TOP 10 TIPS FOR JOINT VENTURES

HANDY GUIDE

BRODIES LLP

Top 10 tips for joint ventures

Has your company spotted a gap in the market for a new product or service but hasn't got the resources to exploit it?

One option to consider is collaborating with another organisation through a joint venture. A joint venture might sound daunting - but essentially it's an arrangement between two or more parties to work together to achieve a common goal – usually increased profits.

Both parties can combine their expertise, skills and resources and potentially achieve more than either could have done on its own. At the same time, risks can be shared or even reduced.

Joint ventures are found in most industry sectors and there are a variety of ways to structure them.

If you are thinking about a joint venture, here are our top ten tips:

1. Who's my partner going to be?

It will depend on what resources and skills your company needs. It may be that the specialist technology or know how that you need is held by another company in the same marketplace, or perhaps by a research team in a university. Maybe you're looking for a quick route to new customers or another geographic market. Either way, you're looking for a partner who will help you develop your idea or technology or otherwise get your product or service to market more quickly than would otherwise be possible.

> Both parties can combine their expertise, skills and resources and potentially achieve more than either could have done on its own.

2. Can I work with my partner?

Collaboration is the key to successful joint ventures: you will have an ongoing working relationship with your partner. So is your proposed collaborator someone with whom you can work closely? If you have any reservations (for example, perhaps the way that they operate their existing business) then pause for thought before you commit to working together on a joint project.

Like any relationship, underlying tensions are likely to be exacerbated over time, particularly if things do not go according to plan.

3. How should my joint venture be structured?

There are various options. These range from a purely contractual arrangement (for example, a collaboration agreement between the two parties) through to forming a separate vehicle such as a company to conduct the joint venture business and into which both parties invest.

There are pros and cons for each type of structure. The one that's most appropriate for you will depend on what you are trying to achieve and the associated risks. You'll want to consult with professional advisers to run through the options.

The decision will be influenced by factors such as: whether the joint venture is for a one-off project or ongoing; what the joint venture needs in terms of cash or other assets; how the joint venture will be managed; how the parties want to share the profits and risks; the source of finance and other resources for the joint venture; how the rights in the resultant product or service are to be held and exploited; how the interest in the joint venture will be treated for accounting purposes and tax implications.

4. What exactly will the joint venture do?

It is important to establish this from the outset to avoid any later misunderstandings. Both parties need to be clear on the purpose of the joint venture (for example is it to carry out a specific project or will it be a continuing business?) and also what each party will be allowed to do in relation to their existing business.

For example, will there be any restrictions preventing either party from competing with the joint venture business and, if so, what is the scope and duration of those restrictions? Ensure that your existing business is not going to be unduly hampered.

5. How will the joint venture be funded?

How the joint venture business is going to be funded both initially and on a continuing basis is extremely important. New businesses can burn through significant cash in the early stages due to set up costs and high initial investment in product development.

Think big and try to raise as much as possible to allow you to concentrate on growing the joint venture and making it a success.

Having worked out how much funding is needed, you will then need to consider where the cash is to come from. How much cash can each joint venture party contribute and on what basis? Is borrowing from a third party an option? Lenders may be reluctant to lend to a new company with minimal assets without some form or security or guarantee from one or both of the joint venture parties.

6. Can non-cash contributions be made to the joint venture?

As well as (or instead of) cash, parties to a joint venture may agree that they will each contribute assets such as intellectual property, access to facilities, or personnel.

The way in which the contribution is made will depend on the structure that's been adopted. In any case, it is important that each party understands and agrees the basis on which the asset is being contributed.

For example, if your company will provide the joint venture company with access to your intellectual property, then you will likely want to grant a non-exclusive licence of the rights so that your company retains ownership and can grant third parties access to it in the future.

7. How will profits be dealt with?

Making money is why businesses get into joint ventures in the first place. So you need to be clear what will happen if the joint venture generates profits. Should profits, at least during the initial years, be ploughed back into the joint venture to help it grow or should the parties be able to access them?

These questions will depend to an extent on the intended purpose and lifespan of the joint venture but it's something to cover off in detail in the paperwork so that there are no nasty surprises in the future.

Join the conversation at our corporate blog

brodies.com/blog/corporate

8. How is the joint venture to operate day to day?

This will depend on the structure of the joint venture, and the skills that each party is bringing to it.

If a new company is to be set up, your company will want the right to appoint directors to the joint venture's board.

Just because you can nominate someone to the joint venture company's board doesn't mean that person will automatically do whatever you tell them. While they are there to represent your interests, the director will owe legal duties to the joint venture company as a whole, not to the person who appointed them.

Consider what matters can be decided by the board and what matters require to be agreed by the shareholders. Bear in mind where overall control lies or whether there is a 50:50 deadlock. If the latter, consider what mechanism you may wish to provide for resolving a deadlock.

If the joint venture is not being conducted through a separate vehicle such as a company, how will the activities be managed? What rights will each party have, for example, to veto actions or to force the other party to perform, for example?

> What happens if there is a change in ownership of the other party to the joint venture so suddenly you find yourself in business with someone you would rather not be?

9. What if I want out?

No-one wants to think about exit when a relationship is beginning. But it's far better to agree how you'd handle this before the joint venture gets underway, while relations are good and constructive.

Circumstances change and either party might want out for any number of reasons e.g. change of strategy, or financial reasons. The joint venture agreement should be clear about the grounds on which each party can get out, and also cover off the consequences of exit. Things to consider include the impact of exit on: the joint venture relationship or entity (will it continue or terminate if one party exits); any rights that have been contributed/licensed to the joint venture by the outgoing party (will the joint venture still be allowed to use them?); and any rights that have been developed during the joint venture.

For example, if a joint venture company has been formed, should you have the right to buy the shares of the other party if that other party wants to leave? What should happen if someone external comes along and wants to buy up the company? What happens if there is a change in ownership of the other party to the joint venture so suddenly you find yourself in business with someone you would rather not be?

10. Always take advice at an early stage

Taking advice from professionals such as accountants and lawyers at an early stage is crucial. They will advise you on the appropriate structure, help you to avoid the many pitfalls that can catch the unwary, and document the arrangement. That leaves you free to concentrate on making your new business a success which will benefit both parties.

Key contacts

Shuna Stirling
PARTNER
+44 (0)141 245 6201
shuna.stirling@brodies.com

Tom Boulton-Jones
PARTNER
+44 (0)1224 392 284
tom.boulton-jones@brodies.com

Will McIntosh
PARTNER
+44 (0)131 656 0154
william.mcintosh@brodies.com

Join the conversation at our corporate blog
brodies.com/blog/corporate