Tamara L. Harper
BUSINESS ATTORNEY · LA & VENTURA COUNTY
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FEATURED · BUSINESS PLANNING — GOVERNANCE & SUCCESSION

FROM THE SHORE *Two roots, one tree — governance and succession hold a business steady through every season.*

CORPORATE GOVERNANCE & OWNERSHIP

Two Agreements, *One Plan*

A Shareholder Agreement runs the business day to day. A Buy-Sell Agreement decides what happens when an owner exits. You need both — and they should stay separate. Here's why.

TAMARA L. HARPER, ESQ. • 6 MIN READ • GOVERNANCE · SUCCESSION

Neither agreement is legally required — and that is exactly why so many businesses skip them to save time and money.

A **Shareholder Agreement** and a **Buy-Sell Agreement** are two of the most important documents for managing, and ultimately buying or selling, a business. Without them, the questions that decide a company's future — who votes, how profits are split, what happens when a co-owner dies, divorces, or wants out — get answered in the middle of a dispute, when emotions and legal fees run highest. The two documents are not interchangeable, and they should not be rolled into one. This issue explains what each does and why keeping them separate is best practice.

AT A GLANCE **What this issue covers**

01 **Two documents, two jobs**
One governs daily management and voting; the other governs ownership transitions.

02 **Why keep them separate**
Privacy, cleaner amendments, and the right signatories on the right document.

03 **Six reasons for a Shareholder Agreement**
From deadlock and disputes to protecting minority and majority owners.

04 **Your action items**
Funding, review cadence, and coordinating with estate planning after Connelly.

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GOVERNANCE VS. TRANSITION

Two documents, two jobs

These agreements address different aspects of ownership and management. Understanding which does what is the first step to knowing why you need both.

ALWAYS ACTIVE

Shareholder Agreement

Governs daily managing, voting & dividends

It gives every shareholder clarity on their **roles, powers, and how decisions are made** — especially when shareholders are also directors and officers. That clarity reduces disputes and confusion as the business grows or changes direction.

TRIGGERED ON EXIT

Buy-Sell Agreement

Governs the transition of ownership shares

It takes over when a co-owner **sells, dies, divorces, files for bankruptcy, or becomes incapacitated** — setting the terms of sale, the valuation of shares, and payment arrangements, so an uncertain moment follows a clear plan.

DIMENSION	BUY-SELL AGREEMENT Ownership transfers	SHAREHOLDER AGREEMENT Ongoing governance
PURPOSE	Governs **ownership transfers**	Manages **ongoing governance**
ACTIVATION	Triggers during **specific events**	Remains **continuously active**
FOCUS	Establishes **valuation & payment terms**	Defines **voting & decision rights**
TIMING	Addresses **future transitions**	Governs **current operations**
PARTIES	Involves **buyers & sellers**	Binds **all current shareholders**

> *The Shareholder Agreement remains active throughout normal operations. The Buy-Sell stays dormant until a triggering event — which makes them complementary, not competing, documents.*
>
> TAMARA L. HARPER, ESQ.

Most multi-owner businesses benefit from both. Companies with multiple shareholders or partners should put a **Shareholder Agreement** in place early — before disagreements over operations, profits, or strategy ever surface. A **Buy-Sell Agreement** becomes essential the moment owners want to protect their investment: family businesses use it for succession, and professional firms and medical practices rely on it to handle both voluntary and involuntary departures.

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THE CASE FOR GOVERNANCE

Six reasons for a Shareholder Agreement

Directors run the day-to-day, so shareholders often have surprisingly limited say. A well-drafted agreement changes that — here is what it protects.

1 Disputes

Minimizes the potential for disputes by setting a framework and procedure for resolving them, and by spelling out how key decisions are to be made.

2 Management of the company

Directors run daily operations, so shareholders have limited decision-making rights. A properly drafted agreement **holds directors accountable** and can require them to seek shareholder consent before key moves — amending governing documents or incurring large expenditures. Vital when directors are not shareholders.

3 Protection for minority shareholders

Reserves certain decisions for **unanimous consent** and gives minority owners a veto. **Tag-along** rights let them join a majority sale on the same price and terms.

4 Protection for majority shareholders

Drag-along provisions let majority owners require minority owners to join a sale of the company on the same terms — so a single holdout can't block a deal from closing.

5 Deadlock

When owners can't reach consensus on key matters, the business can grind to a standstill. A **deadlock provision** resolves it quickly, including buy-out mechanics for the parties.

6 Control the transfer of shares

Without pre-emption rights, shares may be freely transferable — to a stranger, a competitor, or a divorcing spouse. The agreement gives remaining owners and the company **rights of first refusal** and binds any new shareholder to its terms.

Plan for the horizon you can't yet see.

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BEST PRACTICE

Why keep them separate

It is tempting to fold everything into one document. Four practical reasons argue for keeping the Buy-Sell on its own.

01

Targeted dispute resolution

Governance disagreements shouldn't complicate time-sensitive ownership transitions. Separation keeps the forced-buyout mechanics clean.

02

Privacy control

Share the governance document with banks or key employees, while keeping transition triggers, valuation formulas, and funding private.

03

Streamlined amendments

Ownership percentages shift more often than management rules. A separate Buy-Sell means updating one without renegotiating the other.

04

Differing signatories

California community-property law often requires spouses to sign the Buy-Sell — but not everyday management decisions.

CASE TO KNOW

The Connelly decision changed the math

In 2024, the U.S. Supreme Court reshaped how life-insurance-funded buy-sell arrangements affect a company's value for estate-tax purposes.

In *Connelly v. United States*, the Court held that life-insurance proceeds a company receives to fund a buyout can **increase the value of the business** for estate-tax purposes — without an offsetting reduction for the obligation to redeem the deceased owner's shares. For many closely held companies, that means a buy-sell structured the old way may now produce a larger taxable estate than the owners expected. Reviewing your agreements in its wake ensures your documents still meet your goals, reflect current law, and coordinate with your estate plan. Read the full opinion →

WHY IT MATTERS

Review your buy-sell before it costs your estate more than you planned

If your buy-sell relies on company-owned life insurance, the structure that worked before Connelly may now inflate your taxable estate. A review — coordinated with your tax and estate advisors — can restore the outcome you intended.

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BEFORE YOU CLOSE THIS ISSUE

Your action items

Five checkpoints to run against your current documents — or your reasons to start putting them in place.

- **Review both agreements annually — and after any major change.**
  Confirm they still work the way you intend, and refresh valuations so pricing stays current with the market.
- **Verify a plan to fund the Buy-Sell.**
  Key-person life insurance is the most practical option; if that's not possible, plan to borrow or structure installment buyouts.
- **Match the agreements to your ownership structure.**
  Equal splits need clear voting and valuation methods; unequal splits need minority protections and fair-compensation terms.
- **Have a Shareholder Agreement but no Buy-Sell? Mind the gap.**
  Governance documents rarely address valuation, payment terms, or transfer procedures — the very things that spark disputes when an owner exits.
- **Coordinate your Buy-Sell with estate planning.**
  Predetermined valuations and life-insurance funding provide liquidity and help set estate values — coordinate with counsel, especially after *Connelly v. United States*.

LET'S TALK

Secure your business's future.

We assess your needs, update existing documents, and create agreements tailored to your business. More than a law firm — your trusted advisor for your business and family, from beginning to end.

BOOK A MEETING →

CALL 805-409-0530 ↗

FOR YOUR READING LIST

- California Secretary of State — bizfile Online
  bizfileonline.sos.ca.gov · corporate filings & governance
- Connelly v. United States — Full Opinion
  supremecourt.gov · buy-sell valuation & estate tax

A note from counsel

Business ownership requires planning for both the expected and the unexpected across the life of your California company. Reviewing your current agreements — especially in the wake of Connelly — ensures your documents actually meet your goals and protect your interests.

This article is provided for general informational purposes and does not constitute legal advice. Shareholder and Buy-Sell Agreements are not legally required, and the right approach depends on your specific business and ownership structure. For guidance specific to your situation, please contact our office in Westlake Village.