Joint Ventures: Control and Minority Protection (Ireland)

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A Note on the management, control and protection of minorities in joint ventures in Ireland.

This Note looks at how joint venture companies (JVCs) in Ireland are managed and controlled. It assumes that the parties have examined the various joint venture structuring options in Ireland (see *Practice Note, Joint Ventures (Ireland): Choice of Structure*) and have settled on a joint venture company (see *Practice Note, Joint Ventures (Ireland): Choice of Structure : Joint Venture Company*).

The Note first considers the management of the JVC and how the board might be constituted, its role and how much authority might be delegated to the management team. It then addresses the setting up of board committees and the position of the directors of JVCs. In particular, it looks at the duties they owe, the competing interests of nominee directors, and the provision of confidential information by directors of JVCs to their appointors.

In a 50:50 joint venture, deadlock often arises. The Note looks at mechanisms to get around such difficulties. It also considers the position of minority shareholders and how best to protect them.

It also examines how the shareholders' agreement or constitution of a JVC should deal with the above issues and which document is best for a particular provision. Finally, the Note briefly looks at how to terminate a JVC arrangement; in particular, the intellectual property issues that then frequently arise.

Managing the JVC

An important function of the shareholders' agreement and the constitution of the JVC is to reflect the agreed arrangements for managing the JVC. These will be crucial to the success of the venture. It will always be necessary to tailor the management structure of the JVC to deal with requirements of each individual set of circumstances. Different considerations will apply, for example, in a 50:50 joint venture where equality of representation and voting rights are often deliberately engineered, compared with a joint venture involving minority shareholders who require special protection. Interests need to be balanced:

- Those managing the JVC will generally wish to run its business in an autonomous fashion with the minimum of outside interference.
- The joint venture parties will wish to ensure that they retain appropriate safeguards, or "reserved rights" over certain major or strategic decisions, to protect their investment, while often agreeing for day-to-day management and less important decisions to be taken by the management team.

For discussion on the shareholders' agreement and the constitution of the JVC, see *Shareholders' Agreement or Constitution?*.

Board of the JVC

How should the board of the JVC be constituted? Is it to have an active executive role or is it essentially a supervisory body consisting of representatives of the shareholders, reviewing overall strategy and important decisions?

If it has a supervisory role:

- Where two parties are contributing equally to the joint venture and take equal proportions of equity, they will expect to be able to nominate equal numbers of directors, thereby creating equality at board level (but with in-built potential for deadlock). Usually, even the initial quorum for board meetings will require equal representation by nominees.
- Where one party is making a significantly greater contribution than other parties, that party will seek the final say on matters to be decided at board meetings either through the right:
    - to appoint a chairperson with a casting vote;
    - to appoint a majority of directors; or
    - for its nominee directors to have weighted voting rights.
- Directors appointed by each party should, broadly, have comparable status within the respective parent organisations (or where this might not be appropriate if, for example, one party is a much larger institution, sufficient status to bind the nominating shareholder).

- It will usually be appropriate to establish a management committee for the day-to-day executive team.

As to decision making, much will depend on the scale of the joint venture, the seniority of the directors and the management reporting lines envisaged by the shareholders. Particularly in the case of larger joint ventures, there will be certain matters which the joint venture parties regard as central to protecting the value of their investment (for example, some of the items listed under *Protecting a Minority Shareholder*). It is not uncommon to see these matters withdrawn from the authority of the board of the JVC and made subject to shareholder approval, either through the shareholders' agreement or (as is necessary in some jurisdictions) through the JVC's constitution. In this way, the joint venturers can review such matters at their corporate level and will not have to rely simply on their appointees making the right decision.

Executive Management

How much authority should be delegated to the day-to-day management team of the JVC? While practical internal guidelines can usually be devised for any corporate structure, legal issues can arise:

- In Irish law, the main board may establish committees to assist in carrying out the board's oversight role, unless the constitution provides otherwise. Such committees must be made up in whole or in part of members of the main board (*section 160(9), Companies Act 2014* (CA 2014)). However, irrespective of any delegation, the main board will retain legal responsibility for the overall management of the JVC. It is important to ensure that clear written terms of reference setting out the responsibility of each committee are put in place.
- If the management team is formally a management board (as in some continental European corporate models with "two-tier" boards), statutory rights and responsibilities under the laws of the relevant country will need to be considered. This formal two-tier approach is relatively uncommon in Ireland.
- In some EU jurisdictions, the chief executive (or equivalent) will have considerable formal authority to bind the JVC in its relations with third parties. This is also the case in Ireland, where the managing director (MD) (also often called the chief executive officer (CEO)) will typically have ostensible authority to bind the JVC. Section 159(1) of the CA 2014 allows a managing director (by whatever name called) to be appointed by the board and confer on the MD "any of the powers exercisable by them upon such terms and conditions and with such restrictions as they may think fit." Subject to very limited exceptions, the board of a company (or MD or CEO) dealing with third parties on behalf of the JVC "shall each be deemed to have authority to exercise any power of the company and to authorise others to do so" (*section 40(1), CA 2014*). Further reassurance is provided by section 40(9) of the CA 2014, which states that in determining any question as to whether a person had ostensible authority to exercise any of a company's powers in a given case, no reference may be made to the company's constitution.

It is not essential that management rights and responsibilities must correspond to equity ownership. One joint venture party may be given greater rights of management, for example, by having specific rights over appointments to particular management posts (such as the chief executive or finance director), or over decisions affecting particular technical or management areas. Alternatively, full day-to-day responsibility may be vested in one party under a management contract with the JVC.

At a practical level, it is important that the joint venturers and JVC management are each clear as to how their relationship is to be conducted. The shareholders' agreement should provide the framework for this ongoing relationship, for example:

- Which decisions are to be referred to the joint venturers at corporate level?
- What information and management reports are to be provided and when?
- How are budgets and business plans to be approved?

Duties of Directors

The CA 2014 sets out the codified directors' duties in a non-exhaustive list of pre-existing common law rules and equitable principles (although regard still needs to be had to those rules and principles when interpreting and applying the codified duties).

The duties are set out in section 228(1) of the CA 2014. They are:

- To act in good faith and in what the director considers to be in the best interests of the company.
- To act honestly and responsibly in relation to the conduct of the affairs of the company.
- To act in accordance with the company's constitution and exercise their powers only for the purposes permitted by law.
- Not to use the company's property, information or opportunities for their own or anybody else's business.
- Not to restrict their power to exercise an independent judgement.
- To avoid conflicts of interest between the director’s duties to the company and the director’s other (including personal) interests.
- To exercise reasonable care, skill and diligence.
- To have regard to the interests of employees in general and of its members.

In certain circumstances, these duties may be modified by the company's constitution or by a resolution of the company in general meeting, or infringement may be avoided if authorised by the "non-interested" directors. It is also prudent for a nominee director’s protection to include explicit recognition of particular aspects in the JV shareholders' agreement, for example, by providing consent to the provision of JVC information by a nominee director to the third-party appointer. See further *Practice Note, Directors' Fiduciary Duties Under the Companies Act 2014 (Ireland)*.

Section 227 of the CA 2014 confirms that the duties are enforceable only by the company. Unlike the UK, Ireland does not provide a statutory right for a shareholder to bring a "derivative claim" in the name of the company against a director (and any relevant third party) as a result of a director's breach of duty, but there is a common law right to bring a derivative claim which may, in some circumstances, provide a potential legal remedy for an aggrieved minority shareholder. For more on this, see *Practice Note, Shareholder Remedies: Derivative Actions (Ireland)*. Further, where a shareholders' agreement confers explicit rights on a shareholder, it may be possible also for the shareholder to enforce those rights on behalf of the company.

Competing Interests of a Nominee Director

Inherent in a joint venture is the risk that an appointed director may face a conflict between the interests of the JVC and the interests of their appointor. Nominee directors will usually be under a duty to exercise their powers for the benefit of the members of the JVC as a whole and not for the particular shareholder who appointed them.

In Ireland, the term "nominee director" does not have a statutory definition and nominee directors owe the same duties to the company as the other types of directors. However, their position is formally recognised in section 228(3) of the CA 2014, which provides that without prejudice to the directors' duty under section 228(1)(a) of the CA 2014 (to act in good faith in what the director considers to be the interests of the company), a director of a company may have regard to the interests of a particular member of the company in certain circumstances. These circumstances are where the director has been appointed or nominated for appointment by that member, being a member who has an entitlement to so appoint or nominate under the company's constitution or a shareholders' agreement (*section 228(4), CA 2014*).

Therefore, despite section 228(3) to (4) of the CA 2014, nominee directors can, in practice, be in a difficult position as although their primary duty is to the company, they must also consider the interests of their appointing shareholder or other third-party appointor (in particular, where the nominee may also be a director in the third-party appointer group).

Therefore, in Ireland a nominee director can have regard to the interests of the party appointing them. An example of this which pre-dated section 228(3) to (4) is the High Court decision of Barron J in *Irish Press plc v Ingersoll Irish Publications (unreported), 15 December 1993* where he noted the difficult position that a nominee director will be in if they disagree with the view of their third-party appointor. While they must act in the best interests of the company, they also have a duty to the person appointing them. Barron J pointed out that "acting in the interests of the company is no more than acting in the interests of all its shareholders" and therefore:

"there is nothing wrong with the appointing body or party having a view as to where the interests of the company lie and ensuring that its nominees follow that direction provided that in so doing they are not seeking to damage anyone else's interest in the company."
The approach of English courts to nominee directors is set out in *Boulting v Association of Cinematograph etc Technicians [1963] 2 QB 606* in which Lord Denning MR (dissenting) said that he saw nothing wrong with nominee directors representing the interests of their appointor "so long as the director is left free to exercise his best judgment in the interests of the company which he serves."

Lord Denning said that if the nominee is appointed on the basis "that he is bound to act in the affairs of the company in accordance with the directions of his patron, it is beyond doubt unlawful" (*Kregor v Hollins, (1913) 109 LT 225*). Further, "if he agrees to subordinate the interests of the company to the interests of his patron, it is conduct oppressive to the other shareholders for which the patron can be brought to book" (*Meyer v Scottish Co-operative Wholesale Society Ltd [1959] AC 324*). The decisions of English courts are persuasive in Ireland with both jurisdictions being common law and many legislative provisions quite similar. For more on this, see *Practice Note, The relationship between English and Irish law*.

For more detailed commentary on this issue, see *Practice Note, Types of Director (Ireland): Nominee Director*.

In the UK, where nominees had put their duty to the holding company before their duty to the subsidiary, minority shareholders were able to bring a successful action for oppression under section 210 of Companies Act 1948, a predecessor of section 994 of the UK Companies Act 2006 (*Scottish Co-operative Wholesale Society v Meyer [1959] AC 324*). This approach was endorsed in Ireland by Barron J in *Irish Press plc v Ingersoll Irish Publications Ltd* (15 December 1993).

In practice, an appointee can usually exercise their powers in accordance with the wishes of the appointing shareholder provided that, in exercising those powers, the appointee does not act blindly but considers the interests of the members of the JVC as a whole. However, difficult situations can occur. As a shareholder is not generally under a duty to take wider interests into account but can act in its own interests, it may be preferable for areas of conflict to be dealt with at shareholder rather than board level.

Concern has been expressed in the UK as to the application of the general duty of directors to avoid conflicts of interests (section 175 of the CA 2006; equivalent to section 228(1)(f) of the CA 2014) in relation to directors who sit on more than one board. There is a view in the UK that a board authorisation of another directorship would "frank" any conflict that later arose as a result. However, a general authorisation may not be wide enough to cover the conflict in question, and a director may be unable to disclose details to the company when they arise (for example, for reasons of confidentiality). In these circumstances, directors should seek independent legal advice.

To overcome any such problems, companies should provide for these issues in their constitutions (or in shareholders' agreements). For example, the constitution could state that directors may hold additional directorships and do not need to disclose confidential information obtained through those other directorships.

GC100 has published various materials relating to the UK's section 175 of the CA 2006 (which are worth considering for Irish companies, once suitably adapted). These include:

- A guidance paper (*GC100: Guidance paper on directors' conflicts of interest (January 2008)*).
- A questionnaire for directors to help them to identify conflicts of interest for subsequent authorisation by the company's board (*GC100: Guidance on directors' conflicts of interest authorisation process: Questionnaire for directors (August 2008)*).

Confidential Information

In Ireland, fiduciary duties include a duty not to use confidential information obtained by a director otherwise than for the benefit of the company: *Spring Grove Services (Ireland) Ltd v O'Callaghan [2000] IEHC 62*. In this case, Herbert J noted:

"... these obligations commonly referred to as, 'fiduciary duties', include a duty not to compete with the company, a duty to act in the best interests the company and a duty not to use confidential information obtained as such director otherwise and for the benefit of the company."

Motive is irrelevant. This can be seen from Lord Russell's judgment in *Regal Hastings*, cited with approval by Clarke J in *Allied Irish Bank plc and others v Diamond and others [2011] IEHC 505*:

"The rule of equity which insists on those, who by use of a fiduciary position make a profit, being liable to account for that profit, in no way depends on fraud, or absence of bona fides; or upon such questions or considerations as whether the profit would or should otherwise have gone to the [company], or whether the [director] was under a duty to obtain the source of the profit for the [company], or whether he took a risk or acted as he did for the benefit of the [company] or whether the [company] has in fact been damaged or benefited by his action. The liability arises from the mere fact of a profit having, in the stated circumstances, been made. The [director], however honest and well-intentioned, cannot escape the risk of being called upon to account."

A particular problem can be the release of confidential information. If a representative director is to be free to release confidential information to colleagues in the "parent" company, this should generally be made clear in the legal agreements and appropriate confidentiality obligations should be imposed on the "parent" (see *Practice Note, Directors' duties and shadow directors: joint ventures* (UK)).

Deadlock

What happens if the parties to the JVC or their appointed JVC directors cannot agree? *Deadlock* can arise either in a 50:50 joint venture where the shareholders' appointed directors take opposing views or where a director appointed by a minority shareholder has exercised a right of veto. Similarly, deadlock can arise at shareholder level in relation to matters which have been withdrawn from the authority of the board and require shareholder approval. The lawyer is frequently asked, "How should we cater for such a deadlock?". There is no easy solution. Several ways of approaching this situation are:

- Chairperson's casting vote for a deadlock at board level.
- Outsider's swing vote.
- Mediator, expert or arbitration.
- Reference to parties' chairperson or chief executive.

Other methods inevitably involve termination of the joint venture or at least the "exit" of one party (see *Practice Note, Termination joint ventures (Ireland)*).

Chairperson's Casting Vote

Giving a chair of the board of directors a casting vote will unlock deadlock at board level, but it will do so by giving one party an advantage which negates the concept of joint control and is, therefore, not usually acceptable. One possibility to mitigate this effect in a 50:50 joint venture is for the appointment of the chair of the board (with a casting vote) to be on a rotating basis between the parties.

Outsider's Swing Vote

Giving an independent third party the balance of power as an additional non-executive director will unlock deadlock at board level. The attractiveness of this will depend on whether a suitable person with appropriate business expertise can be found and it may well be difficult for the shareholders to find a candidate who is acceptable to both. It may be an appropriate method in a venture where prompt and certain decisions must be taken to run the business.

Mediator, Expert or Arbitration

Referring matters in dispute to an agreed expert or arbitrator will unlock deadlock at both board and shareholder level. The expert or arbitrator may be appointed by agreement of the parties or by an independent body, such as the president of the Chartered Institute of Arbitrators, depending on the nature of the dispute. However, leaving matters to be decided by third parties in this way is usually inappropriate for business decisions. The arbitrator will generally not have sufficient knowledge of the business and it will only be a short-term solution which is unlikely to resolve more basic differences in approach between the parties, perhaps relating to future funding or the strategic direction of the business. However, there may be a role for a mediation structure in the dispute resolution procedures of some international joint ventures involving different cultures, where the function of the mediator is not to determine the dispute but to assist the parties to do so.

Reference to Parties' Chairperson or Chief Executive

A residual, but often the most practical, method is for unresolved deadlock issues to be referred to the chairperson or chief executive of each parent shareholder. It may well be that the chairpersons themselves are unable to agree. However, the main advantage of this method is that the threat of unresolved issues being referred to the highest authority within the joint venturers' organisations will concentrate the minds of the management of the JVC to find a solution for themselves. In some ventures, provision may be made for review by an intermediate executive panel appointed by the parties before further escalation within the parent groups. These methods carry the merit of allowing for a greater degree of independence and for greater shareholder strategic perspectives to be taken into consideration.

None of these mechanisms provides an ideal solution. However, some consider that a company with the potential for deadlock deliberately built into the structure provides in itself the strongest incentive for encouraging agreement and a common policy; the dire consequences of an insoluble deadlock generally ensure that a sensible compromise is reached. Where an insoluble deadlock does arise, it will rarely be an option to continue with the joint venture and the parties should decide what will happen in those circumstances.

In practice, the deadlock provisions in the shareholders' agreement will usually serve as a backdrop to a commercial arrangement to be negotiated between the parties for terminating the joint venture. Even if they are not operated in full, such provisions are nevertheless important since they may materially affect a party's tactical position if these circumstances arise.

The two main options to consider for terminating the joint venture are:

- Transfer of shares.
- Voluntary liquidation.

See *Transfer and Termination*.

Protecting a Minority Shareholder

In the absence of express contractual rights, a minority shareholder's rights will depend on relevant corporate legislation; in Ireland, for example, the CA 2014, the applicable provisions of which depend on the size of the minority shareholder's shareholding.

A special resolution is a resolution which for it to pass needs not less than 75% of the votes cast by the members of the company concerned as, being entitled to do so, vote in person or by proxy at a general meeting of it (*section 191(2), CA 2014*). Therefore, if a minority shareholder holds more than 25% of the voting share capital in a JVC, it will have the power to block special resolutions, which are required under the CA 2014 to:

- Reduce share capital.
- Disapply the statutory pre-emption rights on new share issues.
- Approve the restriction of a director's independent judgement.
- Release a director from a conflict of interest.
- Alter the constitution.

- Change the name of the JVC.
- Commence a voluntary liquidation.

However, a minority shareholder cannot block ordinary resolutions, which are decided by a simple majority vote (*section 191(1), CA 2014*). Ordinary resolutions cover, for example, resolutions to:

- Appoint and dismiss directors.
- Authorise the directors to allot shares.
- Declare dividends.
- Control the exercise of borrowing powers.

A minority shareholder may, in extreme circumstances, be able to apply to the court on the basis of conduct which amounts to oppression or in disregard of their interests as a member under section 212 of the CA 2014, but the remedy is expensive, time consuming and discretionary in nature (the relief ordered by the court can even include variation of the company's constitution). The outcome is therefore often uncertain and rarely a satisfactory protection. Accordingly, a minority shareholder is usually advised to seek express contractual protections beyond those afforded by statute (see *Standard Documents, Minority shareholder protection* and *Joint venture shareholders' agreement: majority and minority shareholder: Schedule 1* (UK)).

A minority shareholder will often seek a right to appoint a director supported, perhaps, by a requirement that its representative is a necessary part of a *quorum*. However, non-attendance may not be used as a perpetual block (*section 179, CA 2014* and the English case of *Re Opera Photographic Ltd [1989] 1 WLR 634*) and shareholders' agreements will usually provide for a revised quorum after an agreed period of non-attendance.

A party with a shareholding more than, for example, 30%, might in practice also seek veto rights over certain major matters, such as:

- Changes in the JVC's constitution.
- Issues of shares, including grant of share options.
- Capital expenditure or contract commitments in excess of pre-agreed limits.
- Borrowing limits.
- Major acquisitions or disposals.
- Significant changes in the nature of the business of the JVC.
- Dividend distribution below an agreed minimum level.
- Appointment and dismissal of key personnel and directors.
- Material dealings with intellectual property.
- Dealings between the JVC and any of its shareholders (except arm's length dealings in the ordinary course of business).

Having negotiated the matters over which the minority shareholder is to have a right of veto, it is necessary to decide whether these matters should be "entrenched" at board or shareholder level (whether the unanimous or a "super-majority" approval of the directors of the JVC (including the minority shareholder's appointee) will be required or whether the shareholders (including the minority shareholder) will be granted class rights or weighted voting rights). As to the question of whether these matters should be covered contractually in the shareholders' agreement or in the constitution, see *Shareholders' Agreement or Constitution?*.

An additional protection is for a minority shareholder to establish a *put option*, whereby the majority shareholder can be obliged to purchase the shares of the minority shareholder, often in accordance with a predetermined price formula and at a defined stage. This will provide an opportunity for a minority shareholder to review its position; it prevents it being "locked in" if the joint venture is unsuccessful from its viewpoint.

A minority shareholder should generally also seek a *tag along right*, under which it can require a majority shareholder to include the minority's stake (on the same terms) in any sale it makes to a third party (see *Standard Clause, Tag along rights on a change of control: articles of association joint ventures* (UK)). Adding provisions to give minority shareholders rights through internal shareholder offer-round on share sale and pre-emption rights on new share issues can also be helpful to protect minorities.

Shareholders' Agreement or Constitution?

The shareholders' agreement and the constitution contain the important legal rules governing the venturers' relationship in the JVC. What provisions should appear in each document? Drafting tastes vary. Additionally, there are substantive differences in the analysis of the two documents: the shareholders' agreement is governed by the ordinary rules of contract, while the constitution is a creature of company law, regulated in material respects by statute.

The most obvious distinction between the two is that the constitution can be amended from time to time by shareholders holding 75% or more of the voting rights.

The constitution should generally include:

- Rights to appoint and remove directors.
- Provisions dealing with the authorisation and management of directors' conflicts of interest.
- Quorum provisions, both at director and shareholder level.
- Procedures for shareholder meetings.
- Pre-emption provisions on share issues.
- (Possibly) pre-emption provisions on transfers of shares.
- Division of shares into separate "classes" to which the parties' respective rights can attach.
- Board chair's casting vote (or its exclusion).
- Appointment of *alternate directors*, flexible provisions for resolutions by "agreement" and notices.

The constitution can be amended by shareholders holding 75% or more of voting rights. Minority shareholders may therefore wish to protect certain rights relating to matters such as the appointment of directors and pre-emption.

If so, it may be appropriate to create specific *class rights*. This is usually done by creating new classes of shares, for example, "A" and "B" shares, and attaching the specific rights to the "A" and "B" shares held by the shareholders respectively. However, varying these rights under Irish law is not straightforward and there are detailed rules setting out how they can be varied in section 88 of the CA 2014. Depending on the type of rights in question, the variation will be either be determined solely by the relevant constitutional provision or by requiring the consent of 75% of the members of that class.

Alternatively, a minority shareholder could insist that such rights are incorporated in a shareholders' agreement. On normal contractual principles, the agreement cannot be varied without the consent of all parties, unless the shareholders' agreement provides for variation by a majority of less than all parties. However, some argue that inclusion of provisions such as veto and pre-emption rights in the constitution creates stronger rights, including enforceability directly against the JVC and the directors of the JVC (who may not be parties to the shareholders' agreement). Restrictions in the constitution will also be in a public document, available to third parties dealing with the JVC which means that it prevents a third party from disregarding the restrictions because they are deemed to be on notice of them.

An advantage of incorporating rights in a shareholders' agreement in Ireland is that it is not a public document. Ireland does not have a direct equivalent to sections 29 and 30 of the UK CA 2006, which provide that certain agreements made by all the members of a company must be forwarded to the UK Registrar of Companies within 15 days of being made.However, section 33 of the CA 2014 requires notification to the CRO of any document which amends the company's constitution. This has a bearing on the use of "supremacy" clauses which impose the provision of a shareholders' agreement where a conflict arises with the provisions of the constitution. The solution often chosen is to have the shareholders agree in the shareholders' agreement to procure that the company will act in accordance with the terms of the shareholders' agreement where the constitution conflicts with the agreement.

The shareholders' agreement can set out personal rights between the members, dictating how they will exercise their voting rights in certain circumstances or what level of majority is agreed to be necessary for certain decisions. However, the same provisions relating to members' personal rights in the constitution could be invalid as fettering the company's statutory powers (following the House of Lords decision *Russell v Northern Bank Development Corp [1992] 1 WLR 588*; see also *Article, Enforceability of restrictions in shareholders' agreements, PLC Magazine, 1992*). In the UK, shareholders can entrench provisions in the constitution in such a way that such provisions can only be amended or repealed if conditions are met which are more restrictive than for a special resolution (*section 22, UK CA 2006*). This enables UK joint venture parties to overcome some of the difficulties of *Russell v Northern Bank Development Corp* and may be used to entrench some minority rights more fully in the constitution without formally creating "class" rights. Unfortunately, there is no similar provision in the Irish CA 2014. Given the persuasive nature of decisions of the English courts and as Ireland does not have an equivalent of section 22 of the UK CA 2006, the decision in *Russell* should always be borne in mind in framing such rights in a shareholders' agreement.

The shareholders' agreement will normally be expressed to be the prevailing contract as between the parties themselves in the event of any conflict with the constitution. The remedy of an injunction will usually be available under Irish law to ensure that each party takes the necessary voting action when voting as a shareholder of the JVC to give effect to its terms (see the Irish case of *TGM v Al Babtain Trading and others [1982] ILRM 349* and the English cases of .*Greenwell v Porter [1902] 1 Ch 530* and *Puddephat v Leigh [1916] 1 Ch 200*).

It can be cumbersome, as a drafting matter, to try and make the detailed pre-emption provisions the same in both documents. It may be easier for the constitution to prohibit transfers except with consent and for the shareholders' agreement to specify the detailed procedures governing transfers and the circumstances in which consent is, or must be, given.

In favour of a third party dealing with the JVC in good faith, the power of the directors to bind the JVC (or authorise others to do so) is deemed to be free of any limitation under the JVC's constitution (*section 40, CA 2014*).

A question that often arises is whether the JVC itself should be a party to the shareholders' agreement. If a party, the JVC can be made subject to direct restrictions or procedures. In most situations, though, the joint venture parents may prefer their contractual relations not to involve the JVC, so that they can take any wider issues into account without the consent of the JVC management being required in the event of disputes or variations. In such circumstances, it is usual for the parties to commit to procuring that the JVC will be managed in accordance with the terms of the shareholders' agreement. If the JVC is made party to a shareholders' agreement which contains terms that fetter the JVC's exercise of its statutory powers, those terms will be unenforceable against the JVC but may be enforceable as between the other parties if the restriction on the JVC can be severed (*Russell v Northern Bank Development Corporation*). It is more common for the JVC to be a party in a multi-shareholder joint venture where each of the parties is in a minority position.

Transfer and Termination

Although the parties may be reluctant at the inception of the joint venture to discuss the possibility of its termination, a well-prepared joint venture should provide for that possibility. There are three basic situations where there is a 50:50 JVC:

- One party simply decides to "get out" by selling its shares.
- A fundamental management deadlock or breakdown has been reached.
- An event occurs (for example, default, liquidation, change of control, completion of project or loss of licence) which the parties expressly agree should give rise to termination or a party's right to institute a termination procedure.

Transfer of Shares

Parties entering into a joint venture do not normally expect either party to have the right to dispose freely of its shareholding to a third party, since the result could be that two incompatible parties would be thrown together. Therefore, it is common for joint ventures to adopt legal arrangements restricting free transferability, typically providing that:

- The transfer of shares without consent of the other parties to the joint venture is either:
    - forbidden indefinitely (which is not acceptable in some jurisdictions);
    - prohibited for a stated period; or
    - made subject to board approval.
- The transferability of the shares is not prohibited as such, but the other shareholder is given a pre-emption right (a right of first refusal).

It is common, whatever rules govern the transferability of the shares, to permit only the disposal of a party's entire holding so that small "split" shareholdings do not arise. Other points on transfer which should be considered at the outset are:

- Should intra-group transfers be permitted?
- Should transfers to a third party (without consent) be permitted? If not, should a party have a right to call for liquidation if consent to a transfer to a third party is refused?
- Is an initial period during which transfers are prohibited appropriate to establish the parties' commitment to the venture and to allow the business of the JVC to get established?
- Is it practicable to require a third-party purchaser to be identified (that is, for a sale to be a "real" possibility), before the pre-emption right is offered to the other party? If not, should the other party be given a "second bite at the cherry" if, not having exercised its pre-emption right at the outset, it wishes to do so when the identity of the chosen third-party purchaser actually emerges?
- Should the other party have a right to call for a "fair price" to be fixed by an expert? If so, what criteria (if any) should be set down for fixing the price? Perhaps the parties will set down an earnings basis or a net asset test; alternatively, they may specify that the expert should have regard to all factors the expert deems relevant. Should the price per share be fixed irrespective of any premium or discount attributable to the size of holding being transferred?
- Is it likely that anti-trust or other regulatory issues will affect any transfer?
- Will any change of control consequences for key business contracts arise as a result of the transfer?
- Will any employment law or pensions issues arise as a result of the transfer?
- Will any data protection issues arise as a result of the transfer?
- Should a transferee be required to take over any loans or guarantees made by the transferor for the benefit of the JVC?
- If a majority partner wishes to sell, should it be obliged to "bring along" (tag-along) the minority partner by procuring that the third-party offer extends also to the latter, or should a significant majority partner be entitled to drag along minority partners?
- A pre-emption provision should be drafted expressly to cover purported dealings in the beneficial interest (as well as the legal interest) in shares. In the absence of an express provision, references to "transfer" of shares only cover the legal interest (*Lyle & Scott v Scott's Trustees [1959] AC 763*).

These transfer provisions are important. Even if rarely followed in full in practice, they provide the background against which the joint venturers will often negotiate an agreed arrangement and can therefore be important in establishing the strength of a party's negotiating position (see *Practice Note, Termination: Joint Ventures (Ireland)*).

Change of Control

No transfer of shares in the JVC is involved where one of the participants is acquired by someone else or control of that party changes: the transfer of ownership occurs higher up than the JVC. A change in control can, however, bring about an unacceptable situation in which the other party is unwilling to continue the collaboration with a party under that new ownership. In such circumstances, it may be desirable to give the other party a right to acquire the "changed" party's holding in the JVC or to dispose of its own holding. A clear definition of "control" for this purpose is necessary. For example, see English case of *Philip Morris Products v Rothmans International [2001] EWCA Civ 1043*, where the High Court was required to apply the concepts of "acting in concert" and "control" by reference to the City Code on Takeovers and Mergers in the circumstances of a right to terminate a contract on a "change of control", as defined in the Code.

It is also important to consider other factors:

- Consider the possible implications of such a provision acting as a *poison pill* against an unwelcome third party predator. In some circumstances, directors may not be acting in a way that promotes the success of the company for the benefit of its shareholders by including such a provision, particularly if the interest in the JVC is a significant part of that party's overall assets and that party is a listed company. Even if directors are acting in accordance with their duties, most forms of poison pills are not likely to be permitted for Irish listed companies which are subject to the *Irish Takeover Rules*, where a takeover is imminent and/or where the directors are required to exercise discretion in order for the poison pill to become operational. Rule 21.1 of the Irish Takeover Rules restricts target companies and/or their boards from taking defensive action which would prevent the target's shareholders from being given the opportunity to consider an offer to acquire their shares but the restriction is premised by the context of an imminent offer. Following the restructuring or merger into Ireland of a number of US corporations (where poison pills are a regular feature of corporate governance and M&A), certain of those companies have adopted poison pill structures as a matter of course while no offer/change of control is imminent and where the pills take effect automatically (without the need for directors to take action) in specified circumstances. The compatibility of such provisions with Irish company law has not yet been tested.
- Remember a board's duty to shareholders to ensure a full price on disposal (the valuation method for establishing a fair price can require careful structuring).
- The existence of joint ventures with "change of control" restrictions can have a practical effect on a party's freedom to move swiftly in relation to other ventures or corporate re-organisations.

Even more sensitive can be the question of whether pre-emption provisions on transfers should apply if a takeover bid for one party is made by the other joint venture party itself. The existence of such a pre-emption obligation can be a restrictive factor on a party's choice of action in the face of an unwelcome bid.

Termination

What should end the joint venture? It is important to identify at the outset any events which it is agreed will terminate the joint venture. If the joint venture is to terminate (otherwise than through a transfer of shares), the only practical legal step is for the JVC to go into liquidation and for its various assets to be sold (possibly by an auction to the shareholders themselves) and/or distributed. Events which will terminate the joint venture commonly include the following:

- The expiry of a definite term, for example, a certain number of years or the completion of a particular project for which the venture was formed.
- The insolvency of either party, although it may be more appropriate in such circumstances to grant the other party a *call option* to allow that party the opportunity to buy the insolvent party's shares in the JVC at fair value.

- A change of control of one of the joint venture parties; again, a call option will generally be appropriate.
- A material breach by the other party of the terms of the shareholders' agreement (or of a material ancillary agreement) which the "innocent" party elects to treat as a terminating event.
- The unwillingness of one party to continue to fund the operation of the JVC.

See *Practice Note, Termination: joint ventures (Ireland)* and *Standard Documents, Joint venture shareholders' agreement: 50:50 deadlocked joint ventures* and *Joint venture shareholders' agreement: majority and minority shareholder* (UK).

Intellectual Property

Particularly important in the event of a transfer of a party's shares, or the termination of the venture, is the need to establish what happens to the technology and other intellectual property rights of the JVC.

These points are often neglected at the outset: they should not be. Points to consider for the shareholders' agreement include:

- Should "foreground" rights, assigned initially by the venture parties to the JVC, be reassigned to them respectively on termination?
- Should the JVC be required to give up or change its corporate name or other trade marks if they incorporate "house" names or marks of an outgoing party?
- Should each party be free, on termination, to use and exploit any "arising" intellectual property generated during the course of the joint venture?
- On a transfer of shares, should the outgoing party lose the benefit of any licence of intellectual property from the JVC or only lose the benefit of rights generated in the future?

See *Practice Note, Intellectual property: joint ventures* (UK).

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