PHILIPPINE COMPETITION COMMISSION
Ensuring businesses compete and consumers benefit

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PCC GUIDELINES ON NOTIFICATION OF JOINT VENTURES

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1. INTRODUCTION

1.1 These Guidelines on Joint Ventures ("JV Guidelines") are issued pursuant to the power of the Philippine Competition Commission ("Commission") to issue guidelines for the effective enforcement of Republic Act No. 10667, or the Philippine Competition Act (the "Act"), specifically, Section 17 of the Act. These Guidelines are issued to supplement the Rules on Merger Procedure and Merger Review Guidelines.

1.2 These Guidelines shall apply to all joint ventures as defined under the Implementing Rules and Regulations of the Act ("IRR"), between public or private entities, including those sanctioned by other laws, rules and regulations. The purpose of the Guidelines is to aid parties in assessing whether their proposed transaction is required to be notified as a joint venture.

1.3 Joint ventures and other similar kinds of collaborative agreements are used to conduct business projects to generate economic benefits through pooling of assets, skills and resources. The benefits include streamlined processes, eliminated redundancies and cost savings to market players.

1.4 While recognizing that joint ventures can result in business efficiencies, the Commission is mindful that such agreements may pose competition concerns when they may result in a substantial lessening of competition ("SLC") in the relevant market.

1.5 As joint ventures involve obtaining control over an entity by two or more entities, or joining of two (2) or more entities into an existing entity or to form a new entity, they would be considered a merger and, in turn, subject to the compulsory notification requirement under Section 17 of the Act if the thresholds are met.

1.6 These Guidelines offer clarification and explanation with regard to (i) joint ventures; and (ii) the application of the thresholds under the IRR to joint ventures.

1.7 Collaboration agreements between economic agents can take many different forms. In applying these Guidelines, the facts and circumstances of each case will be considered, taking into consideration that not all competition issues that may arise in a joint venture can be covered and they do not set a limit on the investigation and enforcement activities of PCC. Entities who are in doubt about how they and their commercial activities may be affected by the Act may wish to seek legal advice.

1.8 The Commission will consider each joint venture with due regard to the attendant circumstances, including the information available and the time

constraints, and will apply these guidelines flexibly, or where appropriate, deviate therefrom.

1.9 An agreement that does not qualify as a joint venture as clarified under these Guidelines may, however, be subject to Section 14 of the Act.

1.10 Any legal concept, definition or clause used under these Guidelines shall only apply in the conduct of merger review.

2. DEFINITION OF TERMS

2.1. For purposes of these Guidelines, the following terms shall mean:

(a) *"Entity"* refers to any person, natural or juridical, sole proprietorship, partnership, combination or association in any form, whether incorporated or not, domestic or foreign, including those owned or controlled by the government, engaged directly or indirectly in any economic activity.

(b) *"Joint Venture (JV)"* refers to a business arrangement whereby two or more entities or group of entities contribute capital, services, assets, or a combination of any or all of the foregoing, to undertake an investment activity or a specific project, where each entity shall have the right to direct and govern the polices in connection therewith, with the intention to share both profits and risks and losses subject to agreement by the entities.

(c) *"Contractual JV"* refers to a legal and binding agreement under which the contributing entities shall perform the primary functions and obligations under the JV Agreement without forming a JV Company.

(d) *"JV Company"* refers to a juridical entity formed, organized or existing under Philippine laws, or under laws other than those of the Philippines.

(e) *"Joint Venture Partners" or "JV Partners"* are entities intending to form part of a JV Company or Contractual JV, whether existing or yet to be formed.

(f) *"Control"* refers to the ability to substantially influence or direct the actions or decisions of an entity, whether by contract, agency or otherwise as defined under Section 4(f) of the Act.

3. FILING A NOTIFICATION IN JOINT VENTURE TRANSACTIONS

3.1. This part provides an account of the application process, explaining how parties to a JV should make a merger notification. It also sets out the

process for the determination of sufficiency of the submitted filing to the Commission.

3.2. A JV may be formed (i) by either incorporating a JV Company, (ii) entering into a Contractual JV, or (iii) by acquiring shares in an existing corporation.

3.3. In determining whether an acquisition of shares in an existing corporation constitutes a JV or an acquisition of shares under Rule 4, Section 3 (b)(4) of the IRR, it must be examined if joint control will exist between or among the new and existing JV Partners as provided under Section 5 of these Guidelines.

3.4. In the absence of joint control, the relevant thresholds for acquisition of shares shall be applied to determine if the transaction should be notified to the PCC.

A. Formation of a JV Company or a Contractual JV

Joint Venture Between Gugo Inc. and Ion Chemicals

Gugo, Inc. ("Gugo") is a Philippine company engaged in the manufacturing, packaging, and distribution of premium all-natural shampoos and conditions. Ion Chemicals ("IC") is a Philippine company engaged in the manufacturing, packaging and distribution of chemical commercial shampoos.

Gugo and Ion Chemicals decided to form a Joint Venture Company, "Friendship Plastics, Inc." ("Friendship") to manufacture shampoo bottles (refer to **Figure 1**).

Example 1: For the year 2017, Gugo, Inc. recorded Five Billion Two Hundred Thousand Pesos (PhP 5,000,200,000.00) in gross sales. Gugo and IC have agreed to initially contribute an aggregate One Billion and Eight Hundred Thousand Pesos (PhP 1,800,000,000.00) and for each to make an additional contribution of Two Hundred Fifty Million Pesos (PhP 250,000,000.00) in two (2) years.

For purposes of filing a notification with the PCC, Gugo and IC shall submit their respective notifications as the Acquiring Entities. In lieu of the notification form to be submitted by Friendship as an Acquired Entity, Gugo and IC must submit the information and documents enumerated in Section 3.7. below.

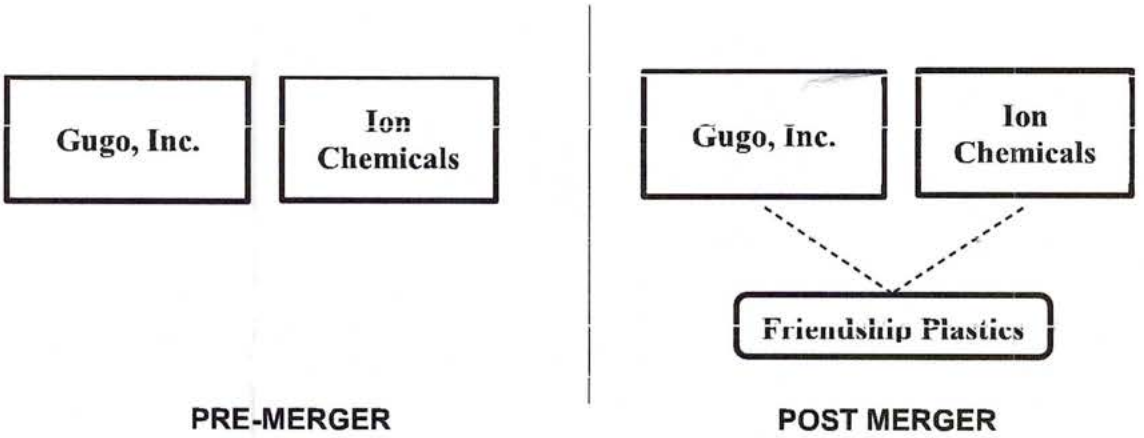

Figure 1. Creation of a Joint Venture

3.5. Entities to a proposed JV that satisfy the thresholds in Section 3 of the Implementing Rules and Regulations[1] are required to notify the Commission. If notice is required, then all acquiring and acquired pre-acquisition ultimate parent entities ("UPEs") or any entity or entities authorized by such UPEs to file notification on its behalf must each submit a Notification Form and comply with relevant rules and procedures. For purposes of notifying a proposed JV, the JV Partners shall be deemed as the Acquiring Entities while the JV Entity is the Acquired Entity.

3.6. All entities whether directly or indirectly controlled by the UPE of each Acquiring and Acquired Entities shall form part of their respective Notifying Group.

3.7. If the JV Company or a Contractual JV is yet to be formed, only the Acquiring Entities are required to file their notification forms. In lieu of the notification form of the Acquired Entity, however, each JV Partner must submit the following information accompanied by all the relevant documents:

a. Business objectives or purposes of the JV;
b. Term of the JV;
c. Degree of participation and management roles of each JV partner;
d. Respective rights and powers in the management of the JV;
e. Defined combination or contribution of assets;
f. Division of profits, risks, and losses;
g. Dispute mechanism to avoid deadlock or litigation;
h. Termination or liquidation of the JV Company and/or relevant buy-out provisions;
i. Terms of confidentiality and non-compete clauses; and
j. Indemnification mechanisms.

[1] R.A. 10667.

B. Acquisition of shares in an existing Entity

3.8. In the case of acquisition of shares in an existing Entity, the prospective JV Partners are the Acquiring Entities. The Acquired Entity shall be the existing Entity, as well as the existing shareholder/s exercising control over such Entity. For this type of transaction, all the Acquiring and the Acquired Entities must file their respective notification forms.

3.9. Where a transaction is notified as an acquisition of shares, but is determed by the Mergers and Acquisitions Office as a JV, the parties will be required to notify as a JV.

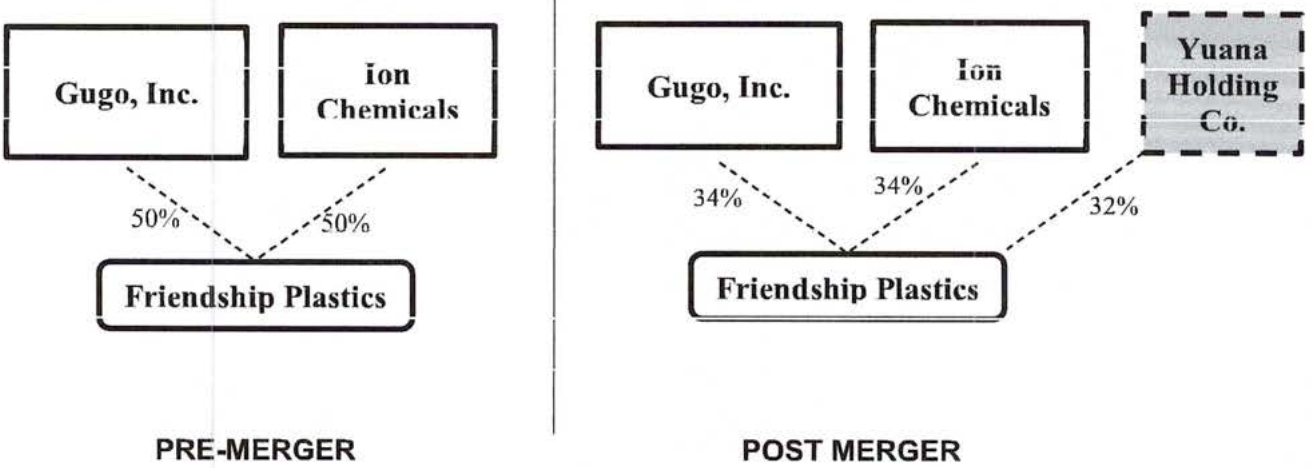

Figure 2. Acquisition of shares in a joint venture

Example 2: Suppose that after the formation of Friendship Plastics JV, Yuana Holding Co. ("Yuana") proposed to acquire shares in Friendship Plastics from Gugo and IC. To facilitate Yuana's entry as a JV Partner, Gugo and IC each sold 16% of its shares to Yuana (see **Figure 2**). Post-merger, Yuana will hold 32% of shares in Friendship Plastics. The remaining shares will be owned equally by Gugo and IC, or 34% each.

Assuming that, post-transaction, there will be joint control among Gugo, IC, and Yuana over Friendship Plastics in accordance with Section 5 of these Guidelines, the Acquired Entities are Friendship Plastics, Gugo and IC, while the Acquiring Entity is Yuana.

4. BASIS FOR COMPUTATION OF THRESHOLDS

4.1. As provided under the IRR and Memorandum Circular No. 18-001, JV transactions must be notified with the Commission when parties to a joint venture meet the size of party and size of transaction test.[2]

A. Size of party test

4.2. A proposed JV meets the size of party test when the aggregate annual gross revenues in, into or from the Philippines, or value of assets in the Philippines of the ultimate parent entity of at least one of the acquiring or acquired entities, including that of all entities that the ultimate parent entity controls, directly or indirectly, exceeds Five Billion Pesos (PhP 5,000,000,000.00).

B. Size of transaction test

i. Formation of a joint venture

4.3. In addition to the size of party test, for a JV to be subject to compulsory notification, (i) the aggregate value of the JV Partners' assets that will be combined in the Philippines or contributed into the proposed JV should exceed Two Billion Pesos (PhP 2,000,000,000.00), or (ii) the gross revenues generated in the Philippines by assets to be combined in the Philippines or contributed into the proposed JV exceed Two Billion Pesos (PhP 2,000,000,000.00).[3]

> Assets refer to tangible and intangible assets. *(Sections 2.19 – 2.21, p. 5, Guidelines on the Computation of Merger Notification Thresholds)*

ii. Acquisition of shares in an existing Entity

4.4. In the case of a formation of a JV through acquisition of shares in an existing corporation or JV Company, the assets to be combined or contributed through such acquisition will include the assets or gross revenues generated by such assets of the existing corporation or JV Company.

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[2] *See* Rule 4, Section 3 of the Rules and Regulations to Implement the Provisions of Republic Act No. 10667 or the Philippine Competition Act approved May 31, 2016 (IRR).
[3] *See* Rule 4, Section 3 (d) of the IRR.

Example 3: In the given Example above (refer to **Example 2**), instead of selling a portion of Gugo and IC's respective shares in Friendship Plastics, the Board of Directors of Friendship Plastics approved an increase in its authorized capital stock which Yuana agreed to subscribe to for the amount of Five Hundred Million Pesos (PhP 500,000,000.00).

In determining the size of transaction test in an acquisition of shares in an existing JV Company, the aggregate initial and additional contributions of Gugo and IC and the additional contribution of Yuana to Friendship Plastics shall be the basis thereof. Thus, the aggregate size of transaction is valued at Two Billion Five Hundred Fifty Million Pesos (PhP 2,800,000,000.00).

4.5. Joint ventures are formed by JV Partners with the purpose of exercising joint control over the JV business and operations. Subject to the provisions contained in Section 5 of these Guidelines, JV Partners are presumed to acquire joint control whether through the formation of the JV or through the acquisition of shares in an existing entity conferring joint control, post-transaction.

4.6. Consequently, in an acquisition of shares in an existing entity, there is no minimum percentage of shares that must be acquired to establish joint control.

4.7. When a proposed JV is undertaken by JV Partners operating outside the Philippines and they agree to combine their assets in the Philippines, the joint venture transaction is likewise notifiable should the aggregate value of assets to be combined in the Philippines or the gross revenues generated by the assets to be combined in the Philippines exceed Two Billion Pesos (PhP 2,000,000,000.00).

Example 4: Assume that Gugo and IC are operating its businesses in China. However, Gugo has a manufacturing facility in the Philippines whose value exceeds Two Billion Pesos (PhP 2,000,000,000.00). Gugo and IC agreed to form a joint venture, "Friendship Plastics, Inc." which shall take over the manufacturing of shampoo bottles in several jurisdictions, including the Philippines.

For the year 2016, Gugo, Inc. recorded worldwide sales of Five Billion Two Hundred Thousand Pesos (PhP 5,200,000,000.00). In this scenario, the formation of the JV is subject to compulsory notification since Gugo and IC will combine assets in the Philippines exceeding Two Billion Pesos (PhP 2,000,000,000.00).

4.8. Pursuant to Rule 4, Section 3 (d) of the IRR, in determining assets of the JV, the following shall be included:

(a) All assets which the JV Partners agreed to transfer, or for which agreements have been secured for the JV to obtain at any time, whether such entity is subject to the requirements of the Act;

(b) Any amount of credit or obligation of the joint venture which a contributing entity has agreed to extend or guarantee shall also be included in the computation of the aggregate contribution

4.9. A JV Partner may opt to defer its contribution to the joint venture. Such deferred contribution forms part in determining the amount of contribution to the joint venture as assets which the JV Partner agreed to transfer, *Provided*: such contribution is contemplated in the JV agreement.

4.10. Should the JV Partners agree to transfer assets which, in effect, constitute successive contributions not included in the JV agreement, such subsequent transfer of assets expressly contained in any subsequent agreement shall be treated as part of the JV agreement, *Provided*: the subsequent agreement is executed within one (1) year from the JV agreement. Thus, the JV Partners are required to notify should the initial and successive contributions exceed Two Billion Pesos (PhP 2,000,000,000.00).

4.11. In the event that the JV Partners agree to transfer assets subject to conditions that may or may not occur, the JV Partners are required to notify the Commission within thirty (30) days from the fulfillment of such condition, *Provided*: that the combined initial and the conditional contribution(s) exceed Two Billion Pesos (PhP 2,000,000,000.00).

> Example 5: Suppose that Gugo and IC decided to launch a new product, "Shamao" and "Fluri", a new line of affordable all-natural shampoo and conditioner. Friendship Plastics shall operate a separate distribution facility which shall cater directly to retailers and wholesalers. To be able to successfully launch such product into the market, Gugo agreed to contribute a 1,500-hectare property where a distribution facility will be constructed for Friendship Plastics to be able to expand in the Visayas Region. The value of the contributed asset is One Hundred Million (PhP 100,000,000.00). In addition, the Board of Directors of Friendship Plastics increased its authorized capital stock to which Gugo and IC subscribed to an aggregate of Five Hundred Million (PhP 500,000,000.00).
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> The transfer of significant additional assets and the aggregate assets of Friendship Plastics shall be notifiable if it meets the size of transaction test. In this example, the aggregate additional assets is valued at Six Hundred Million pesos (PhP 600,000,000.00) and the aggregate assets of Friendship Plastics is valued at Two Billion and Three Hundred Million pesos (PhP 2,300,000,000.00). Thus, the transfer of such assets together with the aggregate assets of the JV Company meets the size of transaction test.

4.12. For purposes of determining the aggregate value of the assets or revenues generated by assets in the Philippines to determine the size of the transaction, the Guidelines on the Computation of Merger Notification Thresholds shall be applied.

5. ELEMENT OF JOINT CONTROL

5.1. In determining whether a JV is subject to merger notification, the Commission shall asses and evaluate if the Joint Venture is subject to **joint control** post-transaction.

5.2. In the context of JVs, joint control refers to the ability of the JV Partners to substantially influence or direct the actions or decisions of the joint venture, whether by contract, agency or otherwise.

5.3. Joint control exists when an entity has the ability to determine the strategic commercial decisions of the joint venture (positive joint control), or to veto such strategic decisions (negative joint control). Consequently, in determining strategic commercial decisions and policies of the JV, the JV Partners must reach a consensus between or among them.

5.4. Positive joint control is normally carried out by acquiring or possessing the majority of voting rights in a joint venture.

5.5. The exercise of veto power granted to JV Partners is a form of negative joint control. The veto power allows the holder to use the threat of creating a deadlock situation to determine the strategic behavior of the joint venture.

5.6. Joint control may be established on a *de jure* or *de facto* basis. Forms of joint control may be seen in the equality of voting rights or appointment to decision-making bodies, veto rights, joint exercise of voting rights, or in similar or analogous cases.

5.7. Thus, equity ownership does not solely establish the presence or absence of joint control. The Commission recognizes that although a JV Partner has a minority stake in the JV, it may still exercise substantial influence on the JV. Substantial influence can mean the power to direct or block actions that determine the strategic commercial decisions and policies of the JV.

(a) Equality in voting rights

5.8. Joint control is apparent in instances where there are only two JV Partners having equal voting rights in the joint venture and none has a casting vote. Equality in voting rights also exists when the JV Partners to the joint venture each have the right to appoint an equal number of members to decision-making bodies.

5.9. Such arrangement may or may not be embodied in a formal Agreement between the parties to the joint venture.

(b) Veto Rights

5.10. Veto rights refer to the power of a JV Partner to halt certain decisions or policies of the joint venture or any similar power granted to a JV Partner.

5.11. Joint control may still exist even in the absence of equality in votes or in representation in the board of directors or other decision-making bodies. Instances where minority shareholders have additional rights which allow them to veto decisions can confer joint control if such decisions are essential for the strategic commercial behavior of the JV. The veto rights may operate by means of a specific quorum required for decisions taken at the shareholders' meeting or by the board of directors. Strategic decisions can also be subject to approval by a body, where the minority shareholders are represented and form part of the quorum needed for such decisions.

5.12. The veto rights may be conferred in an agreement between the JV Partners or in the statute of the JV.

5.13. It must be emphasized that not all forms of veto rights confer or establish joint control. Such veto rights must be related to strategic decisions in the business policy or activities of the joint venture. This includes decisions on issues such as the appointment of corporate officers or key management personnel, determination of the budget, adoption of and amendments to the business plan and other similar aspects of business management.

i. Appointment of corporate officer or key management personnel and determination of the budget

5.14. The power to determine the members of the Board, or key management personnel, usually confers upon the holder the power to exercise decisive influence on the strategic commercial decisions of a JV Company, and thus may be sufficient to confer joint control. Similarly, veto rights conferring the power to veto a proposed budget is sufficient to confer joint control over the JV, since the budget determines the framework of the activities of the JV and the investments it may make.

iii. Adoption of and amendments to the business plan and other similar aspects of business management

5.15. The business plan normally provides the details of the aims of a JV company together with the measurers to be taken in order to achieve those aims. Thus, a veto right conferred over such business plan may be sufficient to confer joint control even in the absence of any other veto right.

5.16. Veto rights over specific decisions critical or essential for the JV in the particular market it operates or will operate may be an important element in establishing the existence of joint control.

5.17. There is no requirement for a minority shareholder to have all the veto rights mentioned above to establish joint control. In some instances, it may be sufficient that one such right exists, depending upon the content of the veto right and the importance of this right in the context of the specific business of the JV.

iv. Veto rights not sufficient to confer joint control

5.18. Veto rights allowing minority shareholders to prevent the sale or winding-up of the business, changes in the statute, investment of corporate funds

in another corporation or business or increase or decrease in the capital stock, are not normally sufficient to confer joint control.

5.19. For investment of corporate funds to sufficiently confer joint control, such investment must constitute an essential feature of the market in which the JV is active or intends to operate. The veto right conferred in relation to such investment must be specific and would affect the behavior of the JV Company in such market.

5.20. In other instances, veto rights conferred upon minority shareholders with respect to investment of corporate funds are considered as a right normally conferred upon them. Thus, it does not, in itself, establish the existence of joint control.

5.21. It is not required that the JV Partner has the power to exercise influence on the day-to-day operations of the JV. What is crucial is that the JV Partners are able to exercise such influence in relation to the strategic business behavior of the joint venture through such veto rights. The possibility of exercising influence or the mere existence of the veto rights is sufficient to establish the existence of joint control.

(c) Joint Exercise of Voting Rights

5.22. Even in the absence of specific veto rights, two or more minority shareholders may obtain joint control in the JV in instances where the minority shareholdings provide for the means of controlling the JV. The cooperating minority shareholders between them will have a majority of the voting rights, and agree to act together in the exercise of voting rights. This may be established through an agreement, or it may be established on a *de facto* basis.

5.23. The joint exercise of voting rights may be exercised in the form of a holding company in which voting rights are transferred by the minority shareholders, or a pooling agreement by which the minority shareholders undertake to act in the same way. It can occur on a *de facto* basis where strong common interests exist between the minority shareholders such that they would not act against each other in exercising their rights.

5.24. Strong commonality of interests may be seen in the existence of mutual dependency between the shareholders to reach the strategic objectives of the JV. For example, each JV Partner's contribution to the JV is vital for its operations (e.g. technologies, access to market, local know-how), such that the JV Partners can operate the JV successfully only with each other's agreement on strategic decisions, even without provision for veto rights.

5.25. Such a scenario also applies when a majority shareholder is highly dependent on a minority shareholder.

(d) Other Similar or Analogous Cases

5.26. Passive investment in a joint venture does not preclude the existence of joint control. A party to a joint venture may opt not to participate in the management of the joint venture. However, joint control may still exist when the

passive JV Partner retains power to contest decisions or policies undertaken by other JV Partners to the joint venture as discussed in these Guidelines.

5.27. The examples set herein is without prejudice to other similar or analogous cases of joint control which may be established by an independent assessment and analysis of the Mergers and Acquisitions Office.

5.28. The review of a proposed JV transaction shall be conducted in accordance with the Merger Review Guidelines and the Rules on Merger Procedure. If the JV does not meet the criteria set forth in these Guidelines, such does not preclude the Commission from initiating a *motu proprio* investigation pursuant to its powers under Rule 4, Section 1 of the IRR.

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