Framework of a Successful Joint Venture

Joint venturing provides contractors a tool to expand into new markets, construct more complex projects, spread resources and risks, and increase productivity. A joint venture is a contractual partnership between multiple companies that typically exists for a limited scope or duration. A joint venture is typically unincorporated, meaning the joint venture is not an independent legal entity that exists outside the contractual agreement between the joint venturers.

At its essence, a joint venture is a partnership between firms that exists to perform a project or projects in a way that the joint venturers can share resources. While a joint venture can be formed as a single-purpose entity, no legal barriers exist that would require a single project or a unique purpose.

The law recognizes a joint venture as a viable entity but it does not shield its members from liability in the same manner as an independent limited liability company or corporation. A joint venture entity operating under a typical agreement will be treated under law as a general partnership with no liability shielding protections for its members. Thus, the member entities of a joint venture are typically jointly and severally liable for any obligations, debts, or claims of the joint venture. Furthermore, any internal agreements in the operating agreement to limit liability as to third parties are often unenforceable.

Should partner companies to a joint venture wish, they may form a limited liability company, a limited partnership, or corporation that will provide liability shielding benefits. However, under Texas law, certain formalities may be required in order to retain the benefit of the protection. Failure to maintain independent operations, for example, is one way that the shield may be pierced should there be a claim.

The heavy and highway segment of the industry is mostly populated with public works. Because of the statutory framework regulating public work, significant projects require bonding. Additionally, the self-perform model exists primarily on the civil side of the industry. That model requires significant capital investments of labor and equipment. Because of the capitalization required to perform many public infrastructure projects, a joint venture is an attractive way for a company to move into larger projects that would otherwise stretch bonding capacity and resources.

It is no longer uncommon to see public entities building projects that cost hundreds of millions of dollars. There are few companies that can bond a project of that size, and many others that, while the capacity may exist, are unwilling to tie-up capacity and accept the amount of risk associated with such an expensive endeavor. A joint venture allows the risk to be shared. It also allows the partners to bring certain expertise and experience to a job that the co-joint venture might desire.

When deciding on whether a joint venture makes sense for your company, there are a number of factors to consider:

- 1) Is the project or project-type one that your company would be capable of performing on its own?
- 2) Can your company accept and manage the risks associated with the project on its own?
- 3) Is your company willing to accept the investment and risk associated with the project?
- 4) Would a partner company provide expertise, resources, or processes valuable to the project that you cannot bring to the project alone?
- 5) Does your company seek to gain access into new or more markets?
- 6) Is your company compatible with the proposed joint venture partner?

While, this list is certainly not exhaustive, it provides a few items worthy of consideration when a joint venture opportunity presents itself.

Assuming the participating companies agree that a standard joint venture is the desired manner of association, a joint venture can be formed by drafting and executing a contractual agreement establishing the existence of the entity and terms of governance. The operating agreement does not need to follow any formalities in order to be valid under the law.

The joint venture agreement should contain terms addressing the following core terms that will be essential to the successful partnership desired by the members:

- 1) Governance – how will the parties allocated responsibilities such as control of the entity's resources and activities?
- 2) Capital contributions – both initial and recapitalization, if necessary, should be considered and addressed as well as boding capacity.
- 3) Operational concerns – project management, safety training and oversight, subcontractor selection and direction, among others
- 4) Procurement – how will the joint venture secure projects?

Because the joint venture agreement is typically a custom, manuscript contract, the parties are free to shape it in any manner they desire. The items above should be considered in memorializing the agreement.

The agreement should also address whether the joint venture will be populated or unpopulated. The distinction lies in whether the joint venture will have its own employees (populated) or rely on the partner entities to allocate their own resources to allow the joint venture to perform its work (unpopulated). Most construction joint ventures are unpopulated. In an unpopulated joint venture, the partner firms allocate their own resources to the project based on their agreement. That agreement and asset allocation should be specifically addressed in the joint venture agreement.

In most cases, the member companies will allocate a certain portion of their internal resources to the joint venture and its projects. The agreement should address this as part of the capital contribution and operational terms. Each party will bring certain strengths to the entity and those contributions should be leveraged to best service the entity and its goals. If one member entity has an excess capacity of equipment and the other member entity has an excess capacity of skilled management and labor for a particular component of a project, the agreement should have terms enabling the allocation of those resources.

Following this basic framework and taking time for careful consideration of the joint venture's components and goals will help establish a successful partnership.

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