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Business Joint Ventures

In this article, I explain business joint ventures. A joint venture exists when two or more businesses team up to engage in a limited activity, for example, one business has customer relationships in a particular market while the other has back-end personnel, so they team up to offer a vertically integrated service in that market.

There are four basic concepts in structuring your joint venture: corporate structure, control, money, and exit. *First*, choose a structure for the JV, perhaps a corporation or a partnership. *Second*, decide who will control the venture, including the votes needed to make decisions, and day-to-day operational control. *Third*, decide how you will split the profits of the venture, and which partner will initially receive and hold the money from customers. *Fourth*, create an exit – before you enter any business relationship, you need to prepare your exit.

Corporate Structure. You can form a new corporation or LLC to operate the joint venture. Usually I advise clients to form a JV corporation because it gives limited liability protections to the JV members. In the alternative, you can operate the JV without a legal entity, in which case you are partners in a general partnership. The primary drawback here is that partnerships don't have limited liability, that is, all partners are liable for the partnership's debts. In some cases, however, keeping it simple makes sense, for example if JV activities have little risk of liability. You should talk with your attorney about whether or not to form a corporation or LLC for the JV.

Note: Irrespective of the JV's corporate structure, all JVs need a Joint Venture Agreement.

Control. Control means voting rights and veto rights. Voting is a positive form of control, in that you make decisions about projects and other matters based on the affirmative vote of members. Do not assume that a JV will have simple 50/50 voting for all matters, because there might be 3 or more members in the JV or one member might have a greater voting interest. Also identify the JV managers who will control day-to-day operations.

Veto rights are a negative form of control. A veto right lets you stop certain JV actions. For example, you might require that a 75% vote approve the sale of the JV or the purchase or sale of JV property. Veto rights generally protect minority owners from the actions of the majority.

Money. Clearly state how the members will share in the profits. Consider such factors as money and other resources invested, and time and labor spent in operations. An ancillary requirement is to map out how money flows into the JV and into what account. For example, if money flows through one member's website and into its account, the other member will need accounting rights and other protections.

Keep your eyes on who employs the personnel that carry out JV activities – a member or the JV itself? The employing member must receive reimbursement for all related expenses and perhaps indemnity for employment law disputes. Be careful also if a member can use JV assets to its personal benefit, for example through the use of JV equipment or through related party contracts.

Exit. All business partnerships end sometime, usually sooner than you think. You need a structure that permits an economic divorce among the members. The Joint Venture Agreement should provide this structure, which will consist of a trigger event followed by the separation.

A common trigger event is irreconcilable dispute among the members. If the members can't get along, then one or more of them can require the economic divorce. In the divorce, each member should receive a fair division of the JV's assets. The easiest way to separate the members is for each member to take back the assets it brought to the JV. The division is harder for assets that the JV itself acquired, like the JV's name, website, goodwill, customer relationships, and software developed for the JV. Consider also an allocation of JV obligations, such as taxes, lease rentals, guaranties and litigation related liabilities. You need special drafting in the Joint Venture Agreement to handle these more troublesome assets and liabilities. The goal is always the same, however: an efficient seperation through the fair division of assets and liabilities.

It is with great joy that I find myself here, at the conclusion of this article. Call me if you want to talk more.

A Friend in Need

That's the title of this oil painting by C.M. Coolidge, originally used in 1903 to advertise cigars. I call your attention, in the bottom middle part of the picture, to a business joint venture in action.

- Friendship is born at that moment when one person says to another: "What! You too? I thought I was the only one." -- *C.S. Lewis*
- Friendship is everything. Friendship is more than talent. It is more than the government. It is almost the equal of family. -- *Don Corleone*