

Equity Investments In Privately Held Companies

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The information below is a continuation from the article on Equity Investments In Privately Held Companies that can be found at <https://www.huntonak.com/en/africaprojects/>.

Minority rights

The rights of minority shareholders in a private company will often be the subject of negotiation and be a function of the bargaining strength of the parties, the expertise that the minority investor brings to the transaction and the capital invested and ownership percentage that the minority investor holds.

Governance rights

While each transaction will have to be considered on its own merits, the table below sets out typical investor governance rights at differing levels of equity ownership.

	1% - 5% Investor	10% - 30% Minority investor	25% - 40% Co-investor	40% - 50%+ Lead investor
Board Composition	Observer	Board member	Either: (i) Lead Investor controlled board, or (ii) balanced board with non-executive directors carrying casting vote and "reserved matters"	Either: (i) deadlocked board or (ii) balanced board with non-executive directors carrying casting vote and "reserved matters"
Participation in Committees	No	No	Yes	Yes
Investor attendance required for quorum for board and shareholder meetings	No	First meeting only	First meeting only	Yes; deadlock procedure applies if meeting unable to be held
Appointment of non-executive directors / chairman	No	No (but may provide that non-executive directors / chairman will be independent)	Consultation right only re independent non-executive directors / chairman	Yes

Reserved matters

Given the absence of board control, minority investors typically request vetoes on fundamental business decisions. While each transaction will have to be considered on its own merits, the table below sets out possible rights at differing levels of equity ownership.

	1% - 5% Investor	10% - 30% Minority investor	25% - 40% Co-investor	40% - 50%+ Lead investor
Amending constitutional documents / transaction documents	Yes, if it has a detrimental impact on legal, economic or tax position of the investor	Yes, if it has a detrimental impact on legal, economic or tax position of the investor	Yes	Yes
Dividends	No (but participate as per constitution)	No (but participate as per constitution)	Yes (and participate as per constitution)	Yes (and participate as per constitution)
Material M&A	No	No	Possibly	Yes
Related party transactions	Often	Yes	Yes	Yes
Changes to equity share capital	No, but have pre-emption rights	No, but have pre-emption rights	Yes	Yes
Changes to loan capital	No	No	Yes	Yes
Adoption of business plan & budget and material deviations therefrom	No	No	Yes or perhaps consultation	Yes
Appointment and removal of key executives and their remuneration (including share options)	No	No	Yes or perhaps consultation	Yes
Change in scope of business	No	No	Yes	Yes
Winding up				
Changing auditors or year end				
Material contracts, litigation or capex	No	No	Yes	Yes

Share transfers

The ability to sell shares and exit an investment will also be a crucial issue, in particular for financial investors. The table below sets out typical rights at differing levels of equity ownership

	1% - 5% Investor	10% - 30% Minority investor	25% - 40% Co-investor	40% - 50%+ Lead investor
Dividends	Entitled as per constitutional documents	Entitled as per constitutional documents	Entitled as per constitutional documents (dividends may be a reserved matter)	Entitled as per constitutional documents (dividends may be a reserved matter)
Pre-emption Rights For Fresh Issues	Yes	Yes	Yes	Yes
Ability to Drag	No	No	Often	Yes
Tag-along rights	Yes (complete tag upon change of control)	Yes (pro-rata tag)	Yes (pro-rata tag)	Yes (pro-rata tag)