

NEGOTIATING A JOINT VENTURE AGREEMENT? 11 IMPORTANT CLAUSES TO CONSIDER.

In an attempt to enhance their competitive advantage, businesses often forge strategic alliances. To birth and reinforce such internally fragile alliances, it is common for businesses to enter into Joint Venture Agreements (“JVA” or “Agreement”). A Joint Venture (“JV” or “Venture”) is a business arrangement that accommodates two or more entities (corporate or individuals) to run a certain business or undertake a specific project together.¹

Take for instance a manufacturing company with a need to market its products on large scale awareness campaign across Nigeria. With the right Joint Venture between that company and a marketing/distribution company, significant sales and profits can be made. A Joint Venture Agreement is the document which sets out the terms and conditions of the business relationship. Hence, it is important for parties, during negotiation, to ensure careful consideration of key clauses to be included in the JVA. The contents of JVAs are not always uniform and vary depending on the peculiar needs and circumstances of parties. However, there are some provisions which a typical JVA may contain, some of which are mentioned here.

1. Corporate Structure for the JV

First, it is important to consider which corporate vehicle would align the disparate needs of parties in the Joint Venture?

Joint Ventures can take various forms. They could be an incorporated companies (whether private or public) or unincorporated business entities (such as partnerships). It is important for parties to pick the appropriate vehicle due to the different legal considerations for each option.

Factors such as taxes and duration of the business association also need to be thoroughly considered. For example, while a company’s profits are directly taxed,² a partnership as a business entity is not taxed. Rather, the shared profits accruable to each partner will be taxed.³

Also, parties need to consider the procedure for the dissolution of different corporate structures. For instance, the dissolution of a public company is always more tedious and rigorous than a partnership.

2. The Objective and Scope of the Venture

This clause will describe the overall purpose of the Venture. An ideal objects clause should ordinarily answer the following questions:

- What purpose are the parties trying to achieve?
- What is the operational scope of the Venture?

Ideally, such a clause should also be devoid of ambiguity to avoid complications with the interpretation of its provisions interpretation in the event of a dispute on the objects of the JV.

It may not be possible for parties to anticipate, in specific terms, all the objective(s) of the Venture during negotiation. Hence, in addition to the identified objective(s) and scope, an omnibus provision covering "all such other things as are incidental or conducive to the attainment of the objectives" of the JV may be useful.⁴

3. Capital Contribution and Venture Financing

The success of the Venture is largely dependent on getting this clause right during negotiations.

For instance, parties may want to contribute capital equally or otherwise. A party may, in addition to its equity investment, assume responsibility for providing debt financing for the Venture.

Generally, the capital contribution of parties determines the ownership structure of the JV.⁵ The implication of not inserting this clause is that capital will be deemed to have been contributed equally and liabilities too will be borne in the same manner.

Capital contribution is not limited to money: it may also be in other forms of assets. This may include land, manpower, machinery, intellectual property, goodwill and reputation, amongst others.

It is preferable that parties agree on the valuation method that would ascertain the monetary equivalence of such contribution during negotiation. This would prevent the occurrence of divergent estimates of the value of capital contributions made.⁶

Other sub-clauses that can be inserted include the interest dilution and damage/remedy clause.⁷

4. Composition of the Management Body

The JVA should identify the number of representatives each party will appoint for the purpose of managing the affairs of the Venture.

An equal number of representatives may be appointed by parties. In this case and for the purpose of vote casting, the head of the management body (usually the Chairman) may be given the power to break a tie.

It is also important that the JVA indicates the senior officers of the Ventures and the party that will appoint them. For example, which party will have the powers to nominate the Chairman or CEO?

Depending on the corporate structure adopted, parties may be represented in the proposed business by appointed partners or directors.

5. Decision-Making

It is not unlikely that decisions regarding the affairs of the Venture would have to be made almost at every turn. How will such decisions be made? For instance, Senior Officers of the management team may have the power to make certain decisions on behalf of the Venture. In other instances, the acceptance and approval by a majority of shareholders (if the Venture is an incorporated company) may be required.

It is also important to consider how deadlocks are to be broken. Parties should envisage such possibility and devise mechanisms that could liberate the Venture from the deadlock.

6. Termination

Typically, termination could occur due to breach of the JVA by a party, bankruptcy, where the Venture has achieved or unable to achieve its purpose, amongst other reasons.

A termination clause provides for the conditions and circumstances upon which the Agreement would be terminated either by a party or by both parties.

7. Dispute Resolution

An effective JVA should contain provisions regarding the resolution of disputes between parties.

The underlying justification for including the dispute resolution provision is to allow parties to resolve their differences in an expeditious, fair and cost-effective manner. For instance, parties may opt for one or more Alternative Dispute Resolution mechanisms such as conciliation, mediation or arbitration. In the absence of a disputes resolution provision in a JVA, either party litigation will be the default mechanism for resolving disputes under the JVA where parties are unable to amicably resolve their disputes.

Conclusion

Drafting a Joint Venture Agreement may not be as essential as paying attention to the clauses it contains. Therefore, it is useful for parties to carefully consider their positions and ensure that they understand the basis of Joint Venture Agreements that they enter into.

Disclaimer: This article is only intended to provide general information on the subject matter and does not by itself create a client/attorney relationship between readers and Twelve Legal nor does it serve as legal advice. However, readers may contact us for industry-specific legal advice.

¹ M.T Wroblewski, ' What is a Joint Venture Agreement Between Two Companies? Chron (15th November 2019) <<https://smallbusiness.chron.com/joint-venture-agreement-between-two-companies-23727.html>>

² S. 9 Companies Income Tax Act CAP. C21 L.F.N. 2004

³ S. 8 Personal Income Tax Act CAP. P8 L.F.N 2004

⁴ Michael E. Horton, 'Structuring and Negotiating International Joint Ventures', (1994) 27 Creighton Law Review p1022.

⁵ Stan Silverman, 'Follow this Advice When Negotiating a Joint Venture Agreement' The Business Journal (18th September 2018) <<https://www.bizjournals.com/bizjournals/how-to/growth-strategies/2018/09/follow-this-advice-when-negotiating-a-joint.html>>

⁶ Michael E. Horton, 'Structuring and Negotiating International Joint Ventures', (Supra, 1023).

⁷ Borden, Bradley T. and Rutledge, Thomas E., Interest Dilution and Damages as Contribution-Default Remedies in Failing LLCs and Partnerships (December 4, 2018). Business Law Today (Nov. 2018); Brooklyn Law School, Legal Studies Paper No. 578. Available at SSRN: <https://ssrn.com/abstract=3295793>