Technology Transfer through Joint Venture
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Lecture – 08
Issues Frequently Arise During JV Negotiation

I welcome you in the 8th lecture, relating to technology transfer through strategic alliance and joint venture.

And in this module I was basically discussing with you relating to the joint venture, and now my talk will be more concentrated to issues frequently arise during the joint venture negotiation.

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Now, I believe you need to negotiate the joint venture, before you formalize a terms of joint venture agreement, and before you create a formalised joint venture organization, business organization, and these negotiation can be divided into a couple of heading, which are quite standard, or if you think there is a need to add some more heading you can do it for your convenience, which I generally suggest the people that this is some kind of creating a checklist, or some kind of a key terms which you decide before you go with the joint venture. Now, in some sector, you need this, you need additional key terms, then whatever I am going to discuss with you, and this might be very sector specific. So, I am going to talk with you relating to the valuation issue, then on transparency.

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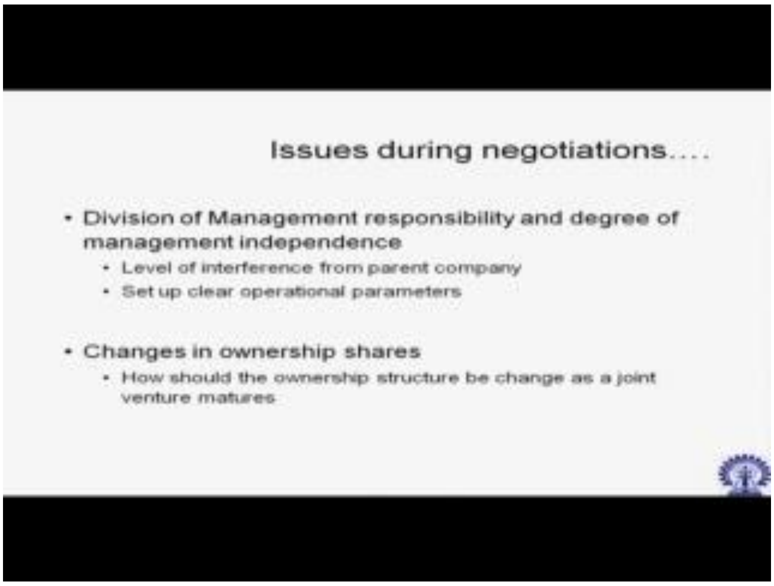

Then I will talk about the division of management and responsibility then I will talk about changes in ownership shares.

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Then I will talk with you dividend policy, and other financial matter, marketing and staffing issue, then operational problem, conflict resolution.

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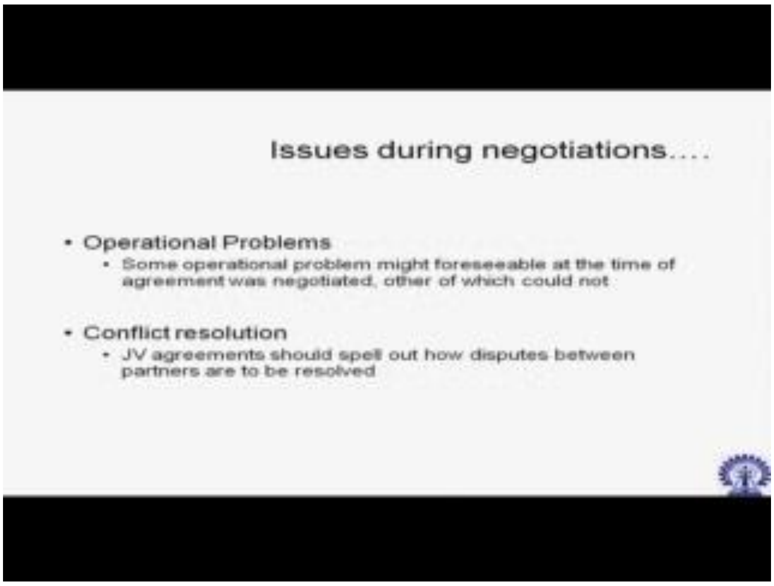

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Problem relating to multi nationalism, when you are doing a cross boundary joint venture, and then the changing relationship which might occur due to the several reason. So, let me take you through one after another; that is relating to valuation of the issues. Now, in the joint venture it is always a difficulty, to assess that what kind of assets you are getting out of that particular joint venture. Or the value you are assigning for the asset which you are getting, are of a after value, or you are paying a higher price for that particular asset itself, because in many of the time the type of assets you are acquiring, there is a no market exist for that kind of asset in that particular market, that you can readily get the reference of the valuation for those particular assets. Sometimes the markets do not develop, because of controlled economy, sometimes markets do not develop on that particular product, because of the command economy.

Sometimes that particular product is quite unknown in that particular market, so there is a no understanding of the value. Then let me give you example of a virtual space. If your partner brings a virtual space, which you are going to use for purpose of developing your product, what kind of value you are going to assign. Because in case of the virtual phase there might be a lot of issues relating to the quality, and that particular quality is embedded in the service which your partner might give or provide during the business. Similarly, if some product which is of a financial in nature, similarly, some product which is best on R and D, similarly, some product which is not a popular in a particular market, there can be several issues relating to determining the worth of the asset, or valuation of the asset, and it can be a tough negotiation between both the partners who ultimately wanted to form a joint venture.

Now, the valuation of the technology, this is another contains such issues. Now you wanted to get a technology from your partner, and that particular technology do not have a known market. Let me give you one example, like you might have seen some company has brought a technology which is called laser keyboard, and you can connect this laser keyboard with your tablet or any mobile device, and you can keep on typing as you do with your normal keyboard.

Now the technology is new, you are not sure how many people will like this particular technology. You will also not sure that in what segment or what type of customers you are going to get for this particular technology. So, in this circumstance valuing that particular technology is very difficult. Maybe tomorrow this might be proved to be a cutting technology, but today nobody knows about the efficiency of this technology, or the convenience which it might provide. So, the market does not exist. Now, this is also, this example can be given in case of the pharmaceutical industry.

Now somebody has brought the insulin which can be consumed through the mouth or by the spray in mouth. So, it relief lot of pain to the people who are suffering from diabetes, but you are not sure that you are going to get the permission of marketing this particular medicine, in how many market in the world. you might say that well I have completed the drug trial in a x country, y country might say that you have not trial that particular drug into a particular environmental condition, and how it is reacting that particular drug on the human on a particular environmental condition that you have not tested, how you are going to price the technology. So, pricing the technology many of the time is a huge concern. Sometimes even the valuation of the equity share of a non listed firm is, very difficult, because you do not know that how people use or how much premium you are going to pay, for the shares which you are acquiring in your target company, or in a joint venture partners company, because there is a no transaction on those particular share. It was closely held by a particular family.

The product which they sell in to the market might have a huge you know market at present, but tomorrow that particular product might not be a good into that particular market. It might so happen that organization is not a very flexible organization to the changes. So, getting the valuation of the equity shares of a non listed firm is sometimes a huge issue.

Now, the next point is the transparency. Getting the data which is based on the, which will be the best for the valuation is always a challenge. The company with whom you are entering into a joint venture, they might not maintain any structure financial information. It might be simply a private limited company. So, they do file annual financial report, but the financial mechanism within the company is not very a robust, or you are entering into a overseas market or a new market where the accounting standard is not developed according to the international standard. So, the company with whom we wanted to enter into relationship, they do not maintain any structural financial information.

Similarly, you release a command economy then you might not find any real market for output, suppliers, or the financial instrument. So, getting some kind of understanding about the equity which you are purchasing, or the asset which you are purchasing, or which you are getting as a joint venture agreement, it is not quite transparent. So, negotiation on the transparency is a contention issue in many joint ventures negotiation.

Now, the next important issue, which you need to sort out as a part of the joint venture, is a division of management responsibility, and degree of management independence. Now it is well established; that joint venture entity will run better, if there is a least interference from it is parent organizations, because one thing you will appreciate that in case of the corresponding joint venture, the parent entity might be staying thousands mile away, and doing a remote control from there, is itself a huge problem, and many of the time the joint venture fails because of that.

So, you need to negotiate hard that how much you should allow to control of the parent company in the joint venture entity. It is always advisable that instead of trying to control your joint venture entity, you set up an operational parameter, which the joint venture entity will follow, and the outcome will be must standardised and desirable than if you do a remote controlling. Then next important thing is change in the ownership structure. Now initially when the joint venture started, and if the joint venture is through the equity participation then there might be an initial agreement of capital contribution in a particular manner. And it might so happen that one of the partners, might have a ambition to have a greater share in a joint venture entity with both of time, or they might want to exit that particular joint venture entity after a passage of time. So, what should be the ownership structure of the joint venture entity in different phases that you need to consider? It is not necessary that always there will be change in ownership structure.

It might continue as a initial understanding ease, but it is depending on ambition of the parties in the joint venture. The ownership structure or equity structure might change. So, in those circumstances it is again advisable that you should negotiate that what should be the ownership structure in future in that particular joint venture entity? Now, let me take you to the next point is, determining relating to the dividend policy and the financial matter. sometimes you will find that one of the partner, is aggressive to gain the market share, while the other is interested in quick increase in cash flow, and this may create a kind of conflicting objectives, and you need to sort out this particular issue through the negotiation, because the varying objective of the partners in a joint venture might be a killing of the joint venture arrangement.

Next thing you need to talk about the marketing and staffing issues. Now who is going to take care of local market? Is it the local partners' management? Or even you wanted to have interference relating to the marketing policy? Because, many of the time, the multinational try to inject their experiences in the other market, to have a better result into the new market, the experience might work might not work. I was reading some of the report, wherein people said that the amazon experience in the European market, did not really work in the Chinese market, because the market culture might be different, consumer behaviour might be different from one to another one, so one need to be careful about this particular negotiation.

The next point is maintaining the control over the distribution channel your partner locally might have a very strong distribution channel. All these shares are exist in distribution channel, and in that particular distribution channel they are one of the dominant supplier, but may be the foreign partner are interested that there should be independent distribution channel will be created by this joint venture entity. Then in those particular circumstances you need to negotiate. Now, there can be operational issues. Some of the operational issues might be forcible, at the time of agreement was negotiate.

And in some cases this problem might not be understood at the time of entering into an agreement. So, you should create a adequate mechanism, to address this operational problem, within the joint venture agreement or the terms of the joint venture. Next is there might be a conflicting, or there might be a conflict between the partners of the joint venture, and this is a very natural that there will be some conflict in future at the time of joint venture operation. So, resolving this particular conflict, you should put a mechanism in place. And please remember this conflict settlement should be in a different layer in different stages. instead of simply relying on arbitration, or the existing code process, because if there is a correct communication channel created, or whenever the dispute arises between the two partner, and can be addressed that particular dispute in the early stage.

The major problem in the joint venture can be addressed in early stage, and it will help to sustaining this relationship, joint venture relationship for long time. So, the joint venture agreement should create a provision for conflict resolution, between the partners, and during this joint venture negotiation both the partner should negotiate on that.

Next is the problem might come, because of multi-nationalism. The local joint venture partner, might have a different objectives, or might have a different way to operate, or might have a different policy relating to the production, and that might create a potential conflict between the partners. The firm might have a different objective which I have explained to you. There might be a conflict relating to export right. your foreign partner might not be interested to give you right to export, which is developed out of the joint venture agreement, because if the export right has been given to you, then it might get or it might find a difficulty to sell his own product in a different market where it has a dominance.

So, you need to negotiate relating to the export right. The last point is relating to the changing relationship, and you should be always careful about this particular changing relationship, and there should be adequate provision in corporate relating to the changing relationship in the joint venture agreement. This changing relationship may be because of the change in technology. Now when the joint venture was started it was based on particular type of technology.

Now technology changed, and you need to have a investment, in this changed technology scenario, who is going to make that investment, how much investment in which form you are looking for, who is going to have a control in the post investment scenario, or if there is a mutual control, what is that particular mutual control. there might be some provision in the joint venture agreement which is quite obsolete, and that might create a bottle neck for the joint venture agreement to continue, that particular provision has been created based on some prevalent regulatory you know environment when this particular joint venture has been entire upon, and over the years that regulatory environment is changed.

For example, when the joint venture has been entire upon, the regulatory prescription was that the foreign partner only can invest up to 35 percent of the equity, but at present that particular regulatory environment changed, and it has been open up to 100 percent of equity investment. So, if you have that particular provision in a partnership agreement it might create a problem in the joint venture partner. Similarly, the new technology developed within the joint venture are prevented from being used widely by the foreign partner, because the joint venture developed a technology which is much superior, then the original technology, much cost effective than that of a original technology. And your partners do not want that particular technology to come into the open market, because then in that case it will actually lose the business in the different market.

So, how you are going to sort out this problem, you need to negotiate you need to have a mechanism in place, because this kind of scenario is potentially harmful, not only for that particular joint venture organization, but for the partner organization, which has a dim dream to grow. Now, joint venture management often draw from different cultures, and understanding, misunderstanding can occur very easily. The way the C E O from Japan operates, the C E O from Greece will not operate in the similar manner, and in a joint venture firm you brought the Greece C E O in the Japan, then that might create a potential conflict because of his working style.

So, if you are bringing the Americans in Indian style as a part of the joint venture agreement, which do not have an understanding about the business dealing, business culture, business environment, customer preference, then he might create a potential threat, or he might himself be a potential threat for the continuation of this particular joint venture. So, you need to negotiate on this particular issue, and to try to understand that how you can neutralise this particular potential conflict.

Thank you.