403 Joint Ventures in the International Marketplace

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Faculty Biographies

Sabine A. Chalmers

Sabine A. Chalmers is the chief legal officer and company secretary of InBev SA/NV, the world's largest brewer located in Belgium. Her responsibilities include managing a legal and corporate affairs team of over 200 on a global basis. She is also a member of InBev's executive board of management reporting to the company's CEO.

Prior to joining InBev, Ms. Chalmers was in-house counsel at Diageo plc, where she held a variety of positions in a number of countries, including those of general counsel Latin America, general counsel international, and general counsel North America. While at Diageo, she provided counsel in a variety of substantive areas, including commercial law, mergers and acquisitions, and a variety of international joint ventures.

Ms. Chalmers received an L.L.B. from the London School of Economics.

Stephen Faciszewski
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Cheryl Fackler Hug

Cheryl Fackler Hug is a senior legal director in the legal department of Sun Microsystems, based in Santa Clara, California. Ms. Fackler Hug is currently responsible for managing a team of lawyers supporting business teams that develop and manage global partner strategy, global client solutions, global service delivery, and global alliances, including the Sun-Fujitsu alliance. In addition, Ms. Fackler Hug and her team manage global antitrust compliance issues for Sun.

Previously, Ms. Fackler Hug supported Sun's Europe, Middle East, and Africa sales organization from Geneva, Switzerland, where she managed more than 29 legal professionals based in 13 different countries. Ms. Fackler Hug previously led the legal support for Sun's expanding operations first in Asia and then in Latin America. During her career at Sun, Ms. Fackler Hug has been involved in the setting up of or supporting various international joint ventures in which Sun has or had an interest.

Prior to joining Sun, Ms. Fackler Hug worked in the corporate department of Gibson, Dunn & Crutcher's Washington, DC office. In private practice, Ms. Fackler Hug specialized in commercial transactions, mergers and acquisitions, corporate governance, and compliance work, with a particular expertise in Russian joint ventures, expropriation, and the Foreign Corrupt Practices Act.

Ms. Fackler Hug received her B.A. from Wittenberg University in Springfield, Ohio and graduated from the University of Michigan law school.

Sally March

Sally J. March is a dual-qualified lawyer with nearly twenty years experience in international business transactions. Ms. March went in-house with a California-based media technology company and in 2002 became head of legal for BBC Technology, a group of subsidiaries of the British Broadcasting Corporation which were acquired by Siemens in the fall of 2004. She is currently advising a media start-up.

She has lived and worked in London since 1986 when she joined a Washington, D.C. firm which was one of the first into Moscow during perestroika. From 1988 to 2000, her practice focussed on the former Soviet Union where she advised on dozens of joint ventures and wrote extensively on the Soviet law on joint ventures. From 1993 to 1997, Ms. March was the managing partner of the Moscow and St. Petersburg offices of Pepper, Hamilton, a Philadelphia-based law firm. Ms. March and two of her partners represented a major Russian oil refinery in a dispute with its Swiss joint venture partner. The arbitration took place in Stockholm with ad hoc rules. Pepper, Hamilton advised the Russian and Kazakh governments on law reform and represented the Government of Kazakhstan in its major privatizations. Ms. March led the team advising the Russian Securities Commission on securities legislation and, with PWC, ran the pilot IPOs of two enterprises.

Ms. March is a graduate of the University of California - Hastings College of Law and holds an LL.M. from the London School of Economics.

LEGAL ISSUES COMPARATIVE CHART ON DISTRIBUTION

	Typical Reseller Distribution Model	*Joint Venture*	*Franchise*
Basic Definition	Contractually-based, accredited reseller (often, with marketing help) authorized to sell specific Company products and services, use specific Company logos, depending on level of accreditation	Association between persons or companies engaged in the joint undertaking of some commercial enterprise for mutual profit	Generally defined by statute, but 3 basic elements: (1) trademark or brand identification (e.g., use of Company logo /marks); (2) franchisor control of franchisee operations; (3) franchise fee.
Format Issues			
Basic	Standard Reseller agreements	New entity can take various forms and need not be a separate entity, however contacts involved would likely consist of + SH agreement + by-laws + TM agt + Dist Agt + start-up investment Often incorporated as an LLC	Franchise Agreement + Registration Documents (in certain jurisdictions) + Periodic Disclosure Documentation (in certain jurisdictions)

LEGAL ISSUES COMPARATIVE CHART ON DISTRIBUTION

	Typical Reseller Distribution Model	*Joint Venture*	*Franchise*
Control	Contractually-based, Company's control limited to: 1) accurate representation of Company products/services; 2) geographic and/or skill-based limitations on authorization to resell; and 3) enforcement of reasonable contractual resale restrictions. In the US, usually either party may terminate for convenience or for non-remedial breach. Some jurisdictions (particularly in Latin America and EU and a few US states) may limit ability of company to terminate without cause or without payment of termination damages.	Varies depending on the nature of the JV – for example, if the JV is an LLC, then Company's control over it is hampered; also varies depending on number of seats Company can name on Board and rules of the by-laws Generally, to refrain from counting headcount/opex, Company would need to control LESS than 50% (often, FASB 51 looks for "effective control")	Contractually-based, but Company is able to impose greater restrictions than with Resellers because of grant of the trademark license. Franchisees generally cannot transfer their business without the approval of the Franchisor. Franchisee must comply with business plans and other rules of Franchisor.
Financial Compliance	Partner is an independent company that shares no profits with Company	Company can appoint finance controller of JV, subject to "control" issues. Not a requirement or a right unless specified in formation documents	Profit-sharing dependent on franchise agreement terms; franchisees usually beholden to franchisor for licensing/RTU, leasing/rental, and/or re-payment of initial investments made by franchisor.
Permanent Establishment Concerns	Not relevant to this model – as long as Company does not co-locate employees with partner	There are issues if Company has employees performing work in-country for the JV	May be relevant to this model if Company co-locates employees with Franchisor.

LEGAL ISSUES COMPARATIVE CHART ON DISTRIBUTION

	Typical Reseller Distribution Model	*Joint Venture*	*Franchise*
Ensuring profit mechanisms	Generally,no obligation to ensure profitability of partner, but Dealer Protection laws in some jurisdictions (esp. LA and EU) may require reasonable return on investments for resellers.	Important to ensure success for each venture partner, to minimize disputes. However, can use shareholders' agreement to establish mechanisms to help keep returns equitable for each partner.	In some cases, this is legally mandated.
Legal Issues			
Export Control	Company obligated to put reseller on notice of their obligation to comply with export control laws, but will not be liable for their violation unless had reason to know violation was occurring.	JV Partner has higher level of obligation, depending on size of ownership and level of involvement in the JV. At a minimum, will need to use "best efforts" to have JV avoid export control violation.	Responsibility of Franchisor is similar to that of Company in the reseller situation, although Franchisor may have more deemed knowledge, depending upon how franchise relationship is run.

LEGAL ISSUES COMPARATIVE CHART ON DISTRIBUTION

	Typical Reseller Distribution Model	*Joint Venture*	*Franchise*
FCPA	Company can be subject to violations of the FCPA if it "knows or should have known" that a partner is paying bribes and Company is somehow financially enabling them to do so. This imposes a strong due diligence requirement on Company for any Red Flags and generally to "know your partner". If the Company discovers that a partner has paid a bribe, then Company likely will need to terminate and not make any payments to such reseller (even settlement payments). It is unlikely that Company would be liable for inaccurate accounting of bribery related activity by partners but Company can be liable if it inaccurately accounts for money paid to resellers.	Founder can be subject to violations of the FCPA if it "knew or should have known" that the JV is paying bribes and Company is somehow financially enabling them to do so. This imposes a strong due diligence requirement on Company for any Red Flags and generally to "know your partner". With a JV model, the government will expect that Company do much more due diligence than for partners and have more control, therefore are more likely to "know" about bribes. Discovery of bribery in a JV likely means Company has to terminate the JV unless Company can purge the management, stop the business associated with the bribery, etc. For minority JVs, Company must use "good faith" efforts to ensure that the JV has internal controls that meet the SEC sections of the FCPA.	Company can be subject to violations of the FCPA if it "knows or should have known" that franchisees are paying bribes and Company is somehow financially enabling them to do so. This imposes a strong due diligence requirement on Company for any Red Flags and generally to "know your partner". If the Company discovers that a franchisee has paid a bribe, then Company likely will need to terminate and not make any payments to such franchisee (even settlement payments). It is unlikely that Company would be liable for inaccurate accounting of bribery related activity by franchisees but Company can be liable if Company inaccurately accounts for money paid to franchisees.

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LEGAL ISSUES COMPARATIVE CHART ON DISTRIBUTION

	Typical Reseller Distribution Model	***Joint Venture***	***Franchise***
Disclosure Issues	None, unless there are material disputes, which are very unlikely.	Higher level of SEC reporting required than for resellers. Assuming minority ownership, disclosure is less than for franchises in certain states.	In at least 10 US states, to form Franchises, the Company must file a disclosure statement. This is a very detailed document that requires disclosure of ANY disputes (whether they reached litigation or were settled) with resellers since we began operations. The first disclosure statement can be very costly to complete (upwards of $1 million in outside counsel fees) but thereafter the costs to update are not so significant. May be some disclosure obligations under non-US franchise law statutes also.

LEGAL ISSUES COMPARATIVE CHART ON DISTRIBUTION

	Typical Reseller Distribution Model	***Joint Venture***	***Franchise***
IP Ownership	Contractually-based: each party owns its pre-existing IP (including derivatives, enhancements); any joint IP development subject to same issues as identified in JV section herein.	IP should generally be Company's – need to grant access/use rights and maintain ownership; may need confidentiality protection; need to provide for return of IP at termination or maybe in the event of certain types of disputes Need to determine if JV partner would have IP? Is it possible that the JV would develop IP? Need to anticipate and decide what happens to it upon termination or disputes (IP in escrow) If IP will be developed by JV, where should it be registered/protected? Who can exploit it? Who will protect against infringement?	IP should generally be Company's- usage rights and limitations covered in franchise agreement, including expiration of such rights on termination of franchise relationship. As franchisor, Company should have regular access to market, financial, and other data relevant to franchisee's business. All of these rights and obligations would be contractually based.
Competition/Pricing Laws	Price discrimination laws apply, as do competition law principles of collusion, allocation and resale price maintenance	Price discrimination laws would apply if there is a competing parter in the region, but this is unlikely.	Price discrimination laws apply, as does principle of collusion in relation to franchisee termination. There can be limitations on price increases to franchisees. Exclusive territory rights may prohibit direct or internet sales in some areas.

LEGAL ISSUES COMPARATIVE CHART ON DISTRIBUTION

	Typical Reseller Distribution Model	***Joint Venture***	***Franchise***
Termination	Usually handled as a non-renew, but termination for good cause is often contractually viable available as an option and termination for convenience upon contractually mandated advance notice period is usually an option as well. Some jurisdictions have dealer protection laws that mandate payments to resellers upon termination, similar to agent termination fees. Other issues upon termination include business torts such as interference with economic advantage/ contractual relations.	Termination needs to be addressed and governed in the JV agreement. Can be costly if dissolving a separate corporation.	Can be very expensive. Some jurisdictions require a payout (may be statutorily granted % revenues/profits or subject to common law adjudication). There can be both civil (incl. Punitive) liability for wrongful termination. Other issues upon termination may include business torts such as interference with economic advantage/contractual relations.
Specific legal issues		Generally few laws that specifically deal with JVs; instead, JVs subject to various other laws (such as those relating to corporations, commercial transactions, competition, etc); Also, there is a risk of "piercing the corporate veil" and getting to Parent Company.	Registration requirements, vary from state to state and country-to-country. Sometimes there are disclosure requirements for the franchisor.
Vicarious Liability	Limited risk unless Company employee expressly guarantees reseller action.	Possible, depending on amount of oversight Company has of JV	Possible, depending on how much active control Company takes of Franchise.

LEGAL ISSUES COMPARATIVE CHART ON DISTRIBUTION

	Typical Reseller Distribution Model	***Joint Venture***	***Franchise***
Due Diligence Issues			
Reputation of partner	Required	Very Important	Important
History in partnerships	Must review particularly for history of litigation or bribery	Very Important	Important
Financial Health of partner	Required if Company extends credit	Very Important	Important
FCPA	Will be required in all high risk countries	Very Important, history of bribe-paying will mean JV cannot go forward	Important
Export Control	Required only if Red Flag exists	Very Important	Important
Local Concerns			
Local Protections for partner	Dealer Protection Laws in some jurisdictions.		Some jurisdictions make termination difficult.
Labor	Not relevant unless Company funds reseller employees.	Important	Not relevant unless Company funds JV employees.
Local Tax	Probably not relevant.	May be local tax breaks if have local partner.	Probably not relevant.
Local TM issues	Not relevant	Trademark license is provided for use of Company's name. Local laws may require registration of the TM license.	Trademark license is provided for use of Company's name. Local laws may require registration of the TM license.

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LEGAL ISSUES COMPARATIVE CHART ON DISTRIBUTION

	Typical Reseller Distribution Model	*Joint Venture*	*Franchise*
Local registration	No registration required	If new corporation, need to incorporate per local law.	Some jurisdictions have expensive registration processes, the violation of which can be criminal (see disclosure section above).
Other	Short of contract termination/non-renewal, no right to terminate or influence employment status of poorly performing local management or sales team	Often difficult to dismiss even poorly performing local management team. Need to determine if Company-appointed directors have fiduciary duty to JV or to Company – may be determined by local law.	Limited influence over employment decision-making, any influence must be contractually based and would need to be linked to, for example, a decline in franchise profitability, or damage to franchisor brand.
Critical Legal Terms			
Conflicts/Disputes	Contractually-based: executive escalation, ADR, and use of courts are all options	Define and anticipate deadlocks; provide for their resolution	Contractually based, but many statutes favor franchisee in dispute resolution processes and procedures (ADR, etc.).
Termination/Exit	Competition law issues (e.g., collusion) or business torts. Dealer protection laws may make it expensive or time-consuming to terminate.	Failure rates are high so must be prepared What happens to employees? What happens to assets? What happens to agreements in JV's name? What happens to customers? What happens to IP? What happens to legal entity?	Primary Concern: Mandatory pay-out on termination or program wind down? Secondary Concerns: Any competition law issues (e.g., collusion) or business torts?

LEGAL ISSUES COMPARATIVE CHART ON DISTRIBUTION

	Typical Reseller Distribution Model	*Joint Venture*	*Franchise*
Trademark license	License to reseller for logo only. NOTE: if allow resellers to resell Company-logo'd services, may fall under franchise laws.	Yes	Yes
Investigation Cooperation	May mandate a certain level of cooperation by contract; but reseller failure to cooperate will result only in contract breach for which Company may terminate.	Should be addressed in JV agreement.	May mandate a cooperation by contract and refusal to cooperate may constitute "good or just cause" for penalties to franchise or exercise of termination rights.
Continuation of service responsibilities when relationship ends	By contract. Usually none.	Must be set forth in JV agreement. Likely some continuation at least for a period.	In Franchise Agreement. Possible support of new franchisee.
Access to books and records	May mandate access by contract, but resellers are generally opposed to unfettered access and will require Company to pick up the tab for any audit. May hide behind data protection laws.	In JV agreement. Can have good audit rights, but then increase risk that Company will be liable for things like FCPA and export control violations, because "should have investigated".	May mandate access by franchise agreement with greater success than resellers based on "open books" nature of franchisor-franchisee relationship.
Other key legal terms	Resellers can usually transfer their business easily. Company can also transfer.	Restrictions on transfer of ownership of JV partner. Company may want to preserve "veto rights" over certain actions of the JV.	Franchisor may restrict right of franchisee to transfer its business. Easier to require "Company only" business.

403 JOINT VENTURES IN THE INTERNATIONAL MARKETPLACE

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Sally March

WHY A JOINT VENTURE?

- Local partner essential?
  - Local law may require local ownership
  - Rapidly changing political conditions may dictate need for local partner
  - Local partner be may be favored in licensing or business permits or may be required for sales into certain industries
  - Local partner may have access to tax benefits, etc., reducing cost of doing business
  - Knowledge of local market or incumbent marketshare

- Size of project is beyond the resources of individual company
- Sharing risk
- Testing the water
- Technological developments

WHY NOT A JOINT VENTURE?

- Partners' interests may not be aligned
- Differences in experience, business culture, governance, etc add stresses to management
- May increase risk of failure
- It may be difficult/costly to terminate
- One company will not have complete control

OTHER OPTIONS

- Reseller or distributor
- Franchise
- Joint R&D arrangement
- IPR license
- Wholly-owned subsidiary
- Other

TYPES OF JOINT VENTURE

- Limited liability company
- Limited liability partnership
- General partnership
- Contractual co-operation

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WHICH PARTNER?

- Answering “why?” may answer “who?”
- Partner due diligence
- Do you know what you don’t know?
- Do you know what they don’t know?

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Things I wished I’d known…

- The law requiring us to have a local equity partner is likely to change ….

- Cheryl is going to talk about joint ventures vs using resellers and other channels. She'll also talk about partner selection/ investigation.
- Steve is going to cover some legal issues of operations, including transfer pricing
- Sabine is going to focus on what to do when it all goes wrong.

JV vs Reseller vs Franchise To Expand Distribution of Products/Services

- Business Goal: find model where the channel partner looks, feels, and acts like your company, without the Headcount, cost and burden of a wholly-owned subsidiary. (i.e. Legally "off-balance sheet")

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Various Options Exist

- ***Reseller:*** Where you agree contractually to allow another company to sell your products; may be exclusive or non-exclusive. Ability to restrict behaviour depends; is often subject to anti-trust laws.
- ***Franchise:*** Similar to a reseller except the franchisee has the right/obligation to use the supplier's trademark. Franchisor has additional control due to fact that franchisee is using the franchisor's trademark.
- ***Joint Venture:*** An association between companies or persons (a legal entity) engaged in the joint undertaking of some commercial enterprise for mutual profit; All contribute assets and share risks.

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Comparison of Reseller vs. Franchise

FRANCHISE	JOINT VENTURE
Independent Contractors	Partners
Less Control - Enforce Contract	More Control: Shr. Agmt, Board, Audit, Choosing Mgmt.
Different Companies, Trademark use only	TM use for trade and company name, full look and feel
ROI "guaranteed" to franchisee	Shared Profits and Risks (in Theory)
High cost to Terminate	Greater flexibility with regard to exit
High initial investment for franchisee	Flexible initial investment for either party
Possibly less risk of liability for Franchisee's actions	Limited Liability (in theory) but probably greater fiduciary liability

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Sun's Experience

- A low cost way of having a Sun presence
- Former resale partner (now JV partner) trades under Sun's brand and name (Sun Microsystems of ...)
- Sun holds a minority equity (49%)
- Sun appoints members of the Board
- Sun appoints the Finance Manager, who reports to Sun Finance (dotted line)
- Currently two in APAC, considering Latin America

WHICH PARTNER?

- Answering "why?" may answer "who?"
- Partner due diligence
- Do you know what you don't know?
- Do you know what they don't know?
- Easier to control a weaker/poorer partner, but they become more financially dependent, harder to get out.

PARTNER DUE DILIGENCE

- Internal Resources (finance, sales, etc.)
- External Resources:
  - Control Risks, Accounting Firms, etc.
- Research officers, directors and management, as well as company.

FCPA (Post-Sarbanes-Oxley)

- Potential Liability for Bribery/Other Fiduciary obligations by JV Partner and/or its management/directors
  - Majority Ownership = Full obligation for adequate internal controls and compliance program.
  - Minority Ownership = Use "best efforts" to ensure effective compliance program and internal controls PLUS broad rights to terminate and audit JV
- Any government ownerships/close relationships by JV partner must be researched carefully.
- JV agreement: reps/warranties, termination rights, set policies, approval rights for contractors; may need to terminate if problem arises

Lessons Learned

- Minority ownership without "effective control" means no consolidated reporting.
- However, FASB 51 requires some level of autonomy to avoid "effective control"; this means less control than business often wants.
- Although in theory one owner can force the change of the JV management team, in practice it is very difficult.
- "Maintenance cost" of JV higher than for subsidiary, because must actually hold directors meetings, etc.
- Will be continual pressure to add additional capital.

Lessons Learned

- 50/50 JVs can work, e.g. Fujitsu-Siemens in Europe (however, Fujitsu has greater Board membership).
- General Manager can have a great deal of power, particularly in less developed jurisdictions. Make sure understand local rules on management, how you can remove GMs, etc.
- Potential conflict of interest for Board Members between the interest of the JV and the interest of the Shareholder.
- If IP will be created by the JV, need to consider IP issues up-front. Need to revisit question if business changes over time.

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Lessons Learned

- Antitrust issues:
  - Less of a concern if the partner is a vertical competitor only.
  - Can be significant if partner is a horizontal competitor
  - R&D JVs can have issues too.

Operational Issues to be Considered at the Outset

OPERATIONAL SCOPE

- JV´s success correlates to parties´ ability to create and implement mutually satisfactory JV operational structure
- Collective decision-making by JV parties consciously negotiated (as distinct from respective parties´ positions in the JV)
- Ensure JV parties´ management supports operational structure established
  - Identify:
    - at least one key decision-maker in JV jurisdiction as "point person"
    - composition of decision makers

OPERATIONAL SCOPE-Topics

- Specific topics to consider (varies with ultimate JV legal structure):
  - Create cross-functional team staffed with key decision-makers from JV parties
  - 3-5 year JV operating plan, specifically addressing
    - Products within scope of JV
    - Steps in the value chain
    - Target territories

OPERATIONAL SCOPE-Topics (cont.)

- Document core responsibilities and corresponding allocation among the JV parties (as relevant) and JV:
  - Exemplary issues:
    - » Raw material supply/procurement;
    - » Product manufacturing (at least one of JV parties, or another?);
    - » Product recall process;
    - » Enforcement of rights in JV market—local jurisdictions may require that JV have responsibility; and
    - » Technical consumer/product information and support.

OPERATIONAL SCOPE-Topics (cont.)

- Develop JV organizational structure, as relevant
- Procurement/management of physical office/building space;
- Create JV operating infrastructure
  - Integrate with JV party (ies) infrastructures
  - Avoid JV party playing too dominant an operational role, unless mutually consciously established

- Cultivate and engage relationships with local resources:
  - Local regulatory and other relevant government offices
  - Key service providers (external auditors and legal resources)

OPERATIONAL SCOPE-Topics (cont.)

- Establish broad policies, procedures and systems
  - Maintain as broad scope as possible, yet remain open to modification that a JV party requires
  - Example:
    - Document retention
      - Legal Privilege
      - Cross-border data privacy
  - Ensure
    - JV party compliance
    - consistency with local legal requirements/practice

PERFORMANCE (OPERATIONAL)

- JV success hinges on JV´s/JV parties´efforts in achieving agreed-upon performance standard
- Technology Improvements (when R&D is component of JV)
- Technology Rights Enforcement
- Quality
  - Raw materials
  - Manufacturing and packaging processes
  - Marking, advertising and marketing product (and packaging generally)
  - Technical product information
    - Manufacture
    - Documentation
      - Reports/Communications

Transfer Pricing

- Cross-border transfer pricing issues arise when:
  - At least one JV party (or affiliates) engages JV in connection with:
    - Movement of tangible products;
    - Transfer of intangibles
      - Royalties
      - Cost-sharing arrangements
      - Ownership and use of intangible property
    - Performance of Services (including professional and financial); AND
  - At least two jurisdictions having disparate marginal tax rates.

Practical Advice

- A solid legal framework (with all relevant ancillary components committed to written documents) will facilitate operational success
- Understand the business deal and the parties' respective objectives in creating the JV
- Early on, distinguish between business and legal considerations and track them
- May be useful to create Deal Synopsis as part of document execution process

Lessons Learned

- Never conclude a JV, without hiring a local authority to identify any issues with the other party (ies)—when questions arise during due diligence process.
- From the beginning, understand how employee termination process is conducted in the local jurisdiction, and act swiftly, when necessary.

Planning the Exit

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Duration and Termination

- Limited or unlimited duration?
- Conditions precedent to commencement
  - Agreement on business plans
  - Regulatory permits and licenses
  - Shareholder approval
  - Tax clearances
  - What happens if they don't happen?

- Reasons for Termination
  - time
  - event (other than time)
    - regulatory action
      - e.g., loss of licence, anti-trust authority order
    - by agreement of partners
    - right given to a partner
      - liquidate/dissolve/ withdraw
    - change of control of one of the partners
    - insolvency – JV, partner, parent
    - default
    - force majeure or frustration
    - completion
    - forfeiture

- unsuccessful joint venture
- joint venture successful in reaching limited purposes
- Reasonable belief by one party that the other has or will commit a violation of FCPA or other anti-bribery law
- Reasonable belief by one party that continued participation in the JV would cause it to commit a violation of FCPA
- Other potential fiduciary issues, e.g., violation of export control laws
- partners goals have diverged
  - most frequent
  - corporate policy decision rather than conflict between partners

Disputes

- Need to consider at the outset what types of disputes are likely to arise and what is most efficient/effective way of resolving each type of dispute
  - Partner/partner
  - Expert
    - technical matters, including accounting
    - binding
  - Mediation
    - structured negotiation process
    - non-confrontational environment
    - independent mediator assists partners resolve dispute
    - usually not enforceable
  - Arbitration
    - binding
    - non-binding
    - adversarial process
    - award can be enforced in most jurisdictions
  - Courts

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- Think creatively about escalation of disputes, e.g.,
  - within the management team
  - one director from each party
  - then CEO of each party
  - then mediation or arbitration

If opting for arbitration or courts, think through where all the parties can be joined, convenience of venue, language, enforcement

Things I wish I'd known…

- When the JV is incorporated under the laws of one jurisdiction and the shareholder's agreement is governed by the laws of another jurisdiction with an arbitration clause and the finance arrangements (which will include guarantees from the partners) permit the banks to sue in the courts of their own jurisdiction, then there is no place where all the parties can resolve everything when the venture goes sour.

Additional Issues to Consider

JV Partners

- Parent or subsidiary
  - parent guarantee
- Good standing
  - legal and reputational
- Creditworthiness
  - of partner(s)
  - inequality of creditworthiness

- Restraints
  - foreign ownership
    - control
  - exchange control
    - convertibility of currency
  - anti-trust
    - will join joint venture result in significant market share in a particular market
    - notification/registration required/desirable
  - licences and permits

Consequences of being a partner

- Taxation
    - consortium or group relief availability
- Accounting
  - full consolidation and recognition of interest
    - e.g., subsidiary undertaking
  - exercise majority of votes
  - exercise control over management
    - appoint majority of management
  - exercise "dominant influence"

Consequences of being a partner (cont.)

- equity accounting
  - associated undertaking
  - e.g., "severe long-term restrictions"
- investment with recognition of distribution income
- proportional consolidation
  - e.g., unincorporated association, partnership, limited partnership
- Disclosure and reporting requirements
  - stock exchange
  - accounting
  - other regulatory

Interests and Contributions

- Design critical to joint venture success
- Aim to:
  - avoid haggling about limited issues
  - encompass both some mutual stimulation to excel independently and to support each other
  - adjust as
    - external environment changes
    - partner(s) learn more about others contributions and benefits
  - recognise that some contributions may be assessed differently from an economic (efficiency) and strategic (risk dependence) standpoint

Objectives may define contributions

- Specify what goes into and out of joint activities
  - products
  - technologies, know-how, information
  - cash
  - management practices
  - less tangible
    - use of a brand
    - borrowing of a reputation

- Examples of contributions
  - assets
    - licence of intellectual property rights
      - technology to be provided
        - » covered/not covered by intellectual property rights
      - licence or transfer
      - anti-trust application to terms of intellectual property rights
      - terms and conditions of licence
        - » time
        - » procedure
        - » geographic scope
        - » exclusive/non-exclusive
        - » right of partner(s) to use
      - availability of improvements

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Valuation of Contributions

- Valuation difficulties arise with:
  - "embedded" contributions and benefits
  - reconciling book value and market value
  - unequal distribution of information
  - lack of transparency about benefits obtained and costs incurred

- Need to prevent or minimise valuation conflict:
  - gain experience in evaluating each partner's contributions
  - find external benchmarks to assess each partner's performance and evaluate each partner's contribution
    - critical in assessing true value
  - if no external benchmark, reduce range of interdependencies between joint venture and activities performed by each partner
  - adjust valuation of contribution over time, occasionally after the fact
    - minimise short term reaction

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Things I wish I'd known…

- If valuations of contributions have to be juggled in order to reach pre-agreed ownership interests then it probably isn't a true "joint" venture.
- If the JV is dependent on the other party for certain goods or services, I want to understand their costs and transfer pricing.
- If one partner is noticably "poorer" than the other, yet has greater ownership, the other partner will routinely be pressured to provide additional capital.
- The local partner may not be a good asset manager, but may find "suggestions" from the foreign partner offensive.

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Applicable Jurisdiction

- Not just a question of enforcement – but see Disputes
- Is jurisdiction dictated by scope of operations, geographic or otherwise? Or by regime for necessary licenses?
- Other issues
  - applicable employment laws
  - applicable taxation regime
  - applicable anti-trust regime

Applicable taxation regime

- duties on equity and debt
- withholding tax on distributions
- capital allowances
- rates
- holidays or incentives
- import duties
- tax on establishment of joint venture
- transfer of tax losses
- stamp duties
- thin capitalisation
- transfer pricing

Tax Issues (cont.)

- situation of headquarters
  - tax impact
  - benefit of tax treaties
- restriction on repatriation
  - profits
  - other distributions
  - convertibility of currency

Applicable anti-trust regime

- will joint venture result in significant market share in particular market?
- do relevant thresholds apply?
- notification/registration required/desirable?

OPERATIONAL SCOPE

- Defines activities and tasks performed by joint venture
  - products
  - functions
  - steps in the value chain
  - geography
- Conscious joint decision of partners
  - unlike strategic interests and potential benefits of each partner
  - which are largely determined by individual partner's position
    - sets strategic and economic scope of joint venture

- The goal is for partners with divergent strategic interests and potential benefits to arrive at a shared operational scope for the joint venture
  - sometimes opposite happens
    - partners strategic interest and potential benefits may be aligned, yet their expectations of what the joint venture operational scope ought to be divergent
- Operational scope should be negotiated and arrived at ahead of joint ventures creation
  - unless explicitly negotiated, partners may have different expectations about the operational scope of the joint venture

- Simplest and most effective operational scope is one that fully aligns operational scope with strategic and economic scope of joint venture
  - in way that prevents or minimises conflict
  - complete alignment may defeat the purpose of joint venture
- Operational scope can be made wider or narrower to prevent or minimise conflict
- Prevent or minimise conflict by:
  - including activities that would become sources of conflict if left within partner firm
  - adjusting partner's economic scope (e.g., side payment) so as not to let economic performance of each to get too far out of balance
    - divergent economic performance could compromise agreement on key issues

- Ensure Certainty
- Clarity of objectives
  - agreed business plan
  - specific project
  - continuing business
- Design for contingencies
  - external shocks
    - exchange rate/business cycle shifts
    - change in government policies
    - technological change
  - internal shocks
    - management/ownership turnover
    - serendipitous opportunities
    - allow for termination

Create 3-5 Year Operating Plan

- Consider initial and evolutionary model
- Assess how quickly the model will evolve
- Provide for contingency to accommodate dynamic circumstances

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Governance and Management

Joint Venture Governance

- Define how joint venture:
  - is managed
  - how it is organised
  - how it is regulated
    - by agreements and processes
  - how partners control and influence its evolution and performance
- Forms of governance can be chosen in terms of ability to foster co-operation
- Choice between contractual and institutional forms of governance

- institutional form does not exclude contractual
  - e.g., shareholders' agreement
- but provides institutional context for contractual
- Choice may hinge on whether a "complete" contract can be drawn up
  - that can account for specific future events
  - Choice may hinge on cultural expectations, e.g., local partner must appoint the Director General/CEO who has apparent authority
- Don't overplay the difference between contractual and institutional forms
  - possible to "nest" institutional governance within a contractual design
  - possible to simulate institutional governance through a set of contracts

Joint Venture Management

- Manage the trade-off between control and shared effort
- there are two different dimensions of control:
  - ownership control
  - management control:
    - control over decisions
- the partners need to negotiate on both dimensions

- ownership control
  - a 50/50 share may work best since it allows both partners veto rights but risks stalemate
  - it may be beneficial to cede management and ownership control to the other
  - often in such cases, options to buy or sell are built in to protect the bargaining power of the ceding partner
  - while ownership control may vest with one partner, the other may have veto rights on critical decisions
- management control
  - determined by twin considerations of: (1)who is in the best position to contribute by managing, and (2) who feels most at risk in handing over management control to the other partner
  - often works best by allowing one partner dominant control but allowing the other partner board oversight
  - shared decision making may be the most appropriate mechanism to achieve co-operation

Management (cont.)

- Do any existing employees of the partners have the necessary skills to manage the JV?
  - Business
  - Language
  - Cultural
- Are there any restrictions on nationality of directors?
- How will conflicts of interest be resolved if management is seconded by the partners?
- Are the incentives of the JV management aligned with the objectives of the business?

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Management (cont.)

- Create cross-functional team staffed with key decision-makers from JV parties
- Identify at least one key decision-maker in JV jurisdiction as "point person"
  - Current employee (employed by party in the JV) who will have ultimate responsibility for JV operations
  - New JV employee
  - Consultant/expert (third party)

Develop Organizational Structure

- What staff will service the initial/projected needs of the JV?
- Will the JV operation rely on personnel who are:
  - Permanent/temporary
  - Foreign employed (seconded or otherwise)
  - External, third party contractors
  - Currently employed with a party to the JV (therefore suggesting a consulting or similar relationship)
  - Other employment relationships

Map Needs to Organizational Structure

- What resources/positions are:
  - Critical
  - Secondary
  - Tertiary
  - Non-essential?
- When possible, consolidate functions
- Create timeline to implement structure
- Amend to reflect dynamic circumstances

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RIGHTS AND DUTIES OF MANAGEMENT

- Need to define rights and duties of management vis a vis what is reserved to the shareholders
- Right to contract with third parties/related parties
- Extent of agency
- Representation of partner(s)
  - dealing with authorities
- Records
  - books, records, and inventory
  - compliance with accounting procedure
  - compliance with legal requirements
  - preparation and filing of accounts and returns

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Operating Infrastructure – Records and Reporting

- Jurisdiction- and region-specific conformance
  - Policy documentation
  - Forms
  - Inter-company documentation
- Integrate with those of respective JV parties
  - Supplemental but not supplantive
- Establish JV party reporting process
  - Periodic
  - Consistent and shared commitment

- Avoid
  - Excessive JV party (or corresponding affiliate) dominance
  - Onerous reporting and unnecessary compliance requirements
- Require
  - Accountability
  - Consistency in ethics, compliance, and similar critical areas
- Seek, where appropriate
  - Economies of scale across jurisdictions with JV parties
  - Unified systems, methodology and practices

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Personnel

- Know the local (JV *situs*) hiring markets
  - Jurisdictional/regional nuances
  - Cultural and professional standards
  - Compensation ranges
- Engage appropriate search consultant to assist
- Complete job descriptions for all positions
  - Must map to organization structure
- Document appropriate requirements for terminating
  - Don't wait until faced with an impending termination

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Engage Key Third Parties

- External Service Providers
  - Business consultants (tax and similar)
  - Local auditors
  - LEGAL COUNSEL
  - Insurers
  - Search consultants (hiring/firing)
  - Payroll and other similar financial functions
  - Relocation Agents
- Establish written agreement for all relationships

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Key Contacts

- Identify and establish contacts with relevant offices/officials:
  - Business and personal taxing authorities
  - Regional and national regulatory offices
  - Commercial record-keeping officials
  - Relevant courts, embassies, consulates, etc.
  - National, provincial and communal visa and residency/work permit agencies
- Engage strategic local consultants (legal, tax, business, and the like) to facilitate developing these relationships

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RIGHTS OF PARTNERS

- Access and Inspection rights
  - business
  - accounts, books and records
  - who, when and how often
- Freedom to compete with the JV
- Right to exploit IPR or technology developed by JV
- Obligation to refer business
- Restrictions on contracting
  - Transfer pricing

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Lessons Learned

- Identify and designate accountable personnel
  - Preferably single manager within JV
  - Understand local rules on apparent authority!
- Eliminate as much redundancy as possible between JV parties (and corresponding affiliates) and JV
- Seek assistance from local "experts" early in process
  - Confirm periodically throughout process of establishing foreign/subsidiary operations
- Continue to maintain frequent and consistent dialogue between JV parties (affiliates) and JV
- Personal relationships are key