



MANAGING CORPORATE RELATIONSHIPS IN THE GCC

Having seen a significant increase in the number of Joint Venture (“JV”) disputes in the GCC, Addleshaw Goddard’s Commercial Litigation and Corporate teams have pooled their expertise to provide a JV ‘toolkit’ which reviews the most common causes of JV disputes and how they can be avoided.

Whilst the focus of this guide is JV disputes, the lessons learned and the pitfalls to be avoided apply equally across all manner of corporate relationships in the GCC from distribution agreements to franchise arrangements, and from mergers to acquisitions.

The GCC Market

In order to trade in many jurisdictions across the Middle East and North Africa, it is often mandatory to enter into a formal arrangement with a local partner or sponsor in that territory. Common methods of obtaining or broadening a presence in the GCC include entering into a distribution agreement, forming a JV, or through a merger or acquisition.

With so much invested in a corporate relationship, it is crucial to ensure that the set-up and management of the business is handled correctly. Careful consideration of the following issues could help you avoid protracted and costly disputes.

Set-up

Underlying documentation

No matter the governing law and jurisdiction provisions of the corporate agreements, ensure that they do not conflict with mandatory local laws. Ultimate enforcement of the agreement will most likely take place in the home jurisdiction of the business, so corporate documentation and governing agreements should be drafted with the local laws in mind.

Ensure that you negotiate your position carefully and your agreement on issues that are likely to be important during the course of the relationship is clearly recorded. In particular, care should be taken when negotiating and recording agreement on the following points:

- ▶ Initial and ongoing funding obligations;
- ▶ Control and decision making;
- ▶ How and when profit will be taken out;
- ▶ When and how the relationship can be terminated; and
- ▶ What happens post-termination.

Running the Business

From our experience of JV disputes, there are three issues that are consistently shown to lead to a deterioration in the relationship between the partners. They are:

Economic distributions and profit share

The payment of dividends can become a contentious issue during the course of the JV if the two partners’ objectives are not in alignment and, as is often the case, the JV agreement is silent on the issue. In order to avoid disputes around the distribution of dividends, it is recommended that the JV agreement deals expressly with the treatment of profits.

The ‘international’ company may take a long term view to its investment in the territory and seek to establish a solid financial foundation before it begins taking dividends from the JV. Its partner, on the other hand, may only be tied into the JV for a fixed period of 5 or 10 years and will naturally want to see a more immediate return on its investment during that time.

As is often the case, agreement and alignment of interests from the beginning of the relationship is

key as is transparency when dealing with dividends.
Tip – try to avoid a situation where the decision not to declare a dividend is made by way of board resolution in circumstances where one partner's appointed directors can push decisions through by a majority.

Uncertainty around directors' duties

When a JV is formed, the board will invariably consist of a mix of directors (also known as managers) appointed by both parties. As a result, the directors can find themselves seemingly in a conflicted position. Whilst it can be tempting to act in the best interests of the 'parent' in support of their global policies, it is important for the directors to remember (especially where their actions can attract individual liability with civil and criminal sanctions) that they are appointed by the JV company and obliged to exercise their duties in the JV's best interests.

Misalignment on key issues

Issues can also arise where one partner has a dominant position over the other. Whilst international companies may be keen to maintain absolute control over their business or brand, care must be taken to treat your counterpart as a partner and not simply a means to an end when entering a new market.

One of the major strains on corporate relationships in the GCC is a breakdown in communication between the partners or a clash of cultures. Before forming a corporate entity, care should be taken to ensure that you are the right fit for one another. Once the partners are working together, it is essential that lines of communication remain open and they are in agreement on the main issues.

Ending the relationship

In addition to the important stages outlined above, a final but equally important consideration is how and when the relationship ends.

Exit Strategy

Whilst it can be tempting, during the honeymoon period of a new venture, to proceed on the basis that relations will always be strong, it is vitally important to agree and record an exit strategy at the outset of the relationship.

Share Sales & Call options

In the event that one partner wishes to exit the relationship, disputes can often arise in relation to the sale of shares. This risk can be mitigated by carefully recording issues such as how shares are to be valued, lock-in periods and pre-emption rights.

Care should be taken in relation to put and call options because even where the option is detailed in the agreement, should one partner refuse to sell, specific performance (i.e. an order compelling a shareholder to sell its shares) is notoriously difficult to obtain in many GCC

jurisdictions, so the ability to compel a reluctant partner to transfer shares cannot be guaranteed and damages may be the only available remedy.

Conclusion

Given the potential pitfalls of entering into and exiting foreign corporate relationships, all efforts should be made to carefully record the agreement between the parties and to maintain cordial relations with your local partner. By taking care to preserve an amicable commercial relationship you can avoid lengthy and costly disputes where, ultimately, it may be difficult to compel your partner to transfer its shares.

You should ensure that you are aware of your rights and obligations throughout the life of the business and that where a dispute or difference between the parties does arise, that you seek early strategic advice in order to try to preserve the relationship between the partners.

When a difference does arise between the partners, seeking early legal advice will assist you in understanding your rights and obligations and allow you to adopt a strategy to best protect your interests in the event that the difference can be resolved, or if the matter cannot be amicably settled and becomes a dispute.



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