

The Right Combination: Considerations When Teaming Up for Large Construction Projects

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Introduction

As construction projects increase in size and complexity, many small and mid-size sub-contractors are finding it difficult, if not impossible, to bid on these undertakings as they lack, for example, the necessary knowledge or expertise, capital, or bonding capacity. Accordingly, small and mid-size sub-contractors are looking for innovative ways of participating in these potentially lucrative endeavours.

One method of winning bids for large construction projects, while allocating risk, adding expertise and increasing capital investment and bonding capacity, is to team up with another business entity offering similar or complimentary services. This article will examine two forms of such collaboration: general partnerships (“GP”) and contractual joint ventures (“CJV”).

Structuring the Business

There are important legal differences between GP’s and CJV’s. However, regardless of which structure is considered, underlying issues of compatibility, mutual trust and full commitment to the arrangement are key elements and form the foundation for the success or failure of the business relationship.

General Partnerships¹

In British Columbia, the *Partnership Act*, the legislation which governs GP’s, defines partnerships as “the relation which subsists between persons carrying on business in common with a view of profit”. Whether or not a partnership exists is determined by provisions of the *Partnership Act*.

A partner is an agent of the GP and the other partners respecting the business of the GP. Accordingly, in most cases, the acts of a partner while carrying on the business of the GP bind the GP and the partners. A partner is liable jointly with the other partners for all debts and obligations of the GP incurred while he or she is a partner and this liability survives his or her termination as a partner (or the partnership’s termination) and binds the partner’s estate. In addition, a partner is jointly and severally liable with his or her partners for the wrongful acts of any partner acting in the ordinary course of the GP, loss or injury caused to any person who is not a partner or any penalty incurred.

¹ Limited and limited liability partnerships are not considered in this article.

The *Partnership Act* requires that each partner must “act with the utmost fairness and good faith towards the other members of the firm in the business of the firm” and a partner cannot compete with the partnership without the consent of the partners. These are referred to as fiduciary duties which cannot be derogated from or otherwise circumscribed.

Subject to any agreement between the partners, all the partners are entitled to share equally in the capital and profits of the GP and must contribute equally towards the losses, whether capital or otherwise, sustained by the GP. Further, assets of the GP are usually held in the name of the GP and not the individual partners. With respect to dissolving a partnership, if no set term has been agreed on for the duration of the GP, any partner may end the GP at any time on giving notice to all the other partners of his or her intention to do so.

While GP's are governed by the *Partnership Act*, a partnership agreement plays a central role in defining the duties and obligations of the partners and explaining how the GP will be structured and run. Important points to consider when drafting a partnership agreement include clauses establishing:

- that the GP is being created;
- the term (i.e. duration) of the GP, if the GP is not indeterminate;
- what each partner contributed to the GP (e.g. property, services, capital);
- how assets and profits will be distributed between the partners;
- the partners' ability to execute contracts and take on obligations on behalf of the GP;
- GP meetings and reporting;
- indemnification of the partners;
- how GP interests can be transferred;
- tax consequences of GP;
- confidential information and intellectual property issues;
- how the GP can be dissolved; and
- dispute resolution procedures.

Contractual Joint Ventures²

In British Columbia CJV's are not governed by statute and have no specific legal definition. From a business perspective, a CJV is a combination of two or more individuals or legal entities which join together under a contractual agreement to conduct a specific business enterprise under which profits and losses will be shared. Accordingly, a CJV is not a separate legal entity (like a GP) and is governed by the contractual arrangement reached between the parties.

² Joint venture corporations and joint ventures with title to all property held by a trustee are not considered in this article.

Unlike a GP, a typical CJV is created for one particular project and has a set termination date. Similar to GP's, individual venturers can be sued directly and owe fiduciary duties to the other venturers; however, such duties can be and usually are limited in the CJV agreement. In the normal course, each venturer retains its interest in the specific assets it contributes to the CJV and venturers participate in the profits and losses of the CJV in proportion to their share of the CJV. In addition, CJV agreements usually provide that venturers are liable only for the proportionate share of the total CJV.

As CJV's are governed by a contract and not a statute, the terms of the CJV agreement are of paramount importance. Points to consider when drafting a contractual joint venture agreement include clauses setting out:

- the parties;
- that a partnership is not created;
- what the equity ownership of each venturer is;
- the duration of the CJV;
- what each venturer will contribute to the venture;
- what the funding responsibilities of each venturer are;
- the order of return of contributions and profits;
- indemnity for the venturers;
- fiduciary obligations of the venturers;
- the management and decision-making structure of the CJV;
- tax consequences of the CJV;
- confidential information and intellectual property issues;
- alienation of interests in the venture and early termination of the venture; and
- dispute resolution procedures.

Conclusion

From a practical standpoint, once a construction project has been identified in which collaboration with another business entity is advantageous or necessary; the search for a potential partner or venturer should start (if that process hasn't already begun). It is essential that the prospective partners or venturers compliment the skill sets and expertise offered by the other. Once a pool of candidates is created, the next step is to undertake a due diligence review to ensure that there are no financial, management, labour relations or reputation concerns affecting the candidates. Next, there should be meetings with the possible partner or venturer chosen from the pool of candidates to discuss collaboration on the construction project and the form that the collaboration will take. The final step is to sit down with a lawyer to structure the business relationship and draft the agreement.

GP's and CJV's make it possible for sub-contractors to participate in large construction projects on which they would otherwise not be able to bid. They also allow for risk and costs to be allocated, improve access to financial resources, increase bonding capacity and potentially introduce the parties to new clients and new technologies (subject to the confidentiality and intellectual property provisions of the agreement) and new managerial practices. From a business standpoint, they also may pre-empt competition, create stronger competitive units and improve speed to market and agility and flexibility once in the market.

Both GP's and CJV's also have pitfalls and disadvantages. Most important are the areas of trust, reliability, compatibility, control and commitment. If these cornerstones of a successful business relationship do not exist, the GP or CJV will likely fail. There are also important legal consequences of forming a GP or CJV. Most notable are the fiduciary duty, liability and confidentiality issues which may arise once a GP or CJV is created. However, if the GP or CJV agreement is properly drafted and the parties are committed to its success, the collaboration may very well be profitable and may lead to greater opportunities in the future.