## HOW TO REMOVE A SHAREHOLDER

Shareholders do not always work out. There sometimes comes a point where one shareholder wants to cut ties with another in their company. While it's a complicated process, it is not impossible – especially if you take precautions. Our recommended five steps you should consider taking when making moves to remove a shareholder. This list is not exhaustive and it is subject to the Companies Act.

### 1. Refer to the shareholders' agreement.

A shareholders' agreement outlines the rights and obligations of each shareholder in an organization. Typically, it is created and agreed on by all shareholders to ensure everyone is fairly represented. That way, if you want to cut ties with a shareholder down the line, you can refer to this document for guidance.

In plain terms, the shareholders' agreement is a contract between all the shareholders that they will not do certain things. If the conduct rules are specific enough, getting rid of a shareholder for misconduct becomes much simpler.

This is especially useful when removing a majority shareholder – someone who owns more than 50% of the company's outstanding shares. If they violate anything explicitly stated in the agreement, you can remove them solely based on that offense. To avoid this issue, you can also make a provision in the agreement to elect a director annually.

Make sure to be specific with the agreement. It's important that you review details that can influence how and when to remove a shareholder, as well as any consequences for doing so. Look for details like the dates, the number of issued shares, anything related to shareholder equity, and the rights of shareholders in the event of a company sale, among other clauses that may impact the shareholder removal process.

**Tip:** You should also include a buyout clause that allows directors to purchase a minority share for an agreed-upon price. This will prevent minority shareholders who cannot be voted out from refusing to surrender their shares.

### 2. Consult professionals.

Before acting, especially without a shareholders' agreement in place, you need to reach out for professional insight to avoid any legal issues. While you might think the process is simple, it requires much thought and attention.

In short, removing a shareholder is not something for amateurs. You should consult with counsel, under attorney-client privilege, as early as possible. An agreed-upon voluntary

buyout between the company and the targeted will almost certainly cost far less than the expense of a contested removal.

Professionals can help you approach the matter in an objective, negotiable manner, while ensuring you meet any regional requirements in your area. This is crucial in any business decision, particularly ones that might cause tension among business partners. You don't want to skip this step in the interest of time or money.

In some cases, the expense of an independent attorney may even be necessary, if the company's counsel has ethical or legal obligations to the target of the removal.

**Bottom Line:** Don't go it alone. Consult your attorney and other relevant professionals before taking any action.

**3. Claim majority.**

Without an agreement or a violation of it, you'll need at least 75% majority to remove a shareholder, and said shareholder must have less than a 25% majority. The removal is accomplished through votes, and the shareholder is then compensated upon elimination.

While claiming majority might work in some cases, it doesn't against majority shareholders who already acquire more than 50% majority alone, or even majority shareholders with more than 25% majority.

**4. Negotiate.**

If all else fails and you find yourself with no legal reason to remove the individual, you should sit down and negotiate with them, discussing a fair value of their shares.

Although the shareholder may not be able to keep his shares, he almost certainly can dispute the value of what will be paid for the shares, and whether his removal occurred for an improper purpose.

Once you reach an agreement, you can buy back and distribute their shares to individuals in the company.

If during negotiations you succeed in ousting a shareholder, you must ensure that no shares remain unallocated. All shares will have to be either gifted or transferred to another shareholder by using a stock transfer form.

**FYI:** If they absolutely refuse to negotiate and you have no agreement in place to force the removal, you might have to face a tough decision: parting

ways with the company or learning to work with the individual regardless of your concerns.

**5. Create a non-compete agreement.**

If you’re successful in removing your shareholder, proceed with caution. Because the process is often rocky, you want to impose a non-compete agreement on your departing shareholder. This will ensure they do not start or enter a business that directly competes with your organization for a set number of days after leaving.