

## Chapter Five: Respect for Human Rights in Joint Ventures Relationships

### Overview

#### *Brief overview of joint ventures relationships*

Joint ventures (JVs) are formed when companies combine their resources and expertise to pursue a common business goal that is typically limited in scope. Companies initiate JVs by entering into an agreement that sets out their goals, duties and rights. JVs can be structured in different ways. A JV typically involves the creation of a new entity, in which each JV partner takes specific roles. One partner may be responsible for funding a percentage of the venture, while another runs day-to-day operations. In some instances, partners second staff to fill JV positions.

JVs are often vehicles for major projects that companies are unable or do not desire to fund and manage on their own. JVs are increasingly used in the oil, gas, and mining industries and for major infrastructure projects (dams and electricity generation plants), because these investments typically involve significant outlays of capital, sometimes over the course of many years. Oil and gas JVs often do not create a new legal entity, and are purely contractual. JVs typically include majority and minority owners, and operating and non-operating partners, whose relations are defined by agreement. Policies and procedures are similarly defined by agreement. In part due to potential liability, companies normally carry out substantial financial and other due diligence on potential JV partners. If they are not the operator, partners in JVs typically maintain audit rights over some issues.

JVs are also employed in research and development, to launch new products, and to support manufacturing processes with local partners.

#### *Human rights and joint ventures*

Businesses may consider human rights impacts for a number of reasons when they enter JVs. For example:

- Managers and technical experts in JVs often come from diverse backgrounds and corporate cultures. This creates challenges and positive opportunities for exchange of experiences, including around adherence to international social and environmental standards, including human rights.
- The largest infrastructure projects and extractive projects (mines, dams, integrated industrial plants, transport and logistics hubs) are frequently operated as JVs. They tend to have a high profile and to affect local communities and environment significantly. They frequently generate human rights issues, *inter alia* around land use, resettlement, cultural heritage, security, and access to basic services such as water and sanitation. In addition, they tend to employ a large number of skilled and unskilled workers, who are rarely available in the immediate vicinity. The responsible recruitment of migrant and other workers is another issue with a human rights dimension. Finally, large JVs generate a complex network of subordinate business relationships, which tend themselves to generate human rights impacts.

- In recent decades, many businesses have been exposed to reputational, operational, financial and legal risks due to actions by JV partners. Both majority and minority partners can be affected, because stakeholders are less interested in whether a company is an operator or controlling partner, especially in situations where the company is the better-known company and is viewed as having the capacity to encourage its JV partner to behave more responsibly. As accountability becomes more globally networked and sophisticated, even a minority involvement in a JV can bring exposure – sometimes even after a company has exited the JV. As accountability becomes more nuanced, all partners, whether minority or majority, will be exposed to risk and criticism. Additionally, partners that leave the JV in question may be held accountable for human rights abuses that occurred during their watch.

## The Business Relationship Cycle

### Selecting and Starting the Relationship

*Setting expectations and communicating them to business partners*

**Companies can help to manage human rights-related risks by choosing their JV partners with care, but their choices may be limited in some circumstances.**

Companies usually make a significant effort to identify and investigate potential JV partners, since the relationship is important and often long-term. Many companies observed that the best method of reducing the danger that a JV will be embroiled in human rights problems is to select its partners with care. At the same time, in some sectors and circumstances, companies have little or no choice. For instance, many governments require oil and gas companies to ally with the state-owned national oil company as a condition for securing a concession agreement.

**Before forming a JV, companies use various avenues to convey their human rights expectations to business partners.**

As they do with other forms of business relationship, companies typically address human rights issues with JV partners by reference to their own values and policies. When a potential JV partner is like-minded and has similar policies, such discussions are relatively straightforward, and the parties may explicitly focus on human rights. When the JV partner is sceptical of human rights, companies sometimes introduce human rights concerns indirectly, by discussing ethical policies or other policy positions and referring to environmental and social practices and expectations.

*Understanding the issues – Assessing human rights impacts in joint venture relationships*

**Companies do serious due diligence for certain JVs, and often consider human rights.**

When they form larger JVs, particularly to implement large infrastructure projects, companies reported spending significant amounts of time and money on initial due diligence. They investigate potential business partners, and sometimes consider human rights when they do so, though they may not use the term explicitly. Companies often

consider the environmental, health, safety, labour, and security practices of potential JV partners, for instance. When a partner has a poor record or capacity in these areas, companies take steps to limit risk, by taking particular roles in the JV, or inserting specific policies and procedural safeguards in contracts (see below). In a few sectors (support manufacturing, research and development), companies reported that they conduct little due diligence on JVs (including human rights), because they believed that the projects they undertake have a different and lower risk profile. They admitted, however, that this practice created blind spots.

**Due diligence appears to vary in scope, and is more extensive when a company operates or holds a majority stake in the JV.**

Companies may conduct more detailed due diligence if they are operators of the JV or project, or hold a majority stake. Companies in this position usually presume that their operating procedures will apply. On these grounds, they focus on the national environment in which they will be operating and may spend less time scrutinising the operating practices of their partners. An exception is made for corruption. Companies with a majority interest are likely to consider the corruption safeguards of JV partners. Initial due diligence on the national context includes: expropriation; political instability; corruption; poor rule of law; weak enforcement of international labour standards; claims of indigenous peoples; and other human rights concerns.

By contrast, the due diligence process may look quite different when companies are minority stakeholders in a project, do not operate it, or have little leverage on a JV—though most understand that they may still be held liable, legally or reputationally, for the JV’s actions. Some companies have therefore developed specific due diligence processes for JVs, and increasingly consider their partners’ environmental, health, safety, labour, and human rights practices. Where pertinent, companies also sometimes consider a partner’s history of working with private and public security forces. One company involved in the research has developed a list of due diligence questions on human rights that it specifically uses when it has a minority stake in a JV.

**To understand country situations and challenges, companies may consult external stakeholders but more frequently speak to potential business partners.**

Most companies seek to keep confidential the possibility that they will form a JV until they decide whether to proceed. If the JV is in a high-risk country, they sometimes reach out to civil society, think tanks, and government officials to better understand the country’s risk profile – sometimes using a third party to maintain their anonymity. In one instance, a company said that it consulted an environmental NGO it knows well about the practices of potential business partners; but this practice appears to be infrequent.

Companies typically ask potential partners to provide additional information about their environmental and social practices, though they more frequently ask about their record on corruption. In the course of due diligence, for example, several companies regularly ask potential business partners to disclose corruption investigations and lawsuits, which helps them to quantify risk. In principle, companies could also ask about NGO

campaigns and human rights-related cases; but it is not common to do so. In some industries (oil, gas, and mining), large and mid-sized companies are already aware of the environmental, social, and human rights practices of their peers, both through their industry groups and because they often work together in JVs.

### **Formalising the Relationship**

#### **JV agreements can be designed to consider human rights explicitly.**

JV agreements create a new structure with specific operating and governance procedures. The structuring of the JV provides the main opportunity for a company to create long-term leverage within the JV – around human rights or any other issue. For example, companies may:

- Integrate language on human rights into the agreement or its annexes.
- Ensure that the project adopts specific environmental, social, or human rights policies and procedures.
- Obtain relevant management positions in the new organisation, allowing them to oversee operations that are relevant to human rights. (One company places “governors” in its JV’s management structure, with authority over particular topics that are of interest to the company.)
- Require audit rights in relation to social policies and procedures, enabling the company to determine whether the JV is implementing its commitments.
- Require the JV to report to the management, a designated official, or JV partners on specific topics of interest to the company.

When two companies with similar human rights practices form a JV together, an agreement may declare their human rights expectations explicitly. Texts typically focus on specific rights (labour or health and safety), although they may include a more general reference to human rights. Some companies bring human rights into agreements by making reference to external standards (such as the Equator Principles<sup>78</sup> or IFC Performance Standards<sup>79</sup>), which refer to specific human rights. One agreement referred to the Equator Principles and required the JV to develop an additional environmental and social policy for implementing them. Where one partner is recognised as a global leader, other JV partners may accept its policies in order to learn from its environmental, social, and human rights practices.

#### **Contractual language on human rights is considered mandatory by some companies, whereas others include it where possible.**

Some companies would not sign a JV agreement unless it contained certain human rights commitments. Other companies would not sign a JV agreement that did not require the operator to respect social and environmental standards (including explicitly or by implication human rights standards) that were at least as high as those of the company.

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78 At: <http://www.equator-principles.com/>.

79 At: <http://www.ifc.org/performancestandards>.

One company noted that, when it has a minority stake in a JV, it expects potential partners to make representations and warranties regarding their human rights records and compliance efforts; it also seeks to include an exit clause if serious human rights abuses arise. Other companies consider that human rights language is not mandatory. Although some have developed model language for JV agreements that explicitly refers to human rights, they admit that they will agree to changing or dropping that language if the partner is not willing to accept it.

Some companies hold the view that it is not possible to address all the human rights issues that might confront a JV during its lifetime. These companies suggested that in practice other mechanisms can more effectively ensure that JVs address human rights issues. Obtaining key positions in the venture that provide leverage over social issues is an example (see below).

### **Rethinking Investment Contracts, Including JV Contracts, to Promote Sustainable Development**

The International Institute for Environment and Development (IIED), an international development and environment policy research organisation, has undertaken detailed research into contracts that cover natural resources. Several of its reports examine JV agreements.

- **How to scrutinise a Production Sharing Agreement (PSA): A guide for the oil and gas sector based on experience from the Caspian Region.**<sup>80</sup> This report provides a guide for civil society to oil and gas contracts. It outlines key characteristics of PSAs, focusing on JVs, concessions, and PSAs. Action points for civil society organisations involved in monitoring contracts made by extractive industries include: public participation in the contracting process; economic fairness; integration of social and environmental concerns; and consideration of economic, social and environmental issues over the project's lifetime.
- **Investment contracts and sustainable development: How to make contracts for fairer and more sustainable natural resource investments.**<sup>81</sup> This report identifies the main contractual issues and processes associated with exploitation of energy, minerals and agricultural commodities, and suggests how investment contracts, including JV agreements, could be drafted to maximise the contribution of such investments to host countries' sustainable development.
- **Land deals in Africa: What is in the contracts?**<sup>82</sup> This report analyses twelve land deals in Africa, and their wider legal frameworks, from a sustainable development perspective. It suggests ways to improve large land-acquisition contracts.

80 At: <http://pubs.iied.org/pdfs/16031IIED.pdf>.

81 At: <http://pubs.iied.org/pdfs/17507IIED.pdf>.

82 At: <http://pubs.iied.org/pdfs/12568IIED.pdf>.

**JV agreements may stipulate operating procedures that explicitly or implicitly address human rights.**

Some companies noted that embedding good human rights practices implicitly or explicitly in the JV's policies or operating procedures is the most effective way to ensure that human rights are addressed on an on-going basis. If the companies forming the JV are committed to human rights, the venture will typically adopt the human rights policies and procedures of the operating or majority partner.

If the JV partners have different approaches to human rights, the situation becomes more complicated. At least one company involved in the research requires partners in a JV to adopt the company's social practices or their equivalent, even if it is a minority or non-operating partner. Other respondents said that, if the operating partner was hostile to human rights or unwilling to discuss them, their companies might seek to have the JV agreement state that the operator would use their social and ethics policies. Since the social and ethics policies of these companies refer to and therefore incorporate their human rights commitments, the companies in question believe they can thereby create space for a discussion of human rights in the future.

**Companies create long-term leverage by their choice of roles and procedures in the JV.**

Companies may seek to fill specific positions in a JV to promote strong social, environmental, and anti-corruption practices, extending in some instances to human rights. When it is not the operator, one company places its staff in legal, financial, and compliance positions from which they can manage key risks, such as corruption and human rights. Another appoints a "governor", with authority to take decisions and report to partners, to manage topics in which the company has a particular interest. The company trusts its employees to robustly implement the JV's policies, and spot problems, including human rights challenges that its policies might not address.

Opportunities to advance human rights also occur when JV committees are formed, and powers are assigned to them. One company seeks to control the JV's compliance committee, to give that committee oversight of environment, health, and safety issues, and to have the JV agree to a compliance plan which the committee then monitors. Another company seeks, through the JV agreement, to set up a social responsibility committee.

The design of voting rules can create further opportunities. One company seeks to ensure that a supermajority is required for decisions related to compliance and human rights-related procedures, so that it can block problematic proposals.

**Internal coherence and alignment may affect the human rights content of the agreement.**

Whether the JV agreement includes human rights or other social concerns depends in part on who negotiates the agreement and the extent to which negotiators consider such concerns important, or are incentivised to do so. As noted in Chapter 3, performance incentives can help to determine whether issues like human rights are addressed in negotiations and included in agreements.

In some companies, lawyers are closely involved in drafting agreements. A number of companies rely on standard contractual language that they modify for specific deals. Unless company lawyers are instructed to include human rights issues in the template, or to address human rights in the agreement, these issues may not be raised. Lawyers also sometimes find it challenging to draft language on human rights that is specific and enforceable, and may therefore choose to avoid the subject.

In other companies, business units negotiate JV agreements; company lawyers merely review them technically. Unless business units are convinced that social and human rights issues present material risks to the venture, they are unlikely to highlight such topics if they are not required to include it as mandatory language in the agreement. One company involved in the research found that employees of local business units who were charged with forming JVs did not consider the company's commitment to the Equator Principles to be important and therefore made limited efforts to reference them in agreements. The employees believed that local law provided sufficient protection, and just wanted to "get the deal done". To ensure the Equator Principles are adequately addressed, the company's investment committee at headquarters now reviews JV agreements before they are concluded.

**Some companies treat regulatory and reputational risks as conditions precedent.**

At least one company involved in the research uses conditions precedent to protect itself against unwittingly assuming human rights-related risks that would otherwise only become apparent by carrying out in-depth due diligence. It also requires JV partners to provide warranties regarding compliance and their human rights history.

**Referring to third party standards, including MSIs, builds further leverage to address key issues.**

Some JV agreements refer to industry or multistakeholder principles or codes of conduct, or include language that draws from them. Oil, gas, and mining companies sometimes refer to the Voluntary Principles on Security and Human Rights, or include language from the Voluntary Principles to require the JV to implement security practices that safeguard human rights. Such language has been included in some agreements with state-owned enterprises (SOEs) from emerging economies such as China. The Voluntary Principles do not presume that companies should adopt their language in JV agreements; the practice appears to have developed because companies are concerned about legal, reputational, and operational risks related to poor security practices. Another company participating in the research seeks to include the Equator Principles in JV agreements for similar reasons. The company is not an Equator Principles bank, and appears to be motivated by its own commitment and concerns about environmental and social risk.

**Seeking finance for the JV from financial institutions that have a clear set of social and environmental standards is often a sensible way to establish leverage over JV partners.**

In some sectors, JVs seek loans from international financial institutions such as the International Finance Corporation (IFC) or an Equator Principles bank. The IFC

requires organisations that it funds to adopt its Environmental and Social Performance Standards, and to report on their compliance with them as a condition of continued funding. Conditionality of this kind can be helpful when projects operate in locations in which the authorities are hostile to human rights concerns, because the JV can argue that its human rights standards are externally imposed rather than self-initiated. The same argument may be used when dealing with SOEs that are disinclined to address human rights concerns.

### **Managing the Relationship**

**When companies are not operators of a JV, they usually involve themselves less in its regular social and environmental assessments, rarely build capacity in human rights, and do not consistently report on its human rights practices.**

When companies operate a JV, they typically audit its performance against relevant environmental and social policies and procedures, as they would for any of their operations. When companies are not operators, they rarely do so. Audits focus primarily on financial practices and, in some instances, corruption.

That said, some companies do audit the environmental and social practices (including human rights) of JVs in which they hold a minority stake. Such audits, often jointly conducted by the operator and non-operator, are more likely to occur when the JV is working in a high-risk environment. One company in the research seeks to ensure that the JV has the right to have its first tier suppliers audited, to verify that they comply with certain human rights standards; this is a relatively new practice.

If they are the operator, companies seem to invest in the capacity of JV staff, because they apply their own social, environmental, and human rights policies and procedures, and train staff in them. A company that is not the operator is far less likely to provide human rights training, and more likely to do so on an ad-hoc basis because it has identified a risk to the company. By contrast, a number of companies systematically provide anti-corruption training even when they are non-operators.

**Some companies receive consistent reporting on their JVs' human rights performance.**

JVs report formally and informally to their owners, providing opportunities to discuss human rights challenges. JV board and committee meetings provide a venue for discussion of human rights concerns. Some minority partners require incidents to be reported. However, if non-operators do not raise questions on human rights at the board or in committees, and do not audit compliance with the JV's social policies, it is difficult to see how they can make themselves aware of human rights challenges until the issues catch the attention of the media, NGOs, or social investors.



**Grievance mechanisms for employees and affected communities are variable.**

Typically, a JV's operating procedures determine whether employees or affected communities have access to grievance mechanisms for alleged human rights abuses, in addition to remedies available through the judicial system. JV grievance mechanisms vary according to the industry, and can be robust or non-existent. What is offered depends on the operator and the operating procedures defined in the JV agreement.

**Ending or Renewing the Relationship****JV agreements rarely consider human rights-related problems to be material breaches.**

Few JV agreements define environmental, social, or human rights problems as material breaches or grounds for terminating a relationship. Were agreements to do so, companies would still have to balance this against the time and money they have invested. Companies indicated that generally they preferred to influence a JV's actions, through the JV's board or committees. Under oil and gas agreements, a material breach of environmental, health or safety obligations by the operator may trigger its removal as operator.

**Legacy issues (including human rights), can affect the reputation of former owners.**

In a few instances, companies that wish to sell their shares in a JV have considered the effect on communities or employees of selling their assets to purchasers that do not respect human rights. Some of these companies have sold their stakes to purchasers that offered slightly less money, but were more likely to operate the asset responsibly.

After a JV closes, or a company sells its stake, human rights problems can continue to affect a company. For example, plaintiffs may sue a company for human rights abuses that occurred on its watch. (The extent of a company's liability will be influenced by the structure of the sale and whether it transferred relevant liabilities to the buyer.) A purchaser of a company's stake in a JV might also, as part of its initial due diligence, request information about human rights incidents that occurred, which might reduce the price the purchaser is willing to pay.