

## Potential Partnership Problems Paramount

*“A Partnership is just as unpredictable and satisfying as a marriage.”*

Perhaps you are a sole proprietor in an existing business or an individual who has great ideas about a prospective business. In either case, you would like to expand your horizons and add another person into your venture, ultimately starting a partnership. A partnership differs most from a sole proprietorship in that each partner has the legal right to make decisions and enter into contracts on behalf of the whole partnership.

A partnership can offer you many advantages such as:

- (1) Having an additional perspective on a problem that the business may be facing;
- (2) Additional capital to contribute and provide added vigor to your business,
- (3) Bring in diversity of skills, training, experiences and talents, and
- (4) Simply alleviate some of the loneliness that comes with being a sole proprietor in a business.

However, in the face of these advantages there are many real and important problems that a partnership can produce for one or both of the partners involved. One of the most important dangers of a partnership is that one of the partners can make an unwise decision and get the entire partnership into financial trouble. If this should happen, it would mean that you, the individual who is not responsible for making that fatal decision, would have to be responsible for all the mistakes of your partner and the liabilities of the business. Also, the same diversity in skills, training and experiences that you may want to add into your business, can destroy it if you and your partner cannot work together. In the face of these dangers, you need to keep several important considerations in mind when forming the partnership.

First, the selection of the prospective partner may be the most important decision you make in regards to your new venture. Some questions or points to think about when choosing a partner are as follows:

- (1) What are the financial resources of your prospective partners? Will you be contributing equally to the formation of your business?
- (2) Does your potential partner have the financial ability to withstand possible financial reversals and economic challenges?
- (3) You should think about what the age disparities are between you and your potential partners.
- (4) Are your prospective partners going to be trustworthy? Do you trust them to handle large amounts of capital, including your own money? Do you feel comfortable for them to borrow funds for which you may be held solely responsible?
- (5) What is the business competence and skill of the prospective partners? Do you believe that you and your prospective partners have the personalities required to get along?
- (6) You should also look at the individual work habits of your prospective partners. Are their work habits something that you could accommodate to and work with?

- (7) What synergies exist between the partners? Your skills and the skills of your prospective partners not only have to complement each other, but rather, you should depend on each other's skills, such that without each other, your joint business would fail. For example, a weak artist but a renowned medical doctor, Vesalius searched for a partner until he discovered Titian, a master painter. The two collaborated successfully to create "On the Fabric of the Human Body", considered to be a work of both artistic and medical genius.

Second, when forming a partnership, you should always create a Partnership Agreement. It is simple to set up a partnership because no legal documents are needed. Partnerships are often an oral agreement between two or more persons. However, complex and potentially costly problems can be avoided in the long run, by drawing up a partnership agreement that would contain the exact terms and conditions for the partnership and the particular responsibilities of each partner. A good partnership agreement must contain the following:

- (1) Amount of equity invested by each partner;
- (2) Type of business;
- (3) How profits and losses will be shared;
- (4) Each partner's compensation and benefits;
- (5) Distribution of assets and property upon certain events, including sale of the business and dissolution;
- (6) Provisions for changes in the partnership;
- (7) Dispute settlement clause;
- (8) Settlement in case of death or incapacitation;
- (9) Restrictions of authority and expenditures; and
- (10) Restrictions on the transfer of the partnership units.

The potential problems of a partnership may be paramount but they are certainly not impossible to prevail against. Creating a successful business partnership is very attainable, if you keep in mind the following tips:

- (1) **Have the Same Vision-** For a partnership to be successful, all parties must agree on the same strategic direction of the company.
- (2) **Define Business Roles-** A winning business partnership capitalizes on the strengths and skills of each partner. Thus, divide business roles according to each partner's business strengths and interests.
- (3) **Avoid the 50-50 Split-** It may seem fair and logical to split shares of ownership into a 50% split. However, this ownership structure can impair decision making in the future, if there is a disagreement vital to the business. Meet with an experienced corporate attorney to discuss decision-making and tie-breaking procedures and mechanisms. For example, one such mechanism is called "Russian Roulette". Russian Roulette is a provision found in the partnership agreement, forcing a sale or purchase to remedy a deadlock. This provision enables one partner to become the sole owner of the company by forcing his hand to either sell his own interests or buy-out his partner's interests. For example, if Sasha and Boris are partners in a company and are deadlocked on a decision and are facing costly litigation or liquidation

of the company, they could take advantage of this procedure. Sasha would offer to buy the interests of Boris at a price set by Sasha. Boris would then have the option to either sell his interests or buy Sasha's interests at that same price. It is called "Russian roulette" because you can't predict the outcome in advance, other than the fact that one partner will be bought out.

- (4) **Hold Frequent Partner Meetings-** A strong business partnership is built on open communication between all parties. Thus, it would be a good idea to have meetings for partners to communicate their visions, goals, concerns or ideas regarding the partnership. Also, knowing that your problems do not go unheard would improve business partnership morale.

If a business partnership is right for you, you should be assured in knowing that it is a very attainable and realistic venture as long as you capitalize on having the requisite foresight to avoid many of the possible partnership problems. If you require assistance in forming a partnership or drafting a partnership agreement please contact Serge Biberman at 312.410.7863.