

A CRITICAL ANALYSIS OF SHAREHOLDER WITH REFERENCE TO SHAREHOLDER AGREEMENT AND ITS RIGHTS

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WHO IS A SHAREHOLDER?

A Shareholder, also referred to as Stockholder, may be a person, company or an establishment that owns least one share of a company's stock. Shareholders are the owners of the company. They get all the benefits of the company's success in form of increased stock evaluation. They play an important role in framing and profit of the company. They are the main stakeholders of the company. There are two sorts of shareholders during a company:

Common Shareholders

Common shareholders are the main shareholders in a company. They enjoy the voting rights over matters concerning the company. They also have many other rights including filing class action lawsuits against any matter that can harm the company.

Preference Shareholders

Preference shareholders are the shareholders that have no voting rights because of their preferred status but enjoy precedence over common stockholders. They receive fixed dividends, larger than those paid to common stockholders.

WHAT IS A SHAREHOLDERS AGREEMENT?

A Shareholders Agreement is additionally referred to as Stockholders Agreement. It is basically an arrangement among company's shareholders, which outlines their rights. It also includes information on the management of the corporate and therefore the privileges and protection of the shareholders. It regulated the sale of shares of the company and determine how important decisions are to be made.

The number of shareholders during a company depends upon the sort of company:

- **One person** for a **One-person company**.
- **Two persons** for a **private limited company**.
- **A minimum of seven persons** for a **public limited company**.
- **Basics of Shareholders Agreement**

The main motive of the shareholders agreement is to make sure that the shareholders of the company are treated fairly and to protect their rights.. It provides safeguards of minority positions and also allows shareholders to decide on who can become a shareholder in future. It is an optional agreement and is often by and for shareholders, outlining the rights and obligations.

A shareholder's agreement includes a date, the number of shares issued, a capitalization table, outlining shareholders and their percentage of company ownership, any restrictions on transferring shares, and pre-emptive rights for current shareholders to purchase shares.

NEED OF A SHAREHOLDERS AGREEMENT

A shareholder agreement is entered to found a solution of any disputes between the shareholders and any types of the company. There is no surety that nothing will ever go wrong, in such cases these agreements helps in dissolving the disputes if it occurs and maintains a healthy relationship between the shareholders and the company. It lays down the rules and regulations for the shareholders and also protects the investment made by them. Regulating A shareholder's agreement is important as not every shareholder is same. An agreement has got to be drafted keeping in mind that each person is different and has the various opinion on subjects or matter concerned. And that they'll or might not agree with one another.

MAIN PROVISIONS OF A SHAREHOLDERS AGREEMENT

A Shareholders Agreement contains of the following provisions:

- Management of business and business plan of the company.
- Funding of the company.
- Proportion of shares and different class of shares for different category of shareholders.
- After then the Representation and warranties of the shareholders and the company.
- Restriction on share transfer and pre-emptive rights.
- Method of valuation of share.
- Voting and management rights of the shareholders.
- Deadlock resolution process.
- Additional information rights.
- Exit rights of shareholders, termination clause, indemnity.
- Confidentiality, non-disclosure and non-compete clause.
- Governing law and dispute resolution clause.

RIGHTS OF SHAREHOLDERS UNDER SHAREHOLDERS AGREEMENT

There are several rights of a shareholder under shareholders agreement:

1. Appointment of Directors

Shareholders play a significant role in the appointment of the directors. An ordinary resolution is passed in order to appoint the directors. Apart from this, they can also appoint various types of directors.

- **Additional Director**- who will hold the office until subsequent general body meeting.
- **Alternate Director**- who will act as an alternate director for the period of three months.
- **Nominee Director**
- **Director appointed in case of a casual vacancy** in the office of any appointed director.

2. Legal actions against Directors

Shareholders can also give detailed information related to legal actions against directors by the rules that are laid down in the Companies Act 2013. They are as follows:

- The first one is that any act which is done by the director in any manner which is prejudicial against the affairs of the corporate.
- Second is any act which is done which is beyond the law or against the constitution.
- Fraud.
- After when all the assets of the company are being move at an underrate.
- When there's a diversion of funds of the corporate.
- Any act wiped out a mala fide (bad intention) manner.

3. Appointment of Company Auditors

Shareholders even have a right to appoint the corporate auditors. Under Companies Act 2013, the primary auditor of the corporate is to be appointed by the board of directors. Further the shareholders at the annual general body meeting at the advice of directors and audit committee. The appointment is usually finished five years and further are often ratified by passing a resolution within the annual general body meeting.

4. Voting Rights

Shareholders even have the rights to attend and vote at the annual general body meeting. Every company registered in India should suits the provisions of the businesses Act 2013. It is mandatory for each Indian company to carry an annual general meeting once per annum. The meeting is often held anywhere at the top office of the corporate or the other place as given by the corporate. These include the adoption of monetary statements, appointment or ratification of directors and auditors etc. When a resolution is brought by members of a corporation then

consistent with companies act 2013, it is often passed only by the means of voting by the shareholders. Companies Act 2013 recognizes following types of voting.

- **Voting by the showing of hands** – Every member present within the meeting has one vote. So, during this sort of voting shareholders vote just by showing of hands.
- **Voting done by polling** – during this sort of voting the chairman or the shareholders' demand for a poll. However, just in case of differential rights on voting, a specific class of equity shares can also have weighted voting rights.
- **Voting done by electronic means**– every company who has quite 1000 shareholders has got to put up a facility of voting through online means. Every member should be given the means of voting of online.
- **Voting by means of postal ballot**– any resolution within the meeting also can be gone by means of a postal ballot.

5. Right to call for General Meetings

Shareholders have the rights to call for a general meeting. They have a right to direct the director of a corporation to call all extraordinary general meeting. They can also approach the corporate Law Board for the conduction of general body meeting, if it's not done consistent with the statutory requirements.

6. Right to inspect registers

As shareholders are the most stakeholders during a company, they need the proper to examine the accounts register and also the books of the firm and may ask questions on the same if they feel so.

7. Right to get copies of financial statements

Shareholders have the right to urge copies of monetary statements. It is the duty of the corporate to send the financial statements of the corporate to all or any of its shareholders either during a quarterly or annual statement.

8. Winding up of the Company

Before the corporate is aroused the corporate has got to inform all the shareholders about an equivalent and also all the credit has got to tend to all or any the shareholders.

9. Consent of Shareholders

The consent of a shareholder will be taken in the matters mentioned below:

- Whenever any of the members; manager or any member of the supervisory board is appointed, or is to be dismissed or main consent of shareholders is a must necessary.
- Whenever drafting a budget or distributing the dividend.
- When the corporate wants to amend the articles of association.

- When getting into amalgamation or filing for bankruptcy.
- When dissolving the company.

10. Amendment of AOA & MOA

Amendment to article of association/memorandum of association are often done by means of convening a general meeting of the corporate. The shareholders of the corporate have the proper to cast their votes regarding any amendments made to AOA/MOA.

11. To receive dividends

Shareholders have a right to receive dividends as a part of the Company's profits in a proportion equivalent to the number of shares that the holder owns, in accordance with the provisions set forth by Law and under the company Statutes. Equity shares don't guarantee a hard and fast return and, during a liquidation scenario, equity shareholders are entitled to a return in any case statutory and other pay-outs are made. Preference shareholders are given a preference with reference to payment of dividend and repayment just in case of liquidation of the corporate.

LIABILITIES OF A SHAREHOLDER

There is limited liability of a shareholder as the company is a separate legal entity, hence separate from the shareholder.

- Shareholders aren't responsible for the acts of the corporate.
- Shareholders are held liable only to the extent of the unpaid amount of share capital with reference to the share held by them.
- Where it's a corporation limited by guarantee, the shareholder is liable only to the extent of the quantity guaranteed by him.

DUTIES OF A SHAREHOLDER

Beside several rights of the shareholders, there exist several duties as well, which they should perform. They are:

- Act that is in line with the company's articles of association.
- Act in straightness so as to push the objects of the corporate for the advantage of its members as a whole, and within the best interests of the corporate, its employees, the shareholders, and therefore the community and for the protection of the environment.
- Exercise their duties with due care, skill and diligence and exercise independent judgement.
- Should not get themselves involved during a situation during which they'll have an immediate or indirect interest that conflicts, or possibly may conflict, with the interests of the corporate.

MECHANISMS THAT LAW OF INDIA PERMITS FOR REGULATING SHARE TRANSFERS

To regulate transfer of shares commonly used mechanisms are:

- a. **Right of first refusal**-This is an agreement between the prevailing shareholders whereby the shareholder wishing to sell to a 3rd party must first offer the shares to the holder of the primary refusal right. If the holders of the proper of first refusal don't buy the shares, the shareholder can normally sell freely to a 3rd party.
- b. **Right of first offer**-This may be a variation of the proper of first refusal during which a hard and fast price is agreed to from the outset. The shareholder wishing to sell shall first offer the shares to the holder of the proper of first offer holder at the fixed price. If the holder of the proper doesn't purchase the shares, the shareholder wishing to sell is liberal to sell it to a 3rd party.
- c. **Drag-along and Tag-along Rights**-Drag-along right is an agreement between the shareholder, where the shareholder wishing to sell his shares to a 3rd party has the proper to tug all the opposite shareholders and make complete exit from the corporate. Tag-along right is simply the opposite where the other shareholders have a right to accompany with the shareholder wishing to sell his shares to a 3rd party.
- d. **Another term that is Buy-back rights- According to** these it's gives the corporate the correct to save the shares of a specific shareholder in specific situation, like withdrawal or may be death of the shareholder.
- e. **Call Option**-Call option gives its holder the proper to shop for a specified number of shares of the underlying stock at a strike price between the date of purchase and therefore the options expiration date.
- f. **Put Option**-Put option gives its holder the proper to sell a specified number of shares of the underlying common shares at a predetermined price (strike price) on or before the expiration date of the contract.

RIGHTS OF MINORITY SHAREHOLDERS

Minority shareholders are those that don't enjoy much in terms of powers when it involves the management of the corporate. Since the introduction of the businesses Act, 2013, the rights of the minority shareholders are given importance. There are not any specific provisions under Indian law to make sure participation of minorities on the board of directors of a corporation. Also, Indian law doesn't provide for provisions ensuring minority control over board of directors. However, the minority shareholders are often given the proper to nominate directors on the board of directors by contractual arrangement between the shareholders. Under a shareholders' agreement minority shareholders are often given the facility to appoint directors on the board of directors of a corporation. However, that doesn't in any way mean that the minority shareholder has control over the corporate. The recent judicial trend shows that Indian courts interpret 'control' to mean effective control of the management of the corporate and not merely having the proper to appoint nominee directors. The test of 'control' is satisfied when a shareholder has the power to regulate and choose the management decisions of the

corporate.

The minority shareholders of a company have certain statutory rights. Their rights include:

- **Right to requisite a general meeting**-A minimum of 10% of the shareholders carrying voting rights within the company have the proper to requisition the administrators to convene an unprecedented general meeting of the company. If the administrators fail to convene the meeting then those shareholders have the proper to call the meeting on their own.
- **Right to vary shareholders' rights**-A minimum of 10% of the holders of the category of shares whose rights are being varied have the right to use to the Tribunal to possess the variation of rights attached to their shares cancelled if they are doing not consent to the present variation.
- **Right to Oppression and mismanagement**-A minimum of 100 or 10% of the entire number of members, whichever is a smaller amount, or any member or members holding a minimum of 10% of the issued share capital of the corporate have the proper to approach the Tribunal:

a) If the affairs of the corporate are being conducted during a manner that's either:

- The first one is Prejudicial to public interest, or the interest of the company; or
- The second one is Oppressive to any member of the corporate .

b) The other change that might materially affect the management of the corporate in order that the affairs of the corporate are (or are being or are likely to be) conducted during a way that's prejudicial to the interests of the corporate or any of its members.

Right to class-action suit Under the businesses Act 2013, a category action suit is often initiated by either:

- a) At least 100 members or a minimum of 5% of the entire number of its members (whichever is less).
- b) Any member or members holding a minimum of 5% of the issued share capital in an unlisted company, or a minimum of 2% of the issued share capital during a listed company.
- c) In addition to the statutory rights, minority shareholders may have certain contractual rights towards other shareholders which include veto rights, board representations, and exit rights.

Enforceability of Shareholders Agreement According to the provisions of 2013 Act, any provision which isn't consistent or not incorporated within the Articles of Association is ultra vires and hence void.

It is a standard practice to change the Articles of Association of the investee company to reflect the position in SHA. This helps make sure that none of the provisions of the SHA are rendered inoperative by virtue of them being contrary to the constitutional documents of the investee company. A breach of SHA which doesn't breach the articles of association may be a valid

corporate action but the parties aggrieved can get the remedy under the overall law of land for any breach of that agreement.

In India, judges during a number of cases have held that a SHA is claimed to be void if an equivalent isn't embedded into the Articles of a corporation. Therefore, mere execution of SHA isn't sufficient; it's required to be duly incorporated into the Articles in order that its enforceability isn't put to challenge. Any provision during a SHA, if not incorporated within the Articles are going to be deemed inconsistent and hence void.

In the case of **V.B. Ranga raj v. V.B. Gopalakrishnan**, it had been cited that whenever it involves challenging the enforceability of a shareholder's agreement. during this case, Hon'ble Supreme Court held that "a restriction which isn't laid out in the articles of association isn't binding either on the company or on the shareholders." Further, the Supreme Court accepted the proposition of the parties that an agreement between two shareholders of a personal company, by which restrictions are imposed on their ability to transfer the shares, is wholly ineffective unless it's incorporated within the Articles of the company.

In the case of **Western Maharashtra Development Corporation Ltd. v. Bajaj Auto Ltd** one Judge Bench of the Bombay Supreme Court had also pronounced a judgment on the enforceability of a right of first refusal clause during a shareholders' agreement. The supreme court examined Section 111-A read with Section 9 of the sooner Companies Act. Section 9 essentially lays down that the provisions of the businesses Act shall have effect notwithstanding anything to the contrary contained within the memorandum and articles of a corporation or in any agreement executed by it and any such provision within the memorandum, articles or any agreement shall, to the extent of such repugnance, be void.

DRAFTING OF A SHAREHOLDERS AGREEMENT

- It is important to understand the purpose of the shareholders' agreement, the need to balance the interests.
- The terms of the agreement need to be clearly defined to avoid it any ongoing confusion.
- The rights, duties and responsibilities of the company and shareholders must be stated briefly.
- The agreement must not be compromised taking into account the shared interests of the company and the shareholders.
- The policies, procedures and guidelines set out in the agreement should be concise and consistent.
- All matters specified in the agreement must be provided in accordance with applicable laws

CONCLUSION

A shareholder may be a part-owner of an organization who acquires his interest by contributing capital towards the formation of the corporate or by buying its shares. Shareholders of a

corporation enjoy variety of rights and powers in exchange for his or her investment within the company and even have responsibilities that arise from their ownership of the corporation. Shareholders thereby play a crucial role within the functioning of a corporation.

The Shareholders Agreement was introduced with a view to reinforce the operations associated with the functioning of the corporation, and supply clarity and structure with reference to the connection between the corporation and its shareholders at any given point in time. This helps in quicker resolution of disputes and results in the undeterred and smooth functioning of the corporation and its operations. Shareholders thereby play a crucial role within the functioning of a corporation. They need various rights which include the appointment of the company's director, auditor etc., to voting rights and having a say when the corporation goes insolvent. With every right, comes a corresponding responsibility which the shareholder must perform diligently.

Though, execution of Shareholders Agreement has become a daily practice amongst the corporation, yet the question about its enforceability can't be ruled out. The underlying question that whether there's any real conflict between the Articles and Shareholders Agreement remains a mystery which has got to be cracked after a due examination of the precise clauses of a shareholder agreement read in light of the aforesaid cited judgement.

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