Briefing

BURGES SALMON

Real Estate

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Real Estate Development Joint Ventures

Introduction

This guide provides an overview of the most common legal structures used in real estate development joint venture arrangements in the UK. It assumes that the venture itself, its operations and participants are all UK-based.

What is a joint venture?

Put simply, a joint venture is a commercial arrangement between two or more participants who agree to co-operate to achieve a particular objective. Joint ventures cover a wide range of collaborative business arrangements which involve differing degrees of integration and which may be for a fixed or indefinite duration.

Why enter into a joint venture?

Essentially it is a way of sharing the costs and risks associated with a development project. A party may be looking to tap into a partner's greater or more specialised expertise or resources – be they financial, technical or marketing.

The potential benefits may be easy for those involved to see but will be difficult to achieve without a clear-cut strategy, mutually understood objectives, thorough documentation and plenty of commitment from all involved.

What are the structuring options?

There is no distinct legal form for a joint venture in the UK, allowing each joint venture relationship to take the form which is best suited to its own circumstances and specific purpose. Factors to consider include the differing tax treatment of the possible legal structures, the nature of the property to be developed or the degree of technical complexity involved in the development. Some commonly used structures, their key features and the advantages and disadvantages associated with each are reviewed in this note. Other forms of joint venture are also used in the UK (such as geared leases) but we have not explored these in this note.

Contractual Development Agreements

Advantages	Disadvantages
■ Flexible option – can be quick to set up and easy to dismantle as no separate entity is created. Useful for strategic alliances or short term, single-goal ventures. ■ JV parties retain ownership of their own assets. ■ JV party is not normally liable for the debts of the other JV party but they may share liability on specific contracts with third parties. ■ Each JV party will be taxed directly on its share of the profits and losses of the venture.	■ Lacks a separate legal identity – can suffer from a lack of clear structure and identity which may affect both internal operation and dealings with third parties. ■ Risk of creating a partnership, giving rise to unlimited joint and several liability where each of the JV parties is liable for all losses of the venture. ■ Potentially difficult to raise external loan finance as not a legal entity and does not own assets – it cannot grant a floating charge as security for financing.

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JV Company

Advantages	Disadvantages
■ JV company is a familiar structure with a clear corporate identity and established corporate governance regime. ■ Can own its own assets, sue and be sued and enter into contracts in its own right. ■ Liability is limited to the amount each party contributes by way of share capital. ■ Tailored share rights can reflect the size, contributions and motivations of the JV parties. ■ Realising an interest by way of a sale of shares will not disrupt the legal ownership of the underlying business.	■ Potential for double taxation – tax will be applied at the JV company level and possibly again on the JV parties directly when they take profits out of the JV company or realise their investment in it. This lack of tax transparency is, however, not always a disadvantage in practice and the tax position will depend on the nature of the JV parties themselves. ■ Reporting and compliance requirements bring increased administration and public disclosure of information. ■ Limited liability may be undermined in practice by guarantees and security required to support external financing and third party contracts.

Limited Liability Partnership

Advantages	Disadvantages
■ Treated as a partnership for tax purposes – each JV party will be taxed directly on its share of the profits and losses of the venture. The LLP is not taxed on its profits. ■ Limited liability of members. ■ Separate legal identity – benefits from a clear corporate identity both internally, in terms of a dedicated management and workforce, and to the outside world.	■ The roles and responsibilities of LLP members are not as familiar as the defined roles of directors and shareholders in limited companies. ■ Public filing requirements exist, in particular in relation to accounts (but these are not as extensive as for limited companies). ■ Limited liability may be undermined in practice by guarantees and security required to support external financing and third party contracts.

General or limited partnership

Advantages	Disadvantages
■ Flexible – governed by the agreement between the members, not restrained by a rigid legislative regime. ■ Fiscal transparency means that the individual JV parties will be taxed directly. The partnership is not taxed on its profits. ■ Sensitive details of the venture can remain completely private between the JV parties. ■ Limited partnership – popular as investment vehicles (where the majority of participants are passive investors) but not suitable for commercial joint ventures as limited partners must not be involved in the management of the venture.	■ General partnership – unlimited liability of each JV party for the whole of the liabilities of the venture (although JV parties can be corporate entities). ■ Limited partnership – general partner manages the JV and has unlimited liability. Limited partners have limited liability but must play no part in day to day management or the benefits of limited liability are lost. ■ Potentially difficult to raise external loan finance as lacks a separate legal identity and does not own assets – it cannot grant a floating charge as security for financing. ■ Any change to identity of JV parties will entail a new partnership arrangement which can be an expensive and time-consuming process.

What does a typical JV Agreement include?

Whatever structure is chosen the parties will have to agree the terms which will govern their relationship as each party needs to be satisfied it can control management of the project in key areas. Typically an agreement might restrict:

- the sale or purchase of assets or rights
- any compromise or settlement of disputes
- operational expenditure over a set threshold, or
- the assumption of debt

without the prior approval of both parties.

There will also need to be provision for dispute resolution between the parties themselves, default by either party and for exit from or termination of the agreement.

Further information

There are many commercial, legal, tax and regulatory factors which play their part in determining the most appropriate structure for a particular joint venture. If you would like any further information on development structuring options or any other aspect of a joint venture, please speak to your usual contact at Burges Salmon or:

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