Last Modified on 09/01/2026 6:58 pm MDT

A cautionary tale for new business owners

Jake and Aaron had been friends since meeting as freshmen in college. After graduation, they decided to turn a shared idea into a business. Their plan was simple enough. Jake had savings he was willing to invest, and Aaron had the time and expertise to run day-to-day operations. They trusted each other. That felt like enough.

It wasn't.

They never formally chose a business entity. No LLC, no corporation, just two friends going into business together. They opened a joint bank account to handle expenses and revenue. Jake transferred money in while Aaron started working.

There was no written agreement. No discussion about ownership percentages beyond vague assumptions. Jake believed his financial contribution meant he owned more. Aaron believed his sweat equity entitled him to an equal share. Neither pressed the issue. It felt premature and awkward to lawyer up so early.

The business got off the ground just as the friends imagined. They landed clients and money started coming in. Bills got paid. But tension grew as quickly as revenue.

"When do I start seeing a return on my investment?" Jake began asking, noting that Aaron was drawing funds from the business account every couple weeks. Aaron saw it as a well-earned salary for working long hours. Jake saw it as Aaron dipping into his investment. Without an agreement, there was no clear answer to who was right.

Then came the contract

A new client wanted a larger project, something that could take the business to the next level. Aaron signed the agreement on behalf of the business without consulting Jake. From Aaron's perspective, this was part of running operations. From Jake's perspective, it was a major commitment and potential risk to his investment.

Three months later, the project began going sideways. Unanticipated supply delays caused deadlines to slip. The client said this wasn't her problem and demanded results…fast. She had a contract with dates that weren't being met. Eventually, her dissatisfaction turned into a lawsuit alleging breach of contract and seeking damages.

That's when Jake and Aaron learned what they had created. Without realizing it, Jake and Aaron found they had formed a general partnership: No filing required and no paperwork needed. By simply agreeing to go into business together and acting on it, the law saw them as partners. Their lack of planning came with unanticipated but very real consequences neither had anticipated.

In a general partnership, each partner can bind the business. Aaron's signature on the contract didn't just affect him; it affected Jake. More importantly, both could be personally liable for the obligations of the business. The lawsuit wasn't just against the company; it was against *them* individually.

Jake was stunned to learn his personal assets could be at risk for an unwritten contract he didn't even know existed. Aaron was equally frustrated. His efforts to grow the business had exposed both to serious financial liability. As the lawsuit progressed, their internal dispute worsened.

"Who owns what percentage of the business?" Aaron asked. There was no written record.

"Who has the authority to make decisions?" Jake countered. No agreement addressed it.

"How should profits — or losses — be shared?" Aaron wondered. They had never clearly decided.

"What happens if I want out?" Jake grumbled. There was no exit plan.

What started as a promising partnership between friends had unraveled into legal exposure, financial strain, and a fractured relationship.

The outcome was costly. Legal fees mounted. The lawsuit was eventually settled out of court, but at significant expense. Even more damaging was the breakdown of trust between Jake and Aaron. The business didn't survive it.

The sad fact is that most of this could have been avoided

A simple decision at the outset to form a limited liability company would have created a separate legal entity. An operating agreement could have addressed ownership percentages, decision-making authority, compensation, and exit rights. It wouldn't have eliminated all risk, but it would have provided structure, clarity, and a measure of protection.

Instead, they relied on assumptions and a handshake. That's a risky foundation for any business.

The moral of the story

- Choose a business entity at the outset. Doing nothing is still a choice, and it may default you into a general partnership with personal liability.
- Don't rely on a joint bank account as your business structure. This provides no legal protection or clarity.

- Put the agreement in writing. Even a simple operating agreement can prevent major disputes.
- Clearly define ownership percentages, especially when one party contributes money and the other contributes labor.
- Establish rules for decision-making, including who can sign contracts and bind the business.
- Address compensation and distributions early to avoid misunderstandings.
- Plan for the end at the beginning. Exit rights matter more than most founders expect.

Starting a business with someone you trust is common, but assuming trust will resolve legal and financial issues is a recipe for heartache.