



- a joint venture is a strategic conglomerate between two or more otherwise unrelated enterprises or organizations engaging in a common undertaking with the hope of achieving a common goal

# Elements of a joint venture

- A contribution by the parties of money, property, effort, knowledge, skill or other asset to a common undertaking; a joint property interest in the subject matter of the venture; a right of mutual control or management of the enterprise; expectation of profit, or the presence of “adventure,” as it is sometimes called; a right to participate in the profits; most usually, limitation of the objective to a single undertaking or ad hoc enterprise

- oil and gas joint ventures are found to differ from business joint ventures in the sense that no joint profit is made. In this regard, however, researchers are divided with respect to the common goal of a joint venture. The common goal can be the pursuit of profit or the carrying out of particular operations together.
- The common goal depends on the type of industry in which the joint venture is utilized. Accordingly, for the oil and gas industry the common goal is to generate a product to be shared among the co-venturers.

- With respect to the element of “limitation of the objective to a single undertaking” (hereafter, single undertaking), this is an insignificant factor in the determination of a joint venture though such an element has its merits from philosophical or theoretical points of view. “Single undertaking” was utilized to distinguish joint venture from partnership on the basis of the duration of the business. While partnership was considered an association carrying on a general, continuous business until its dissolution, joint venture was viewed as an association carrying on a business over a limited period of time. This distinction made the single transaction or undertaking a necessary element of the definition of the joint venture. As a result, the definition of “single undertaking” was based on the time-scale of the project rather than on the objectives of the resulting association. Today, however, this is not the case. Joint ventures currently may last over 30 to 40 years, which is a very long period for a single project. Such a period of time may resemble, in reality, a continuous transaction. Furthermore, even if we accept the “single undertaking” element as a part of the definition of joint ventures, it is by no means an essential element, because there are a number of legal vehicles available for co-venturers to adopt. These vehicles include partnership or corporation. If co-venturers choose to incorporate their joint venture business the element of a single undertaking becomes irrelevant because the duration of a corporation is infinite. In addition, current joint ventures in the oil and gas industry usually last as long as the oil and gas reservoirs, which might be for a very long period

- The elements of joint ventures have developed over time, as have the definitions of the joint venture. Joint ventures during the period of the late fifties to the late seventies had a number of elements that, to some extent, differ from those of nowadays. For example, the FOC was responsible for carrying out exploration activities, and hence had the burden of final decisions, at its own risk and expense, until the occurrence of commercial discovery. Upon commercial discovery, an operating company, joint venture corporation or partnership, whose legal status depended on both the desire of its parties and the legislation involved, was established to carry out the exploitation and related operational activities. Generally, the governing body (consisting of partners or co-venturers) was evenly distributed between the parties to the joint venture (i.e. most of the joint ventures at the time were shared 50-50) or according to the capital contributed by each party. The chairman's post was reserved for the representative of the host state, while the FOC was entitled to appoint the executive manager. Finally, the production was divided between the FOC and host state in accordance with the capital contributed and the operating expenses incurred
- expenses incurred

The common elements of present-day joint ventures, on the other hand, can be summarized as: (1) the venture must be a particular commercial or business project, (2) there is a common ownership of assets and (3) co-venturers must have the ability to participate in management and control of the joint venture on an equal footing. As mentioned, joint ventures can be created through a number of legal vehicles, structures or frameworks. The literature provides three different structures under which a joint venture may be formed: Corporation, Partnership and Contractual Joint Ventures. Another possible classification is to categorize these vehicles into “incorporated joint ventures” and “unincorporated joint ventures.” Under the former, we find the corporation vehicle. This group is also called equity joint ventures. General Partnership or Limited Partnership and Contractual Joint Ventures, on the other hand, are referred to as unincorporated joint ventures or non-equity joint ventures. Regardless of the legal vehicle a joint venture might take, the dominant feature is that the joint venture is the creation of a contract: The law of joint ventures is not being made in the courts or the statute books but in the voluminous documents which order the complex exploration, development and financing activities that modern mining and energy operations involve. The child of convenience is assuming a character of its own

- The mineral and petroleum joint venture is an association of persons (natural or corporate) to engage in a common undertaking to generate a product to be shared among the participants. Management of the undertaking is divided: specified activities are to be performed by a designated person (the operator or manager) as agent for the participants; the power to determine certain matters is vested in a committee (the operating or management committee) upon which participants are represented and entitled to vote in accordance with their interests in the venture; and other matters are decided at the outset by the participants as terms of the association. The relationship among participants is both contractual and proprietary: the terms of the association are fixed by agreement, and property employed in the undertaking is held by the participants as tenants in common

# Contractual Joint venture

- So far, it has become clear that the most significant document for joint ventures is the contract between the co-venturers. In contractual joint ventures the relationship of the parties and the structure of the joint venture are documented and implemented in legal instruments called “Joint Operating Agreements,” (JOAs). Accordingly, there is no separate legal entity created; the legal framework for the operations of exploration, exploitation, and other activities is established by the JOA.

- JOAs are considered a necessary extension of a joint venture agreement. In other words, JOAs are the mechanism by which joint ventures are put into operation. Therefore, it is expected that either JOAs or different arrangements will be necessary to accommodate the various activities and relationships of an oil and gas business. Nonetheless, JOAs in general consist of an operator, charged with the responsibility of the exploration and development operations, supervised by an Operating Committee. The Operating Committee is composed of all co-venturers who have a vote proportionate to the size of their ownership. The Operating Committee protects the rights of the non-operating co-venturers against any possible loss resulting from the work of the Operator. Therefore, the role of both the operator and the Operating Committee is and should be unequivocally defined in the JOAs.
- In sum, the contractual joint ventures are based purely on a contract, i.e. JOAs.

- 1. Ownership
- Under the JOAs, host states and FOCs own both the equipment and facilities of the project, as well as the oil and gas productions. With regard to the latter, it is not uncommon to stipulate that each participant is to take its share in kind. Therefore, host states and FOCs also have direct ownership of the project and the
- production. This privilege is considered a fundamental advantage of contractual joint ventures when compared to joint venture corporations where shareholders do not have direct ownership.

- 2. Control
- There are two levels of control between which the mutual interest might be challenged if the JOAs are not precisely drafted. The power to control and manage the activities of a joint venture, except for the exploration and exploitation operations, is vested in the Operating Committee. On the other hand, the Operating
- Committee is entitled to and does supervise the work of the operator. The exploration and exploitation operations are, on the other hand, under the sole control of
- the operator

- 3. Risk
- JOAs usually provide that both parties, host states and FOCs, are jointly and severally liable for the obligations of the venture. Hence, there is an unlimited liability, which would be avoided if the joint venture were a limited liability company, for example. Other possible risks to the co-venturers are associated with the acts of the operator. As pointed out earlier, the operator can enter into binding
- agreements, usually permissible in advance by the JOAs, and carry out operations without obtaining the non-operating co-venturers' approval. Hence, unless other co-venturers can prove negligence of the Operator, they will all share the losses and damage caused by the acts of the Operator

# Joint Venture Corporation

- The second available legal vehicle under which a joint venture may be formed
- is the corporation. The legal affairs of incorporated joint ventures are governed
- by the corporation law of the relevant state.
- 1. Ownership
- When co-venturers elect to use this legal vehicle, their ownership will be vested in the shares of the corporation and is in proportion to the capital contributed by each co-venturer. The restriction on the maximum ownership to which FOCs are entitled is conditional on both the relevant legislation and any exemption obtained from the government of the host states. The implication here is that the
- host states, as well as the FOCs, will be entitled only to receive the proceeds of the
- oil and gas sales and have no direct access to the crude oil and gas production.
- The host state and the FOCs are the shareholders of the separate legal entity (i.e.
- joint venture corporation) that independently owns the oil and gas production.
- This might not suit the host states that prefer direct access to and ownership of the backbone of their economy

## 2. Control

- The control and management of joint venture operations and affairs are vested in both the Board of Directors (BOD) and the executive management of the corporation. The BOD is responsible for setting the overall policies and strategies as well as approving major decisions. The management of the corporation is responsible for the day-to-day operations and works under the supervision of the BOD. Hence, there is no direct control by the shareholders (host states and FOCs), though they exercise indirect control through the appointment of the members of the BOD who are, in turn, responsible for appointing the executive management. The voting on the appointment of the BOD, including the chairman and the executive general manager, is usually in accordance with the percentage of ownership of each shareholder. In partnership joint ventures and contractual joint ventures, however, control and management are directly exercised by the partners or co-venturers which might give these two vehicles an advantage over the joint venture corporation. Also, incorporating the joint venture would necessitate the integration of both the NOC and FOC. This is the major disadvantage of JVCs because the host state or its NOC and the FOC prefer to maintain their original identity. This is why contractual joint ventures and partnerships are preferred

- 3. Risk
- By virtue of incorporating the joint venture, the shareholders, host states and
- FOCs will have a limited liability up to their paid-in capital or investment. How
- -
- ever, the joint venture corporation itself has an unlimited liability with respect to
- its obligations. The limited liability of the shareholders is an advantage of utilizing
- such a legal form. In practice, however, this advantage is lost either by the fact that
- the shareholders act as a guarantor of the loans of the joint venture, and the fact
- that the joint venture corporation may very well recover contributions from the
- shareholders in order to pay off its obligations

- Joint Venture Partnership
- Unincorporated joint venture partnerships are governed by the partnership laws of the relevant state. In theory, a partnership can be created by either a written or an oral contract. However, to avoid any misunderstanding, co-venturers in the oil and gas industry usually put their agreement in writing. As explained earlier, joint venture is an ambiguous term, and courts and writers tend to classify
- it as a form of partnership. A partnership can take one of two forms. In a general partnership, all parties are personally liable for the debts of the partnership. In a limited partnership, at least one general partner has unlimited liability while dormant partners have limited liability but no rights to control or manage the business. The oil and gas industry prefers general partnerships.

- 1. Ownership
- The ownership is divided into interest according to the contributed capital (either cash or property) by each partner. However, such ownership is not traced directly to individual assets; it is a qualified ownership. In contrast to the joint venture corporation, there is a direct ownership of (and access to) the oil and gas
- production in addition to the equipment and facilities.

- 2. Control
- Generally, the management structure of a partnership is more flexible when
- compared to a corporation. However, given the special nature and sensitive operations of the oil and gas venture, the management structure and formalities need to be tailored with care so that they reflect and accommodate the essence of the relationship between the partners, host states and FOCs. In theory, all partners have an equal right to participate in managing and controlling the affairs of a joint venture partnership. In practice, a management committee consisting of representatives of the co-venturers is responsible for running the business. The management and voting rights are allocated in accordance with the weighted size of either the capital contributed or the profit shares of the co-venturers. However, unless otherwise agreed to, a minority of partners has the right to participate in the management and control of the joint venture on an equal footing with the majority partners.
- This right of direct control should be structured well in advance. Finally, the principle of “reserved matters” is necessary to protect the interest of minority partners. Reserved matters are any acts that require the consent of other partners.
- So, the control and management of a joint partnership is a sensitive and delicate issue that requires tremendous attention and care.

### 3. Risk

The unlimited liability of each partner creates a great deal of risk, which has caused general partnerships to become unpopular. Partners are personally, jointly, and severally liable for the debts of the ventures. Although a limited partnership can resolve these difficulties, such an arrangement results in another disadvantage:

the loss of the right to control and manage the business—the essence of a joint venture. For example, sleeping (or limited) partners cannot get involved in the Management of the business for they would become general partners with unlimited liability.

Finally, according to the principles of the agency theory, each partner is considered an agent of the partnership. In other words, the act of each partner is binding on all of the partners. Therefore, host states and FOCs must agree on and carefully draft the management structure and formalities to prevent any possible dispute.