

# Joint Ventures

## Two Heads are Better than One

Joint Ventures and alliances are vital to business. They have become an important strategic option for many companies, particularly those operating internationally. As joint ventures become more commonplace, Chris Guy, a partner in the Corporate team of Mills Selig, explores key issues and potential pitfalls.

Businesses of any size can and do use joint venture (JV) models to strengthen long-term relationships or to collaborate on short-term projects. The term “joint venture” has no specific legal meaning. Rather it refers to a commercial arrangement between two or more companies for the purpose of a particular business undertaking.

JVs may take many legal guises but they will usually fall into one of the following categories: a company; a limited liability partnership; a partnership; or a purely contractual co-operation agreement. The vehicle that should be used will depend on the circumstances of the particular joint venture and it is important to take legal advice early so that the most appropriate vehicle is identified.

The formation of each JV will be different but in each case the parties need to address the principal issues requiring resolution. A target timetable should also be established which takes into account the following:

- Undertaking appropriate due diligence;
- Legal and tax structuring;
- Negotiation of key commercial issues;
- Valuation of the contributions made by each party to the JV; and
- Applying for relevant third party consents and, if appropriate, regulatory approvals.

JVs offer an array of benefits which make them an attractive option for businesses with the primary benefit being access to new and/or greater resources including markets, distribution networks, capacity, staff, purchasing, technology/

intellectual property and finance.

There are also pitfalls associated with JVs. Problems often arise whenever the interests of the partners are not properly aligned. This can occur when the objective of the venture is not 100% clear and communicated to everyone involved or when different cultures and management styles result in poor integration and cooperation. Similarly, if there is a perception that one of the partners is not “pulling their weight” or if there is an imbalance in levels of expertise, investment or assets brought into the JV by the different partners, then the venture may not be as successful as hoped.

It makes sense for the parties to address these potential pitfalls as early as possible and certainly during the drafting and negotiation of the legal framework of the JV. Depending on the legal vehicle used, the agreements required will differ slightly. However, in all JVs there will effectively be a joint venture agreement similar to a shareholders’ agreement or partnership agreement. This will aim to establish the basic rights and obligations of the parties, ensure that the JV and its business is established and run in accordance with the partners’ objectives and prescribe, as far as is practicable, what happens if difficulties occur.

One of the key legal issues that will need to be addressed in any JV agreement is the issue of control and, if appropriate, minority protection. Many JVs are 50:50 ventures creating the potential for ‘deadlock’, which, in this context, means the inability of the parties to agree on strategy or other important decisions affecting the JV.



Chris Guy, Corporate Partner, Mills Selig.

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This inability may be due to genuine disagreement between the parties or a fundamental breakdown in their relationship. In order to deal with such circumstances, the JV agreement may set out measures to avoid deadlock arising, mechanisms enabling the JV to continue in the event of deadlock (such as one party having a casting vote, an independent director’s swing vote or referring the issue to the Chairmen of the partners) or, as a last resort, “divorce” measures (for example, a voluntary winding up of the JV, sale of the JV or procedures where one party buys the other out such as “Russian Roulette”).

In the event of there being a minority partner in a JV the parties will need to consider what rights

or protections are appropriate for the minority partner. Underlying statutory and corporate rights for a minority shareholder are limited and provide no realistic safeguards or influence in relation to a corporate JV. A minority partner will expect stronger rights which may include consent rights (in relation to certain major management and policy decisions), rights ensuring the stake of the minority partner cannot be diluted without consent and rights to information.

It is clear that there are significant advantages for businesses in entering into JVs. However, if a joint venture is to be successful and profitable there are a number of issues that need to be explored and dealt with in the context of its legal framework.