A 'Breakup Clause' for Kemica's Joint Venture Agreement

A Case Study in Joint Venture Formation & Dissolution

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Abstract

Joint venture governance is a tricky business. Shareholders accustomed to giving marching orders to affiliates suddenly discover that now a partner's agreement must be obtained. Such agreement is not always easily secured. Partners frequently have different objectives, motives and views of their venture's business. Considerable time and effort can be consumed while the partners sort out their differences. Often this results in "lowest common denominator" decision making. Venture management is also quick to exploit divisions among the partners for its own reasons. If the owners are at loggerheads, venture management gains considerable freedom to ignore the owners and run operations as they see fit. No wonder many well managed companies consider joint ventures to be a "last resort" strategic option.

A carefully crafted Joint Venture Agreement (JVA) is one key to avoiding the worst ills of operating a joint venture. Such an agreement must contemplate potential partner deadlocks in advance and provides means for the venture to function through such periods. It also must provide some means for ending standoffs before they paralyze the venture and destroy value.

One key to anticipating/ending partner deadlocks is a well-defined "Breakup Clause." It seems that providing a clear path for dissolution of a venture is the best way to ensure that all partners look to resolve their disputes amicably until the time for exiting is right.

In this case study the partners forming Kemica have finished negotiating much of the JVA. The Breakup Clause remains to be done. One partner, Orca, is concerned that Flagler will try to dominate the venture and block Orca's exit. Flagler, for its part, is concerned that Orca is not sufficiently dedicated to maximizing value. The partners struggle to find breakup language that will reconcile their divergent interests and allow the venture to function well. Flagler tries to help its negotiators by forwarding wording from several other venture agreements. This wording demonstrates how the language of this critical clause can be shaped to favor either partners interested in acquiring a venture or those interested in controlling their exit. Drawing upon these alternatives, students need to craft breakup wording that will work for Kemica and its partners

This case is based upon negotiations which took place in 1998-99 to form a polyolefins joint venture in Australia.