

AGREEMENTS

Deadlock and Exit Planning

Mechanisms for 50/50 and closely held companies, from buy-sell clauses to cross-option agreements funded by shareholder protection insurance.

Why equal shareholdings stall

A company owned 50/50 works smoothly when the owners agree. When they do not, neither can pass an ordinary resolution, neither can remove the other as a director, and the business can be stuck. Courts are reluctant to step in unless a company is being run unfairly or there is no reasonable way forward. Planning the way out while the owners are on good terms is far cheaper than arguing it out later.

Closely held companies with three or four owners face the same problem in a different form: any two can block the other two, or a single holder with a small stake can hold up a sale.

Mechanisms for deadlock

A shareholders' agreement can set a ladder, starting gently and ending decisively:

1. **Escalation.** The directors meet, then the shareholders themselves.
2. **Mediation.** A neutral mediator is appointed, with a deadline.
3. **Casting vote or independent director.** A chair or independent person breaks the tie on stated issues.
4. **Buy-sell.** One shareholder names a price and the other must buy or sell at it, often called a Russian roulette or shotgun clause.
5. **Texan shootout.** Each side bids in sealed envelopes, and the higher bid buys.
6. **Sale or winding up.** If nothing else works, the company is sold or wound up.

Choosing a mechanism

Buy-sell clauses are quick but favour the shareholder with more money. A shareholder with a weaker bank balance may be forced out at a price they cannot match. A mediation step first, and a fair valuation by an independent accountant, make the clause more balanced.

Spotting deadlock early

Deadlock rarely arrives suddenly. Warning signs include board meetings that no longer happen, decisions made by one director alone, bank mandates being changed, and shareholders communicating only through advisers. A clause that lets either side call a meeting and requires a response within a set time helps to catch problems before positions harden.

Key points

- Plan for deadlock in a shareholders' agreement before it happens.
- Use a ladder: talk, mediate, then decide.
- Buy-sell clauses favour the better-funded shareholder.
- Cross-option agreements and insurance can fund a buyout on death or serious illness.
- Valuation method should be agreed in advance.
- Review the arrangements regularly, since values and circumstances change.

Planning for death or serious illness

If a shareholder dies, their shares pass to their estate, which may be a spouse or children with no interest in running the business. The surviving shareholders may not have the money to buy them out.

A common solution is to combine two things:

- **Shareholder protection insurance.** Each shareholder takes a policy on the others' lives, or the company takes the policy, so that a lump sum is available on death or critical illness.
- **Cross-option agreement.** The survivors have an option to buy the shares, and the estate has an option to sell, at an agreed price, using the insurance money. Neither side is forced to proceed, which can matter for tax.

The agreement should say who owns each policy, how premiums are paid, how the value of the shares is set, and what happens if the policy pays out more or less than the price. How the policy is held can affect tax, so take advice from the clients' tax adviser or an independent financial adviser before arranging it.

Planning for a planned exit

Owners also leave by choice: retiring, moving on or selling to a third party. Plan notice periods, the valuation method and the payment terms, and whether the leaver remains liable under any company guarantees.

Documenting it

All of this sits in the shareholders' agreement, backed by the articles. A short document that is complete and signed is worth more than a long one that nobody has agreed.

Valuation: the point of most disputes

Most exit disputes are really about price. Agree the method in advance: a fixed formula, an independent accountant acting as expert, or a figure agreed each year. State whether the price reflects the whole company or a pro rata share, whether discounts apply for a minority holding, and the date as at which value is measured. Say who pays the valuer. A method that both sides understand and accept at the start is far less likely to be challenged.

Paying for the buyout

A buyer may not have the cash. The agreement can allow payment in instalments, secured on the shares, or fund the purchase by the company buying back its own shares. See our guide on purchase of own shares for the conditions.

Before you start

- Is the shareholding equal or close to it?
- What is the escalation route?
- Who values the shares, and how?
- Is there insurance in place, and who owns it?
- Are the owners personally guaranteeing company debts?
- When were the arrangements last reviewed?

How MTM can help

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We draft deadlock and exit provisions for shareholders' agreements and articles, and cross-option agreements to match your client's insurance arrangements. We work through you or directly with the shareholders, and we leave tax advice and insurance selection to you and your clients' advisers.