ABSTRACT

Shareholders’ Agreements are contractual devices to manage tensions among shareholders of a corporation. These agreements have a wide scope related to shareholders’ interest. Nevertheless, before subscribing a shareholder agreement is important to determine the requirements to make it enforceable. This issue has been addressed in the last twenty years by state corporate statutes following the Model Business Corporation Act and the Delaware General Corporation Law and in different court decisions. Today, shareholders’ agreements will be enforced according to the terms defined by the parties unless the agreement injures non-participating shareholders, third parties or is against public policy.

Key words: shareholders’ agreements, enforcement, close corporations, internal affairs doctrine, minority shareholders.
ACUERDO DE ACCIONISTAS EN SOCIEDADES CERRADAS Y SU IMPLEMENTACIÓN EN LOS ESTADOS UNIDOS DE AMÉRICA

RESUMEN

Los acuerdos de accionistas son mecanismos de tipo contractual que permiten resolver las tensiones que existen entre los accionistas de una sociedad. Estos acuerdos de naturaleza contractual tienen un amplio alcance relacionado con los diferentes intereses y necesidades de los socios. En todo caso, antes de suscribir un acuerdo de accionistas es muy importante determinar cuáles son los requerimientos que harán el mismo aplicable y ejecutable. Este tema ha sido considerado en los últimos 20 años por las regulaciones de los diferentes estados en los Estados Unidos de América tomando como base la Ley Tipo de Sociedades y la Ley de Sociedades del estado de Delaware. En la actualidad, los acuerdos de accionistas serán objeto de aplicación, de conformidad con los términos recogidos por las partes, a menos que el acuerdo afecte a los accionistas que no participen en el mismo, a terceras partes o el mismo resulte contrario al orden público. El presente artículo es un producto del proyecto Interpretación y Aplicación del Derecho Privado del grupo de investigación en derecho civil y comercial de la Facultad de Ciencias Jurídicas de la Pontificia Universidad Javeriana.

Palabras clave: acuerdos de accionistas, sociedad cerrada, accionistas minoritarios, implementación, aplicación.

INTRODUCTION

Closely held corporations are the most common corporate forms of organization\(^1\). Most of the enterprises in the United States are closely held corporations\(^2\). The close corporation category includes a whole variety of enterprises like family-owned business, high-tech start-ups, small firms and mature publicly held

\(^{1}\) Frank H. Easterbrook and Daniel R. Fischel, Close Corporations and Agency Costs, 39 Stan. L. Rev. 271, 271 (1986). The terms “close corporation” and “closely held corporation” will be considered to be synonymous and will be used interchangeably. See infra Chapter II Section B of this document for the concept of close corporation.

corporations, post-leveraged buyouts\textsuperscript{3}. Closely held corporations are corporations with concentrated ownership\textsuperscript{4}.

Shareholders of close corporations, either small, family-owned or big in assets and structure, ordinarily enter into different kinds of agreements to regulate the most important relations of the corporation\textsuperscript{5}. Shareholders’ agreements could include a whole variety of issues, like voting of shares for the election of directors, who are to be officers of the corporation, long-term employment for some of the participants in the agreement and salaries, a power to veto corporate decisions, circumstances to declare dividends and methods of resolving disputes, among others\textsuperscript{6}.

In the past, the norms in state statutes were established mostly to protect shareholders and investors in publicly held corporations where management and ownership are divided and the mechanisms established address this reality\textsuperscript{7}. At the same time, court decisions were uncertain and confusing about the validity and enforceability of shareholders’ agreements in the context of close corporations\textsuperscript{8}. Decisions were normally hostile to contracts which modified the classic structure of functions and roles among shareholders, directors and officers\textsuperscript{9}. This situation has changed in recent years.

Modern state statutes contain provisions regulating shareholders’ agreements validating their celebration and implementation\textsuperscript{10}. In addition, modern court decisions have shown a favorable view toward shareholders’ agreements, considering them enforceable and valid\textsuperscript{11}. Under this new trend, the legal system recognizes the existence of fundamental differences in structure, functions and necessities between publicly-held corporations and closely-held corporations\textsuperscript{12}.

\textsuperscript{4} Id.
\textsuperscript{5} Official Comment Model. Bus. Corp. Act § 7.32.
\textsuperscript{6} F. Hodge O’Neal and Robert B. Thompson, O’Neal and Thompson’s Close Corporations and LLCs: Law and Practice Volume 1 1-2 (West Third Revised Edition 2005) [Hereinafter, O’Neil and Thompson].
\textsuperscript{7} Id. at 5:2-5:24.
\textsuperscript{8} Id. at 5:103-104.
\textsuperscript{9} Id.
\textsuperscript{10} Official Comment Section 7.32 Model. Bus. Corp. Act. See Robert B. Thompson, The Law’s Limits on Contracts in a Corporation, 15 J. Corp. Law 377, 393-394 (commenting that “[i]n most states, modern corporation statutes now permit contracting around those statutory rules which previously mandated that centralized control rest with the board of directors. Most statutes now also recognize agreements to limit the transferability of shares or to authorize voting requirements for corporate action that differ from “majority rule” norms specified in the statute. In most states, these changes appear in the general corporations codes and are available to all corporations even though the impetus seems to have been to assist closely held corporations. Special status, now found in almost half the states and available only to certain statutorily defined close corporations, allows even greater freedom for parties to depart form statutory norms.”).
\textsuperscript{12} See Easterbrook and Fischel, supra note 1, at 271.
This document explores the requirements for enforcement of shareholders’ agreements in the context of the close corporation. Chapter II will present a basic approach to the internal affairs doctrine and the concept of close corporation. Chapter III will explain the nature and basic functions of shareholders’ agreements. Chapter IV will explain the classes of shareholders’ agreements and the issues which are normally covered in them. Chapter V will consider the evolution process for the enforcement of shareholders’ agreements, the statutory requirements for enforcement in the Model Business Corporation Act and the Delaware General Corporation Law and the issues which concern judges when enforcing these agreements.

AN APPROACH TO UNITED STATES CLOSE CORPORATIONS

A. Internal affairs doctrine

The American Corporate System is state-centered\(^{13}\). Every state offers a specific set of rules for the business interested in incorporation\(^{14}\). In this manner, corporate statutes could be viewed as state by-products and the private corporations as their consumers\(^{15}\). This system creates a competition among the states to get the companies and, consequently the fees and taxes which come with incorporation\(^{16}\).

The question to be answered is which state’s law is applied to the corporation. Two different subjects must be separated in this matter: the internal affairs of the corporation and the business of the corporation\(^{17}\). The internal affairs of the corporation refer to the relationship among the corporation and its current officers, directors, and shareholders\(^{18}\). The business of the corporation is considered the relationship among the corporation and its clients, creditors and workers\(^{19}\). For the scope of this document, the question will focus on the internal affairs issue.

The internal affairs of the corporation are covered by the Internal Affairs Doctrine\(^{20}\). Under this doctrine, courts look to the law of the state of incorporation in dealing with a corporation’s internal affairs\(^{21}\). Therefore, businessmen decide the rules for

\(^{13}\) ROBERTA ROMANO, Foundations of Corporate Law 84 (Foundation Press ed. 1993) [Hereinafter ROMANO].


\(^{15}\) ROMANO, supra note 13, at 82.

\(^{16}\) O’KELLEY and THOMPSON, supra note 14, at 140.

\(^{17}\) See FRANKLIN A. GEVURTZ, Corporation Law 35-36 (West Group ed. 2000) [Hereinafter GEVURTZ].

\(^{18}\) Id.

\(^{19}\) Id.


internal affairs by choosing the state of incorporation. At the same time, this doctrine guarantees that other states will recognize corporations incorporated in another state and that their courts will apply the law of the state of incorporation in matters of internal affairs.

The United States Supreme Court stated in Edgar v. MITE Corp, the usefulness of this doctrine as follows: “The internal affairs doctrine is a conflict of laws principle which recognize that only one State should have the authority to regulate a corporation’s internal affairs … because otherwise a corporation could be faced with conflicting demands…”

In this context, this document will consider mainly two statutes in the United States: The Model Business Corporation Act [Hereinafter MBCA] and the Delaware General Corporation Law [Hereinafter D.G.C.L.]. The MBCA was developed by the American Bar Association Section of Business Law, Committee on Corporate Law; most states based their rules on this statute. On the other hand, the D.G.C.L. has become the preeminent American corporate law jurisdiction, playing a dominant role in the United States corporations system.

B. Concept of close corporation

The concept of ‘close corporation’ seems difficult to reduce to an all-purpose description. In fact, it is possible to find a variety of definitions describing what it is. The scope of the concept will depend on the statute of the state, the court

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22 O’KELLEY and THOMPSON, supra note 14, at 140.
23 Id.
25 See O’KELLEY and THOMPSON, supra note 14, at 141. See also Committee of Corporate Laws, ABA Section of Business, Managing Closely Held Corporations, A Legal Guidebook, Preface vii (2003). (commenting that “[t]he Model Act serves as the primary basis for the corporation statutes in approximately half of the states, and many of its provisions have been adopted in almost all of the other states.”).
26 O’KELLEY and THOMPSON, supra note 14, at 141 (commenting that “[d]ifferences among the states are not as great as they once were. Successful Delaware innovations are quickly copied by the MBCA, and vice versa. In addition, there is substantial uniformity in the so-called common law of corporations. Courts in one state may borrow freely from the jurisprudence developed by courts in other states. Delaware, as the home of so many publicly traded corporations, again played a dominant role. Delaware courts are frequently called on to decide major questions of corporate law and have developed a large body of judicial rules and precedent on major corporate law issues, and courts in other jurisdictions routinely cite their decisions. Indeed, Delaware case law frames much of the debate about the structure of corporate law.”).
28 See O’NEIL and THOMPSON, supra note 6, at 1-2.
29 See Del. Code Ann., Title 8 § 342(a) (2005) (“(a) A close corporation is a corporation organized under this chapter whose certificate of incorporation contains the provisions required by §102 of this title and, in addition, provides that: (1) All of the corporation’s issue stock of all classes, exclusive of treasury shares, shall be represented by certificates and shall be held of record by not more than a specified number of persons, not exceeding 30; and (2) All if the issued stock of all classes shall be subjected to 1 or more of the restrictions on transfer permitted by §202 of this title; and (3) The corporation shall make not offering
which has decided the case\textsuperscript{30} or the author’s opinion\textsuperscript{31}. Nevertheless, the definition of a ‘close corporation’ normally includes three different aspects of the structure of a corporation\textsuperscript{32}.

The first aspect is related to an objective feature of shareholders. The objective characteristic is the number of shareholders\textsuperscript{33}. Normally, a small number of shareholders are the owners of the complete stock in close corporations\textsuperscript{34}. The D.G.C.L. and the MBCA include a limit in the number of shareholders for a corporation to be considered ‘close’\textsuperscript{35}. This feature is a consequence of the fact that participants in close corporations normally are familiar or have other personal relations in addition to the business relationship\textsuperscript{36}.

The second aspect is related to a feature of the shares. In the case of a close corporation, there is a lack of an organized market for the trade of the shares\textsuperscript{37}.

\textsuperscript{30} See United States v. Byrum, 408 U.S. 125, 149 N.34 (1972) (describing that the typical close corporation “is small, has a checkered earning record, and has nor market for its shares.”). See also Donahue v. Rodd Electrotype Co., 367 Mass. 578, 586, 328 N.E. 2d. 505, 511 (1975) (“We deem a close corporation to be typified by: (1) a small number of stockholders; (2) no ready market of the corporate stock; and (3) substantial majority stockholder participation in the management, direction and operation of the corporation.”).

\textsuperscript{31} See Melvin Aron Eisenberg, Contractual Freedom in Corporate Law: Articles & Comments: The Structure of Corporate Law, 89 Colum. L. Rev. 1461, 1461 (1989) (describing a close corporation as a “corporations that have a small number of shareholders, most of whom either participate in or directly monitor corporate management.”) See also O’Neil and Thompson, supra note 6, at 1-2 (describing that “close corporation is a corporation whose shares are not generally traded in the securities market.”). See also Committee of Corporate Laws, supra 27, at 3 (“A closely held corporation is most commonly defined as a corporation that has a relatively small number of shareholders and no active trading market for its securities”). See also Israels, supra note 29, at 488 (describing that “[t]he “close corporation” is an enterprise in corporate form in which management and ownership are substantially identical.”).


\textsuperscript{33} See O’Neil and Thompson, supra note 6, at 1-5.


\textsuperscript{35} See O’Kelley and Thompson, supra note 14, at 141.

\textsuperscript{36} Easterbrook and Fischel, supra note 1, at 271. See Douglas K. Moll, Shareholder Oppression in Close Corporations: The Unanswered Question of Perspective, 53 Vand. L. Rev. 749, 757 (2000) (explaining that “close corporation investors are often linked by family of other personal relationships that result in a familiarity between the participants.”).

\textsuperscript{37} Easterbrook and Fischel, supra note 1, at 271. See Millar, supra note 36, at 383 (commenting that “[i]n contrast to the stock of the public corporation, the stock of a private company has no ready market. Each owner is dependent on the other to buy out the ownership interest in the event of a dispute.”).
The free transferability of shares common to public corporations is not present in close corporations\(^{38}\). In close corporations, there is a restriction in the ability of investors to alienate their shares\(^{39}\). Shareholders control the transfer of shares in a way that unwanted interested investors cannot participate in the company\(^{40}\).

The third aspect considers the relation between shareholders and directors concerning ownership and management. In close corporations exists a close identity between shareholders and managers, which contrast radically with public corporations wherein ownership and control are clearly separated\(^{41}\). The close identity comes from the fact that the same people both manage and bear the risk of investment\(^{42}\). Shareholders, directors and officers of the corporation are normally the same individuals\(^{43}\). Under these circumstances, it could be very common to find in close corporations that earnings of the corporation are distributed among the shareholders not as dividends but as a salary\(^{44}\).

For the purpose of this document, close corporations are those whose stock is not publicly traded.

**NATURE AND FUNCTIONS OF SHAREHOLDERS’ AGREEMENTS**

**A. Nature of shareholders’ agreements: a contractual device**

A corporation from the economic perspective has been described as a “firm”\(^{45}\). Corporations are for-profit-seeking enterprises composed by persons and assets and organized by rules\(^{46}\). The rules could be determined by i) law, ii) contracts or other forms or agreements, iii) corporate organs and officials and, iv) market

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41 Peeples, *supra* note 38, at 466.
42 Easterbrook and Fischel, *supra* note 1, at 274.
43 Millar, *supra* note 34, at 383.
45 See O’Kelley and Thompson, *supra* note 14, at 1 (describing the concept of a firm from an economic perspective: “The “firm” is what we call the set of relations that arise when resources are allocated by the entrepreneur via commands to her employees rather than the set of relations that arise when an entrepreneur allocates resources via contract with outsiders. Thus, depicted as a circle, and using Mary, the classic owner/entrepreneur as an example, the Coasean firm includes Mary and her employees, but excludes the customers, suppliers, and creditors with whom Mary does business.”).
46 Eisenberg, *supra* note 31, at 1461.
Shareholders’ agreements are part of the rules determined by “contracts or other forms of agreements”.

A shareholder agreement is a contract. The object of this contract is to define the scope and extent of the relationships among the shareholders and between the shareholders and the corporation. The extent of the object of the contract will depend on flexibility of the legislation and public policy constraints on the participants.

Additionally, from a contractual approach, the close corporation is gaps. Existing rules do not have an answer to all the different contingencies that the corporation will face in the future. In this context, shareholders’ agreements pretend to avoid in advance some of the most important problems for a close corporation using a before-the-fact perspective. Shareholders’ agreements give flexibility to the participants in the corporation, bearing in mind the fact that the problems in close corporations are quite different from those in public corporations.

Also, legislation has provided in recent years flexibility for the participant in business. The legislation has transformed from less prescriptive rules to more enabling rules. In this manner, shareholders can reach almost any kind of agreement. Shareholders have a wide road to define the terms of their relationship and avoid other mechanisms that come into play.

B. Functions of shareholders’ agreements: a way to solve tensions among shareholders

The central problem in the corporate governance structure of close corporations is how to find the most reasonable degree of adaptability and protection from

47 Id.
49 Id.
51 Id.
52 Gevurtz, supra note 17, at 481.
54 Easterbrook and Fischel, supra note 1, at 279-80.
55 Id.
56 Id.
57 O’Kelley, supra note 50, at 216 (commenting that “[a]s a result, these gaps must be filled ex-post, as a need to adapt actually occurs. Normally, gaps are filled by shareholders themselves acting by consensus. If consensus is not possible, then the close corporation contract’s gap-filling process will come in to play.”).
the opportunism of either the majority or minority shareholders\(^\text{58}\). At the same time, shareholders in close corporations require flexibility for their business and personal interests\(^\text{59}\). Shareholders’ agreements are the most successful device to mitigate the application and effect of traditional corporate rules in the context of close corporations\(^\text{60}\). Besides, shareholders’ agreements could be a very helpful instrument in the environment of international commercial transactions and corporations with shareholders in different nations\(^\text{61}\).

1. PROTECTION FOR MINORITY SHAREHOLDERS IN CLOSE CORPORATIONS

A close corporation is the perfect environment for majority opportunism\(^\text{62}\). Majority opportunism is possible if the following aspects are combined together in a close corporation\(^\text{63}\): i) application of the majority rule\(^\text{64}\); ii) separation of functions among shareholders, directors and officers; iii) lack of guaranteed employment or dividend rights for shareholders; and iv) impossibility to apply the unilateral dissolution mechanism.

In a close corporation, the traditional norms of corporate governance structure plus the lack of a public market for shares\(^\text{65}\) leave the minority shareholder vulnerable to the majority.\(^\text{66}\) Under the majority rule, the relationship between majority-minority shareholders might finish in what is called a “freeze out/squeeze-out”\(^\text{67}\). In a freeze out/squeeze out, a majority shareholder uses his/her control over

\(^{58}\) O’Kelley and Thompson, supra note 14, at 383. See Millar, supra note 34, at 383-384 (explaining that “[s]hareholder disputes present one of the most difficult and potentially destructive problems which arise in the context of the close corporation. A U.S. study conducted in Chicago, Illinois revealed that shareholder dissension was a major cause of business failures for the close corporation. Shareholder disputes are responsible for a wide a variety of business problems including loss of management time and increased cost.”).

\(^{59}\) Siedel, supra note 2, at 384.

\(^{60}\) Hornstein, supra note 53, at 1041.

\(^{61}\) Millar, supra note 34, at 417 (commenting that “[p]articularly for the international investor, well-drafted contractual shareholder arrangements can be critical in governing the shareholder relationship. Contractually agreed upon choice of law provisions, buyout provisions, provisions permitting minority veto power in certain circumstances, employment contracts, and other special agreements which provide for dividend payments or other matters are extremely helpful in reducing potential shareholder disputes. Thus, provide for dividend payments or other matters are extremely helpful in reducing potential shareholder disputes. Thus, contractual arrangements should be encouraged in the case of corporations owned by shareholders of different nations.”).

\(^{62}\) O’Kelley and Thompson, supra note 14, at 383.

\(^{63}\) Id.

\(^{64}\) See Millar, supra note 34, at 386 (explaining that “[t]he doctrine of majority rule creates the possibility for majority shareholders to make decisions which further their own interest at the expense of the minority owners.”).

\(^{65}\) Id. at 385 (suggesting that the main reason for close corporation problems is the no existence of a market mechanism and the fact that each shareholder is dependent on the other shareholders either to buy or sell their shares when exists irreconcilable positions.).

\(^{66}\) O’Kelley and Thompson, supra note 14 at 382.

\(^{67}\) Gevurtz, supra note 17, at 450.
the corporation against a minority shareholder in a way that the latter could not participate in the management and earnings of the corporation.  

Therefore, a shareholder agreement may be a key instrument to protect minority shareholders from the majority. The agreement’s primary goal is to give the minority shareholder participation in the management of the corporation or a more important role in the decision-making process. In this case, the majority is willing to share some of its control in order to encourage people who, under normal circumstances, would not buy a minority interest.

2. BALANCE AMONG SHAREHOLDERS WITH SIMILAR POWER AND INTERESTS

In a close corporation, two or more not controlling shareholders could constitute a majority whose primary objective is to assure that the parties in the agreement will make decisions concerning the corporation together. In fact, no shareholder has majority over the other shareholders by him/herself. The corporation has a control group composed of a small number of shareholders instead of a controlling shareholder. In this case, the existence of equilibrium among shareholders is a feature of the business agreement.

Shareholders want to maintain the control of the corporation regardless of the changes in the future. At the same time, shareholders in a close corporation expect to have employment, role management and return on their investment. In addition,
most of the shareholders in a close corporation have their wealth invested in the corporation. Therefore, the decisions made by the corporation could affect each shareholder significantly.

In this context, shareholders will implement specific devices to protect their investment. A very useful solution for shareholders is to have in advance a contractual device, applicable when it is needed to solve differences among shareholders. The contractual device solution could work really well in the closed corporation environment because there is a small number of shareholders in the negotiation process.

**CLASSES AND ISSUES COVERED BY SHAREHOLDERS’ AGREEMENTS**

The issues normally covered by shareholders’ agreements are related to those which regulate shareholder actions and those which control director functions.

**A. Shareholders’ agreements concerning shareholder decisions**

The agreements which regulate shareholder actions cover issues agreed in advance among the participants as to how to act in the exercise of their rights as shareholders. In the group of shareholder actions we find those called “shareholding” or “pooling agreement”, [this is a simple contract providing that the shareholders will vote their shares as a unit in the election of directors and other matters] proxy agreement, [this is a contract that creates irrevocable proxies which take away the shareholders’ power to vote their shares and vest that power in one or more of the shareholders or in other persons] and voting trust [this is a contract which transfers legal title of the share to trustees, who vote the shares in accordance with the terms of the trust instrument].

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76 Chooper et al., supra note 44, at 711. Thompson, supra note 10, at 394 (explaining that “[u]nlike shareholders in public corporations who develop diversified portfolios to eliminate the risk of some losses, shareholders in a close corporation often do not or cannot develop a diversified portfolio, thus exposing them to increased risk of loss because of their limited holdings. A participant in a close corporation is more likely to have a firm-specific investment in the enterprise, thereby increasing the risk that other participants may act opportunistically to appropriate for themselves the quasi-rents of these specialized assets.”).

77 See Id.

78 See Id.


80 Thompson, supra note 10, at 393.

81 O’Neil and Thompson, supra note 6, at 5:2, 5:6.

82 O’Kelley and Thompson, supra note 14, at 401.

83 Gevurtz, supra note 17, at 486.

84 Id.

85 Chooper et al., supra note 46, at 736 (according to the authors voting trust came in to existence for two main
B. Shareholders’ agreements concerning director decisions

The agreements concerning directors’ functions are about management of the corporation. Management in a close corporation usually depends on shareholders’ will. The concept of an independent board of directors separated from the shareholders is a fiction that does not apply in the close corporation context. Therefore, shareholders celebrate agreements to adapt the traditional corporate rules according to their needs. The new rules determine who is to have control of the corporation and how that control is to be exercised.

The aspects included in these agreements could determine many different issues which normally are functions of the board of directors. Many agreements contain provisions like: i) designating corporate officers and determining their compensation and tenure; ii) undertakings by shareholders assuring permanent employment by corporation; iii) agreements providing veto arrangements; iv) reasons: (1) “Designed in response to the judicial aversion to the separation of ownership from control, it results in the trustees having legal title to the shares, as well as the right to vote in the manner agreed on”; and (2) “Existing creditors or senior security holders of a financially unstable corporation may require, as a condition of permitting the corporation to continue (or be reorganized), that they be given control through the mechanism of a voting trust. Lenders or providers of fresh capital may utilize a voting trust to afford them control of or a voice in the selection of new management or assurance that the corporation’s present successful management will be continued.”.

LAVALLE, supra note 48, at 109.
87 O’NEIL and THOMPSON, supra note 6, at 5:25.
88 LAVALLE, supra note 48, at 109.
89 Id. See O’NEIL and THOMPSON, supra note 6, at 5:25.
90 See MODEL BUS. CORP. ACT § 7.32 (a)(3) (2005) (providing that “(a) An agreement among the shareholders or a corporation that complies with this section in effective among the shareholders and the corporation even though it is inconsistent with one or more other provisions of this Act in that it: (3) establishes who shall be directors or officers of the corporation, or their terms of office or manner of selection removal;”). See DEL. CODE ANN. tit 8 § 354 (2005) (providing that “[n]o written agreement among stockholders of a close corporation, nor any provision of the certificate of incorporation or of the bylaws of the corporation, which agreement or provision relates to any phase of the affairs of such corporation, including but not limited to the management of its business or declaration and payment of dividends or other division of profits or the election of directors or officers or the employment of stockholders by the corporation or the arbitration of disputes, shall be invalid on the ground that it is an attempt by the parties to the agreement or by the stockholders of the corporation to treat the corporation as if it were a partnership or to arrange relations among the stockholders or between the stockholders and the corporation in a manner that would be appropriate only among partners.”). See O’NEIL and THOMPSON, supra note 6, at 5:114 (commenting that “[m]any agreements among shareholders in close corporations contain provisions naming the persons who are to occupy some or all corporate offices or granting one or more of the contracting parties the privilege of naming corporate officers.”).
91 O’NEIL and THOMPSON, supra note 6, at 5:127 (commenting that “[c]losely related to provisions in shareholders’ agreements naming persons to corporate offices are undertakings by shareholders guaranteeing one or more individuals permanent employment for a long or indefinite period or time.”). See MODEL BUS CORP ACT § 7.32 (a)(4) (2005) (providing that “(a) An agreement among the shareholders or a corporation that complies with this section in effective among the shareholders and the corporation even though it is inconsistent with one or more other provisions of this Act in that it: (4) governs, in general or in regard to specific matters, the exercise or division of voting power by or between the shareholders and directors or by or among any of them, including use of weighted voting rights or director proxies;”).
agreements controlling dividend policy or providing for distribution of corporate assets or profits (agreements could include a prohibition of declaring dividends for a limited period of time or under specific circumstances, a shareholder veto power to declare dividends, a provision which provides that not dividends could be declared until the corporation pay a loan); 93 v) inclusion of arbitration clauses for settling a dispute among shareholders; 94 vi) agreements governing dissolution, buyouts and other remedies for deadlock; 95 vii) agreements about transfer restrictions among the shareholders and the corporation; 96 and viii) any other issue dealing with the relationship among shareholders or which governs the exercise of corporate powers and is not contrary to public policy 97.

93 See Model Bus. Corp. Act § 7.32 (a)(2) (2005) (providing that “[a]n agreement among the shareholders or a corporation that complies with this section is effective among the shareholders and the corporation even though it is inconsistent with one or more other provisions of this Act in that it: (2) governs the authorization or making of distributions whether or not in proportion to ownership of shares, subject to the limitation in section 6.40.”). See Del. Code Ann. tit 8 § 354 (2005). See O’Neil and Thompson, supra note 6, at 5:133 (commenting that “[p]articipants in a close corporation occasionally attempt to control its dividend policy by agreement among themselves.”).

94 See Del. Code Ann. tit 8 §354 (2005). See O’Neil and Thompson, supra note 6, at 5:138 (commenting that “[a]rbitration is one of the least expensive and least disruptive ways of settling a dispute among shareholders, and shareholders’ agreements often contain a clause providing for the arbitration of disputes arising out of the agreement.”).

95 See Model Bus. Corp. Act § 7.32 (a)(6)(7) (2005) (providing that “[a]n agreement among the shareholders or a corporation that complies with this section is effective among the shareholders and the corporation even though it is inconsistent with one or more other provisions of this Act in that it: (6) transfer to one or more shareholders or other persons all or part of the authority to exercise the corporate powers or to manage the business and affairs or the corporation, including the resolution of any issue about which there exists a deadlock among directors or shareholders; (7) requires dissolution of the corporation at the request of one or more of the shareholders or upon the occurrence of a specified event.”). See O’Neil and Thompson, supra note 6, at 5:138 (commenting that “[s]hareholders in a close corporation may enter into a contract for the dissolution of the corporation in the event of a deadlock among its shareholders and directors, or on the happening of specified contingencies perhaps different form those which otherwise would justify dissolution under the statutes. Similarly, they may contract for on or more shareholders to buy out others rights in the event of deadlock or other stated contingencies.”).


97 See Model Bus. Corp. Act § 7.32 (2005) (providing that “[a]n agreement among the shareholders or a corporation that complies with this section is effective among the shareholders and the corporation even though it is inconsistent with one or more other provisions of this Act in that it: (8) otherwise governs the exercise or the corporate powers of the management of the business and affairs of the corporation or the relationship among the shareholders, the directors and the corporation, or among any of them, and it not contrary to public policy.”). See Del. Code Ann. tit 8 § 354 (2005).
ENFORCEMENT OF SHAREHOLDERS’ AGREEMENTS

A. Enforcement of shareholders’ agreements concerning shareholder decisions

1. EVOLUTION

In the U.S. courts, the enforcement of shareholders’ agreements concerning issues normally in the power of shareholders has been an object of discussion\(^98\). Most of the initial decisions of courts considered voting agreements invalid\(^99\). The main two reasons for invalidating the agreements were i) the idea that the power to vote was treated as inseparable from the shares and ii) the idea that shareholders owe to the each other a duty to vote in the corporation meetings in the best interest of the corporation\(^100\).

Today, the trend toward the validity and enforcement of shareholders’ agreements concerning shareholder issues has a most positive perspective in courts\(^101\). The enactment of statutes expressly authorizing this kind of agreement has been the best way to avoid discussion about the validity of shareholders’ agreements concerning

\(^{98}\) O’NEIL and THOMPSON, supra note 6, at 5:11.
\(^{99}\) Id.
\(^{100}\) Id. at 5:12-13.
\(^{101}\) Id. at 5:15.
shareholder decisions\textsuperscript{102}. The MBCA and D.G.C.L. provide specific rules for the enforcement of pooling agreements,\textsuperscript{103} proxy agreements,\textsuperscript{104} and voting trust\textsuperscript{105}.

\textsuperscript{102} \textit{Id.} at 5:17.

\textsuperscript{103} \textit{See Model Bus. Corp. Act} § 7.31 (2005). It provides that:

"(a) Two or more shareholders may provide for the manner in which they will vote their shares by signing an agreement for that purpose. A voting agreement created under this section is not subject to the provisions of section 7.30.

(b) A voting agreement created under this section is specifically enforceable".

\textit{See Del. Code Ann. tit 8 §2 18 (c) (2005)}. It provides that:

"(c) An agreement between 2 or more stockholders, if in writing and signed by the parties thereto, may provide that in exercising any voting rights, the shares held by them shall be voted as provided by the agreement, or as the parties may agree, or as determined in accordance with a procedure agreed upon them".

\textsuperscript{104} \textit{See Model Bus. Corp. Act} § 7.22 (a)(b)(d) (2005). It provides that:

"(a) A shareholder may vote his shares in person or by proxy.

(b) A shareholder or his agent or attorney-in-fact may appoint a proxy to vote or otherwise act for the shareholder by signing an appointment form, or by an electronic transmission. An electronic transmission must contain or be accompanied by information from which one can determine that the shareholder, the shareholder’s agent, or the shareholder’s attorney-in-fact authorized the electronic transmission.

(d) An appointment of a proxy is revocable unless the appointment form or electronic transmission states that it is irrevocable and the appointment is coupled with an interest. Appointments coupled with an interest include the appointment of:

(4) a pledge;

(5) a person who purchased or agreed to purchase the shares;

(6) a creditor of the corporation who extended it credit under terms requiring the appointment;

(7) an employee of the corporation whose employment contract requires the appointment; or

(8) a party to a voting agreement created under section 7.31”.

\textit{See Del. Code Ann. tit 8 § 212 (c)}.

\textsuperscript{105} \textit{See Model Bus. Corp. Act} § 7.30. It provides that:

(a) One or more shareholders may create a voting trust, conferring on a trustee the right to vote or otherwise the act for them, by signing an agreement setting out the provisions of the trust (which may include anything consistent with its purpose) and transferring their shares to the trustee. When a voting trust agreement is signed, the trustee shall prepare a list of the names and address of all owners of beneficial interest in the trust, together with the number and class of shares each transfer to the trust, and deliver copies of the list and agreement to the corporation’s principal office.

(b) A voting trust becomes effective on the date the first shares subject to the trust are registered in the trustee’s name. A voting trust is valid for no more than ten years after its effective date unless extended under subsection (c).

(c) All or some of the parties to a voting trust may extend it for additional terms of not more than ten years each by signing written consent to the extension. An extension is valid for 10 years form the date the first shareholder signs the extension agreement. The voting trustee must deliver copies of the extension agreement and list of beneficial owners to the corporation’s principal office. An extension agreement binds only those parties signing it”.

\textit{See Del. Code Ann. tit 8 § 218}.
2. STATUTORY REQUIREMENTS FOR ENFORCEMENT

i) Pooling agreements

Pooling agreements are contracts in which shareholders agree to vote their shares in a specific manner. Pooling agreements could include a variety of issues relating to shareholders’ needs. Normally, pooling agreements include: i) agreement to vote shares for directors; ii) agreement giving voting power disproportionate to shareholdings; or iii) agreement to vote shares so as to effectuate a particular corporate policy. Pooling agreements regulating these issues have been considered lawful and enforceable. Nevertheless, courts have invalidated agreements when a shareholder sells his vote or compromises voting power under considerations of some personal benefit.

The statutory requirements for pooling agreements in the MBCA and DGCL are: i) Two or more shareholders must participate in the agreement (shareholders part of the agreement could be a minority, a majority or all of them, the requirement is quantitative and not qualitative); ii) the agreement must be in writing; and iii) the agreement must be signed by all the participating shareholders.

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106 GEVURTZ, supra note 17, at 486.
107 O’NEIL and THOMPSON, supra note 6, at 5:45-5:63.
108 See MANSON v. CURTIS, 223 N.Y. 313, 319, 119 N.E. 559 (1918) (providing that: “[a]n ordinary agreement, among a minority number, but a majority in shares, for the purpose of obtaining control of the corporation by the election of particular persons as directors is not illegal. Shareholders have the right to combine their interest and voting powers to secure such control of the corporation and the adoption of and adhesion by it to a specific policy and course of business. Agreement upon a sufficient consideration upon them, of such intent and effect, are valid and binding, if they do not contravene any express charter or statutory provision or contemplate any fraud, oppression, or wrong against other stockholders, or other illegal object.”).
109 See HALL v. JOHN S. ISAACS & SONS FARMS, INC. 37 Del. Ch. 530, 549, 146 A.2d 602, 613 (1958), aff’d in part, 39 Del. Ch. 244, 163 A.2d 288 (1960) (“The rule which forbids the voting of purchased votes is not limited to instances where the consideration for the purchase is strictly a corporate office and its emoluments. Shareholder votes may not be purchased for any consideration personal to the stockholder.”). See RESTATEMENT (SECOND) OF CONTRACTS §193 (1981) (providing that “[a] promise by a fiduciary to violate his fiduciary duty or promise that tends to induce such a violation is unenforceable on ground of public policy.” The comments to this Section establish: “The rule applies by analogy to shareholders with reference to their voting powers, although it does not preclude agreements where the only advantage bargained for is one that will accrue to all shareholders through the ownership of shares.”).
110 See MODEL BUS. CORP. ACT § 7.31 (a) (2005) (requiring the participation of “[t]wo or more shareholders” in voting agreements). See DEL. CODE ANN. tit 8 § 218 (c) (2005) (providing that a voting agreements is “[a]n agreement between 2 or more stockholders”).
111 See Official Comment Section 7.31 (a) MODEL BUS. CORP. ACT (2005) (providing that “[t]he only formal requirements are that they [voting agreements] be in writing and signed by all the participating stockholders”). See DEL. CODE ANN. tit 8 § 218 (c) (2005) (providing that “if in writing and signed by the parties thereto” the voting agreements may regulate the exercise of voting rights among stockholders).
112 See MODEL BUS. CORP. ACT § 7.31 (a) (2005) (providing that it is necessary to sign “an agreement for that purpose [way to vote their shares]”). See DEL. CODE ANN. tit 8 § 218 (c) (2005) (providing that “if in writing and signed by the parties thereto” the voting agreements may regulate the exercise of voting rights among stockholders).
ii) Proxy agreements

Under the proxy agreement, the pooling or voting agreement goes one step further\(^\text{113}\). Besides the existence of an agreement covering how the shareholders are suppose to vote certain matters, shareholders create irrevocable proxies which vest the power to vote their shares in one or more persons, who could be either shareholders or other persons\(^\text{114}\). The reason for the further step is a way to secure that the shares will be voted according to the terms of the agreement without delays and uncertainties\(^\text{115}\).

Historically, the idea of an irrevocable proxy has been questioned\(^\text{116}\). However, statutes have established the requirements for an irrevocable proxy to be enforceable\(^\text{117}\). The requirements solve clearly many of the questions used in the past to challenge irrevocable proxies\(^\text{118}\). The statutory requirements are: i) the proxy must be in writing;\(^\text{119}\) ii) the proxy must be signed or must contained information from which it can be determined that the writing document was authorized by the shareholder;\(^\text{120}\) iii) the proxy will have a time limit, unless it provides for a longer period;\(^\text{121}\) iv) the proxy is irrevocable if it states that it is irrevocable and it is coupled

\(^{113}\) O’NEIL and THOMPSON, supra note 6, at 5:8-9.

\(^{114}\) Id.

\(^{115}\) Id at 5:64-65 (commenting that “[a] proxy may be advantageous in a voting agreement to facilitate the carrying out of the agreement and to avoid the possibility that a suit for specific performance, with the attendant uncertainties and delays, will be necessary to implement decisions reached under the agreement”).

\(^{116}\) Id. (commenting that the different attacks on the idea of an irrevocable proxy are: “(1) the right to vote is an essential attribute of stock, and consequently the owner cannot irrevocably detach it form the shares; irrevocable proxies are void as against public policy in that they unreasonably restrict the free alienability of the shares by preventing the purchaser form exercising one of the essential rights of stock ownership, namely, the right to vote the shares; (3) some agreements utilizing irrevocable proxies are indistinguishable in affect from voting trust and should be invalided if they do not comply with the requirements of the voting trust statute; (4) a proxy, being an agency, is revocable unless coupled with an interest, and that is so even though it is stated to be irrevocable; and (5) an irrevocable proxy violates a statutory limitation on the duration of proxies or a statutory rule providing that all proxies shall be revocable.”).

\(^{117}\) See supra note 104.

\(^{118}\) Id. at 5:75-78.

\(^{119}\) See MODEL BUS. CORP. ACT § 7.22 (b) (2005) (providing that a shareholder “may appoint a proxy to vote or otherwise act for the shareholder by signing an appointment form or by an electronic transmission”. DEL. CODE ANN. tit 8 § 212 (c)(2) (providing that “[a] stockholder may authorize another person or persons to act for such stockholder as proxy by transmitting or authorizing the transmission of a telegram, cablegram, or other means of electronic transmission to the person who will be the holder of the proxy”).

\(^{120}\) See MODEL BUS. CORP. ACT § 7.22 (b) (2005) (providing that shareholders “may appoint a proxy to vote or otherwise act for the shareholder by signing an appointment form or by an electronic transmission. An electronic transmission must contain or be accompanied by information from which one can determine that the shareholder, the shareholder’s agent, or the shareholder’s attorney-in-fact authorized the electronic transmission.”). See DEL. CODE ANN. tit 8 § 212 (c)(2) (2005) (providing that there must be “information form which can be determined that the telegram, cablegram or other electronic transmission was authorized by the stockholder.”).

\(^{121}\) See MODEL BUS. CORP. ACT Section 7.22 (c) (2005) (providing that “[a]n appointment is valid for 11 months unless a longer period is expressly provided in the appointment.”). See DEL. CODE ANN. tit 8 § 212 (b) (2005). (providing that “no such proxy shall be voted or acted upon after 3 years from its date, unless the
with an interest; and v) the writing document or the electronic transmission is received by the corporation.

**iii) Voting trust**

Under this method, shareholders transfer their shares to trustees, who vote the shares in accordance with the terms of the agreement. Therefore, the trustee becomes the legal owner of the shares but usually the former shareholder retains economic benefits of the shares. Generally, the trustee gives to the former shareholder “voting trust certificates” as evidence of the economic benefit of the shares. Provisions in a voting trust could regulate any material and procedural issues concerning shareholders’ decisions.

The statutory requirements for voting trust agreements in the MBCA and D.G.C.L. are: i) One or two or more shareholders must participate in the agreement (there is not a quantitative requirement for shareholders to enter in a voting trusts, [e.g. one, two, all] the only requirement is qualitative: being a shareholder of the corporation); ii) the agreement must be in writing; iii) the agreement must be a proxy for a longer period.

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122 See Model Bus. Corp. Act § 7.22 (d) (2005) (providing that “[a]n appointment of a proxy is revocable unless the appointment form or electronic transmission states that it is irrevocable and the appointment is coupled with an interest. Appointment coupled with an interest includes the appointment of: (5) a party of a voting agreement created under section 7.31”). See Del. Code Ann. tit 8 § 212 (e) (2005) (providing that “[a] duly executed proxy shall be irrevocable if it states that it is irrevocable and if, and only as long as, it is coupled with an interest sufficient in law to support an irrevocable power. A proxy may be made irrevocable regardless of whether the interest with which it is coupled is an interest in the stock itself or an interest in the corporation generally.”).

123 See Model Bus. Corp. Act § 7.22 (c) (2005) (providing that “[a]n appointment of a proxy is effective when a signed appointment form or an electronic transmission of the appointment is received by the inspector or election or the officer or agent of the corporation authorized to tabulate votes.”). See Del. Code Ann. tit 8 § 212 (c)(2) (2005) (providing that “[i]f is determined that such telegrams, cablegrams or other electronic transmissions are valid, the inspectors or, if the are no inspectors, such other persons making that determination shall specify the information upon which they relied.”).

124 Gevurtz, supra note 17, at 492.

125 Id. (explaining that “[s]ince the trustee receives their title in trust to act for the benefit, typically, of the former shareholder, the former shareholders give up legal title but retain beneficial ownership. This means that the trustees normally forward to the former shareholders any dividends received form the corporation, and transfer the stock back to the former owners upon termination of the trust.”).

126 O’Neil and Thompson, supra note 6, at 5:78-79.

127 Id. at 5:80-81 (mentioning matters ordinarily cover in a voting trust: how trustees are to be selected and how vacancies among the trustees are to be filled, whether trustees can be removed, the responsibility and liability of the trustees for their actions, circumstances in which the trust can be amended or terminated, if trustees may elect themselves as directors or officers of the corporation, if the voting rights are limited to some decisions or if they include fundamental corporate changes, etc).


129 The Model Business Corporation Act does not explicitly state that the agreement must be in writing but the requirement could be clearly understood from the context of the following provision: “One or more
signed, iv) the transfer of the shares to the trustee or trustees by the shareholder; v) the voting trust have a statutory time limit under the MBCA and a contractual time limit under D.G.C.L. This is an important difference between the two statutory rules; and vi) the corporation must be informed of the voting trust agreement but the two statutory models have different rules for this process.

The MBCA requires the trustee to prepare a list and “deliver copies of the list and agreement to the corporation principal office”. In addition, this statute states that the voting trust “becomes effective on the date the first shares subject to the trust are registered in the trustee’s name”. On the other hand, the D.G.C.L. requires the filling of a “copy of the agreement in the registered office of the corporation” and the copy shall be available to the inspection of any stockholder of the corporation.

Finally, the MBCA and the D.G.C.L. establish clearly that the requirements of the voting trust are not applicable to other kinds of agreements which could exist without interference of the special rules for voting trust. The reason for this...
provision is related to judicial decisions which in the past left some uncertainties about the validity of shareholders’ voting agreements different from voting trust agreements.\footnote{O’Neil and Thompson, supra note 6, at 5:95-96.}

B. Enforcement of shareholders’ agreements concerning director decisions

1. EVOLUTION

Historically, shareholders’ agreements concerning director decisions were held invalid by courts.\footnote{Model Bus. Corp. Act § 7.22 Official Comment (2005).} The arguments to invalidate shareholders’ agreements were:\footnote{O’Neil and Thompson, supra note 6, at 5:22}

i) shareholders’ agreements violate a statute (an article or a section), in this case for instance, the fact that directors shall manage the affairs of the corporation;

ii) the fiduciary duties of directors to exercise their best judgment for the benefit of the corporation and the shareholders as a whole may be disregarded by the agreement; and

iii) the agreement is unfair and fraudulent to shareholders who do not participate in it.

On different occasions, courts held that shareholders’ agreements were void if they regulated the management and operation of the corporation in a way different from what had been established by the corporation statute.\footnote{See Id. 5:2, 5:23.} The concept behind these holdings was that incorporation and limited liability were special features given by the state.\footnote{See Id. 143} Therefore, if shareholders wanted to enjoy these privileges, the condition was to follow strictly the traditional roles of corporation management and operation.\footnote{See Id. 145}

A good example of courts unfavorable view of shareholders’ agreements is the case McQuade v. Stoneham.\footnote{McQuade v. Stoneham, 263 N.Y. 323, 189 N.E. 324 (1934).} In this case, Defendant Charles Stoneham, the majority shareholder of the National Exhibition Company, also called the Baseball Club (New York Nationals or “Giants”) sold minority stock interest in the company to defendant John J. McGraw and to plaintiff Francis X. McQuade.\footnote{McQuade v. Stoneham, 263 N.Y. at 325-26, 189 N.E. at 235.} The corporation’s business was the New York Giants baseball team and McGraw was the team’s manager.\footnote{McQuade v. Stoneham, 263 N.Y. at 326, 189 N.E. at 235.} As part of the transaction, Stoneham, McGraw and McQuade entered into a shareholder agreement in which they agreed that they would use their best endeavors for the
purpose of continuing as directors and officers of the corporation, decided what their salaries would be, and decided that not changes in corporate structure or policy would occur without their unanimous consent. Nine years later, Stoneham and McGraw breached the agreement. The board of directors controlled by Stoneham discharged McQuade as an officer and later on he was not reelected as Director. McQuade was dropped from his post because he antagonized the dominant Stoneham, not for misconduct.

McQuade sued Stoneham and McGrew for breach of the shareholder agreement. The New York Court of Appeals ruled for defendants Charles

149 See McQuade v. Stoneham, 263 N.Y. at 326, 189 N.E. at 235. The shareholder agreement provided that:

“VIII. The parties hereto will use their best endeavors for the purpose of continuing as directors of said Company and as officers thereof the following:

Directors:
Charles A. Stoneham,
John J. McGraw,
Francis X. McQuade,

with the right to the party of the first part [Stoneham] to name all additional directors as he sees fit:

Officers:
Charles A. Stoneham, President
John J. McGraw, Vice-President
Francis X. McQuade, Treasurer.”

150 See McQuade v. Stoneham, 263 N.Y. at 326, 189 N.E. at 235. The shareholder agreement provided that:

“IX. No salaries are to be paid to any of the above officers or directors, except as follows:

President $45.000
Vice-President 7,500
Treasurer 7,500”

151 See McQuade v. Stoneham, 263 N.Y. at 326-27, 189 N.E. at 235. The shareholder agreement provided that:

“X. There shall be no change in said salaries, no change in the amount of capital, or the number of shares, nor change or amendment of the by-laws of the corporation or any matter regarding the policy of the business of the corporation or any matters which may in anywise affect, endanger or interfere with the rights of minority stockholders, excepting upon the mutual and unanimous consent of all of the parties hereto.”

152 McQuade v. Stoneham, 263 N.Y. at 327, 189 N.E. at 235.

153 See McQuade v. Stoneham, 263 N.Y. at 326-27, 189 N.E. at 235 (“The board of directors consisted of seven men. The four outside of the parties hereto [Stoneham, McGraw and McQuade] were selected by Stoneham and he had complete control over them. At the meeting of May 2, 1928, Stoneham and McGraw refrained from voting, McQuade voted for himself and the other four voted for Bondy. Defendants did not keep their agreement with McQuade to use their best efforts to continue him as treasurer. On the contrary, he was dropped with their entire acquiescence. At the next stockholders’ meeting he was dropped as a director although they might have elected him.”).

154 McQuade v. Stoneham, 263 N.Y. at 327-28, 189 N.E. at 236 (“The cause for dropping McQuade was due to the falling out of friends. McQuade and Stoneham had disagreed. The trial court has found in substance that their numerous quarrels and disputes did not affect the orderly and efficient administration of the business of the corporation; that plaintiff was removed because he had antagonized the dominant Stoneham by persisting in challenging his power over the corporate treasury and for no misconduct on his part. The court also finds that plaintiff was removed by Stoneham for protecting the corporation and its minority stockholders.”).

155 McQuade v. Stoneham, 263 N.Y. at 325, 189 N.E. at 235.
Stoneham and John J. McGraw. The court concluded that it was possible to celebrate an agreement among shareholders as to determine who would be directors of the corporation. But the court concluded that an agreement which contractually restricted the director's discretion and precluded them from acting in the best interest of the corporation and all shareholders was against public policy. A shareholder agreement which sterilized the board of directors of a corporation was not enforceable.

In recent years courts have shown a favorable trend in the enforcement of shareholders' agreements in close corporations concerning control over management. This trend recognized the differences between publicly-held business and closely-held corporations. A good example of courts favorable view of shareholders' agreements is the case Zion v. Kurtz.

In this case, Zion and Kurtz were the two shareholders of a Delaware Corporation called Lombard-Wall Group, Inc. As part of the transaction in which Zion's bought a minority interest in Lombard-Wall Group ("Group"), the two shareholders entered into a shareholder agreement providing that the corporation would not engage in any business or activities without Zion's consent. Despite this agreement, Kurtz...
engaged the corporation in certain activities without Zion’s consent. Zion then sought declaratory and injunctive relief against Kurtz.

The shareholder agreement provided that it should be governed and enforced in accordance with the laws of the State of Delaware. Delaware legislation allowed agreements in which shareholders of close corporations manage the business and affairs of the corporation, rather than the board of directors. Nevertheless, the Delaware statute required the articles of incorporation to reflect the agreement about management by shareholders. In the present case, the articles of incorporation did not reflect the existence of the shareholder agreement celebrated between Zion and Kurtz.

The Court stated that the articles of incorporation could be reformed to include provisions restricting directors’ authority. At the same time, the court stated that the defendant (Kurtz) had the responsibility to file the statutory documents, so the lack of fulfillment of formal requirements could not be taken as a reason to not enforce the agreement. Most importantly, the conclusion of the court stated

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164 Zion v. Kurtz, 50 N.Y.2d at 98, 405 N.E.2d at 683, 428 N.Y.S.2d at 201 (“Notwithstanding that provision, Group and Lombard some eight months thereafter, at the suggestion of Group’s account, entered into an agreement which made the previously non interest bearing loan form Lombard to Group bear interest provided interest could be paid out of earnings, and an escrow agreement with Chase Manhattan Bank pursuant to which Group deposited $580,000 in bonds to secure payment of the note. The two agreements were authorized by Group’s board over Zion’s objection.”).
165 Zion v. Kurtz, 50 N.Y.2d at 99, 405 N.E.2d at 683, 428 N.Y.S.2d at 202. Zion v. Kurtz, 50 N.Y.2d at 100, 405 N.E.2d at 684, 428 N.Y.S.2d at 203 (“The stockholders’ agreement expressly provided that it should be “governed by and construed and enforced in accordance with the laws of the State of Delaware as to matter governed by the General Corporation Law of the State”).
170 Zion v. Kurtz, 50 N.Y.2d at 101, 405 N.E.2d at 685, 428 N.Y.S.2d at 203 (“Defendants argue, however, that Group was not incorporated as a close corporation and the stockholders’ agreement provision was never incorporated in its certificate. The answer is that any Delaware corporation can elect to become a close corporation by filing an appropriate certificate of amendment (Del General Corporation Law, §344) and by such amendment approved by the holders of all of its outstanding stock may include its certificate provision restricting director’s authority.”)
171 Zion v. Kurtz, 50 N.Y.2d at 101-02, 405 N.E.2d at 685, 428 N.Y.S.2d at 203-04 (“Here, not only did defendant Kurtz agree in paragraph 8.05(b) of the stockholders’ agreement to “without further consideration, do, execute and deliver, or cause to be done, executed and delivered, all such further acts, things and instruments as may reasonably required more effectively to evidence and give effect to the provisions and the intent and purposes of this Agreement”, but also as a part of the transaction by which the Half Moon guarantee was made and Zion became a Group stockholder, defendant Kurtz, while he was still the sole stockholder and sole director of Group, executed a consent to the various parts of the transaction under which he was “authorized and empowered to execute and deliver, or cause to be executed and delivered, all such other and further instruments and documents and take, or cause to be taken, all such other and further action as he
that the shareholder agreement between Zion and Kurtz was enforceable. The court considered the following reasons to support its decision: \(^{172}\) i) there were not intervening rights of third parties; ii) the agreement was not prohibited by statute, in other words, this kind of agreement was permitted; and iii) the notice device could not be applied to protect a party (Kurtz) who agreed in advance to this limitation in the decision-making process of the corporation.

Today, the pattern is that shareholders’ agreements could modify the traditional rules of corporate control in the corporation \(^{173}\). Courts are aware of the reality of close corporations as a different structure from publicly held corporations \(^{174}\). This reality has been reinforced by special legislation enacted exclusively to close corporations \(^{175}\).

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\(^{172}\) Zion v. Kurtz, 50 N. Y.2d at 102, 405 N.E.2d at 685, 428 N.Y.S.2d at 204.

\(^{173}\) O’Neil and Thompson, supra note 6, at 5:18-19.

\(^{174}\) Id. at 5:2, 5:24.

\(^{175}\) See Model Bus Corp Act § 7.32. (a) (2005). It provides that:

“(a) An agreement among the shareholders or a corporation that complies with this section in effective among the shareholders and the corporation even though it is inconsistent with one or more other provisions of this Act in that it:

1. eliminates the board of directors or restricts the discretion or powers of the board of directors;
2. governs the authorization or making of distributions whether or not in proportion to ownership of shares, subject to the limitation in section 6.40;
3. establishes who shall be directors or officers of the corporation, or their terms of office or manner of selection removal;
4. governs, in general or in regard to specific matters, the exercise or division of voting power by or between the shareholders and directors or by or among any of them, including use of weighted voting rights or director proxies;
5. establishes the terms and conditions of any agreement for the transfer or use of property or the provision of services between the corporation and any shareholder, director, officer or employee of the corporation among any of them;
6. transfer to one or more shareholders or other persons all or part of the authority to exercise the corporate powers or to manage the business and affairs or the corporation, including the resolution of any issue about which there exists a deadlock among directors or shareholders;
7. requires dissolution of the corporation at the request of one or more of the shareholders or upon the occurrence of a specified event;
8. otherwise governs the exercise or the corporate powers of the management of the business and affairs of the corporation or the relationship among the shareholders, the directors and the corporation, or among any of them, and it not contrary to public policy”.

See Del. Code Ann. tit 8 §350-351. Section 350 [Agreements Restricting Discretion of Directors] provides:

“A written agreement among the stockholders of a close corporation holding a majority of the outstanding stock entitled to vote, whether solely among themselves or with a party not a stockholder, is not invalid, as between the parties to the agreement, on the ground that it so relates to the conduct of the business and affairs of the corporation as to restrict of interfere with the discretion or power of the board of directors. The effect of any such agreement shall be to relieve the directors and impose upon the stockholders who

2. STATUTORY REQUIREMENTS FOR ENFORCEMENT

i) Model Business Corporation Act

Section 7.32 of the MBCA added in 1991 answer many of the challenges to the validity of shareholders’ agreements.176 The requirements for a shareholder agreement to be enforceable under the MBCA are:

- The agreement shall be set forth in the articles of incorporation,177 or in the bylaws,178 or in a written agreement signed by the shareholders; 179
- The agreement must be in writing and be approved or agreed to by all the shareholders of the corporation at the moment the agreement is close;180

are parties to the agreement the liability for managerial acts or omissions which is imposed on directors to the extent and so long as the discretion or powers or the board in its management of corporate affairs is controlled by such agreement.”).

Section 351 [Management by Stockholders] provides:

“The certificate of incorporation of a close corporation may provide that the business of a close corporation shall be managed by the stockholders of the corporation rather than by a board of directors. So long as this provision continues in effect:

1. No meeting of stockholders need be called to elect directors;
2. Unless the context clearly requires otherwise, the stockholders of the corporation shall be deemed to be directors for purposes of applying provisions of this chapter; and
3. The stockholders of the corporation shall be subject to all liabilities of directors”.

176 O’NEIL and THOMPSON, supra note 6, at 5:38.
177 Black’s Law Dictionary 120 (8th edition 2004) describes the articles of incorporation as “[a] governing document that sets forth the basic terms of a corporation’s existence, including the the number and clases of shares and the purposes and duration of the corporation”. See COMMITTEE OF CORPORATE LAWS, ABA SECTION OF BUSINESS, supra note 27, at 1-2 (providing that “[i]n addition to being the “birth certificate” of the corporation the articles of incorporation also served as a basic public record of legally required information about the corporation. Corporation statutes typically require that the articles of incorporation contain, at a minimum: (1) the corporate name, (2) the name of the corporation’s agent for service of process and its registered office in the state of incorporation, (3) the type and amount of authorized capital stock of the corporation and (4) the name and address of the incorporator (the person who caused the articles to be filled). In addition to required information, the articles are also the place in which the corporation may opt in or opt out of very important elective provisions under the governing corporate state, (…) In addition, corporate statutes permit inclusion of practically any other provisions desired in the articles of incorporation. Typically, however, participants in closely held corporations prefer to keep the content of the articles sparse because the articles are available to the public and because provisions in the articles generally require a shareholder vote to change. The articles of incorporation or certificate of incorporation are sometimes referred to as the “charter” of the corporation.”.

178 COMMITTEE OF CORPORATE LAWS, ABA SECTION OF BUSINESS, supra note 25, at 2 (providing that “[t]he bylaws are a set of more detailed rules of corporate governance that are required by most corporation statutes. Corporate bylaws usually lay out rules for shareholder and board meetings (e.g. when, where, who can call, notice, quorum and voting requirements), officer titles and duties, indemnification of directors and officers and other important matters. Unlike the articles of incorporation, the bylaws are not required to be filed with the state government and are a private document typically kept in the minute book. The bylaws may generally be amended by action of either the board or the shareholders.”).

179 See MODEL BUS CORP ACT § 7.32 (b) (1) (2005).
180 See Official Comment Section 7.32 (b) MODEL BUS CORP ACT (2005) (commenting that “[t]he principal requirements are simply that the agreement be in writing and be approved or agreed to by all persons who are then shareholders. Although a writing signed by all the shareholders is not required where the
The agreement must be unanimous;\textsuperscript{181} 

The agreement shall be known by the corporation;\textsuperscript{182} 

The liability for the acts or omissions imposed by law on directors shall be imposed upon the person or persons in whom the powers of the board of directors are invested, and the directors will be relieve of their responsibilities to the extent that the discretion of powers are limited by the agreement;\textsuperscript{183} 

The corporation must not become a publicly-held corporation;\textsuperscript{184} and 

The agreement will be valid for 10 years, unless other period of time is set in the agreement\textsuperscript{185}.

\textbf{ii) Delaware General Corporation Law}

The D.G.C.L. 8 §350, §351 and §354 regulate shareholders’ agreements and the requirements to be enforceable\textsuperscript{186}. The requirements for a shareholder agreement to be enforceable under the D.G.C.L. are:

- The agreement shall be set forth in the certificate of incorporation\textsuperscript{187} if the purpose is to establish direct shareholder management of the corporation rather than by directors,\textsuperscript{188} or a written agreement signed by the different shareholders. Similarly, while transferees are bound by a valid shareholder agreement, it may be desirable to obtain the affirmative written assent of the transferee at the time of the transfer."

\textsuperscript{181} See Official Comment Section 7.32 (b) MODEL BUS CORP ACT (2005) (commenting that “[s]ection 7.32 (b) requires unanimous shareholder approval regardless of entitlement to vote. Unanimity is required because an agreement authorized by section 7.32 can effect material organic changes in the corporation’s operation and structure, and in the rights and obligations of shareholders.”).

\textsuperscript{182} See Official Comment Section 7.32 (b) MODEL BUS CORP ACT (2005) (commenting that “[t]he requirement that the shareholder agreement be made known to the corporation is the predicate for the requirement in subsection (c) that the share certificates or information statements be legended to note the existence of the agreement. No specific form of notification is required and the agreement need not be filed with the corporation. In the case of shareholder agreements outside the articles or bylaws, the requirements of signatures by all of the shareholders will in virtually all case be sufficient to constitute notification of the corporation, as one or more signatories will normally also be a director or an officer.”).

\textsuperscript{183} See MODEL BUS CORP ACT § 7.32 (e) (2005) (providing that “[a]n agreement authorized by this section that limits the discretion or powers or the board of directors shall relieve the directors of, and impose upon the person or persons in whom such discretion or powers are vested, liability for acts or omissions imposed by law on directors to the extent that the discretion or powers or the directors are limited by the agreement”).

\textsuperscript{184} See MODEL BUS CORP ACT § 7.32 (d) (2005) (providing that “[a]n agreement authorized by this section shall cease to be effective when shares of the corporation are listed on a national securities exchange or regularly traded in a market maintained by one or more members of a national or affiliated securities association.”).

\textsuperscript{185} See MODEL BUS CORP ACT § 7.32 (b) (3) (2005) (providing that “[b] An agreement authorized by this section shall be: (3) valid for 10 years, unless the agreement provides otherwise.”).

\textsuperscript{186} The Delaware statute refers initially to corporations which are incorporated as close corporations according to Title 8 Section 342. Nevertheless, shareholders’ agreements will be enforced even if firms are not incorporated as close corporations. In practice, the concept of close corporation will not be limited to the formal requirement of incorporation but to those whose stock is not publicly traded. See supra note 161-172.

\textsuperscript{187} The articles of incorporation are known as a certificate of incorporation under Delaware law.

\textsuperscript{188} See Del. Code Ann. tit 8 § 351 (providing that “[t]he certificate of incorporation of a close corporation may
parties participating in the agreement if the purpose of the agreement is to restrict discretion of directors; 189

- The agreement must be unanimous if the purpose is to establish direct shareholder management of the corporation, 190 or must be approved by a majority of the outstanding stock entitled to vote if the purpose of the agreement is to restrict discretion of directors, 191
- The agreement shall relieve directors and impose upon the stockholders parties of the agreement the liability for managerial acts or omissions, 192 and
- The corporation must be a close corporation 193.

C. Issues that still worry judges about enforcement of shareholders’ agreements

The common law has followed the trend included in statutes about respecting and enforcing the agreements reached between the participants in a close corporation 194. The reasoning is that if the statutes provide room to depart from traditional standards of management, the state policy is permissive in departing from the traditional model 195. Shareholders’ agreements should be valid and enforceable, so long as these agreements do not affect other shareholders, creditors, or the public 196. In this context, the roles of unanimity, third parties interest and public policy have become very important to control the enforcement of shareholders’ agreements 197.

189 See Del. Code Ann. tit 8 § 350 (providing that “[a] written agreement among the stockholders of a close corporation” is the instrument for agreements restricting directors decisions.).
191 See Del. Code Ann. tit 8 § 350 (providing that “[a] written agreement among the stockholders of a close corporation holding a majority of the outstanding stock entitled to vote, whether solely among themselves or with a party not a stockholder, is not invalid, as between the parties to the agreement, on the ground that it so relates to the conduct of the business and affairs of the corporation as to restrict or interfere with the discretion or powers of the board of directors.”).
192 See Del. Code Ann. tit 8 § 350 (providing that “[t]he effect of any such agreement shall be to relieve the directors and impose upon the stockholders who are parties to the agreement the liability for managerial acts or omissions which is imposed on directors to the extent and so long as the discretion or powers of the board in its management of corporate affairs is controlled by such agreement.”).
194 Easterbrook and Fischel, supra note 1, at 281.
195 O’Neil and Thompson, supra note 6, at 5:30.
196 Hornstein, supra note 53, at 1056.
197 See O’Neil and Thompson, supra note 6, at 5:39-44 (suggesting that if the shareholder agreement is not authorized expressly by statute, “the following factors are considerer to decide its validity:

1. The purpose and objective of the agreement; courts have clearly left behind the time when they held shareholders’ agreements invalid per se, without regard to their purpose and effect;
2. The conceptions of public policy prevailing in the particular jurisdiction regarding the separation of voting power from beneficial ownership of the shares and the extent to which shareholders can interfere
1. THE ROLE OF UNANIMITY

In shareholders’ agreements, the importance of unanimity is related to the issue of judicial scrutiny. For those shareholders’ agreements which do not require unanimity, enforcement will require greater judicial scrutiny. In contrast, shareholders’ agreements which require unanimity will initially have a more positive approach from the judge. The idea behind this difference of treatment is the possibility of prejudice to nonparticipating shareholders and the interest of the corporation.

The considerations in support of unanimity are: i) all shareholders should decide about the corporation and their assets; ii) the possibility of injury for minority shareholders is reduced if all shareholders participate in the agreement; and iii) shareholders’ agreements can affect the structure and operation of the corporation and shareholders’ obligations and rights. Nevertheless, even unanimous

with discretion in managing a corporation;

3. Whether all of the shareholders in the corporation are parties to the agreement; if all shareholders are not parties to the agreement, a factor considered important by courts is whether the agreement will have a detrimental effect on nonconsenting shareholders;

4. Whether the contracting shareholders are directors or expect to be directors at the time of the performance of the contract. Some early decisions permitted shareholders to enter into agreements which purported to affect management decisions (e.g., to designate the corporation’s officers), but refused to enforce those agreements if the shareholders were also directors or were likely to become directors, because such an agreement was thought to deprive directors of their supposed independence. That shareholders executing an agreement are also directors does not appear to be a significant facto in modern decision;

5. The length of time during which the agreement is to remain in effect. Some statutes, such as most of those voting trusts, establish a maximum time limit; the duration of an agreement may be a factor in determining its validity if the statute covering that type of agreement is silent about time;

6. Whether the party challenging the validity of an agreement is a party to the agreement or is a corporate creditor or a shareholder not party to the agreement. Some courts that permit departures from the traditional corporate management norm by agreements executed all shareholders might required adherence to the norm whenever necessary to protect creditors or shareholders not parties to the agreement;

7. Whether the person challenging the agreements is simply trying to “welch” on his undertaking;

8. Whether consideration other than the mutual promises of the parties supports the parties’ undertaking to act in accordance with the terms of the agreement. A few judicial decisions refused to apply shareholders’ agreements the rule of contracts law generally that mutual promises of the parties to a contract are sufficient consideration for each other, but this notion does not appear to have gained wide acceptance;

9. How long the contract has been in operation and the extent to which action has been taken or positions have been changed in reliance on it.”

198 Easterbrook and Fischel, supra note 1, at 283.
199 Id.
200 Id. See Thompson, supra note 10, at 394 (commenting that “[j]udicial decisions and legal commentary reflect widespread support for unanimous agreements in close corporations.”).
201 Easterbrook and Fischel, supra note 1, at 283.
202 O’Neil and Thompson, supra note 6, at 5:151.
203 Id. at 5:152.
204 Official Comment Section 7.32 Model Bus Corp Act.
shareholders’ agreements will not be enforceable if the provisions are against creditors or public policy.\textsuperscript{205}

If shareholders’ agreements are not unanimous, courts will place a particular interest in the negative effects of non-participating shareholders.\textsuperscript{206} Besides, depending on the court position, even “potential” risks to non-participating shareholders could be a sufficient reason to strike down shareholders’ agreements.

2. THE ROLE OF THIRD PARTIES

Third parties could be creditors, the state and all others who are not part of the agreement but have some kind of interest in the corporation’s development. The private ordering recognized that shareholders’ agreements will be limited in consideration of the effects on third parties.\textsuperscript{207} Nevertheless, the effects of shareholders’ agreements on third parties are difficult to predict in the long-run and the effects cannot be determined completely by an \textit{ex ante} mechanism.\textsuperscript{208} In this manner, the limit will be placed in those cases where any part of the agreement injures third party rights.\textsuperscript{209} Depending on the court position, a judge could focus principally on the effects flowing from the contract or upon its purpose (even if the agreement harmed no one),\textsuperscript{210} when determining the enforceability of shareholders’ agreements.

\textsuperscript{205} \textsc{O’Neil} and \textsc{Thompson}, supra note 6, at 5:152 (commenting a New York decision that provide that: “the complete owners of a corporation may, by agreement among themselves, control the exercise of power and discretion by the directors of the corporation, provided that the interest of creditors of the corporation are not prejudiced and the public policy of the State is not offended.”).

\textsuperscript{206} \textsc{O’Neil} and \textsc{Thompson}, supra note 6, at 5:39-5:44.

\textsuperscript{207} \textsc{EastErbrook} and \textsc{Fischel}, supra note 1, at 279-80. \textsc{See} \textsc{Thompson}, supra note 10, at 394 (commenting that “[a] view of law that defines law as only a standard form contract or a supplement to private ordering fails to provide for those situations when legal rule blocks private ordering by providing a mandatory rule. Effects on this parties, a common cause for limiting private ordering in other fields of law, has some influence in corporate law but does not exhaust the reasons for legal intrusion into private ordering.”).

\textsuperscript{208} \textsc{Id}.

\textsuperscript{209} \textsc{See id}.

\textsuperscript{210} \textsc{O’Neil} and \textsc{Thompson}, supra note 6, at 5:158 (commenting that “[s]ome courts, in passing the validity of a voting agreement, focus principally on the effects flowing from the contract, and make little inquiry into its purpose.”).

\textsuperscript{211} \textsc{O’Neil} and \textsc{Thompson}, supra note 6, at 5:159 (commenting that “some courts...unfortunately have sometimes invalidated shareholders’ agreements, even though they harmed no one, because the agreements supposedly deviated from a broad statutory norm or conflicted with some nebulous public policy.”).

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3. **THE ROLE OF PUBLIC POLICY**

A transaction is to be enforced according to the terms negotiated by the parties. The enforcement principle is based on the fact that fully informed parties are the best judges of their own utility or interests in the bargain. Therefore, agreements are valid unless they go against the interests of society. The rule is that contracts will not be enforced if they go against public policy.

In this manner, the mandatory rule prevails over the private ordering. Classical examples are when the legal system will not enforce bargains based on theft, fraud or duress. Initially, the sources of public policy will be found in constitutions, statutes, regulations and ordinances of a specific jurisdiction. In this case, the explicit rules facilitate the job of courts by clearly pointing out which agreements are not enforceable. But in practice, courts are one of the most important sources of public policy.

In fact, courts find and declare the public policy of the jurisdiction. Courts judge contracts according to the time and place of a specific jurisdiction. In this context, the concept of public policy is very sensitive to the passage of time.

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212 Black’s law dictionary 1245 (7th edition 1999) describes public policy as “principles and standards regarded by the legislature or by the courts as being of fundamental concern to the state and the whole society. Courts sometimes use the term to justify their decisions, as when declaring a contract void because it is “contrary to public policy”. See Grace McLane Giesel, Corbin on Contracts, Contracts Contrary to Public Policy Vol. 15, 1 (Matthew Bender & Co., Inc., Revised Ed. 2003) (commenting that “one court has stated that “public policy” is an easily defined concept. The concept embodies the common sense and common conscience of the community. Public policy is that principle of law under which ‘freedom of contract … is restricted by law or good of the community.”).

213 *Eisenberg*, supra note 31, at 1462.

214 *Id.*

215 O’Neil and Thompson supra note 6, at 5:29.

216 *Giesel*, supra note 212, at 1.

217 *Id.* at 1-2 (commenting that “[t]his is a clear limitation [public policy] on the freedom of contract because, regardless of the parties’ intention to be bound or manifestations of that intent, the courts have refused to give such contracts the full enforcement to which they would otherwise be entitled.”).

218 Thompson, supra note 10, at 394 (commenting that “[a]part from any third party effects, there are times when a legal rule is mandatory because the law does not trust the bargaining process. For example, American law prevents bargains base on theft, embezzlement, fraud, or duress. In part, these rules are based on prevailing views of morality.”).

219 *Giesel*, supra note 212, at 5-6.

220 *Id.* at 6.

221 *Id.* at 9 (commenting that “a court may determine a public policy and may determine that a particular contract contradicts that policy by simply evaluating the prevailing practices and notions of the community as to what is in the interest of general welfare of the society.”).

222 *Id.*

223 *Id.* at 1.

224 *Id.*
Nevertheless, courts are conscious of the problems of abuse when using the rule of public policy\textsuperscript{225}.

The Restatement (Second) of Contracts suggests a specific process when evaluating the conflict between public policy and private ordering\textsuperscript{226}. The Restatement considers that an agreement should not be enforced only if the interest in its enforcement is clearly outweighed by the interest in not enforcing the contract\textsuperscript{227}.

The Restatement suggests different issues that should be analyzed when weighing public policy against the enforcement of a contract\textsuperscript{228}: i) the parties’ justified expectations; ii) the forfeiture that would result from non enforcement; iii) any public interest in enforcing the provision; iv) the strength of the policy against enforcement; v) the likelihood that a refusal to enforce the contract will further the policy; vi) the seriousness and deliberateness of the misconduct; and vii) the closeness of connection between the misconduct and the provision. In different decisions, courts have considered this factor-balancing analysis in the Restatement (Second) of Contracts\textsuperscript{229}.

\textbf{CONCLUSION}

Modern state statutes and court decisions support the validity and enforcement of shareholders’ agreements. In the past, these statutes and decisions have answered

\begin{footnotesize}
\textsuperscript{225} \textit{Patton v. United States}, 281 U.S. 276, 306; 50 S. Ct. 253, 264; 74 L. Ed. 854 (1930). The court provided that: “The truth is that the theory of public policy embodies a doctrine of vague and variable quality, and unless deductible in the given circumstances from constitutional or statutory provisions, should be accepted as the basis of judicial determination, if at all, only with the utmost circumspection.” Black’s law dictionary 1245 (7th edition 1999) concept of public policy (commenting “[t]he policy of law, or public policy, is a phrase of common use in estimating validity of contracts. Its history is obscure; it is most likely that agreements which tended to restrain trade or to promote litigation were the first to elicit the principle that the courts would look to the interest of the public in living efficacy contracts. Wagers, while they continued to be legal, were a frequent provocative of judicial ingenuity on this point, as is sufficiently shown by the case of Gilbert v. Sykes X16 East 150 (1812)X….: but it does not seem probable that the doctrine of public policy began in the endeavor to elude their binding force. Whatever may have been its origin, it was applied very frequently, and not always with the happiest results, during the alter part of the eighteen and nineteenth century. Modern decisions, however, while maintaining the duty of the courts to consider the public advantage, have tended more and more to limit the sphere within which this duty may be exercised.”). Giesel, supra note 212, at 18 (commenting that “courts generally have acted cautiously in declaring a contract contrary to public policy.”).

\textsuperscript{226} \textit{Restatement (Second) of Contracts} § 178 (1981).

\textsuperscript{227} \textit{Restatement (Second) of Contracts} § 178 (1981).

\textsuperscript{228} \textit{Restatement (Second) of Contracts} § 178 (1981).

\textsuperscript{229} Giesel, supra note 212, at 19 (citing a court decision as follows: “U.S. Cain v. Darby Borough, 7 F.3d 377 (3d. Cir) cert. denied, 510 U.S. 1195 (1993) (stating that “[t]he public policy implications must be examined on a case-by-case basis to determine whether the public interest in enforcing the agreement outweighs any harm”: the court then listed a set of factors to considered that tailored to the facts of the question before the court and which greatly resembles the Restatement section 178 factors.”).
\end{footnotesize}
many questions which challenged the role of private ordering in the context of the closed corporations. Shareholders can change, in advance the structure, roles and functions in the shareholder-director-officer relationship of the close corporation. Nevertheless, shareholders’ agreements in closed corporations still face important limits for enforcement. The main limits are the right of the non-participating shareholders and third parties and the role of public policy. The limits must be defined and measured by courts on a case-by-case basis.

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