

Research paper

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Investment Agreements



**Business Laws**

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## TRANSACTIONAL DOCUMENTS

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In simple language a transactional document is one which set-outs details of a proposed transaction, in our context an investment transaction such as purchase of equity or preference shares or subscribing to debentures and their conversion, if at all. All investment transactions are not identical. Sometimes the drafting of definitive documents begins before negotiation. Parties exchange the first draft of documents and then negotiate to resolve major outstanding issues. In other cases, parties begin to negotiate major issues even before the first draft is complete. They may either negotiate while the agreement is being drafted or commence drafting only after major issues have been resolved. Irrespective of the approach, a lawyer's job is to draft the best possible agreement to suit each party's need. Let us discuss the agreements that one will find most commonly in an investment transaction. Remember that since such transactions are of various types, this is not an exhaustive list but an informative one.

## SHARE PURCHASE AGREEMENT

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Let's assume Evaluator Private Limited ("**Evaluator**") has two shareholders, Prabhjit and Rahul. Prabhjit intends to sell its shares in Evaluator to Zinc Limited for a specified monetary consideration. This understanding between the parties will be recorded in a share purchase agreement ("**SPA**"), a legally binding agreement. This agreement is important as it contains all the terms and conditions relevant to the sale such as:

- (a) the exact description of the sale (including the number of shares, the names of the seller and the purchaser, and the consideration for the sale);
- (b) the conditions that must be satisfied before the sale takes place;
- (c) the date on which the sale will be completed;
- (d) the manner in which the transfer will be made;
- (e) any indemnities or protections available to the parties;
- (f) the representations and warranties made by either party; and
- (g) the conditions upon which the agreement will terminate.

The parties to a SPA are typically the seller, the purchaser, and the company whose shares are being sold. Often shareholders who may not be selling their shares may also be a party to the agreement if specific consents are required from them for the transfer to take place.

## SHARE SUBSCRIPTION AGREEMENT

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A new investor Arun wishes to invest in Evaluator, the company in the example above. However, instead of purchasing shares held by Prabhjit or Rahul, Evaluator will issue fresh shares to Arun. In other words, Arun will subscribe to fresh shares in Evaluator. This understanding is typically recorded in a share subscription agreement (“SSA”). A SSA is similar in nature to a SPA. The only difference is the subject matter of the agreement. A SPA is executed when there is a transfer of shares from a shareholder to an investor while a company executes a SSA in case of a fresh issue of shares. The parties to a SSA are typically the new investor and the company that is issuing fresh shares. The shareholders of that company are also parties to the SSA if certain consents are required from them before the transaction can be completed.

## SHARE HOLDER AGREEMENT

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A shareholders’ agreement is a contract that contains the rights and obligations of the shareholders in a company. Typically, this agreement supplements a SPA or a SSA. However, a shareholders agreement is not necessary in all cases. Let’s understand this better with the help of certain examples:

Assume Evaluator is purchasing 100% of the shares of ABC Limited. ABC Limited’s existing shareholders are transferring all their shares to Evaluator. After the share transfer, Evaluator will be the sole shareholder of ABC Limited. In this case there is no need for a shareholders agreement. This is because there will be only one shareholder after the transfer and that shareholder has full control over the company. Look at a slightly different scenario. Assume ABC Limited has two shareholders P and Q. P is selling all his shares to Evaluator. After the share transfer, Evaluator and Q will be the two shareholders in the company. In such a case, a shareholders agreement is

typically entered into to regulate the relationship between the shareholders. In other words, a shareholders agreement is usually entered into when a company has more than one shareholder. The parties to a shareholders agreement are typically the shareholders of the company and the company itself. This agreement contains the rights and obligations of each shareholder on various matters such as:

- (a) the manner in which shareholders can exit the company;
- (b) the procedure for transfer of shares (whether in whole or part);
- (c) the manner in which to wind up the company (in case of insolvency);
- (d) the manner in which to resolve a disagreement between the shareholders;
- (e) the manner in which the company will operate on a day-to-day basis and the rights of each shareholder regarding such operations; and
- (f) the composition of the board of directors.

The SPA (or the SSA) and the shareholders agreement are often combined into one document that contains all the details of the proposed investment transaction and the manner of operation of the company after a transaction has been completed.

Additionally, a joint venture agreement (“**JVA**”) is similar to a combined shareholders agreement and SPA or SSA. It is essentially an agreement that parties enter into when they wish to run the company as partners. JVAs are executed between parties who intend to set up a new joint venture company or invest in an existing company. More often than not, if the company in which the investment is being made already exists, that company is also a party to this agreement. This is done to ensure that the provisions of the agreement are binding on the company. The provisions of JVA are similar to that of a shareholders agreement and SPA or SSA.

Besides the above, there are other agreements that usually form an integral part of investment transactions. These include a non-disclosure agreement, employment agreements, indemnity bonds, agreements related to appointment of directors or advisors, employee stock option agreements and the like.

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**About the author:**

The author is a corporate lawyer empaneled with Evaluator. Views expressed are personal.