FAQs ABOUT PARTNERSHIP, SHAREHOLDER & LLC DISPUTES
February 16, 2011
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Frequently Asked Questions about Partnership, Shareholder and LLC Disputes

Q: I am in a dispute with my partners, what should I do?
Get a copy of all agreements that the partners signed. Many people refer to their co-shareholders as "partners," when in fact, they are not truly partners, but rather all shareholders in a corporation, or members of an LLC. Different rules apply for different types of business entities. So, the first step is to determine what you own.

Q: Okay, I checked, and I am a "partner" - now what?
If you truly have a partnership, the first step is to see if you have a Partnership Agreement. A partnership does not require a written agreement. If there is an agreement, then the partners are free to determine in that agreement their rights, including how and when and on what terms a partner can withdraw from a partnership.

If you do not have a written partnership agreement, then any partner can withdraw at any time under New York Partnership Law. By withdrawing, a partner is entitled to be bought out. The first step is to get an "accounting" which is a financial snapshot. Then, the bought out partner is to be paid for his share.

Q: My partners refuse to pay me, now what?
If your partners will not honor the agreement, or if you have no agreement, won't honor New York's common law and partnership statute, then you have a right to sue your partners to get an accounting and a monetary award for your partnership interest.

Q: I have a written partnership agreement that has an arbitration clause, now what?
If you have a partnership agreement that includes an agreement to arbitrate, then you need to serve a "notice of intent to arbitrate" and follow the steps of the arbitration clause. However, you may have certain remedies available in court, too, including an injunction in aid of arbitration, to protect bank accounts, for example, from a partner making improper withdrawals, or to prevent a partner from using partnership funds to pay for legal fees.

Q: My partners are excluding me from the business of the partnership and are refusing to let me see financial information, what can I do?
Every partner under the New York Partnership Law has a right to manage and be involved in the partnership and a right to see the books and records of the partnership. The right to manage, however, can be modified by a written partnership agreement. For example, a partnership could name a committee or a manager to be the managing arm of the partnership. You would, however, still have the right to review the partnership's books and records.

Q: What is the difference between a general partnership and limited partnership?
New York permits a partnership to be a "limited partnership." In a general partnership, all general partners have the right to manage and all have personal liability for the debts and obligations of the partnership. In a limited partnership, one partner is designated the general partner (and he has personal liability) and the other partners are "limited partners," which means that their liability has been limited for exposure for partnership debts and obligations.

Q: Okay, I checked and I am a shareholder in a corporation. I'm feeling abused, now what?
Again, the first step is to look and see what agreements there are. If you have a shareholders' agreement, then does it promise employment? Does it promise a role in management? You do not need to have a shareholders agreement, and if you do not have one, then the questions to ask are:

- how much stock do I own?
- has my role in the corporation changed?
- what payments am I getting from the Corporation?
- how much money are the other shareholders taking out? more than me?

As a shareholder, you have a right to the "reasonable expectations of your investment" in the corporation. That means that you have the right to return on your investment. A court will look at whether there is a history of dividends, or whether the shareholders are all just getting paid salaries. If you are a shareholder who does not work at the company, and you are not being paid dividends (and you are receiving no salary), a court may consider this "oppression." Whether there is oppressive behavior, or not, is a question for the court to decide.

If you have no contract right to employment, then being fired may or may not be evidence of oppression.

Q: What remedies do I have if I am "oppressed"?
"Oppression" can be a basis for a shareholder lawsuit. In New York, if you own 20% of the stock of a privately held company (or collectively own 20% with one or more other shareholders), you can bring a suit that seeks to dissolve the corporation. This right is found in section 1104-a of the Business Corporation Law. A court will look at the facts and determine if the way the corporation is being managed by those in control is "oppressive," and if it is, and your reasonable expectations of your investment in the Corporation are being denied by the majority, then a court may order the Corporation liquidated.

Q: One of the shareholders has sued the Corporation for dissolution under section 1104-a, now what do we do?
First, take a look at the shareholders agreement, if you have one. If there is an arbitration agreement, the Court will order the parties to arbitrate their dispute, if you timely make a motion to stay the court proceedings. You need to act quickly, however, so that there is no waiver of the right to arbitrate.
Next, make sure that the disgruntled shareholder actually owns the minimum 20% of the voting stock in the corporation.

There are two choices once confronted by a shareholder lawsuit: either to fight over whether there has been oppression (or waste or looting) by the majority, or elect to buy-out the shares owned by the petitioning shareholder(s) for "fair value."

Q: How do I elect to buy-out?
Once a shareholder brings a section 1104-a dissolution proceeding, the other shareholders and/or Corporation have a 90-day period to elect to purchase the shares owned by the petitioning shareholders.

Often, emotionally, the respondent shareholders are prepared to fight the oppression allegations, rather than buying out the shares. If the 90-day period has passed, however, the statute provides that the corporation or the defending shareholders can ask the court for permission to buy-out the petitioners.

Be careful, though, as the decision to elect to purchase is irrevocable.

Q: What is "Fair Value"?
"Fair value" means that you will pay the petitioner(s) what a willing purchaser would offer to pay for the shares in the corporation as a "going concern." This means that the entire business is valued and the petitioner is paid his percentage of the business. The purchaser can be the company or any or all of the other shareholders. A discount can be taken for the "lack of marketability" or "illiquidity" of the shares. The corporation is valued as of the day before the petition was filed.

Q: What is the discount for lack of marketability?
The courts recognize that it is much more difficult to sell shares in a privately held company than it is to sell shares of stock that are sold on a stock exchange. A reduction is taken due to the "illiquidity" or "lack of marketability" of the shares. This discount is often in the range of 25-40%. This is not a discount due to the fact that the party seeking dissolution owns a minority interest.

Q: Is there a discount for owning a minority interest?
New York does not permit a "minority discount" (which is also called a discount for "lack of control").

Q: How do you determine what is "fair value"?
"Fair value" is not defined by the statute. Generally speaking, an appraiser is hired who will give an opinion of value. Appraisals are done in a variety of ways, and the appraiser determines which methodology is appropriate (it can even be more than one method). The appraiser may look at "investment value" or "market value" or "net asset value" or an "income" (also called a discounted cash flow) method.

These cases often become a battle of the experts, as it is up to the court (or the arbitrators) to set the price.

Q: Can the parties agree in advance to a buy-out price that will be used to determine "fair value"?
While it is a great idea for shareholders to agree in advance to a buy-out method or price in advance and to put such an appraisal or price in their shareholders agreement, such an agreement may not be binding on the court (or the arbitrators) in a "fair value" setting. Sometimes it may just be evidence of what the price should be. Careful drafting in advance my allow the shareholders to agree to a mechanism for a buy-out that would be used in the 1118 election.

Q: I own 50% of a corporation, can I still bring a dissolution proceeding?
Yes, you can. Even a 50% shareholder, if he can establish oppression, waste or looting by the other shareholders, can have grounds to seek dissolution of the Corporation as a remedy.

Q: I have a different problem, our management is deadlocked? What do we do?
If the directors or shareholders are deadlocked 50-50, the statute permits a petition to be filed to seek dissolution on grounds of the deadlock. It isn't an automatic dissolution however. Rather, the deadlock must be about issues that are central to the management of the company. The statute that permits a dissolution petition on grounds of deadlock is section 1104 - not section 1104-a. Don't confuse the two!

Q: What are the differences between the section 1104-a and a section 1104 proceeding?
The most important difference is that the respondents who are defending the 1104 deadlock suit have no right to buy-out the shares of the petitioner. That remedy only is available to the oppressed holder of 20% or more of the voting stock who alleges oppression, waste or looting.

Q: Would fair value include the waste or looting by the majority?
Yes. Once an election to purchase is made, the stock if valued as of the day before the petition was filed and such value can include a surcharge if the court finds that there was waste or looting that affects the value of the shares.

Q: I've been oppressed. Can I get my attorney's fees paid by the Corporation?
I'm afraid not - unless it is a part of a settlement. The Corporation's attorney's fees can be paid by the Corporation. You may be able to get a court order preventing the other defending shareholders from using the corporate treasury to finance their defense, however.

Q: What if I am a member of an LLC instead of a corporation or partnership?
An LLC is a creature of statute and of its Operating Agreement. The rights of a member, while similar to those of a shareholder or partner, are not identical. For example, both a member of an LLC (that's what a "partner" in an LLC is called) and a shareholder in a corporation have a right to inspect records of the company, and to bring a "derivative" lawsuit on behalf of the company (if the company refuses to do so), against directors, officers, and shareholders or others who are harming the company, there are different rules that apply. Thus, as a member of an LLC you have different rights and there are different remedies available under the applicable statutes. And, of course, take a look at your Operating Agreement.

The right of inspection of corporate records is governed by a different law and different cases than the right of inspection of an LLC's records. Similarly, the right of a shareholder to bring a derivative suit on behalf of the corporation is governed by a section of the Business Corporation Law, the right of a member to bring a derivative suit on behalf of the LLC is not found in the LLC Law. Rather, the New York Court of Appeals found that all members have such a right.

The oppressed shareholder who holds 20% of the stock of a corporation may be able to sue to dissolve the corporation, but the member of the LLC has different rights. This is why it is important to know precisely what type of entity the business is.

Q: When can a member seek to dissolve an LLC?

The NY LLC Law provides, at section 702, a limited right to dissolve an LLC: "whenever it is not reasonably practicable to carry on the business in conformity with the articles of organization or operating agreement." This section has been interpreted narrowly and to not include "oppressive conduct" against the member, or similar grounds that are found in the statutes applicable to business corporations, as a ground to dissolve an LLC.
Thus, members should consider whether they should add to their Operating Agreement any additional grounds for dissolution, or to keep the limited basis contained in section 702.

Q: What if I have an arbitration clause in my Shareholders Agreement or Operating Agreement?
Courts will enforce the arbitration clause, and require arbitration, even though the statutes talk about "judicial" dissolution.

Arbitration is similar to court proceedings, whether the issue being tried is the "fair value" or whether there has been "oppression" or whether there are grounds for dissolution or other relief regarding a dispute among the owners.
We look at the arbitration clause to determine what disputes must be arbitrated.

Also, some dispute resolution clauses may require the parties to arbitrate disputes before a party can invoke a "termination" provision. These clauses will also likely be enforced.

For example, if two 50/50 owners cannot agree on whether to sell a piece of property owned by the company, can use the arbitration clause to have that arbitrator – a neutral third party – decide the issue. In other words, that arbitrator becomes the "tie-breaker."

Q: What are the advantages of arbitration? How is it different from litigation?
Arbitration is usually less expensive and faster than pursuing a lawsuit in court. This is because, in arbitration, an expensive part of litigation is avoided. In arbitration, discovery is generally kept to a minimum – often just an exchange of documents. Usually no depositions are taken and no interrogatories propounded and answered. After the exchange of documents, the parties proceed to a hearing at which time witnesses testify and exhibits are introduced into evidence. The arbitrator makes his or her award. But, there are very limited rights of appeal from an arbitration award.

Q: Can I mediate my dispute?
Litigation can be costly, so thinking of mediation is a good idea. Most arbitration associations, such as JAMS or the AAA, have mediators available to help with your dispute - whether or not you are using them to determine the underlying dispute. Firms such as Meyer Suozzi also have attorney who are experienced mediators on hand who can be retained to help the parties reach a settlement.

The New York Supreme Court Commercial Part courts also have mediators available to help resolve disputes that have been filed. Your attorney can ask the court for assistance in getting a mediator assigned. The Federal courts also have a roster of mediators to assist the parties.

Mediation is an important tool of alternate dispute resolution. In a mediation the mediator does not decide issues and it is almost always non-binding. It is just a way for the parties to reach an agreement, with the assistance of a neutral third-party. Mediation is also attractive because it provides the parties with a way to find a business solution to resolve their differences. (This might include selling/buying a book of business or buying out an interest.) These solutions may not be available to a judge who is presiding over a court case. Some agreements require that the parties try to mediate their disputes before filing a lawsuit or demand for arbitration.

Q: My company is not a New York company. What do I do?
Some corporations are incorporated or registered in other states. Sometimes you have agreements that state that the law of another state may apply. The best thing to do is to have an attorney review the agreements and filings and determine what your rights are under that state's law, and whether you can sue for relief in New York, or whether you must bring suit elsewhere. Even if you sue in NY, the other state's law (such as Delaware) might be applied by the NY judge or arbitrator.

Erica Garay has been handling business disputes for nearly 30 years. Her practice has an emphasis in shareholder, LLC and partnership disputes. She represents both management and business owners in litigation, arbitrations and mediations. Ms. Garay is a frequent lecturer regarding shareholder disputes, and counsels other attorneys and clients regarding the enforcement of confidentiality agreements (trade secrets) and non-compete agreements. Ms. Garay is also an arbitrator with the American Arbitration Association, hearing commercial and complex commercial cases, as well as a mediator with the New York Supreme Court Commercial Division.

A sample of her engagements in disputes concerning business owners includes:

- Dissolution of medical practice (P.C.) - multiple day arbitration and court proceedings and mediation (issues include buy-out; restrictive covenants; breaches of duties and contract)
- Dissolution of real estate corporation (valuation) - Nassau County - multiple day trial (valuation hearing under section 1118)
- Shareholder dispute - SDNY and mediation -(buy-out and breach of contract; complex accounting issues)
- Dissolution of real estate brokerage and valuation proceeding under section 1118- arbitration (multiple day arbitration)
- Dissolution (and related shareholder disputes and claims) of medical practice (P.C.) - multiple day arbitration and court proceedings (complex valuation issues and post-award proceedings)
- Dissolution of 5 real estate partnerships - Nassau County (3-week accounting proceeding)(including successful post-judgment appeal)
- Dissolution of corporation and shareholder disputes (arbitration and court proceedings)
- Dissolution of high-tech manufacturing corporation - Nassau County -(complex oppression issues)
- Dissolution of service corporation - Nassau County - (including post-settlement enforcement hearings)
- Dissolution of LLC - Suffolk
- Dissolution of construction management company - New York County - (mediation and court proceedings)(including post-settlement court proceedings)
- Dissolution of LLC and related disputes - Colorado and EDNY - (including complex valuation and accounting issues)
- Dissolution and shareholder disputes of real estate corporation - Queens County - (including derivative claims)
- Dissolution and shareholder disputes of real estate corporation - Nassau County - (including derivative claims and settlement)

- Partnership disputes concerning 3 real estate partnerships - worked with partner to gain control of entity through negotiation and partnership meetings
- Shareholder dispute (regarding buy-out) - SDNY
- Dissolution of retail corporation (valuation) - NY County
- Shareholder dispute (regarding acquisition of interest) - NY County
- Shareholder dispute (regarding acquisition of interest in accounting firm) - pre suit
- Dissolution of law firm - Bronx County
- Dissolution of service corporation including other shareholder claims -Nassau County
- Shareholder Dispute and dissolution - Nassau County
- Shareholder Dispute (pre-litigation) regarding law firm dissolution
- Membership Dispute LLC - EDNY (post-arbitration)
- LLC/PC Break-up (Pre-litigation and settlement)
- Shareholder Dispute and enforcement of buy-out of accounting firm PC (pre-litigation)
- LLC dissolution proceeding – Kings County
- Shareholder derivative suit – Kings County
- Buy out of Shareholder interest – Kings County
- Successful Mediation of Complex Shareholder/Member Dispute
- Shareholder Dispute (D. Mass)
- Arbitrator in Shareholder oppression case
- Arbitrator in Shareholder Buy-Out Dispute
- LLC Dispute/Termination of Employment (of own) Dispute (Pre-Litigation)
- Shareholder Dispute (EDNY)
- Arbitrator in LLC Dispute
- Pre-suit negotiation of Partnership Dispute (medical practice)