



## CHECKLIST FOR A NEW EQUITY HOLDERS AGREEMENT

Set out below are some of the initial queries that we send prospective clients whenever they are considering putting in place an appropriate Equity Holders Agreement (obviously, we suitably adapt this for companies, partnerships and unit trusts).

We work towards developing a 'modular', schedule-driven form of our Equity Holders Agreement for which clients can work through with our team paying particular attention to their relevant key business/board/member requirements, thresholds and variables so that each agreement addresses all their requirements and is completely customised for their needs.

In the below illustration, we use a company with shareholders and directors as a specific example of an Equity Holders agreement.

A shareholder agreement broadly covers the contractually agreed funding, structure, management and direction of the company and particularly the responsibilities and obligations of the shareholders. It is designed to deal with particular issues that may arise by determining in advance, how such issues must be dealt with.

These usually significantly enhance and may materially differ to the Company's standard, generic Constitution or the Corporations Act replaceable rules (if the company's shareholders did not originally have such when it was first formed), or Articles of Association if the company usually pre-dates July 1998.

Accordingly, the process of developing a shareholder agreement and the content included will differ for certain entities in certain contexts. The kinds of issues that the shareholder agreement contemplates includes, but is not limited to, the following:

1. How many shareholders will there be? Will they personally own their shares or through a trust?
2. Are each of the shareholders going to have equal shareholdings? (e.g. one has 50% and the other has 50% or one has 90% and the other has 10%)
3. Are there different 'classes' of shares (e.g. Ordinary, A, B, C Preference shares etc.)?



4. Are there to be 'active' shareholders (i.e. if they are personal shareholders (or their related individual) working in the company's business) and 'silent' shareholders (i.e. they just own share(s) and do not work and/or are not directors in the company)? If so, what is the payment that the active shareholder will receive for working in the business?
5. Is the active shareholder "earning" his/her equity interest? What are the benchmarks he/she must meet to earn that shareholding interest, is there a related sale or issue of share capital agreement?
6. If he/she earns his/her interest immediately but is reliant on subsequent performance what happens if his/her promises fall short of his/her performance?
7. What will be the entitlement to profits/dividends for the different classes of shareholders (if any)?
8. What financial and other relevant benchmarks must be met for the shareholders to draw dividends (i.e. "Dividend Policy")?
9. What additional authority and right, if any, will active shareholders have over what they are statutorily entitled to?
10. Is there to be a Board of directors which meets regularly?
11. Is the Board to have an independent director and/or chairperson?
12. Do the directors have one vote each or do they vote according to their shareholding?
13. Is the working capital of the company to be provided by way of equity (the issue of shares) or a loan?
14. Is any loan to the company to be secured and if so are directors' guarantees required to be given?
15. What happens if the initial share capital (usually \$xx per share issued) provided is not sufficient? Is more share capital issued (and paid for) or does the company borrow money / incur debt?
16. If each shareholder agrees to put in extra capital (if required) what happens if a shareholder ultimately cannot or refuses to put in the capital?
17. What happens if an active shareholder is not "pulling his/her weight"?
18. If the shareholders cannot agree about anything, is there to be a 'deadlock breaking' mechanism in addition to a dispute resolution provision?
19. What happens if an active shareholder is sick or injured so that they cannot participate in the business for an extended period?



20. Is there to be insurance to cover the death or incapacity of any shareholder or, more specifically say, their 'key' related director? If so, to what value? (i.e. "Key Man Insurance" or "Buy/sell Insurances" – note: these are materially different types of insurance arrangements).
21. If no insurance, what would be the source of any funds to buy out a retiring/incapacitated shareholder's interest?
22. Who is to have authority to operate the company bank account?
23. Are there to be varying \$ limits on a Director's authority to incur liabilities or purchase assets, as well as operate the company's bank account (i.e. less than \$2,000 and greater than \$2,000)?
24. What constitutes grounds upon which one shareholder can compulsorily acquire another shareholder's interest? (sickness/incapacity/insolvency/breach of agreement or fiduciary duty etc)?
25. Have the parties agreed an accountant to act as the accountant for the business?
26. Are the accounts to be audited?

Our shareholders agreement is very comprehensive as it not only addresses matters such as corporate governance, day-to-day management and company policies, it also contemplates a myriad of future events that may occur in the longer term, as the Company's business and its shareholders' circumstances change. It is better in the long run for the company if a wide range of issues are provided for in the agreement.

The key features of our shareholders agreement include, but are not limited, to the following:

- (a) Provides for enhanced pre-emptive rights, and last rights of refusal, of existing shareholders and also drag-along and tag-along rights.
- (b) Provides mechanisms (including the agreed valuation formula or method of the relevant shares) to deal with voluntary and involuntary succession events:
  - (i) such as death/mental incapacity/ill health for prolonged period;
  - (ii) criminal conviction;
  - (iii) bankruptcy/liquidation;
  - (iv) gross misconduct; and/or
  - (v) unremedied breach of the shareholders agreement by a shareholder (or its related director).
- (c) Confidentiality and Intellectual Property rights undertakings.



- (d) Restraints of trade on an exiting shareholder and its related director(s).
- (e) Dispute resolution and Mediation clause.
- (f) Limited Powers of Attorney.
- (g) Arrangements for additional capital contributions and loan arrangements.

There are other provisions which deal with management and Company's policies (e.g. power and authority of directors in relation to cheque withdrawals and bank overdrafts). If you have any other specific requirements, please instruct us and we will draft provisions to address those requirements as well.

For further information contact Murfett Legal by telephone on +61 8 9388 3100, via our website at [www.murfett.com.au](http://www.murfett.com.au) or email one of the following directors:

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