

# Great Business Partnerships and How To Create Them

By Barri Carian

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“It has become increasingly difficult to achieve great success in today’s complex business environment by forging ahead on your own.” When I wrote that sentence in 1999, partnerships and strategic alliances were starting to gain traction as viable business models. Very little was written on the subject other than the legal and tax aspects. It was extremely difficult to find data showing how many business enterprises were partnerships, what the success rate was, and the factors contributing to success and failure of these collaborations. Today, ten years later, it still is.

The principles outlined in this paper are useful for all forms of business collaborations, not just legal partnerships. They can be applied to strategic alliances, formal affiliations, and joint ventures, any time two or more parties come together voluntarily for a common interest.

In researching the data on business partnerships, the most common statistics cited for the failure rate ranged between 51% and 67%, with most failing in the first five years. This confirms my experience in partnership intervention work. I am usually called in around year two or three of the partnership when the relationship begins to fall apart.

Given the statistics and horror stories of partnerships, why would anyone enter into one? The emotional and financial cost of failure and recovery is enormous.

In the following discussion, we will examine the benefits and pitfalls of business partnerships, the critical path before and during the partner relationship, and the planning for after. We can learn much from the anecdotal evidence of successes and failures.

## Why Partner?

This is the first question you should ask yourself if you are contemplating taking on a partner. Some reasons will provide more sustainability for the partnership than others.

The second question you should ask: is there another way (other than partnership) to meet that need? Could you hire or outsource and get the same--or better--result? Could you develop that product or service from scratch without the risks inherent in a partnership *and* without losing focus on your core business? Is there another way to infuse capital into the company? Getting clarity on your motivation, needs, and expectations will help you determine if partnering is the best avenue for you.

In today’s economic environment, strategic partnering can provide substantial competitive advantages to the small or mid-size business owner. Some of the most powerful benefits of partnering are:

- Access to new vertical and/or geographical markets
- Addition of new lines of products and services to your existing market
- Addition of critical knowledge, functional experience, and skills
- Addition of new distribution/sales channels
- Access to new technologies
- Infusion of capital
- Risk reduction/sharing

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Partnering can add tremendous value for the business owner looking to create quantum leaps in company growth. As global markets continue to open and competition grows, small and mid-size companies need to be increasingly creative about how they go to the market.

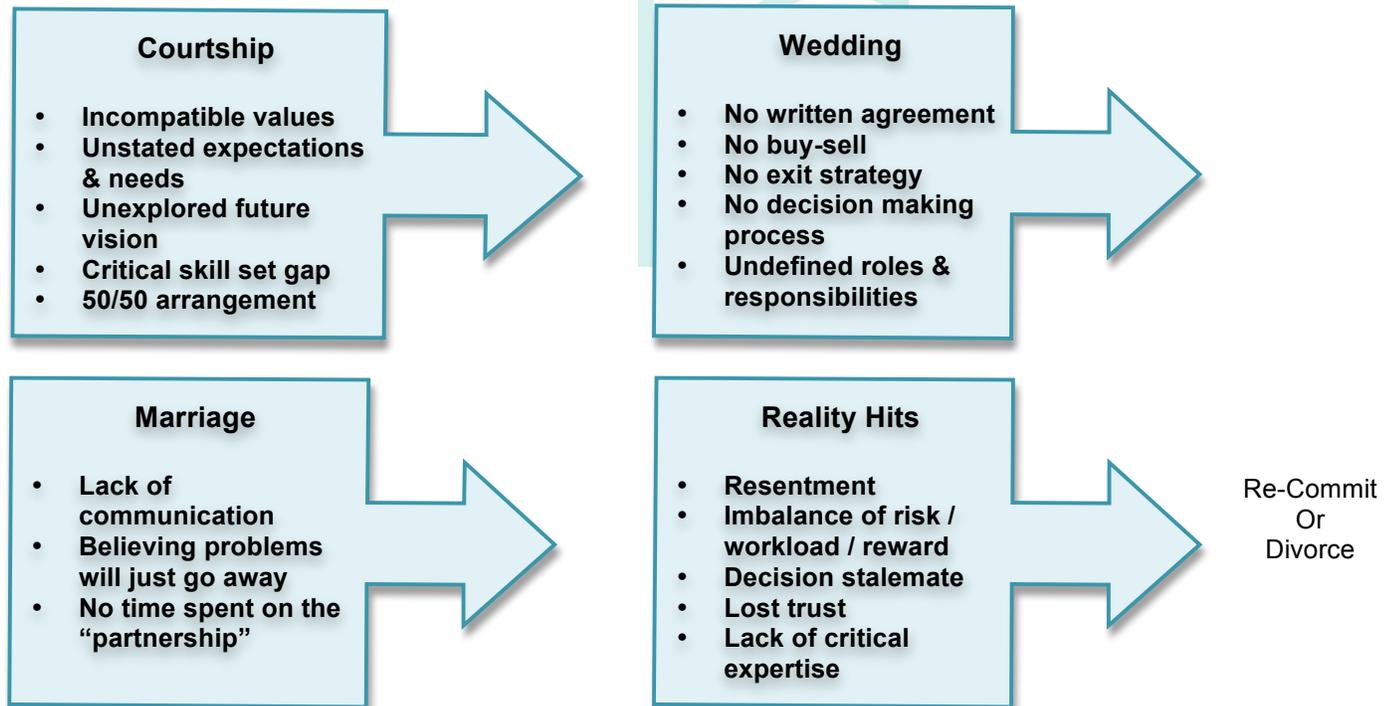
## Beware The Pitfalls

Business partnerships, like marriage, will succeed or fail largely on the compatibility of the people involved and the mutual investment of time in the relationship. Also like marriage, most people in the courtship phase of a business partnership are so caught up in the excitement of the possibilities and the newness of the relationship that they do not do their due diligence. As a result, only basic questions are asked of each other and superficial answers are accepted without further questioning.

It might go something like this: "Oh, we'll be great partners. You have the sales and marketing experience and I have the financial background. We complement each other and will make a great team."

While knowing your potential partner's skills and functional expertise is important, it's only the beginning of the selection process. Creating great partnerships requires doing your homework up front, asking a myriad of questions, and communicating with deep honesty, authenticity, and directness. Once you've asked the right questions, it is important to establish the relationship and business rules *before* cementing the partnership.

Continuing with marriage as a metaphor, here's the typical path of business partners in crisis.



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If you have decided that partnering is the best course for you to take, then the next challenge is selecting the right partner.

## Courtship – Do Your Due Diligence

Unfortunately, many people ignore or gloss over this phase because they are uncomfortable asking personal and probing questions or they are too vested in the outcome of selecting a particular person as a partner. If you're smart, you'll use this time to really explore compatibility on multiple levels. *Most fatal conflicts will arise as a result of skipping this step.*

➤ **Know thyself.** Do you like to collaborate or work alone? How good are your communication skills? Are you flexible? Can you respond to problems quickly? Do you have the time and inclination to invest in the *relationship*, not just the business? What are your work habits and work ethic? Do you expect others to have the same? What level of risk are you comfortable with?

➤ **Explore compatibility.** It's not enough to say, "We get along well." Do you share core values? Get beyond the pat answers of "honesty & integrity." Find out what those values *look like* when they are at play in the business. How will you know when they are lacking?

Do you have the same vision and expectations for the company or project? Are you in sync as to the size of the business and speed of growth? Are you in the same stage of life or is there a significant age gap contributing to different exit time frames and needs?

Do you have overlapping strengths or weaknesses? How will you shore up gaps in skills sets? Do a complete skills, knowledge, experience, and expertise inventory to understand what each of you brings to the business and what will still be required. It's more important to find partners who are skilled where you are weak than settling on people who are just like you or you just like.

➤ **Understand the financial.** What are your individual expectations of ownership percentages? (I do not recommend 50/50 partnerships.) How much money is each of you willing to put into the business? How strong is everyone's credit rating? Can you each provide loan guarantees if necessary? If married, how willing are your spouses to undertake financial risk? What personal financial obligations are anticipated in the near future that might impact your ability to infuse capital if necessary?

Personal financial conditions can derail a good partnership, particularly if one party experiences an increasing need for more cash. If your potential partner has difficulty managing personal finances, it is highly unlikely that he/she will have the capability to manage the changing financial condition of a business. It is important to have open dialogue with a partner regarding financial expectations for the business. How long can you maintain without taking home money? What backup plan do you and your partner have for personally getting through the lean times?

Is there any expectation of non-monetary contributions (intellectual property, contacts or clients, etc.) to the business for equity? How will you value it?

How will each of you be compensated? Many do not understand the difference between equity distribution and salary compensation, and believe that because they have equal shares for example, that the salaries should be equal. Make sure you reach agreement on the method of splitting the profits for when your business starts to make money. If one partner thinks he or she

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is the primary driver of the company's success, without an agreement ahead of time, there will be a problem.

➤ **Establish roles and responsibilities.** Fortunately, most people do team up with someone who has complementary skills and knowledge and they understand that these differences are strengths in the business.

What strengths and weaknesses are you bringing to the partnership? What likes and dislikes? What about your partner?

Defining roles and responsibilities based on a candid assessment of these areas, allows partners to avoid ego issues, stepping on each other toes, duplicating efforts, and giving mixed signals to the organization. Who is responsible for which "departments" in your company? Finance? Marketing? Internal operations? Who is responsible for sales, inventory, advertising, housekeeping, or any of the many tasks in a business? It is vital that each partner know his or her agreed upon responsibilities. This does not mean inflexible job descriptions. Like any business, you will want your company to be fast and flexible to respond to any challenge.

It is also critical to address company leadership. Partnerships are not completely flat organizations; they have leaders (sometimes multiple leaders) depending on the situation or task at hand. What is the most effective leadership model for your organization? Who will be the president of the company? Will you choose based on skills and ability or equity stake?

If you cannot work it out in the courtship phase when everyone is excited and happy, how are you going to agree when you are facing tough times?

➤ **Define your decision making process.** How will both the day-to-day and major decisions be made? Look at every aspect of running an organization, the innumerable decisions, their impact on the organization, and then define how those decisions will be made. Will they fall under each partner's functional area or will decision-making be shared? How will differences of opinion be handled? Partnership does not mean consensus, and disagreements are inevitable. Know how you will deal with them before it happens. If you do not work this out, you may be condemning your business to a state of paralysis due to decision stalemate.

Equally important is the need to define authority limits. What are the individual limits of each partner? What requires joint authority? Who has the final say? Who can sign checks, hire employees, fire employees, purchase inventory and for how much, sign contracts? Who can make commitments to customers or suppliers? Because problems can arise from misunderstandings over turf and the right to make decisions, it is important to agree on the limits of individual authority.

➤ **Establish a communication blueprint.** Know and respect your partner's communication style—and your own. How does each of you best receive and process information? How often should you be communicating and about what?

Be aware of the quality of your communications—are you falling into the trap of "group think?" Successful partners know how to *cultivate disagreement* by challenging the other's position in an effort to reach the best solution for the business.

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➤ **Conduct a test run.** Have you worked together before? Words are important, but actions are the true test of compatibility. If you can, work on a few projects or deal with clients together to truly understand your differences and similarities in ethics, work style, skills, and communications. Who you select to be in business with is as important as selecting what business to be in.

## The Wedding – Making It Legal

If you have successfully made it through courtship and want to continue working together, then it is important to formalize your relationship. Every detail and obligation should be clearly defined, written out, and agreed upon. All of that work you did in the courtship phase; exploring, discussing, deciding, and then testing will now be codified.

In my experience, once an agreement is in place, everyone feels better. You will have removed much of the possibility of unpleasant surprises from the relationship.

➤ **Execute a partnership agreement.** Engage an attorney to draw up a partnership agreement. You have done much of the hard work in the courtship stage and just need to provide your attorney with the information on your mutual decisions (roles and responsibilities, decision making process, equity split, authority limits, compensation, etc.). Your attorney and tax advisor can also consult with you on the best legal structure for your business.

➤ **Execute a buy-sell contract.** A buy-sell contract can be part of the partnership agreement or a separate document. Either way, make sure you have one. If one partner desires to sell his/her shares, he or she must be treated honestly and fairly, while at the same time protecting the other partner and the financial well-being of the company. The contract should also address what happens if one partner dies (do you want your partner's spouse as a business partner?), becomes disabled, or files for bankruptcy.

If your venture has been successful, profit may be a strong inducement to cash out. Unless you determine in advance the method to be used to calculate the buy-out price, inflated perceptions of the value of the business can lead to extremely difficult and emotional exchanges between partners.

## Marriage – Keeping It Going

If you thought the hard part was over, think again. Like marriage, partnerships require nurturing and a significant investment of time. Because they spend so much time together *in the business*, many partners erroneously believe that they do not need to invest additional time *in the relationship*.

➤ **Communicate, communicate, communicate.** Establish regularly scheduled off-site partner meetings and have a set agenda. This is a time to get out of the day-to-day aspects of the business and have both strategic *and* personal conversations. Where do you see the business going? Is the market changing? What are your customers saying? Should we be anticipating any challenges? How's our financial health? As partners, are we still speaking with one voice?

How is the family? Is everybody healthy, doing well in school, etc.? Partners must also clearly communicate changing personal situations that could affect the business. Anything that's going

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to change creditworthiness, ability to perform duties, and future plans must be discussed openly.

➤ **Embrace and plan for change.** Understand that everything you put in place in the beginning will change, with the exception of core values. As your partnership matures, the need to confer on every decision, for example, will probably wane. Markets change, customer needs change, and products and services may change. How will these changes impact the company? How will they impact your initial agreements on roles, leadership, decision-making, etc.? Planning for and agreeing up front on how you will tackle these critical junctures is key. What if one of you gets married and the new spouse gets a job offer in another city? Would you move away? How will employees, customers, suppliers, etc., all be treated?

➤ **Make it fun.** I'm assuming you actually like your business *and* your partner, so enjoy! Create opportunities for fun inside and outside of the business.

## Reality – Can It Really Last Forever?

➤ **Have an exit strategy.** Entrepreneurs spend countless hours discussing how to build the business and spend too little time discussing how and when they would like to exit the business. The excitement and stress of day-to-day business keep entrepreneurs focused on the here and now. Dialogue and planning about the future for both partners and the business is crucial to a happy ending for all involved. How long do you and your partner intend to stay in this business? Is there a triggering point by age, lifestyle, or financial gain at which one or the other of you will be ready to exit the business? Will you sell the business? You may have planned for this in your initial partnership agreement but that was before you experienced success. If your agreement no longer represents your future consider rewriting it.

Unexpected personal circumstances, such as death or divorce, may also force one partner to reevaluate his or her commitment to the business. A once thriving partnership can become untenable. If you can't renegotiate the terms of the relationship, know ahead of time how you will handle it if you decide to part ways.

Nobody lives or works forever so it is okay to discuss the future of the business outside of the partnership. Everybody comes out ahead when there is a plan for an exit strategy.

➤ **Plan for life after the partnership.** I see many business owners hanging on to their businesses and partnerships, not because it still makes them happy and "fires their jets," but simply because they have no idea what they will do if they leave the business. It's really rather sad. I encourage my clients to prepare for the next phase, which could be another business, time with family, giving back to the community--the possibilities are endless.

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