



Trustee Shareholders - Selling a Private Company's Shares

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Introduction

This article reviews the issues a UK resident trustee shareholder should consider when disposing of private company shares in England and Wales and identifies certain steps that the trustee shareholder may take to protect themselves. For the purposes of this note, it is assumed that the trustee shareholder has capacity under the trust deed (and/or any required third party consent) to negotiate the terms of a share sale and purchase agreement ("**SPA**") - including the giving of warranties and indemnities - and to dispose of the shares.

Warranties and Indemnities

Warranties and indemnities are one of the most heavily negotiated areas of the SPA. Trustee shareholders should approach the giving of warranties and indemnities with caution, particularly where they are not involved in the day-to-day management of the company (as will usually be the case).

The buyer is likely to insist that the trustee, at the very least, give warranties as to their title to the shares and their capacity to sell the shares. However, where the trustee lacks the requisite knowledge, it should resist giving any warranties (beyond title and capacity) and indemnities.

A trustee that holds a significant shareholding in a private company should ensure it has adequate control measures in place to be sufficiently well-informed to protect the trust asset. Although this note does not deal with the investment duties and rights of a trustee shareholder, a trustee involved in the day-to-day affairs of a company - for example, by having a representative on the board - should expect to be required by the buyer to give a broader range of warranties.

Where the buyer is insisting that the trustee gives warranties beyond title and capacity, it would be advised to:

- 1 remember that it owes an overriding duty to the beneficiaries of the trust and must exercise appropriate care;
- 2 make reasonable enquiries about matters outside its knowledge and consider asking for statements to be substantiated by the company's directors, auditors or financial advisors;
- 3 request that any sellers who are involved in the running of the company to provide warranties on a broader basis;

4 if a particular warranty cannot be removed completely, include a knowledge qualification, such as '*as far as the trustee is aware...*'; and/or

5 seek to obtain third party guarantee and indemnity of the trustee's obligations (though this is rarely given as there may be adverse tax consequences for the trust and the guarantor if such guarantee is deemed to constitute additional property to the trust, making the guarantor a settlor).

Limiting Liability

Where a transaction involves more than one seller, the buyer will usually insist that the warranties and indemnities are given on a joint and several basis. In that case, the trustee shareholder may find itself liable for the performance of an obligation owed to the buyer by another seller.

Ideally, the trustee should:

1 ensure that liability is several, and apportioned by reference to the warrantor's respective shareholdings in the company; and

2 where a particular warranty relates to matters outside of the trustee's control (such as the capacity of another seller to transfer their shares), exclude liability altogether.

However, a prudent buyer is unlikely to accept this as it makes enforcement of a breach of warranty more difficult. A trustee may wish, therefore, to consider entering into a contribution agreement with the other sellers under which liability is apportioned between them in relation to any claim.

In addition, a trustee shareholder should look to cap its liability to the value it is receiving under the SPA for the trust shares - this will ensure can be fully indemnified by the trust fund.

If the buyer insists that the trustee should be held personally liable in case of breach of warranty, or wishes to attribute personal liability to the trustee in any other circumstances, the trustee should seek to obtain trustee indemnity insurance, provided that is permitted by the trust deed.

Future Considerations

The buyer will want to restrict the trustee's ability to dispose of the funds it receives under the SPA following completion, to ensure it has sufficient funds to satisfy any potential future claims. The extent to which any restrictions on the trustee in this respect are included in the SPA will depend on the parties' respective bargaining powers. The trustee must balance its duty to the beneficiaries with its responsibility to ensure there are sufficient funds in the trust to satisfy any potential future claims.

For further information, please contact Isobel Symonds by email or on 020 7465 4300
