When two's no longer company

Teaming up with a partner is a popular way of starting in business, but why do more than half of all business partnerships fail? BETTER BUSINESS investigates the reasons and the fallout for those involved.

According to the Department for Business, Innovation and Skills (BIS), there are approximately 450,000 private sector business partnerships in the UK. A partnership helps spread the load and many great enterprises have been forged by two individuals working together. Yet various experts estimate that more than half, perhaps even up to 70%, of all business partnerships do not survive. Why? And what does it mean for the business, and the careers and personal lives of those involved?

Joining forces

In a business partnership, two or more people share all the risks, costs and responsibilities, as well as the profits. A partnership can exist with no written contract or partnership agreement, and the partners are not required to submit their business' accounts to Companies House. However, the lack of admin is not the main reason why many budding business owners decide to join forces.

When best friends **James Steed*** and **Tony Webb*** left their respective employers to start a financial consultancy five years ago, they worried about getting everything wrong. *"So we made all the business decisions together, from small stuff like ordering stationery to critical issues like the location of our premises so that we were visible to our target clients,"* says James.

"Starting out in business with a friend or someone else wanting to work on the same idea is less daunting," says corporate solicitor **Jonathan Lea** (www.jonathanlea.com).

Having a partner also helps when you need to complement your skills or expertise and when you want to spread the initial investment. *"You can bring together technical and personal skills, experiences and management styles to create a stronger business than either of you could build on your own,"* says **Paul Griffith**, business tutor at Ashridge Business School. *"For example, one partner may be proficient in finance, the other may have sales or people-management skills."*

Marketing specialist Adam Redcliffe* started a small marketing and design agency two years ago. *"I didn't have some of the skills, or the capital to pay upfront for things, so I teamed up with a designer," says Adam. "I felt I had to do it with someone else or not do it at all."*

Risky business

While making business decisions together is important for some partners, others do not see it as a joint exercise. Sisters **Jane** and **Kathy Corville*** used to be joint owners of a gift shop in Devon. *"Kathy nearly always ordered stock without checking with me first and with no consideration for what might attract new customers,"* says Jane.

Unfortunately, in a business partnership, this is perfectly permissible and one partner can legally bind the whole partnership when contracting with outside parties, even if the partnership agreement says the contrary. "That's because a deed of partnership, or a partnership agreement, is a private document and the outside party cannot be expected to know what it stipulates," explains Jonathan Lea.

Shared responsibility can therefore also be a liability – literally. *"A partnership that is not an LP (Limited Partnership) or an LLP (Limited Liability Partnership) has no separate legal identity,"* says **Carl Bowles**, partner and insolvency practitioner at Carter Backer Winter. Like sole traders, business partners have unlimited liability for the debts and obligations of their business and are liable both jointly and severally. This means all the partners can be personally responsible for transactions or contracts entered into by any one or more of the other partners.

"In practice, the joint and several liability means that the person suing can go after just one of the partners or all of them," says Jonathan. *"They can choose the 'best' partner to sue – the one with the most personal assets."*

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More pitfalls

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In Jonathan's experience, 50:50 partnerships usually suffer from 'creative tension', as a result of which each partner may start pulling the business in a different direction. *"I was focussed on getting larger clients and promoting their business through billboards and advertising campaigns, whereas my partner wanted to keep the cost of client marketing down,"* admits Adam.

Changing personal priorities and inability to commit fully can stall the partnership, too. *"I had a baby coming and was running the agency part time alongside my full-time work; my business partner was involved in another venture,"* says Adam. *"We did put in equal amounts of time and effort but sometimes it seemed like one or the other was doing more so someone always felt hard done by."*

A partner may lose their initial enthusiasm and stop pulling their weight as soon as it becomes clear that winning customers is hard work. *"After only six months, it became apparent I was the only one chasing leads and Tony was chasing another 'opportunity',"* says James Steed.

Experts also cite loss of confidence in the competence of your partner and conflicts over money as some of the main reasons for business partnership breakdown. But what are the specific pitfalls of doing business with family and friends?

"When we go into business with a friend or a relative, we often don't choose them on merit but for convenience, or to do someone a favour, or because we like them," says **Dr Tomas Chamorro-Premuzic**, business psychologist and co-founder of www.metaprofiling.com, an online profiling tool measuring entrepreneurial talent. *"Then we feel pressured to make concessions and expect the other party to do the same."*

Jane and Kathy Corville opened the gift shop with money inherited from their grandparents. *"I had previous experience of running a business while Kathy had none but I felt pressurised to include her,"* says Jane. *"I'm not blaming her for everything but some of her actions lost us money."*

Finally, when the resentment and the frustration spill over, the personal relationship between the partners breaks down and working together becomes impossible.

The fallout

"I've dealt with two brothers who'd inherited a farm, farmed the land for many years with no formal partnership agreement in place, then fell out, split the business and the land, and went their separate ways," says Jonathan Lea. *"To avoid a 'messy divorce', a partnership deed of dissolution detailed how the split would work. You can have it drawn up even if there was no formal partnership agreement in the first place."*

On top of the partners' relationship not working, sometimes the venture fails because it does not make any money. *"To win a share of the market, we priced ourselves a bit too low. The business wasn't profitable and there wasn't enough in it for us to pull out of all the other commitments,"* says Adam Redcliffe. *"My mindset changed, I started to think a lot about exit strategy rather than focusing on building the business. After a year we made a mutual decision to shut things down."*

Financial consultants James and Tony parted ways after only 12 months, too. "I wanted to get out before my savings ran out completely," admits James.

But when the business can be salvaged, a buy-out may be possible. In Devon, Jane Corville bought out her sister last year. *"In hindsight I should have done it sooner,"* says Jane. *"We constantly argued, we were losing customers and were drowning in debt. Had it not been for a cash injection from a third, unrelated party (who is now my new business partner), we would have gone bust."*

When the extent of the business failure is such that the partnership cannot meet its debts, the partnership may have to be wound up via a formal insolvency procedure such as a voluntary arrangement with its creditors (a Partnership Voluntary Arrangement). *"Because their personal assets and the assets of the business cannot be separated, the partners may also have to enter into interlocking Individual Voluntary Arrangements or even become bankrupt,"* says Carl Bowles.

The latter may scupper, or at least seriously curtail, any new business plans. Carl explains: *"When a partner becomes bankrupt, they are prohibited from doing a number of things. They cannot borrow more than £500 without telling the lender they're bankrupt; act as a director of a company; create, manage or promote a company without the court's permission; and manage a business without telling people they do business with that they're bankrupt. These restrictions usually apply for one year. The Bankruptcy Order will be shown on their credit report for at least six years."*

The fallout may be personal, too, when some business feuds destroy friendships and marriage, undermine our sense of self worth and make us doubt whether we can trust others again. *"Currently, Kathy and I are not on speaking terms,"* says Jane Corville.

The aftermath

Yet you can survive the failure of a business partnership and even turn it into a positive experience. *"How you surface from it depends on your personality,"* says Dr Tomas Chamorro-Premuzic. *"Our character defines how we react to critical life events – for some people, a single business failure means a lifelong curse and they will never recover, for others, it just makes them more resilient."*

It helps if you understand failure is an intrinsic part of success and we only learn from mistakes. *"Good judgment comes from experience, which in turn comes from bad judgment,"* says Tomas. *"In order to make an impact in any field – and business is no exception – you need constant trial and error and you need to go outside your comfort zone and take risks ... and taking risks means failing sometimes too."*

Try to maintain a positive outlook on life. *"In all honesty, I can't say it was a negative experience,"* says Adam. *"I learnt a lot about myself and became more commercially astute. Now the baby's getting older I'm planning to set up a new business by myself."*

How to dissolve a partnership

Unless the partnership agreement contains specific dissolution provisions, a partnership can be dissolved in accordance with *The Partnership Act 1890*:

Automatic dissolution

- On death or bankruptcy of a partner.
- Technical dissolution, if members of the partnership change.
- On grounds of illegality, when an event occurs that makes it unlawful for the business or the partnership to continue.
- On expiration, if the partnership was formed for a fixed term or for a single undertaking.

By notice – when notice is given by one or more partners to the others.

By agreement – when all partners mutually agree on dissolution.

Rescission – if a partner has been induced to join the partnership by fraud or misrepresentation, they may treat the agreement as if it had never existed.

By the courts

- When a partner becomes permanently incapable of performing their part of the partnership contract.
- When a partner's conduct is believed to prejudice the business.
- When a partner wilfully or persistently breaches the partnership agreement, leading to breakdown of trust.
- When the partnership is incapable of ever running at a profit.
- When circumstances are such that dissolution is 'just and equitable' (when reconciliation is ruled out).
- When a partner assaults another or makes unjustified allegations of misconduct.

Always seek legal, tax and financial advice before dissolving a partnership.

This is exactly what James did, three years after his and Tony's partnership was dissolved, albeit following another stint with a corporate employer. *"I went back to employment until I got more confident about business development and knew I could start and grow a business by myself,"* he says. And what of their friendship? *"Luckily, it survived although the experience left a sour aftertaste for a while,"* says James.

On the other hand, you may have learnt that running a business was not for you, or that another partner might suit you better. *"My advice would be to think carefully about whether you really need a business partner,"* says Jonathan Lea. *"But if you decide you do, avoid a 50:50 split, think about exit when you start and put everything in writing. If there's a dispute, your partnership agreement can help you resolve it and you may be able to move forward without further problems."*

And if you have bought out your partner? Granted, there is no one to share the risks with, but if you have a sound business concept, your business is likely to survive. *"Depending on who leaves and what skills they take with them, the operational management of the business, your customer relationships and your sales results may all suffer and have a detrimental impact on the bottom line,"* says Paul Griffith.

On the other hand, without the animosity and the frustrations that have led you to this point, both you and the business may now begin to thrive.

One obvious way to limit the risk and your personal liability is to incorporate your new business. *"This is now so straightforward that most partnerships sooner or later go down this route,"* says Jonathan. *"Business and personal identities become separate, the company is more tax efficient and, with web filing available to limited companies, the 'less admin' argument no longer stands."* ■

*(*names changed)*