there is a consequential right of others to sell their shares too, giving them the opportunity to make use of a favourable disposal of their shares. With the "Drag Along", the right - normally granted to the majority of shareholders - exists to force other shareholders to sell their investment at the same time. This makes sense in a case in which a third party is interested in buying the company at a good price for the vendor, but the purchase is linked to the condition that 100% of the capital has to be acquired.

The (not conclusive) checklist shown on this page provides an overview of the normal points included in a shareholders' agreement.

4. Penalty for breach of agreement

The penalty for breach of agreement is the Sword of Damocles hanging over the head of all the contractual parties to a shareholders' agreement. This clause normally foresees payment of a sum of money by a party that infringes the agreement to the other contractual parties. An example is that a shareholder who, at General Meetings, fails to vote in accordance with the stipulations of the shareholders' agreement has to pay a penalty defined in the agreement to the other parties.

5. Conclusion

When drawing up a shareholders' agreement, a specialist should be involved who can check the agreement for contradictions, conformity with the law and ability to be enforced. In addition, the agreement should be regularly reviewed to ensure that it constantly complies with current requirements.

Checklist for a shareholders' agreement (not conclusive)	
1. Contractual parties	<ul style="list-style-type: none"> ▶ Shareholders at given point in time ▶ Details and addresses of parties ▶ Number of shares held by each of the parties
2. Purpose of agreement	<ul style="list-style-type: none"> ▶ Field of activity and chronology of the company ▶ Strategy of the company and business plan ▶ Contribution of additional assets ▶ Distribution (or not) of dividends ▶ Employee participations (Stock Option Plan) ▶ Further objectives
3. Limitations of share transfers	<ul style="list-style-type: none"> ▶ Retention of a limited number of shareholders ▶ Confirmation of statutory limitations ▶ Purchase or pre-emptive purchase right ▶ Call-and-Put option, description of the process ▶ Valuation of the shares ▶ Consequences of infringements
4. Exercising of voting rights	<ul style="list-style-type: none"> ▶ Voting agreement for General Meetings ▶ Designation of a representative ▶ Consequences of infringements
5. Representation on Board of Directors	<ul style="list-style-type: none"> ▶ Composition of Board of Directors ▶ Signatory powers ▶ Qualified majority for defined resolutions ▶ Compensation for Board members ▶ Adaptation of articles of incorporation and organisational regulations
6. Anti-competition ban	<ul style="list-style-type: none"> ▶ People affected ▶ Time and geographic validity ▶ Connection with mandate or employment contract
7. Penalty for breach of agreement	<ul style="list-style-type: none"> ▶ For breaches of the agreement ▶ Payable to parties or the company ▶ Amount for each infringement of agreement ▶ Additional claims for damages ▶ Guarantee for payment of the penalty
8. Closing conditions	<ul style="list-style-type: none"> ▶ Duration and termination of agreement ▶ Confidentiality ▶ Deposit of shares with a third party ▶ Place of jurisdiction and applicable law

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