

Time to Say Goodbye to Your Business Partner: When Subtraction Can Result in Addition for the Company

Article By:

Ladd Hirsch

Successful private company owners often share the traits of having vision, passion and a strong sense of purpose. That does not mean that they govern their companies without having any disagreements with their minority partners. In fact, it is common for business partners to have divergent views about the company and its growth plans, because there are different ways to grow a business successfully, and when challenges arise, the best path forward is not always clear. When a majority owner has serious disputes with a minority business partner, however, the question the owner has to answer is whether it is time to say goodbye. This post provides some thoughts for majority owners to consider in answering that question.

Is a Business Divorce Available?

The first question the majority business owners need to answer when serious conflicts arise with their business partners is whether it is even possible to secure the redemption (exit) of partners who hold a minority stake in the business. In other words, does the majority owner have a valid contract right to remove a dysfunctional business partner from the company? This legal means will exist if the majority owner has a buy-sell agreement in place or some other means to trigger a redemption of the minority partner's stake in the company.

It is always best to create a partner exit plan at the time that minority partners join the business so that it is clear the majority owner has a redemption right if things go south. In the absence of this type of contract right, the majority partner may be unable to secure the exit of a disruptive minority owner without mutual agreement. There are limited circumstances under which majority owners can create a new right to secure the exit of a dysfunctional minority business partner, but this will require a detailed review by legal counsel of the company's governance documents and any other agreements that exist among the owners.

Defining the Nature of the Dispute

When businesses are on a successful track, they are vibrant, they are creative, and they are nimble in meeting challenges. They have engagement among the leaders who operate as a team. The company may have a dynamic leader, but he or she will want to be surrounded by bright colleagues who offer new ideas and do not merely serve as an echo chamber for the majority owner. In this

environment, it is common for respectful disagreement to exist among the leaders, and their efforts to develop consensus are both healthy and necessary.

When disagreement among business partners becomes dysfunctional is when one of the minority owners or a small group does not work toward this shared purpose, and instead, pursues a separate agenda that elevates their own importance. In this situation, the company will be split by competing visions of the business plan, factions will develop among employees, and this will lead to internal strife that will either slow down the company's growth or, in a worst case scenario, completely derail the company's success.

The question the majority owner should strive to answer promptly is whether disputes with a minority business partner merely reflect differences in approach, style, or tactics, but are still consistent with a desire for the company to prosper. If so, it may be that aspects of the minority partner's views can be incorporated into the business plan. But if the minority partner is clearly ego driven, if the partner will not support the decisions of the team, if the partner is demanding distributions to be issued and is unwilling to re-invest in the business, and finally, if this partner takes actions that undermine the company when his or her ideas are not adopted, this partner's continued involvement will be a drag on the company that will likely become more acute over time. When this conclusion is reached, the majority owner needs to act decisively to seek a separation from the minority partner that preserves the company's culture and vision.

The Valuation Process

As discussed above, the redemption of a minority partner is likely only possible if the majority owner is able to exercise a buy-sell agreement or has a similar redemption right in the company's governance documents. In the buyout process, the majority owner will want to pay close attention to the valuation process, and the calculation of the amount that will be paid for the minority partner's interest. The formula that is used to determine the purchase price will be set forth in the buy-sell agreement or in the governance document.

In many cases, the formula for determining the purchase price of the minority interest will specify that the price will be subject to discounts based on the lack of control and the lack of marketability of the minority interest. Even if the formula does not refer to these discounts being applicable, unless they are specifically excluded, the majority owner will want to insist that the valuation be subject to these discounts because they are substantial and they are supported by Texas legal authority and by customary valuation practice.

Conclusion

Whether a majority owner should take action to secure the exit of a business partner who holds a minority stake in the business is a tough decision. Before going down this path, the majority owner will first want to confirm that: (1) he or she has the right to redeem the partner in a written agreement, and (2) that the nature of the disputes with the partner are serious enough to warrant taking this decisive action. Finally, once the decision has been made to redeem the minority partner, the majority owner will want to monitor the valuation process to ensure that the purchase price paid for the minority interest comports with industry standards and includes all applicable minority discounts.

[Listen to this post](#)

National Law Review, Volume XIII, Number 145

Source URL: <https://natlawreview.com/article/time-to-say-goodbye-to-your-business-partner-when-subtraction-can-result-addition>