AVOIDING PARTNERSHIP AND STAKEHOLDER DISPUTES
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Across the U.S. each day, thousands of business deals are being put together by teams of partnering entities, entrepreneurs and investors. In most cases, these team members will end up owning minority interests in a newco or project company with little long-term control over daily operations and company decisions. Most often, your companies' ability to negotiate control or veto power will depend on the perceived value of its contribution to the partnership or project. However, even if your role or contribution doesn't give you a lot of leverage, there are still a number of things you can do to mitigate the risk of a disruptive and often expensive partnership or stakeholder dispute. This article provides some key advice derived from 30 years of representing companies and individuals in a myriad of business transactions and projects across many different industries.

1. Deal Structure. There are many ways to structure complex transactions between entities. Risk profiles will vary, as will tax ramifications and cost. Your team should be able to identify and compare the available deal structure options before you enter into any business marriage. Don't forget to consider the difficulty and cost of unwinding failed business arrangements.

2. Due Diligence. Make it standard operating procedure to do background checks on principals of small business partners and investors especially if you are looking at an international deal. Verification should be a key goal. Pay particular attention to litigation history, liens, and assets owned. Due diligence should also be done on the reputation risk of doing business with larger entities. Unfamiliar deal metrics should be reviewed to ensure that market rates are being paid on fees, commissions, compensation, and equity.

3. Discount Stakeholder Alliances. Stakeholder alliances are fickle. They seem to evaporate when interests are no longer aligned. Don't count on alliances to stack votes on important issues or to protect your influence on the Board or otherwise.

4. Understand Minority Ownership Limitations. A deep understanding of the limitations of your minority ownership can help you mitigate risk. Carefully review operating, shareholder and partnership agreements to identify problem issues. Pay particular attention to voting rights, distributions, capital calls, limitation on transfers of interest, and removal of managers and officers.

5. Negotiate Protections. Ideally, important company decisions should not always rest with the majority owner. A seat on the Board may keep you informed while you have it, but it won't give you any real protection from an oppressive majority owner. Push for veto rights, limitations on use of funds, favorable distribution rights and employment agreements. Document all loans made to the company and deferred compensation. Provide for tax payments to cover K-1 taxes to prevent abuse. All organizational documents governing stakeholder rights differ. Negotiate to the absolute limit of your leverage.

6. Buy-Back Provisions. Don't overlook this easily negotiated protection at the front end. Always insist on a "put" right. Ideally, stakeholders should be able to give or sell back their equity to the company or remaining stakeholders through a reasonable process. If things get ugly,

not being able to extricate yourself from involvement in the partnership or newco could lead to a disastrous and costly ride.

7. Deal Documents. Use a business-savvy attorney and CPA to review all transactional documents. If good at their job, these folks will identify important deal risks and provide you with a list of drafting and strategic options to help mitigate those risks. Your attorney should have high-level transactional drafting skills, but understand that business decisions are made by management not legal.

8. Investors. Deals don’t get done without capital, which puts investors in a class of their own. A savvy investor will protect itself by requiring such things as a priority distribution rights; control over the use of funds and capital, inspection rights, and voting controls until full or partial payback. Passive investors who ignore these protections often suffer the most.

9. Capital Contributions. Potential equity holders should not underestimate the value of their contributions whether cash, intellectual property, real estate, equipment or a brand. Be wary of trading a significant capital contribution for equity. It is often safer and more advantageous to grant a license, take convertible debt or a profits interest rather than a flat-out trade for a minority equity position.

10. Control Conflict. Business leaders should be plugged into important transactions. Potential conflicts should be flagged for strategic resolution by leadership. Multi-dimensional teams should advise on potential strategic options before contentious decisions are made. Communications should be monitored and carefully controlled at the first sign of conflict.

11. Dispute Resolution. Most transactional documents specify arbitration or litigation in a particular forum. As an effective alternative, disputing parties should be required to hold face-to-face negotiating sessions followed by meditation. Mediation is relatively inexpensive and if taken seriously by both parties, usually results in an acceptable conflict resolution. Settlement agreements should be detailed. Keep in mind that arbitration is as expensive as litigation, is more arbitrary and affords fewer opportunities for strategic maneuvering.

12. Tie-Break Provisions. Do not underestimate the importance of tie break provisions when entering into transactions where voting stalemates could occur. Common resolutions involve different forced buyout mechanisms or appointment of third-party advisors to make decisions for hopelessly deadlocked parties.