Joint ventures in Lebanese and European law

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I. Context

It is often noted that joint ventures lack legally defined boundaries in the United States, which is the country in which the concept first developed. This is not any different in other countries, whether European or Lebanese.

In the US, a distinction is often made between contractual, or non-equity joint venture, on the one hand, and equity or corporate joint venture on the other. Narrowness of purpose and closeness to the two main US types of companies – partnerships and corporations – are the guiding points of difference between the two. The first type – non-equity joint venture – is a special case of partnership. The second type brings the joint venture into the corporate world, which is much wider in scope, time, and institutional organisation, and offers limitation on the liability of the investor.

A parallel distinction is made between putting together resources for a durable or open time, or more narrowly for a particular venture the partners set out to accomplish. Once the purpose (building a factory, carrying out an infrastructural project under a BOT contract etc.) accomplished, the contract of joint venture comes to an end.

In European law, joint ventures are similarly elusive legal concepts, which are better defined under the rules of company law. In England "joint ventures" are frowned upon as a category which lawyers do not recognise outside the specific rules of company law. In France, the word is still translated variously by French lawyers, as *association d'entreprises, entreprise conjointe, co-entreprise*, or even *entreprise commune*, that is of course when the word joint venture itself is not used. And in Germany, the area in company law which the joint venture falls in belongs to various combination of companies, such combination possibly obtaining under the rules of the German law of groups (*Konzern*).

After the failure of the European Union in creating a special type of European company which would bring together English, French and German company law traditions, joint ventures remain therefore a fleeting concept which is regulated, from the inside, by the complex laws of contract and of company. These are specific to each tradition (English, French, German). From the outside, joint ventures are subject to a regulatory framework comprising anti-monopoly principles, EU competition laws, and, depending on the field, technological norms, environmental concerns and so forth.

Nor is the concept clearly delineated in a Middle Eastern, and more specifically Lebanese framework. In Lebanon, international joint ventures also dovetail with rules of the law of obligations, company law, and foreign investment. To that extent, they are not self-standing legal vehicles, but must be viewed as commercial partnerships with a foreign participation/control, and

appreciated against other such vehicles of foreign participation as appear in distribution networks – mainly agency –, and the French equivalent of the public limited company, the Société Anonyme (SAL, with L for Libanaise).

The choice for a foreign company into the Lebanese market is therefore one of three: (1) by way of agency rules, and variations thereof in new fields such as the franchises. (2) by way of opening branches/subsidiaries in Lebanon; (3) by joining or creating a company, typically a Société Anonyme.

The issue of agency is special, and corresponds to distributorship/ importation schemes with special regulations falling outside the field of "joint ventures".

The other two possibilities offer each advantages and peculiarities which are now analysed in some more detail, whilst comparisons will be made from time to time with other countries, including a rapid overview of the impact of the EU on the European joint venture in terms of competition law, and the interface between these constraints and the proposed Euro-Med Treaty.

It is in the context primarily that the efforts of the legislator in recent years, and the discussions with the EU over the Euro-Med agreement, should be appreciated.

II. Lebanese law

Under Lebanese law, the approach to joint ventures is not intrinsically different from the hybrid state one finds in most Western systems. The concept of joint venture does not stand as a separate legal category, even though business men and lawyers in Lebanon carry out joint ventures readily in the shape of commercial companies. The terminology itself suffers from this "speaking in prose" without knowing it, and one can hear several corresponding terms in Arabic, including *sharaka mahsura*, or *mashru‘ mushtarak*, or simply *sharika*, which is indeed not off the mark despite its generality. After all, *sharika* (or *shirka* for the purists) in classical law in an Islamic-Middle Eastern context is defined as the "mixture of money", *khalt al-mal.* If one wanted to be more precise, an exact correspondence to joint venture may be found in classical law as *sharikat al-‘inan*, which one still encounters on the books in a country like Saudi Arabia. The famed Ottoman Majalla consecrates a full chapter 6 and some fifty articles (1365-1403) in the book on companies to this type of corporation. The lawyer will find in it a close equivalent, both in its general terms and in many of its characteristics, to the joint venture.

This, however, is Ottoman law, and *sharikat al-‘inan* did not survive in the Lebanese commercial code which was put in effect during the second world war. As in France, one needs to go back to the full spectrum of companies, together with, for the case of foreign participation, to rules regulating foreign investment in Lebanon. We shall deal here simply with the French form of joint stock companies known as Société Anonyme, which is the most common vehicle for foreign participation, as opposed to the other types of partnerships and corporations, ranging from the smaller Société à Responsabilité Limitée, where all shares are nominal, to unlimited liability in the equivalent of Anglo-American partnerships (the sociétés de personnes), to the more recent offshore and holding regulations. Offshore companies are an interesting development in Lebanese law for foreign participation, mainly because an annual flat fee is paid

in lieu of profit and dividend taxation for other companies. However, the offshore company is by definition barred from carrying out business in Lebanon, so we leave it out of our present concerns. The holding is another recent development of Lebanese corporate law, which is interesting mostly for the type of taxation regime it allows, even if holding companies remain subject to most regulations which govern SAs, the exclusive corporate form holdings may take under Lebanese law.

A foreign investor is not however forced to adopt the Société Anonyme as the exclusive conveyor of its commercial interests. Two other possibilities are available: by way of agency, exclusive or otherwise; and by directly establishing a branch in the country.

In the case of agency, Lebanese law is strictly regulated by a 1967 decree-law (reinforced in 1975) which became a model for the rest of the Middle East, and which imposes some exorbitant contractual rules on the scheme of exclusive distribution/importation of foreign good. The manufacturer/exporter/ principal is held liable for compensation if the contract is not renewed. This is true even for contracts which are entered into for a limited period of time. Procedural means are made available to the importer/distributor/ agent to tie the new agent to the compensation which the court may pronounce. The Lebanese law of agency would be subject to severe scrutiny under the draft dispositions of the Euro-Med Agreement. Whilst crucial to the distribution networks in the country, and to the European-Lebanese trade which remains the most important sector in the international trade of Lebanon, this law is relevant to our examination only in so far as it illustrates another common business contract which can be loosely conceived of as a form of 'joint venture', alongside such newer models as international licensing or leasing. It is true that in most cases of the sort, the Lebanese importer/distributor/ agent retains, under the law, a wide range of manoeuvre. In any case, the foreign party hardly invests any money in the venture. If, however, the agency is conceived under a joint venture agreement, that is as a company, then it becomes at the cross-roads of strictures imposed by the 1967 Decree-Law, as well as those regarding SAs in general.

The two other legal models for a foreign presence in the Lebanese market are the subsidiary or branch in the country; or the formation of a shareholders' company. Let us examine the two models in turn.

Branch

The law governing the establishment of branches or subsidiaries of a foreign company goes back to Decree 96 of the French Haut Commissaire, 30/1/1926. This decree continues to regulate, in the main, the Lebanese branch of a foreign SA.

Under the law, there is in theory no requirement for a previous agreement from the Lebanese authorities to open up a branch in the country. In practise, however, declaration is followed by registration, which obeys certain rules.

The company must first declare an interest in opening up a branch or a subsidiary in the country. The declaration, which must be made before the company establishes the branch, is directed to

the section on companies in the Ministry of the Economy by a representative of the company. The declaration includes a number of documents:

1- Articles of Association of the foreign company

2- By-laws

3- Power of attorney to the representative in Lebanon, officially translated to Arabic, and notarised. The representative may be a foreign national, but he needs a residence permit delivered by the Ministry of interior.

All these documents must be signed by the foreign company which intends to open up the branch in Lebanon. They must be rendered official by the seal of the relevant officials in the ministry of foreign affairs of the country concerned, before being also countersigned by the Lebanese ministry of foreign affairs.

If all these conditions are met, the appropriate stamp fees are paid, after which proof of payment by the treasury is added to the declaration, and the branch is registered in the special section of foreign companies. The certification is sent thereafter to the official journal for publication.

Disregard for these formalities is conducive to the payment of fines, in addition to the danger of being paralysed legally and unable to conduct its case before the Lebanese jurisdictions (Art.3 of Law dated 30/9/1944, with Art.16 of D-L 96)

Once the formalities completed with the Ministry of economy, registration with the Commerce Registry is required. This, in contrast to the declaration, does not prevent the branch from appearing before the court, but fines may be imposed. Registration was introduced principally to protect third parties.

Branches in specific areas of the economy (such as banking), as will be specified in the case of SAs, require a special permission. A branch, however, is typically one in which the foreign investor does not wish to tie his investment up with a Lebanese partner. The normal route for teaming up capital and human resources while securing some local participation is to adopt some form of corporation under Lebanese law. The most common for larger endeavours is the SA.

Sociétés Anonymes

The SA, like all other companies, is regulated by the Lebanese Code of Commerce. Four chapters in Book 3 and some 200 articles are devoted in the Code to the SA (Arts 77-225). Several articles have been modified, by special legislation, over the years, and there are specialised areas where supplementary legislation must be considered, notably real estate, banking and financial services, and shipping.

Formation of the SA and its constraints

The SA established in Lebanon has, by law, Lebanese nationality. The minimum number of founders is three, and the capital 30 m LP. Articles of association must be registered with the notary public, and the memorandum of association includes name, main location, object, duration, amount of capital and shares, the value of non-liquid assets, dividends, board of

directors (three to twelve members), competence, assemblies, and the signatures of the shareholders. Public subscription may then be opened.

In the first meeting of the founders, the board is elected if not established in the memorandum. The board chooses the president, and carries out publicity requirements.

There is in reality little that renders an SA differ in essence from its European cousins, except for the combination of 'national' requirements which, together, create a backdrop to the traditional openness of the Lebanese corporate sector.

For the formation of the company, irrespective of the type of activity, the only tangible constraint is the requirement, under Art.144 of the Code of Commerce, that "the majority of the members of the board of directors (*majlis al-idara*, conseil d'administration) must be Lebanese." The chairman of the board need not be Lebanese.

This is a seemingly superfluous constraint, which does not correspond to any mirror requirement in the nationality of shareholders.

However, foreign investors must remain attentive to two other types of constraints: the first is linked to land; the second to the type of corporate activity.

Land. Presumably, any foreign company needs premises, and a complicated law dating back to 1969 imposes restrictions to foreign ownership of land, be it individual or corporate. The law is complicated and poorly drafted. In addition to distinctions made between individuals and companies, it addresses four different nationality degrees: a full Lebanese national, a foreign national of Lebanese descent, a citizen from an Arab country, and a 'full' foreigner. The foreign SA is defined, for the purposes of the law, as a company in which at least one third of the shares are not owned by Lebanese individuals. The gradation between the four categories moves from the fully Lebanese company, who does not encounter any constraint in the acquisition of Lebanese land, to one where the foreign company cannot, without a special permission from the government, own more than 10000 sq. metres in Lebanon as a whole. For any industrial concern, such a limit is important. Special derogations are however possible.

Type of activity. Apart from professional associations, such as those of engineers, lawyers, and medical doctors, where nationality is important and where the exercise by a foreigner may depend on a special leave by the professional syndicate concerned, institutionalised joint ventures are not in theory subject to constraints on foreign participation. Originally, the Code of Commerce required a special dispensation by the Council of Ministers for the registration of any SA, but this requirement was abolished in 1977. From the original constraints is only left a section of Art.78, which requires any SA "whose object is the exploitation of a public interest", to retain a third of the nominal actions with Lebanese shareholders.

In practice, problems emerge in special areas such as agency, real estate, banking and financial institutions, shipping, and insurance companies. As in many other countries, these areas are

regulated by special legislation, and Lebanese ownership may be important for the various regulations attaching to each. While, as in the case of real estate and agency, a special regulation might make a clear distinction between foreign and local investment, there are also other considerations which play a role, notably the permits allowed in some key sectors like banking and insurance for companies with significant foreign participation.

III. Lebanese joint ventures and the Euro-Med draft agreement

Considering the disparity between company rules in Europe, and the several forms that joint ventures may take, the European Commission, the Council and the Court have ensured that horizontal cooperation, that is co-operation between companies, will be regulated by competition law irrespective of the legal form taken by the agreement. Hence, some joint ventures are treated under cartel law, other under merger law.

If the creation of joint venture qualifies as a concentration, the 1989 EEC Merger Regulation applies. This is a fairly complex set of rules which applies to huge concerns, and is of little potential application in the Lebanon in the immediate future. What is important is the definition of concentration joint venture, because, simply put, co-operative joint ventures are those joint ventures which are concentrative. The 1990 Commission Notice on Co-operative and Concentrative Joint Ventures offers a set of useful, if not decisive, definitions.

First, a joint venture is defined as "an undertaking under the joint control of other undertakings", meaning that there is no joint venture if one of the parent companies can decide alone on its commercial activities. Weighting of share ownership and management control are therefore important.

Secondly, a concentrative joint venture is one where two conditions are met. The first, positive, condition is the autonomy of the joint venture, which must be its "full function on a lasting basis." The second, negative, condition is that the joint venture does not lead to the co-ordination of the competitive behaviour of undertakings that remain independent of one another.

So defined, the concentrative joint venture is subject to the investigation of the Merger Commission, and deemed possibly incompatible with the Merger Regulation.

If it is not considered as concentrative, it may be deemed co-operative. If co-operative, the joint venture falls under Art.85 (1). In the Notice on Co-operative joint ventures, published in February 1993, it was noted by the Commission that, because of the diversity of situations in which joint ventures my be encountered, "it is impossible to make general comments on the compliance of joint ventures with competition law." Still, a set of five issues was developed by authors to assess whether the joint venture in question restricts competition:

"- Does the agreement restrict competition between the parent companies ?

- Does the agreement restrict competition between the parent companies and the joint venture ?

- Does the agreement have an anti-competitive effect on third parties?

- Does the agreement have an appreciable effect on competition ?

- Does the agreement establish a network of joint ventures that could restrict competition ?"

An instance where the Commission found infringement of Art.85 (1) is Re Henkel and Colgate (1972) in a case of joint venture for research, in which the agreement did not specifically prevent the parent companies from carrying on their own research, but did in practice prevent it through a clause limiting the transmission of information to the parent companies. The list of possible infringements is long, and covers specialisation joint ventures (where firms enter into joint ventures which allow them to specialise in a specific marker segment); joint sales; joint purchasing; manufacturing; standardisation; restrictive covenants...

These regulations can be remarkably complex, but they underlie the concern of the community with facilitating healthy competition as big companies enter into multi-million dollar joint ventures in ways that are bound to affect the markets. The Middle East market, except arguably for oil, is too small for any such competition problems affecting it in the near future. Still, as in the case of agency, it is arguable that the language of the Euro-Med Agreement draws on the acquis communautaire in a way which introduces the more complex areas of European in a completely alien foreign legal environment. This is plain in Title 4, chapter 2, on competition, and draft Art.40 states categorically that "sont incompatibles avec le présent accord et interdits tous accords entre entreprises, toutes décisions d'associations d'entreprises et toutes pratiques concertées, qui sont susceptibles d'affecter le commerce entre la Communauté et le Liban et qui ont pour objet de restreindre ou de fausser le jeu de la concurrence...". The whole paragraph is a verbatim reproduction of the language of Art.85, and is followed by the Euro-Med draft treaty's rendering of Art.86 prohibiting abusive exploitation of a "dominant position".

This leads, as in agency, to open challenges, possibly before Lebanese courts which are not equipped to deal with European law, with the most complex rules of competition law as developed by the European Court of Justice and other agencies. Nor is the problem of monopoly one which would necessarily elude litigation: the fierce competition over joint ventures in the cellular phone sector over past years would show that Lebanon, despite its size, may not be a hurdle-free stage for commercial competition.

IV. Conclusions

From a comparative perspective, the main problem of joint ventures has been defined as one where "once we recognize the fact that an enterprise can be controlled by more than one company, it follows that the dependency created by joint control can be increased to the point where centralized management is introduced... This raises the question of how to regard joint ventures in the context of a regime of affiliated groups."

Further problems raised include the "exercise of the rights of direction, obligatory safeguards for outside shareholders, and the application of the rules for the protection of creditors." While the application of the regime for the de facto affiliated groups to the relationship created between parent companies and their joint venture has not been fully discussed to date, as noted in the context of the Societas Europae, one can imagine the ripple effect on an inexperienced legal framework as the one prevailing in Lebanon.

Beyond these problems which may be said to be typical the world over, and whatever form the joint venture might take upon the decision to invest in Lebanon by a foreign company, investors will need to give practical attention to the usual constraints one might face in the field. The country is famed for its liberal attitude and the absence of constraints on cash flow, in addition to the banking secrecy and a reformed and simplified system at a low percentage of taxation. In all these matters, Lebanon is at a comparative advantage in the region, as well as in an international setting. Few Western countries benefit from such a relaxed legislation. Where however foreign investors might find a joint venture troublesome is in those specific areas where the state is attentive to foreign ownership. On a ladder of constraints, agency and distributorship appear the most adverse to foreign ownership or management, and they are important in so far as trade is the nerve of the country. There are also constraints with regard to the banking and other so-called "strategic" sectors, such as real estate. In addition, the situation is in a state of flux in the financial services sector, and the government and the Central Bank have been keen to open up the field to foreign investment in recent years. There remains that the more civilised way to deal with these problems is to list, in detail, those constraints which the potential investor might face, and address them in the best interest of the country before entering into a binding agreement with the EU.

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