KEY POINTS

- The JVCo's statutes contain its DNA, its genetic code, within the parameters prescribed for the relevant entity type in the jurisdiction where it is incorporated.
- The choice of jurisdiction and entity type will largely define the appropriate statutes that are required for the JVCo.
- Though the statutes regulate the rights and obligations of the JV parties, the JVA will trump the statutes if any conflict arises between them.

Feature

Author Richard Keck

Joint venture agreements: part 8 – coding the DNA for the JVCo

This article is eighth in a series examining project development and finance joint ventures ('JVs') based on the International Trade Centre incorporated joint venture model agreement ('JVA') among three or more parties.[1] This instalment discusses art 7 of the JVA, which sets forth the responsibilities of the JV parties to adopt the 'statutes' of the joint venture company ('JVCo').

Article 7 uses thrifty wording. Article 7.1 requires the JV parties to adopt the 'statutes' of the JVCo and directs that the statutes provide for (1) meeting of the shareholders, (2) board of directors, and (3) auditors. Article 7.2 directs that the form of the statutes must be agreed by all the JV parties and conform to the substantive provisions in arts 8 (meeting of shareholders), 9 (board of directors), 10 (auditors and independent expert) and 11 (accounts and dividends). Finally, art 7.3 provides that, though the statutes regulate the rights and obligations of the JV parties, the JVA will control internally – and so trump the statutes, if any conflict arises between the JVA and the statutes.

Article 1 defines 'statutes' as the JVCo's 'corporate instruments'. These generic terms are driven by the model JVA's need to work across multiple entity types in any jurisdiction. The lawyers drafting the JVA should replace them with the applicable governing instruments for the type of entity chosen in the jurisdiction where the JVCo will be incorporated.

Two starting points, therefore, are the jurisdiction in which the JV parties choose to incorporate the JVCo and the type of entity they choose for the JVCo (both of which were discussed in part 4 of this series). Broadly speaking, the jurisdiction in which the JVCo will be incorporated may either be a common law jurisdiction (which primarily includes the UK and its former colonies) or a civil law jurisdiction (virtually everywhere else). However, on the subject of corporate/company law, there has been significant convergence across jurisdictions such that the modern day distinctions between common law and civil law systems are less relevant with respect to the specifics of entity law. Each jurisdiction's entity law will largely be set out in relevant laws, and, in some jurisdictions, interpretive or implementing administrative regulations and decisions and/or judicial decisions.

Choice of entity will also be based on the options available under local law. Virtually every jurisdiction today allows some form of limited liability entity, and many offer more than one option. Different types of limited liability entities can significantly impact corporate governance structure and the tax status of the entity and its owners, among other things. Most jurisdictions have an entity that is roughly equivalent to an English company limited by shares or a US corporation, two entity types familiar to a large portion of the readership of this journal, and therefore those that the author will use as examples.

Some jurisdictions also distinguish between, on the one hand, company/corporate entity types with more relaxed and flexible governance rules, which are particularly attractive to closely held entities such as the JVCo, and, on the other hand, those entity types with more heightened and rigid governance rules intended to protect passive minority shareholders of listed or other publicly traded entities who are unable to protect themselves by private contract. England does this by distinguishing between a private limited company ('ltd') and a public limited company ('plc'). The US generally does not distinguish between private and public entity types under state law, but adds protections for public shareholders through a layer of federal and state securities laws and regulations. However, some US states have begun to adopt special 'close corporation' provisions in their corporate codes that allow even the basic corporate rules to be further relaxed. For tax purposes, the US has also seen the proliferation of the so-called limited liability company ('LLC') over the past two decades. An LLC is essentially a hybrid between a partnership and a corporation that attempts to achieve partnership-like tax treatment with the governance features and continuity of existence of a corporation.

In choosing where to incorporate, choosing an entity type (where such choices are allowed by the licence, contract or concession to be held by the JVCo) and preparing the relevant corporate instruments, lawyers for the JV parties should consult the relevant laws, regulations and decisions, and always seek advice of local counsel. Traps for the unwary abound.

The choice of jurisdiction and entity type will largely define the appropriate statutes that are required for the JVCo. For example, in England and in those common law jurisdictions which base their entity law on English company law, a JVCo that is a 'company limited by shares', or simply a 'company' as it is often called, whether public or private, would require a memorandum and articles of association as its statutes (although the memorandum has ceased to be of any practical significance since 1 October 2009 when the Companies Act 2006 came into force). In the US, depending on the specific state, a 'corporation', whether public or private, would have articles or a certificate of incorporation and bylaws. The memorandum of association of an English-style company and the certificate/articles of incorporation of a US-style corporation are similar, containing only such basic information as the name of the entity, its

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Biog box

Richard Keck is a partner in the New York office of Macmillan Keck, Attorneys & Solicitors. He regularly acts for government authorities in designing and implementing competitive tenders, and evaluating applications, for telecom licenses, and for project developers and sponsors, and other investors, in forming and negotiating JVAs for bidding consortiums and in connection with the preparation and submission of competitive license applications. Email: richard@macmillankeck.pro

authorised share capital and certain other fundamentals. The articles of association of an English-style company and the bylaws of a US-style corporation are also similar, containing detailed rules for corporate governance and a variety of other matters governing the relationships among the entity, its shareholders or members and its board of directors (and, in the US, its officers). The US-style LLC also has two principle corporate instruments – the articles of organisation, which are akin to the articles/certificate of incorporation for a corporation, and the operating agreement, which is akin to the bylaws (although it may be, and often is, expanded to include matters typically found in a shareholders agreement).

One difference between the English and American approaches, as applied to closely held entities such as the JVCo, is that in England the memorandum and articles of association are both public documents, whereas in the US only the articles/certificate of incorporation/organisation is a public document, while the bylaws (for a corporation) or operating agreement (for an LLC) are private documents to which only the shareholders, directors and officers have access.

In drafting the JVCo's statutes, lawyers for the JV parties should consider whether, under the host jurisdiction's laws, some matters are required to be expressly addressed in a particular document to be enforceable. For example, certain voting agreements, if only in the JVA but not in the JVCo's 'statutes', may not be legally effective, even as between the JV parties. Such requirements, in the author's experience, can vary widely and surprisingly from one jurisdiction to the next. Another matter meriting attention is the desirability of keeping certain matters private, by only addressing them in the JVA or any private statutes, but not putting them in the public statutes. Where there is a tension between the enforceability objective and the privacy objective, the lawyers must draft with care.

Although the model JVA contemplates that the JVCo's statutes will be prepared after the JV parties enter into the JVA, their lawyers should consider preparing them concurrently, and attaching agreed forms to the JVA. This advance planning may reveal any discrepancy between what the JV parties intend to agree in the JVA and the requirements of local law, allowing the parties to negotiate alternative arrangements at an earlier stage in the relationship, before they have invested heavily in the JV and committed themselves to third parties (such as by submitting an application for a licence, contract or concession). Indeed, in some cases, submission of draft statutes for the JVCo may be required as part of the tender process for the licence, contract or concession, so the JV parties must address them at an early stage.

Although art 7.1 lists only three topics to be addressed in the statutes, meeting of shareholders, board of directors and auditors, in fact, the statutes will need to incorporate a number of other matters covered by the JVA, such as its name, its period of duration, and its authorised share capital. The subjects of shareholders, board and auditors will be discussed at length in future instalments in this series. In art 1 of the model JVA, 'meeting of shareholders' simply means the shareholders acting as a governance body through voting on various matters reserved for a shareholder vote as well as in the election of directors. 'Board of directors' refers to the principal executive body of the JVCo., so, for example, in the case of an LLC, the term would usually refer to the managers. As discussed in previous instalments of this series, where there are only a small number of JV parties, each of whom has representation on the governing body of the JVCo, it may be appropriate to dispense with the notion that they have fiduciary duties to all the shareholders and expressly acknowledge that they will be acting individually in the best interest of the JV party that appointed them to the board. An LLC permits this by allowing the members to dispense with managers, whereas English company law and US corporate law are typically less flexible on the subject.

In a somewhat circular fashion, the model JVA defines 'auditors' as the JVCo's 'external' auditors. These are essentially independent intermediaries to protect the shareholders by confirming the financial information provided by the board. Again, where all the shareholders are represented on the board, the role of auditors may be less about protecting shareholders, and more about confirming financial information for lenders, fiscal authorities and the regulator or other government agency overseeing the licence, contract or concession.

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Finally, JV parties sometimes want to agree to quite sophisticated arrangements that are customary in more developed jurisdictions but cannot be confirmed with local counsel in the jurisdiction where the JVCo will be incorporated as either being permitted or enforceable. Must the arrangements be in the statutes to be enforceable? Or will putting the arrangements in the statutes actually increase the risk of their being held unenforceable? These are difficult questions, and there is sometimes no clear way to eliminate the risks. One way to mitigate them is to have the JVA governed by the laws of a jurisdiction other than that in which the JVCo is formed where the law is more predictable. In these circumstances, the JV parties are relying heavily on the directive in art 7.3 that the JVA trumps the statutes where the two come in to conflict.

The JVCo's statutes contain its DNA, its genetic code, within the parameters prescribed for the relevant entity type in the jurisdiction where it is incorporated. Careful attention to select the appropriate combination of genetic code for the JVCo can help the JV parties ensure that its legal existence is consistent with their expectations as set forth in the JVA. ■

The model JVA discussed may be found at www.jurisint.org/doc/orig/con/en/2005/2005jiconen1/2005jiconen1.pdf.