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To the reader of this brochure

Re: Simplified Shareholder Agreement for a new company with two shareholders
(50/50)
Presentation, purpose and limitations

August 2019

By email

For the attention of:

Reader

Please reply to:

Maëva Slotine

mslotine@slotine.hk

Our ref.

S_SHA

Your ref.

Shareholders

Dear Sirs,

Working with a partner that has complementary talent and skills may contribute to the success of a venture. But nothing in life is guaranteed. The business environment will change. People change. A few years from now partners may have disagreements over how the business should be run or one of them may want to leave the company. If the shareholders don't have a process agreed in advance on how to deal with these serious issues, and others, each of them may end up with nothing.

With this in mind it is important to have a written agreement drawn up by a lawyer that covers areas including compensation, exit clauses, and roles and responsibilities.

The idea behind Slotine's **Simplified Shareholders 'Agreement**, is to offer a simple agreement, which is drafted for entrepreneurs at an early stage of their venture.

This **Simplified Shareholders 'Agreement** covers some clauses – see attached. But does not include all, see also the non-exhaustive list of those that are not included. It is not meant to provide for any situation which may arise, therefore, in case of significant change (e.g. new shareholder, investors), the agreement shall be reviewed by a lawyer.

You will also find attached information relevant to a director or shareholder of a Hong Kong private company limited by shares.

The agreed fee for the **Simplified Shareholders 'Agreement** includes two hours meeting with all shareholders to understand the background and explain the various clauses as well as answer any questions they may have. Some simple or formal amendments may also be included, up to two hours additional work. Any other additional requirement shall be invoiced on a time spent basis, at the rates of the team members involved at the time.

We look forward to working with you in the future, should you need any advice or assistance with legal matters, whether for commercial agreements, employment agreements, dispute resolution, tax issues or negotiations with investors or prospective buyers.

Do let me know if you have any questions.

Yours faithfully,

Slotine

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Inventory of clauses

Main clauses included in the simplified shareholders' agreement

Directors and management: limitation to directors' authority; matters reserved for shareholders' approval

Finance for the Company: expose principles agreed by shareholders

Business Plan: set the standard for these key documents whose yearly approval is a matter reserved for shareholders' approval (see "Directors and management")

Accounting and other information: set the standard; extend shareholders information rights

Dividend policy: expose principles agreed by shareholders

Restrictions on shareholders: non-competition; non solicitation of clients, customers, suppliers and employees as long as a person is a shareholder and usually for 12 months thereafter

New shares and Transfers of issued shares: to keep it simple, issue of new shares are forbidden and sale of shares to third parties are framed as follows (i) forbidden for the first year of the company; (ii) thereafter subject to pre-emption right of the other shareholder and (iii) alternatively subject to tag along right of the other shareholder

Pre-emption rights on the Transfer of shares: the other shareholder has the absolute right to purchase all shares put on sale

Tag along: if the other shareholder is not willing to purchase the seller's shares, he is entitled to substitute some of his shares to those of the seller; in proportion of their respective stakes

Death: provisions for the purchase of the deceased shareholder by the remaining one

Fair Value: flexible definition; financial advisor to be appointed only in last resort

Resolution of a deadlock: mechanism of Russian roulette

Intellectual property: all belongs to the company

Governing Law: Hong Kong Law

Dispute resolution: Hong Kong International Arbitration Centre

Non-exhaustive list of clauses which are not included

Drag along: a clause which permits a shareholder to force the other one to sell his shares, so that the third-party buyer can purchase 100% of the company's shares

Deed of adherence: a document to be signed by a new shareholder in order to be bound by the shareholders' agreement. No template is attached because the simplified shareholders agreement is designed for two shareholders and should be reviewed if a third one was to become a member of the company.



Bad leaver or good leaver: clauses which cause a shareholder to sell his shares at a discounted price in case of breach of the shareholders agreement or other “bad leaver” cases or at a fair value in case of death or invalidity or other “good leaver” cases.

Provisions of Hong Kong law

These derives from the Hong Kong New Company’s Ordinance (Cap 622) (hereafter **CO**) and its Schedule 2 which contains standard Articles of Association for private companies limited by shares.

Shareholders rights in a nutshell

1. Vote in shareholders meetings or written resolutions of members (see below ordinary and special resolutions)
2. Dividends (in proportion of stake: only if profits available for distribution + decision of the board)
3. Maintain stake in the capital of the company (issue of new shares not allotted to shareholders in proportion to their shareholdings is subject to ordinary resolution)
4. Portion of the assets if the company is liquidated
5. Information: once a year, board and audit reports together with the company’s financial statements
6. Propose shareholder resolutions (according to the section 580 CO, the shareholder must represent at least 2.5% of the total voting rights of all the shareholders who have a relevant right to vote or at least 50 shareholders who have a relevant right to vote)

Ordinary resolutions (simple majority, i.e. 50% +1 vote):

- Appoint or remove directors
- Appoint or remove auditors

Special resolutions (qualified majority of 75% +1 vote):

- Turn a company “dormant”
- Alteration of the company’s articles of association
- Change the name of the company
- Varying class of shares rights
- Reduction of share capital

- Share buy-back by the company under general offer
- Appoint a person to investigate the company’s affairs

General meeting or written resolution

A general meeting is a physical meeting of the company’s. Two members present in person or by proxy constitute a quorum for a general meeting. Any resolution can be voted on this occasion.

A written resolution is a resolution that is taken without having a general meeting. This is strictly framed by the law and requires the signature of all shareholders.

Derivative actions

In the case of director’s misconduct which might be dangerous for the company’s assets, minority shareholders have the power to bring a derivative action against the directors (section 732(2) CO). An application to court will be required to this effect.



Collective power of the board in a nutshell

The board of directors is entitled to take any decision with regard to the company, except where this power has been reserved to the shareholders by the CO, by the Articles of Association or by a valid agreement. Decisions of the board require only a majority vote. The quorum for a board meeting to take the decisions is stated in the Articles of Association which normally requires a quorum of two or a number set by the directors.

The board of directors is responsible for:

- Determining the company's strategic objectives and strategic policies
- Appointing the company's top management
- Monitoring progress towards the achievement of objectives and compliance with policies
- Giving an account of the company's activities to the parties to whom an account is properly due

Individual power of the directors in a nutshell

Director's authority to act

- The Standard Articles of Association (Schedule 2 CO) says: "*Subject to the Ordinance and these articles, the business and affairs of the company are managed by the directors, who may exercise all the powers of the company*".

Who can commit the company?

- Directors' powers are not individual but collective. However, a board can delegate powers to committees or individual directors and in practice individual directors carry out many of a company's activities. An individual director who acts without the board having delegated the requisite authority can be liable for breach of duty to the company.
- In cases where a company denies liability on a contract with a third party because of some irregularity in the company's procedures or a lack of actual authority or appointment on the part of someone purporting to act on the company's behalf, the third party may nevertheless be able to claim that the contract is valid. He or she might rely on the "indoor management rule" of *Turquand's case* (1856) or claim that the person purporting to contract on behalf of the company had "apparent authority".
- The rule in *Turquand's case* protects a person dealing with a company in good faith and without notice of the fact that the company's internal management requirements have not been followed. A third party is entitled to assume that all internal procedures and requirements of the Articles of Association have been complied with unless he or she is alerted to the fact that this is not the case.

