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Exclusion of shareholders: The French Supreme Court endorses a by-laws provision that excludes the vote of the excluded shareholder

There are many legal cases and court decisions concerning the exclusion of shareholders because disputes between shareholders are frequent and the exclusion sensitive to implement practice.

While judges ensure strict compliance with the terms and conditions that govern the exclusion of shareholders, some legal tricks do enable to circumvent the inflexibility of the rules of law.

This is the case in a decision handed down on October 24, 2018 by the *Cour de Cassation* (French Supreme Court) in which it approved a by-laws provision that deprived the shareholder whose exclusion was contemplated of his right to participate in the decision and to cast a vote on the exclusion resolution.

The basis principle: The shareholder's right to remain within the company

The principle is that any shareholder has the right to remain within the company in which he/she holds shares. In other words, he/she may not be excluded nor forced to sell his/her shares against his/her will. This principle

is, however, tempered by the possibility to exclude a shareholder by applying the rules set forth by law or in the by-laws.

Indeed, French law foresees cases in which a shareholder can be excluded, such exclusion resulting in the compulsory sale of his/her shares.

As such, the exclusion can be provided for by law: Nullity of the company or nullity of acts/agreements based on the lack of consent or legal incapacity of the shareholder.

On the other hand, the exclusion can also be provided for in the by-laws insofar as the French Commercial Code leaves open the possibility to include in the by-laws of a company a provision allowing for the exclusion of shareholders.

The exclusion of a shareholder is regulated

While the Commercial Chamber of the *Cour de Cassation* has admitted the principle that a shareholder can be excluded, it has, however, made this right to exclude a shareholder conditional upon compliance with a number of rules that it has set.

First, the terms and conditions governing the exclusion must be set forth in the by-laws and specify the corporate body that has authority to decide the exclusion, the procedure to be followed, as well as the grounds that can justify the exclusions, it being specified that such grounds must be objective and in the interests of the company^[1], such as the loss of a required capacity or the breach by the relevant shareholder of his/her obligations.

Second, the relevant by-laws provision must have been unanimously adopted by the shareholders.

Lastly, even though French courts allow shareholders a large degree of freedom to determine how the exclusion is to be implemented in practice, Article 1844 §1 of the French Civil Code stipulates that “*every shareholder has the right to participate in collective decisions*” and the *Cour de cassation* has further specified that a shareholder whose exclusion is contemplated may not be deprived of his right to cast a vote on the exclusion resolution^[2].

While some drafters have tried to by-pass this prohibition by entrusting the exclusion decision to a management body, they did not anticipate that judges would systematically refuse to endorse these circumvention practices.

New developments brought about by the October 24, 2018 decision

In the decision handed down on October 24, 2018^[3], the *Cour de Cassation* further refined its interpretation of Article 1844 of the French Civil Code.

In that specific case, a nontrading private company had specified in its by-laws that the exclusion of the shareholder would be adopted “*by unanimity of the votes cast less the votes of the relevant shareholder*”

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[whose exclusion is contemplated]. »

While Article 1844 of the French Civil Code requires the participation of the relevant shareholders in the decision concerning his/her exclusion, it does not, however, require that his/her vote be efficient. As a result, the *Cour de Cassation* endorsed the drafting of the clause, which means that while the vote of the to-be-excluded shareholder is required for the calculation of the quorum, it is not, however, required for the voting results.

By ruling so, the *Cour de cassation* made a strict application of Article 1844 of the French Civil Code. This interpretation may be seen as unfortunate by the excluded shareholder but, as a matter of fact, it makes the judge's reasoning more fathomable and enhances legal certainty for litigants.

Is it possible to consider that this decision – which concerns a non-trading private company but should logically extend to other forms of companies – opens the door to all kinds of abuses? It will be interesting to see what happens in the future.

In any case, this decision serves as a reminder of how important it is to exercise care in the drafting in the by-laws of a company and to entrust this task to specialized lawyers.

[1] Cass. Com., 8 mars 2005, n° 02-17692

[2] Cass. Com., 23 octobre 2007, arrêt d'Hem

[3]

<https://www.legifrance.gouv.fr/affichJuriJudi.do?oldAction=rechJuriJudi&idTexte=JURITEXT000037556279&fastReqId=1186936969&fastPos=1>

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