PRESCRIPTION FOR SANITY IN RESOLVING BUSINESS DISPUTES: CIVIL COLLABORATIVE PRACTICE IN A BUSINESS RESTRUCTURING CASE

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One of the ideal target markets for the application of Collaborative Law ("CL") in civil disputes (i.e. disputes other than divorce or family law cases) is the closely-held or family business dispute. The dispute that is the subject of this article is that of a closely held corporation owned by four partners. The successful use of CL in this case, one of the first truly collaborative civil cases using the purist CL model, validated our views and gave us an excellent case to analyze in this article.

Summary of the case:

This collaborative case involved the break up and restructure of an "S" Corporation incorporated in Massachusetts by the four original and equal shareholders. The four shareholders also constituted all the directors and officers as well as key employees of the corporation, thus making the entity a "closely held corporation" under Massachusetts law. As legal counsel reminded the parties on several occasions, the shareholders/directors/officers in a closely held corporation owe fiduciary type duties to each other under the Commonwealth's common law.

The profitable business in question had grown over five years to gross revenues of approximately $1 million and provided computer and software consulting services to the life science industry. No shareholder agreement existed at the time that three of the shareholders informed the fourth shareholder that a restructuring (buy out) needed to take place due to "irreconcilable differences" that did not reflect questions concerning the fourth shareholder's technical competence, work ethic, or new client development acumen. Nonetheless, it was a painful and difficult revelation for the fourth shareholder to hear. As part of the CL settlement included a confidentiality agreement, the name of the corporation as well as the four partners will remain confidential. However, the clients were so satisfied with both the CL process and the result, they volunteered to offer us quotes of their views and authorized us to use them in articles about the case.

The case raised both business and employment issues; and the solutions memorialized in the written restructuring agreement ("RA") included typical business law elements (restructuring, stock buy out, non-competition and software reseller agreements) as well as employment considerations. Using CL, the parties and their attorneys were able to navigate through the departure of one of the shareholders, the restructuring of the original corporation ("OC"), the compensation of the minority shareholder/departing shareholder ("MS/DP") for his equity and final employment wages, the creation of a new company by the MS/DP (with the cost of incorporation funded by OC). The parties

also laid the groundwork for a joint public announcement, continuing cooperation and productive relationships between the two businesses after the separation. The CL process began shortly after the dispute arose, in January, 2007 and was successfully concluded in May, 2007. Legal fees incurred by all parties and the elapsed time to resolve the dispute were both a fraction of what would have been required in litigation.

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The Process:

The co-authors were the two CL lawyers in this case, both members of the Massachusetts Collaborative Law Council ("MCLC"). R. Paul Faxon of The New Law Center in Cambridge, MA represented the OC and three continuing shareholders of the OC (to also be referred to herein as "OC"). Michael Zeytoonian of Hutchings, Barsamian, Mandelcorn & Zeytoonian in Wellesley Hills and Westborough, MA represented the MS/DP. Faxon, who had been the OC lawyer since its inception, suggested the idea of using CL to all four shareholders as an alternative way of working through the dispute rather than litigation. The four shareholders agreed to consider using this approach and Faxon took the valuable opportunity presented to provide all parties with contact information on CL lawyers, including Zeytoonian in particular. After an initial meeting between the MS/DP and Zeytoonian as his lawyer in which Zeytoonian informed the MS/DP on the CL process and the differences between it and litigation or arbitration, the MS/DP retained Zeytoonian as his CL counsel. Then the three remaining shareholders of the OC confirmed Faxon's retention. All four shareholders gave their informed, written consent to Faxon's representation of the three remaining OC shareholders.

This was a pure CL case and process that incorporated the many elements of CL. The parties agreed to use best efforts to refrain from litigation. The lawyers affirmed their Collaborative Commitment by agreeing that their representation of the clients would be limited only to the collaborative process and would not extend to serving as litigation attorneys should the CL process fall short. The parties also agreed to the open and voluntary exchange of all relevant information; the use of interest-based, non-adversarial negotiation at all times in the CL process; the use of two shared neutrals in the form of independent and jointly retained business valuators; respectful and civil behavior and communications at all times; six-way meetings; confidentiality; and the collaborative development of options that would serve the interests of all parties and facilitate a final resolution. These agreements and commitments were reflected in a written process agreement signed by all parties and both lawyers, which became an exhibit to the RA.

Description of the CL process

After Faxon explained the CL process to the four shareholders, both Faxon and

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Zeytoonian took the time to further explain the CL process to their respective clients separately and answer any questions and review the pros and cons of the CL process and the litigation process. The separate informed consent of the parties was important, particularly in the case of the MS/DP, so that he would recognize that his rights and interests were being protected and represented in a process that was not adversarial.

The CL process included several pre-meeting planning conferences and de-briefing conferences between the two lawyers. Two six-way meetings took place among counsel and the four shareholders; the first lasting about 2 hours and the second lasting nearly 6 hours. Rather than present a chronology or a play-by-play, this article focuses on some of the highlights of using the CL process in this case, some "Monday morning quarterback" observations and some lessons learned.

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As part of the advance planning for the first six-way, the lawyers jointly developed an agenda and determined that the meeting should be held in Zeytoonian's office, because as the party being asked to leave the OC by the majority of other shareholders, it was important that the meeting was held on MS/DP's "home turf". The lawyers carefully planned the agenda, determined who would present what and determined how and when to actively engage the parties in presenting and assessing issues and concerns. Once the stage was properly set with advance planning, discussions in the six-ways flowed fairly freely and openly.

Joint experts were utilized efficiently and made important contributions to reaching a resolution. While neither joint expert was present for the six-way meetings, the findings of both joint experts were available prior to and presented at the second six-way meeting and were useful to the parties in determining business value, the basis for the valuation and the MS/DP's share of the value. The parties agreed to jointly hire an accounting expert to give an independent limited valuation of the business for the purposes of the collaborative process. They later agreed to hire a second valuation expert, also retained jointly, to offer a second, more formal appraisal and to approach the business valuation from a different perspective. Both CL attorneys encouraged the parties to meet independently with the two experts, which was done before the second six way meeting.

The work of the parties outside of the six-way meetings was critical to advancing

the CL process and in reaching a deeper, more lasting resolution. Both Faxon and Zeytoonian gave the clients joint "homework" assignments during the process. These included discussing and reaching an agreement on how the company's existing clients would be divided, developing a set of public "talking points" to address the restructuring; and setting a discounted rate for MS/DP to resell certain difficult-to-value software being retained by OC. The counselors asked the parties to think about how a reseller agreement might look, anticipating the need for the parties to continue to work together as two separate companies and entities, servicing the same clients.

Before the first six-way, Zeytoonian met with his client, the MS/DP, to get acclimated, to discuss format and environment for meeting. Zeytoonian suggested that MS/DP decide ahead of time where he and his counsel should sit. MS/DP wanted to be facing his lawyer across the table and not next to him, but next to his fellow shareholders. Zeytoonian decided to position himself in the middle of the table opposite his client. During the six-way meetings, the two lawyers sat side by side, four shareholders sat next to each other along an oval table. Counsel for MS/DP purposely took the two "head" and "foot" chairs off the table before the meeting began. Drinks, coffee, tea and light refreshments were on the table for the first six-way meeting. This meeting began around 2 p.m. with a pre-determined decision to end no later than 5 and a goal of ending by 4 p.m. or whenever it became clear that the point of diminishing returns had been reached. (The meeting did end precisely at 4 p.m.)

The second six-way meeting began around 5:30 p.m. and dinner was brought in for this longer meeting, which went deep into the night. Both CL counsel did not hesitate to give their respective clients the evaluation that the window for a successful settlement was closing.

In both six-way meetings, there was a good deal of cross communications, the parties talking with each other, with their own counsel as well as counterpart counsel. Among the issues collaborated upon were business valuation considerations, future dividing of clients in both a fair and practical way, assets brought to the company by each of the shareholders, the equitable and mutually efficient division of the company, the need for restrictive covenants and agreements between the parties going forward as two separate companies, drafting the language for jointly issued press releases announcing the restructuring of the existing business and the initiation of the new company, etc.

Both lawyers freely talked with all parties during both six-way meetings. In several instances, Faxon as the OC's corp. counsel would suggest proposals that would benefit the MS/DP and Zeytoonian as MS/DP's counsel made suggestions and offered counsel to the OC suggesting advantages of the non-compete and non-solicitation clauses to the OC in the event of its growth. Often parties and lawyers together freely brainstormed and looked at pros and cons of ideas.

Once all the relevant information had been gathered and assessed, creative ideas were suggested and weighed concerning

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cross-talk

issues decided collaboratively

how to treat income and cash flow, effective dates, announcements, etc. The OC shareholders acknowledged, appreciated and looked for ways to meet the MS/DP's interests and needs, such as his requirement for immediate funding for the new company without necessarily relying solely on an outright payment from the OC to the MS/DC. In delegating action items to be carried out between the six-way meetings, counterpart parties were often assigned tasks to perform together.

Throughout the process, the parties would reach an agreement on an issue and the lawyers would confirm it and check back to make sure that the agreed upon option satisfied all interests and did not work against any interests.

During the collaborative conferences, both CL lawyers modeled cooperative and collaborative efforts, freely allowing and then commending parties for coming up with excellent ideas and making important observations. The exercise of having the parties take turns on the white board to either present ideas or assess them proved effective. Parties were truly looking to find ways to benefit both the existing company and the emerging new one, discussing shared licensing and reseller agreements and subcontracting between each other so that the strengths of both counterparts would serve the interests of both.

Throughout the process, the parties would reach an agreement on an issue and the lawyers would confirm it and check back to make sure that the agreed upon option satisfied all interests and did not work against any interests. The CL attorneys commended the clients for the way they worked together as well as the collaborative and creative spirit that they employed.

In discussing the dispute resolution clause language, which the parties would eventually include in the RA, the parties agreed to use CL as their alternative dispute resolution vehicle of first resort. A conversation that quite transparently flowed from that discussion was the desire of the lawyers to use this case as a teaching and model CL case. The parties were willing to be interviewed and quoted as to their thoughts about the process, one joking that he would be happy to be interviewed in exchange, of course, for some reduction on the legal fees! The joke served to show the atmosphere of trust and cooperation, punctuated not by animosity and position taking but rather by commending each other for good ideas and the presence of humor.

Lessons Learned:

What were the key components for accomplishing the collaborative commitment and to maintaining a "container of safety and trust" in this case? These included: (i) the specific facts of the case, including the opportunity to have all parties represented by CL counsel from the start; (ii) the complementary lines of business between

the two corporations that emerged, (iii) the fiduciary requirements imposed under Massachusetts law on closely held business owners; (iv) the strong desire of the parties to resolve their issues through this process and their discipline in not allowing their emotions to overwhelm rational self interest; (v) the opportunity to add value to both the OC and the MS/DP's new businesses through a RA that included positive public "spin" on the restructuring, non-competition covenants and software re-seller agreement where none existed before; and (vi) critically, the level of trust between the two lawyers that would stay true to both CL's approach and values.

Every minute of both lawyers' time billed in the CL process was spent directly on working to achieve a favorable resolution, as opposed to time spent complying with civil procedural discovery requirements, motion practice or waiting for a case to be called in court proceedings.

How critical was the trust between the lawyers? Vital. Both lawyers were trained in CL and had worked together on MCLC governance matters. Both of these factors proved to be essential, as not only did the CL training serve them well in strategizing for the meetings and working through impasses, but the fact that the two lawyers knew each other well and trusted each other was an essential component in the six-way meetings. This trust was crucial during the six-way meetings in several instances when one or the other lawyer would read the situation and essentially "call an audible" or need to improvise at the moment and when information was presented that was a complete surprise to the MS/DP and his counsel. In this particular case, the collaborative commitment was facilitated and carried out because of the above-referenced factors. Although the "litigation-attorney-disqualification" agreement in the RA may have helped to reinforce the collaborative commitment, it did not provide the critical element to preserving a container of safety and trust within which to operate. That environment was more a result of the trust between the lawyers and the willingness of the parties to choose to approach their dispute through CL and work well together within the process.

Why did the parties choose CL? The corporation's Treasurer gave some insight on this choice: "We had heard horror stories about companies that almost went bankrupt on lawyers' fees while restructuring a business partnership. We wanted to prevent that from happening to us. We decided to give CL a shot, although it sounded too good to be true." Sharing his post-agreement thoughts about using CL, one of the corporate directors/shareholders in this dispute put it this way: "CL allowed us a kinder, gentler and cost-effective way to restructure our company."

Was CL cost and time efficient? By utilizing this innovative form of

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alternative dispute resolution, the parties came to an agreement in four months, expending approximately twenty percent of the time and legal costs that would have been incurred if the dispute had gone to litigation. One feature of using CL that appeals to clients in business or employment disputes was borne out in this case: Every minute of both lawyers' time billed in the CL process was spent directly on working to achieve a favorable resolution, as opposed to time spent complying with civil procedural discovery requirements, motion practice or waiting for a case to be called in court proceedings.

Was the scope of the results broader, deeper and more meaningful than what a court would have typically provided? The final settlement resulted in a new corporation being spun off for the departing shareholder/officer; compensation to the departing shareholder for his stock on equitable terms based on a jointly commissioned valuation but in a manner that did not cripple the other shareholders; a constructive and equitable process of mutually determining and agreeing on which customers would go with the newly created company; mutually beneficial non-competition covenants; a software re-seller agreement covering a difficult-to-value software product; a positive, jointly issued statement to the public; and maintenance of working relationships among the principals for future business joint ventures.

Did CL provide value added to the clients? One of the corporation's founders concluded: "Our experience with CL was a very pleasant surprise; I would recommend it as a first step to dispute resolution. It worked for us because we were committed to the CL process. Our attorneys acted as facilitators to keep the process moving and to iron out the differences among the parties. The process was almost painless; even with a few bumps along the away. In the end, all of us walked away from the process feeling like everyone was treated fairly and all parties were satisfied with the outcome. CL also preserved the company's capital, so we could build two strong companies from the one we all started."

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