



# Successful Joint Venturing in Construction Starts with and **STRATEGY** **RELATIONSHIPS**

By Thomas Julian & David Carrithers

Most joint ventures (JVs) fail; more than 80 percent in the first two years and more than 99 percent within five years. Perhaps that is because many companies consider forming a JV to develop additional business, particularly in the short term. However, a JV can be a beneficial long term solution.

There are two key questions that should be addressed when exploring a JV:

- Will joint venturing offer strategic value to both parties? The leaders must understand and share a clearly defined, documented and agreed upon strategy for the opportunity.
- Do the individuals running each company trust one another? The key to successfully joint venturing is to understand the people with whom you will be working. Both parties need to be confident they can see these individuals as people they want to work with over the next five to ten years.

A JV is typically pursued to go after a specific project or targeted opportunity. The parties then hope to grow the bottom line by winning that specific contract or project. Too often this decision occurs on a tight timeline to meet the bid date; when a JV chases a bid, finances, potential revenue and profits drive the decision. Making money should factor significantly into the strategic decision, but it only accounts for one part of the equation.

## **Strategy to Drive the Thinking, Not Newly Discovered Opportunities**

Rushing out to form a JV to go after a specific project is like getting married to get a meal at the wedding reception. A company that thinks a JV is a quick fix answer to immediate market growth or a short term opportunity is headed down the wrong path.

“Joint venture partners should look more at the culture their two companies would form rather than the opportunity at hand,” says Mike

O’Neill, Mid-Atlantic regional vice president of Centennial Contractors Enterprises, Inc. “A sure recipe for disaster is rushing to an opportunity, and then trying to find a partner as a result,” he added.

The strategy cannot be a pop-up, scattershot approach that acts as a stop-gap against eroding market share or decreasing profits. Instead it is critical for a construction business to determine why, where, and how they want to expand the business.

One means for forming a JV is for a company to pursue additional business in markets or with clients the company already serves. Alternatively, the company can look to grow into new markets (defined, for example, by client, geography, scope, size or type of project).

“The biggest benefit is getting access to a market you do not have experience in but where you think you could add value,” says O’Neill.

While many JVs are formed by two companies that share complementary project experience, others bring together companies with complementary services. “We are looking at joint ventures with A/E firms to pursue design-build projects,” O’Neill said.

Further, a well defined strategy cannot include a one-sided win. Good JVs provide both companies with work in new markets, round out their skill sets with knowledge gained from each other, increase their financial capability, reduce risk and learn proven processes and procedures from each other.

Coming together to form a JV combines the strengths of both companies. The strategy gels when the new thinking of both companies together forms something new that could not be found as two separate stand alone entities. It is then that the companies realize new growth and profits.

### **Joint Venturing Is Not Speed Dating, Fast Can Be Deadly**

Few companies considering a JV spend the time and effort needed to get a real sense of the individuals and the organization they will be joining.

When forming a JV the companies shape the future operating team, business model and plans, mission and vision together. Both companies must be aligned and speak the same language around vision, ethics and direction to gain a positive end result.

“A sure indication that a joint venture will not succeed,” cautions O’Neill, “is if the two partners have divergent goals, dissimilar cultures or are simply rushing to fill an opportunity.”

### **Amicable Separation for Irreconcilable Differences Is Not Always an Option**

The decision to form a JV involves significant legal considerations, in addition to the financial and human concerns. Properly planning and patiently developing the JV can mitigate some of the potential challenges, but forming a JV still has inherent risks.

While no one likes considering negative possibilities, it is important to discuss, during negotiations, the operational structure, capitalization and re-capitalization, levels of authority, decision making, insurance and bonding issues and indemnification(s), as well as how the companies will allocate the JV’s losses, both operational and potential legal claims.

Depending upon the nature of the JV and the legal relationship of the parent companies, the law may impose fiduciary duties upon them. These legal duties attempt to force companies to behave in a trusting manner to each other by requiring them to act in good faith. It will be easier for the people running both companies to fulfill these obligations when they like, trust, and respect those individuals leading the other company. Breaching these duties, however, out of spite, ignorance or neglect could have significant impacts on the JV and the parent company’s

bottom line, especially if litigation occurs. Therefore, getting to know and like the people running the partner company, in addition to opening the door to frank and honest communication, greatly limits the need for litigation and in-fighting within the JV.

Further, in the age of 24/7 media coverage and sensationalism, a company’s reputation and good name may be its most valuable asset. Thus when a company partners with another, it risks its reputation. If the partner or the JV itself does something to damage their reputation, all three companies’ names may be tainted by the same broad brush. If you would not want to bring someone home to meet Mom because of the way they may act at the dinner table, maybe you should consider whether you want to bind yourself to them as a business partner.

Another consideration when forming a JV is the termination and end point. Sometimes, things can go wrong and the JV may need to terminate prior to successful completion. This can happen when one company becomes bankrupt, the government disbars one of the companies, one (or both) of the partners cannot adequately capitalize their share of the JV or the parties cease to get along and the JV stops providing benefits.

When things go wrong, the parties could simply execute the plan crafted and agreed to in the JV formation documents, when the parties were getting along well. If the parties, however, failed to sufficiently consider the premature failure of the JV, the termination could be very messy. In addition to costing a lot of money, the risk of the JV’s non-performance on an existing project could harm both parent companies’ reputations and future ability to bond work.

### **“It’s Not You, It’s Me. Maybe We Should Just Be Friends.”**

As the companies discuss joint venturing, one or both may get scared off or decide not to complete the transaction for numerous reasons. While this could (and probably should) halt the formation of the JV, there

may remain real value in the companies’ further cooperation. In that case, a prime/sub or mentor/protégé option could capture some of that value while mitigating some of the risk and concern.

Many of the advantages of the synergy of a JV can be captured through a prime contractor/subcontractor relationship. Even before the prime submits a single bid, the prime contractor and subcontractor could enter a teaming agreement that offers the potential client many of the advantages of the JV and permits the prime and sub to get to know each other better.

Alternatively, many federal agencies offer mentor-protégé programs that permit larger companies to mentor smaller companies. While these programs offer obvious benefits to smaller companies, larger companies benefit from preferential treatment under some SBA regulations. This preferential treatment helps the larger company obtain better access to federal government contracts and subcontracts.

Though two companies may not be ready to joint venture, they may still be able to capture some new business opportunities and develop a potential future partner in the process.

### **NICC JV LLC – A Joint Venture Case Study**

When it is clear from the outset that all parties will benefit, the hard work necessary to make a JV succeed is justified. That is the opinion and experience of Tom Kearney, president and founder of North Island Corporation, a JV partner with Centennial Contractors Enterprises, Inc., of Vienna, Virginia.

North Island is an 8(a) certified small business that first heard of Centennial, a large national contractor, through networking. After several meetings and lots of due diligence, each firm independently realized it could help the other achieve their growth goals by forming a JV.

Under the federal government Small Business Administration's 8(a) rules, a JV must be created with a specific contract solicitation in mind. If a JV wins the solicitation, it must typically continue until they complete the project. Generally, unless the JV wins a solicitation, the JV fails to exist. These rules put substantial pressure on the parties to ensure that they fit well together, have all their systems and documents in place and have their marketing and business plans established before pursuing any specific work.

According to Kearney, trust is the most important ingredient for a successful JV. "It's a very close relationship," Kearney said of his company's involvement with Centennial. "They are very generous with their time and resources, which I am sure they would not be unless they trusted us."

For a small business like North Island, Kearney said having a major player like Centennial as a partner presents key opportunities for their success. However, he insists that being an 8(a) certified small business means that his company has to "be ready to roll up the sleeves and do the work." In other words, there is no riding the coattails of the larger partner.

The JV, officially known as NICC JV, LLC, has provided benefits to both parties. For North Island, it has given them the opportunity to gain experience and obtain access to federal contracts they could not get on their own.

The JV responded to two solicitations for the Naval Facilities Engineering Command (NAVFAC), each up to \$20 million dollars per year over multiple years. "These types of projects require significant bonding capabilities," said Centennial's O'Neill. "For a small company, it would be an enormous challenge."

Moreover, the solicitations are indefinite delivery-indefinite quantity (IDIQ) job order contracts (JOC). NAVFAC could not specify the individual projects that would ultimately be awarded under the solicitation. Instead, NAVFAC established an overall quantity

of work basis of decision where individual projects are awarded on a task order basis. "JOC projects require sophisticated computer systems to manage all the documentation needed," said Kearney. "We couldn't do it all without Centennial."

For Centennial, one of its main benefits from joint venturing was its ability to continue to support its long term federal clients that increasingly have federal projects set aside for small businesses.

### Check the Egos at the Door

Egos during negotiations often seem to derail true opportunities early. The companies should go in with the mindset that each partner company and the joint venture will come out as winners. Focus on what can be done to make the JV the most successful business possible.

It is important for the companies to place all of their respective thoughts and ideas on the table during negotiations and while drafting the operating agreement. This includes good things, bad things, things that could go wrong, managing the replacement of key leaders within the JV, planning the exit strategy for the JV, and so on. The companies cannot be afraid to approach these awkward topics or take any issue personally. If the companies cannot discuss potential failures before things go wrong, they probably will not be able to work through problems if they go wrong later.

Seeing great opportunities fall apart because of egos or because the strategic value of the JV was not fully understood or embraced by the leadership of one of the partners, can be very disappointing.

Despite running all the numbers and performing all the due diligence needed for planning a JV, a company will be wasting its time and energy unless the JV will create long term strategic value and will be with people you can trust. In the end, non-aligned goals of the parent companies, a lack of trust, a lack of similar values and the people-focused issues are the key drivers to the failure of a JV. So go with your gut; if you would not have

someone over for dinner with your mom and family, you should not be looking at joint venturing with their company.

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### Tips on Joint Venture Development

- It always takes longer than planned to form a successful JV; make sure you give it enough time.
- Write down what value you believe your company and the other company can bring to the JV. Include what you believe the JV's unique value will be to your market and clients (its competitive advantage) and what deal killers would not allow this JV opportunity to continue. Ask your potential JV partner to do the same. Share the results with each other; if you cannot talk through these issues openly, the potential partner may not be the right fit.
- Do something more than a lunch meeting. Go to a conference or event where you can spend several hours in a controlled environment. Be sure to do this again with the entire management team once the JV is in place.
- The key executive from each company should have a causal dinner at home, in a relaxed environment. Nothing shows the true character of a person than dinner at home with family.
- Ask what industry associations the potential partner company participates in, and then ask the associations what they know about that company.
- Ask your bonding/surety agent or insurance broker what they know about the potential partner.
- Google key members of the leadership team of the potential partner company; see what pops up.