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Introduction

Forming a “joint venture” between one or more companies is one of the most frequent means of conducting international business. This form is most commonly used as a way to share the risks associated with a new enterprise and take advantage of the relative skills or assets of the venture partners.¹

Joint ventures can take many forms. Domestic joint ventures occur between two partners or parties from the same country conducting business in the same country. If a joint venture is to be conducted in the United States, the most basic decision to be made in structuring a domestic joint venture is whether the joint venture entity should be structured as a partnership or corporation for United States tax purposes.² If the joint venture partner is a foreign entity joining with a United States company in a United States venture, the choice is between operating in the United States through a domestic branch of a foreign corporation or as a United States subsidiary.

International joint ventures involve joint venture partners from different countries who may conduct the venture in one of partner countries, in a third country, or in multiple countries. When a United States-based group decides to participate in a foreign-based joint venture, a number of issues having important consequences should be addressed, including, but not limited to, general planning considerations; determining commercial objectives; development of new markets for existing products of technologies; developments of new products or technologies; exploitation of synergies between joint venture partners; determining local partner requirements; intended duration of joint venture (single transaction or short-term relationship vs. continuing business or indefinite relationship); general funding requirements; analyzing factors influencing choice of joint venture vehicle; restrictions imposed by local law (e.g., restrictions on ownership of property or conduct of business by foreign persons that mandate use of locally formed corporation); forms of joint venture

vehicle permitted under local law (e.g., corporation, partnership, limited liability company or equivalent, trust, contractual arrangement); shareholder rights and related issues; potential tax liability; available “exit strategies”; establishment and maintenance costs; determining respective economic contributions and interests of parties; funding requirements and pay-in schedule (how much required and when); allocation of costs among parties; and a range of other considerations. 3

This chapter is not intended to be a comprehensive treatise with full scope treatment of all aspects of international joint ventures. 4 Rather, this chapter intends to address some of the threshold issues and considerations that flow from the formation of international joint ventures, with a focus on the United States perspective.

Reasons Underlying Joint Venture Relationships

A joint venture carries with it a number of advantages and disadvantages. A joint venture can provide a party with access to resources and skills that are unavailable to it at any reasonable cost. However, a joint venture also can be risky because of the reliance that must be placed on the ability and willingness of the other party to perform its obligations during the term of the joint venture agreement. 5

The success of the venture depends on both parties fulfilling their respective roles in the venture. Thus, before entering such a relationship, a party should understand the range of reasons for and against entering into a joint venture relationship:

- Share financial burdens — A party may not have sufficient financial resources to take on a particular project by itself and, accordingly, may seek a partner to share the financial burdens and other risks of the project.
- Accelerating market penetration — A party may seek a joint venture with a foreign partner in a foreign market as a means of accelerating the pace of its market penetration in the foreign market. Here, the party would look to the foreign party to provide the requisite knowledge of local tastes, customs, government relations, and advertising, if needed. A joint venture also may be required for a party entering a foreign market to satisfy foreign country rules requiring local participation and/or ownership.

4 This chapter does not constitute legal advice, and any person seeking legal guidance regarding joint ventures, international or domestic, should consult with an attorney regarding his/her/its specific questions that relate to their specific entity or joint venture.
• Obtain technical resources and skills — A party may want to gain access to the technical resources and skills of another party. A joint venture bringing together managers and scientists from each party may facilitate the rapid exchange of such information regarding existing and new technologies.

• Achieve direct management of research, manufacturing, or distribution — A party may choose a joint venture structure, rather than a network of contractual relationships, to ensure that it is in a position to directly manage research work, manufacturing, distribution, or technology.

• Decrease manufacturing costs — A party may use a joint venture to decrease the current costs associated with the manufacture of its products while retaining some control over the quality of the process and the technology used in the course of completing the manufacturing activities.\(^6\)

**Joint Venture Risks and Due Diligence**

**Partner Risks**

Devoting substantial and critical time and effort to locating appropriate candidates for a joint venture is a paramount step in the joint venture process.\(^7\) While an existing relationship with a current supplier, distributor, or customer may evolve into a desire to form a joint venture relationship, in instances where there is no prior familiarity with the prospective partner, information about potential joint venture candidates can be solicited from a variety of sources. These sources include trade associations, the chambers of commerce, investment and commercial bankers, lawyers and accountants and independent consultants, and published reports filed with the United States Securities and Exchange Commission and with similar regulatory agencies in other countries. Government organizations in many countries (e.g., Ministry of Commerce, Ministry of Trade and Industry) often serve as good sources for foreign investment and joint venture transaction information.

There is no single formula or quantitative analysis available for choosing the right joint venture partner. Narrowing the list of qualified candidates may be based on their financial resources, reputation, skill-set, expertise in technology, market access, labor pool, or other qualities. However, once appropriate candidates are identified, an extensive due diligence investigation should then be conducted to determine whether the prospective partner will provide the party seeking the partner with the best opportunity to meet its business objectives. By its very nature, a joint venture requires two or more parties or groups to partially integrate their skills, attitudes, biases, experiences of the organizations of each

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of the partners, as well as many of the persons within them. Among the factors to be considered when choosing a joint venture partner are:

- Compatibility — The compatibility of the prospective partner with the company seeking the partner in areas such as the level of commitment to the joint venture, the size and structure of the prospective partner, and its underlying national and corporate cultures. Under the best of circumstances, the parties will have had a prior working relationship with one another prior to forming a venture, and will have some familiarity with each other. In more challenging circumstances, the prospective partner will be identified through a search process and due diligence evaluation. In these instances, identifying compatibility may be a slower process and may meet with mixed success until the parties establish a working synergy based on their experience together.

- Functional skills and resources — The functional skills and resources of the potential partner, as they relate to the objectives of the joint venture, must complement those of the party seeking the partner. If the potential partner adds value to the underlying purposes of the joint venture, that fact should be more important than a potential partner’s areas of weakness that may not otherwise be relevant to the objectives and requirements of the joint venture.

- Managerial resources — The potential partner should have the managerial resources required to provide all needed assistance to the joint venture, specifically in those areas in which the partner will have primary functional responsibilities.

- Facilities and administrative support — The potential partner may need to provide facilities and administrative support for a portion of the joint venture’s activities, such as office space, clerical and administrative assistance, particularly, when the joint venture is based in the potential foreign partner’s home country.

- Governmental relations — If the joint venture requires in-country assistance, coordination, official approvals, and licenses, the foreign partner’s ability to assist with and facilitate governmental relations can be extremely important. For example, in a number of foreign countries, the government exercises actual or de facto business industry and administrative authority over local activities, agencies, and departments, and no venture can be successful without such government approvals and support.

- Financial resources — In addition to providing any functional activities that it will be called upon to undertake for the joint venture, the potential partner should have sufficient financial resources to support the joint venture. Otherwise, an investor party may find itself over-budget and over-invested in the venture in a foreign country with a foreign partner who can benefit, but cannot contribute financially to the venture.

- Reputation in the market — The potential parties should have a solid reputation in the market in which the joint venture will operate. The reputation of the foreign party will facilitate the success of the venture. This

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factor is particularly important if the venture’s success relies, in part, on the foreign partner having or building a customer base to promote the venture’s products in the foreign partner’s country.

Once a prospective list of potential partners is identified, information on all of the above factors, as well as the specific skills and resources to be contributed by the prospective partner to the joint venture, should be gathered during the formal due diligence investigation. During this period, the company should focus on the overall strategic objectives of the prospective partner in entering into the joint venture, with particular attention being paid to the possibility that the prospective partner may ultimately use the knowledge obtained in the course of the joint venture to compete against its joint venture partner.

Venture Risks

In considering an international joint venture, especially in an emerging market country, the party should consider a number of risks in assessing the type of venture to pursue and the form of the entity to be employed. Among these are:

- Political risks — A party seeking a joint venture should consider the stability of the government in the country where the venture is to be performed. Is the local government a mature democracy, a kingdom, an emerging democracy, a current or former communist, or socialist state? Do they have representative-prohibited parties? Does the military have control of the government? Is there freedom of the press and assembly? Have there been recent public disturbances, labor strikes, government shutdowns, or riots? Is corruption in the foreign government common? Will the venture need government support to succeed? At what price will the government or local government support come? Can a United States venture partner operate in this environment without running afoul of the Foreign Corrupt Practices Act? Among the ways these risks can be reduced and be addressed are: (a) if future regulatory needs are anticipated, build them into agreements early before the project’s expected life span; (b) build in as much certainty as possible regarding foreign country government regulatory matters; (c) build in anticipated regulatory needs early before the project’s usefulness is obsolete; (d) be wary of becoming involved with politically-connected partners whose fortunes may change with a new government administration; (e) early on involve international institutions in the venture’s life to obtain political cover from local government interference and to obtain outside oversight by more neutral institutions; (f) involve suppliers, subcontractors, and other local participants in political risks so they also have vested interests in assisting the venture with government relations; and (g) avoid making secret side deals with in-country political players that may later be exposed and exploited when those political players fall out of favor.

• Venture maturity risks — While the risk of expropriation of joint venture assets or opportunities in the country of operation or formation is typically viewed as a political risk triggered by change in government or political climate, effective expropriation may occur in other ways.9 In early years of a venture with the infusion of capital, technology, plant, or other matters, the benefits to local government are clear. However, in the later years of a venture, the non-resident partners’ contribution may be less obvious, their return on recent investment is viewed as high, and the assets on the ground are attractive. In these cases, local competitors may put pressure on local governments to start reducing advantages for the non-residents or for the local joint venture. Such risks may be minimized in several ways such as (a) choosing projects that sell wholesale rather than retail; (b) building in an ability to increase capacity if local demand outstrips projections; (c) investigating whether a management and operating agreement may be an equally effective means of meeting venture objectives since they are less susceptible to nationalization and expropriation than actual ownership; and (d) consider obtaining appropriate forms of public or private insurance prior to committing capital and resources to the project in question.

• Currency risks — Is the local currency convertible? Is the local currency stable? Does exchange control currency laws of the jurisdiction restrict the payment of dividends or movement of capital? Does the joint venture entity form restrict the payment of dividends? Are there any ways to overcome the restrictions through hedging of risks with derivatives or obtaining exemptions as a condition to investment?

• Local business risks — Is the local economy stable? Will manufacturing costs, including labor costs, increase dramatically? What is the strength of labor unions in the country where the venture will be performed? Are there existing or potential local competitors to whom the government will provide special privileges that will create an uneven playing field to the detriment of the joint venture? Are there any ways to address these risks, such as working with a politically connected local partner or working with the labor unions or political leaders to obtain fairness in investment and local support?

• Legal risks — Does the targeted country respect the Rule of Law? Do government officials, including judges, have significant discretion with respect to interpretation and enforcement of laws? Is there corruption in the judicial system? Can the risks be offset by choosing a dispute resolution forum that is neutral or outside the influence of the local country? Is there a reliable appellate system for seeking relief from unfair, corrupt, or poor trial judges?

• Enforceability of contractual safeguards and joint venture documents — Is the choice of law provision valid and enforceable? Is an injunction order to enforce a contractual right available? Can the venture partners obtain relief

from the courts in the event of a violation? Are judgments in the local courts predictable and/or enforceable once a judgment is obtained? Is there an identifiable appeals process? Is the local country a party to international treaties for an enforcement of foreign money judgments and arbitral awards?

- Selection of entity as risk — What are the available forms for the joint venture: corporation, limited-liability company, partnership? Which of the types of entities typically used for a joint venture is most common in the country where the joint venture will be performed? Does the local law require known capital contribution and/or are contributions in kind allowed or do they require only cash contributions? Can the corporate form pay dividends at any time or are there timing restrictions on the payment of dividends? Can the distributions be made out of capital or only out of profits? Are interests in the particular kind of entity assignable? Does local law require foreign investment in a specific sector of the economy by certain kinds of entities? Are there restrictions on certain types of local companies investing in certain activities? What is the local market’s perception of the type of entity? What are the transactional costs involved in using such an entity? How should income be characterized? Are there any host country grants and incentives available based on entity choice? What labor laws impact any mandatory benefits for employees and may add unanticipated costs to the venture? What United States and foreign tax laws impact choice of entity: Is there an exit strategy from the local country if the market becomes unfavorable? Does a member have any right to withdraw and its interests redeemed by the company? Can members dissolve the company in case of a deadlock and is an agreement concerning such dissolution by a member enforceable? Does the local entity provide limited liability to its equity owners and, if not, what is the exposure to the local owners and can it be predicted?

Structuring Joint Venture and Choice of Legal Form

In General

The choice of the form of legal entity to conduct the actual joint venture operations is primarily a local law issue and is driven by a combination of the foreign investment laws, business considerations concerning the rights and duties of the joint venturers, and the local and United States tax implications of the structure. 10

A joint venture formed to conduct business outside of the United States may be conducted through a foreign corporation. Here, the joint venture agreement is typically separate from the incorporation documents. 11 The joint venture also

may be conducted as a partnership. In a partnership-based venture, the terms of the agreement between the venturers can be spelled out in a separate joint venture agreement or they may be included in the partnership agreement. Similarly, the joint venture vehicle can be a foreign limited liability company.

Depending on the nature of the relationship between the parties, there are also other means of conducting joint venture arrangements, including joint ventures relating to research and development that produces intangible property formed as a cost-sharing arrangement or as a patent pooling arrangement. A lengthy discussion of the advantages and disadvantages of the form of legal entity is beyond the scope of this chapter. The typical United States entity structure of a corporation, limited liability company, or partnership has counterpart entities in many other jurisdictions. The general advantages of the corporation and limited liability company structure is that, under normal circumstances, shareholders will be shielded from personal liability for corporate debt.

**Partnership Tax Issues**

Prior to the Taxpayer Relief Act of 1997, the structuring of a joint venture as a partnership generally would have to have been a United States partnership, not a foreign partnership. Otherwise, foreign partnerships would have been subject to section 1491 on excise tax on any appreciation of United States operating assets (other than cash) transferred to the foreign partnership.

Absent the application of section 367 principles, the section 1491 excise tax would have been imposed. Under section 367, United States trade or business assets cannot be transferred to a foreign corporation without recognition of gain. Consequently, electing the application of section 367 principles would have resulted in the recognition of gain with a corresponding basis step-up in asset basis, whereas not electing the application of section 367 principles would have resulted in the application of the section 1491 35 per cent excise tax without a basis step-up in the transferred assets. Because section 1491 as it applies to transfers to partnerships was repealed by the 1997 Act, the partnership may be either a United States or foreign partnership.

Faced with a United States company’s desire to use a partnership as a joint venture vehicle, a foreign party’s next decision is whether the joint venture should be an eligible hybrid entity that is treated as a corporation for foreign tax purposes but is treated as a partnership for United States tax purposes pursuant to a “check-the-box” election. The principal reason for considering the use of a hybrid entity would be to achieve deferral from a foreign tax perspective.

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In most countries, however, any deferral benefit would be of limited value if distributions made by the joint venture are taxable to a foreign-owned corporation, because deferral would continue only so long as the foreign-owned corporation is willing to leave its joint venture profits invested in the joint venture with the United States company. If, instead, the foreign company’s country of residence exempts dividends received from a foreign joint venture entity, either pursuant to its internal law or pursuant to the double-taxation provisions of an income tax treaty (e.g., Canada generally), then the use of a United States or third-country hybrid entity may be beneficial.

The considerations relevant to the foreign party in a United States joint venture differ if the foreign party is an individual or a closely held group. Depending upon the application of United States estate tax treaties, an interest in a United States or foreign partnership that holds United States operating assets may be includible in the gross estate of a nonresident alien individual, and an interest in a United States corporate joint venture will be includible in his or her gross estate. From that perspective, a nonresident alien individual generally would not wish to own a United States joint venture other than through a foreign corporation. Using a foreign corporation to avoid United States estate tax, however, involves a cost in the form of a branch tax (if a foreign corporation holds a partnership interest) or United States withholding tax (if a foreign corporation holds a partnership interest through a wholly owned United States subsidiary).

Management and Control of the Joint Venture — Board of Directors

Under United States law, the board of directors, typically elected by the shareholders, will be responsible for the overall direction and management of the corporate entity. The procedures for selection of the board of directors should be set forth in the charter documents of the joint venture (e.g., certificate of incorporation and bylaws) or in the other agreements between the parties that describe their voting rights. Among the issues which should be considered in setting up a board of directors is the actual size and composition of the board; the procedures for allocating control of the board in those cases when the parties do not choose equal representation; selection of the chairman of the board of directors; determining the role of the board of directors in relation to the officers, on the one hand, and the shareholders, on the other hand; and, the circumstances under which control of the board may shift to one of the parties.

The composition of the board of directors is largely dictated by the role that it will play in the day-to-day operations of the enterprise. In some cases, the board

of directors will serve a largely ceremonial purpose, and active management will be vested in the officers and managers of the joint venture. However, if the parties anticipate that the board of directors will take an active role in the management of the joint venture, it is likely that its membership will include one or more of the senior officers and operational managers to be selected by the joint venture parties.

Each party should make an effort to ensure that its designees to the board of directors have specific experience in either the functional or the geographic areas in which the joint venture will be operating. As the venture develops, the composition of the board of directors should reflect its changing business activities. A shift in emphasis of the joint venture from development stage to implementation and marketing stage may create a need for different board members. Sometimes one of the parties, themselves a separate operating company, also may reorganize its own internal structure, thereby causing responsibility for a given product or function to change. In those cases, it is important to ensure that the directors selected by that party continue to support and be able to articulate the needs of the joint venture within the new organization.

With respect to control of the board of directors, for example, one of the parties may be given the right to designate the number of directors necessary to control the board of directors, such as the right to designate three members of a five-member board of directors. In other instances, one of the parties may be given the right to control the board of directors, subject to the prohibition that certain actions cannot be taken without the consent of all of the directors, or, the parties may pre-agree to shift control at some designated benchmark point in the future. Finally, the parties may wish to provide for one or more mutually selected independent directors and implement a voting procedure that vests final decision-making authority in the independent directors in those situations where the parties are unable to reach a consensus.

Change in Control upon Maturation

The control structure for the joint venture entity can be implemented in any number of ways. When the corporation has a single class of outstanding shares of capital stock, the parties will agree by contract to vote their shares for the designees of the other party, and vacancies will be filled by the party having the right to select the nominee for the specific position. Alternatively, when each party has been issued a separate class of capital stock, the charter documents may provide for the election of a designated number of directors by the holders of each class of stock.

17 Many commentators consider this to be the most appropriate structure for the joint venture form, since it vests in one of the parties the ability to initiate actions and manage the joint venture while preserving appropriate protections for the non-controlling party.
As the venture matures, the changing needs of the joint venture may require that the parties consider providing a mechanism to shift effective control of the board of directors from one party to the other party. After the passage of a specified period of time or upon the occurrence of one of several events to be agreed on by the parties, such “vote-switch” procedures would allow one of the parties to elect a majority of the board of directors, without altering the respective financial interests of the parties in the profits of the venture.

Depending on the circumstances, a change in control of the board of directors may be accompanied by corresponding changes in the scope of authority provided to the body in the charter documents of the joint venture. A change or assumption of control of the board of directors upon a certain specified date need not be punitive and may simply recognize the development and maturation of the joint venture and its activities.18

**Change in Control upon Failure to Reach Objectives**

In addition to the primary business activities of the joint venture, it is common to see the parties provide for a shift in control if the joint venture fails to achieve certain pre-agreed performance objectives. For example, a party engaging in the joint venture to improve distribution of its existing products in the local market may seek more control of the enterprise if the level of sales does not meet certain specified minimum revenue figures. Once control has been achieved, the party may initiate appropriate changes in local personnel, modify the business and marketing plans of the enterprise, or even suggest that the local party cannot provide the anticipated amount of distribution support.

A change in control also may be dictated by the occurrence of one or more specified external events, such as the inability of the joint venture to meet its obligations to third-party vendors, the onset of bankruptcy or similar proceedings, or to preserve the value of the assets of the joint venture. Change in control also may be needed if a party breaches its contractual obligations to the joint venture and/or to the other party, or otherwise harms the joint venture.

A change in party control may give rise to a need to change the “control model” whether the new Board or Manager reverts to the existing model or a new model is implemented. The ease of accomplishing this transition depends, in large part, on the type of default and the degree of authority being exercised by the parties with respect to essential functions of the enterprise. Moreover, many of the

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18 For example, if the business plan contemplates an initial period of joint development activities, each of the parties should share in the control of the joint venture during that period, particularly if one of the objectives of the enterprise is to ensure appropriate transfer of technology. However, upon completion of the development stage, the activities of the venture will shift toward sales and distribution; and, at that time, it may be appropriate for the party with the specific distribution capabilities to assume responsibility for the day-to-day operations of the joint venture.
events that trigger a shift in control may be so serious that it may be appropriate for the parties to restructure, or even terminate, the activities of the joint venture.

Management and Control of the Joint Venture

In General

The management and control structure of the joint venture is one of the most important matters to be negotiated between the parties. Assuming that the choice is made to utilize the corporate form of business entity, the parties must consider various issues involving the composition of the board of directors, the election of the board of directors, the selection of the emerging officers and key managers, the respective voting rights of each of the parties and the matters on which each will be allowed to vote, and the specific duties of the board of directors, the officers, and any committees created by the parties to manage one or more of the business functions of the enterprise.

Board of Directors' Decisions

The parties should decide whether and how to designate one or more representatives to act as members of the board of directors, or as officers of the joint venture. In addition, each of the parties should have voting rights on matters of importance to the joint venture. While oversight authority should remain in the board of directors, the joint venture parties may decide to hire or delegate someone to assume day-to-day control over material aspects of the operations of the joint venture. The actual participants in a joint venture may be business units of their respective companies, such as a division or a wholly owned subsidiary, or they may be a separate entity created solely for the purpose of managing and operating the joint venture. The board of directors, which will include the managing director and representatives from each of the parties, will have the role and responsibility to review the operational activities, approve and monitor the strategic plans and budgets, approve major transactions relating to the joint venture, and provide advice and consent on important personnel decisions.

In addition to choosing the board of directors, the most important decision faced by the joint venture is the selection of the manager of the joint venture, who may be referred to as the “managing director” or “president”. It is common to provide from the outset a rotation for the managing directors’ position, based on objective performance measurements of the business of the joint venture. In some cases, the local partner may have the right to designate the initial general manager, while the foreign party would have the right to interview and approve proposed managing director candidates. Once the foreign party has had an opportunity to gather information and experience in the new market and the joint venture has grown to a specified size in terms of revenues and/or employees, the

foreign party should have a right of increased involvement in designating the
general manager.\textsuperscript{20}

Another possibility is to plan on development of independent leadership for the
venture. In this scenario, the general manager position will be awarded to
qualified candidates that are mutually agreed upon by the parties, but who have
no prior relationship with either of the parties.

Balanced leadership also may be achieved by allowing one party to designate
the general manager while the other party has the right to select the chair of the
board of directors. Depending on the prior relationship between the joint
venturers, their familiarity and comfort level in delegating various aspects of the
joint venture to each other, the success or failure of the joint venture in meeting
its objectives, and different management and operational models may be
appropriate.

Management Models

In General. There are three basic governance structures or models from which
the joint venture parties can choose when deciding how to manage the business
operations of a joint venture, i.e., (a) operator, (b) shared, or (c) autonomous.

Operator Model. The operator model of management is often used when one
party has little experience in the joint venture market.\textsuperscript{21} When the “operator
model” is selected, the management responsibilities for the joint venture are
assigned to one of the venture parties.

However, the assignment of management responsibilities does not necessarily
flow from ownership interests. A majority interest owner may or may not be the
operator. In fact, a minority owner in the venture may be designated as the
operator when it has more experience in the project of the joint venture than the
majority owner, or when the majority owner is a partner who does not reside in
the location of the joint venture.

The operator will be responsible for management of the day-to-day activities of
the joint venture, including coordination between business units and
establishment and operation of management systems and processes. The
operator will typically have the right to designate the managing director and
persons who will serve as managers of the main business units and functions
within the joint venture. Under this model, the decisions made regarding the
operations of the joint venture will be primarily based on ongoing

\textsuperscript{20} Gutterman and Brown, Going Global: A Guide to Building International Business
(2011), at s 31.17.

\textsuperscript{21} Provision can be made to moving to one or both of the other models as time goes by
and the new party gathers more knowledge and experience in the market. The joint
venture also may be converted to a wholly owned subsidiary of one of the parties if it
elects to “buy out” the ownership interest of the other party and continue to operate
the business on its own.

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communications between the venture managers and their colleagues who work full-time in their separate organization of the operating party.

The operator model may be most appropriate when one of the parties is new to the market in which the joint venture will be operating and the other party to the venture has the requisite experience and contacts in that market. In that situation, the non-operator partner will focus on transferring its unique technical, business, or financial advantages to the joint venture operator, and may provide its own personnel to the operator to ensure that the transfer of its advantages to the operator proceed smoothly. Once the initial transfer has been completed, the non-operator may maintain personnel within the joint venture to observe the operator’s conduct of business, and learn about the venture market environment so that the non-operator is better prepared to expand its responsibilities in the joint venture on its own, at some point in the future.

However, a venture party, which is new to the geographic market, may still assume operator responsibilities. For example, a United States manufacturer may be interested in reducing its production costs by establishing a manufacturing joint venture with a partner in a foreign country where labor costs are much lower than in the United States. Here, the United States manufacturer may have a strong interest in managing the entire process of setting up the factory, the assembly line, training the workers, and monitoring the quality of the production, but may not have in-country experience in a foreign country. If the primary market for the goods manufactured is outside of the foreign country where the manufacturing facility is located, then it may be appropriate for the United States manufacturer to build, equip, and manage the foreign-based manufacturing operation.

This type of approach also may be attractive to the local foreign partner, who may have less knowledge and expertise in the manufacturing process, but who will benefit from the transfer of technical knowledge from the United States manufacturer. The operator model also is commonly utilized by companies that need a high level of cross-border coordination and need to transfer knowledge or technologies to the foreign entrant’s global network. To ensure that the production of the joint venture will continue to be available, the non-operator may bargain for inclusion of an option in the joint venture documents, that would allow it in the future to purchase the interest of the operator in the joint venture and, thus, eventually convert the joint venture into a wholly owned subsidiary.

**Shared Control Model.** A “shared control” model is based on the premise that both parties have complimentary skills and resources that can be contributed to the joint venture in order to create a fully-functional business, and which neither party, working alone, could launch and operate on its own. The shared control model contemplates that each party contributes the resources for which it has a comparative advantage over the other party at the time the joint venture is formed. The most commonly described example of the shared control model is a
A company that wishes to enter into a foreign market in which it has little or no knowledge, and does so by selecting a local partner to provide the foreign market support for commercializing its technology and products. In this example, the new partner entrant into the foreign country would be committed to contributing technology, existing products, product development skills, experience, capital and manufacturing processes and the local partner would provide the necessary resources, labor, personnel and in-country government relations, sales, marketing, and distribution networks.

In a shared model, there will be a number of functions and activities in which the parties must learn how to effectively share control. For example, the foreign party should insist on sharing responsibilities in the financial market area with the non-resident venture party. The parties should share the accounting systems of the joint venture.

This ensures not only that the venture parties are in compliance with the in-country tax requirements of their respective home countries and in compliance with the tax reporting requirements of the joint venture host country, but sharing accounting systems also builds mutual trust among the parties in one of the most important areas of the venture — the financial accountability of the venture parties.

To avoid any perceived preference to one of the parties by an accounting firm from one of the venture party’s home country, and to ensure independence, a joint venture party may require that the books and records of the joint venture be audited or reviewed by an international accounting firm. While transporting supplies from outside the foreign venture country may be the original source of the venture, as the joint venture grows and local firms in the venture country are qualified, there may be a shift toward purchasing necessary supplies from sources within the local venture country. With regard to banking requirements, the foreign party should require that the joint venture use a local affiliate of a multinational bank that also has offices in the foreign parties’ home country.

In the shared control model, the size and composition of the board of directors is an important consideration. Whenever possible, the board of directors should include a senior executive from each of the venture parties since their input can be particularly valuable if conflicts arise, and the assumptions regarding the shared control model begin to unravel. This may occur when one of the parties appears to be exercising more control than the other party anticipated it exercising.

22 There should be a preference for a small board of directors, perhaps no more than five people, who can oversee the joint venture activities and act quickly to work out any problems that may occur in the course of day-to-day operations. If it necessary for the board of directors to be larger than five members, it is recommended that a small group be designated as members of a “management committee” so that they can keep a closer eye on how decisions are being made and monitor the execution of the joint venture strategy.

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For all of its potential advantages, the shared control model carries a higher risk of failure than the operator model. A joint venture, working under the shared control model, can become paralyzed by indecision, conflict, and gridlock regarding important operational initiatives.

There are other dangers associated with the model. For example, when employees, working within the joint venture, are initially taken from one partner who itself has independent operations, those employees may continue to have strong loyalties and ties outside of the joint venture organization to key joint venture personnel, including ongoing reporting responsibilities to those joint venture executives outside the context of the joint venture.

The keys to overcoming the risks of using the shared control model appear to be active participation of the board members, and implementation of staffing policies, as described below, that ensure that the foreign party participates in and learns from the joint venture experience from the beginning. Therefore, requiring recognition of these potential problems and allowance for an effective dispute resolution mechanism to resolve ongoing issues between the parties will be important.

**Autonomous Model.** The third business management model employed in a joint venture is called the “autonomous” model. This model is used when the parties have agreed that the joint venture will operate as an independent entity, free of excessive daily controls imposed by one or both of the parties.

While the autonomous model may be implemented at the time the joint venture is formed, the more likely scenario is that the joint venture would evolve into this model after the operator or shared control models have already been deployed and not worked, or after the joint venture has reached the point of economic and financial maturity where it can be self-sustaining.

Companies that need a high degree of cross-border coordination are unlikely to allow the joint venture to migrate to the autonomous model since they need quick access to management of the joint venture to satisfy needs in other areas of their global network.

**Allocating Control of the Joint Venture**

The relative interests of the parties in the profits of the joint venture are usually determined by their ownership interests in those classes of shares that are entitled to share in any distributions made by the corporation. But share ownership does not always dictate the degree of actual financial or operational control exercised by the parties.

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While a majority ownership interest in a joint venture might mandate the assumption that the majority owner will control the entity, there are situations where the majority owner is a non-active investor or where the nature of the party’s contribution to the enterprise or the local laws will require that a party having a minority interest in the profits of the joint venture may be better able to control certain of its activities.

For example, in a joint venture to develop a real estate project (such as a hotel) in a foreign country, the non-resident majority partner may require a local operator or manager to meet local law requirements regarding real estate ownership. In the course of allocating control of the joint venture, several different factors should be considered including:

- Relative expertise — Which partner possesses the requisite expertise necessary for achieving the functional and operational objectives of the joint venture? In most cases, control should be allocated in relation to the partner’s respective substantive contributions to the joint venture. A party contributing technology to the joint venture, for example, should have the primary right to control the use of the technology in development efforts; a party with responsibility for sales and distribution of the products of the joint venture should be given primary authority over various marketing matters.

- Board versus management control — What is the appropriate scope of authority to be exercised by the shareholders, the directors, the officers, and managers of the joint venture? If the success of the venture depends on its ability to move rapidly to exploit opportunities in the local marketplace, it may be advisable to delegate broad discretion to the officers and managers of the joint venture, with the role of the directors and shareholders being more advisory in nature. Alternatively, in those cases where the development of the joint venture involves completion of a series of tasks, requiring joint efforts, shared decision-making procedures may be more appropriate.24

- Impact of shared control — The parties should consider how the use of shared-control requirements (i.e., provisions that require that specified actions must be approved by both parties) will impact the day-to-day actions of the joint venture. While shared control might appear to be an attractive means for easing concerns that might exist at the outset of the relationship, the practical effect of such an arrangement is that burdensome meetings and coordination efforts may unnecessarily divert the parties’ attention from, and slow the progress of, the core objectives of the joint venture.

24 Even in those cases where the parties share nominal control of the board of directors, they may agree as to the delegation of decisions in specified areas to a subcommittee of the board of directors controlled by the party having the expertise in that area. For example, decisions regarding research and development activities might be left to the chief technical officer of the joint venture, appointed by the party with expertise in that area, and a subcommittee of the board of directors controlled by representatives of the appropriate party.
• Financial and technical commitments — The manner in which the financial and technical benchmarks of the joint venture are to be monitored and assessed is a key aspect of control. In the course of developing the overall strategic business plan for the joint venture, the parties should carefully identify material and largely irreversible commitments of cash and other resources, as well as the key technical and financial objectives of the joint venture. In some cases, it may be appropriate to abandon or modify the original business plan or transfer control of the joint venture from one party to another.

• Agreed allocation of control — A joint venture may be established as a “50-50” enterprise. This generally means that the parties each contribute a relatively equal amount of cash and assets to the joint venture and agree that profits and distributions also will be shared equally. While an economic agreement of this type might suggest that the parties also equally control the management of the joint venture, the partners nevertheless may allocate control over certain decisions of the venture in a manner that departs from shared control. For example, one party might be issued a class of stock having the right to elect a majority of the members of the board of directors, while the other party might be issued a class of stock providing the right to approve certain major actions relating to the affairs of the corporation. It also is common for joint venture partners to enter into a contractual agreement providing for the right of each of the parties to designate specific officers and managers of the joint venture. 25

• Use of Voting Class Rights to Dictate Control — With respect to a joint venture in which one of the parties has a greater interest in the profits than the other party, it is still possible to utilize special class voting rights to provide a minority interest partner with effective control of the joint venture. In addition, local law may provide certain voting rights to minority shareholders that effectively allow them to veto actions taken by the majority shareholder, either directly, or by virtue of their right as minority shareholders, to demand an appraisal of the value of their shares and the repurchase of their interest by the joint venture at the specified value. 25

25 While the creativity of the parties with respect to allocation of control may be almost limitless, consideration should be given to the requirements of the law under which the joint venture was formed and organized. For example, local law will generally specify certain matters that require separate class votes and also may substantially limit the ability of the entity to issue non-voting securities. In addition, regardless of the law under which the joint venture is formed and organized, foreign investment laws and regulations in the home country of the foreign partner may require that local parties have certain minimum rights with regard to control of a joint venture.

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Operational Activities of the Joint Venture — Covenants

Covenants regarding the internal operations of the joint venture serve several purposes. Most importantly, they cause the parties to focus on the day-to-day operations of the venture and the resources that will be required for successful operation.

In addition, in those situations where one of the parties will be given control over the management of the enterprise, covenants of this type ensure the non-active partner that due care and attention will be paid to the business and provide certain standards for measuring the performance of the managing partner.

Typically, a breach of any of the covenants will trigger a “vote switch”, in which control of the enterprise reverts to shared management responsibilities or the existing management is replaced in its entirety by agents and representatives supplied by the other party.26

26 The content of the various covenants between the parties will vary depending on the specific activities of the joint venture; however, one or more of the following items are usually worth considering: (a) The joint venture should be managed in a manner that complies with all applicable laws and regulations, and all filings should be made, and fees should be paid, to maintain the good standing of the business form under the laws under which it is organized. In the event that the activities of the joint venture will be subject to specified regulations, such as export control laws, procedures for ensuring compliance with such regulations should be described in some detail. (b) The parties should agree that all taxes, assessments, and governmental charges will be paid and discharged promptly, subject to the rights of management and the board of directors. In addition, properties of the joint venture should be maintained in good repair, working order, and condition. (c) The parties should agree to cause the joint venture to purchase and maintain appropriate types and amounts of insurance relating to its activities, such as property damage, fidelity bond protection, public liability, workers’ compensation, directors’ and officers’ insurance and indemnity bonds. (d) In the event that the joint venture incurs any external indebtedness, an undertaking should be provided to ensure that such obligations are paid in a timely fashion. (e) Provision should be made for the deposit of the funds and capital of the joint venture into mutually agreed bank accounts. All withdrawals from the accounts should be strictly regulated in accordance with internal control procedures established by the parties. (f) The expectations of the parties regarding staffing of the joint venture should be included in the agreement, particularly if there are persons the parties consider essential to the success of the enterprise. In some cases, a provision might be included regarding the purchase of “key person” insurance for one or more individuals. When the joint venture is to be engaged in detailed development work relating to technology and the associated intellectual property rights, the covenants should describe the plans of the enterprise with respect to securing appropriate statutory rights, including patents, trademarks, and copyrights. As with any transaction involving intellectual property rights, the joint venture documentation should cover the procedures for protecting the technology to be owned or used by the joint venture.
终止合营企业

一般

研究表明，联合企业的人均寿命在4到7年之间，很少会持续超过15年。因此，虽然联合企业双方在开始时的良好意图可能会使双方不愿考虑其解散或终止，但实际上，双方应采取这一措施以便预见联合企业的不可避免的变化，联合企业中的各方可能会离开联合企业，或停止联合企业。

当双方预计长期关系时，第一选择是转移其联合企业份额；一个更累赘的选择是出售公司，而最不理想的选择是联合企业的解散。希望退出联合企业的方可能希望得到补偿。一般来说，转移利益可以发生在：

- 第三方；
- 其他联合企业方；或
- 合营企业本身。

虽然不是一份详尽的清单，但在形成联合企业和考虑退股方的问题时，双方应考虑以下方面。

基本规划

合营企业协议中，在适用法律下，转让股份的依据是什么？当地的法律是否适用于合营企业协议的任何方面？如果出现僵局，会发生什么？合营企业将如何处理一方管理内部变化，如果新管理的一方不支持合营企业？双方是否会选择将其利益固定在一个特定的时间内？如果一方申请破产，另一方的合营企业利益会发生什么？是否有转让利益的条款如果出现持续的分歧在资本支出？如果一方退出，合营企业是否有优先购买权？他们是否有权购买退股方的股份？是否有机制公平地评估退股方的股份如果这些股份不是公开交易的？一方的利益是否可以转让？如果是的话，如何实现转让？有转让限制吗？退股方是否允许部分转让其份额，而必须完全退出？双方是否允许内部转移在对方的同意下？


（发布1-2012）
venture party? Will the minority party have tag-along rights? Will the majority partner have drag-along rights?

**Sale or Distribution**

If it is not possible for one venture party to purchase the other party’s interests, then the next best solution may be to provide for a sale of the company as a going concern. Such a sale will tend to maximize shareholder value since it will require independent valuations and appraisals from sources outside of the joint venture company. In a partial sale of venture interests, the risk is that a competitor may try to take control of the venture.

Here, valuation and appraisal mechanisms, knowledge of local laws and restrictions on the sale of the joint venture, and termination and dissolution will be critical. When a member-party exits the venture, is the exiting/withdrawal party in a position to compete with the venture? If so, it may be appropriate to implement a non-competition agreement with exiting/withdrawing parties. These will be subject to time and geographical considerations.

There are a number of other considerations to contemplate and incorporate regarding exiting/withdrawing/departing parties, including how disputes regarding exiting parties will get resolved. Disputes regarding withdrawing parties, and dissolution of the joint venture, may be addressed in an arbitration clause or they may be subject to local courts. If such disputes are subject to an arbitration clause, depending on the arbitral tribunal selected by the parties, and scope of the dispute issues involved, the arbitral tribunal may decide it can hear such matters, or it may refer those disputes to the local courts that have a nexus to the parties or the joint venture locale.

**Winding Up of the Joint Venture Company**

Unlike bankruptcy, which involves the rights of the creditors and hence third parties, arbitration disputes are, in theory, not matters of public policy. Nevertheless, because of the statutory nature of a company or limited liability partnership and the right to apply to have it wound up, in some jurisdictions only local courts have the power to grant such relief. Whether arbitrators have the powers to wind up a company will again depend on the relevant national law. For example, in England, in *In re Magi Capital Partners LLP*, a party applied to stay the other party’s petition for the winding up of their limited liability partnership. The court granted the stay on the basis that before it could make a winding up order, it had to be satisfied that it was just and equitable.

The court found that the allegations that were before the arbitrator could be material to the decision to be made on the hearing of the winding up petition. In its reasoning, the court indicated that if the partnership at stake had been an

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28 International Chamber of Commerce, Mazza Report, “Non-Monetary Relief in Selected ICC Cases”.

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ordinary partnership — as opposed to a limited liability partnership — the arbitral panel would have had jurisdiction and adequate power to wind up the partnership. However, since the entity to be wound up was a limited liability partnership, which is a creature of statute, the court declared that parties could not forfeit their statutory right to apply to have the statutory entity wound up by the court.

Similarly, in France, in ICC Award Number 11090, the arbitrator refused to dissolve the joint venture company. The law applicable to the joint venture contract was French and the arbitration was sited in Paris, but the joint venture company was incorporated in a third country. The arbitrator denied its jurisdiction to grant such remedy on the basis that the dissolution of the company would have an impact on third parties and could contravene with that third country’s public policy.

In a New South Wales case, the High Court held that the right of a contributory to apply to the court for a winding-up order cannot be limited by agreement. The court refused to stay a winding-up petition because it did not fall within the scope of the discretionary provisions of section 53 of the Commercial Arbitrations Act 1984.

On the other hand, under Belgian law, a claim requesting the dissolution of a company can be subject to arbitration if the articles of association provide for an arbitration clause that is formulated in a fashion that gives it a wide scope. With regard to the latter requirement, it has been recognized that as the dissolution of the company would not only impact the shareholders but the company as well, the arbitration clause contained in the articles of association must specifically refer to disputes between shareholders as well as disputes between shareholders and the company.

Equally, in an arbitration case administered under the Zurich Chamber of Commerce Rules, upon request of both parties, the tribunal ordered the termination of the joint venture agreement. In a first interim award, the tribunal declared the joint venture (two companies) between the parties dissolved and appointed a liquidator. In a further interim award, the tribunal ordered that the sale of the shares of the joint venture companies be carried out in an auction to be held under its supervision and according to procedures decided by it. As the parties subsequently settled, how these awards would have been enforced will remain unknown.

29 Insolvency Act of 1986, s 122(1)(g).
30 International Chamber of Commerce Arbitration Award no 11090, 2002.
31 International Chamber of Commerce Arbitration Award no 11090, 2002.
32 Best Floor Sanding Ltd v Skyer Australia Ltd [1999] VSC 170.
Other Issues

Dispute Resolution Clauses and Mechanisms

The global financial crisis has triggered a lot of litigation and arbitration in Europe, as well as in Asia, particularly in intellectual property litigation. In addition, the construction industry has seen the downsizing of projects, late payments, and contract terminations. These factors have combined to create an “arbitration boom”. The turmoil in financial markets also has led to a swift increase in international disputes, particularly involving investments and financial institutions. The advantages commonly associated with arbitration are even more relevant in the context of joint venture disputes.

International joint ventures often involve not only the joint venture partners, but also multiple contractors and subcontractors to each party, or to the joint venture, or to all. Accordingly, arbitration may be the only acceptable and viable dispute resolution method where all relevant parties to a dispute can appear and resolve their differences. Arbitration permits the resolution of international disputes in a neutral forum by independent decision-makers. By choosing a neutral arbitral tribunal as the arbitration seat, the joint venture partners can avoid litigating in courts of the country in which one of the parties is based and avoid the perceived favoritism or bias of those courts.

While a United States party may be comfortable litigating in United States courts, foreign party venture partners, particularly from non-common law-based jurisdictions, may be uncomfortable with United States courts, costs, time, the confrontational nature of aggressive discovery, foreign language and possible unsympathetic courts, judges, and juries. Likewise, United States parties may lack confidence of enforcing their legal rights in the courts of the venture partner’s home country or the courts of the venture itself, particularly in undeveloped or emerging countries with un-established or unreliable judicial systems. Accordingly, the joint venture parties should address early on their agreement to a mutually agreeable neutral tribunal.

In those rare instances of appeals of arbitration awards, or challenges to the enforcement of such awards, even such published cases do not discuss in detail the testimony of the parties or the evidence. Tribunals, such as the ICC, that do publish summaries of awards, do so by omitting party names, thereby preserving their privacy. Being able to resolve disagreements in private in international joint venture relationships is crucial in cases where the joint venture project is still ongoing.

Here, the joint venture partners are attempting not only to conduct their joint venture business together, but also to conduct their respective individual businesses. More and more, parties realize that the disclosure to the public of the joint venture’s internal problems and disputes bring unwelcome press and media attention which can damage the reputation of the parties, the business of the joint venture, and impact the viability of the joint venture project itself. Parties also should be aware that self-proclaimed business ethics monitoring...
organizations and NGOs now use the internet to publish “exposes” and “investigative reports” about Western companies doing business in foreign venues alleging exploitation of foreign parties and foreign natural resources. The presence of the internet and the impact such publications can have on businesses increases the need for joint venture parties to increase privacy and private dispute resolution mechanisms.

When technical disputes within a particular industry are involved, the parties may want to provide for the appointment of arbitrators with specific technical expertise within the arbitration agreement itself. Different types of joint venture projects and their expected disputes may dictate the need for more technical expertise among arbitration panel members.

In those cases, the arbitration clause should stipulate the requisite qualifications of the arbitrators, and whether their selection should occur before, or after, a dispute has arisen. Projects that likely give rise to more general legal disputes involving less technical-based evidence may be better handled by arbitrators drawn largely from the legal industry and pre-approved by the chosen arbitral forum.

Arbitrability of Joint Venture Disputes

Depending on the nature of the issues involved, most of the disputes arising out of, or in relation to, joint venture agreements are arbitrable. This includes issues relating to breach of contract, competition law, and intellectual property rights.

However, under the law of some jurisdictions such as France, Spain, and Brazil, issues relating to the validity of registered intellectual property rights are deemed not arbitrable. Other issues usually considered not arbitrable include bankruptcy and matters involving corruption and fraud (as a result of the general prohibition on arbitration of criminal matters).

Minority shareholder claims and statutory claims in general also may be excluded from arbitration in some jurisdictions. These are typically provided for by company legislation in the jurisdiction where the joint venture company is incorporated. This jurisdiction does not necessarily correspond to either the arbitration seat or the applicable law.

As previously set forth, the winding up of the joint venture company (e.g., resulting from the termination of the joint venture agreement) also may raise arbitrability issues. Here, the ultimate question is whether the arbitral panel can dissolve the company, if the company’s shareholders are unable to resolve the dispute.

However, this question is viewed differently in different legal systems. Whether arbitrators can validly wind up a company can be viewed as a matter of arbitrability jurisdiction or as a matter of availability of the remedy in arbitration.
United States

Scope of the Arbitration Agreement

In General

The scope of the arbitration clause tends to be a relevant issue in joint venture disputes. Subject to their arbitrability, disputes covered by a standard arbitration clause containing the common expression “arising out of or in relation to” include not only contractual but also tort and statutory claims.

Such clauses can be included in the letter of intent, joint venture or cooperation agreements, as well as the company’s articles of association. In some circumstances particular to joint venture disputes, the scope of the arbitration clause may be extended *ratione materiae* and/or *ratione personae*.

Scope Ratione Materiae

In the absence of a conflicting clause in the contract deprived of an arbitration clause (usually an implementing contract or a contract subsequently negotiated in the context of the joint venture), the scope of the arbitration clause included in joint venture agreements may be extended to this contract.

Such extension *ratione materiae* will be subject to the existence of a substantial link between the two contracts. This link can be economic or structural, i.e., one contract is complementary to the other or refers to the performance of the other.

Scope Ratione Personae

The scope *ratione personae* relates to who can or should be party to arbitral proceedings. The contractual nature of arbitration means that only parties who undertook to submit their disputes to arbitration can be party to it. It often means that there can be no joinder of a third party to the arbitration agreement unless the latter, as well as all current parties to the arbitral proceedings, consent to it.

This mechanism is reflected in article 22 of the London Court of International Arbitration Rules that empowers the tribunal to allow joinder of a third party upon application of one party provided any such third party as well as the applicant party consent to it. This “extra” power of the tribunal appears to replace the need of the other parties’ consent and thereby facilitates such joinder.

Pursuant to the International Chamber of Commerce (ICC) International Court of Arbitration, article 6(2), if the respondent does not file an answer or if any party raises one or more pleas concerning the existence, validity, or scope of the arbitration agreement, the court itself — rather than the tribunal — may decide that the arbitration shall proceed if it is *prima facie* satisfied that an arbitration agreement may exist (without prejudice to the admissibility or merits of the plea or pleas). When the claimant files its request for arbitration against multiple respondents amongst whom at least one is a non-signatory, the court applies the
provisions of article 6(2) to determine whether the matter can proceed against all the respondents.

As frequently occurs in joint venture disputes, the joint venture agreement can be assigned or a third party could simply acquire shares in the joint venture company.

In that instance, the question is whether the original arbitration agreement binds the third party. The answer depends on the validity of the assignment and the applicable provisions in the agreement. If the assignment is valid under the applicable law, it is generally accepted that the new party to the agreement is entitled to commence arbitration pursuant to the arbitration clause contained in the assigned agreement. 35

In Marchetto v. Dekalb, 36 one of the 50/50 shareholders sold its shares in the joint venture company to third-party A, which was a partnership formed between this original shareholder and third-party B.

Later, the original shareholder became third-party C and third-party D replaced the original shareholder as a partner in third-party A. The District Court held that given that third-party C is the successor of one of the initial shareholders, the other defendants also may be joined.

Non-Signatories to Arbitration Agreements under United States Domestic Law

Generally, “arbitration is a matter of contract”. A “party cannot be required to submit to arbitration any dispute which he has not agreed so to submit”. 37 While a contract cannot bind parties to arbitrate disputes that they have not agreed to arbitrate, “[i]t does not follow . . . that under the [Federal Arbitration] Act an obligation to arbitrate attaches only to one who has personally signed the written arbitration provision”. 38

A party can agree to submit to arbitration by means other than personally signing a contract containing an arbitration clause. Well-established Common Law principles dictate that, in an appropriate case, a non-signatory can enforce, or be bound by, an arbitration provision within a contract executed by other parties.

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35 Cedrela Transport, Ltd. v Banque Cantonale Vaudoise, 67 F Supp 2d 353 (SDNY 1999).
36 Marchetto v Dekalb, 711 F Supp 936 (ND Ill 1989).
Which Law Governs the Issues of Arbitrability of Non-Signatory Claims or Against Non-Signatories

In General

United States Federal and state courts have recognized, that “[i]t does not follow ... that under the [Federal Arbitration Act] an obligation to arbitrate attaches only to one who has personally signed the written arbitration provision”; instead, under certain circumstances, principles of contract law and agency may bind a non-signatory to an arbitration agreement. 39

Although state law determines the validity of an arbitration agreement, courts have applied both federal and state law to determine the related, but distinct, issue of whether non-signatory plaintiffs should be compelled to arbitrate their claims. The Federal Arbitration Act does not specify whether state or federal law governs, and the United States Supreme Court has not directly addressed the issue. Federal courts of appeals, however, have frequently applied federal substantive law when deciding whether a non-signatory must arbitrate.

United States Rules Regarding Non-Signatories

Various courts in the United States have developed several rules or theories under which a court may compel a non-signatory to an underlying arbitration to arbitrate. Federal courts have recognized six theories, arising out of common principles of contract and agency law that may bind non-signatories to arbitration agreements:

- Incorporation by reference;
- Assumption;
- Agency;
- Alter ego;
- Equitable estoppel, and
- Third-party beneficiary.

“Direct benefits estoppel” is a type of equitable estoppel that federal courts apply in the arbitration context. 40 Most federal courts, however, list only five of

these theories, omitting third-party beneficiary as a separate ground. Each of these theories have been addressed in a number of cases and the case law in this area is well developed.

Remedies

As a general principle, arbitrators have the powers granted to them by both the parties (directly in the arbitration clause or the submission agreement and indirectly in the arbitration rules adopted by the parties) and the arbitration law applicable to the procedure.

Moreover, because of the contractual nature of arbitration, arbitrators only have powers over parties to the arbitration agreement. This restriction obviously impacts upon the type and magnitude of relief capable of being granted by arbitral panels and the extent to which these are enforceable.

Experience also shows that addressing contractual remedies in the joint venture agreement puts the parties in a better position if disagreement arises as to the future of the joint venture. Providing detailed and comprehensive rights exercisable in case of breach or deadlock, and reducing the tribunal’s discretion to hear the issues in arbitration or defer them to local courts, will help the parties add predictability and security to their agreements.

Final and Enforceable Awards

Often investment projects are operated on an international basis with business partners and/or joint venture companies located in different countries. Under the New York Convention 1958 and its ratification by over 140 countries, a foreign arbitral award is more easily enforced overseas than a judgment delivered by a domestic court. Moreover, joint venture partners are typically keen to obtain a

3d 773, 776 (2d Cir 1995) (citing cases); Bel-Ray Co v Chemrite (Pty) Ltd., 181 F 3d 435, 440-43 (3d Cir 1999); Amoco Transport Co v Bugsier Reederei & Bergungs, AG (In re Oil Spill by the “Amoco Cadiz”), 659 F 2d 789, 795 and 796 (7th Cir 1981).

41 Local Union no 38, Sheet Metal Workers’ Int’l Ass’n v Custom Air Sys, Inc, 357 F 3d 266, 268 (2d Cir 2004); Javitch v First Union Sec, Inc, 315 F 3d 619, 629 (6th Cir 2003); Fleetwood, 280 F 3d 1076; Employers Ins of Wausau v Bright Metal Specialties, Inc, 251 F 3d 1316, 1322 (11th Cir 2001); Bel-Ray Co v Chemrite (Pty) Ltd, 181 F 3d 435, 446 (3d Cir 1999); Int’l Paper Co, 206 F 3d 417; Thomson-CS., 64 F 3d 776.

42 The New York Convention 1958, articles II.1 and V.2(a), as well as most of the international arbitration regimes provide that their application is limited to disputes capable of settlement by arbitration. Excluded from this list are the types of disputes that belong exclusively to the domain of the court under the relevant domestic law. Given that jurisdictional challenges, including on grounds of inarbitrability, can potentially be made at different stages in the arbitral proceedings, the lex arbitri (usually the law of the seat), the law applicable to the substance, and the law of the place of enforcement are likely to be relevant in determining whether the dispute is arbitrable.

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fast resolution of the dispute in order to be able to make a decision as to the future of their joint venture, if still existent/viable. As a result, arbitration's unique features of absence of (or restricted) appeal and limited grounds for challenge of the award increasingly attract parties driven by business priorities and cost control.

Transfer of Shares

Transfer of shares and termination of the joint venture agreement appear slightly more controversial but will sometimes be key to the resolution of a deadlock in a joint venture dispute. Subject to relevant national law, arbitral tribunals generally have the power to order a transfer of shares that was specifically contemplated in the joint venture agreement.

Where there is a deadlock or where some actions on the part of a party have jeopardized the relationship, a tribunal may be unable to resolve a deadlock between the parties because it cannot substitute itself for the board of directors and the shareholders in the decision-making. In some circumstances, a corporate "divorce" and the termination of the joint venture agreement is the only viable solution and a remedy sought by at least one of the parties.

In the presence of an exit or termination clause in the joint venture agreement (e.g., "blind bid mechanism" or "Russian roulette"), the arbitral panel will apply the contractual procedure and remedies. Upon a party's request, the tribunal could declare that the clause requirements are met, and order the failing party to participate in the procedure provided for in the agreement. This is the best scenario; indeed, when no exit clause is provided in the joint venture agreement, granting of such remedy will be at the entire discretion of the tribunal and therefore uncertain.

Multi-Party Arbitration

Joint venture stakeholders should bear in mind that the joint venture company may not become a party to the arbitral proceedings, unless it was party to the original arbitration clause in the joint venture agreement or the joint venture is subsequently joined in the arbitration under one of the theories recognized by the courts for joining non-signatories. Issues inherent to multi-party arbitrations tend to arise with even more relevance in the context of joint venture disputes. These include establishment of the tribunal.

Consolidation of disputes arising out of the same project, but among parties who are not privy to a common agreement with an arbitration clause, can only be agreed on by all the parties to the proceeding to be consolidated as well as the tribunal. Although not excluded in principle, consolidation is far from guaranteed. As a result, failure of the parties to contemplate a dispute resolution mechanism encompassing disputes involving all the stakeholders in the project, may portend a considerable increase in arbitrations, legal costs, and the risk of inconsistent rulings. For instance, parties could agree that a tribunal constituted

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in accordance with the arbitration agreement will remain in existence until it declares itself to be functus officio. In this way, any party to the arbitration agreement will be able to submit a “fresh dispute” within the scope of the arbitration agreement without the need of the consent of the tribunal and the parties to the pre-existing dispute(s).

Conclusion

The globalization of international business relationships inherently leads to both a proliferation of international joint venture and multi-party collaboration agreements. Some will fail, but careful planning will improve the chances of success. Arbitration is the natural dispute resolution method for international disputes, and this is even more true for international joint venture disputes. However, if the remedies required are either not available within the process, or are not recognized by subsequent local court intervention, the international business community will eventually lose faith in arbitration process.

Although international arbitration provides the parties with great flexibility, its span and its applications are somewhat limited by the contractual nature of arbitration. Parties and their counsels should be aware of these limitations and address possible future disputes at the outset through careful and comprehensive drafting of the arbitration clause in their joint venture agreements.