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THE INS AND OUTS OF JOINT VENTURE AGREEMENTS

A PilieroMazza Webinar
April 8, 2014

PRESENTED BY

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OVERVIEW

- What is a joint venture?
- Advantages and disadvantages of using a joint venture
- Starting a joint venture

  Step 1: Find the right partner

  Step 2: Ensure the JV satisfies the applicable set-aside requirements

  Step 3: Choose the legal form (partnership vs. LLC)

  Step 4: Determine the management structure/labor (populated vs. unpopulated)

  Step 5: Draft the joint venture agreement
- Questions

WHAT IS A JOINT VENTURE?

- A Joint Venture is:

  An association of individuals and/or concerns to combine their property, capital, efforts, skills, and knowledge to carry out no more than three specific or limited-purpose business ventures for joint profit over a two-year period

  13 C.F.R. § 121.103(h)

JOINT VENTURE BASICS

- Main Characteristics:
  - Co-management
  - Sharing profits and losses
  - Limited duration
- Competing as a Joint Venture:
  - Joint Ventures should be formed before submitting offer
  - Agreement should provide for contract performance
  - FAR requires disclosure in the proposal
- Forms of Joint Venture:
  - Partnership – referred to by SBA as “informal” joint venture
  - Limited Liability Company
  - Corporation

ADVANTAGES OF JOINT VENTURES

- The Government can look to the resources of two (or more) companies to perform the work
  - The JV partners function as "co-primes" on the project
- Joint venture partners are able to perform a larger contract they might not otherwise have had the capability to perform on their own
- Stay small longer: JV revenue is attributed to the partners in proportion to their ownership interests in the JV
- A minority joint venture partner can exert more control over contract performance to protect its interests than in a traditional prime-sub relationship

DISADVANTAGES OF JOINT VENTURES

- Lead contractor gives up some control
- If the joint venture is a partnership (i.e., informal), the participating contractors are jointly and severally liable to third parties for the acts of their joint venture partners, including criminal acts
- The Government may have questions about:
  - Whether there is a clear point of contact
  - Who is performing the work and how the joint venture will satisfy the limitations on subcontracting
  - Past performance
- Terminating the JV can be more complicated than a subcontract

STARTING A JOINT VENTURE
STEP 1: FIND THE RIGHT PARTNER

- Carefully and thoroughly screen prospective JV partners
  - History of being a good teaming partner? Ask for references
  - Record of being fair, equitable, collaborative, and flexible in teaming relationships
  - Attitude of mutual dependence and benefit
  - Unblemished reputation with the agency
  - Strong technical capabilities to fulfill elements of the Statement of Work (SOW)
  - Proven record of covering elements of the SOW
  - Positive name recognition with the customer
  - Cost competitiveness
  - Proposal support resources
  - Strong infrastructure support

STEP 2: ENSURE THE JV MEETS THE SET-ASIDE REQUIREMENTS

- If the JV pursues a set aside contract:
  - Check the different JV requirements depending on the type of set-aside contract at issue
  - Ask your prospective JV partner to certify to you in writing that it is a small business and any other relevant status, and check SAM.gov to confirm
- Presumed Loss Rule considerations

HOW JVs QUALIFY AS SMALL

- SBA General Rule: JV partners are affiliated for a contract
  - This means a JV will be considered a small business if the <u>combined</u> size of the JV partners meets the size standard for the contract
- Exceptions to joint venture affiliation:
  - When each JV partner is small under the applicable size standard and either: (1) the procurement is bundled or consolidated; or (2) the procurement exceeds one-half the size standard or $10 million (depending on the nature of the size standard)
    - In this scenario, the JV qualifies as small as long as each JV partner meets the applicable size standard, regardless of combined size of the JV partners
  - Joint ventures between <u>8(a) protégé</u> and SBA-approved mentor
    - Look for new rules that may permit JVs with large mentors for SDVOSB, HUBZone, WOSB, and small business protégés as well

THE "3-IN-2 RULE"

- JV may not be awarded more than **three contracts** over a **two-year** period without a finding of general affiliation
  - JV may ultimately receive more than three contracts, as long as the JV submitted the winning proposals before it won its third contract and before expiration of the two-year period
  - Two-year period begins with the award of the first contract to the JV
- Same two entities may form additional joint ventures and each may be awarded three contracts over two years
  - Caution: multiple joint ventures and contracts may lead to a general affiliation over time

PERFORMANCE OF WORK REQUIREMENTS

- The JV must meet the applicable performance of work requirement (i.e., the limitations on subcontracting)
  - The work done by the JV (if populated) or through the JV partners (if unpopulated) counts toward satisfying the performance of work requirement
- For unpopulated JVs, how much of the JV's work must be done by each partner depends on whether the project is a small business set-aside, and if so, what type

JV REQUIREMENTS FOR 8(A) SET-ASIDES

- The Government can award 8(a) sole source and competitive contracts to a joint venture if:
  - At least one firm is 8(a) certified
  - All partners are small businesses, unless in SBA-approved mentor-protégé relationship
- SBA must approve the JV Agreement <u>before</u> contract award
- JV Agreement must specify that the 8(a) firm will:
  - Manage the joint venture and the project
  - Provide an employee to be the project manager
  - Perform at least 40% of the work in an unpopulated JV
  - Benefit from the JV, but also bring something to the JV other than its 8(a) status
  - Among other requirements, see 13 C.F.R. § 124.513(c)

JV REQUIREMENTS FOR SDVOSB SET-ASIDES

- SDVOSB must be managing partner
- Employee of SDVOSB must be project manager, and the individual must be named in the JV agreement
- SDVOSB must receive 51% of the net profits
- JV Agreement must specifically describe both parties' roles in contract performance and how SDVOSB will manage the project
  - Cannot use vague or boilerplate language
  - There is no mandated minimum work share for the SDVOSB, but the SDVOSB must clearly benefit from the JV
- Unique VA requirements:
  - The JV must be a separate legal entity (i.e., LLC)
  - CVE must verify JV <u>prior</u> to contract award

JV REQUIREMENTS FOR HUBZONE SET-ASIDES

- All partners must be HUBZone certified and small
- The contract must meet certain size requirements
  - Revenue-based size standard – contract must exceed one-half of the size standard
  - Employee-based size standard – contract must exceed $10 million
- If contract does not meet size requirements, joint venture may still qualify as long as the two firms, combined, are small
- No SBA approval required
- No required JV agreement provisions like for the other programs, but good idea to follow the other JV rules

JV REQUIREMENTS FOR WOSB/EDWOSB SET-ASIDES

- Lead partner must be designated as WOSB or EDWOSB in SAM.gov
- Written joint venture agreement must:
  - Designate WOSB as the managing party
  - Name a specific employee of WOSB as the project manager
  - Clearly describe how the WOSB and its project manager will manage the project, as well as the WOSB's responsibilities and role in contract performance – WOSB must clearly benefit
  - Specify that 51% of the net profits will go to the WOSB
  - Ensure the WOSB will maintain the JV's records
- WOSB must provide a copy of the JV agreement to the contracting officer, upload to SBA's repository

STEP 3: WHAT LEGAL FORM TO USE?

- Options:
  - Limited Liability Company
  - Partnership
  - Corporation
    - Double taxation
    - Almost never used

LLC STRUCTURE: PROS & CONS

- Pros:
  - Members not liable (beyond capital contributions) to third parties for actions of the LLC
  - May be treated as partnership (or like an S Corp)
  - SBA recognizes LLC structure
- Cons:
  - Requires capitalization
  - Filing/annual LLC fees, plus preparation of documents to obey corporate formalities

FORMING THE JV AS AN LLC

- File articles of organization with your home state to form the LLC
- Draft a joint venture/operating agreement between the parties
  - In some cases, you may want or need the joint venture agreement to be separate from the operating agreement
- Obtain a federal tax ID
- Register at SAM.gov
- Establish a bank account
- Register to do business in other states (if necessary)

PARTNERSHIP STRUCTURE: PROS & CONS

- Pros:
  - Treated as a partnership (or like an S Corp)
  - Simple to set up
  - Informal
- Cons:
  - Partners are jointly and severally liable on debts of the partnership

STARTING THE JV PARTNERSHIP

- Draft a JV/partnership agreement
  - In some cases, you may want or need the joint venture agreement to be separate from the partnership agreement
- No state filing requirement to form the partnership
  - But, lack of filing could present issues in registering the JV elsewhere (such as with bank)
- JV still needs to register at SAM.gov

STEP 4: DETERMINE MANAGEMENT STRUCTURE AND LABOR

- How will the parties manage the joint venture?
  - Management Committee
  - Members
  - Project Manager
- Which party will be responsible for negotiating contracts and subcontracts?
- How will you communicate with the customer?
- What are the sources of labor to be employed?
- How do the parties envision the division of labor on contracts?
- Populated or unpopulated?

POPULATED JOINT VENTURE

- A populated JV is one that has its own employees
- Less common than unpopulated JV
- Pros:
  - One seamless entity performs work
  - All employee benefits are from one organization
  - Possible competitive pricing edge
- Cons:
  - More costly and administratively burdensome to set up
  - JV (not the JV partners) earns past performance
  - Partners only receive proportionate share of the profits

UNPOPULATED JOINT VENTURE

- An unpopulated JV does not have its own employees (except perhaps for admin personnel)
- Pros:
  - Each JV partner performs their portion of the work, essentially as subcontractors to the JV, earning their own fee on the work they perform
  - JV may charge handling fee on top of work done by JV partners
  - Easier to explain structure to the SBA for approval of JV agreement, if necessary
  - Simpler and less costly to set up
- Cons:
  - Procuring agency may not understand who is performing work
  - Companies may have different benefit packages
- Similarities: populated and unpopulated satisfy the performance of work requirements

STEP 5: DRAFTING THE JV AGREEMENT

- Common terms:
  - Purpose of the joint venture
  - Designation of small business as managing partner
  - For certain set-asides, not less than 51% of net profits earned by the JV must be distributed to the small business participant
  - Responsibilities of the parties
  - Both parties must ensure performance of the prime contract, even if the other party withdraws from the JV
  - Designation that accounting/administrative records are kept by managing venturer and requirement that managing venturer retain records of contracts completed by Joint Venture
  - Performance of work requirements
  - Disputes

Questions?

Thank you for joining us today.

If you would like to speak with Pam or Jon about joint ventures, please contact them at:

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