Joint Venture Agreements

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What is a Joint Venture?

- Joint Venture is an agreement between two or more business partners to assume a common business strategy on a project. All partners generally agree to share the profits and losses through their common shareholdings

- The JV partners undertake specific obligations for the effective running of the JV, for example:
  - Grant of technical assistance and know-how
  - Providing facility of established distribution channels
  - Providing marketing expertise
  - Providing management services
  - Separate agreements may be entered into between the respective parties and the JV for some of the above obligations

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Important Terms of a Joint Venture

- Object and scope of JV
- Role and contribution of JV Partners
- Funding / issuance of capital
- Financial arrangements
- Composition of board / governing body
- Management of JV – Appointment of CEO/MD
- Distribution of profits among the JV partners
- Transferability of shares
- Deadlock resolution

Important Terms of a Joint Venture

- Restrictive covenants on JV Partners and the JV company
- Reserved matters / Veto right matters
- Non compete
- Non-solicitation
- Confidentiality
- Representation and Warranties
- Indemnity
- Termination of the JV and the consequences
- Dispute Resolution

Forms of Joint Venture

Unincorporated

- Partnership firm
- Association of Person
- Trust / Society (Not for profit ventures)

Incorporated

- Private Limited Company
- Public Limited Company
- Limited Liability Partnership (LLP)

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Partnership

- 2 or more people up to maximum of 50 partners – No limit in case of HUF and partnership formed by professional who are governed by special Acts
- May/may not be dissolved in case of death of a partner
- No own legal standing although a separate PAN allotted to the partnership
- Unlimited business liabilities
- Losses incurred due to act of one partner is liable for payment from every partner of the partnership firm – Concept of joint liability

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LLP

- LLP is a body corporate
- 2 or more partners can incorporate
- Concept of Designated Partners
- Separate legal entity
- Mutual rights and duties of partners governed through LLP agreement
- Limited liability of partners except in cases of acts done with intent to defraud creditors or for any fraudulent purpose
- Mandatory maintenance, audit and filing of annual accounts
- Existing firms, companies can be converted into LLPs

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COMPANY

DIN & DSC

A Directors Identification Number and a Digital Signature is required to initiate the incorporation process

Incorporation

- ☞ Memorandum & Articles of Association
- ☞ Registered office address
- ☞ 2 shareholders & 2 Directors for Pvt Ltd Co.
- ☞ 7 shareholders & 3 Directors for Public Ltd Co.
- ☞ 1 Director Indian resident
- ☞ No minimum capital required to incorporate a company

Corporate Name Approval

- ☞ Approved by the Registrar of Companies
- ☞ Emblems and Names (Prevention of Improper Use) Act, 1950 compliance

Post Incorporation

- ☞ Within 30 days, hold first Board Meeting
- ☞ Within 30 days, appoint first auditors
- ☞ PAN & TAN applications; tax purposes
- ☞ Bank Account opening

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Conduct of the Joint Venture Company

- Frequency of board and shareholders meetings
- Quorum for meetings
- Appointment of directors/observer
- Board and general meetings
- Appointment of Chairman
- Appointment of CEO/MD/COO/CFO/Legal Head, etc.
- Veto rights
- Dividend policy
- Deadlock
- Management, board rights and control Issues
- Board and management rights in subsidiaries
- Decisions regarding subsequent funding

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Transferability of Shares

- Right of First Offer / Right of First Refusal / Lock in Period on Shares / Tag Along / Drag Along / Call Option / Put Option
- Now enforceable both in a private limited company and a public limited company
- Concept of "absolute discretion of the board" provided in the articles of association of a private limited company
- Section 58(2) of the Companies Act, 2013 provides that a contract with respect to transferability of shares will be enforceable as a contract even in the case of a public company
- **Has to be ensured that provisions of transferability are provided in the articles of association of the company to make them binding on the company and the shareholders – Supreme Court ruling in Rangraj's case**

Non-compete / Non-Solicitation

- Usual to insert a non-compete but enforcement specific or otherwise a big question mark – though Indian law different from usual common law rule of "reasonable restriction" acceptability
- Section 27 of Contract Act, 1872 renders "void" a non-compete restrictions except in case of "sale of a business" with goodwill and that too with specific limitations on duration, scope and geographic extent
- Judicial precedents upholding non-compete during the term of the JV to be enforceable
- Selling shareholders cannot be prevented from undertaking employment in a competing business
- Confidentiality obligations are enforceable
- Non-solicitation is enforceable

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Deadlock

- Arises when the nominee directors of the shareholders or the shareholders themselves take opposing views or where a director appointed by a minority shareholder has exercised a right of veto.
- Most common and complicated in 50%:50% JV
- Resolution may be in the form of;
  - Commercial Mediation
  - Chairman's casting vote for a deadlock
  - Exit by one of the parties, or
  - Buy out of one of the party

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Representation and Warranties

- <u>Representation</u> - statement of fact that relate to a state of affairs that exists in the present or existed in the past
- The purpose of representation is to induce reliance, establish standard and to allocate risk. Remedy for misrepresentation would be indemnity or damages
- <u>Warranty</u> - is a promise that a statement is true
- The purpose of warranty is to provide indemnity if a statement is not true and to allocate risk. Remedy for breach of warranty would be damages
- Who represents and warrants – company or promoter or both?
- Whether absolute or qualified – best knowledge qualifiers
- Limitation (survival provision): different levels – e.g., tax liabilities 7 or more years; *de-minimus* concept

Indemnity

- Indemnities are often considered in the context of liability to reimburse a contracting party from liabilities asserted by third parties (non-contracting parties)
- All possible triggering events need to be considered, and if a party's own negligence is a triggering event, then this should be specified
- Distinction between fundamental warranties and other warranties
- Pre-conditions to indemnity rights (notice of potential claim, restriction on settlement without consent of indemnifier, monetary limits etc.)
- Enforceability of liquidated damages - In India liquidated damages becomes a cap - penal damages will not be enforced
- Threshold for invoking indemnity claims- individual and aggregate thresholds

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Liquidated Damages

- Means fixing of amount of damages in advance at the time of entering into the contract
- A genuine pre-estimation of loss and should not be in the form of penalty
- Any dis-proportionate amount to the actual loss will be treated as penalty and not enforceable
- Such clauses are subject to close scrutiny and are often challenged
- The clause should expressly indicate that the clause is indeed a “pre-estimate of damages”
- Calculations should be made to reflect how the amount was selected

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Thank You

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