Technology Transfer through Joint Venture
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Lecture – 07
Types of Joint Venture [JV]

I welcome you in the seventh lecture of technology transfer through strategic alliance and joint venture. In the last lecture I have started talking with you regarding the joint venture. I am going to continue with that topic, and now I will specifically concentrate my talks on types of joint venture.

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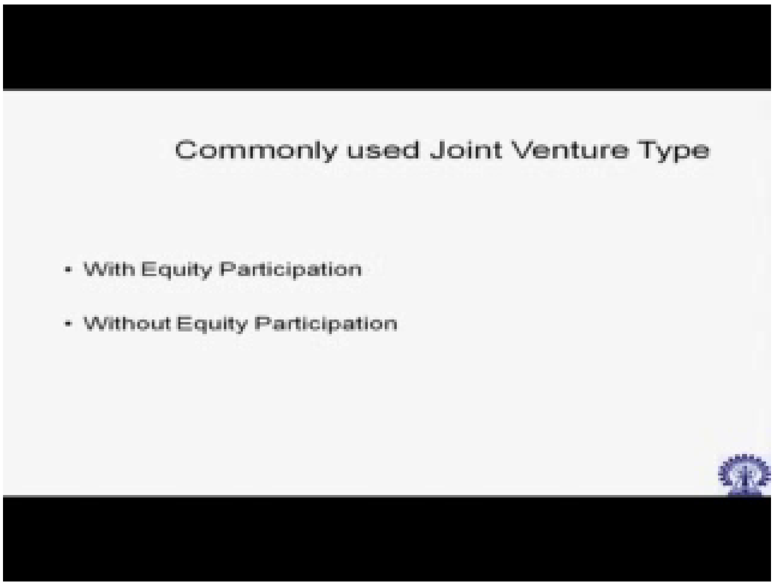

Now, in generally there are two types of joint venture which is, popularly used in Indian market. The first type of joint venture is known as joint venture with Equity Participation and another type of the joint venture is known as without Equity Participation. So, let me explain this two concept what is Equity Participation and what is the joint venture without Equity Participation.

Then, in the last lecture I have said that, you know one of the important criteria to understand that particular agreement lead to the joint venture or not, is there should be some kind of sharing of control and some kind of sharing of liability and that is what supreme court held in a case which I have mentioned in my last lecture. So, when we are talking about Equity Participation we basically talk about the control which both the partner will have into a joint venture entity or the business organization which it forms as the part of the joint venture. Now when we are talking about the Equity Participation we are not really confine ourselves in already the capital instrument, but it can be even kind of a hybrid instrument too were in you try to have a control over the management of the new entity which is coming out of the joint venture agreement.

So, in case of a Equity Participation, your partner not only bring the technology or the knowhow, but at the same time they also make an investment into the new entity. Now if you do have the control over the new entity through your investment, then you have a greater access over the market which you wanted to penetrate in a different territory. So, the foreign partners always want that there should be some kind of control in the new business entity which is coming out of this joint venture agreement.

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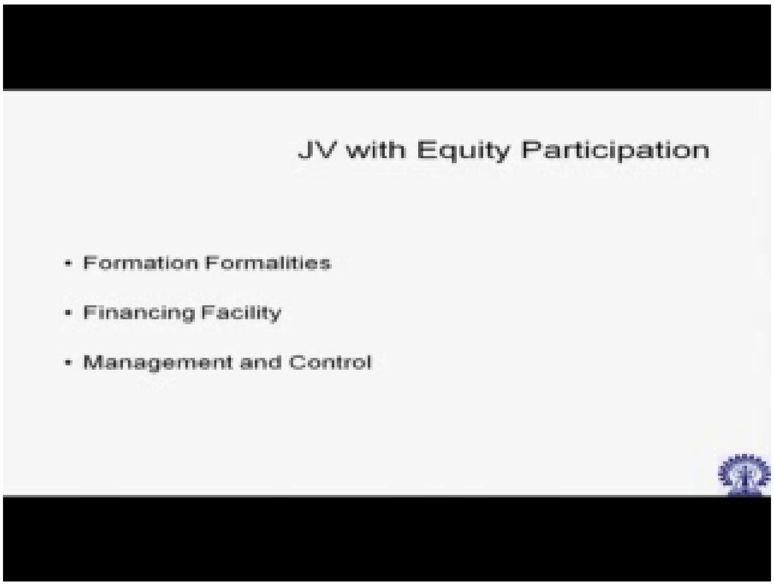

Now, in joint venture with Equity Participation it might required to have some kind of more clarity into this understanding and we can divide this joint venture with a Equity Participation into a 3 broad heading first one is formation formalities second one is financing facility and the third one is management control. Now let me explain to you the formation formalities.

Now, if you remember in the last lecture, I was talking with you joint venture option and therein I said that the outcome of joint venture agreement may lead to formation of association of person, may lead to formation of the partnership and may lead to formation of the company. Now, whatever the form it takes you need to have a formalities to complied with like I have said, some of these business organization or the business form joint venture takes is governed by a particular organisation law like if we talk about the association of the person, many of the time you will find it governed by societies act or the cooperatives act of a particular state as well as the federal laws.

Now, if it is a partnership then again it will be governed by the partnership act and it is a limited liability partnership then it will be governed by limited liability partnership act and if it is a company then again it will be governed by the companies act. So, all this particular act basically provide some kind of a formality requirement; that means, before you incorporate any of this particular business form, you need to go through the series of step which you need to comply because the law mandate that. So, the formalities requirement is one of the important issues in case of the joint venture agreement relating to formation of an organization.

The second issue is, there might be some kind of the sectoral mandate or may be the business segment which you wanted to enter, there is a mended by the regulator that, if you want to incorporate the business it should be of a specific form or specific business organization like sometimes the law prescribe that it should be only a company and it should be only a private limited company or a public limited company. Furthermore it also specifies that what should be the capital requirement for these particular companies. It might also specify that what kind of a human expertization requirement for that type of company.

So, if you want to enter the business in that particular sector in that particular segment then in that case you need to comply that. Apart from that you might required to take permission from the environmental regulators. Whatever you are going to produce, that might affect the local environment or it might potential effect the local environment. If that sure then in that case you need to go for a regulated permission from the environmental regulator of that particular place. Sometimes you will find this regulatory complies requirement is more complex or getting the permission is more complex based on type of the industry you wanted to enter.

The next one might be the permission which you need to take from the fair market regulator popularly which we called it as a Competition Commission of India. If you are entering into a joint venture with a existing plain market and the moment you are entering into a joint venture the concentration of the existing (Refer Time: 08:42) in the market increases and if that is. So, then in that case you need to go back to this fair market regulator and you need to seek the permission that, can you enter into that particular market? Because the fair market regulator will try to understand are you going to polarize the market after these particular joint venture agreements?

So, what I am trying to draw your attention there is a multiple regulator requirement which you might need to comply if you wanted to take if you wanted to incorporate a Formal Business Organization. So, formation formalities is one of the issues which you should be careful in a while you are going for a Equity Participation. I am going to detail more on the choice of law in subsequent lecture of mine. There I am going to you know talk with you that which kind of law you are going to choose or is there in a flexibility to choose a law in a transaction which is in a (Refer Time: 10:05) scenario.

Now let me come into financing facility. Now again this financing facility is highly regulated. If you are entering into a particular sector and if you are entering a joint venture with foreign partner and you are again going for a technology transfer, then there is a several type several financial compliances you need to make.

First of all you need to check that are you allowed to make an investment into a particular segment? So, you need to look into foreign direct investment regulation or you need to look into the RBI guideline or you may need to look into FIPB guideline or you may be look into the government guideline relating to particular sector and the cap which government has suggested, for the particular sector. Second you have to look into is there any restriction has been imposed by Capital Market Regulator for accessing a particular market? That means, if you wanted to bring kind of a FDI and then you want to list that particular company into a stock exchange. Do the security markets regulated prescribe any particular type of regulation which you need to comply? Now sometimes even you will find a Sectorial Regulator which is operating in a particular area prescribed a type of finance which you can seek for from your foreign partner while you are doing the technology transfer.

Now, when I am talking about the type of capital it might be the Equity capital, it might be the date, it might be even convertible debentures or if I go more specific, then even it might prescribe that what classes of Equity you can take? It can also prescribe that; you can take only the shares which do not have a voting right. They can also prescribe that you can take a convertible debenture, but it should be of a particular duration. So, what I am trying to draw your attention even relating to financing facility you might have a lot of restriction even it might also tell you that which are the financial institution you can access for raising the further capital for your business venture. Similarly, if you come into the next point that is the management and control many of the time even the Sectoral Regulator prescribe that what should be the management structure and what should be the control of your foreign partner like a you might be aware of the fact that in the last aviation deal with Jet and Etihad, Jet has allowed to finance by Etihad up to 49%.

So, actually Etihad is not given ultimate control over this particular acquisition or the capital infusion. Though in true sense this was not joint venture because it was not created a new business organization, but in loose term you can say it is a joint venture because in case should joint venture is not always necessary, that you have to have a new business organization. But when we are talking about Equity Participation, we are basically tried to talk about some kind of a control over this particular organization itself.

So, even you know some point of time the government policy might prescribe that what kind of a management control you should have into your venture? Ventures were both the parties are coming together. Now in my lecture whenever I am talking about joint venture or strategical alliance in my last lectures, my specific focus was more on technology transfer issues. The joint venture or strategical alliance is possible beyond the technology transfer. So, you should not be confused that whatever I am telling this is not applicable in the ordinary condition or whatever otherwise I am telling it is not applicable in case of the technology transfer scenario.

You need to understand broader perspective in some cases and in some cases you need to understand in a very specific prospective. So, management and control is one of the important issue in case of Equity Participation. You know if it is PSUs who are going for the joint venture, then these management and control became very very important issue; like if it is 50-50 partnership, then possibly neither of this people have any majority control over the joint venture. So, PSU generally do not prefer that their partner will have same kind of control as they have on that particular company. Now if it is a 51-49 %

joint venture, then may be the person having 51% holding he will have a greater control over that particular joint venture company because it is in majority.

I am going to discuss about this particular model in my subsequent lecture, but never the less what I am trying to drawing your attention that there is a different types of models are available relating to the management control and sometimes even the PSUs do not want that there should be 51% investment by them in the joint venture because the moment they do that, it is become a government company and once it is a government company it is subjected to several restrictions.

So, in case of management and control you need to have a lot of strategy. You need to look into what are the sectoral law prevalent in that particular area? Where you wanted to do the business? Is there any specific law which has been prescribed by the government relating to the foreign direct investment relating to the management and control? Is there any specific policy government is prescribing for a particular segment? Because government wanted to promote that particular segment, one has to be careful in terms in this particular manner.

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Now, let me come into the next issue which is known as joint venture without Equity Participation. Now as I told you in case of the Equity Participation the end result is formal business organization, but in case of the joint venture without Equity Participation there is a no incorporation of business organization as a result of the joint venture. So, it is more like a business relation, were both the party mutually decide that how they are going to operate in the given frame of the agreement joint venture agreement? And these particular relationships may be relating to the sharing of the market, relating to sharing of information, relating to market and understanding of the market. It might be relating to even sharing of the technology. It might be relating to the sharing of a particular supply chain which the local partner uses it. There can be several example of this kind of business relationship, like sometimes you will find the foreign company car company one to penetrate in Indian market and immediately they do not establish the service or post sale service network.

So, what they do in that particular circumstance? They try to create kind of relationship with a existing bid player into that particular market. Then they try to give the service to their customer, postal service. Good example might be the Fiat and Tata. Tata was giving the service of the Fiat cars in the postal service, because Tata has a huge network service network and Fiat thought instead of creating or duplicating this particular facility, let us use this particular service from the Tata themselves. Similarly you will find this kind of business relation in telecommunication sector, like few years back you might heard about the Virgin telecom. Virgin telecom actually launched by Tata telecommunication and what they did? They have actually shared the spectrum as well as year time. So, the Virgin mobiles never created any infrastructure for operation in India. So, you will find there is a many such kind of a example relating to the business relation.

Now, next I might be executing a particular business undertaking. It might show that you wanted to bring some kind of a product into a market and try to promote that particular product in the market or try to customize that with a help of existing player into the market. You will find there is lot of example into the print media relating to that like, a you might heard about this magazine called Reader Digest.

In India reader digest started operating with the particle local group which is very prominent to the print media and with the tablets, because they wanted to bring this customization according to the Indian test of readers. At the same time to make that particular book very popular or the tablets very popular within the Indian readers. You will also find this kind of understanding relating to telecommunication. Different channels which are the foreign companies and they are telecasting their product in Indian market through this particular process. So, actually this is not leading to and they are doing it in the existing platform of their partner in India. So, in this particular kind of joint venture they basically do not incorporate any new business organization and lastly there can be another way to do things it is known as inter-firm co-operative agreement.

Now, through this particular cooperative agreement also, people can carry out the joint venture for both of their benefit. Now it can be sharing of the internal resources. It can be sharing of the knowledge which they have about particular market. It can be sharing of the process, it can be facilitating each other relating to accessing the regulatory barrier and some time people do take a very strategic decision not to form a new company because there might be a regulatory barrier for having a formal organization or even it is allowed to create a formal organization and people if the people duke in corporate of formal organization the entry cost is very high. So, in those circumstances people generally go for this kind of informal relationship which we generally call it as the without Equity Participation, but there is a risk in this kind of relationship. The risk is you might not have any hierarchical control or exposed governance mechanism. But it does not mean that there are no executions of successful a venture through this particular means through this particular process.

So, what my advice is if you are going for non Equity or without Equity Participation joint venture, then in the joint venture agreement itself you clarify this particular process or you create a mechanism how to control or how to participate in decision making or how to carry forward this kind of informal understanding.

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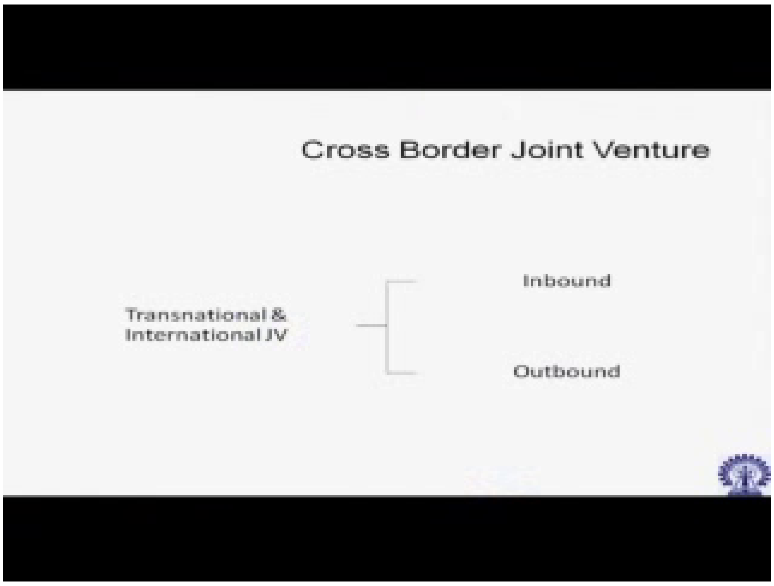

Now, I will take you in the last point of this lecture. This is this is Cross Border joint venture and again you will find we categorize this transnational or the international joint venture into 2 broad category. One is the inbound joint venture and other is the out bound joint venture. Now, when we talk about the inbound joint venture, it basically a company who is coming in and enter into a joint venture in a domestic market when we are talking about the out bound joint venture it means, a domestic company going out in another market and entering into a joint venture.

Now, processes of inbound and outbound joint venture are almost same. You need to go through same kind of agreement, structuring and arrangement. You need to do all the compliances which are required, otherwise for the joint venture, but what further you need to give the attention is that, what are the foreign policies relating to the investment? Is there any bilateral treaty relating to the business between these countries where the inbound or outbound joint ventures is happening? Is that country where you wanted to go or the company which want to come here are under the any international understanding? So, in addition to all joint venture compliances, you are required to understand this international regulations, international treaties or understanding between the countries while you are going for this inbound or outbound joint venture.

Thank you.