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## The Foreign Joint Venture Corporation: Some Legal and Business Considerations

# THE FOREIGN JOINT VENTURE CORPORATION: SOME LEGAL AND BUSINESS CONSIDERATIONS

BY WILLIAM R. ROSS\*

*Private international law involving the organization of corporations under foreign civil and common law systems can be an exciting and challenging experience for an American lawyer. One such corporate organization is the foreign joint venture corporation, involving local ownership and management participation. Mr. Ross discusses some basic requirements of foreign law and major business considerations with which the American lawyer must be acquainted in order to form such a business venture. He emphasizes the importance of participation and counsel of the lawyer during the early stages of negotiation. He points out the importance of choosing the proper foreign corporate form as a firm foundation for immediate and continued success of the venture and offers ways of handling the problem of control of management. Mr. Ross concludes that with proper investigation, negotiation, and planning from both legal and business points of view, the foreign joint venture corporation can be a useful and satisfactory way for American businesses to enter or expand activities in foreign markets.*

## INTRODUCTION

EVER since the famed clipper ships, and before, United States businessmen have sought and discovered new markets in international trade. As the industrial revolution of the 19th century progressed, the export-import trade began to grow and it has continued to expand, picking up momentum particularly in post-World War II years when the industrial nations of Europe began to get back on their feet. Manufacturing subsidiaries of U. S. corporate parents have been established around the world to bring facilities producing U. S. goods closer to the far-flung marketplaces. In recent times it has become the policy of the large industrial concerns of this nation to treat the entire globe as a single market for goods and services of practically every kind.

As a result of this continuing trade explosion, which has made this nation the foremost industrial country in the world, the commercial, financial, legal and governmental interests and problems have taken on new dimensions, creating new complexities and adding new matters which must be considered by the lawyer called into the private international field.

For example, in past years the expansion of foreign trade and

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the in-flow and out-flow of capital and earnings occasioned by international investment have not been as significant in the private and governmental sectors as they have become today. Thus, a matter of which we are much more aware and which is important to all U. S. companies doing business abroad is that of maintaining a favorable balance of payments at the national level. This problem is at the moment of vital concern to the U. S. Government, and while there may be other factors having equal or greater influence on this problem, such as the national government itself, the President of the United States has asked for increased export trade and decreased direct investment in foreign ventures to combat the problem.<sup>1</sup>

International trade is becoming more and more involved as an instrument in foreign affairs. Hardly any policy of the United States relating to international commerce does not first require review by or approval of the United States State Department. For example, recent legislation enacted and approved to permit rationalization of U. S. and Canadian manufacture and trade of automobiles and original equipment automotive parts was first proposed to the Congress by the Administration after representatives of the U. S. Departments of Commerce and State had participated in the discussions and negotiations leading to the rationalization agreement and the preparation of the implementing legislation.<sup>2</sup> The General Agreement on Tariffs and Trade is of major importance in foreign affairs. And a system of import quotas can be detrimental to the commercial interests of a foreign country and, thus, to the foreign relations of the United States; such a system also can be imposed with conditions designed to influence a foreign country's position on important political interests of the United States.

The newly emerging and so-called less-developed nations of the world are more and more becoming a significant influence on international trade by providing new markets and new sources of goods. To these nations world trade is required for their survival and growth, and, to that end, it is a policy of the U. S. Government to foster, encourage and promote participation by private enterprise in foreign economic development.<sup>3</sup> Many of these nations have

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<sup>1</sup> See McQuade, *Corporate Voluntary Balance of Payments Program and the Lawyer*, SYMPOSIUM, PRIVATE INVESTORS ABROAD—STRUCTURES AND SAFEGUARDS 205 (Southwestern Legal Foundation 1966). See also 33 Fed. Reg. 49 (1968) (establishing mandatory controls on foreign direct investment).

<sup>2</sup> *Hearings on H.R. 9042, An Act to provide for the implementation of the agreement concerning automotive products between the Government of the United States of America and the Government of Canada, Before the Senate Comm. on Finance*, 89th Cong., 1st Sess., at 122, 490 (Sept. 14, 15, 16, 20 and 21, 1965).

<sup>3</sup> Important to all U.S. investors considering less-developed countries is the investment guaranty program of the U.S. Agency for International Development under the Foreign Assistance Act of 1961 which guarantees investments against certain political and business risks.

established incentives designed to encourage investment from abroad to develop industrial and trade potential.<sup>4</sup>

In recent years, various countries, both developed and less-developed, have become nationalistic in their attitudes toward world trade and investments from abroad, undoubtedly a result of expanded industrialization and trade programs. Their concern, of course, stems in part from foreign exchange problems and their purpose is to protect industrial and commercial activities which have been established. Attempts to accomplish this purpose are by several means, including raising of tariffs, imposing conditions on investments from abroad and closing their borders to imports of goods also manufactured by newly established local facilities.

This does not mean that the American businessman is no longer welcome in the world of industry and trade; it does mean, however, that he will not be able in all instances to invest as freely as he has in the past. In these circumstances, more and more attention has been directed lately by American businessmen to associating with a local partner in a joint venture corporation as a way of bringing their companies to the markets of the world or of expanding existing international endeavors.

It is the purpose of this article to set down some characteristics of the foreign joint venture corporation — its definition, establishment, management and operation requirements — hopefully raising for the lawyer some practical legal, governmental and business considerations which will be of assistance to him in his private international practice.

## I. THE JOINT VENTURE CORPORATION

### A. *Definition*

A foreign joint venture corporation can be defined as a separate legal entity formed abroad usually by two corporations, one U. S. and one local, to achieve an economic objective in which the participants desire limited liability for an indefinite term and, from the American point of view, a familiar corporate framework of organization, management and operation. It combines the advantages of the incorporated business organization with those of the traditional joint venture relationship.

The joint venture corporation concept has been in existence in

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<sup>4</sup> Typical of such incentives are those offered by Ghana to enterprises that develop the productive capacity of the economy, expand exports and offer management and technical training to Ghanaians. Such incentives include exemption from payment of income and other corporate taxes, special depreciation allowances and waiver of tax on dividends to non-residents. See BUSINESS INTERNATIONAL CORP., INVESTING, LICENSING AND TRADING CONDITIONS ABROAD (May 1966). One should also note that so-called developed nations likewise offer attractive incentives to encourage economic expansion and the establishment of new industries. See, e.g., Law Office, Frank Boas, Esq., *Doing Business in Belgium*, 2 CCH COMM. MKT. REP. ¶ 6455 (1967).

this country for a good many years.<sup>5</sup> And, as we will examine later, it can be quite useful as a successful foreign undertaking to manufacture and to sell locally produced goods. And, it fits in compatibly with the corporation and company laws and commercial codes of the countries of the world.

### B. *Advantages of a Joint Venture*

There are several reasons why an American firm may want to consider the use of a joint venture to enter or expand its activities in the general world market or a particular foreign market. The basic reason, of course, is to take advantage of a favorable and profitable demand for a firm's products in a market area. In so doing, it may be useful and wise to rely on the knowledge and reputation of a well established local business firm in order better to understand the likes and dislikes of the local consumer and to obtain more intimate knowledge of the local customs and practices of commerce; also, manufacturing and marketing skills may be pooled. Another reason is that an American company may be able to furnish idle equipment and machinery which, although used, may be more than satisfactory to local requirements of both a potential partner and the market; it is likely that such equipment can be contributed in return for all or a major portion of the interest in the new corporation. The joint venture also permits the U. S. partner to enter more markets or to diversify by spreading investment capital while at the same time, perhaps, meeting local or U. S. public policies calling for limitations on investments. It limits the financial risks involved in those countries where political and economic stability and commercial benefits are in doubt; it satisfies in many instances the nationalistic attitudes of the local government, a development which, particularly in the emerging nations and in Japan,<sup>6</sup> has effectively restricted the introduction of U. S. capital; it limits resentment toward U. S. investment.

There are disadvantages to the joint venture. In some instances, it is possible that joint ventures may be too rigid to meet today's fluid markets, restricting the American company's capacity to adjust strategy and tactics, like shutting down operations which are un-

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<sup>5</sup> Note, *Joint Venture Corporations: Drafting the Corporate Papers*, 78 HARV. L. REV. 393 (1964).

<sup>6</sup> See FOREIGN TAX AND TRADE WINDS, Oct. 1966 [Release No. 96(10-66), Matthew Bender & Co.], in which it is reported that a U.S. company lost a two-year fight to establish a wholly-owned subsidiary in Japan. A ruling handed down by the Ministry of International Trade and Industry [MITI] required 50% ownership by a local Japanese firm in the undertaking applied for, and consultation by the U.S. company with the Japanese government about its production plans for the first three years. See also FOREIGN TAX AND TRADE WINDS, Apr. 1967 [Release No. 102(4-67), Matthew Bender & Co.], and BUS. INT'L., Mar. 3, 1967, which report some liberalization by the Japanese government of investment requirements.

profitable or no longer necessary, or altering the product mix of a given plant. Another disadvantage is that the American firm could suddenly find itself competing with a joint venture in which it holds an interest in markets where tariff barriers are falling and customs unions or free trade associations are formed, such as EEC, EFTA, LAFTA, CACM and the Arab Common Market.<sup>7</sup> Still another disadvantage — and this may be a quite important one, depending upon the circumstances — the American firm may not have the control of the operation it desires or is accustomed to having. Despite these factors, the joint venture has been useful for American investment abroad.<sup>8</sup>

### C. *Finding the Partner*

Probably the most important initial step in the establishment of a joint venture relationship is finding a suitable local partner. And finding such a partner may take a great deal of time and effort. Careful and painstaking investigation of all potential partners is required. The goal is to find a local partner who has like or nearly like business objectives, corporate history, policies and requirements, management philosophy and the like. Compatibility is the byword, for it, together with complete good faith exhibited and practiced by both partners at all times, really determines in the long run the success or failure of the joint venture. The association hopefully is to be successful and continuing. Keeping this in mind, potential partners should hold extensive "sounding out" discussions to decide, initially, whether the relationship is desirable. All matters pertinent to the venture ought to be discussed, at least to some degree, to the end that the scope of the joint venture can be defined. In this connection, attention should be given to the possibilities of growth. The manufacturing and marketing potential of the products involved, and the ability of the prospective venture to manufacture and to sell them should be studied. The delicate matter of management decision making must be thoroughly explored in depth to determine whether conceivable conflicts between the two exist or could develop over the manner in which the decisions are to be made. Generally, the parties should attempt to discover any reservations either may have with regard to matters which could, slowly or rapidly, deteriorate relationships during the course of the joint venture operation.

These are, essentially, business considerations, but the lawyer will be called upon to render counsel and advice in a number of matters and to draft and review various documents required in the

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<sup>7</sup> 75 BUSINESS INTERNATIONAL CORP., MANAGEMENT CHECKLISTS FOR FOREIGN OPERATIONS 31 (1966), *citing* BUS. INT'L., Sept. 4, 1964.

<sup>8</sup> See JOINT INTERNATIONAL BUSINESS VENTURES (Friedmann & Kalmanoff eds. 1961).

transaction, and he will need to recognize the business problems which arise in order that his analyses and advice can be meaningful and valuable. Hopefully, he will be permitted to attend all or nearly all discussions so that he can become intimately acquainted with all aspects of the proposition.

## II. ORGANIZATION OF THE JOINT VENTURE CORPORATION

### A. *The Preorganization Agreement*

Prior to the establishment of the joint venture corporation, the parties would be well advised to reduce to writing important agreements reached during the negotiation stage. This document, called the preorganization agreement and executed by both parties, will evidence agreement of the partners to proceed with the project. It will constitute a reflection of the intention of the parties, general in some respects and specific in others, with regard to the objectives and policies of the joint venture corporation. It also will serve as a sort of "legislative history" of the joint venture organization which can be used to assist in the interpretation of any agreements the new company might have with either partner.

A typical preorganization agreement should set forth the principal objectives of the new company; the amount of authorized capital it is to have; how much capital is to be issued; how the capital is to be paid in and when; shares of capital each partner is to have; conditions pertaining to transfer of shares (*e.g.*, right of first refusal). It should describe generally what the articles of association of the new company are to contain, such as provisions for compensation of directors, officers or managers and how it is to be determined, voting and quorum requirements, procedure for amending the articles, and the like. It should state the corporate structure and how it can be changed. It should also state whether there are to be any agreements between the new corporation and the individual partners, such as lease agreements covering plant and equipment, agreements to furnish management for the new company, agreements to furnish technical assistance, agreements to license rights respecting patents, know-how and trademarks. There should be a description of the duties of each partner in organizing the new corporation; a provision stating how the costs of organization of the new corporation are to be borne; and a stipulation as to whether any disputes between the partners arising under the agreement are to be referred to arbitration, and, if so, who is to act as arbitrator and where the arbitration is to take place. Finally, dissolution and liquidation procedures should be specified as well as the laws of the country under which the agreement is to be construed and the juris-

diction to which the parties submit. Other matters may be included, depending upon the requirements of the parties.

### B. *Choosing the Corporate Structure*

There are several matters which are primary in choosing the kind of corporate organization best suited to the venture. The size and the objectives of the venture will be important considerations in the choice. Local laws and practices generally will be influencing factors, particularly where they relate to the manner of organization and management and to investment and repatriation of profits and capital. The amount of capital to be required, initially and in the future, and the liability of each partner could be influencing factors. In the final analysis, however, the partners should seek the kind of structure which is easy to organize and which furnishes flexible, economical and profitable operation with only as much publicity as is necessary.

A joint venture corporation, regardless of its type, will encounter in its daily problems the same kinds of laws as will practically any other corporation, such as negotiable instruments law, sales law, customs requirements, property law, insurance law, taxation codes and trade regulations, to name just a few. And, although the lawyer will find it necessary to think through all problems with which he is confronted in choosing the kind of corporate structure, perhaps this is a good time to point out that he will not need, nor will he be able, to gain a comprehensive knowledge of the legal systems of the various countries of the world. He must equip himself with a general understanding of applicable laws of the country in which the venture is to be organized and operated; in some instances, he will have to gain specific knowledge and understanding. Generally, he will find most applicable civil law concepts in force in one civil law country descriptive of the practices in other civil law countries. In all instances relating to problems specific in nature, he should be guided by the advice and counsel of a competent local attorney.

In establishing a foreign joint venture corporation, the American partner will want to give specific consideration to the local laws pertaining to corporate organization, taxation, industrial property rights, special laws or aspects of laws relating to foreigners, and, perhaps, the property law, antimonopoly law and social and labor legislation.<sup>9</sup> Of special importance will be laws and regulations respecting restrictions on remittance of profits and repatriation of

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<sup>9</sup>Not to be overlooked is the applicability of U.S. tax and antitrust laws and trade regulations, topics not covered in this article.

capital, including limitations on payments by local companies of royalties and fees. All such laws will be part of the framework within which the joint venture corporation will be established and operated. They also will furnish the basis for answers to the basic question of whether a joint venture corporation is the kind of operation desirable to the objectives of the American company and whether it furnishes a practicable and profitable method for meeting the business purposes intended.

The American lawyer will most probably find that the form of organization to be chosen for the joint venture corporation will, regardless of its type, resemble fairly closely the corporate structure familiar to him in the United States. The elements of its structure will be drafted to meet the business purpose much the same as the provisions of the articles of incorporation of a company in this country are selected and directed. However, because the foreign joint venture corporation is multi-national, considerations will arise which will complicate usually uncomplicated corporate questions. For example, the local partner probably will not be as large as the American client and his operation may be family-held and managed; he, thus, may take a more personal view of the operation of the venture. The American partner, on the other hand, will consider the venture as a subsidiary or affiliated part of his world-wide organization. The result could be a basic divergence of views, and possibly there will immediately arise the question of whether one or the other is to have control of a particular function, especially where it may be a 50-50 equity ownership venture.

In most foreign countries there are two kinds of corporations. One is the kind which most closely corresponds to our corporation: the *société anonyme*, *sociedad anonima* or *Aktiengesellschaft*. The second form is what is called the limited liability company — known as the *société a responsabilite limitee*, the *sociedad de responsabilidad limitada*, or the *Gesellschaft mit Beschränkter Haftung*.

### 1. The Corporation

Under the civil law, the corporation is a creature of contract and not a creature of charter granted by the state. Simply stated, the shareholders execute a contract of organization similar in form and substance to articles of incorporation. When filed with the proper registry, the contract becomes the basic corporate document and, after completing certain other formalities, the corporation is then authorized to commence operation.

A civil law corporation is similar in many respects to the U. S. corporation. It constitutes an individual legal entity distinct from

that of the associates or shareholders.<sup>10</sup> Each shareholder's liability is limited to a definite contribution.<sup>11</sup> Although not a creature of government charter, the civil law corporation usually is governed fairly strictly by the commercial and civil laws of the nation and by the organization contract.<sup>12</sup> The reason, of course, is to afford protection for its stockholders and the persons with whom it deals. The laws, once properly translated, are quite readily understandable; they normally set down the requirements in logical order and concise terms, and the kinds of requirements are not unlike those prevailing in common law jurisdictions. For example, the formation requirements will specify the number of organizers necessary (the number will vary from country to country, usually from three to seven). And it is not unusual for the laws to require a minimum number of continuing stockholders, usually the same number as that required to organize the corporation in the first instance.<sup>13</sup> Most civil law countries permit some or all of the stockholders to be foreign corporations. This provision is, of course, vital to the establishment of the joint venture.

The capital structure requirements are much the same as in this country: the capital is divided into shares and normally they can be common or preferred, of one or more series, and either nominative or to bearer. No par shares are permitted in some countries.<sup>14</sup> Bearer stock has been used extensively because of its flexibility in transfer and the fact that it provides anonymity, a consideration which has been of significance to stockholders in civil law countries, perhaps to avoid taxes imposed on transfer. Each shareholder has one vote for each share of stock issued to him. However, in some countries the voting powers of holders of large blocks of shares may be limited.<sup>15</sup> Statutory provisions may impose minimum capital requirements and will state how much of the authorized capital must be subscribed. Usually a specified portion of authorized capital must be paid in. Corporate shares are freely transferable after a minimum subscription price has been paid in. It is possible that some countries will require every corporation to list its shares on a stock exchange even though no shares are to be

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<sup>10</sup> See, e.g., CODE OF COMMERCE (TITRE IX DES SOCIÉTÉS) art. 2 (Belg.). See generally 1 DOING BUSINESS ABROAD (H. Landau ed. 1962) for a discussion of civil code corporations.

<sup>11</sup> CODE OF COMMERCE art. 26 (Belg.).

<sup>12</sup> *Id.*, art. 1.

<sup>13</sup> In France, for example, there may not be less than seven shareholders. FRENCH COMPANY LAW OF JULY 24, 1966, art. 73.

<sup>14</sup> See, e.g., CODE OF COMMERCE art. 41 (Belg.).

<sup>15</sup> In Belgium, no person may cast a number of votes exceeding one fifth of the total votes pertaining to all the outstanding shares or two fifths of the votes pertaining to the shares actually represented. CODE OF COMMERCE art. 76.

made available to the public generally. Payment of capital subscriptions usually can be made in cash or kind, but contributions in kind may be subjected to careful scrutiny. In some countries, it is the practice to require appraisal by experts to determine the proper value of the contribution.<sup>16</sup>

It is in the area of corporate management where the peculiarities of the civil law corporation are most recognizable in their differences from the American corporation concept. What we in this country would normally regard as decisions taken by the Board of Directors may in civil law countries be acted upon only by the stockholders in meetings. Under the civil law concept, directors are the officers—they run the corporation in its day-to-day activities. They are elected and may meet in much the same manner as in this country. Usually they will act among themselves to name from their membership the chairman of the board, or the managing director as he may be called, who under our concept would be the president.<sup>17</sup> The American partner will be called upon, and perhaps be hard-pressed, to understand that the question, “Will we be able to control the Board of Directors?” is usually not appropriate or applicable when referring to a foreign corporation. Voting control as we know it must be had in the stockholders’ meetings, for it is by this body that the administrative officers are elected, the dividends to be distributed are determined, and the acts of management are approved.

Directors may not have to be stockholders, nor in all countries must they be nationals, but it may be required that they be residents of the country.<sup>18</sup> Their duties usually are defined as representing and acting for the company, carrying on the operations which constitute its business and appointing employees and agents. Ordinarily each director will have authority to perform all acts necessary to the normal operation of the business, and each may act individually unless the organization agreement provides otherwise.<sup>19</sup> They may meet periodically to decide matters necessary to their functions as administrators, but always subject to the direct control

<sup>16</sup> In Belgium, a certified public accountant is required to report in particular on the description of each contribution in kind, on the methods of evaluation adopted and on the remuneration to be attributed in return for the contribution. CODE OF COMMERCE art. 29 *bis*.

<sup>17</sup> In West Germany, the functions of corporate operation are directed by three main bodies: the board of management (whose members are appointed by the board of directors); the board of directors (some of whose members are appointed by the shareholders and some by the employees); and by the shareholders’ meeting. AKTG, HANDELSGESETZBUCH [HGB] §§ 70, 86 & 105.

<sup>18</sup> In Venezuela, residents may be elected as alternate directors who may substitute for nonresident directors. See J. BENSON, REPORT ON VENEZUELAN TAX, LABOR AND CORPORATION LAW para. 858 (1964).

<sup>19</sup> In Italy, the direction of a corporation (*societa per azioni*) may be placed with a single director (*amministratore unico*). CIVIL CODE art. 2381.

and supreme authority of the stockholders and with the reservation that important policy decisions will be taken by the stockholders in meeting.

Stockholders' meetings usually are called by notice, but sometimes by publication in a newspaper, or by written notice. They usually are required to be held in the country where the head office is located. Proxies are permitted. Voting requirements and majorities may vary depending upon the question, and protection of minority stockholders is handled much the same as it is in common law countries.

One requirement of civil law corporations which American businessmen may find a bit strange and sometimes objectionable is that which calls for the publication, usually in an official gazette, of the corporation's annual financial statements, annual reports of the directors and of a statutory auditor<sup>20</sup> regarding financial and commercial operations, the minutes of the meetings of the stockholders and any amendments to the organization agreement.

Formation of a civil law corporation is relatively easy. The first step is the preparation of the organization agreement. This agreement will contain all provisions relating to the corporate name, principal office, purposes, duration, capital, shares, administration, management, shareholders' meetings, financial statements, dissolution and liquidation and any other provisions which the shareholders may find appropriate to include.

The next step is the subscription of the capital, which may be either public or private. If by private subscription, the incorporation is effected by written agreement to the articles, either in meeting or recorded by notary, signed by the organizers or on their behalf by an attorney-in-fact. When the documents of incorporation, including the minutes of the organization meeting, have been recorded and published,<sup>21</sup> the corporation is then ready to commence operations.

## 2. The Limited Liability Company

Usually we think of corporations as being associations of capital; the shareholders who contribute the capital to the association have little involvement with day-to-day corporate operations. Other types of business organizations, on the other hand, may be thought of as more personally associated with the contributors of capital;

<sup>20</sup> Most civil law countries require by statute the appointment of an auditor or board of auditors whose primary function is to inform the shareholders periodically of the financial condition of the company. In some countries, the authority of the auditor is quite extensive, including the right to call shareholder meetings in the event of the failure to do so by the directors. CIVIL CODE art. 2406 (Ital.).

<sup>21</sup> Filing is with a national governmental agency, usually the ministry serving commerce or industry, and publication may be required in an official gazette.

it is usually the case that the contributors of capital also contribute a great deal of their time and efforts to the day-to-day operation and management of the enterprise. Somewhere in between lies the limited liability company, which involves both the personal and the capital association factors. It combines the benefits of a corporate form with the flexibility of operation of a partnership. It is a legal entity commonly available in most countries of the world; it is used usually for business firms which most closely resemble in character our closely- or family-held corporation. It may also be desirable for almost any small or medium-size enterprise.<sup>22</sup>

Shareholders are referred to as "partners" or "members" and usually only two are necessary to form the limited liability company. Foreign corporations or non-resident individuals<sup>23</sup> may be shareholders, and in many countries it is not necessary for the foreign corporate shareholder to register or qualify in the country in order to hold membership. Requirements as to maximum and minimum capitalization vary from country to country.

As in the case of corporations, the liability of each shareholder is limited to his subscription, but there is an important difference. All shareholders are jointly and severally liable for the total amount of capital not paid in at the time of organization and remaining unpaid. Usually, all capital must be subscribed, but the amount which must be paid in at the time of organization may vary from country to country.<sup>24</sup> Capital contributions in kind are permitted and in some countries may be valued informally,<sup>25</sup> but in others a formal appraisal may be required.<sup>26</sup>

The capital is divided into shares,<sup>27</sup> each share having the same fixed value; there is only one class of shares and there are no bearer

<sup>22</sup> For a discussion of limited liability companies, see Eder, *Limited Liability Firms Abroad*, 13 U. PITT. L. REV. 193 (1952). See generally 1 DOING BUSINESS ABROAD (H. Landau ed. 1962), for a discussion of limited liability companies.

<sup>23</sup> See, e.g., Brazil's DECREE-LAW No. 3,708 of Jan. 10, 1919, which governs limited liability companies in that country. In Belgium, however, only physical persons may be shareholders. CODE OF COMMERCE art. 119.

The author acknowledges the assistance of Dr. Joaquim Renato Correa Freire of the law firm of Davids, Freire, Caiuby & Fernandes, Sao Paulo, Brazil, for the Brazilian authorities cited in this article.

<sup>24</sup> In Brazil, while the entire amount of the capital must be subscribed, there appears to be no requirement as to the amount which must be paid in. DECREE-LAW No. 3,708 of Jan. 10, 1919. In Venezuela, all capital must be subscribed and at least 50% must be paid in. See J. BENSON, REPORT ON VENEZUELAN TAX, LABOR AND CORPORATION LAW para. 894 (1964). In Belgium, all capital must be subscribed and a minimum of 50,000 francs paid in. However, if authorized capital exceeds 50,000 francs, each share subscribed in cash must be at least 20% paid in. CODE OF COMMERCE art. 120.

<sup>25</sup> See DECREE-LAW No. 3,708 of Jan. 10, 1919 (Braz.).

<sup>26</sup> Cf. FRENCH COMPANY LAW OF JULY 24, 1966, art. 40, which requires formal appraisal by a Commission of Contributions appointed by the shareholders for that purpose. Shareholders are jointly and severally liable for a period of five years from organization for the value attributed.

<sup>27</sup> In some countries, a partner's holding may not be represented by shares. Each partner has a single share of the company which represents his proportional ownership in the company.

certificates. Normally, however, ownership is evidenced by the organization agreement, which is amended to reflect the transfer of ownership.<sup>28</sup> In any event, generally, ownership is not readily transferable.<sup>29</sup> One aspect of a limited liability company which is different from the corporation form and which may be of particular interest to American businessmen is that it is not required, usually, to publish minutes of meetings or annual financial statements.

Management of a limited liability company is carried out with much greater flexibility than is the case with a corporation. Regular, formal meetings of shareholders may be provided for (with provisions for proxies) but ordinarily they are neither required nor held. Some decisions of shareholders may be agreed to by correspondence — even by cable.

Responsibility for conduct of company business normally is placed with one or more managers rather than with a board of directors. Usually one or more of the managers must be a resident; and in some countries the managers must be shareholders.

The limited liability company is organized by execution and filing<sup>30</sup> of an organization agreement that may be in the form of a private instrument, and it need not be published. Normally the organization agreement will set forth the nationality of the founders, the amount of the capital, each member's share, how the capital is realized — *i.e.*, in cash or through contributions in kind — how the financial statements are to be prepared and distributed, rules for distribution of profits and a provision for an auditor, if desired or required by local law.<sup>31</sup> Additionally, it may be advisable to include in the organization agreement provisions specifying how management is to be carried out (especially who is to have management authority regarding particular matters), a description of duties of the managers, a provision for compensation of the managers, grounds for which a shareholder may be excluded, special voting requirements, if any, for particular purposes, how amendments to the agreement may be made, and any other matters which in the circumstances may be important to the protection of the investment.

<sup>28</sup> It is advisable, even though provided for by law, to include in the organization agreement a restriction on the transfer of shares, especially where such transfer may be occasioned by the death of an individual shareholder. In Belgium, transfers between living persons and upon death can be made only with the consent of 50% of shareholders holding three fourths of the capital, excluding the capital represented by the shares in question, unless the shares are transferred to the surviving spouse, to ascendants and descendants in direct line, to another shareholder, or to someone approved in the organization agreement. CODE OF COMMERCE art. 126. This kind of provision is particularly important where it is necessary to use nominee-shareholders.

<sup>29</sup> Ordinarily, a share can be transferred only with the consent of a majority of the shareholders. Sometimes the consent of all shareholders is required.

<sup>30</sup> See note 21 *supra*.

<sup>31</sup> The appointment of an independent auditor normally is not required but probably is desirable.

### 3. Which One?

Which of the corporate forms the partners to the joint venture choose is vitally important; whether the venture is successful in "getting off the ground" may depend in large measure on the corporate structure selected.

Both the corporation and the limited liability company have acceptable features; individual advantages of one may be preferable to those of the other in meeting the requirements assigned by the partners. Generally, however, it would appear that for most foreign joint venture endeavors, the limited liability company form will more nearly meet the tests of ease of organization, flexibility and economy of operation and privacy in its business affairs.

#### *C. This Matter of Control*

A matter which can become a serious problem, and one which can be most misunderstood in negotiations between the parties to a joint venture corporation, is that of control of the corporation, either in its executive management or day-to-day operation, or both. For some years now American business usually has had the luxury of having control of a foreign operation, either by ownership of a majority of the equity or by voting arrangements where a board of directors is controlled by the American company. The traditional reasons therefor have been quite logical: to exercise independence in the operation of the venture, to integrate the local operation into the world-wide operation of the American corporation with minimum influence by local ownership, and to obtain as much of the profits from the business operation as possible, all justified by the American investor on the basis that he has filled an investment void. Lately, however, local investors are demanding at least equal representation by ownership or otherwise, and, as indicated earlier, their governments are backing them up. Consequently, the American businessman is now forced to reappraise his philosophy and approach regarding foreign investments. Even so, American businessmen, in a great many instances, are still called upon to contribute a great deal more than the local partner is able in the circumstances to produce.

Usually the American partner will be the one who furnishes technical assistance and know-how needed in the manufacture of the products of the joint venture corporation. Often the U. S. company will be able to furnish the benefits of its marketing experience in the marketplaces around the world. Also it may be that the U. S. partner has a patent which is particularly attractive to the local partner. Another important consideration is the fact that the American partner might bring to the joint venture a world-wide reputation

which could foster an immediate market penetration and provide the impetus for fast growth in the market. And it is also possible that the American partner will be able to provide business and management consulting services.

More often than not, these are the reasons why the local partner wants to become associated with the American partner in the first place. And to the American businessman, these reasons justify his expecting final authority on various matters, if not the total operation, while at the same time splitting the profits on the basis of the investment contribution of each. The American partner, however, should not overlook equally important contributions which can be made by the local partner. As already indicated, his knowledge of local customs regarding acceptable marketing practices and consumer demands will be extremely valuable to the venture. As a matter of fact, the local partner's marketing organization may be entirely satisfactory for the distribution of the new company's products. Capable management may be furnished by many local partners. Contacts with governmental officials and practices, at all levels, may be beneficial. Accordingly, the local partner, as well, may be able to expect final authority in matters in which he is competent and, thus, complement the joinder — a desirable end.

But in these circumstances, and certainly in a 50-50 ownership joint venture corporation, the stage is set for the ever-present possibility of deadlock, regardless of the good faith both parties sincerely indicate and intend in the negotiations and establishment of the undertaking. Therefore, positive steps ought to be taken to express or provide a means of resolving differences, particularly where they vitally affect the purposes and objectives. Such measures should be discussed and adopted prior to organization, or at least during the early stages of operation, to avoid as much as possible the danger of deadlock resulting from the veto power accompanying evenly-divided ownership.

There are various means by which the problem can be handled. One is for the principal partners to own 49% each of the equity of the new company with the remaining 2% owned by a third, independent party who would be called upon to break any deadlock. Another is to state simply in the organization agreement that one or the other is to be responsible for the management. A more satisfactory arrangement is to provide in the organization agreement for the assignment to each partner of responsibilities and authority for various functions necessary to the operation of the venture. In this way successes and failures in each of the functions can be identified with the partner responsible.

Authority can also be granted by operating and management contracts. For example, it is not uncommon (or unreasonable) for the partner furnishing technical assistance to have control over the quality of the products manufactured, a factor vital to the objectives of the venture. The quality standards to be maintained will, of course, be established by the partners based on the requirements of the markets served. But to meet and maintain those standards, acceptable production practices and techniques may be necessary and ought to be established and supervised by the one furnishing the assistance. Obviously this kind of authority must be exercised wisely and with restraint.

Another way in which the matter can be handled is by arbitration. But an objection in principle to this kind of procedure is that the partners really are parties to a proceeding which is adversary in nature, while actually the carrying on of a joint venture operation contemplates something other than adversity. Sometimes, however, arbitration can be useful, and if the parties should decide that it would be desirable, the provision therefor should state that a court or body of a specified third country be used and that the matters be resolved according to the laws of that country. This would assure that the controversy would be heard before a neutral court or body of arbitrators.

#### CONCLUSION

For the American businessman, association with a local partner in a foreign joint venture corporation offers many advantages. An established local partner can furnish part of the capital, thus decreasing the amount of the investment required of the American investor; he can provide knowledge of the local market, distribution facilities and qualified management. In recent years, American businesses of many kinds have discovered this form of investment a satisfactory way to enter and expand activities in foreign markets. The lack of complete financial control has not appeared to be a serious problem to either partner. Joinder with a local partner also helps to meet requirements of local governments and to support the policies of our own national government.

For the American lawyer, it is a challenging and exciting experience to join together two different legal systems, taking desirable features from each for use in achieving for his businessman client a workable framework for, hopefully, a profitable and long-lasting undertaking.