

LEGAL ALERT

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AUGUST, 2005

All this for 7 Shares of Stock and \$350

Why selling a small amount of stock to an employee can create a big problem

By Charles E. Ringer, Esq.

Occasionally a small business owner talks to me about his desire to bonus out or sell stock to employees to reward them for years of loyalty and to make them feel and maybe even work more like an "owner."



The client often says: "It's only a couple shares – I will still own the majority of the shares and maintain control." A June 2005 court decision highlights one of the many reasons why in most cases I discourage sharing even a small amount of ownership with employees.

An employment agency, Callos, Inc., sold 7 shares of its stock to Lillian Greco, an employee, for \$350. Later the company was sold in a merger and the majority owners and all the other employees who held a few shares of stock sold to the successor company --- that is all except Lillian. Lillian refused to sell her shares. Although in most cases a buyer would not go forward under such a scenario, in this case for unexplained reasons the merger closed. After the closing, the buyer determined it had a shareholder, Lillian, it did not want and attempted to force a sale. When discussions broke down, the new owner sued Lillian. In response, Lillian hired her own attorney and filed a cross-claim asking the court to set aside the merger, to order an accounting, to award damages, and to award a statutory forfeiture.

Prior to trial, Lillian asked the court to rule early that she was not required to sell her shares since there was **no written agreement** between herself and the company requiring her to sell nor was there any provision in the company's articles of incorporation requiring redemption or sale. **The trial court agreed with Lillian and held that she was not required to sell her 7 shares. The buyer immediately appealed and the court of appeals agreed with the trial court.**

It is unclear from the court of appeals decision but the matter was most likely sent back to the trial court to further rule

on Lillian's cross-claim against the company to set aside the merger, to order an accounting, to award damages, and to award a statutory forfeiture. **All this for \$350 and 7 shares!**

Selling stock or giving stock as bonuses to employees is a transaction that is very easy to do **wrong** and many times should not be done at all. For most small businesses, selling or giving a small number of shares of stock to employees will not net an owner a return that justifies the expense or added risk. Anytime you have a transaction involving your stock, hire a legal professional's assistance for the tax planning and to prepare a buy/sell agreement as well as other necessary documents.

Note: The general summary of the law should not be used to solve individual problems since slight changes in the fact situation may require a material variance in the applicable legal advice.

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