Starting a joint venture

The purpose of this guide is to examine what is involved in SMEs entering into a joint venture with one or more other organisations.

The terms 'strategic alliance' and 'joint venture' are often used interchangeably, but for the purpose of this guide a joint venture involves setting up a third-party legal entity, whereas a strategic alliance does not.

In a nutshell a joint venture, or JV, is an entity created by two or more parties to undertake a particular activity together. The parties each agree to contribute equity to the new entity and to share in its control, revenues, and expenses. It can be formed to last for the duration of a particular project or to remain on an ongoing basis.

WHY FORM A JOINT VENTURE?

Businesses can enter into a JV for many reasons, but the commonest are to increase capacity, access certain technology or other resources, enter new markets, improve distribution, or develop new products.

A JV does not need to be a multi-million pound venture. There are many examples of small businesses entering into successful JVs with other small businesses. Equally, in the right circumstances, a small business can enter into a JV with a larger concern, and again there are many examples of these.

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GROWING YOUR BUSINESS WITH A JV

There are basically three main ways a business can grow:

1. Organically - growth from within
2. Through a joint venture or strategic alliance
3. Through a merger or acquisition (M&A)

In recent times, the credit crunch and cash squeeze brought on by the economic downturn have severely limited the first option for many businesses and research suggests that JVs have now become the preferred vehicle of growth.

Generally JVs offer the same benefits as M&A but without the irreversible commitment and the time-consuming process of integrating assets etc.

BENEFITS AND DISADVANTAGES

JVs can deliver a number of advantages including:

- Increased capacity
- Access to new markets, especially overseas
- A wider distribution network
- Access to additional technology, staff, and finance
- Spreading of risks and costs with other parties

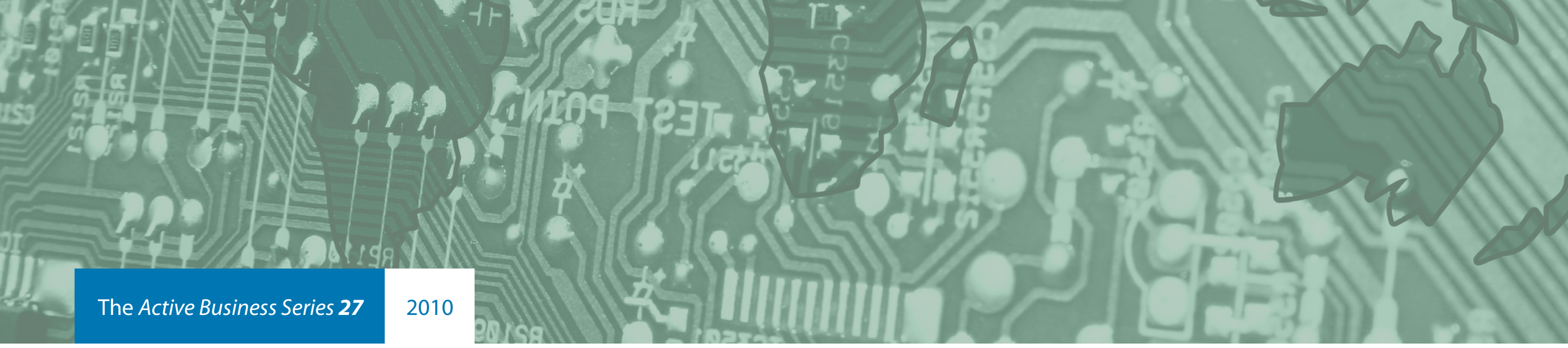
However, they can and do go wrong, especially if they are not well researched beforehand or there is a fundamental incompatibility of aims or expectations between the partners.

JVs are more likely to be successful if the partners:

- Share common goals and objectives
- Will be more effective working together on the designated project than alone or with another party
- Can agree a balanced contribution of investment and expertise to the venture by each party

Mutual trust, good communication, and clear understanding are also key to forming and maintaining a successful venture.

JVs are particularly vulnerable in the early stages and all parties must be prepared to provide as much leadership and support as is needed to help the



venture get up and running.

Sometimes there will be differences in the business culture or management style that might cause problems, but ideally these should be identified and addressed at an early stage before any enduring arrangement is agreed.

THE STAGES OF FORMING A JV

Entering into a JV with one or more other organisations is potentially a big step for your business and we would encourage you to proceed with caution and diligence at every stage. There are many potential pitfalls and we strongly recommend you seek professional help and advice throughout.

There are four basic stages to forming a JV:

1. Assess suitability

The first step is to clarify what you want the proposed venture to achieve and to define specific goals and objectives for the project.

Then, to establish if a JV is the best approach, ask the following questions:

1. Could the objective(s) be better accomplished by another means?
2. Is a JV compatible with your overall business strategy?
3. Will a JV fit in with your business culture?
4. Will your staff be able to adapt to and embrace the proposed venture?
5. Will you be able to protect your own interests, especially intellectual property and other assets, if you enter into such a venture?
6. Could the venture undermine your competitive position in any way?

2. Identify and research potential partners

If you are satisfied that forming a JV is the right approach, the next stage is to identify a potential partner.

Sometimes a business will have a partner in mind, perhaps from among their existing suppliers or customers. Others may have to look further afield. Some degree of previous familiarity can be very helpful, but is not essential.

The important thing is to look for a good match, where the resources, skills and assets of the target complement yours. Here, it can help to conduct a SWOT analysis to identify strengths and weaknesses of both parties.

Once you have identified a potential partner the next stage is to conduct comprehensive background checks to determine, among other things:

- Are they financially sound?
- Are they profitable?
- Are they trustworthy?
- What sort of reputation do they have among their customers, suppliers, and competitors?
- Are they engaged in any other joint ventures?
- Is their business culture, management style, etc compatible with yours?

If having exercised appropriate due diligence the candidate seems suitable you can approach them with a view to opening up discussions.

3. Discuss possible structures, arrangements and procedures

Before sealing any deal you will need to engage in wide ranging and thorough discussions to establish common positions on, among other things:

- The precise objectives and duration of the venture
- The legal structure of the new entity
- Where relevant, any cross-border issues
- Any compliance, tax and other regulatory issues that might apply
- What financial contribution each partner will make
- What assets, employees, etc if any will be transferred to the new entity
- How you will share liabilities, profits and losses
- Ownership of any intellectual property the entity creates
- Arrangements for employee recruitment, remuneration, pensions etc
- How the entity will be managed and controlled
- Procedures for resolving disputes
- How the venture will be terminated

This last point is very important, and all parties should agree on an exit strategy before formally entering into an agreement.

4. Draw up and sign agreements

Once you have agreed terms the next stage is to draw up and sign a joint venture agreement. Of course, this needs to be legally binding and professional advice is essential at this stage.

You might also consider whether to include other agreements such as a confidentiality agreement at this stage.

HOW WE CAN HELP

We have considerable experience in this area and can advise and assist at every stage of the process. As your representative we can ensure that your best interests are served throughout. We can also co-ordinate with all other agencies, professionals, etc.

If you are considering entering into a joint venture, contact us first to see how we can help.