CLIENT NOTE

SHAREHOLDER AGREEMENTS UNDER ARMENIAN LAW

OVERVIEW

A shareholder agreement (in the United States those are often referred to as Stockholder Agreements) is a contract between a company's shareholders. It is generally agreed that shareholder agreements emerged in the United Kingdom in the mid-1800s. These instruments later spread into the other corners of the world, and they are widely used in other jurisdictions.

Often, shareholders privately enter into agreements and agree upon certain arrangements that regulate their "life together". These arrangements are usually not exposed to the customers, suppliers, or the employees of the company. What view does Armenian law have on Shareholder Agreements and how are those regulated? In this Client Note our firm's Managing Partner Varoujan Avedikian discusses how.

Although in most jurisdictions incorporated companies are viewed as distinctly standing legal entities operating mostly independent from their shareholders, yet the development of legal tradition, organic law, and in many instances case law has given shareholders the right to enter into agreements that usually privately regulate issue otherwise unregulated in the company's by-laws. Here in this client note, we will discuss how Armenian law views and regulates shareholder agreements.

DEVELOPMENT OF THE LAW

Armenian company law didn't mention shareholder agreements until 2019 until the Law on Joint Stock Companies was amended, and Article 38.1 "Shareholder Agreements" was added into the body of the law. Before this addition, some Armenian corporate lawyers believed that even without any language in the company law, shareholders of Armenian companies could still negotiate and execute shareholder agreements under the general principle of freedom to contract, but this is debatable, and to be on the safe side, many of these agreements were entered into foreign (mainly English law).

WHAT CAN BE INCLUDED

Under the dedicated article, by entering into a shareholder agreement, the shareholders can

1. Decide how to execute certain rights attached to their shares or abstain from exercising those rights;
2. Agree on voting in the Shareholders' Meeting as to format, process, and requirements or getting the consent of others (Interestingly the law does not use the words "other shareholders", but instead uses "others". Deductively, the consent may come from third-parties (explained below not from the Board of Directors and the management) on the vote;
3. Agree on voting per other's instructions (Again, no mention of other shareholders, but excluding the Board of Directors and the management as explained below);
4. Set the pricing mechanism of shares to be sold or bought in the future or upon the occurrence of certain predetermined events (although the clause does not specifically mention put and call options, the language suggest that those "share option" clauses may be added);
5. Agree on cases when a shareholder shall abstain from transferring the ownership of shares before certain events occur;
6. Agree on certain coordinated actions regarding the management, operations reorganization, and liquidation of the company (somewhat a "catch-all" phrase);
7. Decide upon modes of securing the obligations as well as liability measures for violations of the Shareholder Agreement.

There are several clauses widely included/regulated under Shareholder Agreements in many other jurisdictions, that have not been included in the language of article 38.1, such as "piggy-back" clauses, deadlock provisions, pre-emption rights, etc., but this is a separate topic to be discussed in another client note.

It should be noted that the shareholder agreement cannot change the number of votes required by the Joint Stock Company Law or the charter of the company to pass certain decisions in the Shareholders' Meeting. In addition, the Shareholders Agreement may not include clauses that oblige any of the parties to the agreement to vote under the instruction of the management or the Board of Directors of the Company.

FORMAT AND PARTIES

Obviously, the Shareholder Agreement should be in writing and is mandatory only for those who are a party to it. Thus, verbal arrangements are not enforceable. The shareholders, the company itself, and those who have subscribed to the shares of the company but have not yet become shareholders may be parties to a Shareholder Agreement. It should be further noted that the law mandates to comply with the "Transactions with Affiliated Parties" rules of the Joint Stock Company Law (another client note is brewing on this!) if and when the company itself is becoming a party to the Shareholder Agreement.

CONSEQUENCES OF VIOLATION

Article 38.1 of the law stipulates that the resolutions of the Shareholders' Meeting, Board of Directors, or the Executive may be annulled, in case such resolutions are adopted in violation of the Shareholders Agreement and respective fiduciary duties. This is the most obscure clause of the article, for several reasons.

First, both Armenian law and case law are not very explanatory on the notion of fiduciary duty (another English law doctrine that has "crawled" into the Armenian body of law without much application), therefore from a corporate litigation perspective, it may be unclear on what should be proven first: the existence and consequential violation of the fiduciary duty or the violation of the term(s) of the Shareholder Agreement.

Second, does a shareholder own a fiduciary duty toward the company when voting in a Shareholders' Meeting under Armenian law? Doubtful.

HOW CAN WE HELP?

Our team has extensive experience in helping both shareholders and companies agree upon Shareholder Agreement terms and put together a comprehensive deal. We have done so for a host of companies, both international and local. So please, do get in touch when you want to get sophisticated advice.

NOTE: This material is for general information only and is not intended to provide legal advice

Varoujan Avedikian, Managing Partner
vavedikian@tk.partners