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'Til Deadlock Do Us Part

As the love-struck engaged couple idyllically plans their new lives together without ever imagining divorce, many soon-to-be joint venture partners draft their joint venture agreement without ever contemplating dissolution. Unfortunately like too many marriages, joint ventures end in dissolution because the parties disagree on key issues. However, a properly drafted deadlock provision in a joint venture agreement can prove to be helpful (just as a properly drafted prenuptial agreement) as it can provide an efficient manner to preserve the value of the enterprise underlying the joint venture.

In the event of a deadlock in a joint venture, it is helpful to have a clear mechanism in the agreement for resolving the conflict as that will streamline the process, avoid confusion and uncertainty, and save time and money. A principal goal of the deadlock provision is to have in place a mechanism that will treat the partners fairly while at the same time allowing the business to continue. Without a deadlock provision, dissolution of the enterprise is often the only choice. Below are some commonly used deadlock provisions to accomplish this goal:

1. Escalation. In the event of a deadlock, the joint venture agreement can provide that the issue is escalated to certain key executives of each partner in an attempt to solve the problem; unfortunately, this often results in the same deadlock.
2. Chairman Tie-Breaking Vote. The joint venture agreement can provide that the Chairman of the Board has the right to cast a tie-breaking vote in the event a Board vote results in a tie (which was not resolved after escalation). The problem with this approach, however, is that this does not work in every deadlock scenario (e.g., a partner defaults on its capital contributions). Also, this gives one party control, which is contrary to the entire purpose of the 50/50 joint venture in the first place.
3. Independent Tie-Breaking Vote. To eliminate the problem of one party having too much control, rather than providing the Chairman with the tie-breaking vote, the joint venture can provide that an independent, non-executive director has the right to cast the tie-breaking vote. However, finding an independent director that the partners agree on may prove difficult for various reasons (and no person may be willing to take on this burden without any upside). Also, as with the Chairman tie-breaker vote, this does not work in every scenario.
4. Mediation. Rather than merely casting a vote, the partners can hire an independent expert or arbitrator to find a solution to a deadlock. There are many different forms of mediation, ranging from a more formal arbitration and having the mediator make its own binding decision to "baseball mediation," where each side writes down its final position and the mediator picks one side or the other (this should lead to the partners presenting their most reasonable position in order to be picked), to "golf mediation," where the mediator writes

down the most equitable solution and whichever partner presents a solution closest to the mediator's wins. Mediation works well for factual matters but not so well for solving multi-faceted business issues, such as determining the best capital raising terms or whether to admit a new strategic partner.

5. **Buy-Sell.** When the parties do not want to let a third party settle the deadlock, one solution is the buy-sell provision pursuant to which one of the partners buys the other partner out. This can be handled in many different ways but the following are commonly seen favorites:
 - a. "**Russian Roulette.**" One partner serves notice to the other partner stating the notifying partner's perceived value per share of the joint venture. The partner receiving the notice must then either sell all of its shares to the other partner at that price per share or purchase all of the other partner's shares at that price.
 - b. "**Texas Shoot-Out.**" Each partner submits a sealed bid containing its perceived value per share of the joint venture. The partner with the higher bid buys the other partner out.
 - c. **Dutch Auction.** Each partner submits a sealed bid containing the lowest price per share at which it would sell all of its shares. The partner with the higher price buys the other partner's shares at the lower price submitted.
 - d. **Adjusted Fair Market Value.** An expert or auditor determines the "fair market value" of the price per share. Once determined, the partner triggering the buy-sell provision will either buy the other partner's shares at a set premium (e.g., 20%) or sell its shares to the other partner at an equivalent discount.

Buy-sell provisions are the last resort because, once implemented, the joint venture arrangement terminates and one partner acquires 100% of the joint venture vehicle. Careful consideration should be given to a partner's future liquidity position because a less liquid partner could find it being forced out of the joint venture at a less than fair price.

Although deadlocks are an unfortunate occurrence, they do happen and carefully drafted and negotiated deadlock provisions in the joint venture documents can ease much of the agony that deadlocks cause. Each joint venture has its own unique set of circumstances surrounding its endeavors, so what may work for one joint venture may not be the best solution for the next. Before executing joint venture documents, partners should explore which deadlock provisions best meet their needs to allow them to live "happily ever after."

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