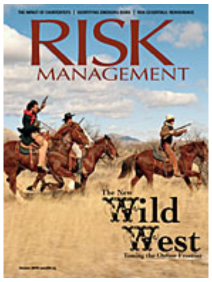

Time for a Business Divorce?

by Curtis L. Golkow

When times are tough, even healthy business relationships can become strained. Challenging times force business owners to assess their own, and their partner's, contributions and commitment to the business and generally reexamine their priorities. Through this process, business owners may come to realize how they differ in visions for the business, risk tolerances, levels of commitment or values. For these reasons and others, economic woes often cause business owners to seek a business divorce. And with business valuations at their lowest levels in years, what better opportunity will the controlling business owner have to buy out a minority business partner?

Depending on the type of business entity, state of incorporation or formation, and various other factors involved, the controlling owner may have the ability to squeeze-out the noncontrolling owner through a merger, share exchange, reverse stock split, redemption or other transaction that would compel the noncontrolling owner to sell or extinguish its interests. If there is a shareholders agreement, LLC operating agreement, partnership agreement or other "pre-nuptial" agreement between the business owners that requires a buy-out upon termination of the noncontrolling owner's employment or some other event, the controlling owner may wish to pull the trigger.

If, however, the "pre-nuptial" agreement between the owners prohibits or impedes the controlling owner's forcing a buy-out, techniques that otherwise might be considered "oppression" of the non-controlling owner might be justified. After all, in an uncertain economy, might it not be prudent for management to reduce or eliminate dividends or distributions, or to reduce salaries or other compensation? These actions might benefit the company and, at the same time, induce a noncontrolling owner to succumb to the controlling owner's desire to buy.

Additionally, if declines in the stock market or real estate values have put the noncontrolling owner in a cash squeeze, the controlling business owner might have extraordinary leverage. With aid from the down economy, the controlling owner may be able to negotiate a buy-out of the noncontrolling owner without having to resort to tactics designed to increase bargaining leverage.

On the other hand, economic difficulties may present a unique opportunity for the noncontrolling business owner who has been waiting to exit. Typically, the noncontrolling owner has no way to force a buy-out of its interests. The controlling owner, knowing that the noncontrolling owner is trapped, generally offers a low price and unfavorable terms-if it makes any buy-out offer at all. In most situations, the law protecting noncontrolling owners does not provide sufficient rights to enable noncontrolling owners to exit from the company on fair and reasonable terms.

A troubled economy may create opportunities for the noncontrolling owner to improve its negotiating leverage. If the company is experiencing strained relationships with the bank, key customers, vendors or other important contacts, the business and its controlling owner may find themselves in a vulnerable position. Furthermore, if the controlling owner wants to make major changes to adapt to economic conditions, the noncontrolling owner may be in a position to challenge those initiatives. Conflicts between business owners are often highly disruptive to the business and can cause a loss of valuable relationships, and sometimes even jeopardize the company's viability. In short, economic adversity may put the noncontrolling owner in an unprecedented position of leverage, giving the controlling owner reason to negotiate a fair and reasonable buy-out.

In the current economy, the opportunity for business partners to separate from each other may have improved. A business owner who wishes to take advantage of the downturn and separate from their partner should develop a strategy now, along with the advice of experienced counsel, to seize this valuable opportunity.

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