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Joint Venture Trends:
JV's between Private Equity
Investors and Public
Companies

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Reasons for Investment



Benefits to a Public Company

Reduce Capital Spend

- Expand its business without an outlay of additional cash or incurrence of debt. Public Co will want to ensure that PE Investor (portfolio entity) is creditworthy and has sufficient resources to fund its obligations going forward.
-

Maintain Control

- Allows Public Co to retain control and operatorship of the business and expand to create additional synergies.
-



Benefits to a PE Investor

Diversify

- Allows PE Investor to participate in more investments.

Synergies

- PE Investor can “ride the coattails” of Public Co’s synergies with the target.
- May provide PE Investor the ability to invest and influence the business while also building synergies between the business and its other portfolio businesses.

Industry Expertise

- PE Investor has the benefit of Public Co’s industry expertise applied to the JV and may seek to gain industry expertise itself to enhance current or future investments.

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How do their priorities differ?



PE Fund Priorities

Vary depending on PE firm or funds managed by the same PE firm – some have different investment horizons, target returns, and risk profiles. Important to understand the goals of your counterparty.

Liquidity: Buy-to-sell

- PE Investor has limitations on the life of its investments, whereas Public Co is free to hold on to an investment indefinitely.

Maximize Returns

- Enhance performance and manage cash flows. PE Investor seeks stable cash flows and rapid margin improvement to increase return potential in the short to medium term.

Manage Risk

- PE Investor wants to minimize the risk of its investment.

Preserve ability to diversify

- PE Investor will be resistant to terms that limit PE Investor's ability to make other investments or otherwise bind its current or future investments.



Public Company Priorities

Synergies and organic growth

- Public Co plans to hold its investment and integrate the JV business into Public Co's other operations.

Prevent disproportionate allocation of expenses

- Public Co will want to ensure that PE Investor bears its proportionate share of JV expenses, including for services provided by Public Co.

Avoid conflicts

- Due to the long-term nature of Public Co's investment, Public Co desires to avoid conflicts with other businesses held by the PE Investor.

Regulations

- Public Co has reporting and regulatory requirements not applicable to PE Investor.

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Addressing Unique PE Investor Priorities



PE Investor Priority: Liquidity

Limit Transfer Restrictions

- PE Investor will want uninhibited sale rights – i.e., without restrictions on identity, creditworthiness and experience of buyer.

ROFO in lieu of a ROFR

- A ROFO allows PE Investor to run a robust sales process, whereas a ROFR chills third party interest.

Put Rights

- In some deals, allow PE Investor to sell its interests to Public Co at a pre-determined price (e.g., a price based on performance of JV or pre-determined return to PE Investor). May only apply if a certain rate of return has not been achieved during an agreed investment period.

Use of drag rights

- One approach is to allow PE Investor to drag Public Co in a sale. May only apply if PE Investor has not received a certain rate of return during an agreed investment period. Public Co will want the option to buyout PE Investor prior to PE Investor's exercise of its drag rights.



PE Investor Priority: Liquidity

Narrow scope of AMI

- Narrowly tailor AMI restrictions to increase marketability and maximize value to PE Investor.

Lock-up Public Co as operator

- Requiring PE Investor's approval for transfer of operatorship will enhance marketability to financial acquirers



PE Investor Priority: Maximize Returns: Enhance Performance

Through operational controls (e.g., board representation and approval rights) and JV reporting obligations, PE Investor can manage cash flows and influence JV performance.

Ability to influence management

- PE Investor's ability to enhance JV performance turns largely on the extent of its board representation and ability to approve and veto JV actions. PE Investor will seek controls over capital expenditures, budget variances, customer and revenue contracts and additional business opportunities of the JV.

Incentivize Management

- Tie management compensation to performance metrics of the JV (not the Public Co) such as EBITDA.

Minimize allocation of Public Co's shared costs

- Improve profitability by limiting Public Co's ability to allocate shared costs to the JV (e.g., cap overhead costs via a management fee and specify which operating costs, if any, can be passed through to the JV).



PE Investor Priority: Maximize Returns: Manage Cash Flow

In order to manage the PE Fund's capital commitments invested at any given time, PE Investor will seek to control the JV's ability to call capital.

Controls on cash distributions

- In order to maximize cash distributions, limit JV's discretion in determining cash distributions, and restrict the JV's ability to recycle cash (i.e., use cash on hand to fund additional expenditures in lieu of calling additional capital).

Restrict capital calls

- Restrict capital calls in excess of PE Investor's capital commitment. Limit (or eliminate) PE Investor's obligation to contribute capital above its commitment amount.

Control budget overages

- Minimize acceleration of cash call schedule by prohibiting budget overages without PE Investor's approval.
- Narrowly define the scope of emergency and compliance expenditures the JV can incur in excess of the budget.

Business opportunities

- Seek veto right's on JV's ability to pursue additional business opportunities. Ring-fence any JV opportunity pursued without PE Investor's approval.



PE Investor Priority: Manage Risk

Impose terms that minimize the risk of the investment.

Obtain controls
on JV's ability to
incur debt

- Prohibit JV from incurring debt without PE Investor's approval.

Expand JV
insurance
requirements

- Limit downside by requiring JV to maintain additional insurance coverage.

Limit recourse
against PE
Investor

- PE Investor will want to cap its liability at the amount of PE Investor's capital commitment. In addition, PE Investor will want to limit its liability to Public Co.

Limit dilution risk

- Restrict ability of Public Co to dilute PE Investor's interest to fund JV expenditures or sole risk projects through additional capital contributions above commitment or through third party investments.

PE Investor Priority: Preserve ability to diversify

Limit application of AMI

- Narrow AMI to avoid limitations on PE Investor's current or future activities and to allow PE Investor to build synergies among portfolio businesses.

Melissa Persons

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Melissa L. Persons is an associate at Gibson, Dunn & Crutcher LLP and is a member of the firm's Corporate Department and practices in the Capital Markets, Mergers and Acquisitions, and Energy and Infrastructure Practice Groups.

Ms. Persons' practice focuses on mergers and acquisitions, private equity investments, and advising clients in the oil and gas, energy and infrastructure industry.

Ms. Persons received her law degree in 2009 from the SMU Dedman School of Law, where she was a member of the Dean's List. While in law school, she served as Articles Editor of the SMU Law Review. She earned her Bachelor of Science in chemistry, with a concentration in biochemistry, from Duke University in 2005.

A member of the Dallas Bar Association, Ms. Persons is admitted to practice in Texas and before the U.S. District Court for the Northern District of Texas.

Representative Experience*

Domestic U.S.

- Counsel to Williams Companies in its \$3.8 billion pipeline joint venture with the Canadian Pension Plan Investment Board in the Marcellus and Utica Basins.
 - Counsel to Summit Midstream Partners in its Double E Pipeline Project joint venture to provide natural gas transportation service from the Delaware Basin to the Waha Hub in Texas.
 - Counsel to Williams Companies the sale of its olefins plant in Geismar, Louisiana to NOVA Chemicals for \$2.1 billion.
 - Counsel to American Midstream Partners in pending \$815 million acquisition of Southcross Energy Partners and substantially all of the assets of Southcross Holdings.
 - Counsel to Encino Energy in connection with the \$1.0 billion equity commitment by Canada Pension Plan Investment Board in Encino Acquisition Partners.
 - Counsel to Williams Companies in connection with its \$50 billion merger with Access Midstream Partners, L.P.
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- Counsel to Luminant Holdings in its agreement to acquire natural gas generation facilities from NextEra Energy for approximately \$1.3 billion.
- Counsel to Woodbine Holdings in its sale of its E&P assets in the Woodbine Shale for approximately \$140 million.
- Counsel to Woodbine Holdings in its sale to a Chinese buyer for approximately \$560 million.
- Counsel to TEAK Midstream in the sale of its pipeline and natural gas processing plants in the Eagle Ford Shale to Atlas Pipeline Partners LP for \$1 billion.
- Counsel to Saddle Butte Pipeline in connection with the sale of its Williston Basin crude oil pipeline and terminal system and natural gas gathering and processing operations to Targa Resources Partners for \$950 million.
- Counsel to Chief E&D Holdings in the sale of its Marcellus Shale pipeline system to PVR Partners for \$1 billion.
- Counsel to Cardinal Midstream in its acquisition of Woodford Shale Assets for \$268 million.
- Counsel to GAIL India in its joint venture with Carrizo Oil & Gas.
- Counsel to Meritage Midstream Services in its sale of Eagle Ford Shale assets.

International

- Counsel to Murphy Oil in its \$2.13 billion sale of Murphy Sabah Oil Co. Ltd, and Murphy Sarawak Oil Co. in an all-cash deal that includes five oil exploration and production projects.
- Counsel to Murphy Oil Corporation in connection with the sale of 30% of its participating interests in several exploration and producing PSCs in Malaysia to PT Pertamina (Persero) for a consideration of \$2 billion.
- Counsel to PT Medco Energi Internasional Tbk in connection with the acquisition of the shares in Lundin Indonesia Holding B.V., which has interests in several PSCs in Indonesia.
- Counsel to Murphy Oil Corporation in connection with the farm-in to a 50% participating interest and operatorship in the Deepwater Block 2C PSC in Malaysia from SapuraKencana, Mitsubishi Corporation and PETRONAS Carigali Sdn. Bhd.
- Counsel to Murphy Oil Corporation in connection with the acquisition of a 40% participating interest and operatorship in the Deepwater Block 2A PSC in Malaysia from BHP Billiton Petroleum.

**Includes matters handled prior to joining Gibson, Dunn & Crutcher LLP*



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Joint Ventures

September 20, 2019

NYSE: WMB
williams.com



Joint Ventures - Governance and Operating Terms

- > **Discussions with other inhouse counsel resulted in “we should have a discussion on this topic”**
- > **JVs can be a challenge – culturally and legally**
- > **Today’s scope**
 - Private equity and public company joint ventures
 - Reasons for investment
 - Party priority differences
 - Unique PE investor priorities
 - JV Operating Agreements
 - Negotiating Challenges
 - Operating Challenges
 - Recommendations

JV Operating Agreements – Negotiation Challenges

- > **Often negotiated concurrently or after the JV governance / contribution agreements**
- > **M&A teams don't always include SMEs in timely or effective manner (operations, accounting, tax, IT, land, etc)**
- > **Difficult to determine all possible scenarios and create solutions**
 - Emergency spending, budget overages, regulatory compliance...there are countless tasks and obligations of an operator
 - Changing overhead structures of operator (re-org to or from matrix organization)
 - Really a pre-nuptial agreement, down to details of failure to take out trash (consequential damages for odor or bug bites?)

JV Operating Agreements – Negotiation Challenges

> Challenging Provisions of JV Operating Agreements:

- Scope of authority (commercial/operations)
- Budgeting (& risk of OPEX increases)
- Compliance
- Standard of Care
- Defining Services
- Insurance
- Disputes
- Capital Projects

JV Operating Agreements – Negotiation Challenges

> **Scope of Authority:**

- Operator authority on behalf of JV
- Commercial agreements
- Capital Commitments
- Agent?

JV Operating Agreements – Negotiation Challenges

> Budgeting:

- Contentious enough in wholly owned entities
- Cycles for review and approval
- Approval requirements
 - If no approval, what is the fall back?
 - If disputes remains, how is it resolved?
 - ADR
 - Funding and dilution
 - Operator takes liability
- OPEX exceedance of budget
 - Emergencies
 - Change in law
 - Compliance with law (changes or otherwise)

JV Operating Agreements – Negotiation Challenges

> Standard of Care:

- The best my overworked and underpaid employees can do...
- Be cautious with “standard of care”
 - Prudent Industry Practices
 - Endeavor to operate with good industry practices
 - Compliance with Laws
 - Current and future?
- Limitation of Liability
 - But you are the operator – I shouldn’t be liable as the non-operator
- Exceptions to Limitation of Liability
 - Gross negligence and willful misconduct
 - Consider defining gross negligence and willful misconduct (or leave it up to a jury...)

JV Operating Agreements – Negotiation Challenges

> Services Defined:

- Definition of Services set the scope of obligations
 - Commercial
 - Construction
 - Operations
- Direct charges vs Management Fee recovery for Services
 - Normally described in Accounting exhibit
 - Need to have cogent explanation for methodology for allocation to JV services
 - Corporate overhead
 - PP&E
 - Capital projects
 - O&M
- General obligations regarding services can be fodder for litigation later
 - Maintain the plant in good working order
 - Provide services in accordance with all laws
 - Some laws give discretion to Operator (PHMSA/API references to RAGAGEP)

JV Operating Agreements – Negotiation Challenges

> Insurance:

- Really an extension of liability
 - Property
 - Business interruption
 - Comprehensive and General Liability
- Separate policy vs insurance to extent of ownership interest
 - If carried by each owner, brings additional considerations
 - Self insurance is a credit risk
 - Operator indemnification
 - Third party tort liability
 - Separate insurance policies can muddle the litigation waters
 - Collateral source rule
 - Waiver of subrogation?
 - Rebuild
 - Operator should not have to wait on insurance to fund repair / rebuild
 - Should there be capital call requirements related to rebuilding facility?

JV Operating Agreements – Negotiation Challenges

> Disputes:

- ADR
 - Confidentiality
 - Panel size determined by dispute size
 - Can limit discovery
- Consider handling budgeting disputes distinctly
 - Need a faster resolution than most disputes
- Intra-JV disputes in third party litigation
 - Joint defense agreements
 - Operator defense and obligation of JV members in that defense

JV Operating Agreements – Negotiation Challenges

> Capital Projects

- Stages of approval
 - Concept
 - Design
 - Construction
 - Commissioning
- CAPEX Budgets
 - Overages
 - Contract disputes
 - Force Majeure
- Used to expand the business of JV
 - LLC governance issue
 - Funding

Joint Ventures: Operating Challenges

Selection of Representatives on JV:

- > Representatives on JV management committees should be determined by the appropriate business person in consultation with Legal
 - Consider LLC governance provisions that may restrict who can be appointed

- > Be clear with representatives what level of authority is necessary to transact the JV business
 - Reps need to understand internal and JV requirements for budgets, capital projects, and delegation of authority

- > Non-officer representatives should be advised to consult with RMID to understand the D&O coverage available to them
 - Some JV agreements may provide for indemnification of its officers or representatives

- > Consider targeted antitrust training for your representatives
 - Antitrust opening statement for JV meetings

Joint Ventures: Operating Challenges

> Transition of JV from negotiations to operations

- Consider developing process for transition of the JV from the deal team to the operating team that will include involvement from Legal (deal lawyer should take active role in the transition)
- Communication of key deal terms is critical
 - Accounting is your friend...
 - New cost centers / allocation methods that comply with JV Operating Agreement terms
 - New billing or timekeeping entries may be required

> Corporate Support

- Corporate support (normally defined in Services) requires additional work
- Minute books should include:
 - approved minutes of each meeting of the management committee of the JV,
 - all actions by written consent, and
 - the organizational documents of the JV.
- Clean copies of the meeting materials (both pre-read and handouts) should be retained in addition to the minute books.

JV Operating Agreements – Recommendations

- As Operator, you should know your corporate culture and be able to explain
 - Organization structure: separate business units or matrix
 - Method of corporate allocation
 - Accounting for direct billing and work orders/capital projects
 - Understand and be able to articulate and defend
- Lessons Learned exercises
 - Management Fee analysis
 - Budgeting experience
- Form agreement
 - Drafting exercise is beneficial, paced interaction with SMEs and deal team
 - Eliminates (or easier to quantify) contractual or cultural gaps in different operating agreements
 - Know your positions before the negotiations begin
 - Facilitates SME review and SME/Management/Deal Team interaction
 - Quicker review cycles because only reviewing revisions to standard provisions
 - Each SME already familiar with term and defense of position (ie corporate overhead, allocation methodology,

Mary Frances Edmonds - VP & AGC of The Williams Companies, Inc. (NYSE: WMB)



Began career at Williams in 1996 and worked in very distinct roles and business units:

- Attorney, Unregulated mergers and acquisitions
- Senior Attorney, Commodity trading, structured transactions (including joint ventures and M&A)
- Manager, Commodity Contracts administration and risk management
- Senior Counsel, Gulf of Mexico / offshore construction and commercial agreements, structured transactions (including joint ventures and M&A)
- VP & Assistant General Counsel
 - Williams Midstream (all unregulated business units) (2011-2013)
 - Northeast and NGL/Petrochemical Operating Areas, Engineering & Construction, and Operational Excellence (2013-2014)
 - Commodity Trading, Project Execution, EH&S, IT, Supply Chain (2014-present)

