Disputes Digest | Joint Venture Agreement: Personal Claim or Derivative Action?

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Overview

Can a joint venture partner pursue a personal contractual claim against its fellow joint venturers to recover funds advanced under a joint venture agreement, or must the claim be pursued by way of a derivative action on behalf of the joint venture company?

In ***Pelorus Holding Sdn Bhd v Jaffa Roger Dawkins & Ors***[1], the Federal Court ("**FC**") considered whether the appellant ("**Plaintiff**") was confined to pursuing a derivative action in the name of the joint venture company, to the exclusion of any personal contractual cause of action under the joint venture agreement ("**JVA**").[2]

The FC answered the question in the negative. It held, amongst others, that the Plaintiff's claims were rooted in the JVA, which created distinct, direct and enforceable personal obligations between the contracting parties[3].

The FC distinguished between:
(1) a claim seeking to vindicate a right belonging to a company, which may be pursued through a derivative action where the statutory requirements are met; and
(2) a claim arising from an independent contractual cause of action belonging personally to the claimant.

The decision demonstrates that the mere involvement of a joint venture company, or the fact that the company may have suffered concurrent loss, does not automatically convert a personal contractual claim into a derivative action. The determining consideration is the substantive nature of the rights being enforced, the obligations giving rise to the claim and the loss sought to be recovered[4].

BRIEF BACKGROUND FACTS[5]

The Plaintiff entered into a JVA with the 1st and 2nd respondents (collectively, "**D1&D2**") to establish a joint venture company ("**the JV Company**"). D1&D2 were shareholders and directors of the 3rd respondent ("**D3**"). The JVA set out, amongst others, the objectives of the JV Company and the composition of its Board.

Pertinently, the JV Company had already been incorporated before the JVA was executed, but was **not made a party to the JVA**.

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[1] *Civil Appeal No. 02(f)-51-11/2024(B)*
[2] ibid, para [23]
[3] ibid, paras [24] – [30]
[4] ibid, paras [62] – [65]
[5] ibid, paras [2] – [10]

The Plaintiff provided financial resources for the venture. Over time, the relationship between the parties deteriorated, and the Plaintiff alleged that the JV Company had not been managed in accordance with the JVA.

The Plaintiff commenced proceedings in the High Court seeking, amongst others:

- repayment of the RM1,000,000.00 loan advanced to D3;
- repayment of RM516,972.02 advanced to the JV Company;
- RM1,188,691.94 allegedly belonging to the JV Company but diverted for the benefit of D3; and
- RM1,213,060.00 advanced to D1&D2 and D3 to service D3's Agrobank loan.

D1&D2 and D3's principal defence was that the Plaintiff lacked the locus standi to pursue claims in its personal capacity, on the basis that the alleged losses were suffered by the JV Company. Accordingly, any action had to be brought by the JV Company itself, or where appropriate, by way of a derivative action. The JV Company subsequently intervened and brought a counterclaim on the same basis.

LOWER COURT DECISIONS[6]

HIGH COURT ("HC")	COURT OF APPEAL ("CA")
The HC allowed the Plaintiff's claims in **part,** finding, amongst others, that D1&D2 and D3 were liable for the sums claimed. It also dismissed the JV Company's counterclaim.	The CA allowed the appeal **in part,** while affirming the dismissal of the JV Company's counterclaim. The CA, amongst others, upheld the RM1,000,000.00 claim based on personal guarantees given by D1&D2, but found the RM516,972.02 claim unsubstantiated. Importantly, the CA held that the remaining claims concerned sums belonging to the JV Company and therefore had to be pursued by the JV Company itself, either through a direct or derivative action.

FEDERAL COURT DECISION: SPOTLIGHT

The central question of law before the FC was:

> "*… whether the Plaintiff was confined to pursuing a derivative action in the name of the JV Company, to the complete exclusion of any personal cause of action in contract under the JVA.*"[7]

The FC answered the question in the **negative**.

[6] ***Pelorus Holding*** (n 1), HC at para [11] – [12]; CA at para [13] – [14]
[7] ibid, para [23]

(1) Independent personal contractual rights under the JVA

The FC drew a distinction between rights belonging to the JV Company and the Plaintiff's independent contractual rights under the JVA. The distinction was central to the application of the rule in ***Foss v Harbottle***[8] and the statutory derivative action mechanism under s.347 of the Companies Act 2016 ("**CA 2016**").

Generally, the rule in ***Foss v Harbottle*** prevents a shareholder from bringing a personal action to recover losses that are merely reflective of losses suffered by the company. Such claims must ordinarily be brought by the company itself. A derivative action enables a qualifying shareholder, subject to the requisite statutory requirements, to enforce such rights on behalf of the company.[9]

However, the FC found that the Plaintiff was merely seeking to enforce the personal and distinct obligations undertaken by D1&D2 as contracting parties and co-joint venturers under the JVA.

Significantly, the JV Company had already been incorporated before the execution of the JVA. The parties therefore entered into the JVA with actual knowledge of the JV Company's existence, yet deliberately chose not to make it a party to the JVA[10]. The FC regarded this as a clear indication of the parties' intention to assume contractual obligations towards one another:

> "*…the significance of not including the JV Company in the JVA cannot be overstated. It directly undermines the defendants' invocation of the corporate form as a shield against personal liability."*[11]

(2) The Plaintiff's loss was direct and personal

Further, the FC held that the losses claimed by the Plaintiff were personal, direct and legally distinct from any loss that may have been suffered by the JV Company.

The Plaintiff was not seeking recovery of any diminution in the value of its shareholding or any dividends or profits belonging to the JV Company. Rather, the Plaintiff sought, amongst others, the return of its own capital and advances pursuant to the personal obligations undertaken by D1&D2 under the JVA.[12]

In this regard, the FC emphasised the fact that certain funds had passed through the JV Company's accounts did not, by itself, "*transform a personal contractual claim into a derivative one*". The critical question, instead, was: [13]

> "*… not through whose account the funds transited, but from whose pocket the funds were extracted and to whom the personal obligations of repayment were owed."*

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[8] (1843) 2 Hare 461
[9] ***Pelorus Holding*** (n 1), para [33] – [35]
[10] Ibid, paras [26] – [27]
[11] ibid, para [29]
[12] ibid, paras [52] – [55]
[13] ibid, paras [56] – [59], in particular para [59]

Here, the FC found that the Plaintiff's own funds had been solicited, received and misapplied in breach of personal obligations undertaken by D1&D2 under the JVA. The loss therefore flowed from an independent contractual wrong suffered by the Plaintiff, rather than from an injury to the JV Company's assets.[14]

Accordingly, the FC held that the Plaintiff was not required to pursue its claims through a derivative action under s.347 CA 2016. The fact that the JVA may have also caused harm to the JV Company does not convert a joint venture's partner claim under the JVA into a derivative one or extinguish the claim altogether[15].

To confine the Plaintiff exclusively to the derivative route would, in the FC's view, defeat the contractual rights which the parties had expressly undertaken.[16]

(3) Illegality of the transactions

D1&D2 and D3 also argued that certain advances made by the Plaintiff constituted unlawful moneylending and were therefore unenforceable.

The FC accepted that illegality may be considered by the court even where it had not been pleaded. However, the FC found that no illegality had been established on the facts.

In particular, the relevant advance to D3 was made pursuant to the contractual arrangements under the JVA and formed part of the Plaintiff's performance of the joint venture arrangements. It was therefore not an independent moneylending transaction. In this regard, the FC distinguished *Triple Zest Trading & Supplies & Ors v Applied Business Technologies Sdn Bhd*[17] and was not prepared to extend its reasoning to funding arrangements integral to the implementation of a joint venture, as doing so could potentially expose ordinary funding by joint venture partners to characterisation as unlawful moneylending.[18]

CONCLUSION

Accordingly, the FC allowed the appeal in respect of the RM1,188,691.94 and RM1,213,060.00 claims, upheld the RM1,000,000.00 claim based on the personal guarantees, and dismissed the appeal in respect of the RM516,972.02 claim as unsubstantiated.

The FC's decision highlights the distinction between a shareholder seeking to vindicate a right belonging to a company and a contracting party seeking to enforce its own contractual rights. It clarifies that a joint venture partner is not necessarily confined to a derivative action where it seeks to enforce personal contractual rights under a JVA. The court will examine, amongst others, the substance of the contractual arrangements, the obligations undertaken by the parties and the nature of the loss claimed, notwithstanding the involvement of a separate corporate vehicle in implementing the joint venture.

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[14] ***Pelorus Holding*** (n 1), paras [43], [60] – [65]
[15] ibid, para [76(e)]
[16] ibid, paras [36] – [38], [48]
[17] [2023] 6 MLJ 818
[18] ***Pelorus Holding*** (n 1), paras [70] – [73]

Key Takeaways 💡

- ✓ **The contractual source of the claim matters.**
  A joint venture agreement may create distinct and enforceable personal obligations between its contracting parties, giving rise to a personal contractual cause of action upon breach.

- ✓ **The nature of the loss matters.**
  A claim arising from direct and personal loss suffered pursuant to an independent contractual cause of action is distinct from a claim seeking to recover losses suffered by the company.

- ✓ **Corporate structure does not automatically determine the cause of action.**
  The mere existence of a separate joint venture company does not, by itself, confine a joint venture partner to a derivative action. The court will examine the substance of the contractual arrangements and the rights sought to be enforced.

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This is a summary for general reference and does not constitute formal legal advice. Kindly refer to the full judgment and reasoning in ***Pelorus Holding Sdn. Bhd. vs Jaffa Roger Dawkins & Ors [Civil Appeal No. 02(f)-51-11/2024(B)]****.*