THE NEW YORK AND NEW JERSEY

PARTNERSHIP DISPUTE GUIDE

A practical no nonsense guide to educate, inform and empower partners, shareholders and members faced with a serious partnership dispute

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INTRODUCTION

IS THIS BOOK FOR YOU?

Yes, if you have partners who now jeopardize and threaten your business and livelihood.

For far too many business owners in New York and New Jersey, the unfortunate reality is that the greatest threat to your business, your livelihood and the equity that you have built, is, not an act of your competitor, but, rather, a dispute with your business partner and the actions that your partner may be undertaking right now. After much hard work and the promise of success, partner and shareholder relations are, many times, challenged due to disputes over business decisions, cash flow, overreaching by a majority partner, non-performance by a non-controlling partner, economic pressure and, even, the prospect of greater business success that may be on the horizon.

If you are experiencing a serious dispute with your partner that is escalating and affecting your business operations, you must establish a plan of action and implement immediate measures to secure your business and the equity interest that you have built. In this book, we will discuss your rights, the options that you should be considering and a proven plan of action for dealing with your partnership dispute.

WHO WROTE THIS BOOK?

I am a business and partnership lawyer. I represent partners, shareholders and members of various New York and New Jersey businesses when they are faced with the "internal threat" of a partnership dispute. When appropriate, I negotiate resolutions for my clients and, when necessary, I promptly commence litigation that is designed to protect my client's business interests, stabilize his or her negotiating position and rebalance the playing field.

WHY DID I WRITE THIS BOOK AND WHAT SHOULD YOU SHOULD EXPECT FROM IT?

I wrote this book because partnership disputes are serious—extremely serious—and, more often than not, they are extremely disruptive and prompt many questions and concerns. The content of this book was originally prepared to provide my clients with answers and information: answers to important questions and information about legal options and a proven course of action. Along the way, in this book, I have also sought to identify the typical patterns and "legal tactics" that many litigants wrongfully adopt and a proven course of action that I am convinced may be established and adopted to successfully resolve your dispute.

The information contained in this book has helped my clients and I hope it will help you. If you are a client then it is my hope that the content of this book, along with other materials and information that I will be providing to you, will serve to foster a strong working relationship.

THE DISTINCTION BETWEEN CORPORATE ENTITIES: CORPORATIONS, LLC'S AND PARTNERSHIPS.

As you are probably aware, in New York and New Jersey, corporations and limited liability companies constitute the typical corporate entities by which a business is owned and operated. The "equity owners" of a corporation are known as "shareholders" and the equity owners of a limited liability company are known as "members". Shareholders of a corporation utilize a "shareholder agreement" to define and establish their contractual rights while members of a limited liability company utilize an "operating agreement". Shareholders of a corporation own "stock" while members of a limited liability company own "membership units".

Separate and apart from the traditional corporate entities of a corporation and limited liability company are unincorporated partnerships. That is, many New York and New Jersey businesses are owned by two or more individuals that form a partnership. These partnerships are, typically, unregistered and are formed by either a written agreement or oral agreement.

In this book, when I refer to "partnerships", "partnership disputes" and "equity interests" please keep in mind that I am generically referring to all forms of ownership. That is, I am referring to shareholders of a corporation, members of a limited liability company and partners of a partnership. When an important legal variation exists, *i.e.,* such as for a shareholder but not a partner or member, I point out these distinctions.

THIS BOOK SHOULD NOT AND MUST NOT BE USED AS LEGAL ADVICE.

This book is all about information and should not be relied upon as legal advice. That is, as a lawyer, I must advise you that you should not rely on this book for legal advice or as a substitute for the legal advice by a licensed New York or New Jersey attorney. Partnership disputes are serious and involve many unintended consequences—so, you must consult an attorney to review your legal rights and the accuracy of the information contained in this book. Also, please note that this book does not serve to create an attorney client relationship. An attorney client relationship can only be established after an in depth review of your case and a written retainer agreement.

IMPORTANT NOTE ABOUT THE INFORMATION THAT YOU WILL AND WILL NOT FIND IN THIS BOOK:

As an active partnership dispute lawyer with clients and cases throughout New York and New Jersey, in preparing this book, I have tried to walk a fine line between: (i) providing you with critical information and tools that I know you need to know about now—before selecting the right course of action, and (ii) not revealing too much about the planning, strategy and steps that I develop and implement on behalf of my clients—you know, just in case "other individuals" get a hold of this book. I hope I have done a good job of balancing these goals.

More importantly, I hope this book serves as a beneficial tool and resource to get you from dispute and uncertainty to a clear course of action and success for many years to come.

So, now, lets get to some important information …

1

PARTNERSHIP DISPUTES: A THREAT TO YOUR BUSINESS AND THE ASSETS THAT YOU HAVE BUILT

No matter the type or size of your business, the products or services that you offer or the assets that you control, an unmanaged partnership dispute will jeopardize your business and livelihood. The reality is that you already know this and that, right now, you are faced with either a *full scale* partnership assault or a partner who, *if left unchecked,* will act to undermine your legal rights and impair the value of your equity interests.

PARTNERSHIP DISPUTES ARE MANAGABLE AND MAY BE CONTROLLED—IF YOU TAKE THE RIGHT STEPS

The fact that you are looking for information about managing your partnership dispute—or potential dispute—is a good thing and, in the end, will prove to be an invaluable asset because the *right information* coupled with the *right approach* will, much more often than not, lead to the *right result*. **How do I know this? Because in the course of successfully representing many intelligent and hard working business owners who also faced this**

"internal threat", I have consistently encountered and identified a pattern of "partnership behaviors" and "legal tactics" that the vast majority of litigants—both the individuals themselves and their attorneys—insist on following. I happen to think (in fact I know) that these typical "behaviors" and "tactics" are ineffective (if dealt with properly) and wasteful.

So, to avoid the typical reactive measures that many litigants and their attorneys follow, a critical first step for managing your dispute is to:

- **Obtain Information** – Information about the basics and the legal underpinnings of all partnership disputes. These legal underpinnings relate to the "fiduciary duties and obligations" that we will discuss in this book;

- **Understand Your Options** – Options that are not based on generic recitation of New York or New Jersey law but, rather, options that are based on a specific plan of action focused on the particular strengths and weaknesses of *your* equity status, the overall dynamics of *your* partnership relationship and the operational controls relating to *your* business and business assets;

- **Learn About A Proven Course of Action** – This proven course of approach is one that first, recognizes that partnership disputes are factually dynamic but fundamentally static. That is, although every business is different and the list of partnership offenses (*i.e.,* lock-out, misappropriation of assets, diversion of business opportunities, minority shareholder oppression…) far to numerous to

ever list in complete detail, there are, nevertheless, certain fundamental factors and tools common to all partnership disputes and necessary to successfully manage and control partnership negotiations and litigation.

WHAT DOES THE "RIGHT RESULT" AND "SUCCESS" MEAN IN TERMS OF YOUR PARTNERSHIP DISPUTE?

In the first few paragraphs of this chapter I use (and even underline) positive terms such as the *"right result"* [when faced with a partnership dispute] and positive phrases like "Successfully Influencing and Controlling…" [your partnership dispute]. Since these terms possess a different meaning for different people, it is critical for me—right now—to clearly explain what I understand and believe success to be when you are faced with a partnership dispute.

As an attorney who represents hardworking business and equity owners, success means the preservation and protection of your equity interests, the recovery of misappropriated or diverted assets and the protection of the underlying business. Success does not and should not include unrealistic goals focused on obtaining more than you are entitled to.

When faced with a partnership dispute, you must work with your attorney to identify and establish a clear understanding of what "success" will mean for you. Once understood, your attorney will evaluate your case, advise as to a realistic outcome and establish a specific plan of action. So, when it comes to establishing a working relationship with your attorney, your attorneys understanding of your expectations and goals will be critical.

WHAT IS THE BEST COURSE OF ACTION?

The best course of action is a "proven course of action" that, first, identifies the facts concerning your partnership, the legal rights associated with your partnership interests and the actions of your partners and, second, is focused on rebalancing the negotiating playing field and adopting a litigation strategy focused on action and pre-emption.

I understand that this may all sound vague, but, as we move forward in this book I promise that I will add more substance to what—for your dispute—is a proven course of action that must be considered. So, for right now, I want you to understand that there is a proven course of action—I know because over many years I have seen and used it in action. How this proven course of action is adopted and utilized will depend on facts specific to your dispute.

SOME FACTORS THAT WILL INFLUENCE THE PROVEN COURSE OF ACTION THAT IS RIGHT FOR YOU

- **Percentage of Equity Interest.** Whether or not you are a minority partner (less than 50%), an equal partner or a majority partner? Your legal rights and legal strategy will vary depending on your status as either a minority, equal or controlling partner. Each status—minority, equal and controlling—have their own litigation advantages and disadvantages.

- **Control of Critical Assets.** Whether or not you control or possess significant influence over critical assets of the business. The assets that I am referring to are, typically,

not the tangible assets but, rather, are the intangible relationship type assets that involve customers, suppliers and key employees. Your control over these assets will greatly influence and determine the right course of action for you. While it is always better to control these assets, if you don't, there are absolutely proven courses of action that may be taken to "rebalance" this playing field.

- **Agreement Provisions.** The terms of your partnership, shareholder or member operating agreement will, naturally, influence your legal rights and legal strategy. The most common agreement provisions to look out for relate to voting rights, majority rights, dissolution, non-competition, arbitration and buy-out rights. Less common but definitely important are agreement provisions that identify specific duties of partners, officers or directors and provisions that guarantee or fix an individuals employment status or roll as an officer or director. Although agreements are important, if structured properly, there are proven courses of action to help mitigate against an agreement provision that may be detrimental to your current negotiating position.

- **Pre-Dispute and Post-Dispute Actions of Your Partner.** Partnership disputes follow consistent patterns of behavior that involve the action or inaction of a particular partner. Actions undertaken by your partner will play a critical role in how your rebalance the playing field and develop an effective litigation strategy. These actions will, almost always, play the biggest role in your litigation strategy and I can tell you that, more often than not, this is where many

cases are won or lost. A proven course of action requires that you consult with your attorney to strategically gauge your actions and to honestly document the improprieties of your partner through accurate and contemporaneous business communications. (Note: I am not talking about threatening lawyer letters).

- **Your Goals.** Whether or not you wish to maintain your equity interest, structure a buyout, dissolve the business or establish a new competing business. Your specific goals must play a critical role in the planning and structuring your negotiation and litigation strategy.

THE BEST COURSE OF ACTION IS A PROVEN COURSE OF ACTION

The best course of action is a proven course of action that acknowledges your weaknesses, focuses on your partnership strengths and establishes a plan that is focused on your goals and the pre-litigation activities and actions of your partner.

The best course of action and a proven course of action is one based on an honest litigation strategy that is designed to pre-empt and push your partner in a "litigation direction" that he or she (including his or her attorney) does not expect or, at least, is not prepared for. Far too often, litigants follow the same dispute oriented direction and tone. This "dispute oriented tone" and strategy may attract attention and raise the noise level but, typically, does not work. What works is a strategy and proven course of action focused on the preservation of your equity interest, the underlying business and the maintenance of your fiduciary duties and obligations.

2

INFORMATION, OPTIONS AND A PROVEN COURSE OF ACTION

To provide you with a solid foundation for understanding your options and an appropriate course of action that may or may not be available to you, in this chapter, we will focus on the basics.

When it comes to partnership, shareholder and member disputes there is much to discuss and, whether or not your business is located in New York or New Jersey, there are many laws and court decisions that will impact the course of action right for you. Fundamental to all of these "partnership laws" are the fiduciary duties and obligations that both New York and New Jersey courts impose on all partners, members and shareholders. These fiduciary obligations form the foundation of both New York and New Jersey "partnership law" and will be fundamental to managing and controlling your partnership dispute.

So, throughout the remainder of this book, we will review the fiduciary obligations owed between partners and other fundamental principals, information and rights that you need to know before determining the right course of action for you.

2.1

SHAREHOLDER, PARTNER OR MEMBER: ALL ENTITLED TO FIDUCIARY RIGHTS

INFORMATION:

In both New York and New Jersey, the courts impose on partners, shareholders and members a fiduciary duty and obligation that mandates that when partners deal with one another they must act in good faith and free of conflict of interest and self-dealing. That is, the rights between partners goes beyond that of any contract and requires each partner to treat the other as a "fiduciary" such that each partner acts for the best interest of the business and not for that partners individual interest. This fiduciary duty applies irrespective of your corporate structure and whether you are a shareholder of a corporation, a member of a limited liability company, partner of a business partnership, and, sometimes even to certain non-traditional business relationships involving joint ventures and business opportunities.

SOME EXAMPLES OF HOW COURTS EXPLAIN AND DESCRIBE "FIDUCIARY" DUTIES AND OBLIGATIONS BETWEEN PARTNERS, SHAREHOLDERS AND MEMBERS:

To better understand how Courts define and describe the fiduciary duties owed between partners, shareholders and members, the following quotes—from court decisions—are helpful:

BUSINESS ASSETS MUST BE PRESERVED AND UTILIZED FOR THE EXCLUSIVE BENEFIT OF THE UNDERLYING BUSINESS

A corporate fiduciary, partner, shareholder or member "is not permitted to derive a personal profit at the expense of the corporation...his dealings with respect to corporate assets are subject to close scrutiny and must be characterized by absolute good faith, he may not appropriate corporate assets or opportunities to himself or to a new corporation formed for that purpose". (*In re Greenberg*, 206 A.D.2d 963, 964).

FIDUCIARY DUTIES OF PARTNERS, SHAREHOLDERS, MEMBERS, OFFICERS AND DIRECTORS

Directors and officers shall discharge the duties of their respective positions in good faith. They may not assume and engage in the promotion of personal interests which are incompatible with the superior interests of their corporation. Officers and directors of a corporation owe to it their undivided and unqualified loyalty. They should never be permitted to profit personally at the expense of the corporation. Nor must they allow their private interests to conflict with the corporate interests. These are elementary rules of equity and business morality. Courts of equity must ever enforce strict compliance with these rules. (*Foley v. D'Agostino,* 21 A.D.2d 60, 66-67)

OPTIONS AND A PROVEN COURSE OF ACTION:

Central to the options that you will possess for managing and controlling your partnership dispute will be the underlying fiduciary duty and obligation that is owed to you from your partners. How you invoke these fiduciary rights and "frame" your dispute and litigation will impact everything. A "proven course of action" is one that first understands this fundamental right and then, based upon an evaluation of your facts, structures a litigation and potential negotiation strategy based upon the advancement of your fiduciary rights. That is, your litigation strategy should be focused on preserving the integrity of the corporate entity and demonstrating why your partners actions—be it diverting assets, threatening assets, withholding distributions, acting without

authority or, even, failing to do any work—constitutes a breach of his or her fiduciary duties. This course of action starts well before actual litigation and involves "pre-litigation" planning and, possibly, strategic "non-litigation" actions on your part.

IMPORTANT NOTE ABOUT FIDUCIARY RIGHTS:

They apply to all partners, shareholders, members, managers, officers and directors, so, be careful before using this "double edged sword". Be more careful about a negotiation and litigation strategy that does not carefully plan out the best methods for invoking and utilizing these rights. Before any lawsuit is filed, ask your lawyer about your partners likely response and the reactive measures that your partner and his or her attorney may take.

2.2

FIDUCIARY RIGHTS AND DUTIES: CRITICAL TO ALL PARTNERSHIP DISPUTES

INFORMATION:

A "fiduciary duty" and obligation underlies each and every business partnership. Irrespective of any partnership agreement, or, the lack of a written agreement, each and every partner owes the other a fiduciary duty and obligation. This fiduciary duty mandates that when partners deal with one another and their underlying business, each partner must "act in good faith", avoid actions of "self-dealing" and act for the collective best interest of the underlying business.

SOME EXAMPLES OF HOW "FIDUCIARY DUTIES" COME INTO PLAY

- A partner must act for the collective best interests of the underlying business and not his or her own personal interests.

- A partner—including a controlling partner—cannot act to divert an "opportunity" away from the business and

redirect it to a new corporate entity owned or controlled by that partner.

- A partner cannot take or divert assets of the business for that partner's own personal benefit or to start a competing business.

- A majority partner cannot take seemingly innocuous actions that, technically, may be permitted but are undertaken for the sole purpose of negating and suppressing the rights of a minority partner, shareholder or member.

- A majority partner cannot restructure and divert compensation structures for the purpose of delaying distributions to minority partners and shareholders.

- A partner must follow and abide by the governing corporate documents, such as the partnership agreement, shareholder agreement, operating agreement, articles of incorporation and corporate by-laws.

- A non-controlling partner cannot divert assets or business opportunities to a competing entity or for that partner's personal benefit.

- A non-controlling partner cannot withhold his or her vote or activities in the business for the purpose of causing a deadlock and inaction.

- A non-controlling partner cannot refuse to perform his or her duties or to undertake an action that was properly voted on by the majority.

OPTIONS AND A PROVEN COURSE OF ACTION:

When it comes to partnership litigation "fiduciary rights" will serve as a significant tool by which you will protect and defend your business interests. In partnership litigation, success requires that you properly structure the claims that you make, the evidence that you use and your own pre-litigation actions and communications that will, almost certainly, come under scrutiny. For a litigant, "fiduciary rights" present a double-edged sword that must be utilized carefully. That is, your partner and his or her lawyer will almost always claim that you are, somehow, violating your own fiduciary obligations. Knowing this, a proven course of action requires that—before you file or respond to any claim—you properly structure your lawsuit and your business actions to pre-empt the predictable claims of your partner. Pre-emption and early pre-litigation planning is critical.

IMPORTANT NOTE ABOUT FIDUCIARY DUTIES, PARTNERSHIP AGREEMENTS AND SHAREHOLDER AGREEMENTS:

They must co-exist. That is, no matter what your partnership, shareholder or member operating agreement says, each and every partner is obligated to operate and conduct his or her business activities in accordance with their fiduciary duties and obligations. When faced with litigation and a partnership dispute, these agreements must be reviewed with an understanding as to how issues of fiduciary obligations may or may not come into play. Also, many times partners do not possess a written partnership, shareholder or member agreement or, worse, they possess one that is poorly drafted. If this is the situation that you are faced with, it is important to understand that the fiduciary duties that I have described will be even more important for you.

2.3

INJUNCTIONS AND THE TACTICAL ROLE OF LITIGATION:

INFORMATION:

Far too often endless "negotiations" and improperly structured litigation serve to amplify and prolong a partnership dispute, increase fees and reduce the likelihood of settlement. Negotiation without a rebalanced or amplified paying field is wasteful and, although counterintuitive, litigation—if planned and structured properly—will present the most timely and cost effective solution for your dispute. When it comes to litigation and partnership disputes, injunctive relief—relief where you request the emergency intervention of a court—represents the most important "litigation tool" that may be available to you.

SOME EXAMPLES OF HOW AN INJUNCTION MAY COME INTO PLAY

- **Non-Controlling Partner Faced with a Lock Out.** For the minority partner, shareholder or member who is locked-out or slowly being denied access to the operations of the business, a court ordered injunction will serve to

rebalance the playing field and give you a fighting chance by forcing your partners to recognize your equity status and your right to participate in the day-to-day operations of the business.

- **Controlling Partner Faced with Dissention and Inaction.** For a controlling partner, shareholder or member faced with a non-controlling partner intent on causing disruption and continuing a "free ride" on your work and efforts, a court ordered injunction may serve as a legitimate basis to pressure your partner, document his or her improper actions, and, if in the best interests of your business, to legitimately lock him or her out of the business or restrict his or her day-to-day access.

- **Partner Faced with Threat of Misappropriation and Competition.** For a partner, shareholder or member faced with the threat of a partner's misappropriation of business assets or actions that would divert business opportunities, a court ordered injunction will restrict your partners actions, prevent him or her from competing with the business and preserve the assets of your business.

AN EXAMPLE OF HOW A COURT MAY EVALUATE YOUR REQUEST FOR INJUNCTIVE RELIEF

To better understand how a court may evaluate your request for an injunction or, possibly, your opposition to an injunction, the following quote from a court decision is instructive:

PRIMARY GOAL OF AN INJUNCTION: PROTECT THE BUSINESS WHEN MONETARY DAMAGES ARE NOT ENOUGH

We believe that a legal action for [monetary] damages against these defendants is impracticable and inefficient, particularly as compared to the equitable one. Moreover, the use of a preliminary injunction is well designed for this type of action.... The failure to grant the motion would prevent the court from utilizing the typical remedy in a corporate opportunity suit, i.e., the constructive trust. Additionally, we believe that denial of the motion would be inconsistent with the purposes of this doctrine, namely, to prevent a breach of trust, and to restore to the corporation property which rightfully should belong to it... Finally, the balancing of equities favors the plaintiff since the irreparable injury to be sustained by the plaintiff is more burdensome to it than the harm cause to defendant[s] through imposition of the injunction... (*Poling Transportation Corp v. A&P Tanker Corp,* 84 A.D.2d 796)

When evaluating an application for injunctive relief the courts will evaluate:

- **Threat of Irreparable Harm.** Whether or not the threat of irreparable harm exists, *i.e.,* damage to your business that cannot be compensated by money such as the loss of goodwill associated with your business reputation, competition, diversion of business, diversion of business assets and diversion of business opportunities;

- **Likelihood of Success on the Merits.** Whether or not you have demonstrated a likelihood of succeeding on the merits of your lawsuit, *i.e.,* where you have submitted detailed and credible information and evidence demonstrating the wrongful actions of your partner; and

- **Balancing of the Equities.** Whether or not a balancing of the equities favors the imposition of an injunction, *i.e.,* where the court finds that the imposition of an injunction will do much less harm than if no injunction were to be granted.

OPTIONS AND A PROVEN COURSE OF ACTION:

If you are presented with a non-performing partner, an oppressive partner, or a partner misappropriating funds, assets or business opportunities, early and aggressive action (that is, starting a lawsuit and seeking an injunction) will not only serve to protect your business interests but, in the long term, reduce your overall litigation costs and increase the likelihood of reaching a negotiated settlement. When it comes to partnership disputes, indecision and half-hearted measures only lead to prolonged litigation and

unnecessary legal fees. Decisive action will preserve your business and expedite the settlement process.

Much more often than not, injunctions obtained by way of an emergency court action will serve as a decisive step necessary for preserving your business, enhancing your negotiating position and expediting an eventual settlement. Courts view "injunctions" and the award of "injunctive" relief as an extraordinary remedy and, as such, your litigation strategy and approach must be extremely precise and carefully structured to ensure a successful application to the court. When it comes to obtaining injunctive relief, your lawsuit and emergency motion must be focused on preserving the assets of the business and the integrity of your corporate structure.

A proven course of action recognizes the substantial value of injunctive relief and requires the development of a carefully planned lawsuit that presents a credible case and incentive for a court to intervene and restrict the actions of your partner. Prior to filing any lawsuit, a proven course of action requires that, with your attorney, you carefully examine the actions of your partner and properly gauge your own actions and communications.

EXAMPLES OF SOME CIRCUMSTANCES WHERE YOU SHOULD BE SEEKING AN INJUNCTION

Designed to prevent irreparable harm and to preserve the *status quo*, injunctive relief is best suited for the following circumstances:

- Where a partner threatens to divert business to a competing entity;

- Where a partner threatens to compete with the business;
- Where a partner is misappropriating and transferring assets of the business;
- Where a partner is misusing his or her controlling interest and is diverting business assets;
- Where a partner is utilizing his or her controlling interest to lock you out of the business;
- Where a partner is utilizing his or her controlling interest to block your access to books and records;
- Where a non-controlling partner is misappropriating assets;
- Where a partner is using his or her controlling interest to engage in business actions that do not serve a legitimate business purpose;
- Where a partner engages in acts of self-dealing whereby your partner acts to advance his or her individual interests to the detriment of the business;
- Where a partner fails to perform his or her duties and threatens relationships with customers, suppliers or vendors;
- Where a partner fails to protect the intellectual property assets of the business, including, customer lists, sources of supply, contracts and other confidential information

In Chapter "3" we will discuss and review injunctions in some more detail. Chapter "3.1" includes some examples of actual Orders to Show Cause and requests for injunctive relief that I have filed on behalf of certain clients. Of course, client information and corporate information is redacted to preserve privacy. Also, not every motion for injunctive relief is successful.

IMPORTANT NOTE ABOUT INJUNCTIONS AND WHY AN INJUNCTION MAY BE A CRITICAL REMEDY FOR YOU

Partnership disputes typically involve an imbalance of control. That is, even when dealing with equal partners, one partner typically has more "hands on" control over the businesses day-to-day operations. When a dispute arises, the partner "in control" or with a "majority equity position" may misappropriate assets or attempt to exclude his or her other partners from business decisions. When this occurs and you are the partner being "locked-out" it is critical that you discuss the role of "injunctive relief" and how a New York or New Jersey court imposed restraining order may get you back in the door and in a rebalanced negotiating position. On the other hand, if you are a controlling partner faced with a minority partner, shareholder or member who is neglecting his or her duties or other wise violating his or her fiduciary obligations, injunctive relief may be equally applicable to you and, quite possibly, may strengthen your negotiating leverage.

2.4

SHAREHOLDER, MEMBER AND PARTNERSHIP AGREEMENTS: DEFINITELY IMPORTANT BUT NOT INSURMOUNTABLE

INFORMATION:

The terms of your partnership, shareholder or member operating agreement—assuming that a written agreement exists—will have an impact on your partnership dispute. This fact is unavoidable. Whether you believe that your agreement is favorable or unfavorable to your position you need to know that what you believe to be the terms of your agreement are not insurmountable. That is, many agreements are poorly drafted and the subject of much interpretation. Moreover, irrespective of the terms of an agreement and the apparent rights that one partner may or may not be believed to possess, the underlying fiduciary duties and obligations imposed on all partnership relationships may trump the terms of your agreement and provide you with an effective remedy regarding the actions of your partner.

FACTORS TO DISCUSS WITH YOUR LAWYER ABOUT YOUR PARTNERSHIP, SHAREHOLDER OR OPERATING AGREEMENT

- Whether or not an agreement exists.
- If no agreement exists, whether of not there are important emails or other written communications that relate to the operation of your business and the obligations of your partner.
- Voting control requirements for ordinary business decisions.
- Voting control requirements for extraordinary business decisions, including acts of dissolution and transfer of corporate assets.
- Buyout rights of majority and minority shareholders.
- Notice requirements for shareholder meetings.
- Rights respecting termination of officers and directors.
- Whether or not disputes require arbitration.
- Choice of law provisions: what state law applies to your dispute.
- Non-competition of partners, shareholders or members.

OPTIONS AND A PROVEN COURSE OF ACTION:

If no agreement exists, your legal rights will be governed by New York or New Jersey Law. Since fiduciary duties and rights are central to the partnership laws of both states it is not at all a negative if you do not possess an agreement. A proven course of action requires that your attorney thoroughly evaluate and "map-out" the terms of your partnership agreement, the actions of your partner and the best course of action for you. If a written partnership agreement does not exist, a proven course of action requires that your attorney thoroughly evaluate and "map-out" the legal rights and remedies offered to you under New York or New Jersey law and to apply these rights in a cohesive plan designed to preserve and advance your equity interests.

Far too many mistakes occur when attorneys just take action or worse, react, without fully understanding the unintended consequences that he or she may be triggering.

IMPORTANT NOTE ABOUT ARBITRATION PROVISIONS:

The majority of partnership, shareholder and member agreements include an "arbitration provision." That is, the agreement states that if there is a dispute between the partners, that rather than starting a lawsuit in a state or federal court, the parties must submit their dispute to "arbitration". Arbitration is an abbreviated "court like" process that is structured by private organizations such as the American Arbitration Association. Many lawyers just, reactively, include arbitration provisions in their partnership agreements based upon the erroneous belief that arbitration is less expensive than court based litigation. I happen to disagree and I believe that arbitration, many times, is more expensive and less effective than court based litigation. Nevertheless, if your agreement contains an arbitration provision it is something that must be dealt with. I commonly deal with disputes involving arbitration provisions and, although courts commonly enforce arbitration provisions, poorly drafted agreements and arbitration provisions may be challenged. *More significantly, I am a strong advocate of the litigation position that arbitration provisions cannot and do not prevent a partner from starting a court based lawsuit where that partner seeks the intervention of a court and imposition of a preliminary injunction and temporary restraining order.* Court imposed injunctions are critical in partner disputes—even where arbitration provisions exist.

IMPORTANT NOTE ABOUT CORPORATE BY-LAWS:

If you are a shareholder of a New York or New Jersey corporation, in addition to the obligations set forth in your shareholder agreement, your rights as a shareholder will be influenced by the corporation's by-laws. At the time of incorporation a corporation will, typically, adopt by-laws that, essentially, serve as the procedural rules for conducting corporate affairs such as the number of directors, notice requirements for shareholder meetings and quorum requirements for shareholder meetings. These procedural "ground rules" must be evaluated prior to and during your partnership dispute.

IMPORTANT NOTE ABOUT INTERPRETING YOUR SHAREHOLDER, PARTNER OR OPERATING AGREEMENT—DON'T GIVE UP!

The majority of partnership, shareholder and member agreements include many ambiguous provisions. More importantly, many of these provisions conflict with others. So, if you are concerned about a particular provision (such as a non-compete, buyout or majority shareholder right), don't give up since a careful review of the agreement by your attorney may provide you with agreement based defenses or countermeasures that you did not know existed.

2.5
THE DISSOLUTION THREAT

INFORMATION:

Both New York and New Jersey law provide mechanisms and procedures for the dissolution of a corporation. There are comparable provisions applicable to New York and New Jersey partnerships and limited liability companies. These "dissolution laws" play a common role in partnership disputes and require careful evaluation and consideration. In addition to New York and New Jersey's statutory "dissolution laws", your shareholder, partnership or member operating agreement may include "contract based dissolution rights". When faced with a dispute, the threat of dissolution and, possibly, the actual act of court ordered dissolution, plays an important role and may benefit one party. The party that is typically benefitted is the one who controls the intangible assets of the business such as customer and client relationships and sources of supply. If you don't control these intangible assets then great care and planning must be applied when you face a dissolution threat.

FACTORS TO CONSIDER AND DISCUSS WITH YOUR LAWYER ABOUT DISSOLUTION

- The percentage of your equity interests: are you a minority, equal or majority equity holder.

- Whether or not your shareholder, partner or member agreement includes a procedure for dissolution.

- Whether or not your shareholder, partner or member agreement includes a non-compete that may prevent you from establishing a competing business.

- Whether or not your shareholder, partner or member agreement includes buy-out provisions that could possibly be triggered by a dissolution event.

- If the primary assets of your business include real property, whether or not a real estate based partition lawsuit should be commenced or considered.

OPTIONS AND A PROVEN COURSE OF ACTION:

If you control key operational assets of the business—intangible assets that may be easily transferred to you, such as, customers, suppliers or unique sources of supply, dissolution is an option that you must consider. However, this "option" may present unintended consequences and you must ensure that (a) you do not trigger or violate a non-competition obligation, (b) you do not trigger a buyout of your equity interests, and (c) you do not expose yourself to claims related to a violation of your fiduciary duties and obligations.

IMPORTANT NOTE ABOUT THE DISSOLUTION THREAT: UNINTENDED CONSEQUENCES

Your shareholder, partner or member agreement must be carefully reviewed prior to sending only notice or filing any lawsuit or motion seeking dissolution. Why? Because, in certain instances, an application for dissolution may trigger a buyout of your own equity interest. That is, rather than dissolving your company and proceeding on your own, you may be triggering a buyout of your equity interests and possibly exposing yourself to future non-competition covenants that may take you out of your business and industry.

2.6

THE NON-PERFORMING PARTNER: HOLDING THE MAJORITY HOSTAGE

INFORMATION:

In referring to the fiduciary duties and obligations owed between partners, many times in this book, I describe a situation involving the wrongful actions of a "majority" or "controlling partner". However, this is not always the case and, many times, a minority or non-controlling partner—expecting a continued "free ride"—will engage in a pattern of non-performance, disruption or outright misappropriation. That is, one partner does everything and the other partner, the non-performing partner, just assumes that his or her time has come to sit back and enjoy the profits. Many times this non-performing partner actually believes that he or she is doing something of value when, in reality, he or she is doing nothing. These situations are extremely difficult because you are left with devoting your time, energy and efforts to a successful business, yet, your non-performing partner, who devotes much less, is receiving the same benefits. Worse, your non-performing partner may be damaging profits and creating a negative business environment for your customers and employees.

FACTORS TO CONSIDER AND DISCUSS WITH YOUR LAWYER ABOUT A NON-PERFORMING PARTNER

- The percentage of the non-performing partners equity interest: is he or she a minority, equal or majority equity holder.

- The terms of your shareholder, member or partnership agreement: does this agreement specify certain obligations and duties that must be performed by the non-performing partner.

- Whether or not the non-performing partners actions are "objectively" damaging business.

- Whether or not the non-performing partner, based on objective facts, has abandoned his or her obligations to the business.

- Whether or not the non-performing partner has engaged in acts that violate his or her fiduciary obligations, *i.e.,* has he or she misappropriated funds, failed to repay shareholder loans, misused corporate assets, overdrawn corporate accounts, or otherwise engaged in actions that jeopardize the business?

- Whether or not you control the goodwill assets associated with your business. For example, if your business is dissolved, will customers and suppliers follow your new business? If so, does your agreement include a non-competition covenant?

OPTIONS AND A PROVEN COURSE OF ACTION:

When faced with a non-performing partner, it is critical that you carefully plan a clear course of action. Consider that if and when litigation occurs, a court will be evaluating the actions that you take. So, your approach must be methodical and carefully planned with your attorney. Your approach for dealing with this partner must (i) be focused on documenting (not by attorney letter—but by letters, emails and other correspondence approved by your attorney but generated by you in the ordinary course of business) the wrongful actions or inaction of your partner, (ii) be focused on following the corporate procedures set forth in your agreement and as may be required by New York or New Jersey law, and (iii) carefully consider the preemptive advantages of filing a lawsuit and seeking injunctive relief respecting the improper or wrongful actions of your partner.

2.7

SETTLEMENT AND LITIGATION: ACTION REQUIRED PRE-EMPTION PREFERRED

INFORMATION:

Characteristic of so many partnership disputes is that fact that, many times, these disputes arise from a series of very steady but slowly developing events. That is, although you may now be faced with an accelerated event—such as a lockout, dissolution proceeding, lawsuit or buy-out offer—chances are that the underlying problem has been building for quite some time. When faced with this uncertain environment, the threat to your livelihood and the potential cost of litigation become significant issues of concern and you start to question the best course of action, *i.e.,* "do I hire lawyer", "is it necessary to start a lawsuit", "do I start a lawsuit", "how do I stop my partner", "should I negotiate" and "how do I try to work this out".

The natural inclination and approach is to try to settle and, although I am a strong advocate for cost effective out-of-court settlement, much more often than not, *settlement cannot be*

realistically and effectively unless and until you have first stabilized your negotiating position and rebalanced the partnership playing field. To do this, action is required and pre-emption is preferred. Many times the commencement of a lawsuit seeking immediate injunctive relief will serve the preemptive benefit of (i) preventing your partner from damaging the business and impairing the value of your equity interest, and (ii) mitigating the damage to you from any potential lawsuit that your partner may be planning against you.

FACTORS TO CONSIDER AND DISCUSS WITH YOUR LAWYER TO DETERMINE THE RIGHT ACTION FOR YOU

- **Negotiations are good—but only if you are negotiating from a position of strength.** Negotiations favor majority partners and partners that possess greater control over the business operations. When I am representing a controlling partner I prefer negotiations. When I am representing a minority partner or partner that lacks control over business operations, I prefer a more formal approach that first focuses on whether or not corporate formalities are being followed, *i.e.*, such as a noticed meetings, a demand for accounting and, my clients access to books and records. If this cannot be obtained, or, there is too great an imbalance between the parties, I then evaluate the potential of obtaining a court imposed injunction to preserve my clients rights, access to the business and, depending on the circumstances, to prevent the majority partner from diverting business and assets.

- **Examine what events may or may not trigger a corporate dissolution.** The threat of dissolving your corporate

entity is a serious threat and, quite frankly, one that many attorneys improperly evaluate and utilize. Consider that by triggering a dissolution event there may be many unintended consequences that involve buyout rights, non-competition covenants and the transfer of business assets. So, it is critical that any action seeking dissolution be carefully examined and planned by your attorney.

For minority and non-controlling partners, the threat of dissolution and actual acts of dissolution may be of value—but only in limited circumstances. These circumstances usually involve a corporate entity that owns valuable tangible assets (such as specialized equipment and real property) or possesses a client revenue base that is easy to identify and value, *i.e.,* such as in circumstances where your clients or customers are subject to long term contracts. However, if your partner controls the revenue base for your business, *i.e.,* if your business is dissolved your partner will be more effective at convincing your existing clients to switch to your partner's new business, then, the last thing you want—at least at the initial negotiation and litigation stage—is the dissolution of your business. Consider also that by requesting a dissolution of the business you may, inadvertently, be triggering a buyout of your own interests. Once triggering a buyout, your negotiations become limited to numbers (*i.e.,* how much your interest is worth) and, more often than not, this is an extremely weak negotiating position. A minority partner buyout trigger exists in many partnership, shareholder and operating agreements and, in certain circumstances,

under New York or New Jersey law—so be extremely careful with any threat of dissolution.

For a majority or controlling shareholder, the threat of dissolution is extremely valuable. Faced with a non-performing partner, dissolution—if properly evaluated and implemented—may serve as the most cost effective measure for proceeding.

- **Has the majority shareholder properly noticed shareholder meetings to cover and justify his or her actions?** When it comes to partnership disputes, even the small details are critically important. Meetings and votes must follow specific procedures that are mandated by law and, possibly, by your shareholder, partner or member operating agreement. More often than not, corporate and procedural formalities are ignored by majority and controlling partners. The failure to abide by these "rules" is significant for challenging the actions of the majority and seeking the intervention of the court. Once an injunction is put in place, you will have stabilized your rights and your negotiating position.

For majority and controlling shareholders, it is critical that you review, with your attorney, the corporate actions that you would like to take and that you carefully conform to the formalities required for meetings, notice and official corporate actions when it comes time to terminate or limit the rights of your partner.

OPTIONS AND A PROVEN COURSE OF ACTION:

The vast majority of partnership cases and disputes "settle". But the key question for you is when and on what terms does your case settle. *The real question is how do you stabilize your current position, rebalance the playing field and establish a position of strength that will force a certain and fair settlement. The answer? Action and pre-emption.* Action in the form of properly noticed meetings, a review of the actions of your partner, a review of the corporate structure and a review of your negotiating position. Pre-emption in the form of establishing a higher ground by serving notices and demands that demonstrate and document the impropriety of your partners actions and, potentially, the commencement of a highly accelerated lawsuit initiated by the filing of an "Order to Show Cause" wherein an emergency hearing is scheduled and demand is made for a court imposed injunction to restrain the actions of your partner and reestablish your access and rights in the business. If carefully planned and obtained, a court-imposed injunction will serve as your most cost effective asset.

IMPORTANT NOTE ABOUT ACTION, PRE-EMPTION AND THE ROLE OF LITIGATION:

The event that created your partnership dispute is the result of some type of "negotiating imbalance" that presently exists. Based on this imbalance or perceived imbalance, your partner is undertaking the actions that now threaten your business and livelihood. Before you can effectively negotiate, you must rebalance the playing field. The most cost effective way to do this, more often than not, is to take pre-emptive action through the commencement of a lawsuit. In this litigation you will file a legal application for the imposition of an emergency injunction designed to "protect the business" and "preserve your equity interest". *This type of litigation changes the entire negotiating dynamic and more often than not, accelerates the entire process and increases your odds of cost-effectively obtaining a favorable settlement.* The added benefit is that you will be protecting your business from a partner who is intent on misappropriating assets and business opportunities. I can absolutely tell you that this is an extremely effective method for proceeding and one that I have successfully implemented for my clients.

IMPORTANT NOTE ABOUT A NEGOTIATED SETTLEMENT AND AVOIDING AN EXPENSIVE TRIAL:

Leverage is critical to the successful resolution of your partnership dispute. This leverage and the "re-balancing of the playing field" can only be achieved through immediate action and, when appropriate, the commencement of litigation and the imposition of a court imposed injunction. However, once the playing field is leveled and a position of strength is established, in most, but not all instances, it is far more beneficial to reach an out-of-court negotiated settlement than proceed with a protracted, expensive and uncertain trial.

3

THE PARTNERSHIP DISPUTE TIMELINE: WHAT YOU SHOULD EXPECT AND WHEN YOU SHOULD EXPECT IT

When faced with a partnership dispute you will require answers to many questions: questions about protecting your business, the legal process, the options available to you, and, "what's next". When it comes to a partnership dispute and litigation, one of the most important roles that your attorney will undertake is to consistently inform you about the various stages of your dispute, what you should expect during the dispute, and, when you should expect it. Although every partnership dispute, like every business, is different, partnership disputes typically follow the following timeline events:

PARTNERSHIP DISPUTE TIMELINE EVENTS

1. Partnership Decline
2. Pre-Litigation
3. Litigation and Settlement
4. Litigation: Injunction Stage
5. Litigation: Post Injunction Stage
6. Litigation: Discovery Stage
7. Litigation: Motion Stage
8. Litigation: Trial Stage

In this chapter we will review each timeline event.

PARTNERSHIP DECLINE.

This is the stage is where the relationship with your business partner is on an obvious decline. Communications are limited and a confrontational meeting and outright dispute is on the horizon. You know this stage when you are in it and, if you are presently at this stage, you are probably evaluating and questioning:

- What is my next step?
- What is my partner planning?
- Can an agreement be reached?

- How do I protect my business?
- How do I protect my equity interest?
- What are my options?
- Who should I speak to?

In the earlier chapters of this book I addressed and provided answers to many of these questions and, without being too repetitive, it is again important to emphasize that your first step must be to "take action". Action to obtain information, action to learn about your options and, action to develop a proven plan.

If you find yourself in the fortunate position of truly evaluating your options and developing a plan of action during the "partnership decline" stage, I can assure you that you will have placed yourself at a significant advantage. There are significant steps—business steps—that may be taken during this stage and, when you coordinate these "business steps" with a solid legal plan, you will significantly improve your future negotiation and, if need be, litigation position.

WHAT YOU NEED TO DISCUSS WITH YOUR LAWYER DURING THE PARTNERSHIP DECLINE STAGE

- How to document the operations of your business and the actions of your partner through targeted business communications, emails and letters;
- Your legal rights under New York or New Jersey partnership, shareholder or LLC member laws;
- The strengths and weaknesses of your partnership, shareholder or operating agreement—if one exists;
- Methods to avoid a lawsuit and to structure a settlement;
- Why you must carefully document and monitor your own actions;
- How a mistake during the pre-litigation stage may cause unnecessary litigation cost and exposure;
- How to start securing the assets of your business; and
- Why pre-emption may be your best course of action.

PRE-LITIGATION STAGE

This is the stage where an outright dispute is clear and, for the first time, is acknowledged by all partners. At this stage the partnership relationship has reached a clear conflict level and your partner is now engaged in a plan and course of action that, more likely than not, is detrimental to both you and the business. Actions involving lockouts, misappropriation, diversion of business and the possible establishment of a competing business are all quite common at this stage. At this stage, actions of minority or non-controlling shareholders may take the form of business interference and deadlock as to the day-to-day decisions and operations of your business.

The steps that you take at this stage will impact your negotiations, your lawsuit and a potential settlement. Far too often, attorneys and their clients just "jump into litigation" without first planning a clear course of action. The business actions that you take during the pre-litigation stage will significantly impact your case.

WHAT YOU NEED TO DISCUSS WITH YOUR ATTORNEY DURING THE PRE-LITIGATION STAGE

- Your goals and what you believe to be the best outcome for you;
- Whether or not your goals are realistic and what it will take to achieve them;
- How you should go about conducing your day-to-day business activities and why you actions must be focused on the preservation of your business;
- Why you must avoid actions that could be mischaracterized as improper and detrimental to the business;
- The value of structuring clear written communications with your partner—even in the middle of a contentious dispute;
- How to document the improper actions of your partner; and
- Whether or not an immediate application for injunctive relief is the best course of action for you.

LITIGATION AND SETTLEMENT.

Once a lawsuit is filed you are at the "litigation stage". Litigation means that either you have filed or your partner has filed a lawsuit in either state court, federal court or before an arbitration panel such as the American Arbitration Association. There are many stages of litigation and throughout each litigation stage there are numerous events and phases where settlement negotiations may be effective. Settlement is something that must be evaluated at every pre-litigation and litigation stage. However, settlement negotiations are only effective if you operate from a position of strength that, many times, is established by effectively executing an aggressive litigation strategy. Once the playing field is leveled or, if possible, you are operating from a position of strength, settlement must be evaluated.

TYPICALLY, SETTLEMENT OPPORTUNITIES ARISE AT THE FOLLOWING STAGES:

- Just prior to the filing of a lawsuit;
- Immediately following an application for an injunction;
- During depositions and at the conclusion of discovery;
- At the conclusion of the motion stage.

THREE POINTS ABOUT SETTLEMENT

(1) If properly structured, settlement is the preferred course of action;

(2) Settlement is only effective when you act from a position of strength that is backed up by an uncompromised litigation strategy;

(3) Run of the mill litigation tactics –characterized by endless letters, endless calls between attorneys, delay and action without intensity, just waste time and money and reduce the likelihood of an effective settlement.

LITIGATION: INJUNCTION STAGE.

Not every partnership lawsuit involves a request for injunctive relief, but most should. A lawsuit by itself—without an emergency request by your attorney for injunctive relief—involves the typical filing of a complaint seeking damages. Without an application for an injunction, the filing of a complaint, by itself, presents a long and, many times, ineffective road that lacks the intensity and legal tools to protect your business and equity interests and to force a cost effective settlement.

In hostile partnership disputes, injunctive relief is an extremely effective and necessary tool. An injunction is an emergency order by a court where your partner is ordered to take certain actions and to refrain from other actions. Many times, the relief sought by an injunction is to preserve the day-to-day operations of the business and to stop a partner from engaging in

actions of misappropriation, lockout and diversion of business opportunities.

WHAT YOU NEED TO KNOW ABOUT INJUNCTIONS:

- They are effective at stabilizing your business and equity interests;
- To obtain an injunction your attorney will file an emergency motion known as an "Order to Show Cause". The name is descriptive of the process, *i.e.,* your partner is "ordered" by the court to appear at a hearing and to "show cause" why an injunction should not be granted;
- The purpose of an injunction—and therefore the relief sought in your emergency motion—is to prevent irreparable harm to your business and, thereby, your equity interests. Examples of "irreparable harm" include the harm caused by lockouts, misappropriation of assets, diversion of business opportunities, establishment of a competing business, oppression of minority shareholders and actions by non-controlling shareholders causing a corporate deadlock.
- Injunctions and good faith motions for injunctive relief—whether successful or not—tend to accelerate litigation and, in the end, may increase the likelihood of forcing a timely and effective settlement;

WHAT YOU NEED TO KNOW ABOUT INJUNCTIONS:

[*continued*]

- Courts view injunctive relief as an "extraordinary remedy" and, as such, New York and New Jersey courts set high standards for the award of an injunction. Your attorneys application for an injunction must be carefully planned, well documented and be based upon established principals of law.

- A motion for an injunction is, primarily, supported by an affidavit that your attorney will prepare for you. The most effective affidavits are those focused on objective facts and relief designed to preserve the business and its underlying assets.

- In certain cases a court will decline to grant injunctive relief. However, even if unsuccessful, you may benefit from many litigation advantages associated with filing your request for injunctive relief. The primary advantage is that your motion (even if unsuccessful) will have served to accelerate your litigation and, hopefully, will bring about a prompt and more efficient resolution of your case.

4 FACTORS TO KNOW WHEN SEEKING INJUNCTIVE RELIEF

Factor (1). When filing the Order to Show Cause, your attorney should also be filing detailed and well-reasoned factual affidavits, evidence, a memorandum of law and complaint. The factual evidence submitted and referred to in your affidavit will, typically, focus on communications and records that document the improper actions of your partner.

Factor (2). In the Order to Show Cause, your attorney will request that the court grant an immediate injunction known as a temporary restraining order ("TRO"). Since your Order to Show Cause will be prepared and filed on an emergency basis—without time for your adversary/partner and his or her attorney to prepare—the court will typically schedule a more formal hearing to occur within a one to three week period of time. If granted, the TRO will serve as a "mini injunction" for the period of time between the filing of your Order to Show Cause until the formal injunction hearing date.

Factor (3). At the injunction hearing date, the Court will conduct a formal hearing to determine whether or not the TRO will be extended and converted into a "preliminary injunction" that will restrict the actions of your partner throughout your entire lawsuit. Be prepared at this stage for significant opposition by your partner and his or her attorney. This opposition typically takes the form of "reverse allegations" that focus on and allege, essentially, that you are the one engaging in wrongful action. You must anticipate these arguments and prepare for them in your initial moving motion papers.

4 FACTORS TO KNOW WHEN SEEKING INJUNCTIVE RELIEF

[*continued*]

Factor (4). When it comes to injunctions and injunctive relief, far too often, attorneys fail to establish an effective strategy. An effective strategy is *not* one that is focused on alleging each and every wrongful action of your partner but, rather, a strategy that is focused on building credibility with the court and anticipating the typical and extremely common response that should be expected from your partner and his or her attorney. Credibility is established if the injunctive relief that you seek is focused on the preservation of your business and business assets—not harming your partner.

WHAT DOES AN ORDER TO SHOW CAUSE LOOK LIKE?

In Chapter 3.1 of this book I have included four redacted versions—two for New York and two for New Jersey—of actual Orders to Show Cause that I have filed in the course of litigation. I include this information to give you a better understanding of the legal process and what you should expect. Do not use or copy these documents and *always* refer to your attorney for the preparation of legal documents. Please keep in mind that an Order to Show Cause is not a generic document and the content of your Order to Show Cause (if one is required) must be prepared by your attorney and must be specific to the facts of your case. In the attached samples, I have redacted all client information and all reference to specific business entities. I have further revised these sample documents to remove specific injunctive relief that could be used to identify the business of my client and, possibly, his or her identification. So, please understand that he sample documents are not provided to you in their complete form.

LITIGATION: POST INJUNCTION STAGE.

What happens during the post injunction stage will depend on whether or not a preliminary injunction was issued. If a preliminary injunction is issued then your actions and the actions of your partner will be subject to and governed by the court imposed injunction order. If a preliminary injunction is not issued, what happens at this stage will depend on facts specific to your case.

Courts are extremely cautious when denying or granting preliminary injunctions. So, more often than not, injunctions are not overbearing and success during the post injunction stage and, the rest of your case, will depend on you and your attorney taking aggressive but carefully planned steps in the discovery and motion practice stages of your case.

LITIGATION: DISCOVERY STAGE.

Discovery is all about information. During the discovery stage, attorneys will prepare and serve discovery demands that, typically, take the form of documents demands, interrogatories (which are written questions that your partner must answer) and depositions. First, the parties will exchange documents related to your business and the legal claims that you have made. Interrogatories are critically important questions that your partner will be required to answer and depositions involve your testimony and your partner's testimony before a court reporter.

What you and your attorney do during the discovery stage will be critical to your entire case. Far too often, attorneys let down their intensity, preparation and effort during the discovery stage. Some attorneys get distracted and some litigants loose their desire to

stick with a well-developed game plan. I can tell you that intense and carefully calculated actions during the discovery stage will be critical for your case.

WHAT YOU NEED TO KNOW ABOUT DISCOVERY:

- Discovery can make or break your entire case. Your attorney must develop a clear and aggressive discovery plan that is focused on timely serving discovery demands, timely responding to discovery demands, and pressuring your partner and his or her attorney.
- Keep in mind that the purpose of discovery is to obtain facts and "admissible" evidence that will help you prove your case and disprove the allegations of your partner.
- Many partnership dispute cases are settled after the completion of discovery—so make sure you have approached discovery the right way.
- An effective discovery strategy is one focused on the allegations of your partner and deposition testimony where your attorney requires your partner to itemize and describe each and every claim of damages and wrongdoing.

WHAT YOU NEED TO KNOW ABOUT DISCOVERY:

[*continued*]

- Discovery is a "double edged" sword and it is critical that you thoroughly review and discuss the discovery responses that your attorney will prepare on your behalf. Before you appear for a deposition you must meet with your attorney and spend significant time preparing your deposition responses and discussing what you should expect at the deposition.
- If you take decisive action during the discovery stage, more likely than not, you will be increasing the odds of reaching a settlement favorable to you.

LITIGATION: MOTION STAGE.

Motions are requests to the court for decisions as to certain aspects of your case. Motions are typically filed after the completion of discovery. Armed with information obtained during the discovery process and the deposition of your partner, your attorney may consider filing motions to dismiss certain claims of your partner and, possibly, a motion for summary judgment as to various aspects of your case.

Like the discovery stage, it is important to pressure your partner and his or her attorney during the motion stage. Pressure prompts a favorable settlement or, at the very least, ensures that you and your attorney are well prepared for an eventual trial.

LITIGATION: TRIAL STAGE.

Trial occurs after the completion of discovery and motion stages. There are many trial variables and, depending on how your attorney structures your case, the trial will either be a jury trial (where the facts of your case are presented to a jury) or a bench trial (where the facts of your case are presented to a judge). It is critical to recognize that the vast majority of partnership cases are settled prior to the trial stage. However, if your case does proceed to trial, it is critical that your attorney prepares a detailed outline of your legal claims and the facts that will be used to "prove your case". Depending on the nature of your claims, your attorney may require the testimony of an expert witness.

3.1

EXAMPLES OF AN ORDER TO SHOW CAUSE

To provide you with a better understanding of what an Order to Show Cause looks like and how injunctive relief comes into play, in this Chapter I have included four redacted versions of actual Orders to Show Cause that I prepared and filed in certain cases. Please keep in mind that the examples that I have included (due to space limitations) are only four of the many Orders to Show Cause that I have filed. So, please keep in mind that an Order to Show Cause is not a generic document and that the content of your Order to Show Cause (if one is required) must be prepared by your attorney and must be specific to the facts of your case and the relief appropriate for your case.

In the exhibited examples of this chapter, I have redacted all client and business information. I have further revised the exhibited examples to remove specific injunctive relief that could be used to identify the business of my client or my client's identification. So, please understand that the sample documents are not provided to you in their complete form. Do not use or copy these documents and *always* refer to your attorney for the preparation of legal documents. Not every application for injunctive relief is successful, but,

if properly structured and planned, even an unsuccessful Order to Show Cause may present numerous benefits to your case.

- **Example 1 – New York Non-Controlling Shareholder.** Is a New York Order to Show Cause filed on behalf of a Non-Controlling thirty-five (35%) percent shareholder. The relief sought on behalf of this client focused on preserving his or her right to participate in the day-to-day operations of the business and to prevent continued acts of the controlling shareholders from locking my client out of the business.

- **Example 2 – New Jersey Non-Controlling Member.** Is a New Jersey Order to Show Cause filed on behalf of a member of a New Jersey Limited Liability Company. The member possessed an approximate thirty (30%) percent equity interest in the LLC and was a manager who was locked out of his or her duties and role at the company. The injunctive relief sought in this Order to Show Cause was focused on preserving his or her right to distributions and to inspect the books and records of the LLC. This application also sought the appointment of a judicial receiver and an injunction to prevent the controlling shareholders from diverting corporate funds and assets.

- **Example 3 – New York Fifty Percent Shareholder.** Is a New York Order to Show Cause filed on behalf of an equal fifty (50%) percent shareholder. The relief sought on behalf of my client related to acts of nonperformance and misappropriation by my clients equal "partner". The injunctive relief sought was focused on preserving the assets of the

underlying business and to prevent an equal shareholder from diverting assets and business opportunities.

- **Example 4 – New Jersey Fifty Percent Shareholder.** Is a New Jersey Order to Show Cause filed on behalf of an equal fifty (50%) percent shareholder. Our client was actually sued by his/her partner after our client was locked out of his/her own company. In the lawsuit we filed counterclaims and derivative claims. The nature and basis for relief related to reversing a complete lockout and diversion of corporate assets and opportunities

AFTER YOU REVIEW EACH EXAMPLE, CONSIDER THE FOLLOWING QUESTIONS FOR YOUR ATTORNEY:

- Whether or not injunctive relief is an option for your case?
- What types of injunctive relief would benefit your business?
- What types of injunctive relief would benefit your personal interests?
- What is the likelihood of successfully obtaining an injunction?
- What is the best course of action for obtaining an injunction?
- Can you benefit from the Order to Show Cause even if a court denies your application for injunctive relief?

EXAMPLE 1

New York Order to Show Cause: Non-Controlling Shareholder Oppression. This redacted Order to Show Cause was filed in New York State Court. The nature and basis for relief related to acts of minority shareholder oppression where a non-controlling shareholder with a thirty-five (35%) percent equity interest was slowly locked out of his or her duties and role at the company. The injunctive relief sought in this Order to Show Cause was focused on preserving the rights of the non-controlling shareholder, including his or her role as an employee, officer and director of the company.

At an IAS Part _____ of the Supreme Court of the State of New York, County of _____, at the Courthouse thereof, located at _____, New York on the _____ day of _____, 20____.

PRESENT: Hon. [Judges Name], J.S.C.

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF _____

[Plaintiff Name] Index No.:

Plaintiff

-against-

[Defendant Name],

Defendants

UPON reading and filing the annexed Summons, Verified Complaint, and the affidavit of _____ sworn to on the

_____ day of _____, 20____, and sufficient cause appearing therefrom,

NOW, on motion of the The Internicola Law Firm, PC, attorneys for Plaintiffs,

LET, the Defendants show cause before the Honorable [Judges Name] presiding at _____ Part _____, Room ____ to be held in courthouse located at _____, in the County of _____ and State of New York on the _____ day of _____, 20__, at 9:30 a.m. or as soon thereafter as counsel can be heard why an order should not be made and entered herein pursuant to CPLR Section 6301 *et seq.,* enjoining and restraining the Defendants, and their respective agents, employees and other persons acting on behalf of or in concert with them, during the pendency of this action, from directly or indirectly:

(i) Denying, preventing and/or interfering with the access of any and all shareholders, directors and officers of [XYZ Corp], including that of Plaintiff;

(ii) Terminating the employment and/or interfering with the duties of any shareholder and officer of [XYZ Corp], including, but not limited to Plaintiff;

(iii) Diverting, transferring selling and or encumbering any and all assets of [XYZ Corp.] that occurs outside the ordinary day-to-day operations and business of [XYZ Corp];

(iv) Modifying and/or terminating the compensation that has been commonly paid to each shareholder / officer of [XYZ Corp], including Plaintiff;

(v) Diverting client contracts and projects typically and commonly serviced by [XYZ Corp]—including new clients—to a competing company or entity; and

(vi) Such other and further relief as the court deems just and proper.

ORDERED, that pending the hearing of this application the Defendants and their respective agents, employees and other persons acting on behalf of or in concert with them, be and the same are hereby enjoined and restrained from directly or indirectly.

(i) Denying, preventing and/or interfering with the access of any and all shareholders, directors and officers of [XYZ Corp], including that of Plaintiff;

(ii) Terminating the employment and/or interfering with the duties of any shareholder and officer of [XYZ Corp], including, but not limited to Plaintiff;

(iii) Diverting, transferring selling and or encumbering any and all assets of [XYZ Corp.] that occurs outside the ordinary day-to-day operations and business of [XYZ Corp];

(iv) Modifying and/or terminating the compensation that has been commonly paid to each shareholder / officer of [XYZ Corp], including Plaintiff;

(v) Diverting client contracts and projects typically and commonly serviced by [XYZ Corp]—including new clients—to a competing company or entity; and

(vi) Such other and further relief as the court deems just and proper.

LET service of a copy of this Order and the papers upon which it is granted, together with the Summons and Complaint in this action, in any of the following manners, on or before _____, 20____, shall be deemed good and sufficient service: (i) by personal service upon the Respondent in any manner provided under CPLR Section 308, subsections (1) through (4) and (6)

E N T E R

_____

[**Judges Name**] **, J.S.C.**

EXAMPLE 2

New Jersey Order to Show Cause: Non-Controlling LLC Member Oppression. This redacted Order to Show Cause was filed in New Jersey State Court. The nature and basis for relief related to acts of minority shareholder oppression where a non-controlling LLC member with an approximate thirty (30%) percent equity interest was locked out of his or her duties and role at the company. The injunctive relief sought in this Order to Show Cause was focused on preserving the rights of the non-controlling shareholder, including his or her right to inspect books and records and to access the corporate office. This application also sought the appointment of a judicial receiver and an injunction to prevent the controlling shareholders from diverting corporate funds and assets.

Charles N. Internicola, Esq.
T: 718. 979. 8688
Attorney for Plaintiff

[Plaintiffs]

Plaintiffs,

v.

[Defendants]

Defendants,

SUPERIOR COURT OF NEW JERSEY
_____ COUNTY

CIVIL ACTION

CHANCERY DIVISION

ORDER TO SHOW CAUSE WITH TEMPORARY RESTRAINTS

(NO *EX PARTE* RELIEF REQUESTED)

THIS MATTER having been opened to the court on application of Plaintiffs [PLAINTIFF NAME], as holder of Thirty Percent of the Membership Units of [LLC NAME] and [PLAINTIFF NAME] (hereinafter collectively referred to as "Plaintiffs"), for injunctive relief pursuant to R. 4:52-1 based upon the facts set forth in the Verified Complaint and the legal argument set forth in the supporting Memorandum of Law, and the Court having considered these papers and determined that this matter may be commenced by Order to Show Cause pursuant to R. 4:52-1 and for GOOD CAUSE shown,

IT IS on this _____ day of _____, 2011

ORDERED that Defendants [DEFENDANT NAMES] (hereinafter collectively referred to as "Defendants") shall appear before the Honorable _____, at the Superior Court of New Jersey, Chancery Division, _____ County, at the _____ Justice Center, _____ New Jersey at _____ am / pm or as soon thereafter as counsel may be heard, on the _____ day of _____, 20___ to show cause why an Order should not be issued that:

a. [PLAINTIFF] be reinstated in his position as Chief Financial Officer and a Managing Member of [LLC];

b. [PLAINTIFF] be paid his salary due and owing from August, 2011 to present;

c. [PLAINTIFF] be given full and unfettered access to [LLC]'s facilities and operations;

d. [PLAINTIFF] be paid its due and owing distributions, as customarily distributed by [LLC] in the ordinary course of business, for the period of August, 2011 to present;

e. Defendants' be enjoined and restrained from interfering with [PLAINTIFF]'s full and unfettered access to the business, operations and accounts of [LLC], including but not limited to, client files and records, billing records and invoices, collection records, account statements, computer records, computer hardware, computer software, telephone numbers and/or lines, email accounts, website(s) and servers of [LLC];

f. A custodial receiver and/or fiscal agent be appointed to oversee [LLC]'s: (i) bank accounts, including receipts to and distributions by [LLC]; (ii) client files and records, (iii) day-to-day business operations, (iv) website(s) and mail accounts and (v) to conduct an accounting of [LLC]'s books and records from September, 2007 to present;

g. Defendants be enjoined and restrained from utilizing any funds of [LLC] except those necessary for the day-to-day operations of [LLC] in connection with the appointment of the custodial receiver and/or fiscal agent, the prosecution of the claims set forth in this lawsuit, and other

fees and expenses as directed or appointed by the Court appointed custodial receiver and/or fiscal agent;

h. Defendants' be enjoined and restrained from withdrawing any funds from any account owned and/or maintained by [LLC], or maintained on behalf of [LLC], without the written consent of [PLAINTIFF] and/or the Court appointed custodial receiver and/or fiscal agent; and

i. Defendants' be enjoined and restrained from removing files, computers, monies or assets from the office(s) and/or bank accounts of [LLC].

FURTHER ORDERED that pending the hearing of this application:

a. [PLAINTIFF] be reinstated in his position as Chief Financial Officer and a Managing Member of [LLC];

b. [PLAINTIFF] be paid his salary due and owing from August, 2011 to present;

c. [PLAINTIFF] be given full and unfettered access to [LLC]'s facilities and operations;

d. [PLAINTIFF] be paid its due and owing distributions, as customarily distributed by [LLC] in the ordinary course of business, for the period of August, 2011 to present;

e. Defendants' be enjoined and restrained from interfering with [PLAINTIFF]'s full and unfettered access to the business, operations and accounts of [LLC], including

but not limited to, client files and records, billing records and invoices, collection records, account statements, computer records, computer hardware, computer software, telephone numbers and/or lines, email accounts, website(s) and servers of [LLC];

f. A custodial receiver and/or fiscal agent be appointed to oversee [LLC]'s: (i) bank accounts, including receipts to and distributions by [LLC]; (ii) client files and records, (iii) day-to-day business operations, (iv) website(s) and mail accounts and (v) to conduct an accounting of [LLC]'s books and records from September, 2007 to present;

g. Defendants be enjoined and restrained from utilizing any funds of [LLC] except those necessary for the day-to-day operations of [LLC] in connection with the appointment of the custodial receiver and/or fiscal agent, the prosecution of the claims set forth in this lawsuit, and other fees and expenses as directed or appointed by the Court appointed custodial receiver and/or fiscal agent;

h. Defendants' be enjoined and restrained from withdrawing any funds from any account owned and/or maintained by [LLC], or maintained on behalf of [LLC], without the written consent of [PLAINTIFF] and/or the Court appointed custodial receiver and/or fiscal agent; and

i. Defendants' be enjoined and restrained from removing files, computers, monies or assets from the office(s) and/or bank accounts of [LLC].

FURTHER ORDERED that Defendants may file and serve any opposition papers to Plaintiffs' application by _____ 20__, and Plaintiffs shall file and serve reply papers by _____ 20__; and it is

FURTHER ORDERED that Defendants have the right to seek dissolution or modification of these restraints on two (2) days' notice; and it is

FURTHER ORDERED that a copy of this Order and all supporting papers, together with a copy of the Verified Complaint, be served upon Defendants or their representatives within _____ days of the date hereof, as set forth herein, and in accordance with R. 4:4-3 and R. 4:4-4, this being original process; and it is

FURTHER ORDERED that Proof of Service upon Defendants be filed with the Court no later than three (3) days before the return date, as set forth above, and it is

FURTHER ORDERED that Defendants file and serve upon the attorney for Plaintiffs an Answer to the Verified Complaint together with a check for $35.00 made payable to "Treasurer, State of New Jersey" within 35 days after service of the within Order and Verified Complaint upon Defendants, exclusive of the date of service. If Defendants fail to answer, judgment by default may be rendered against Defendants for the relief demanded in the Verified Complaint. Defendants shall file its Answer and Proof of Service thereof with the Clerk of the Superior Court of New Jersey, Chancery Division, _____ County at the _____

Justice Center, _____, New Jersey, in accordance with the Rules governing the Court of the State of New Jersey.

_____

[**JUDGES NAME**] **Honorable**

EXAMPLE 3

New York Order to Show Cause: Equal Shareholder.

This redacted Order to Show Cause was filed in New York State Court on behalf of an equal fifty (50%) percent shareholder. The nature and basis for relief related to acts of nonperformance and misappropriation by our clients equal "partner". The injunctive relief sought in this Order to Show Cause was focused on preserving the assets of the underlying business and to prevent an equal shareholder from diverting assets and business opportunities.

At an IAS Part _____ of the Supreme Court of the State of New York, County of _____, at the Courthouse thereof, located at _____, New York on the day of _____, 20__.

PRESENT: Hon. [Judges Name], J.S.C.

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF _____

[Plaintiffs Names] Index No.:
Plaintiffs,
against -
[Defendants Name],
Defendant.

UPON reading and filing the annexed Summons, Verified Complaint, and the affidavit of [Plaintiff] sworn to on the _____ day of _____, 20____, and sufficient cause appearing therefrom,

NOW, on motion of The Internicola Law Firm, PC, attorneys for Plaintiffs,

LET, that the Defendant show cause before the Honorable _____ presiding at _____ Part _____, Room _____ to be held in courthouse located at _____ _____, in the County of _____and State of New York on the _____ day of _____, 2011, at 9:30 a.m. or as soon thereafter as counsel can be heard why an order should not be made and entered herein pursuant to CPLR Section 6301 *et seq.,* enjoining and restraining the Defendant, and his respective agents, employees and other persons acting on behalf of or in concert with him, during the pendency of this action, from directly or indirectly:

(i) utilizing, transferring or diverting for Defendant's personal benefit or the benefit of any third party the proprietary assets of XYZ CORP (including customer lists, advertising materials, marketing plans, business plans, client information, financial data and client intake systems and procedures);

(ii) utilizing, transferring or diverting for Defendant's personal benefit or the benefit of any third party the proprietary assets of Plaintiff (including customer lists, advertising materials, marketing plans, business plans,

client information, financial data and client intake systems and procedures);

(iii) filing false documents and/or information in Defendant's alleged capacity as a member or manager of XYZ CORP in connection with any application by Pascarella for insurance and/or disability benefits; and

(iv) withdrawing funds from XYZ CORP's accounts and/or issuing checks from XYZ CORP's accounts except for the payment of ordinary and customary business expenses of XYZ CORP that are approved by Plaintiff and for such other and further relief as the Court deems just and proper.

ORDERED, that pending the hearing of this application the Defendant and his respective agents, employees and other persons acting on behalf of or in concert with him, be and the same are hereby enjoined and restrained from directly or indirectly.

(i) utilizing, transferring or diverting for Defendant's personal benefit or the benefit of any third party the proprietary assets of XYZ CORP (including customer lists, advertising materials, marketing plans, business plans, client information, financial data and client intake systems and procedures);

(ii) utilizing, transferring or diverting for Defendant's personal benefit or the benefit of any third party the proprietary assets of Plaintiff (including customer lists, advertising materials, marketing plans, business plans,

client information, financial data and client intake systems and procedures);

(iii) filing false documents and/or information in Defendant's alleged capacity as a member or manager of XYZ CORP in connection with any application by Pascarella for insurance and/or disability benefits; and

(iv) withdrawing funds from XYZ CORP's accounts and/or issuing checks from XYZ CORP's accounts except for the payment of ordinary and customary business expenses of XYZ CORP that are approved by Plaintiff and for such other and further relief as the Court deems just and proper;

LET service of a copy of this Order and the papers upon which it is granted, together with the Summons and Complaint in this action, in any of the following manners, on or before _____, 2011, shall be deemed good and sufficient service: (i) by personal service upon the Respondent in any manner provided under CPLR Section 308, subsections (1) through (4) and (6)

E N T E R

_____

[**Judge's Name**] **, J.S.C.**

EXAMPLE 4

New Jersey Order to Show Cause: Equal Shareholder.

This redacted Order to Show Cause was filed in New Jersey State Court, Chancery Division on behalf of our client who was an equal fifty (50%) percent shareholder. Our client was actually sued by his/her partner after our client was locked out of her own company. In the lawsuit we filed counterclaims and derivative claims. The nature and basis for relief related to reversing a complete lockout and diversion of corporate assets and opportunities.

CHARLES N. INTERNICOLA, ESQ.
Attorneys for Defendant/Third-Party Plaintiff

[Plaintiffs Names]	: SUPERIOR COURT OF NEW JERSEY
Plaintiffs,	: _____ COUNTY
	:
v.	: CIVIL ACTION
	:
[Defendants Names]	: CHANCERY DIVISION
Defendants,	:
_____	:
	:
[Defendant Name and Now Third Party Plaintiff]	:
	:
Third- Party Plaintiff,	:
v.	:

[Plaintiff Name and now
Third Party Defendant] :
:
Third-Party Defendant, :
_____ :

ORDER TO SHOW CAUSE SEEKING TEMPORARY RESTRAINTS

(NO *EX PARTE* RELIEF)

THIS MATTER having been opened to the Court on application of the defendant/third-party plaintiff [Defendant Now Third Party Plaintiff Name] for injunctive relief pursuant to R. 4:52-1 based upon the facts set forth in the Certification of _____, sworn to on the 31st day of December 2010, the Verified Answer and Counterclaims and the legal argument set forth in the supporting Memorandum of Law, and the Court having considered these papers and determined that this matter may be commenced by Order to Show Cause pursuant to R. 4:52-1 and for good cause shown,

IT IS on this _____ day of _____, 20_____

ORDERED that plaintiff / third-party defendant _____ shall appear before the Honorable [JUDGE'S NAME] , Superior Court of New Jersey, Chancery Division, _____ County at the Courthouse in _____, New Jersey at _____ am pm , or as soon thereafter as counsel may be heard, on the _____ day of _____, 20_____, to show cause why an Order should not issue to:

(a) Enjoin and restrain the plaintiff _____ from interfering with _____'s full and unfettered access to all business records and accounts of the [XYZ Corp], including but not limited to, client files and records, billing records and invoices, collection records, account statements, computer records, computer hardware, computer software, telephone numbers and/or lines, email accounts, website and servers of the [XYZ Corp]

(b) Appoint a custodial receiver and/or fiscal agent to oversee the [XYZ Corp]: (i) bank accounts, including receipts to and distributions by the [XYZ Corp], (ii) [computer] system, (iii) client files and records and (iv) website and mail accounts, and to conduct an accounting of the [XYZ Corp]'s books and records from January 2005 to present;

(c) Enjoin and restrain plaintiff _____ from hiring and/or discharging employees and/or independent contractors of the [XYZ Corp];

(d) Order that the plaintiff _____ retroactively reinstate _____'s family health insurance plan and that plaintiff _____ be enjoined from cancelling, modifying or in any way altering _____'s family health insurance plan;

(e) Enjoin and restrain plaintiff _____ from utilizing any funds of the [XYZ Corp] except those necessary for the day-to-day operations of the [XYZ Corp] in connection with the appointment of the custodial

receiver and/or fiscal agent, the prosecution of the claims set forth in this lawsuit, and other fees and expenses as directed or appointed by the Court appointed custodial receiver and/or fiscal agent;

(f) Enjoin and restrain plaintiff _____ from withdrawing any funds from any account owned and/or maintained by the [XYZ Corp] or maintained on behalf of the [XYZ Corp] without the written consent of _____ and or the Court appointed custodial receiver and/or fiscal agent;

(g) Enjoin and restrain plaintiff _____ from contacting any clients of the [XYZ Corp] for any purpose not related to the ordinary day to day business of the [XYZ Corp] in regard to the rendering of market research service;

(h) Enjoin and restrain plaintiff _____ from removing files, computers, monies or assets from the office(s) and/or bank accounts of the [XYZ Corp]; and

(i) Order that plaintiff _____ reinstate the original website containing information about _____; and it is

FURTHER ORDERED that plaintiff _____ shall file and serve any opposition to defendant _____'s application by _____; and defendant _____ shall file and serve reply papers by _____; and it is

FURTHER ORDERED that plaintiff _____ have the right to seek dissolution or modification of this restraint on two (2) days' notice; and it is

FURTHER ORDERED that a copy of this Order and all supporting papers, together with a copy of the Verified Answer and Counterclaims be served upon the Plaintiffs or their representatives within _____ days of the date hereof, as set forth herein, and in accordance with R. 4:4-3 and R. 4:4-4, this being original process; and it is

FURTHER ORDERED that Proof of Service upon Plaintiffs be filed with the Court no later than three (3) days before the return date, as set forth above.

_____

Honorable [Judge's Name], P.J.Ch.

4

MINDSET AND THE ADDITIONAL CHAPTERS OF THIS BOOK

Since information is critical—critical to selecting the right attorney, asking the right questions and adopting the right course of action, I address additional partnership dispute topics and issues in the chapters that follow. These chapters deal with important topics, including, "How to Get Started with Your Attorney", documents and information that your must review with your attorney and, important legal remedies and rights under New York and New Jersey law. Some of these chapters have application to all disputes and some are fact and state specific. However, even if a particular chapter may not have direct application to your situation *(i.e.,* the chapter relates to an issue of New York law or deals with a corporation and you are a member of an New Jersey limited liability company), you should nevertheless read the chapter as it will give you a better idea and understanding of the numerous legal vehicles and options that play a role in partnership disputes. Hopefully, at a minimum, these chapters will better inform you and give you ideas and questions to discuss with your attorney.

IMPORTANT NOTE ABOUT NEW YORK AND NEW JERSEY LAW: FIDUCIARY RIGHTS APPLY

Keep in mind, that although the laws of New York and New Jersey are definitely different, they share many common components and, most significantly, both New York and New Jersey law recognize and impose the critically important fiduciary duties and obligations that we have discussed.

CHAPTER 4 TOPIC INDEX

4.1

PARTNERSHIP DISPUTES: IMPORTANT FACTORS TO DISCUSS WITH YOUR LAWYER

[NEW YORK AND NEW JERSEY]

The unfortunate reality for far too many business owners in New York and New Jersey is that the greatest threat to your business may be a dispute with your own business partners. After years of hard work and success, partnership and shareholder relations are many times tested due to disputes over business decisions, cash flow shortages, economic pressures caused by a change in a partner's "personal life" and, even, the prospect of greater business success. If you are experiencing a serious dispute with your partner that is escalating and affecting your business operations, you must implement immediate measures to secure your business and the equity interests that you have worked long and hard to establish.

FACTORS TO DISCUSS WITH YOUR LAWYER:

When faced with a partnership dispute in New York or New Jersey, critical factors that you should discuss with your business lawyer include:

- **The Tactical Role of Litigation.** Although it may sound counter-intuitive, when faced with a partner misappropriating funds, misappropriating business assets or diverting business, early and aggressive action (that is starting a lawsuit and seeking an injunction) will not only serve to protect your business interests but, long term, will reduce your overall litigation costs and increase the likelihood of reaching a negotiated settlement. When it comes to partnership disputes, indecisive and half-hearted measures only lead to prolonged, non-productive litigation and unnecessary legal fees. Decisive action will preserve your business and expedite the settlement process.

- **Injunctions are Critical Remedies that must be Evaluated.** Partnership disputes typically involve an imbalance of control. That is, even when dealing with equal partners, one partner typically has more "hand's on" control over the businesses day-to-day operations. When a dispute arises, the partner "in control" may misappropriate assets or attempt to exclude his or her other partners from business decisions. When this occurs and you are the partner being "locked-out", it is critical that you discuss the role of "injunctive relief" and how a New York or New Jersey court imposed restraining order may get you back in the door and in a better negotiating position.

- **Ultimately a Negotiated Settlement – Not an Expensive Trial will Produce the Best Result.** Leverage is critical for the successful resolution of a partnership dispute. This leverage and the "re-balancing of the playing field" can only be achieved through immediate action and, when appropriate, the commencement of litigation and the imposition of a court imposed injunction. However, once the playing field is leveled and a position of strength is established, in most instances, it is far more beneficial to reach an out-of-court negotiated settlement than to proceed with a protracted, expensive and uncertain trial.

If your business is stable and your dispute does not involve the misappropriation of assets, an emergency situation or a partner "lock out", settlement discussions (not litigation) should be the preferred course of action. To be successful, negotiations must be based on a well-defined strategy that your lawyer establishes after evaluating your partnership agreement, shareholder agreement, by-laws and corporate agreements.

4.2

PARTNERSHIP DISPUTES: WHAT ARE THEY REALLY ABOUT?

[NEW YORK AND NEW JERSEY]

Although every business is different and every partnership dispute unique, there are, nevertheless, core characteristics that are common to almost all partnership disputes. These core characteristics relate to an unbalanced business relationship and the actions of either an overreaching or underperforming partner. These core characteristics, include:

- **An Unbalanced Business Relationship.** As a business progresses, over time, partners and shareholders take on different roles in operating, managing and funding the underlying business. Disputes typically arise when one partner or shareholder, over time, loses sight of his or her day-to day obligations to the business. Basically, one partner or shareholder ends up doing more for the business while the other takes the business for granted.

- **Personal Disruption.** Many times a "partnership dispute" has nothing to do with your business and has everything to do with changed circumstances involving your partner's personal life. Good or bad, many "partnership disputes" arise due to various pressures and changes that your partner may experience in his or her personal like.

- **Misappropriation and Fraud.** Although unclear and not easily determined, many, many "partnership disputes" are a function of fraud and the misappropriation of business assets and opportunities. Actions that may have appeared to be benign for many years may only now be recognized as acts of fraud and misappropriation.

Ultimately, "partnership disputes" are always about an imbalance in the business and partnership relationship. Whatever the cause, it is critical that you carefully evaluate your business and partnership interests. Start with your partnership or shareholder agreement. If you don't have an agreement (something that is quite common for closely held businesses) understand that the partnership laws in both New York and New Jersey will, nevertheless, afford you legal remedies to "rebalance" your partnership relationship or, if necessary, terminate the relationship. There are options.

4.3

PARTNERSHIP DISPUTES: GETTING STARTED WITH YOUR ATTORNEY

[NEW YORK AND NEW JERSEY]

For partners, shareholders and members of closely held businesses in New York and New Jersey there are a number of legal options and remedies available to you when faced with a "partnership dispute".

These legal remedies and options are a function of:

1. The terms and provisions of your written partnership, shareholder or member operating agreement—if you have one, *and*

2. The "statutory" protections and rules that will be afforded to you under New York's or New Jersey's partnership and shareholder laws.

Many times, business owners—and sometimes their legal counsel—act too quickly and without a full evaluation and assessment of the contractual and legal options that are available to you and

how these contractual and legal options may be combined to offer you the best avenue for relief.

So, when faced with a partnership dispute, some of the factors and information that you should be assessing and evaluations with your legal counsel, include:

- **Your Shareholder, Partner or Member Agreement.** For many apparent reasons, an honest assessment of your legal rights must start with an evaluation of your shareholder, operating or partnership agreement. If you don't have an agreement, it is important to understand that your situation is quite common (*i.e.*, many "partners" never formalize a written agreement) and that you will nevertheless be afforded legal rights, remedies and options under the applicable "statutory" laws in New York and New Jersey.

- **Relevant Writings.** What are relevant writings? These are the written communications (letters, emails, and invoices) that document, support or contradict the claims and rights that you will be asserting. For example, do you have emails discussing your partnership or how profits are divided? Do you have letters discussing salaries? Do you have "unsigned copies" of the partnership or shareholder agreement that you were negotiating? It is always better to be over inclusive when initially reviewing your legal options with your attorney. Documents that may seem inconsequential could have a positive impact on your case.

- **Tax Returns.** Federal tax returns (especially schedule K-1 for S corporations) are extremely informative and serve

as an important analytical tool that should be initially reviewed with your attorney. Don't be surprised if your tax returns contain errors or inaccurate information that you were unaware of—it happens often.

- **Corporate Records.** Your "corporate records" including your stock/member certificates, corporate by-laws and resolutions contain important information that should be initially assessed.

These documents, if they exist, will serve as a critical base of information that must be assessed and evaluated with your attorney. Once evaluated, you should discuss, in detail, the options available to you and the best course of action.

Remember, if you think a document is important, it probably is.

4.4

PRESERVING YOUR BUSINESS ASSETS WHEN FACED WITH A PARTNERSHIP DISPUTE

[NEW YORK AND NEW JERSEY]

When faced with a partnership or shareholder dispute that challenges the continued viability and existence of your business, it critical that you assess and preserve (fairly) the assets of your business. Consider the following:

- **Maintenance of Day-to-Day Operations is Imperative.** Shareholders and partners owe a fiduciary and, potentially, a contractual obligation respecting the maintenance and preservation of business assets. If you are faced with a partner engaged in the misappropriation or dissipation of corporate assets, speak with your litigation attorney to discuss the necessity of obtaining a preliminary injunction and temporary restraining order. If the partnership dissolution is "amicable" (or at least manageable) speak to your attorney about developing a preliminary agreement respecting the continued operations of your business

pending a final agreement respecting either a buy-out or the dissolution and distribution of your businesses assets.

- **The Significance of "Intangible Assets".** For both service and product based businesses, the most valued asset that your business possesses, most likely, will be the intangible assets associated with your clients, customers and suppliers. Examples of intangible assets that you must evaluate and protect, include:

    - Customer lists
    - Sources of supply
    - Pricing and cost information
    - Customer contracts and agreements
    - Trademarks
    - Patents
    - Goodwill associated with a business location

- **Prepare an Asset List.** Prior to consulting with your attorney, prepare a list identifying the tangible and intangible assets associated with your business and the potential value of these assets to you and your business partner. Also, consider the value of contractual rights and agreements, such as a favorable lease agreement.

- **Your Partnership Agreement is Critical.** Always maintain a current copy of your partnership, shareholder or operating agreement. If you have signed one of these agreements, chances are, that your rights respecting the potential dissolution of your business and the distribution of your business assets will be governed by the terms of your agreement. It is imperative that you provide your attorney with a copy of your agreement. If your agreement is missing or was misplaced, let your attorney know.

- **Decisive Action is Critical.** If you act promptly with a well-developed plan and clear communications with your attorney and, eventually, your business partner, the opportunity for success is greatly enhanced. Prompt action is necessary to avoid what may amount to the protracted dissipation and possible misappropriation of business assets and lost goodwill. Prompt action mitigates against the likelihood of unnecessary litigation and legal fees.

4.5

FIDUCIARY DUTIES AND OBLIGATIONS BETWEEN PARTNERS, SHAREHOLDERS AND MEMBERS

[NEW YORK & NEW JERSEY]

If you are a partner or shareholder of a New York business and you are faced with a "partnership dispute" it is important that you understand your legal rights, including the "fiduciary duties and obligations" owed between the partners and shareholders of closely held New York and New Jersey corporations and partnerships.

- **A Duty of Good Faith and Loyalty.** In addition to the legal rights and obligations defined and created by your partnership, shareholder or member agreement (if one exists), the legal rights and obligations between shareholders, partners and members of a New York and New Jersey businesses are governed, substantially, by the common law fiduciary duties and obligations imposed by New York and New Jersey courts. Under both New York and New Jersey law, partners, shareholders and members owe a fiduciary

duty and obligation to one another and to their mutually owned business. These fiduciary duties and obligations impose on each partner, shareholder and member an undivided duty of loyalty and good faith when maintaining and dealing with the assets of the business.

- **A Partners Common Law Fiduciary Duty Precludes a Partner From:**
    - Misappropriating assets belonging to the company;
    - Diverting assets belonging to the company; and
    - Misappropriating "business opportunities" belonging to the company.

From a tactical standpoint, the invocation of your common law rights as a "fiduciary" (both on your own behalf and on behalf of your company) may be utilized to maintain your business as a going concern and prevent your partner from diverting business assets and business opportunities.

4.6

THE TACTICAL ROLE OF DISSOLUTION

[NEW YORK & NEW JERSEY]

When faced with a "serious dispute" and conflict with your shareholders—that is a dispute that jeopardizes the continued profitability of your business and livelihood—shareholders and partners of small closely held New York and New Jersey corporations must consider their rights under the applicable New York or New Jersey dissolution laws. In particular, you must evaluate your ability to commence an emergency proceeding (commenced by the filing of an "Order to Show Cause") respecting injunctive relief and the dissolution of your business.

FACTORS TO CONSIDER INCLUDE:

- **The Necessity of Preserving Your Livelihood.** The majority of New York and New Jersey "corporations" are comprised of small closely held businesses with two to six shareholders. For these small businesses, chances are that your livelihood is tied to the continued existence of your business. If you are faced with a dispute with your partners, you may face the threat or realistic possibility that

your partner is misappropriating and diverting assets and clients of your business for his or her personal benefit. If this is a situation that you face, it is critical that you take immediate measures to "secure" the assets of your business and prevent the diversion of assets. One critical tool available to you relates to the dissolution rights afforded to you under New York and New Jersey law.

- **Emergency Dissolution Proceeding.** When faced with actual or threatened improprieties by your partner (i.e., the establishment of a competing business or the diversion of corporate assets) it is critical to consider the substantive and strategic benefits afforded under New York Business Corporation Law Section 1106. For New York Corporations, Section 1106 affords aggrieved shareholders the right to an "emergency judicial dissolution proceeding" commenced by the filing of an "order to show cause". The benefits of commencing a Section 1106 proceeding relates to the emergency nature of the procedures and the immediate hearing before a court wherein an aggrieved shareholder or partner could avail himself or herself of the following interim relief:

    - Temporary restraining order prohibiting your partner from establishing a competing business;

    - Temporary restraining order preventing your partner from diverting customers and assets of your business;

    - The appointment of a "receiver" to account for and oversee the assets of your business pending litigation.

NOTE: The request for the appointment of a receiver must be carefully evaluated and should only be used in limited circumstances when necessary; and

- Order directing an accounting of all funds and assets of your business.

There are additional "fact specific" remedies that should be considered and discussed with your attorney. Although "dissolution" is a drastic remedy, this right and the advantages of commencing on emergency hearing under BCL Section 1106 represents a critical tool for an aggrieved shareholder to recapture control over his or her own business. For New Jersey shareholders and members, there are comparable provisions and dissolution laws similar to New York.

4.7

DISSOLUTION BY A FIFTY PERCENT SHAREHOLDER WHEN FACED WITH CORPORATE DEADLOCK

[NEW YORK]

If you are the owner of a small closely held corporation in New York and are faced with a dispute with your partners and a "corporate deadlock", it is critical that you understand your dissolution rights under New York law.

Important factors that you must evaluate and discuss with your lawyer include:

- **Initial Corporate Agreements Are Critical.** Your legal rights as a shareholder, officer and director will be impacted by the terms, if any, of your shareholder agreements, by-laws and certificate of incorporation. In many instances, these documents may expand or limit the legal rights that might otherwise be available to you under New York law.

- **Director and Shareholder Deadlock: Grounds for Dissolution.** Pursuant to section 1104(a) of the New York Business Corporation Law if you are a fifty percent (50%) shareholder, you may petition the court to dissolve your New York Corporation based on one of the following grounds:

    - That the directors are so divided respecting the management of the corporation's affairs that the votes required for action by the board cannot be obtained.

    - That the shareholders are so divided the votes required for the election of directors cannot be obtained.

    - That there is internal dissention and two or more factions of shareholders are so divided that dissolution would be beneficial to the shareholders.

When faced with shareholder disputes and situations of corporate deadlock, the dissolution rights provided under New York law serve as a critical vehicle to protect your overall equity ownership interests and rights.

4.8

DISSOLUTION BY A MINORITY SHAREHOLDER

[NEW YORK]

Minority shareholders who own and hold between 20% to 49% of the outstanding shares of stock in a New York corporation are afforded the critical right to seek "judicial dissolution" under New York Business Corporation Law Section 1104(a). Pursuant to Section 1104(a), a minority shareholder or shareholders who own and control at least 20% of the corporations stock may seek dissolution based on one of the following grounds:

(1) The directors or those in control of the corporation have been guilty of illegal, fraudulent or oppressive actions toward the complaining shareholders;

(2) The property or assets of the corporation are being looted, wasted, or diverted for non-corporate purposes by its directors, officers or those in control of the corporation.

For minority shareholders of small closely held businesses, the dissolution rights afforded under Section 1104(a) represent a substantive legal right that must be evaluated when faced with a serious dispute with your partners and shareholders.

4.9

DISSOLUTION OF YOUR NEW YORK CORPORATION: PROCEDURAL REQUIREMENTS THAT MUST BE FOLLOWED

[NEW YORK]

In Chapter 4.6 we discussed the "tactical role" of commencing a dissolution proceeding and the significant benefit that New York Business Corporation Section 1106 affords aggrieved shareholders. Once the proprietary of Section 1106 has been evaluated with your lawyer, consideration must be given to the following procedural requirements to commence a dissolution proceeding:

- **Right to Commence an Order to Show Cause and Seek an Emergency Proceeding.** The greatest benefit of Section 1106 that is afforded to an "aggrieved" shareholder is the ability to commence an emergency hearing and proceeding. Rather than being forced to wait weeks and even months, Section 1106 affords shareholders the right to an immediate hearing wherein the court (if the case is commenced properly) is granted the jurisdiction

and authority to grant a temporary restraining order. The method for obtaining this "emergency relief" is achieved by filing a "order to show cause" (*See*, Chapter 3).

- **Dissolution in Four Weeks?** Although the dissolution process may take some time—especially in more complex cases. The benefit of section 1106 is derived from the fact that at the initial emergency hearing the court may award "injunctive relief" to preserve the assets of your business. Pursuant to section 1106 (a) the order to show cause must proscribe a proposed dissolution date to take place not less than four (4) weeks from the date of the emergency hearing when the court signed your order to show cause;

- **Publication Requirements.** Pursuant to section 1106(b) the order to show cause must proscribe a notice of dissolution to be published "at least once in each of the three weeks before the time appointed for final dissolution";

- **Service on State Tax Commissioner.** Pursuant to Section 1106 (c) a copy of the order to show cause must be served on the New York State tax commission and the shareholders of the corporation.

4.10

DISSOLUTION BY MINORITY SHAREHOLDERS FACED WITH ACTS OF OPPRESSION

[NEW YORK]

If you are a minority shareholder in a closely held New York corporation, chances are, that you have limited input in the management and affairs of the business that you "partially own". The typical minority shareholder is a passive investor looking to achieve a reasonable rate of return on his or her capital investment. For the minority shareholder, depending on the terms and conditions of your shareholder agreement, your ability to influence business operations (including asset sales, employment contracts, loan obligations and other long-term obligations) may be limited or, even, non-existent.

However, under New York law, when minority shareholders—owning and controlling no less than twenty (20%) percent of the stock—are faced with acts of corporate abuse and misappropriation of corporate assets, they are granted the legal right to petition the courts for a corporate dissolution.

Legal Rights and Remedies: Threat of Corporate Dissolution. This is a critical right afforded to minority shareholders and is designed to prevent majority shareholders from abusing their controlling interests.

Pursuant to Section 1104(a) of the New York Corporate Business Law, shareholders "representing twenty percent or more of the votes of all outstanding shares of a corporation..." may present a petition of dissolution on one or more of the following grounds:

- The directors or those in control of the corporation have been guilty of illegal, fraudulent or oppressive actions toward the complaining shareholders; or

- The property or assets of the corporation are being looted, wasted or diverted for non-corporate purposes by its directors, officers or those in control of the corporation.

4.11

MINORITY SHAREHOLDER RIGHTS: THE NEW JERSEY OPPRESSED SHAREHOLDER STATUTE

[NEW JERSEY]

For shareholders of small closely-held New Jersey corporations, New Jersey law, and, in particular, the New Jersey "Oppressed Shareholder Statute (N.J.S.A. 14A: 12-7), afford a number of legal remedies that you must be aware of when faced with a shareholder dispute. Shareholder disputes are serious and, in most instances, will impact your business and the financial well being of your family. So, when faced with the first sign of a "problem", it is critical that you evaluate your options with an experienced attorney. One such option that you must consider is the New Jersey Oppressed Shareholder Statute and the "substantial" rights and leverage that it affords. Under this statute, an "aggrieved or oppressed" shareholder may seek injunctive relief, the appointment of a fiscal agent and, in certain instances, the buyout of his or her equity interest. Some factors to consider, include:

- **New Jersey's "Oppressed Shareholder Statute"("OSS").** This is a critical tool that must be "timely" evaluated when faced with a dispute with your shareholders. Information you need to know about the OSS:

    - Under OSS even fifty percent (50%) shareholders may qualify as a "minority status shareholder" entitled to protection;

    - When faced with wrongful acts of a shareholder—even a fifty percent shareholder—OSS may provide you with the legal right to sell your shares or buyout the interests of the other shareholder; and

    - Under OSS, the court may order the sale of your company to a third party.

While it is *almost always* preferable to avoid litigation, it is nevertheless critical that you immediately evaluate your legal rights and establish a litigation plan.

4.12

RIGHT OF DISSOCIATION: A SIGNIFICANT TOOL IN NEW JERSEY LLC MEMBER DISPUTES

[NEW JERSEY]

In the state of New Jersey there are various laws and legal decisions that address partnership and shareholder rights and the legal remedies that may be available to you. The legal "rights" available to you will vary depending on the nature of your equity and ownership interests. That is, are you a shareholder in a corporation, a partner in a partnership or a member in a limited liability company? The answer to this question will present different options and legal remedies that may be available to you.

One legal right and option that members of New Jersey limited liability companies must be aware of relate to the "right of dissociation" of an LLC member. If you are a member of a New Jersey limited liability company and you are faced with a serious dispute with your other member(s), it is critical to be aware of and understand the "right of dissociation" that may be available to you under New Jersey law, N.J.S.A. 42:20-24. The New Jersey

"dissociation statute" was designed to protect LLC members from economic harm that may be caused to the LLC by a fellow member. Under the dissociation statute, in certain instances, you may be permitted to terminate a member's interest in your LLC. This is a significant right that is difficult to invoke but nevertheless a legal remedy that you must be aware of and evaluate when faced with a membership dispute.

5

ONE LAST THOUGHT

When faced with a serious partnership dispute, there are many questions and concerns that you will be presented with. So much so, that I am sure that there may be a tendency for you to over evaluate "potential" bad events that may or may not occur. This is normal. However, having helped many clients negotiate this uncertain path, I can tell you that if you deal with the "task at hand" and follow a proven approach—one focused on pre-emption, action and a step-by-step plan—you will successfully navigate this hazard and protect your business and livelihood.

When this dispute is behind you, you may very well look back on this event as a somewhat positive opportunity that led you to a path for future success.

ABOUT THE AUTHOR

CHARLES N. INTERNICOLA is a shareholder and partnership litigation attorney who represents and advises New York and New Jersey business owners, shareholders, members and partners when they are presented with a serious "partnership dispute". Mr. Internicola possesses a significant track record of counseling and representing his clients both, in the courtroom and, when appropriate, at the negotiating table. Mr. Internicola also counsels and advises his clients on issues of corporate governance, partnership agreements, and the structuring of partner and shareholder buyouts.

Many of Mr. Internicola's articles and publications about New York and New Jersey partnership and shareholder laws are published at www.NewYorkandNewJerseyPartnershipLawyer.com.

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