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STRATEGIC ALLIANCES – PART II¹ Going Global in a Changing World

In the last edition of the Barbeau & Company Newsletter, we looked at the role of alliances in a global commercial context, and reviewed the practical alliance planning issues that often arise in domestic and international commercial co-operation. In addition, we examined the strategies for limiting “relationship risk”, through a variety of applicable and compelling principles. In this issue, the second of a two part series, we shall examine the various types of alliances that are prevalent, and look at the various circumstances for employing one type over another.

Confidentiality and Non-Compete “Preliminary Protection”

Prior to examining the type of alliance structures and the advantages and disadvantages of each, there is a preliminary documentation stage that precedes any formal alliance negotiation. The first of the two required agreements will cover matters of confidentiality of

¹ If you did not receive Part I of this two part series of articles and wish to receive a copy of it, please check our web site at www.barbeau-law.com/publications.htm, or email a request to info@barbeau-law.com.

business information, and the second and concluding agreement of this preliminary documentation stage, is the letter or protocol of intent, or memorandum of understanding.

A “one-way” or reciprocal confidentiality and non-compete agreement is essential to protect one or both parties’ proprietary business information (i.e. confidential information protection) and, shall further protect one or both parties from the other who may, absent the non-compete protection, desire to use its alliance partner’s technology against that partner, in the marketplace. A by-product of the negotiation of the confidentiality and non-compete agreement, is that it will expose your alliance partner’s negotiating style, and will give you and your organization a better understanding of your partner’s desires and objectives. It is crucial, that you observe your potential alliance partner’s behaviour at this stage, as it will foreshadow events to come.

This preliminary phase generally ends with the signing of a letter of intent or like document, describing the basic business understanding of the parties which shall set the direction for negotiation of the definitive governing agreement between the participants. The letter of intent phase of the negotiations is

particularly important in an international context where different cultures and perhaps different languages are at play, and will expose the extent to which communication barriers exist and allow the parties to begin to address issues of misunderstanding or miscommunication.

The Alliance Vehicle – Simplicity, Complexity and Everything in Between

The type of alliance vehicle will be dictated by the objectives and desires of the participants and the technology at issue, as well as market, financial and tax considerations. In short, there are a variety of structures available for strategic alliances, ranging from the simple agency agreement to the more complex corporate joint ventures. There are a range of common structures and arrangements for alliance participation, which may be summarized as follows:

- a) Royalty, Licensing and Technology Transfer Agreements;
- b) Production Equipment Lease Agreements;
- c) Agency, Product Supply and Distributorship Agreements; and
- d) Joint Venture Arrangements (contractual and corporate).

Royalty, licensing and technology transfer agreements have a number of common characteristics, both

from the perspective of the limited participation required by the owner of the underlying technology, as well as in relation to the circumstances in which these forms of alliances may be utilized.

While royalty agreements, which provide for specific royalty payments to be made for the use of specified technology, and licensing agreements, which grant a right to some form of intellectual property or proprietary know-how, both involve a fairly passive form of alliance participation on the part of the owner of such technology. These two types of agreements differ substantially, from that of technology transfer agreements, in one significant way.

Technology transfer agreements, by their very nature, presuppose that ownership of some or all of one parties' technology will be transferred to the other alliance participant, on a permanent or enduring basis. The recipient of the technology shall, for all intents and purposes, become the owner of the technology, in the recipient's jurisdiction of operation and, in some circumstances, within some larger market, jurisdiction or territory. Needless to say, proceeding on the basis of technology transfer, involves some very serious consideration regarding the ongoing viability of the recipient of the technology, as this form of agreement may result in the ultimate creation of a future competitor. This type of agreement is often used in circumstances where the national or sectoral market would otherwise be closed to the participant who is the owner of the source technology.

One of the most underutilized and often overlooked forms of strategic partnering, is the lease of proprietary product manufacturing equipment to a foreign non-related party, for the purpose of allowing for the production of a product within the leasee's domestic market. While this type of alliance can require a more complex level of protection over the equipment itself, something that lends itself to jurisdictions which provide for a public system of charges or liens against physical assets, the advantage of this arrangement is that it may provide for a way to circumvent high import levies and duties on finished products imported into that country and allow access to a market that would otherwise be unavailable to your organization and its products.

Agency, product supply and distributorship agreements are commercial arrangements by which the agent, supplier or distributor undertakes to sell the foreign company's product in the target or domestic market and takes as remuneration a profit from the goods sold. These arrangements are generally entered into as a risk avoidance device because the agent, supplier or distributor bares some or all of the risk of selling the product in the host country.

There are further distinctions as between agency, product supply and distributorship agreements, in that the transfer of risk of the product to the representative shall vary and the control over how the product is marketed and sold within the host country will, to varying degrees, be dependant on the effort and capacity of the local representative.

Joint ventures viewed in their most simple form, are contracts that creates a co-operative relationship for the purposes of performing some kind of business operation, such as the manufacture and sale of goods, the construction of a building or the development of real estate. In this regard, there are joint ventures that are contractual arrangements between the parties and there are corporate joint ventures where each of the joint venture participants owns shares in the joint venture corporation which is established to carry on the joint venture business. The business purpose of the joint venture, the jurisdiction of operation, methods of financing, issues of distribution as well as income, capital gains and withholding tax issues will dictate which form of joint venture vehicle is utilized for any particular endeavor.

Conclusion

Clearly, while there are a number of additional alliance arrangements that may be created (e.g. logistics outsourcing and supply management agreements, marketing and research and development agreements, consulting services arrangements, forms of equity and debt investment, etc.), this article has focused on a broad range of alliance arrangements that may be utilized in a variety of differing circumstances.

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