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JOINT VENTURE AGREEMENTS:
MAJOR ISSUES AND COMMON PROVISIONS

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This memorandum provides a checklist of important aspects of arrangements for joint ventures and strategic alliances involving the U.S. or at least one U.S. party for manufacturing, resource extraction, transportation, marketing and research activities. These aspects include major legal and business issues to be considered in structuring such a relationship (Part I), as well as a variety of provisions commonly found in the detailed agreements documenting the transaction (Part II). The checklist is not exhaustive, and many ventures will not address all or most of the listed items. The author nonetheless hopes that this overview of significant questions and clauses will be useful to parties considering joint venture opportunities.

	I. MAJOR ISSUES	√
A.	***Strategic Issues***	
1.	*Assess Own Goals and Resources*. Before entering into a joint venture, each party should seek to define its objectives and assess its resources. Typical business objectives for entering into a joint venture include (i) gaining immediate access to a market; (ii) reducing the commitment of funds; (iii) shortening the learning curve of adapting to the local industry and the manpower necessary to enter that market; (iv) minimizing the risks associated with market entry; and (v) acquiring new capital and technology. The interest may be in a particular identified joint venture, or in a broader strategic alliance including present and future investment opportunities.	
2.	*Compare Parties' Goals and Resources*. Each party should seek to understand the objectives and resources of the other potential investors. Mismatched objectives can make a joint venture less favorable than alternative forms of combinations and relationships such as acquisitions, divestitures, or supply, distribution or licensing transactions. Insufficient human resources to monitor and manage the	

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This memorandum is for background information only. The contents should not be construed as legal or business advice. Legal counsel should be obtained for specific transactions.

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	joint venture can give rise to control disputes, for example. One side's lack of financial resources can create tension over future expansion and new opportunities, and will generate pressure for early payouts. An otherwise self-sufficient prospective partner, eyeing an alliance solely for purposes of gaining a foothold in a new market, may lose interest in the venture as soon as it is formed.	
3.	*Compare Joint Venture with Alternatives.* A joint venture is most likely to succeed where: • the parties' respective objectives are complementary; • the parties' respective resources are both adequate to the task and not disproportionate; • each party is willing and able to commit sufficient resources to the joint venture; and • the parties' timetables for achieving goals are consistent. In circumstances where these factors are not present, the parties should consider other forms of integration. The alternatives include outright acquisition on the one hand, and agency, distribution, supply, toll processing, licensing or trade association arrangements on the other hand.	
B.	***Tax Issues.***	
1.	*Address Structural Tax Issues.* The structure of the joint venture has significant implications under U.S. and local tax law, and tax issues usually are the most important factors in deciding which structure to use. Tax advisors typically consider: • whether the joint venture should be a bare contractual agreement or a separate legal entity; • whether the joint venture entity should be a limited liability company (LLC), a general or limited partnership or a corporation, or a foreign-law equivalent; • under which jurisdiction the entity should be organized;	

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	• what should the tax domicile of the entity be (taking into account any tax "holiday" or incentives); • how to minimize the tax costs of formation and financing; • whether each party's participant in the joint venture should be a branch of a domestic subsidiary or a foreign subsidiary; and • whether such participant should have a permanent establishment in the joint venture's jurisdiction;	
2.	*Address Operational Tax Issues.* The U.S. investor generally desires first to maximize its ability to use foreign tax credits to reduce its U.S. income tax, and second to minimize the foreign taxes paid by the joint venture itself. Tax advisors typically consider: • the location in which title should pass to property that the participants transfer to the venture; • whether the participants should transfer rather than license technology to the venture; • where and how the participants should provide technical services to the venture; • the extent to which the participants' financial contributions to the venture should take the form of debt or equity, or guaranties of loans made to the venture by third parties; and • how and when distributions by the joint venture should be made.	
C.	***Antitrust and Competition Law Issues.***	
1.	*Assess Legality of Core Arrangements.* Each party should consider the consequences for the proposed joint venture posed by U.S. and local antitrust and competition law. Even a joint venture structured and operated wholly outside the U.S. may violate U.S. antitrust law through the activity of the joint venture itself, or through ancillary agreements between the participants. Antitrust concerns should inhibit information sharing in a joint venture among competitors, when the information relates to costs and sales information or plans in areas in which they will continue to compete. The current position of the U.S. enforcement agencies with respect to joint ventures involves two separate inquiries. First, the agencies	

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	consider whether the collaborative activity is of the type that is so likely to be harmful to competition that it does not warrant particularized rule of reason analysis. Such agreement will be condemned as per se illegal. Assuming the joint venture agreement is not per se illegal, the agencies will consider whether the agreement will likely harm competition by increasing the ability or incentive of participants to raise prices above or reduce output, quality, service or innovation below competitive levels. The U.S. Supreme Court has stated that the legality of a joint venture under antitrust laws depends on a number of factors, including: • market power of the participants; • the joint venture's market and its relationship to the markets of its parents; • the potential power of the joint venture in the relevant market; and • an appraisal of what the competition in the relevant market would have been if one or all of the participants had entered it alone instead of through the joint venture.	
2.	*Assess Legality of Collateral Restraints.* Often the joint venture itself is found to be legal, but ancillary agreements among the participants are found problematic if they limit competition between the participants more broadly than necessary to make the joint venture work. The participants should be especially wary of "gun-jumping" activities undertaken before the joint venture has become effective and has obtained all necessary regulatory approvals.	
3.	*Assess Local Competition Law. The Antitrust Enforcement Guidelines for International Operations* (1995) and *The Competitor Collaborations Guidelines* (2000) by the U.S. Department of Justice and Federal Trade Commission, are useful guides to the application of U.S. antitrust laws to international cooperative activity. The *Competitor Collaborations Guidelines* sets forth presumptive safe harbors or "safety zones" for bona fide collaborations where the market shares of the collaboration and its participants collectively account for no more than 20 percent of each relevant market. The *Guidelines* provide a safety zone for R&D joint ventures when three or more independently controlled research efforts, in addition to those of the collaboration, possess the required specialized assets or characteristics and the incentive to engage in an R&D effort that is a close substitute for the R&D activity of the venture. The European Union and many countries similarly prohibit restrictive business practices. For example, Japan's Antimonopoly Act (Act Concerning Prohibition of Private Monopoly and Maintenance of Fair Trade, Act No. 54, April 14, 1947, as amended in 2005) declares that "[n]o	

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	entrepreneur shall effect private monopolization or any unreasonable restraint of trade," and prohibits "unfair business practices." Such local laws can be used to scrutinize the anti-competitive effects of joint ventures even when they are not attacked under the laws of the participants' home countries.	
4.	*Assess Notification or Approval Requirements.* The competition and foreign investment laws of many countries feature pre-combination notification or approval requirements for consummation of transactions including some types of joint ventures. Such laws include the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, in the United States. Even a modest amount of activity in a given country, including a preliminary agreement, may trigger the application of such requirements	
D.	***Local Law Issues.***	
	The joint venture will of course be subject to extensive regulation by local authorities, including foreign investment laws and statutes governing joint ventures in particular, as well as through corporate law, commercial codes and rules concerning agency and distribution arrangements. Local law issues may include: • exclusion of certain sectors of the economy from foreign investment; • requirements as to the relative proportions of equity interest that local and foreign participants may hold; • governmental and central bank approvals for investments and particular transactions; • industry-specific regulation; • restrictions on offshore bank accounts, transactions in foreign currency or repatriation of profits; • currency exchange and export controls, commodity import and export controls, price controls, and anti-dumping restrictions; • worker participation or other labor requirements; • real property ownership or use restrictions;	

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	• environmental regulations; • technology regulations; • intellectual property restrictions; • restrictions on use of foreign governing law; • restrictions on foreign arbitration or other forms of dispute resolution; and • restrictions on assignment, termination and removal rights.	
E.	***Local Incentives.***	
	Local legal and commercial programs may also provide incentives for foreign investors, such as exemptions from certain duties and taxes. The local government may have a an investment board to assist with obtaining local licenses and permits.	
F.	***Limited Pre-Venture Undertakings.***	
	Prior to consummating the joint venture, the participants should consider whether pre-formation activities should be engaged in, and whether such activities should be governed by a limited agreement. Possibilities include: • preparation by one or both parties, or a consultant, of a feasibility study justifying the joint venture and its scope; • development of a pilot plant or other preliminary work product, with limited commitments and relatively easy exit provisions; and • a letter of intent or memorandum of understanding. Such instruments can help to maintain confidentiality at each stage and preserve the participants' expectations on key subjects before concluding a joint venture agreement. The parties to such a document should consider:	

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	• whether the letter of intent will be binding in whole or in part; • whether to impose a covenant to negotiate in good faith; and • whether the agreement will contain an exclusivity or no-shop provision.	

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A.	***Participants & Guarantors*.** Each party must determine through what entity it will participate in the joint venture. Some examples include a branch of an existing offshore company or a special purpose company. The participants must also consider whether the entities should also be included as guarantors to ensure performance, or to enforce non-competition covenants, corporate opportunities and similar covenants. It is important to consider whether the joint venture entity should itself be a party to the principle agreement. If the joint venture is a party, it may be able to directly enforce obligations of co-venturers in a bankruptcy situation where there is a receiver or trust. If the joint venturer is not a party, it will be difficult to get specific enforcement of obligations.	
B.	***Scope*.** It is crucial to delineate at the outset the purpose of the joint venture, both as to present activity and future opportunities. If the participants define the scope of the joint venture with precision, they can avoid costly disputes over what activities are or are not within that scope. The participants should decide, for example, • whether the joint venture will have the right of first refusal as to any future opportunities identified or acquired by the joint venture or any participant; • whether the participants can individually take advantage of new technology or products developed by the joint venture; • whether the joint venture or its participants will be empowered to veto activity of its participants that is competitive with the joint venture; and	

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	• how the joint venture will handle new opportunities. For example, a participant may be permitted to require the joint venture to embark on a new extraction project on a sole-risk basis, or to not consent to investing in a project pursued by the others. In either the sole-risk case or the non-consent case, the agreement may provide that the dissenters will gain the benefit of the new project only after the initial venturers have received a defined multiple of their incremental investment.	
C.	***Duration*.** The agreement should state whether the joint venture will continue for a fixed term with options for extension, or will continue on an "evergreen" basis. The participants should also agree on the conditions and procedures for terminating the joint venture and the procedures to be used for valuing the participant interests upon termination. The joint venture agreement could provide for termination of the joint venture upon • expiration of the agreement, • the agreement of the participants, • an uncured default by a participant (if there are only two participants), • an unresolvable deadlock, and • a significant and detrimental change in relevant local law. The stipulated valuation procedures could vary with the circumstances of termination. For example, the joint venture agreement could mandate the use of the lower of book value or fair market value for elimination of a defaulting participant's interest and liquidation value in other circumstances. There are many possible variations. Where there are only two participants, for example, a "shotgun" clause could provide that one participant may announce a price per share in the joint venture, and the other may then elect either to buy that participant's interest, or sell its own, at the announced price.	
D.	***Legal Form of Venture*.** A joint venture may take the form of a limited liability entity (an LLC, a corporation or limited partnership) or a general partnership under local law. But before evaluating various entities, consideration should be given to a simpler structure: a	

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	bare contractual agreement to share costs and benefits (in which case no new entity is created). The structure of the joint venture will be influenced by a variety of commercial, legal, tax, control, regulatory and accounting considerations. Local corporate law often provides greater protections for investors in entities than are afforded non-corporate investors, such as • protections for minority shareholders; • supermajority requirements for shareholder votes on certain actions, and • fiduciary obligations of directors and officers that may be difficult to disclaim.	
E.	***Initial Contributions.*** The participants should determine the kinds of initial contributions the participants are to make to the joint venture, their timing and their amounts. Contributions can take the form of loans to the joint venture, or equity issued by the joint venture. If the initial contribution is in return for stock, the participants should determine the type of dividend, anti-dilution, preemptive, liquidation, conversion, voting and registration rights. The transfers can take the form of cash, contracts, other tangible property or intangible property rights (although the value of services may not qualify as contributions in all cases). The participants should investigate the legal and tax aspects of these contributions.	
F.	***Allocation of Liabilities.*** The participants should decide if any liabilities will be assumed relating to past operations of the participants or assets contributed to the joint venture. Indemnities among the participants, and with the joint venture itself, can allocate responsibility for claims arising from ongoing operations of the participants and of the joint venture. The participants should take into account the impact of liability and property insurance policies carried by the participants, or by third party contractors.	
G.	***Future Contributions.*** The participants should consider whether the joint venture can require the participants' parents to fund the joint venture at some future time. If future costs can be mandated, the agreement can specify in what manner (e.g., by direct loans, contributions to capital, or guarantees of loans from third parties) and in what amounts. The agreement should delineate what will determine when the financing milestone(s) have been met (e.g., pre-determined metrics, notice by investment entity, mutual agreement).	

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H.	***Dividends and Distributions*.** The participants should consider the basis for allocating costs and distributing profits. If the joint venture is a partnership, the participants must establish a contribution system of capital accounts that is effective under partnership and tax law, and should agree as to the methods for recording accruals and deductions. The local jurisdiction may impose withholding taxes on repatriated dividends or distributions, or on payments of interest on loans made by participants. Special care should be taken to negotiate the currency in which and destinations into which the payments are made.	
I.	***Record and Audit Requirements*.** The participants should consider whether the venture should prepare financial statements in a particular format, whether such statements should be audited, and the identity or process for selecting the auditor. The agreement should include a clause requiring the joint venture to maintain usable and clear accounting records. Entities that enter into auxiliary agreements with the joint venture, such as a parent that furnishes supplies or services to the venture, should likewise be required to maintain clear accounting records. The joint venture participants, and their authorized representatives, should have access to those accounting records.	
J.	***Management of Venture*.** The participants should consider defining and allocating functions and responsibilities of the joint venture's management. It may be useful to provide compensation incentives to existing management. Management issues include: • whether one participant or a third party will act as an operator of the venture; • which individuals will be making the day-to-day decisions; • which individuals have the authority to bind the venture: • the respective rights of the participants to appoint the board of directors and officers of the joint venture; • the scope of these individuals' duties; • selection and replacement of other key joint venture personnel; • the veto (or supermajority voting) rights the minority owner and/or non-management persons have (if any);	

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	• whether local laws require independent board members; • whether employees of the joint venture should be loaned or "seconded" from the participants or directly employed by the joint venture, and the impact of this arrangement on tax, immigration, workers' compensation and employee benefit laws and benefit plans; and • the dissemination of information to the participants.	
K.	***Participant Control of Fundamental Decisions.*** The participants should also consider what kinds of decisions will require a vote by the board or the participants, and the quorum, passmark and procedures for such decisions. The participants should also consider how to decide on deadlock matters (e.g. decided by one of the venturers or referred to the shareholders for a vote). Participants typically consider retaining control with respect to such major issues as: • liquidation or dissolution of the joint venture; • sale or disposition of the assets; • merger or acquisition of new business; • expansion of the scope of the joint venture; • issuance of new stock; • change in the composition of the board of directors; • increase in required contributions; • approval of the annual budget; • major financing arrangements; and • other major operational decisions (such as contracts outside of the ordinary course; long-term business plans; dismissal of	

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	officers; and contracts with participants for supplies or services).	
L.	***Controls, Deadlocks and Disputes.*** Positive controls can be used to require affirmative consent on issues. The parties should consider allowing the party with the most stake in a certain area to have a predominant right of approval. Negative controls (e.g., vetoes and supermajority requirements) can allow a minority shareholder to have a greater voting interest than the number of shares entitled to under their equity interest to safeguard their interests. The participants should agree on the procedures to be followed in the event of a deadlock by the board or other dispute. For example, the participants may agree first to refer the matter to the participants' respective CEOs and then to other forms of alternative dispute resolution. The joint venture agreement should also state the governing law and the jurisdiction in which disputes are to be litigated.	
M.	***Corporate Opportunity.*** A co-adventurer may be required to offer to the joint venture business opportunities within the scope of the joint venture's business. The parties should consider whether, if a co-venturer turns a business opportunity down, the other co-venturer may take up the opportunity on the same (or no more favorable) terms than those offered to the co-venturer. As joint ventures mature, one party may seek its own greater integration with business outside the venture itself, creating conflicts with venture parties. The potential conflicts should be addressed in the agreement.	
N.	***Transfers, Admissions, Withdrawals and Removals.*** The participants should consider the terms and conditions governing transfers of interests and whether transfers trigger buy-sell rights, the admission of new participants into the joint venture and the voluntary withdrawal and involuntary removal of participants. As to exit, the joint venture agreement may restrict the assignability of participant interests by requiring the prior consent of the other participants to any transfer, or by granting rights of first refusal to the joint venture or other participants, or their nominees, to acquire the interest. (However, such provisions may be prohibited or restricted under local law, particularly if ownership by foreign entities would be increased.) As to entry, the joint venture agreement may require the prior, unanimous approval of all or a supermajority of participants before new participants may be admitted. The joint venture agreement may require prior approval of all or a certain number of remaining participants for the voluntary	

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	withdrawal or involuntary removal of a participant. The joint venture agreement should set out the circumstances justifying such actions (e.g., removal based on default, insolvency of the participant or acquisition of the participant by a defined class of third party). The impact of mergers, other forms of corporate reorganization, stock sales and other changes in control should be addressed in negotiating clauses governing withdrawal, removal, assignment and related subjects. Buy/sell agreements can develop goodwill but the participants should consider the use of a corporate trustee for greater neutrality and effectiveness. The buy/sell agreement should specify the events that will trigger default. A drag-along provision forces the remains joint venture parties to sell their interests with the selling venturer. A tag-along provision permits a joint venture party to sell its interest on the same terms as the selling venturer. If one partner asks for tag-along rights, the other may insist on also including drag-along rights that would force the first partner to sell its interest. Buyouts are usually triggered by default, deadlock or business events. The parties can use a so-called "shotgun" provision in which one party states a price per unit of equity, at which it will either buy the other's interest or sell its own interest. The parties may forbid withdrawing parties to compete in the remaining business (noncompetition covenants may be unenforceable).	
O.	***Default.*** If future finance commitments are central to the joint venture, appropriate default procedures should be considered for failure to meeting funding commitments. These can include (usually in stages): • payment of default interest; • loss of voting rights and/or rights to appoint directors of the joint venture company; and • reduction (and, possibly, compulsory sale to other joint venture parties) of the defaulter's shareholding in the joint venture company –although it may be necessary to check that the terms of such provisions do not fall afoul of laws against penalties in the relevant jurisdiction. It will be necessary to decide whether non-defaulting parties should be bound to fill the capital commitment of the defaulter in the meantime. The participants should also consider the point at which failure to provide financing triggers exit rights, liquidation rights, puts, calls or rights to bring in third party investors.	

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P.	***Termination and Resolution of Disputes.*** While participants may be reluctant to discuss termination provisions in the joint venture agreement, joint ventures are exposed to many risks that could lead to dissolution. The participants should not rely on boilerplate dispute clauses, but should plan for potential disputes based on the unique characteristics of the venture. The participants should consider: • what events will terminate the joint venture (e.g., passage of time, breach, failure to reach certain goals, accomplishment of venture's defined purposes); • whether the agreement should include force majeure provisions; • what law should govern the agreement; • what language should govern the agreement and any dispute resolution proceeding; and • whether the parties can opt out of local courts through either local or international arbitration. If the agreement contains an arbitration provision, the participants should consider, among other issues: • what are the relevant countries' laws with respect to local or international arbitration; • whether appeals are to be permitted, and how any award can be confirmed and executed against; and • whether there is a local organization or local rules governing any arbitration that is conducted in a country or that seeks to resolve disputes arising in that country.	
Q.	***Consequences of Termination or Exit.*** As is the case for termination of the joint venture, the joint venture agreement may stipulate the procedures to be used in each circumstance for valuing the participant interests in question. The participants should also consider • whether a participant that withdraws will be prohibited from competing with the joint venture for a certain period of time; • whether a transfer or withdrawal will be deemed a termination of the joint venture for tax or other purposes;	

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	• who will own any intellectual property rights; and • the extent to which the transferring or withdrawing party should indemnify the others for the effects of such a termination. The joint venture partners will have an interest in the capital, goods and inventory that a party may have transferred to the joint venture; technology disclosed to the joint venture; key employees sent from the partner; and goodwill. The partners should also be aware of the host government's issues which include protecting the jobs, retirement benefits, and future job opportunities of the joint venture's employees; assuring payments to the joint venture's creditors; enabling customers dependant on the joint venture to secure needed products or services from alternative services; avoiding disruption to others, such as suppliers and sublicensees; and promoting national interests in technological development or exports of goods or services earning needed hard currency.	
R.	***Confidentiality and Ownership of Proprietary Information.***. The joint venture agreement may provide for the confidential treatment by the participants of the proprietary information of the participants and of the joint venture. Rules should be considered regulating the ownership and use of information developed for and by the joint venture, including licenses from the joint venture to the participants and vice versa. The participants should also consider: • what intellectual property (IP) the joint venture will have access to, e.g. trademarks, patents, processes, etc.? • what will the joint venture be permitted to do with the IP and which, if any, third parties will have access? • what are the economic terms of the transfer or license of the IP? The foreign venturer should be required to acknowledge that the U.S. venturer has all right, title and interest to any proprietary information or material which comes into the possession of the foreign venturer and is not being sold or assigned to the joint venture. Copyrights, trademarks, trade names and patents should all be registered in the territory if possible. The parties should specify whether the intellectual property will be used mainly or partly in any separate operations of the parties.	
S.	***Marketing & Product/Service Lines***. The area of distribution of products or services should be specified and must be drafted carefully to avoid antitrust issues. The participants should determine who will sell the products and services, where the products and services will be offered and the terms of distribution. For example, it is important to determine if royalties or other payment streams will be involved. Sellers may have to take an affirmative marketing obligation. The parties should also determine under what circumstances	

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	the right to sell will terminate.	
T.	***Compliance with Laws.*** The joint venture agreement may bind the participants and the joint venture to comply with applicable laws. A party should inform itself about the Foreign Corrupt Practices Act, which prohibits any U.S. person or firm from knowingly making payments directly or indirectly to officials of foreign government or instrumentalities to obtain or retain business. The Act imposes criminal penalties for violation and as a practical matter may impose on a U.S. business operating in a foreign country the duty to inquire in certain circumstances as to the ultimate designee of payments made to local persons. A U.S. party should also be aware of the Export Administration and IRS regulations that prohibit U.S. persons from agreeing to take certain actions furthering international boycotts and other laws applicable to specific businesses and locales.	
U.	***Miscellaneous*.** A joint venture agreement typically contains other common provisions of general application. Examples include: • representations and warranties as to each participant's authority to enter into the venture, and as to assets, businesses or liabilities to be contributed to the venture; and • information rights and responsibility for public announcements.	
V.	***Ancillary Agreements.*** The parties should consider whether to enter into agreements in addition to the principal joint venture agreement. Common ancillary agreements include the following: • Shareholders' Agreement; • Administrative Services Agreement; • Supply Agreement; • Toll Processing Agreement; • Technical Services Agreement;	

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	• Intellectual Property Licenses and Transfers (patents, trademarks, copyrights and know-how); • Distribution or Agency Agreement; • Loan Agreement or Promissory Notes; • Contribution Agreement or other forms of property transfers and contract assignments; • Guaranties; • Loaned Employee Agreement; and • Delegation of Authority to the management of the venture, with limits based on dollar amounts and duration of the commitments.	