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THE 5 D'S THAT SPELL PARTNERSHIP DISASTER

Is your business prepared for the worst?

Many businesses operate with an inadequate partnership agreement or worse still, no written partnership agreement at all.

This may not prove to be an issue for the business partners while everything is running according to plan, however when the business does eventually experience dilemma, it will often be too late to act.

There are five major dilemmas which often face a partnership business. Call them the five D's:

Death. This will happen to all of us and can place particular strain on a partnership business. The interest of a partner in the business will form part of their estate. You will then be in business with their family. Is that what you planned for? Careful consideration should be given to buy-out rights of the deceased partner's interest in the business. Should you manage this through insurance or buy outs or vendor finance from the estate? How will you value the business?

Dishonesty. Although no one usually wants to consider the possibility that their business partner would act dishonestly in the business, events of dishonesty must be considered in the partnership document. The partners must decide what constitutes dishonesty. If a dishonest partner is to be struck out of the partnership, will they be bought out for a full value, at a reduced valuation or forfeit their share without any compensation?

Disagreement. When times are good and parties have very close working relationships, minor disagreements are often solved through discussions between them. However, when resentment builds and the partners cease to act in a 'reasonable' manner, the partnership documentation should provide a process to be followed.

Divorce. In the event that a partner is to divorce or separate from their spouse or defacto partner, any property settlement between the two would likely include the interest in the partnership as a part of the matrimonial pool. Depending on the financial position of the parties and the split of the matrimonial pool, the partner in question may lose control over their partnership interest or be unable to provide necessary working capital to ensure effective continuation of the business. The partners should consider potential rights to buy-out on divorce or defacto property settlement and partnership voting rights of a partner affected by this.

In any event the fact of their separation and how long the separation takes to be formally resolved will almost certainly mean you have another partner in the business - the Ex. Should this trigger a buy out of the partner's share? What valuation will you pay for it? Will there be some vendor finance?

Departure. How can a partner exit? How much notice do they need to give? What valuation will you use? Do you have to pay them out on the spot? Can they just set up in competition with you nearby or will there be some kind of restraint?

It is a worthwhile investment for any business partnership to take the time and have their partnership documentation professionally reviewed to ensure that the partners' wishes and understandings are properly recorded. We can help you sort the issue for a fraction of the cost (in time, stress and dollars) of solving a problem should you experience one of the D's with a poor agreement.

If you would like to review your partnership agreement or discuss your business situation, please contact Adam Robinson or Ian Portas of Hollingworth & Spencer Lawyers on (07) 3123 5700.

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