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What to Do When Your Partnership Sours

When there's no more middle ground, a strong partnership agreement can save you the hassles of an expensive legal battle.
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Even in the best of circumstances, business partnerships can be fraught with conflict. To handle the twists and turns, smart co-owners put a well-drafted partnership agreement in place to act as a road map. Without one, lack of guidance in the event of a dispute can result in a free-for-all for partners, says Jonathan Levitt, a principal with Outside GC LLC, a team of former senior in-house lawyers who act as "on-demand" in-house counsel for clients.

For partners who don't have an agreement, or even those who do, there are a few things they should consider in order to best protect themselves when conflict arises.

First, business partners need to evaluate whether they can mend fences and settle their differences. Difficult issues surface in all partnerships, and they can create stress in the relationship, "but if you work through these issues, you usually have a stronger partnership," says Steven Thayer, an attorney with Handler Thayer LLP in Chicago.

It's important to figure out what's at the root of the friction. Ask, "What is occurring within the partnership that is causing you to make a decision to [want to] sell or liquidate?" says Terry Mackin, managing director at Generational Equity, merger and acquisition advisor for small businesses. It can come down to rifts, family dynamics or other issues. "How are those things affecting the business?" says Mackin.

Business issues such as not making enough money, having too much debt or realizing your business model doesn't work are situations that may require you to adapt and change your business plan to make it work, says Thayer. Of course, fundamental issues that are hard to move past--lying, cheating, stealing or other illegal activity, for example--can be deal breakers and a legitimate basis to terminate the relationship.

Whether conflicts are resolved to make the partnership work is a business decision based in part on each partner's risk/reward tolerance level. "Each partner should regularly assess the risks and rewards associated with their business […] to make sure they are in check," says Thayer.

To that end, ongoing communication and a periodic review of your partnership (especially the agreement, if you have one) is essential. Just as in any relationship, partnerships grow old and co-owners need to reassess how decisions are made, who makes what decisions, etc., says Kurt D. Olender, a corporate attorney in Manhattan.

What do you do if you're unable to resolve your conflicts? At this point, business partners need to determine whether or not one partner buys out the other or both sell out to a third party. In the case of a partner buyout, the two important questions to ask are "Who has the most passion for the business, and who has an immediate cash need that requires them to cash out of the business?" says Steve Nielsen, CEO of PartnerUp, an online small-business networking community. As one would expect, both partners need to agree on the next course of action. In some cases, reaching an agreement may require a good business attorney to act as a sort of "corporate therapist."

Whatever the decision, make sure you hire a good business attorney to help with the dissolution of the partnership. There is too much at stake to use your friend's uncle or some other attorney who is not an expert in business law. Finally, "It is extremely critical that both parties either have their own independent valuations or that they agree on an independent business-valuation expert to determine the value of the business, " says Nielsen.

Most issues, serious or not, can be resolved at the onset through good communication and effective negotiation skills. "Before you resort to the worst case, try working things out by talking," says Nielsen.

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