Read this post online

The Joint venture: A tool for companies to speed up their international expansion

Faced with a sluggish domestic economy and mature markets, French companies tend to expand internationally and seek new opportunities to secure their business.

The joint venture, irrespective of whether it is imposed by the ever-intensifying global competition or under local laws that require the presence of a local partner, constitutes a development tool that is popular among companies in their quest to conquer international markets.

An opportunity to expand internationally

When preparing their international expansion, companies are confronted with the question of identifying the most appropriate legal form to conquer new markets. A successful international expansion strategy may depend on the choice of the legal structure. If companies do not wish to collaborate with foreign local businesses, they will opt for a subsidiary or a branch. Yet, in certain circumstances, they may be inclined – or obliged – to set up a joint venture with one or several local partners.

What are the economic benefits?

As Ronald Reagan put it "*By working together, pooling our resources and building on our strengths, we can accomplish great things*". Setting up a joint venture has a number of economic benefits exemplified in many entrepreneurial success stories in the insurance, building, research or technological innovation industries[1].

Commercially speaking, by setting up a joint venture, a company relies on a partner that has a perfect knowledge of the local market and of the practices of the competitors, the administrative authorities and the political authorities. The company can thus learn about and adjust more quickly to the specific requirements and needs of the foreign market, through the pooling of expertise, and technical and human means.

Expanding abroad always requires significant investments and may result in economic losses in the first years of operation. A joint venture, the establishment of which is less costly and time-consuming than the creation of a subsidiary or branch, helps mitigate losses thanks to the presence of a local partner who is not only aware of the requirements for entering the local market, but also provides part of the financing and shares the financial and commercial risks.

As a tailor-made solution, a joint venture can be set up for a duration that can range from a limited number of months for a one-time commercial project to several years for a long-term market entry strategy, which requires a specific attention during the determination of the legal terms and conditions that will govern the partnership.

What types of joint-venture?

Derived from the business practices applied in the North American marketplace, the joint venture involves two or more businesses that pool their expertise, technologies or resources to achieve a particular goal.

In practice, the joint venture takes (i) either a contractual form, through the conclusion of a collaboration agreement, (ii) a corporate form, through the creation of a joint entity, or (iii) both of the aforementioned forms.

The choice of the most appropriate type of joint venture will depend on the factual circumstances and economic strength of each of the parties. In any event, the legal relationship between the partners must be based on confidence which is, as underlined by Kenneth Arrow[2], *"is an invisible institution which governs the economic development"*.

Contractual collaboration

To enhance their capabilities and complementarity without, however, losing their legal autonomy or engaging into the creation of joint entity, businesses may consider entering into cooperation agreements that will structure their contractual collaboration[3]. A distinction should be made between two main types of situations: A one-time limited cooperation and a long-term cooperation.

As such, wherever the parties wish to implement a one-off partnership arrangement, they usually enter into grouping agreements, also called "consortium" agreements. This type of partnerships is aimed at defining the internal relationships between several companies that jointly perform a contract for a client. Grouping or "consortium" agreements are primarily used in the building industry to respond to calls for tenders.

Partnerships for a long-term cooperation are different from the above-mentioned type of partnerships as there is no primary contract with a third-party. This type of cooperation contracts usually relates to technology transfers, a joint investment in research or the establishment of a joint industrial presence in a specific market.

The main provisions of these contracts set forth the terms and conditions governing the allocation of contractual liability – usually joint liability – as well as the allocation of powers between the partners to ensure an equal access to the decision making process throughout the performance of the contact.

Regardless of whether the partnership is set up for one-off or long-term collaboration, companies always have the option of setting up a joint subsidiary.

The joint subsidiary

Partners may elect to achieve a greater level of cooperation thorough the creation of a joint subsidiary. Joint subsidiaries are frequently set up by businesses that wish to efficiently establish a long term presence in complex emerging markets such as China, Brazil or the United Arab Emirates.

Through the creation of an ad hoc entity[4], the joint subsidiary serves to structure the partnership by agreeing on the distribution of profits and limiting the corporate liability to limit the risks associated with any given transaction. The export company must be vigilant as regards the ownership structure and the allocation of powers within the joint subsidiary. A number of local regulations, such as those applicable in the United Arab Emirates[5] or China, may require that the local partner holds more than 50% of the share capital.

An access key to foreign markets that must be properly handled

Joint venture arrangements are limited only by the imagination and needs of the future partners. Yet, in practice, partnerships between companies are often structured around a main contractual document, i.e. a framework agreement, that sets forth the pursued objectives, and ancillary contracts, also called "satellite" agreements, that specify the activities carried out by the commercial partners (consortium to respond to a call for tenders, creation of a joint subsidiary to provide operational support, etc.).

While the joint venture is an access key to foreign markets, it remains a risky endeavor and there are countless examples of unsuccessfully joint ventures. As real risks are involved, the rules of the game must absolutely be defined beforehand and set forth in the legal documentation to be signed by the partners.

[1] http://www.lesechos.fr/31/10/2014/lesechos.fr/0203876933845_cfm–la-plus-belle-joint-venture-de-l-histoire.htm

[2] Kenneth Joseph Arrow is an eminent American economist who was the joint winner of the Nobel Prize in Economics with John Hicks in 1972.

[3] In the international trade jargon, these contractual partnerships are referred to as "*non-corporate*" or "*non-equity joint ventures*".

[4] There is no type of company that is perfectly and universally suited to the needs of business partnerships. Local regulations must always be carefully reviewed to understand the legal and tax implications of the contemplated structure.

[5] https://www.soulier-avocats.com/en/blog/conquering-the-uae-through-a-successful-market-entry-strategy/