



When Shareholders Revolt: Succession Planning and Disputes

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Family business succession is complicated, even at the best of times, but becomes even more challenging when stakeholders refuse to play nice. [Paul Denton](#) shares a cautionary tale on how picking the wrong buyer can have a negative ripple effect across the business and even your family.

Some mid-market or family businesses coming out of the pandemic face a host of factors that could morph into a perfect storm if not handled properly. Proceed with caution.

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When you combine the unstoppable wave of Baby Boomer retirement with the exits from an emotionally draining pandemic, these business owners may be motivated to accelerate an exit from their business.

In addition, you have a combination of factors influencing the current economic landscape including:

- curtailment of government pandemic relief



- looming interest rate hikes
- a talent reset wherein key management that were earmarked to be part of the transition and succession plan, have either left or are contemplating leaving
- more stringent requirements from lenders following accommodations made during the pandemic
- potentially a more active M&A market looking at increased transaction flow, including possibly targeting your business

Given the market dynamics profiled above, you need to ensure you have a succession plan in place to address transition objectives in a timely fashion—remembering first and foremost that you should always do what is best for the business and avoid the trap of internalizing the process.

You also need to ensure there's not a rush to cobble together a succession plan for the sake of it, but that the process is done with purpose and thoughtfulness. Especially if you're operating a family-run business—[where things can get even more complicated](#).

Based on decades of experience dealing with succession and contentious shareholder disputes, below is a cautionary tale for business owners—a highly litigious and protracted dispute culminating in a (forced) settlement. Avoiding litigation altogether is always the recommended route, but some instances require intervention by the courts. Let's dive in.

Shareholder Revolt

As a Court Appointed Receiver, B. Riley Farber has been involved in succession situations where family shareholders—those who controlled the business—determined that they wanted to sell a majority stake in their business, to a third party, while continuing in key management positions.

As part of a transaction, parties enter into a Share Purchase Agreement (“SPA”) and Shareholder Agreement, which are intended to manage the conduct of the parties once a transaction closes.

In this instance, the new majority shareholder exercised control and influence at the management and board level, they also took control of the financial management of the business—including control of the banking. While majority owners clearly have rights, its conduct soon ranged from aggressive, and not in the spirit of the deal, to being oppressive to the minority shareholders.

The relationship of the purchaser and minority shareholders soon became very strained and ultimately became litigious.

Grievances from the minority shareholders included that the majority stakeholder:

- unilaterally increased compensation to themselves
- engaged in unauthorized distributions (fees and transfers) to related parties
- oversaw lack of regular and transparent reporting
- levered the business up with debt and stretched accounts payable



- was non-compliant with regulatory returns including non-payment of government remittances (payroll, HST, EHT remittances)
- generated a slew of litigation claims where there had been virtually none previously

The impact of this conduct was to undermine the business on several fronts—including liquidity, customer service levels, impaired the goodwill with various stakeholder groups, and exposed the minority shareholders to a range of [director and officer liabilities](#).

Ultimately the parties were able to settle following extensive litigation, but the events took an emotional toll on the minority shareholder family. To avoid such situations, below are several factors you should consider if you are looking to exit your (family) business:

- consider, first and foremost, what's best for the business
- conduct due diligence to reveal the true intentions of the purchaser, beyond the negotiations stage
- assess the agreements through the lens of potential conflicts—what rights or leverage do you have as a minority shareholder if relations sour?
- maintain some leverage particularly if the payout is not all cash and there is a secured vendor take back note payable over a fixed term
- consider the ongoing cash flow implications if you sell a majority stake and retain a minority stake
- retain an advisor to help formulate an objective succession plan

Light at the end of the litigation tunnel

Once the smoke settled from rounds of intense litigation, the two sides begrudgingly settled. In these types of case, both sides tend to feel like they lost, with no one feeling happy or satisfied at the outcome. Rather, there's often a feeling of relief and finality.

If the sellers considered the factors discussed above, they could potentially have avoided the dispute altogether and found a buyer more aligned with their goals.

In the end, family business succession is complicated even at the best of times, but even more challenging when stakeholders refuse to play nice. When embroiled in a dispute, people tend to lose focus on what really matters and it's typically the business, family, or both that pays the ultimate price.

It is worth noting, that —with positive shareholder outcomes, where family members are aligned, and the business continues down a favourable path going forward. More on that in future piece.



How to Manage Shareholder Disputes

What are the repercussions if they aren't settled in a timely and orderly manner? [Learn more](#)

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