Collaborative Business Structures

Robert George, Managing Director
CHESTERFIELD GROUP

Background

A typical company can be thought of as a Management Group developing and executing strategies and conducting the company's business through a series of ongoing relationships between that management group and at least the following other groups:

- Customers
- Vendors
- Owners, including their representatives, the Board of Directors
- Financing Sources
- Employees
- The Community at large

In its simplest terms, Management's success depends on how well they manage and balance those relationships.

The relationships with these five groups are conducted in very different ways, but, at least in the short term, they are each primarily a "zero sum game". That is to say, a dollar can only be added to one party's pocket by getting that dollar out of the pocket of one of the other groups. Each relationship involves an ongoing negotiation, with each party constantly considering its options to raise price, buy from a competitor, go to work elsewhere, etc., in order to move the "price point" of that relationship away from the other party and toward themselves. Notwithstanding the negative images that go along with this description, this approach is completely appropriate for those situations where the parties have competing goals—as is the case in the great majority of daily business interactions.

A New Paradigm

Occasionally, however, business people—particularly those charged with charting the overall course of the company—are presented with a different kind of situation that calls for a different approach and, very likely, a different structure. In these situations

- The parties share a **common goal**.
- There is **no price point** to negotiate.

- They actually **need each other** to reach their goal in the most effective way.

In the heat of daily battle, the important differences between these situations and those described above involving competing goals often go unappreciated.

Here are some examples of such situations, which are actually quite common and can often be addressed through implementation of a Collaborative Business Structure (see below).

- Your products or services appear to be applicable to an all-new market, but you lack the expertise to successfully enter it.
- You face a promising growth opportunity that carries with it the potential for conflicts of interest with existing customers or vendors.
- You are a financial institution that wants to move beyond simple lending in search of better spreads but lacks the expertise and infrastructure necessary to prudently do so.
- You feel that prudent growth requires an investment in infrastructure beyond what can be justified in the near term, and you would like to be able to "rent" infrastructure—thereby converting a fixed cost to a variable cost—until you are large enough to justify such an investment.

Of course, every situation is different, but these and many other challenges to reaching your company's full potential can often be met through working with another company or companies in a Collaborative Business Structure. We use this term to mean any one of a number of structures through which two or more participants pursue a common goal by pooling some or all of their capabilities.

Collaborative Business Structures

A Collaborative Business Structure is designed to bring parties together in a long-term relationship to achieve a common goal. Sometimes this is done through the formation of a new entity, such as a partnership or joint venture that explicitly sets up an opportunity for each of the participants to combine its strengths with those of its partner to their mutual benefit. Clearly, this works best when the strengths of each one match up well with the constraints of the other. Other situations call for methods of cooperation that don't require a new entity, e.g., a licensing agreement or an outsourcing arrangement.

Of course, the idea of collaborations among companies that capitalize on each other's strengths is not new, nor is its appeal. However, experience tells us that they often fail to fulfill their potential because the participants don't set them up in the optimal way. The most common problem is to use a structure where one of the partners can, on occasion, enhance his own interests by doing something that is contrary to the best interests of the collaboration. Structures that rely on personal trust or legal documents to anticipate all such opportunities for dysfunctional behavior are unlikely to thrive over the long term. **The successful long-term structure must consistently provide rewards for joint action that exceed those for individual action.**

Finding the structure that is effective involves a lot of hard work and thought in choosing partners and structuring the relationship around the concept of goal congruence. Since **you can always trust your partner to act in his own best interest**, the idea is to structure the relationship such that, when he does so, he is also acting in the joint best interest.

As one might expect, that is easier said than done. However, it is usually possible. Successfully structuring such an arrangement requires paying a great deal of attention to the details with respect to the following:

- **Choice of Participants**: How does one find and evaluate a potential partner whose strengths and weaknesses complement our own? Having found one, how do we persuade him of the wisdom of joining with us?

- **Choice of Structure**: From the number of structures are available, including partnerships, joint ventures, outsourcing arrangements, management agreements and licensing agreements, how do we choose the best one? How can we set up a structure such that all participants prosper through the prosperity of the new entity and won't be tempted to work at cross purposes with that entity to promote individual prosperity—in other words, how do we structure our venture to establish and maintain goal congruence? How can we structure a compensation system to work with that goal congruence? How can we work around potential conflicts of interest?

- **Corporate Culture:** This is a different way of doing business. How do we achieve the buy-in necessary to make it work? How do we change "mine/yours" to "ours"?

A properly structured Collaborative Business Structure can provide opportunities for prosperity that leverage up your company's strengths. They often provide an alternative to other structures, such as acquisitions, that will require much less capital, lowering substantially the risk of pursuing the opportunity.

CHESTERFIELD GROUP

The CHESTERFIELD GROUP has a great deal of experience putting together structures that help companies achieve mutual, shared goals. From that experience, we have distilled a number of principles that help us methodically surface alternative structures to achieve those goals while minimizing the potential for unpleasant side effects.

For more information, please refer to our web site at

www.CHESTERFIELDGROUP.com

Please contact us, if we can be of assistance or if we provide you with more information.

58 Reed Ranch Road, Tiburon, CA 94920
(415) 435-8585 fax (415) 435-1726
rgeorge@CHESTERFIELDGROUP.com