

# Joint Ventures 2020

Contributing editors  
**Gavin Williams and James Farrell**  
*Herbert Smith Freehills*





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**Contributing editors****Gavin Williams and James Farrell**

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Lexology Getting The Deal Through is delighted to publish the third edition of *Joint Ventures*, which is available in print and online at [www.lexology.com/gtdt](http://www.lexology.com/gtdt).

Lexology Getting The Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique Lexology Getting The Deal Through format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on China, the Netherlands, Saudi Arabia and Thailand.

Lexology Getting The Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at [www.lexology.com/gtdt](http://www.lexology.com/gtdt).

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Lexology Getting The Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editors, Gavin Williams and James Farrell of Herbert Smith Freehills, for their continued assistance with this volume.



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# United Kingdom

Gavin Williams, James Farrell and Nadine McMahon  
Herbert Smith Freehills

## FORM

### Types of joint venture

- 1 | What are the key types of joint venture in your jurisdiction?  
Is the 'joint venture' recognised as a distinct legal concept?

There is no particular form of association prescribed by English law for the pursuit of an activity in joint venture. As such, joint ventures in the UK can be implemented using the same structures as those available to any business, the most common being:

- a private company with liability limited by shares;
- a limited liability partnership (LLP);
- a general partnership;
- a limited partnership (LP); and
- an unincorporated contractual arrangement.

The key advantages of using a private limited company are limited liability, the company's ability to own assets and to contract in its own right and a clear structure for accounting, governance and reporting purposes. LLPs also offer limited liability along with the advantage of tax transparency, but they are not commonly used in commercial joint ventures.

Partnerships and LPs sit part way between corporate joint ventures and purely contractual joint ventures. A key advantage of using a partnership structure is that the individual partners are taxed directly on their profits. Private equity funds and consortia often use LP structures, as this form of joint venture allows financial investors to take a passive role, providing funding without participating in the management of the joint venture. This form is preferable where parties have mutual business interests and wish to collaborate but prefer to remain more loosely associated with the other participants.

Purely contractual joint ventures, such as oil and gas production-sharing agreements, cooperation agreements or development agreements, are common in certain sectors. In particular, contractual joint ventures are commonly seen in research and development projects and where each party contributes a specific element (eg, assets or expertise) to the joint venture but does not wish to relinquish control of its resources.

Joint ventures are not recognised under English law as a distinct legal concept.

### Common sectors

- 2 | In what sectors are joint ventures most commonly used in your jurisdiction?

Joint ventures are found in all sectors and industries in the UK; however, they have tended to be particularly prevalent in industries and sectors involving long-term projects requiring heavy capital expenditure. Participants seeking to limit their exposure and costs associated with

capital-intensive projects regularly use joint ventures to pool resources and access the margins available at scale. High-profile examples include nuclear power stations, telecommunications companies entering into network-sharing arrangements, offtake arrangements for North Sea oil and gas production, and large-scale infrastructure projects such as the building and operation of high-speed rail networks. Similarly, participants in research- and development-intensive industries, where significant investment is required over a long period of time before any returns can be realised, use joint ventures to spread the costs and risks of development across multiple parties (for example, pharmaceutical companies using joint ventures for co-development of new drugs).

Although typically not identified as joint ventures, joint venture structures are also commonly used by financial investors to make consortium bids where financial sponsors and passive investors pool equity funding and seek leveraged finance for an acquisition that may not otherwise be achievable. Such structures also provide opportunities for fund managers to make diversified investments that still meet their investment criteria (for example, in areas such as real estate and infrastructure).

## PARTIES

### Rules for foreign parties

- 3 | Are there rules that relate specifically to foreign joint venture parties?

Joint venture parties should have regard to certain existing statutory and regulatory restrictions when setting up a joint venture; however, these are not expressly focused on foreign ownership, but rather on protecting fundamental issues of public policy. Under statutory rules, the UK government is able to intervene in transactions to protect legitimate interests, including with respect to national security, media plurality and financial stability.

Certain industries are also subject to separate sectoral regulations, with the relevant regulatory bodies being empowered to assess the impact of transactions in the sector, examples being the financial services, media, transport and aviation sectors.

There is an increasing political appetite in the UK and the EU for governmental oversight and intervention. In June 2018, the UK government temporarily lowered the jurisdictional thresholds under the merger control regime for transactions in the military or dual-use technology, quantum technology and computing hardware sectors, pending the implementation of proposals to introduce a new national security regime that would give the government powers to intervene in any M&A transaction that may give rise to national security concerns. Further details about the form this proposed new regime is intended to take were set out in a subsequent White Paper consultation published in July 2018. The proposed legislative changes would create a distinct regime and standalone powers for the government to scrutinise transactions

on the grounds of national security interests. The government says that the reforms will bring the UK closer in line with other countries' foreign investment regimes. The proposed regime would apply to an acquisition of control or significant influence over assets, such as intellectual property (IP) rights, as well as businesses. There would be no turnover or share of supply tests that must be met in order for the regime to apply. Notification of transactions would be voluntary, but the government would have the right to intervene where parties choose not to notify, if national security risks were perceived to arise from the transaction in question. The proposals, as drafted, are very broad and could potentially catch a vast number of transactions. Investors may therefore wish to notify voluntarily before entering into a binding deal. The White Paper consultation period ended in October 2018, and the government's response to the feedback received and proposed draft legislation is due to be published shortly. While it remains to be seen exactly how the new regime will be enacted and implemented, it will potentially have a very significant impact for foreign joint venture parties (and indeed also domestic joint venture parties) where national security concerns are triggered.

In March 2019, the EU adopted a Regulation setting up a framework for the screening of foreign direct investment (FDI) in the EU that may affect security or public order, which will enter into force on 11 October 2020. The Regulation does not require EU member states to adopt or maintain a screening mechanism, but rather aims to ensure that any existing or proposed mechanisms comply with a set of minimum requirements, and establishes an EU cooperation mechanism for the European Commission and other EU member states to share their views on FDI. The European Commission considers that, because of the high degree of integration within the EU, FDI in one EU member state could pose risks to security or public order in another EU member state, or in the EU as a whole. Therefore, stepping up information sharing and cooperation in the EU is necessary to identify new challenges and to react accordingly. The new framework also allows the European Commission to issue opinions when an investment threatens the security or public order of more than one EU member state or when an investment could undermine a strategic project or programme of interest to the whole EU. The host EU member state must take 'utmost account' of such opinions, but remains the final decision-maker. The European Commission has also published and will keep up to date a list of screening laws in the EU.

Foreign investors should also be aware of draft UK legislation published in July 2018 to establish a register of overseas entities that own UK real estate. Once the legislation comes into force (intended to be 2021), a foreign party will be unable to transfer UK real estate into a joint venture unless it has complied with the registration requirements.

One advantage of establishing joint ventures in the UK is that the UK, unlike several jurisdictions, does not have any foreign exchange controls, meaning that foreign investors are generally free to bring in and take out capital from a UK joint venture as and when required, subject to applicable taxation.

#### Ultimate beneficial ownership

##### 4 | What requirements are there to disclose the ultimate beneficial ownership of a joint venture entity?

Private limited companies and LLPs incorporated in the UK are required to keep and maintain a public register providing details of persons or entities with significant control. Joint venture entities within the scope of this regime will be required to set out in their register those persons or legal entities who directly or indirectly have 'significant influence or control' over the company or LLP (ie, those who hold, directly or indirectly, more than 25 per cent of the shares or voting rights in the company or the right, directly or indirectly, to appoint or remove a majority of the board of directors of the company or who can otherwise

direct the activities of a company or can ensure the company adopts the activities they desire). This may also include joint venture parties who have negative control by virtue of absolute veto rights over key commercial or governance matters. Partnerships, LPs and contractual joint ventures are not subject to this disclosure requirement.

## SETTING UP AND OPERATING A JOINT VENTURE

### Structure

#### 5 | Are there any particular drivers in your jurisdiction that will determine how a joint venture is structured?

The most common factors driving the structure of a joint venture will be the parties' preferred tax treatment (eg, do the parties want the joint venture to be transparent for tax purposes such that profits and losses will pass directly to the joint venture parties (see question 19)?), competition law concerns (see question 13) and accounting (eg, do the parties want to consolidate the joint venture in their accounts?).

The other key drivers of a joint venture's structure will be:

- whether the parties wish to limit their liability exposure;
- the physical location of any assets to be held by the joint venture;
- the anticipated length of the joint venture;
- the preferred management structure;
- whether a listing is anticipated in the future;
- the degree of financial flexibility required by each party;
- the ease of transferring, terminating or unwinding the joint venture; and
- the level of publicity or public scrutiny (eg, a corporate joint venture may be subject to certain public filings that a partnership or contractual joint venture would not).

Another relevant consideration will be whether, owing to the nature of the investment or the nature of the business or asset to be operated, the joint venture parties may wish to access foreign investor protections, including those offered by bilateral investment treaties.

### Tax considerations

#### 6 | When establishing a joint venture, what tax considerations arise for the joint venture parties and the joint venture entity? How can tax charges be lawfully mitigated?

The tax implications of establishing a joint venture will depend on which joint venture structure is chosen. Joint venture parties will need to consider any tax triggered as a result of their respective contributions of any assets or businesses to the joint venture. This could be in the form of a tax on chargeable gains, balancing charges with respect to capital allowances, transfer taxes if shares are transferred or land taxes if interests in UK land are transferred. Value added tax may also be an issue when contributing assets to a joint venture unless the transfer qualifies as a transfer of a business as a going concern. If one or more of the joint venture parties is not UK tax resident, the joint venture parties will also need to consider any withholding tax obligations that may be applicable (eg, on payments of interest if the joint venture is to be funded by way of loan).

There are statutory relief measures available to mitigate chargeable gains on the transfer of assets, including merger relief where there is a transfer of a company to the joint venture, rollover relief on the transfer of certain business assets, the use of losses against chargeable gains arising and, in the case of transfers of shares or interests in shares, the application of the substantial shareholding exemption, if available.

## Asset contribution restriction

### 7 | Are there any restrictions on the contribution of assets to a joint venture entity?

There are no company- or contract-law restrictions on the contribution of assets to a joint venture entity; however, advice on the tax (and other) consequences of the contribution should always be sought (see question 6).

For example, there may be accounting factors to consider; in particular, if the contribution of assets results in one or more parties exercising control, the controlling party (or parties) may have to consolidate the joint venture in its accounts. See also question 3 for possible restrictions on a foreign party transferring UK property if it has failed to comply with proposed registration requirements.

If assets are contributed to a joint venture such that it qualifies as an enterprise for UK merger-control purposes, this may give rise to a 'relevant merger situation', which may be reviewable by the Competition and Markets Authority (CMA) (see question 13). The government's proposed powers to intervene in any M&A transaction that may give rise to national security risks should also be considered (see question 3).

Consideration should also be given to the allocation of liabilities when contributing assets to a joint venture, particularly in relation to environmentally sensitive assets (eg, oil refinery and gas storage facilities). The joint venture parties should clearly agree how liabilities will be shared under the 'polluter pays' principle if the joint venture is operating an asset that may cause environmental damage.

## Interaction between constitution and agreement

### 8 | What is the interaction between the constitution of the joint venture entity and the agreement between the joint venture parties?

As a joint venture is not itself recognised as a distinct form of legal entity in the UK, there is no mandated priority in law between the constitution of a joint venture and the contractual agreement between the joint venture parties. Parties should therefore apply first principles in ensuring that the contractual agreement and the constitutional documents are not in conflict with each other.

It is common practice for joint venture parties to stipulate that, as between themselves, in the event of a discrepancy between the contractual agreement and the constitutional documents, the contractual agreement should prevail. The constitutional documents and the contractual agreement should also conform in relation to the approach to and approval of conflicts of interest between the joint venture entity and the joint venture parties.

Where practicable, the joint venture entity itself should usually be a party to the joint venture agreement. This will make it easier to seek injunctive relief against the joint venture entity in situations where it is proposing to take an action that is clearly in breach of the joint venture agreement (eg, disclosure of confidential information).

## Party interaction

### 9 | How may the joint venture parties interact with the joint venture entity? Are there any restrictions?

The interaction between a joint venture entity and the joint venture parties will be governed by the terms of the agreements between the parties and, in respect of a joint venture that is a company or a partnership, the constitutional documents of the joint venture entity and applicable law.

In addition, and assuming the joint venture parties and the joint venture entity are separate legal entities, there may be ongoing

restrictions imposed by competition laws in respect of the flow of information either between the joint venture parties and the joint venture or between the joint venture parties that take place via the joint venture, if they are actual or potential competitors. A key area of risk is the sharing of competitively sensitive information that could influence the parties' competitive behaviour in the market, in particular the behaviour of the parties outside the joint venture. Examples of competitively sensitive information include information related to prices, marketing strategies, customer contracts, output levels, capacity and input prices. If any such information is exchanged that is not essential to the formation of the joint venture or that goes beyond what is essential for the parties to manage their investment, this may infringe competition law.

The directors of an incorporated joint venture are required to consider their statutory duties, in particular as regards conflicts of interest in relation to transactions between the joint venture and one or more of the joint venture parties, and the duty to act in good faith to promote the success of a joint venture company for the benefit of its members as a whole. (See question 12 for further information on directors' duties.) Such duties can be particularly significant in circumstances where there are related-party transactions or disputes between a joint venture and one of the joint venture parties.

In addition, if, in the case of an incorporated joint venture, the joint venture or a shareholder is a UK-listed company, the related-party transaction rules may apply in cases where the joint venture parties are transacting with one another. Depending on the size of the transaction, public disclosure or shareholder approval may be required, which could limit the parties' appetites to transact.

## Exercising control

### 10 | How may the joint venture parties exercise control over the joint venture entity's decision-making?

In an incorporated joint venture, a shareholder with an interest of more than 50 per cent will be able, effectively, to control the joint venture, including through the power to appoint and remove directors as it sees fit and to pass majority votes of shareholders. Therefore, in the absence of any agreement to the contrary, minority investors have relatively few rights by operation of law to exercise control over a joint venture entity's decision-making. As such, it is customary that minority investors seek additional, supplemental contractual rights, proportionate to the size of their investment in the joint venture, under the joint venture agreement, the constitutional documents or both. For example, it is common in UK corporate joint ventures for the parties to specify the right to appoint directors to the board based on shareholdings in the joint venture entity (eg, one director for every 10 per cent interest held) and to have the right to appoint a non-voting observer to the board.

Minority investors are best protected if the investors agree that certain fundamental actions cannot be taken without the consent of all investors (or at least a supermajority (eg, 90 per cent)). For example, shareholders of an incorporated joint venture can specify that no resolution to amend the constitutional documents of the joint venture company is passed unless all shareholders consent to the amendments.

In certain circumstances, minority shareholders can apply to the court on the basis of conduct that amounts to unfair prejudice by the majority shareholder.

## Governance issues

### 11 | What are the most common governance issues that arise in connection with joint ventures? How are these dealt with?

Resolving governance issues efficiently and to the satisfaction of all parties can be critical to the success of a joint venture. The three most common governance issues are:

- balancing management control of the joint venture company to ensure that the joint venture operates smoothly on a day-to-day basis but that key decisions that could affect the value and liabilities of the joint venture are reserved for the shareholders;
- how to deal with deadlock situations (see question 21); and
- how to manage conflicts between the interests of the joint venture entity and the interests of the joint venture parties (see question 12).

### Nominee directors

- 12** | **With an incorporated joint venture, what controls exist in your jurisdiction in relation to nominee directors? How should a nominee director balance the potentially conflicting interests of the joint venture company and the appointing shareholder?**

Directors of a joint venture company will be subject to statutory duties, including duties to avoid conflicts of interest, to promote the success of the company, and to exercise independent judgement.

There are ways to manage conflict issues at the outset of the joint venture. For example, any conflicted or potentially conflicted directors could be excluded from the relevant decision-making process. Alternatively, company law provides that conflicts can be authorised via the constitutional documents, shareholder resolution or by the directors. As such, the constitutional documents could contain authorisation of conflict situations that arise by virtue of a director being a director or employee of his or her appointing shareholder, and for the directors in their board meeting to acknowledge the existence of that authorisation.

In addition, significant decisions could be reserved for approval by the shareholders, taking the ultimate decision away from the nominee directors. Such an approach can avoid issues of directors' conflicts of interest, as the shareholders will be responsible for resolving the relevant issue and the shareholders are not subject to any duties to avoid conflicts of interest. This would not, however, absolve the directors of any breaches of their other duties. Nor is such an approach appropriate to deal with transactions and disputes involving one of the shareholders and the joint venture company (eg, if one of the shareholders is also a service provider to the joint venture company). The relevant shareholder in such a situation should not be able to prevent the joint venture company taking action against it, even if it is the majority shareholder.

### Competition law

- 13** | **What competition law considerations are engaged by the formation and operation of the joint venture? Is approval needed?**

For UK purposes, the formation of a new joint venture may qualify as a 'relevant merger situation' and thus fall within the scope of the UK merger regime if the activities transferred to the joint venture by one or more parents (or acquired from a third party) are sufficient to constitute an enterprise (ie, if the activities could be carried on for gain or reward) and if the turnover or share of supply or purchases threshold is met.

There is no obligation to notify the formation of a joint venture in the UK, but the CMA may investigate transactions that fall under its jurisdiction up to four months after completion (unless the transaction took place without having been made public and without the CMA being informed of it, in which case the four-month period starts from the earlier of the time that material facts about the transaction are made public or the time the CMA is made aware of such material facts). The CMA has a discretionary power to impose an order preventing any further implementation of the transaction pending completion of its investigation in relation to both anticipated and completed mergers, including joint ventures. In practice, it routinely makes such orders in completed

mergers as soon as a formal investigation is launched. In addition, the CMA has powers to require the reversal of any integration or implementation steps already taken at the time of launching its investigation.

Once the joint venture has been established, the competition law considerations outlined in question 9 will be relevant.

In relation to employee secondments into a joint venture, issues can also arise commercially in circumstances where an employee's secondment ends (either because the joint venture terminates or the secondments are on rotation). A secondee may have had access to competitively sensitive information about the other joint venture party during their secondment and, therefore, the parties may wish to think about the constructive use of a moratorium (ie, a quasi-garden leave period) to ensure that the secondee cannot use that competitively sensitive information with their employer and such information becomes stale before they return to normal duties with their employer.

### Provision of services

- 14** | **What are the key considerations in your jurisdiction in structuring the provision of services to the joint venture entity by joint venture parties?**

The issues that arise in relation to the provision of services to a joint venture entity are not necessarily specific to the UK. Commercially, joint venture parties will want to assess whether the provision of services will be at arm's length and whether they will need to negotiate the provision of any services with the other joint venture parties.

It is also important to consider the nature of the services being provided or whether the joint venture is carrying out regulated activities, as this may lead to additional regulatory scrutiny over the contractual arrangements and may also require specific mandatory terms to be included in any contract.

The joint venture parties should also agree to the allocation of any liabilities that may arise as a result of services provided to the joint venture. There are several high-profile examples of a joint venture party being adjudged liable for damage arising out of the operations of a joint venture as a consequence of inadequate contractual allocation of liability for the actions of employees of the other joint venture party who were providing services to the joint venture.

If there are any competition concerns facing the joint venture parties and entity (see question 9), these may be exacerbated if, for example, the joint venture parties provide back-office services to the joint venture. Parties may need to consider introducing information barriers or other structural safeguards to minimise the risk of problematic information sharing taking place.

A joint venture party may also find, depending on the level of control it holds in the joint venture, that the provision of services to the joint venture is considered intragroup, which may have tax (eg, transfer pricing) and accounting implications.

### Employment rights

- 15** | **What impact do statutory employment rights have in joint ventures?**

If existing businesses or assets are being contributed to the joint venture, UK law can operate to automatically transfer employees associated with the relevant business or assets. If such a transfer occurs, restrictions are imposed on the joint venture's ability to dismiss these transferring employees or make changes to their terms or working conditions. This can make it difficult for the joint venture to harmonise its terms of employment and can cause operational issues for the joint venture by creating a two-tier workforce, with employees doing the same job but on different terms. The parties will therefore need to agree how any liabilities under the relevant employment laws should be allocated.

## Intellectual property rights

**16** How are intellectual property rights generally dealt with on the creation, operation and termination of a joint venture in your jurisdiction?

There is no treatment of IP rights specific to a joint venture entity but the parties should agree at the outset how to address all IP issues arising from the creation, operation and termination of the joint venture.

The joint venture parties may retain ownership of their own IP rights, commonly referred to as background IP, and license these (including any IP created by them during the term of the joint venture) to the joint venture. If IP is to be assigned by a joint venture party to the joint venture, then the joint venture party may require a licence back (eg, if the joint venture party wishes to continue to use the background IP).

If the joint venture is to own the IP created by the joint venture, known as foreground IP, the joint venture parties will need to agree whether this IP will be licensed to them and, if so, on what terms. The joint venture parties may require that foreground IP is owned by either of the joint venture parties (especially if the IP created by the joint venture is derived from IP licensed to the joint venture), although these arrangements must comply with competition law.

Co-ownership of IP between the joint venture and the joint venture parties is possible but seldom advisable. Co-ownership may be cumbersome since, depending on the IP right concerned, a co-owner may not be free to use, license or dispose of the IP right without the consent of the other co-owners.

Parties should also agree at the outset how licences granted by or to the joint venture, and any IP assets held by the joint venture, should be treated upon the exit of any joint venture party or the joint venture ceasing to operate.

## FUNDING THE JOINT VENTURE

### Typical funding

**17** How are joint ventures generally funded in your jurisdiction? Are there any particular requirements relating to funding and security packages?

In an incorporated joint venture, the joint venture parties can choose to structure their investment in the most tax-efficient way by using a combination of shares, shareholder loans, third-party debt, preference shares and forms of quasi-equity, bonds and retention of earnings.

When deciding how to fund a joint venture, the joint venture parties will need to consider the possible dilution of participants' shareholdings (ie, unequal equity funding will be dilutive of the minority investor), the level of flexibility and the level of priority required on any return of profits and the preferred tax structuring (eg, interest paid on shareholder loans may be tax deductible (see question 19)).

The sector in which the joint venture operates and the identity of the joint venture parties can also influence the funding structure adopted by the joint venture. Sectors that require high initial start-up capital (for example, oil and gas ventures) will usually arrange long-term third-party debt financing at the start of the joint venture; joint venture projects with government involvement may receive an element of public funding without an expectation of return on the investment. Venture capitalists, however, will subscribe for equity but negotiate a mechanism to allow them to realise their investment in the short term.

There are no specific requirements for funding partnerships, LPs, or contractual joint ventures; parties will usually negotiate between themselves how costs will be incurred and shared.

## Capital injection restrictions

**18** Are there any legal or regulatory restrictions on the injection of capital into, or the distribution of profits or the extraction of cash by other means from, the joint venture entity?

If the joint venture is structured as a company, as a general rule, it may only distribute value to shareholders where it has sufficient profits available for distribution and not capital. These requirements are based on the principles of capital maintenance, namely that the share capital of a company belongs to the company and not its shareholders, such that the share capital will be available to creditors to satisfy a company's debts.

When recommending or declaring the payment of a dividend by a joint venture company, directors of the joint venture must also have regard to their common law and equitable duties, and their statutory duties owed to the company (rather than to their appointing shareholder). Joint venture parties often choose to fund joint ventures, at least partially, by way of loans to allow value to be extracted by way of interest payments to avoid the need to depend on distributable profits, which may not be available owing to technical restrictions, to pay a dividend.

## Tax considerations

**19** What tax considerations should be taken into account in the operation of the joint venture?

For corporate joint venture parties, profits distributed by dividend, while primarily taxable, are likely to fall within an exemption, such that tax will not be payable on the dividend. In the case of tax-transparent joint ventures (such as partnerships), the profits will accrue directly to the joint venture parties.

Where joint venture parties fund their joint ventures by providing loans to the joint venture, they will generally be subject to tax on the interest received under the loan relationship rules. The joint venture, however, should generally receive a tax deduction for the interest paid. There are, however, a number of rules that can restrict or defer interest deductions, including under circumstances where the parties to the loan relationship are connected or under the rules introduced under the Finance (No. 2) Act 2017, broadly restricting the tax deductibility of interest to 30 per cent of a group's taxable earnings before interest, taxes, depreciation and amortisation.

Where all the parties are UK tax-resident, withholding tax should not be an issue for the joint venture, but it will otherwise need to consider whether it is obliged to withhold UK tax from payments of interest.

The application of the transfer pricing legislation should also be considered where any transactions are undertaken between connected parties other than at arm's length. Joint venture companies and their joint venture parties may be entitled to surrender group relief between them via the consortium relief rules. A company is owned by a consortium if at least 75 per cent of its ordinary share capital is beneficially owned by several companies (none of which owns less than 5 per cent) and as such is only able to claim and surrender group relief if certain economic ownership tests and ordinary share capital tests are met.

## Accounting and reporting issues

**20** Are there any noteworthy accounting or reporting issues for the joint venture parties regarding their investment in the joint venture?

Contractual joint ventures, joint venture partnerships and LPs are not treated as distinct entities from the joint venture participants for accounting purposes, and so separate accounts would be prepared only by agreement of the parties for their own information or if required for tax purposes.

In certain circumstances, LPs are required to file accounts and any private limited company or LLP that participates in such a partnership will be required to append such accounts to their own when filed with the company's registrar. By contrast, a joint venture in the form of an LLP or private limited company is required to file accounts for each financial year, as well as produce them for tax purposes, and depending on their size, they may need to be audited.

Companies that participate in a joint venture will need to consider their own tax position and they will also be required to account for their share of the joint venture's profits, losses, assets and liabilities, so they will need to consider how their participation will impact their accounts. In particular, if a joint venture is considered a subsidiary, as it is controlled, this would require 100 per cent consolidation into the controlling party's group financial statements; alternatively, a deadlocked joint arrangement will likely lead to single-line equity accounting of the investor's proportion of the investment.

## DEADLOCK, EXIT AND TERMINATION

### Deadlock provisions

#### 21 | What deadlock provisions are commonly included in joint venture agreements in your jurisdiction?

The options most commonly used to resolve deadlock in joint ventures range from relationship-based solutions, such as swing votes or escalation of the deadlocked matter to senior representatives of the joint venture parties, to third-party solutions, such as independent directors, mediation or expert determination (where appropriate), to enforced sale type provisions, such as put and call options, Russian roulette or shoot-out provisions and winding up.

In the case of Russian roulette and shoot-out, the mechanisms are only workable where there are a small number of parties (preferably two). In practice, while the mechanisms are often included in joint venture agreements, they are rarely used.

In determining the appropriate deadlock-resolution mechanism, joint venture parties will need to balance the need for a proportionate response with a suitable deterrent effect so that not every decision is subject to the deadlock-resolution mechanism. For example, if decisions are regularly referred to senior representatives or third parties, the decision-making process of the joint venture could become unworkable.

Deadlock mechanisms tend to be most often used to create leverage at the point of exit of one of the joint venture parties. It is therefore common for a significant amount of time to be spent negotiating deadlock provisions prior to establishing a joint venture.

### Exit provisions

#### 22 | What exit provisions are commonly included? Does the law restrict any forms of mandatory transfer provision or any basis of calculation?

Pre-emption rights are commonly included in joint venture agreements, drafted either as a right of first refusal or right of first offer. In our experience, the right of first refusal is most commonly used. Each provides a mechanism for matching another offer, whether that offer be from a third party or the other investor. In each case, the intention is to allow a party to exit the joint venture while ensuring that appropriate protections are in place for the joint venture entity itself.

If the joint venture involves a minority shareholder, drag-along and tag-along rights are often included. Drag-along provisions ensure that a sale of the whole joint venture can be achieved. Tag-along provisions allow minority shareholders to participate in an exit event if the majority shareholder is selling to a third party. Joint venture parties should also include a security power of attorney in the joint venture agreement

granting the board of directors of the joint venture power to effect a transfer on behalf of the party, subject to the drag or tag.

For default transfers, it is important that the parties take appropriate advice when drafting the relevant provisions, as a provision that reduces the price paid for a defaulting party's shares, discounts loan repayments on default, or reduces the level of bonus or incentive payments on default, could be found under English law to be unenforceable under the doctrine of deprivation or as an unlawful penalty clause.

The drafting of mandatory exit provisions, such as the right of first refusal, right of first offer, and drag- and tag-along rights are commonly inadequate. This often leads to uncertainty and dispute as to the operation of the relevant provision.

## Tax considerations following termination

#### 23 | What are the tax considerations on termination of the joint venture?

Tax considerations will depend on the form of the joint venture and the particular transactions that occur in order to terminate the venture. Any transfer of shares or interests in a joint venture by a joint venture party to another joint venture party or a third party will be a disposal potentially subject to tax on chargeable gains. If the joint venture company transfers its assets to the joint venture parties, this may trigger a tax liability for the company on the disposal of the assets. The joint venture party that receives these assets may be treated as receiving a distribution or as making a disposal of its interest in the joint venture, depending on the facts. If a joint venture company is liquidated, the joint venture company would be treated as making a disposal of its assets for chargeable gains purposes and the joint venture parties would be treated as disposing of their shares for chargeable gains purposes. For the joint venture parties, this potential tax charge may be mitigated by the substantial shareholding exemption, if available.

## DISPUTES

### Choice of law and resolution methods

#### 24 | In your jurisdiction, are there constraints on the choice of law or the method of dispute resolution provided for in joint venture agreements?

A joint venture business operating in the UK is not constrained as to the governing law provided for in its joint venture agreement. Similarly, there are no constraints on the method of dispute resolution chosen by a party. The parties should ensure they choose dispute resolution mechanisms appropriate to the various types of dispute that may arise. For example, a deadlock dispute may be better resolved by expert determination (if such a mechanism is recognised under its chosen governing law) than by litigation.

If the jurisdiction clause in the joint venture agreement refers disputes to the English courts, those courts will accept jurisdiction under the Recast Brussels Regulation (subject to limited exceptions set out in that Regulation), if proceedings are commenced while the UK remains a member of the EU, or otherwise under the 2005 Hague Convention on Choice of Court Agreements or common law rules. The English courts will generally give effect to the parties' choice of law, consistent with the Rome I Regulation (again subject to limited exceptions) or equivalent rules that are to be incorporated into English law if the UK leaves the EU.

## Mandatorily applicable local law

### 25 | What mandatory provisions of local law will apply irrespective of the choice of governing law?

A joint venture business operating in the UK will be subject to a wide range of UK laws that govern the operation of the actual business, including laws relating to employment, competition, tax and health and safety.

However, in relation to the joint venture agreement itself, which governs the relationship between the joint venture parties, if the agreement is not governed by UK law, then generally there may be only limited instances where mandatory UK laws (or considerations of UK public policy) may override the chosen law. If the English courts have jurisdiction over disputes relating to the joint venture agreement, they will apply any relevant mandatory provisions of English law. These may include provisions of legislation, such as the Unfair Contract Terms Act 1977 and the Consumer Rights Act 2015, but there may not be much scope for such legislation to operate where the relevant contract is a negotiated joint venture agreement between sophisticated parties. If the performance of the joint venture agreement in the UK is, however, illegal, UK law or public policy may prevent its enforcement (whether by the English court or the courts of some other jurisdiction). In addition, if all relevant elements of the joint venture are located in the UK (which is unlikely to be the case where the joint venture parties are from different jurisdictions), then the choice of some other law will not prevent the application of provisions of English law that cannot be derogated from by agreement (eg, the rules relating to penalties).

If the joint venture parties choose in the joint venture agreement to refer disputes to the English courts, the English courts will apply their own rules of procedure in resolving any dispute, but will apply the chosen governing law in deciding the underlying legal issues.

## Remedy restrictions

### 26 | Are there any restrictions on the remedies a tribunal can grant that would have a bearing on the arbitration of joint venture disputes? Are there any restrictions on the arbitration of shareholder claims?

A tribunal will, in general, be unable to grant remedies that have an effect beyond the parties engaged in the dispute or that, by statute, are remedies that can only be given by the court. This might include, for example, an order for the winding up of a company and an order regulating the conduct of the company's affairs under the Companies Act 2006.

However, the inability of an arbitral tribunal to grant certain types of relief does not necessarily affect the arbitrability of the subject matter of the dispute. There is only likely to be a restriction on the arbitration of shareholder claims where the claim is brought under statute and the provision has a wider public policy purpose aimed at safeguarding the interests of third parties (eg, creditors). Where a claim simply relates to the relationship between the shareholders, or the shareholders and the company, these claims will most likely be arbitrable, whether brought under contract (eg, shareholders' agreement or the constitutional documents) or under statute. For example, the Court of Appeal has confirmed that an unfair prejudice claim under the Companies Act 2006 is arbitrable.

## Minority investor protection

### 27 | Are there any statutory protections for minority investors that would apply to joint ventures?

The statutory protections under English law set out below are principally limited to English incorporated joint venture companies. While these protections are available to all investors, in practice they are more applicable for minorities.

Where the affairs of the company are conducted in a manner that is unfairly prejudicial to a minority investor, that investor may have relief under section 994 of the Companies Act 2006. The court has a wide discretion to grant relief, with the usual remedy being a buyout order. In addition to companies, an investor in an LLP may seek relief under this section.

The Companies Act also entitles a minority investor (with the court's permission) to bring a derivative action on behalf of the company against a director who has acted improperly (by, for example, breaching his or her duty or acting negligently).

A minority shareholder may also apply to the court to wind up a company where it is 'just and equitable' to do so, pursuant to the Insolvency Act 1986, even where the company is solvent (although, in practice, such an action would be rare and it is likely that a claim for unfair prejudice will be preferable).

## Liabilities

### 28 | How can joint venture parties have liabilities to each other beyond what is expressly agreed in the joint venture agreement?

A party can be liable beyond the terms expressly agreed in a joint venture agreement subject to English law.

An untrue statement of fact that induces the other party to enter the joint venture, who then suffers loss, may give rise to a misrepresentation claim (and, in some circumstances, even if the terms of the joint venture agreement purport to exclude such claims).

Terms may also be implied into a joint venture agreement, although an English court will take a restrictive approach when doing so. The proposed term must not contradict the express terms and must be necessary to give business efficacy to the contract or be so obvious that it goes without saying. It may be possible to imply a duty to act in good faith in long-term relational agreements, such as a joint venture agreement, by satisfying the same test.

The joint venture agreement may give rise to fiduciary duties or a partnership, although this will depend on both the facts and the contract terms, and wider duties will not be lightly implied.

In addition, if a joint venture agreement confers a benefit on a third party, under the Contracts (Rights of Third Parties) Act 1999, that third party may enforce the agreement against the investors to secure performance of that benefit (although it is possible for the joint venture parties to exclude the Act in the joint venture agreement).

Using a corporate structure will not necessarily shield an investor from operational liabilities where that investor alone plays a major role in operating the relevant part of the joint venture. In case law, a joint venture investor was deemed to operate one site subject to the joint venture because all staff were engaged and paid for by it, and decisions were made by the investor without regard to the joint venture company. As such, the investor was fully exposed to the liability for third-party claims for the negligent acts committed at that site. Investors should take care when drafting indemnity provisions in the joint venture agreement to ensure that it demonstrates the intention of the parties, in particular where a party is seeking to be indemnified for negligence (as in this case the indemnity was determined not to capture such liability).

## Disclosure of evidence

### 29 | Are there any particular issues that can arise in joint venture disputes in your jurisdiction concerning disclosure of evidence?

In English litigation, the test for control over documents for discovery is whether a party possesses or has a right to possess or inspect a document. However, there are suggestions in the case law that these

categories are not necessarily exhaustive, and the courts may take a broader approach in determining whether a party does in fact have control over a document.

In the absence of an agreement, a shareholder would not typically have rights to possess or inspect documents generated by a corporate joint venture, and the documents would usually fall outside of its control. However, the courts will consider company practice when determining whether a party does in fact have control over a document.

A corporate joint venture cannot assert privilege against its parents other than in relation to a dispute between it and a shareholder. If the advice relates to the conduct of the joint venture's affairs, care should be exercised to ensure that privileged material is addressed to the joint venture, or to the appropriate parent, if the advice relates to its shareholding, to avoid unintended disclosure or waiver of privilege. Nominee directors of the joint venture company should take particular care in this regard when seeking advice.

## MARKET OVERVIEW

### Jurisdictional advantages

30 | What advantages does your jurisdiction offer for parties wishing to set up and operate joint ventures?

The UK is an international financial and legal hub, with a developed body of law and commercial practice and a strong regulatory framework. There is ease of access to capital markets, strong communication and trade links with other jurisdictions and a skilled workforce.

The UK also has a highly attractive low-tax regime designed to encourage investment; this benefits foreign joint venture parties by making it easier to repatriate profits from a joint venture without punitive tax rates being applied.

English law as a governing law is also well understood and embraced by many international jurisdictions, particularly given the emphasis on legal certainty and parties' freedom to contract and ease of enforceability within the English courts. The UK is also a centre for commercial arbitration, allowing parties an alternative and private avenue to resolve disputes. A combination of factors such as these makes the UK a stable environment to set up and operate new business ventures.

### Requirements and restrictions

31 | Are there any particular requirements or restrictions relating to joint ventures in your jurisdiction that could deter international investors?

Directors of an English company who are nominated by joint venture parties must act in accordance with their duties owed to the company rather than as directed by their nominating shareholders. This could at times restrict the ability of joint venture parties to cause actions to be taken by the joint venture if such decisions are deemed by the directors not to be in the best interests of the company.

## UPDATE AND TRENDS

### Key developments of the past year

32 | What are the current trends affecting joint ventures in your jurisdiction? What recent developments in legislation and case law have had an impact on joint ventures?

Large private companies have become subject to greater disclosure requirements, including a requirement for private companies of a significant size to disclose their corporate governance arrangements in the annual report and on their website. Although many of



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these developments are reflective of moves in other jurisdictions and statements of organisations such as the Organisation for Economic Cooperation and Development and the G7 and G8 summits, some foreign investors may find that the level of transparency required of private companies is greater than they are used to.

The UK's anticipated departure from the EU raises some issues that could have an impact on joint ventures, particularly if the UK leaves the EU without a withdrawal agreement. For example, questions have been raised as to whether EU courts will, post-Brexit, continue to enforce judgments given by the English courts. There should be no difficulty in this respect where the English court had jurisdiction pursuant to an exclusive English jurisdiction clause agreed after the UK's exit from the EU. Otherwise, the position is not straightforward, but English judgments are likely to remain enforceable in most EU member states in most circumstances.

Joint venture parties may also question whether they should continue to choose English law to govern their joint venture agreement. Many commercial parties choose English law as it is viewed as certain, stable and predictable, and generally gives effect to the parties' commercial intention, thereby giving limited scope for unexpected implied terms or influence by public policy changes. This reasoning is unaffected by Brexit.



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