



FENWICK & WEST LLP

## Joint Ventures and Other Growth Alternatives

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## Growth Alternatives

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- **Internal Development**
- **Acquiring Technology**
- **Joint Venture (JV) Entities**
- **“Contractual” JV Agreements**
  - > **Joint Marketing**
  - > **Joint Development**
  - > **Outsourcing**
  - > **Hybrids**
- **Acquisitions**



## Internal Development: Pros

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- **Control of Design, Timing and Quality**
- **Design for Integration**
- **Known Team and Technology**
- **100% IP Ownership and Control**
- **Can Control Third Party Access**
- **No Dependence on Third Party (“3P”)**



## Internal Development: Cons

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- **Often Slowest Time to Market**
  - > **Delays in Building a New Team**
  - > **Conflicts in Resource Allocation**
- **May Be Highest Cost Approach**
- **Distracts from Core Competencies?**
- **Excess Baggage After Development Completion?**

## Acquiring Technology License: Pros

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- **Often Fastest Time to Market**
- **Less Expensive, Easier Process**
- **Can Couple With Equity Investment, With**
  - > **Upside Potential to Share Value Creation**
  - > **Control Rights**
  - > **Merger Veto, Refusal Right**



## Acquiring Technology License: Cons

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- **Dependence on Third Party**
- **Risk of Termination or Nonrenewal**
  - > **Licensor Acquisition or Bankruptcy**
- **Costly and Difficult to Get Exclusive Rights**
- **Third Party May Want Grant Back or Equity**
- **Above Unacceptable Risks for “Core IP”**





## Entity Joint Ventures: Pros

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- **Improved Ability to Address New Markets and Technologies**
  - > **Pooling of Resources**
  - > **Time to Market Advantages**
- **Sharing of Profits and Risks**
  - > **IP Royalties Also Possible**
- **Unlike Acquisition, Can “Unscramble”**



## Entity Joint Ventures: Cons

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- **Not Truly Independent**
- **Upside / Liquidity Path Unclear**
- **Joint Control Unworkable**
- **ISOs May Be Unavailable**
- **Risks of Disputes or “Divorce”**
- **Risks of Giving JV Exclusive Rights**





## Entity JVs—Key Issues

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- **JV Structure; Choice of Entity**
- **Tax Planning**
- **Technology (IP) Contributions**
- **Employee Incentive Strategies**
- **Control; “Divorce” Planning**

## Entity JV Structure: Choice of Entity

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- **If Tax Considerations Dominate--LLC**
- **If Equity Compensation or IPO Exit is Key--  
Corporation**





## Tax Planning

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- **Choice of Entity**
  - > **Contract Arrangement May Be Tax Partnership**
- **Structuring of Technology Contributions**
  - > **Grant of “All Substantial Rights”**
- **Cross Border Technology Transfers**
  - > **Royalty Advisable If Contribute IP to Foreign JV**
- **Special Allocation Provisions**
- **Exit Planning Issues**



## IP Complexity

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- **JV vs. Member IP Rights**
- **Rights Pre, Post and During JV**
- **Royalty Structure**
- **JV Field of Use and Sublicensing Rights**
- **Assignability; Terminability**
- **Noncompetes**
- **Assign Parent Opportunities?**



## Control: Member Veto As To:

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- **Business Plan and Scope**
- **Budgets, Financings, Capital Calls**
- **Officers, Compensation**
- **Member Assignments or Admissions**
- **Exit Scenarios--IPO, M&A, Wind Up**
- **Key IP Issues**



## “Divorce” Planning

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- **Clear Initial Agreement On Goals, Tactics, Timing & Respective Contributions Is Key**
- **Escalation & Deadlock Resolution**
- **Clear rights to dissolve JV or terminate its exclusive rights in certain situations**
- **Have mechanism to achieve Exit Strategy by JV sale or IPO or JV partner buyout**
- **Consider Effect of Termination On:**
  - > **IP, Employees, Facilities,**
  - > **Other Assets, Rights & Liabilities**



## Employee Incentive Strategies

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- **Inducement Incentives**
- **Downside Protection--Severance; Vesting Acceleration, Right to Return to Members**
- **Phantom Stock Plans--"JVARs"; SAR Accounting**
- **Option Plans--Effect of Roll Up; Put/Call Rights; LLC Complexities**



## **“Contractual” JVs-Types**

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- **Joint Marketing, Co-branding and Linking Agreements**
- **Outsourcing; Joint Development**
- **Internet Hybrids of the above:**
  - > **e-business Infrastructure Development**
  - > **Sales and Customer Management**
  - > **Web Hosting; Fulfillment; MIS**
  - > **Content/Delivery JVs**
- **Above Often Coupled With Equity Investment**





## Contractual JVs: Pros

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- **Avoids Need for Entity Formation for Shorter Term and Project Specific Cooperation**
- **Retains Focus on Core Competencies**
- **Avoids Need to Build Infrastructure**
- **Fast, Low-resource Way to Add Needed Solutions and Services**
- **Leverages 3P's Superior IP and Resources**
- **Shifts Risk to 3P**



## Contractual JVs: Cons

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- **Dependence on 3P and Contract Continuance**
- **Loss of Control & Flexibility**
- **Risk of Disputes; Termination Planning**
- **Impact on Expenses and Margins?**
- **Dilution If Give up Equity**

## M&A Risks May Favor JVs or Other Growth Alternatives

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- **EPS Dilution if Synergies Don't Materialize**
- **Integration Risks: Employee/Culture, Customer and Market Channel Confusion**
- **Management Distraction**
- **Inheriting Unforeseen Risks (IP, Litigation)**





## Decision Drivers

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- **Core Technology, Control/Exclusivity Critical**
  - > **Buy or Grow**
- **Can't Depend on Others--Buy or Grow**
- **Internal R&D Impossible**
  - > **Buy, License, or Have 3P or JV Develop**
- **Inability to Ramp Infrastructure Quickly**
  - > **Time to Market Critical: Buy or License; Market or Have 3P Provide Solution Via Contract or Entity JV**
  - > **Inability to Afford Rapid Market Segment Penetration—partner With Party With Funds, Market Position or 1st Mover Advantage**