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SOME PROBLEMS RAISED BY THE ESTABLISHMENT OF INDUSTRIAL JOINT VENTURE AGREEMENTS

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V[illegible]

1. [illegible].
2. [illegible] A. [illegible]A.
3. [illegible]
4. [illegible]
5. [illegible].
6. [illegible]
7. [illegible].
8. [illegible]
   [illegible].
9. [illegible]ANA [illegible].
10. CONT[illegible] [illegible]

INTRODUCTION

Joint Ventures

Historically, foreign direct investment in developing countries has generally been in the form of wholly-owned subsidiary corporations. More recently, however, an increasing number of new investments have been joint ventures, involving shared ownership, between local and foreign partners. There are many factors contributing to the growth of joint ventures. One is that developing countries may pass legislation either prohibiting total foreign ownership or else making incentives conditional upon a certain degree of local ownership. More importantly, however, many foreign investors have become increasingly aware of the positive advantages they can derive from sharing ownership with local partners, be they private or governmental. Among these benefits are tangible contributions, such as land, capital, trained personnel, a knowledge of the local language, and familiarity with local markets, suppliers, and conditions of doing business. Some intangible benefits include the good will engendered with employees, customers and the government, and the decreased likelihood of nationalization or discriminatory legislation.

Because of the increase in joint ventures, and the very real benefits they afford, much sophistication has been brought to the negotiation and execution of joint ventures, especially by the larger multinational corporations which have considerable experience in this field. Recognizing

this development, the International Symposium on Industrial Development held in Athens [illegible] UNIDO should:

> Formulate model form agreements which might be required by the developing countries in connexion with bilateral, multilateral, and joint-venture negotiations; such formal agreements should be accompanied by extensive notes on definitions, terms and conditions as well as alternative formulations.

Scope of this study

The Athens Symposium's recommendation may have been overly optimistic in suggesting that any prototype joint venture agreement might be formulated, because in UNIDO's experience, it has been impossible to find any joint venture which can be categorized as typical or serve as a prototype for other agreements. Instead, it is the almost infinite combination of possible terms and conditions within the context of a joint venture arrangement which has led to their utility and popularity.

Because of this diversity, and because large multinational corporations generally are quite knowledgeable about joint ventures, this study has been limited to the achievement of only two very modest objectives. Firstly, the attempt is made to present a number of the major issues confronting the host country partners in the negotiation and execution of joint venture agreements. Some of the topics considered are ownership, capital structure, direction, management, marketing, financial policies, industrial property, technical assistance and know-how, dispute settlement and partnership compatibility arrangements.

Having selected certain topics for discussion, the second objective

of this study has been to suggest only some of the possible alternative approaches that might be considered by the parties. In some instances, approaches which might accord with certain policy goals of the host developing country have been mentioned. Legal clauses for implementing some of the approaches have been included in a number of instances. Throughout, the main purpose of this study is to suggest some of the possible ways in which the rights of the partners might be governed to the advantage of the joint company itself and the host country.

The negotiation and drafting of joint venture agreements is a complex and difficult undertaking. Many large multinational firms attempt to utilize more or less standard agreements, and these agreements often represent their initial bargaining posture. Through being aware of alternative possibilities, however, the local partners will be in a better position to ensure that needs of the joint company, the host country, and themselves are also considered.

Joint Venture Agreements

As mentioned, there is no standard or prototype joint venture agreement, and the rights of the partners are often governed by a series of interrelated agreements. Common to these is the joint venture agreement itself, in which the rights of the partners in respect of the establishment of the joint company and its operation are governed. Then, all of the other provisions may be included either in the one agreement itself, or be provided for in separate legal agreements. Where the matters to be provided for are complex and its provisions are severable from the other questions

[illegible] incorporate [illegible] agreement [illegible] supply of technical [illegible] and [illegible] engineering and construction [illegible] joint venture agreement [illegible] joint venture arrangements.

[illegible] or prompt[illegible] joint venture agreement, there appears to be one common [illegible] pervading all successful joint venture relation[illegible], namely, the [illegible] of the partners. A joint venture requires that the partners work together and cooperate to attain common goals. The parties should therefore not enter into negotiations with the intention of maximizing their immediate advantages, but with a view to creating a legal structure in which they can work harmoniously over the long run to achieve results that neither could achieve alone. The object of the negotiations is primarily to create a successful marriage, not to maximize individual advantages at the expense of the whole.

It is hoped, therefore, that this study might facilitate the conclusion of successful joint venture arrangements through its suggestion of some alternative terms which may enable partners to more adequately provide for their requirements. It is also hoped that the inclusion in the Appendix of the summaries of ten case studies of international manufacturing joint ventures in developing countries might contribute to disseminating knowledge of the

experiences of other [illegible] by UNIDO from a number [illegible] of Columbia University, [illegible] from [illegible] Ford Foundation and [illegible].

[illegible]

[illegible] COMPANY

A. [illegible]

There are two fundamental forms of joint ventures, contractual joint ventures and equity joint ventures.

1. [illegible] are utilized in many [illegible] business operations [illegible] recognise the concept of private ownership of property, such as in a number of countries with centrally-planned economies. Contractual arrangements are made for the supply of capital, equipment, industrial property, technical assistance and know-how by the foreign partner to the government or local partner in return for royalties which may depend on production, sales, profits, etc. Other contractual joint ventures may involve only licensing and know-how or marketing arrangements.

   Because of the more limited use of wholly contractual joint ventures, the direct concern of this study is with the equity joint venture, but it can be seen that many provisions relating to the equity joint venture, excluding ownership considerations, apply, as well to contractual joint ventures.

2. Equity Joint Ventures are by far the most common form of joint venture involving foreign investment in developing countries. They involve participation by two or more partners in the equity capital of an existing company,

or more usually, in the incorporation of a new company in which each partner owns a certain portion of the equity capital. Formation of a new company, is often the most convenient method, because it is often more convenient to obtain new incorporating documents with the desired provisions than to adapt an existing structure to the new way of doing business.

B. JURISDICTION OF INCORPORATION

PROBLEM:

Assuming that an equity joint venture is being adopted, the partners must decide upon a suitable jurisdiction for incorporation of the Joint Company.

POSSIBLE APPROACHES:

The Joint Company may be incorporated in either the host developing country, or in some other jurisdiction and conduct its business in the developing country through a branch of such company.

In a limited number of cases the Joint Company and/or partners may obtain small tax and other advantages from incorporating outside the host developing country, but such instances are so few that they are not considered further in this study. On the other hand, many developing countries have industrial investment incentive laws offering advantages to locally incorporated companies, and in most instances, incorporation in the country where the principal operations are to be conducted offers many administrative conveniences. Accordingly, it is assumed throughout this study that the Joint Company will be incorporated in the host developing country where the principal operations are to be conducted.

C. INCORPORATION OF JOINT COMPANY

(a) Responsibility: Because the local partner will usually be in the best position to have the Joint Company organized expeditiously, this obligation is often left to it. Where the local partner is the Government or a Governmental Agency, the foreign partner will often take responsibility for organizing the Joint Company. In a number of joint ventures, both partners assume responsibility for having the Joint Company incorporated.

(b) Costs: The costs of incorporation are generally shared by the partners pro rata to their equity participation in the company, but other formulae are also applied, such as an equal sharing of the costs or else the partner responsible for having the company incorporated may assume the costs itself.

POSSIBLE CLAUSES:

1. Local and Foreign (or else Local alone) shall take all necessary steps for the incorporation of a (type of corporation to be formed) corporation under the laws of (jurisdiction of incorporation), which said corporation shall be hereinafter referred to as "the Joint Company".

2. Local and Foreign (or else Local alone) shall cause the Joint Company to be duly organized in accordance with the terms and conditions of this agreement.

3. The costs of incorporating the Joint Company shall be borne equally (or according to some other formula) by Foreign and Local.

D. NAME OF JOINT COMPANY

COMMENT:

Where the name of either the foreign or local partner carries goodwill, most joint venture agreements provide that at least a portion of such name be included in the name chosen for the Joint Company (e.g. Merck Sharp & Dome of India Limited). Another possibility is to include one of the trade names under which the Joint Company's products will be sold in the name (e.g. Carling Brewery Hong Kong Limited).

The name is generally included in the application for incorporation, and provision should be made for an alternate name in the event that the first choice is not acceptable to the incorporating authority.

E. INFORMATION CONTAINED IN INCORPORATING DOCUMENTS

PROBLEM:

It is necessary to determine what provisions governing the rights of the Joint Venture partners inter se and with the Joint Company, should be contained in the incorporating documents of the Joint Company.

COMMENTS:

What provisions are to be contained in the incorporating documents will depend firstly, on the laws of the jurisdiction of incorporation and secondly on the extent to which the parties wish to govern their relationship by such inclusions.

Three ways in which the rights of the parties inter se and vis à vis the Joint Company may be protected are as follows:

1. The rights of the partners as shareholders might be protected by company laws in the jurisdiction of incorporation which require a special majority for certain actions, thereby necessitating the consent of both, or all partners to the proposed action.

2. The rights of the partners might be protected by setting them out in the incorporating documents of the Joint Company where either the applicable company law requires a special majority to alter the provisions or the incorporating documents themselves or stipulates that amendments thereto may be made by a special majority only. Under either of these alternatives, the special majority must be sufficiently high so as to require the

consent of both or all partners.

3. The rights of the partners as shareholders might be protected by a shareholders' agreement or voting trust whenever the applicable law permits specific enforcement of such agreements.

Law jurisdictions, specific enforcement of their terms is not available as a remedy, and damages may not be an adequate remedy. One problem with shareholders' agreements and voting trusts is that in a number of civil law jurisdictions, the remedy of specific performance is not available and damages alone may be inadequate.

A further problem is that the laws of many jurisdictions regard directors as fiduciaries of the company and not of the appointing shareholder's specific interest. Accordingly, agreements which fetter the directors' discretion are void. Even if shareholders might enter into binding agreements to appoint certain directors, such directors may not be compelled to act according to the wishes of the shareholders, and their removal and replacement by more tractable directors may be time-consuming and difficult.

Where shareholders' agreements and voting trusts are specifically enforeceable, there will be less need for the incorporating documents to contain provi[illegible]

protecting the rights of the partners inter se as shareholders. Accordingly, the existence of such provisions in the joint venture agreement itself will afford adequate protection.

Where shareholders' agreements and voting trusts are not specifically enforceable, or where the provisions relate to the exercise of powers by directors whose fiduciary powers cannot be fettered by agreement, then it is necessary to insert as many of the protecting provisions as possible in the incorporating documents.

If the law of the jurisdiction of incorporation provides specifically for such protection (such as pre-emptive rights or cumulative voting for directors), then it is not mandatory to insert such provisions in the [illegible] documents, since this is achieved by operation of law. For the sake of clarity and certainty, however, it may still be desirable to include them.

The usual approach in joint venture agreements when special provisions are to be included in the incorporating documents is to draft such documents and annex them to the joint venture agreement as a schedule. Such documents are then submitted to the appropriate authority issuing the certificate of incorporation or final authorization or approval.

<u>POSSIBLE CLAUSES:</u>

1. Local and Foreign (or else Local alone) [illegible] the Joint Company to be duly organised in accordance with the terms of this Agreement, with [illegible] for the incorporating [illegible] under the law of the jurisdiction of incorporation, such as "[illegible]", "Letters Patent of Incorporation", "Memorandum and Articles of Association", etc.) which in the English translation shall read in substantially the form attached hereto as Schedule.

2. If any of the provisions contained in the said Schedule should not be approved by the appropriate authority for inclusion in the incorporating documents of the Joint Company, then the parties agree to make such amendments thereto as shall be acceptable to the said appropriate authority without altering their purpose or intention, or failing such amendments, to take all such other steps and do such other things, including the execution of any other agreements as may be necessary, to achieve the interest and purpose of such of the provisions as may not have been found acceptable by the said appropriate authority.

CHAPTER TWO

OWNERSHIP AND CAPITAL STRUCTURE

1. OWNERSHIP

A. TYPE OF EQUITY JOINT VENTURE

PROBLEM: A difficult problem in negotiating any joint venture agreement is to determine the percentage of shares that are to be owned by each of the partners.

POSSIBLE ALTERNATIVES: Equity joint ventures can take several forms which are often differentiated from each other according to the ownership provisions. Five of the possibilities are listed below, of which the latter two are less common than the first three.

1. Minority foreign ownership
2. Majority foreign ownership
3. 50/50 joint ventures.
4. 49/49 with controlling shares being held by an independent third party.
5. 100% ownership in one partner with an option in other partner to acquire some or all of those shares.

COMMENTS: The number and kind of shares subscribed for by each partner may depend on the degree to which each partner wishes

a) to participate in the profits and growth of the company;

b) to share in the assets upon a winding up or dissolution; and

c) to have voting rights as a shareholder upon questions such as:

  i. appointment of directors;

  ii. distributions of assets;

  iii. changes in the Joint Company's objects;

  iv. changes in the capital structure; and

  v. such other items as may be reserved to the shareholders by the incorporating documents by operation of law, and by agreement or otherwise; and

d) to comply with host country laws in respect of foreign ownership.

Because of the different types of shares which may be authorized, it may be difficult to classify a joint venture according to the percentage of shares owned by each partner. For example, a 51 per cent ownership of all shares entitled to one vote each under all circumstances may represent only a small percentage of the total authorized capital of the Joint Company if non-voting preference shares are issued as well.

Accordingly, where more than one type or class of shares is authorized and issued, a reference to the percentage ownership by each partner is meaningful only if the rights attached to each different type or class of share are specified, but where there is only one type or class of share, the percentage ownership will represent the percentage

[illegible]

1. [illegible]

(a) [illegible]

(b) In addition to compensation in the form of dividends or an ultimate participation in assets, the following are some of the alternate ways in which one or both of the partners might receive financial advantages from the Joint Company, and which are not directly related to their percentage ownership:

i. license fees

ii. management fees

iii. directors' fees

iv. salaries for key personnel

v. interest on debt capital or loans

vi. fees for special services rendered

vii. indirect fringe benefits

2. Management and Control:

A minority shareholder, for instance, might have a disproportionately large voice in the management and control of the Joint Company through some of the following means, namely:

(a) the use of different types or classes of shares;

(b) a management contract;

(c) veto powers contained in the incorporating documents or the joint venture agreement;

(d) through the supply of essential industrial property, technology, materials, services, etc.

In other words, the percentage ownership acquired by each partner will depend on a great many factors, and the parties should realize that there exist many different legal, financial and economic means of achieving many of the objectives that are normally associated with percentage ownership alone.

B. [illegible]

PROBLEM:

Although [illegible] joint venture, the [illegible] greater number [illegible] joint [illegible].

POSSIBLE SOLUTION:

Nominee [illegible] in [illegible] appointed who will hold the minimum number of [illegible] shares. [illegible] shares [illegible] it is usual that they be the chief executive officer [illegible] directors of the Joint Company, [illegible] a declaration that [illegible] one of the partners. [illegible] to be associated with the Joint Company [illegible] partners, the shares will be [illegible].

POSSIBLE TRUST CLAUSE:

I, (name of nominee shareholder), do hereby declare that I am the holder (number and type of shares) of (name of Joint Company) in trust for (name of partner), its successors and assigns, upon such trusts as (name of partner) may from time to time declare, and am not the beneficial owner thereof.

C. NATIONAL OWNERSHIP REQUIREMENTS

PROBLEM:

The laws of the host country may require a certain percentage of local ownership by nationals, residents, or [illegible] but the partners may not be able to agree on such a [illegible]

POSSIBLE SOLUTIONS:

It has not been unknown amongst developing country joint ventures for the foreign partner to subscribe for the maximum number of shares permitted by host country law (e.g. 49%), but to still achieve the desired control participation by having a certain number of shares owned by nominee shareholders who are citizens of the host country.

COMMENTS:

Restrictions on the degree of foreign ownership of corporations in developing countries generally take two forms, namely, an outright prohibition against more than a certain percentage of foreign ownership; or the making applicable of industrial incentive legislation, including tax holidays, etc., to only those corporations which have a certain percentage or less (usually 49%) of foreign ownership. Where such nominee shareholders holding swing shares in trust for the foreign partner contravene in letter or spirit the host country law, there have been instances where the existence of such trusts have been kept secret from governmental authorities. This approach to conducting business in developing countries cannot be condoned even on the basis of answering business exigencies, because both partners must be a party to the deceit, and there are

generally other ways of allocating the required control and participation amongst the partners which can satisfy the legitimate aspirations of all the partners.

2. CAPITAL STRUCTURE

A. TYPES OF SHARE CAPITAL

PROBLEM: The partners must decide what type of capital shares of the Joint Company are to be authorized, and what rights each type of share shall confer upon the shareholder.

POSSIBLE TYPES OF SHARES:

1. Common or Ordinary Shares: Each common or ordinary share usually carries one vote and entitles the holder to participate pro rata in the assets of the company upon a winding up or dissolution. Such shares do not bear guaranteed dividends, but the directors have power to declare that a dividend thereon may be paid out of the profits of the company.

2. Preference Shares: In many jurisdictions, it is possible to create shares which carry special rights or preferences such as the following:

   a) Dividends: Preference shares may give a preferred right to dividends of a fixed amount before dividends are paid on the common shares. The right to dividends may be cumulative or non-cumulative. If non-cumulative, and dividends are not declared in one year, they do not accumulate and become payable the following year.

b) Participation in assets: On dissolution or winding up, preference shares will usually participate up to their face value in the assets of the company in preference to the common shares.

c) Voting: Preference shares may be voting or non-voting. It is common to provide that when their specified dividend is not paid for three consecutive years for example, the non-voting preference shares become entitled to one vote each.

d) Redemption: If the Joint Company wishes to terminate any of the preferences on the common shares, or to terminate its liability with respect thereto, they may be made redeemable at the option of the Joint Company.

3. <u>Convertible Shares:</u> In some jurisdictions (some civil law jurisdictions for instance), it is not possible to have non-voting shares, nor to obtain specific enforcement of a shareholders' agreement to appoint certain persons as directors. In such a case, different classes of shares may be created with each class having the right to appoint a specified number of directors. In this way, each partner can be assured of its own representation on the board.

POSSIBLE CLAUSES: The Joint Company shall have an authorised capital of (amount) consisting of:

1. (number) common (or ordinary) shares with par value of (amount) each (or without nominal, or par value);

2. (number) (interest rate) non-voting (or voting) cumulative (or non-cumulative), redeemable (or non-redeemable) preference shares with par value of (amount) each;

3. (number) (interest rate) non-voting (or voting), cumulative (or non-cumulative), convertible preference shares with a par value of (amount) each, which said shares shall be convertible into common shares on the basis of one preference share for one common share any time after the last business day of the calendar year 19 .

4. (a) (number) Class A shares of a nominal value of (amount) each; and

   (b) (number) Class B shares of a nominal value of (amount) each.

   (c) The said Class A shares shall be entitled to appoint (number) directors of the Joint Company, and the said Class B shares shall be entitled to appoint (number) directors of the Joint Company.

B. PAYMENT FOR SHARES

POSSIBLE FORMS OF PAYMENT:

Depending upon the requirements of local laws, shares may be issued to the joint venture partners as fully-paid or as partially paid with the balance remaining on call. Where not fully-paid, it is usual that the directors will make calls from time to time as further capital is required by the joint company.

Payments for shares may be made in the form of:

1. Cash
2. Machinery and Equipment
3. Land
4. Industrial Property, including
   a) Patents
   b) Trade Marks
   c) Trade Names
5. Technical Data
6. Technical Assistance and Know-how
7. Other Services

COMMENTS:

1. CASH: Most joint venture companies will, depending upon the availability and terms of debt financing, attempt to establish a high debt to equity ratio. The amount of cash paid in by the partners will depend to a large extent on what additional capital is required to meet initial construction and operating costs, upon requirements of creditors that a certain

percentage of cash be paid in, and local company laws which may require certain cash subscriptions. Generally, however, the partners will attempt to keep as low as possible the size of their cash subscriptions to the capital of the joint company.

2. MACHINERY AND EQUIPMENT: The partners, often the foreign partner, will want to contribute machinery and equipment to the Joint Company. The value of such machinery and equipment will be regarded as contributions to capital by the supplying partner or partners.

PROBLEM: The Joint Company will want to ensure that all machinery and equipment supplied to it, whether as a contribution to capital or otherwise, or whether by a partner or an independent party, adequately meet its requirements.

COMMENTS: Some considerations with regard to the adequacy may be that the machinery and equipment

1. be capable of producing the specified products
2. be of the latest design
3. provide maintenance-free service
4. be compatible with existing machinery
5. be compatible with machinery which might be added at a later date

6. meet the highest specifications of quality production
7. be reasonably priced in the circumstances
8. have readily available replacement parts and service facilities.

<u>POSSIBLE APPROACHES:</u>

Some of the following approaches might be adopted to protect the Joint Company against the acquisition of machinery and equipment that is inadequate or unsuitable in the circumstances.

1. Obtain a guarantee and warranties from the supplier of the machinery and equipment that it will meet specified qualitative and quantitative production standards, in default of which the supplier shall be liable in damages to the Joint Company.

2. Require certification from independent consultants as to the fitness of the machinery and equipment for the job required.

3. Require the purchase of all machinery through public tenders upon specifications prepared by independent consultants, including warrantees and guarantees and/or a certification of fitness as above. This approach may be helpful where the foreign partner wishes to supply machinery, as it provides an outside standard for judging its adequacy.

4. It may also help to obtain independent advice from the manufacturers of the equipment and machinery, ensuring that it is

   (a) not obsolete;

   (b) that it will not be obsolete within the foreseeable future, barring a major technological breakthrough;

   (c) that it is compatible with existing machinery and with machinery which the manufacturer will be producing in the future, so that the introduction of new machinery and equipment will not necessitate a scrapping of the old; and

   (d) that replacement parts are readily available.

5. Obtain the assistance of technical experts by making application to international organizations such as UNIDO, for assistance in assessing the tender bids or in evaluating the type and quality of machinery to be supplied.

POSSIBLE CLAUSES: 1. Foreign hereby undertakes to warrant and guarantee to the Joint Company that the machinery and equipment is capable of producing the products in the quantities and according to the required specifications, which said machinery and equipment, quantities and specifications are set forth in Schedule   annexed hereto; is of the latest design and incorporates all workable improvements; shall provide maintenance-free service except for

no [illegible] interest [illegible] obtained [illegible] in [illegible] machinery [illegible] Joint Company [illegible] machinery [illegible] enable [illegible] that [illegible] are [illegible] there.

2. Foreign hereby undertakes [illegible] Joint Company that independent [illegible] or warranties provided by manufacturers, [illegible] consultants [illegible] the said machinery and equipment [illegible] effectively and produce the required [illegible] according to the [illegible]litative and [illegible]titative specifications outlined, for a period of [illegible].

3. In the event of any failure to satisfy the above requirements, Foreign shall be liable to the Joint Company in damages for all costs [illegible] rectify the situation, and for all damages occasioned by the loss of production, including all costs of shut-down and start-up.

3. LAND: If one of the partners is supplying land, it may be regarded as a contribution to the capital of the Joint Company to the extent of its value.

4. INDUSTRIAL PROPERTY: For purposes of this study, it is assumed that industrial property consists of property such as patents, trade marks and trade names which are often protected against unauthorized use by laws requiring their registration, and property such as secret processes, technical information and data, and know-how, which may or may not be protected against unauthorized use by laws in respect of fair business practices.

The assignment, licensing and sublicensing of such industrial property might in certain cases be treated as contributions to capital of the Joint Company, in return for which fully-paid shares might be issued to the contributing partner to the extent of the value thereof.

(a) Assignments: In most instances, the Joint Company will derive the greatest advantages from receiving a transfer or assignment of the industrial property rights possessed by the partners, because it will then have the right to exploit that property everywhere in the world that the law will permit through actual user or licencing. In addition, if the Joint Company becomes the owner rather than a licensee of the industrial property, it will be freed from other constraints upon its use which are normally contained in license agreements.

(b) Licences: While, as mentioned, it will usually be most advantageous for the Joint Company to become the outright owner of industrial property that it will be using in its operations, this course might not be open to it because the contributing partner demands too high a price, or wishes only to license its use to the Joint Company.

The contributing partner may be reluctant to assign industrial property rights to the Joint Company where it is utilizing them elsewhere in the world and is in a position to derive substantial profits from such licensing operations. The alternative is for the Joint Company to also become a licensee of the foreign partner. License royalties may be paid on a lump-sum or continuing basis, or a combination of both. Where there is an exclusive world licence granted to the Joint Company in return for a lump-sum royalty, such a licence may in some limited instances be considered an assignment, and the lump-sum, rather than being paid to the contributing partner, may be treated as a contribution to capital.

Royalties payable on a continuing basis to the licensor partner, instead of being actually paid, may also be utilized to offset such partner's liability for calls on shares, and in this way, will be regarded as part of his contribution to capital.

(c) __Sublicences:__ where a partner is a licensee of industrial property and by the terms of the licence, is not prevented from sublicensing to the Joint Company, lump-sum and/or continuing royalties for the sublicence might go to reduce the foreign partner's capital contribution obligations.

5. __Technical Data:__

Technical data generally includes all the information concerning the operations of the Joint Company which can be transferred by writing, [illegible], etc. [illegible] include such items as formulae; inventions whether patentable or not; secret processes and technical information relating to the production, use and sale of products; manufacturing, engineering and test data; specifications; application instructions; information regarding raw materials, their sources and uses, and methods for analyzing and controlling their quality; sample copies of labels, publicity and advertising materials; etc.

Such technical data will usually be considered as property, and its contribution or supply to the Joint Company by one partner can generally be considered as a contribution to capital.

6. Technical assistance and know-how: The term technical assistance and know-how [illegible] by all information and [illegible] required to carry out the manufacturing [illegible] business operations and to utilize effectively [illegible] property owned by or licensed to [illegible] connotation, it [illegible], [illegible] more narrowly in this context, and technical assistance and know-how [illegible] of training employees of the Joint Company in conjunction with the transfer of technical information and industrial property [illegible] all of the operations required for the production, sales, and servicing of the product being manufactured.

Because technical assistance and know-how in this context consists generally of services in the form of interpersonal contacts to teach and transfer methods, the possibility of treating them as contributions to capital will depend on whether services can constitute contributions to capital under the host country law.

7. Other services: Where the incorporating jurisdiction permits contributions to capital in the form of services rendered by the partners of the Joint Company, such as in organizing the company, etc., shares may be issued to the contributing partners in consideration for the services rendered.

The possibility of so doing must be scrutinized closely under the laws of the incorporating jurisdiction.

POSSIBLE CLAUSES: In payment for the shares of the Joint Company to be acquired by Foreign (Local), at the time of the incorporation of the Joint Company (or, within days after the incorporation of the Joint Company), Foreign (Local) shall assign and transfer to the Joint Company:

1. Cash: (amount) in cash;
2. Machinery and Equipment: all of the machinery and equipment set forth in schedule annexed hereto, which said machinery shall become the sole property of the Joint Company, free and clear of all liens, charges and claims of any kind whatsoever;
3. Land: the absolute title, free and clear of all liens, charges and claims of any kind whatsoever, to the real property and all buildings and other structures thereon, including all fixtures, equipment and machinery located therein, situate at (municipal address), which said real property, buildings, structures, fixtures, equipment and machinery are more specifically described in the Schedule annexed hereto;
4. Industrial Property:
   (a) Assignments:
      (i) Patents: Foreign's entire right, title and interest in and to all unexpired patents and patent applications theretofore issued or assigned to or filed by Foreign anywhere in

the world to the Licensed Products or to the production, manufacture or use thereof (a list of such patents and patent applications heretofore issued or assigned to or filed by Foreign being set out in the attached Schedule), together with all rights which Foreign then has to apply for patents in the world on inventions relating to the Licensed Products or to their production, manufacture or use, and including all of Foreign's rights with respect to patents which may thereafter issue anywhere in the world on any such patent applications and with respect to divisions, patents of addition, continuations, renewals, re-issues and extentions of all such patents, patent applications and patents which may issue on such patent applications.

(ii) Trade Marks and Trade Names: Foreign's entire right, title and interest in and to all world rights which it then has to all of the following trade marks and trade names, namely: (to all of the trade marks and trade names set out in the attached Schedule);

(b) Licences: Foreign shall enter into a Licence Agreement with the Joint Company in the form as set out in Schedule hereto annexed, under which said Licence Agreement the Joint Company

shall become the exclusive licensee for the world for all unexpired patents and patent applications of Foreign for the Licensed Products or to the production, manufacture or use thereof, together with all rights which Foreign then has to apply for patents in the world on inventions relating to the Licensed Products or to their production, manufacture or use, and including all of Foreign's rights with respect to patents which may thereafter issue anywhere in the world on any such patent applications and with respect to divisions, patents of addition, continuations, renewals, re-issues and extensions of all such patents, patent applications and patents which may issue on such patent applications.

(Because of the importance and scope of Licence Agreements, they are more extensively dealt with hereafter).

(e) Sublicences: Foreign's entire right, title and interest in and to all world rights which it then has under patents owned by others relating to the Licensed Products or to their production, manufacture or use, a list of Foreign's present rights under such patents being set out in the attached Schedule.

5. Technical Data: Foreign's entire right, title and interest in and to the use in the world of all Technical Data which Foreign is then entitled to use anywhere in the world; and thereafter during the term of this Agreement, Foreign shall assign and transfer promptly to the Joint Company any and all world rights with respect to Technical Data relating to the Licensed Products and all other products being manufactured by the Joint Company, which Foreign shall acquire during such term incidental or relating to such products.

Foreign shall take all such action and shall execute all such documents as the Joint Company may deem necessary or desirable to effect, perfect or confirm, record or otherwise, the transfers and assignments to the Joint Company referred to above, including, without limitation, the full and complete disclosure to the Joint Company of Foreign's Technical Data, and lists of Foreign's distributors and customers for all of the Licensed Products and other products produced or sold by Foreign which may be similar to the products manufactured or sold from time to time by the Joint Company.

In the above Sections, the term "Technical Data" shall mean formulae, inventions, whether or not patentable, secret processes and technical information relating to the products and to the production, manufacturing,

engineering and test data, specifications, application instructions, information regarding uses, raw materials and methods for controlling and analyzing quality, and sample copies of advertising and publicity material , except that information received in confidence from others or information forbidden to be disclosed by virtue of any law or governmental regulation restricting the dissemination of such information shall not be included.

CHAPTER THREE

DIRECTION AND MANAGEMENT

1. BOARD OF DIRECTORS

In most jurisdictions, the Board of Directors of a company is responsible for its management and control, which includes the establishment of overall corporate policies. Among other things, the Board appoints the officers who implement the policies of the Board and administer the company's affairs from day to day. Depending on the laws of the incorporating jurisdiction, corporate bodies as well as individuals may hold a seat on the Board; if a corporation is a member of the Board, it will designate some individual or representative to occupy that position.

The Board will usually act through resolutions by majority vote, and will be composed of directors appointed by each partner in proportion to its ownership of the joint company. These aspects of the joint company may be altered, however, in tailoring the board to meet the particular needs of the partners, and the following are some of the issues the partners may wish to consider.

A. NUMBER OF DIRECTORS

PROBLEM: The partners must decide on how many directors the Joint Company will have.

COMMENTS: There is no optimum size of Board for all circumstances. Some factors which will influence its size are:

1. the laws of the incorporating jurisdiction requiring a minimum number;
2. the number of partners deserving representation on the Board;
3. the percentage control of each partner;
4. the ability of each partner to provide suitable directors;
5. the desirability of having many different points of view and expertise on the Board;
6. the requirements for a special majority for Board decisions;

   and

7. the requirements of business efficiency.

B. PARTNERS' REPRESENTATION ON THE BOARD

PROBLEM: It must be decided how many representatives each of the partners is to have on the Board of Directors.

COMMENTS: It is common in joint ventures for the representation of each partner on the Board to reflect the ownership of the partners, but other alternatives also exist.

POSSIBLE ALTERNATIVES: Besides having control through directorships in direct proportion to ownership, a minority owner might want of representation on the Board equal to, or greater than, the representation of the majority owner.

One area in which either of these approaches might be useful is where, for instance, local law prohibits majority foreign ownership, but the foreign partner insists on majority representation on the Board. Another is where the partners decide that it is most convenient and practicable for the local partner to exercise control of the joint company through a greater representation on the Board than his shareholdings might otherwise entitle him.

C. CHOICE OF DIRECTORS

COMMENTS:

Since the directors are elected by the shareholders, each partner will wish to appoint its own representatives to the Board.

To facilitate the convening of meetings, the partners will usually wish to have local residents as their representatives on the Board. If the Board is to have non-resident individuals as well, it might be convenient to appoint an Executive Committee composed of residents. The foreign partner will usually find it most convenient to choose his representatives to the Board from amongst those of his employees who are working for the Joint Company.

D. ELECTION OF DIRECTORS

COMMENT:

Directors are normally elected by majority vote of the shareholders. In the absence of cumulative voting requirements in either the incorporating documents or local company laws, the majority shareholder would be able to elect all of the directors.

It is necessary, therefore to assure that each partner is able to secure his agreed-upon representation on the Board.

POSSIBLE SOLUTIONS:

1. Binding Nominations:

In jurisdictions where shareholders' agreements are specifically enforceable, (most common law jurisdictions) provision in the joint venture agreement that each partner shall have the right to nominate a specific number of directors will suffice. In addition, such provisions should be inserted in the incorporating documents where permitted.

2. Different Classes of Shares:

Where shareholders agreements are not specifically enforcable, such as in some civil law jurisdictions, the issuance of different classes of shares, each bearing the right to nominate a specific number of directors, can be utilized. Such provisions are naturally contained in the incorporating documents.

POSSIBLE CLAUSES:

1. The Board of Directors of the Joint Company shall consist of (number) directors.

2. A) Binding Nominations:

(Number) Directors shall be appointed by Foreign and (number) by Local. In their capacities as shareholders, Foreign and Local agree that they shall nominate (number) and (number) directors respectively, and that each shall vote for the nominees of the other.

B) Different Classes of Shares:

As registered owner of the Class A shares, Foreign shall be entitled to make binding nominations for the appointment of (number) directors, and Local, as registered owner of the Class B shares, shall be entitled to make binding nominations for the appointment of (number) directors. Both Foreign and Local agree to take all steps necessary to secure the appointment of the above said nominees in accordance with the laws of (jurisdiction of incorporation of Joint Company).

C) Alternative Clauses:

The affairs of the Joint Company shall be managed by a Board of (number) Directors, (number) of whom shall be nominated by Foreign and (number) of whom shall be nominated by Local. Foreign and Local shall each vote all shares in the capital stock of the Joint Company owned or controlled by them for the election and maintenance in office of the persons so nominated.

Foreign and Local agree that prior to the annual meeting of the shareholders of the Company, each will inform the other of the names of (number) persons qualified in all respects to be elected, such persons being hereinafter referred to as "nominees", and each will support or cause to be supported at each annual meeting the election as directors of the Company for the ensuing year the (number) nominees so selected, by nominating or seconding their names as candidates,

by voting [illegible], and by supporting their election in any other fashion which may appear necessary. In the event that either foreign or local shall fail to notify the other prior to any annual meeting of the names of its (number) nominees, then it shall be deemed to have selected as its nominees the nominees representing it on the board of directors of the Joint Company immediately prior to the annual meeting.

E. REPLACEMENT OF DIRECTORS

PROBLEM: It is necessary to assure means by which the partners can easily replace their nominees on the board of directors.

COMMENTS: Whereas in large, widely-held corporations, there may be a tendency for management to seek safeguards against replacement by adopting policies such as the staggered voting for directors, etc., the boards of directors of joint venture companies, at least while in their infancy, generally are constituted to reflect closely the interests of the partners.

It may be best to stipulate in the incorporating documents, if possible, that casual vacancies on the Board are to be filled by the shareholders. If, however, the local company law provides that casual vacancies are to be filled by the Directors, and that the exercise of the Directors' discretion may not be fettered by agreement, then the replacement of directors by nominees of particular partners will require the cooperation of all the directors.

In the event that between annual shareholders' meetings of the Joint Company, either Foreign or Local desires to replace any or all of its nominees on the Board of Directors of the Joint Company, the other shall join in all necessary acts, steps and proceedings, and shall cause the shares of the Joint Company to which he is beneficially entitled to be voted in favour of the removal or such nominee or nominees, of the transfer of the qualifying share of shares of such nominee or nominees to the person or persons selected by Foreign or Local, as the case may be, and of the election in his or their place and stead of a qualified person or of qualified persons selected by the party hereto whose nominee shall have been so removed.

Nothing contained in this Agreement is intended or shall be construed to bind the parties hereto or their nominees on the Board of Directors of the Joint Company as to the method or manner of the exercise of the discretion vested in them as directors of the Joint Company concerning their management of the affairs thereof. All clauses of this agreement will be read subject to the provisions of this paragraph.

[illegible]

Where a large Board is [illegible] upon, it [illegible] be found convenient to [illegible] an Executive [illegible] of the Board, often consisting of three members of the Board, to whom the Board [illegible] delegate some or all of its powers. The [illegible] might be composed of individuals resident in the [illegible], and carry out all the powers of the full Board between its [illegible] meetings. Where [illegible] the [illegible] of the [illegible] of the Joint Company.

Provision for [illegible] is made in the incorporating [illegible] stipulating that the [illegible] Directors [illegible]gate some or all of its [illegible] consisting of [illegible] Directors.

[illegible] CLAUSE:

The Directors may delegate any of their powers to committees, consisting of such one or more of their body as they think fit. Any committee so formed shall, in the exercise of the powers so delegated, conform to any regulations that may be imposed on it by the Directors. All committees shall in the exercise of the powers so delegated, conform to any regulations that may be imposed on it by the Directors

All committees shall in the exercise of the [illegible] to them, and in the transaction of [illegible], conform to any mode of proceedings and regulations which may be prescribed by the Directors, and subject thereto may regulate their proceedings in the same manner as the Directors may do.

C. [illegible]

PROBLEM:

Because the company law of most jurisdictions [illegible] decisions of the Board are to be taken by majority vote, and because a simple majority might permit the nominees of one partner to make all decisions, provision must be made to protect minority interests.

POSSIBLE SOLUTIONS:

1. Special Majority:

   It is fundamental in most joint venture agreements that the nominee directors of minority partners be given a veto power over all questions fundamental to the Joint Company and the relations of the partners to it, by requiring a special majority vote of the directors. The special majority must be large enough to include at least one director nominated by each minority partner.

All requirements for a special majority or a minimum vote by directors should be inserted in the incorporating documents of the Joint Company.

Rather than specifying merely that decision may be made "by a simple majority vote of those directors present and voting", it is better to stipulate the exact minimum number of votes required, since it assures that at least one nominee of all partners will be required to pass a directors' resolution.

Where the partners decide that such a veto power by each partner is not necessary for all decisions to be taken by the Board, the following is a list of items on which it is common practice to require a special majority vote or veto power.

1. Appointment of Chief Executive Officer
2. Appointment of other officers
3. The sale of a substantial portion of the assets of the Joint Company
4. Loans by the Joint Company to shareholders
5. Choice of auditors
6. Dissolution on Liquidation
7. Increases in the authorized capital
8. Decreases in the authorized capital
9. Transfers of shares
10. Changes in the joint venture agreement
11. Issues of new shares

2. <u>Unanimity:</u>

Another possibility is to require a unanimity of the directors on all decisions. This approach may be practical where the Board is small, but on a large Board, it might unnecessarily impede the Boards' efficiency.

3. <u>Simple Majority:</u>

In a 50/50 Joint Venture, where there is an equal number of directors nominated by the two partners, a simple majority vote will suffice to protect minority interests, provided there is no provision for the chairman or any other directors to have a casting or tie-breaking vote in the event of a deadlock.

4. <u>Casting Vote:</u>

The laws of the jurisdiction of incorporation may entitle the chairman of the Board to have a casting vote in the event of a deadlock, but it is unusually possible to counteract this by a clause in the incorporating documents.

POSSIBLE CLAUSES:

1. Simple Majority:

   All decisions of the Board of Directors shall require an affirmative vote of at least (number--it should be half of the total number of directorships plus one) directors.

2. Special Majority:

   All decisions of the Board of Directors shall require an affirmative vote of at least (number--it should be at least the total number of nominees of the partner with the largest number of nominees on the Board, plus one for each of the other partners) directors.

3. No Casting Vote:

   The Chairman shall not have a casting or second vote in the event of a deadlock.

H. QUORUM AND NOTICE

Where the vital interests of the minority partner are not involved in a question to be decided by the directors, and therefore a special majority vote or veto power might not be desired, it is nevertheless necessary to assure that the nominees' partners have a right to participate in the decision-making process.

By requiring that the directors receive prior notice of all issues to be discussed at directors' meetings, the partners can prepare their points of view, and will be kept informed of the affairs of the Joint Company.

In addition, it may be desirable to require that a number of decisions may be taken by directors without a specified quorum being present. Under the law of many countries, a directors' meeting may consist of as few as two directors. Reasonable notice to all directors may be an adequate safeguard against unauthorized assumptions of power by certain directors. An even surer safeguard is to stipulate a quorum for meetings which will be large enough to require the attendance by at least one nominee director of each of the partners. For convenience it is often provided that in lieu of a resolution of a duly constituted meeting, a resolution will be considered valid if agreed to in writing by all directors.

1. <u>Notice</u>: Prior written notice of all directors' meeting shall be sent to all directors at least 14 days before the meeting, specifying the time and place of the meeting, and indicating all matters to be considered thereat, and including copies of reports, studies, etc., relating thereto.

   Notice may be waived by the unanimous consent of all directors (in writing).

2. <u>Quorum</u>: A quorum of a meeting of the directors shall consist of (number--at least large enough that it cannot be constituted without at least one nominee of each of the partners being present) directors.

   Where a quorum is present, a simple majority vote of those present and voting shall suffice to pass a resolution, excepting where, as referred to herein, a special majority is required.

   In lieu of a validly constituted meeting as above described, any directors' resolution shall be considered to have been validly passed if consented to in writing by all the directors.

2. EXECUTIVE [illegible]

One of the most important problems encountered in every joint venture arrangements is to maximize the utilization of local personnel in the Joint Company on the one hand, and to ensure that the Company receives the best possible management and direction on the other.

It is generally agreed that the long run interests of a developing country are best served if the participation of properly trained and qualified personnel from the developing country in all offices of the Joint Company, including the chief executive office, is maximized.

From the developing country's point of view, maximum participation by local personnel increases the country's level of technical and administrative expertise. The Joint Company also benefits from adopting such an approach because locally recruited personnel may be paid on the host country rather than a foreign scale. The foreign partner benefits because top flight executives can not generally be spared for long periods of time from the head office, and this fact has often been cited by executives as one of the major deterents to undertaking operations in developing countries. On the other hand, one of the most important contributions of the foreign partner to the joint venture is the furnishing of experienced and competent personnel to assure that the Joint Company's operations are conducted in the most competent and profitable fashion.

The requirements for localization on the one hand and executive competency on the other are not incompatible, however, if the personnel provided by the foreign partner assist in training locals to assume maximum and even complete responsibility as expeditiously as possible.

[illegible]

1. <u>The Chief Executive</u>: If the chief executive officer (President or Managing Director) is to be appointed initially by the foreign partner, then provision must be made in a shareholders' agreement, by distribution of voting shares, or in the incorporative documents of the Joint Company for approval of his appointment after a specific period by the local partner. In adopting this approach, each partner must be satisfied as to the competence and desirability of the individual appointed.

ii. <u>Alternating Chief Executives</u>: Another approach is to provide that the right to nominate the chief executive officer shall alternate between the partners after the expiration of each term of, for example, two years.

This system permits the opportunity for local personnel to assume responsibility and achieve on-the-job training, but it does not provide for the consultation of the other partner as a general rule, thereby working against the keynote of every joint venture relationship, namely co-operation between the partners.

iii. <u>Joint Chief Executives</u>: Another possibility is to have joint offices, such as joint presidents or managing directors, with each partner appointing his own nominee.

This approach assures that a nominee of each partner has the same right to all corporate information, and furthermore, that on-the-job training of the local nominee will be as intensive as possible. It may not be a practical approach, however, unless the two nominees are highly compatible.

iv. <u>Functional Chief Executives:</u> One approach frequently adopted is to divide the corporate responsibilities on functional lines, such as administrative and technical. The chief executive officer, for example the President, might be the nominee of the local partner, and his responsibilities in the day to day management will involve all non-technical questions. The Executive Vice-President, for example, might assume responsibility for all technical problems, and be the nominee of the foreign partner who is providing the technical data, information, assistance and know-how to the joint venture.

This approach recognizes the reality of most business operations in any event, where the chief executive officer may not necessarily possess expertise on all aspects of production, and delegate these responsibilities to an expert. Furthermore, as the chief executive officer, the nominee of the local partner is in an ideal position to oversee operations and call upon advice and assistance from the nominee or nominees of the foreign partner.

The functional distribution of offices between nominees of the partners can be carried out at all senior executive levels, with appointees from the foreign partner assuming vice presidential posts in respect of, for example, production, finance, foreign sales, etc., with nominees of the local partner occupying posts in respect of, for example, domestic sales, publicity, personnel, government relations, supply, etc.

In any functional division of powers, it is desirable that local personnel be trained as quickly as possible to assume all operations, and accordingly assistant positions manned by local personnel might be created for each of the posts occupied by nominees of the foreign partner until such time as they might be replaced.

POSSIBLE CLAUSES:

i. <u>One Chief Executive:</u>

The Chief Executive Officer (President or Managing Director) of the Joint Company shall be a nominee of Local (or Foreign).

ii. <u>Alternating Chief Executives:</u>

The Chief Executive Office of the Joint Company shall be the office of the President (Managing Director).

The first President (Managing Director) of the Joint Company shall be a nominee of Foreign (Local), who shall hold such office until the second annual meeting of the company, at which time he shall be replaced by a nominee of Local (Foreign). The said appointee of Local (Foreign) shall hold such office for the ensuing two years, and then, and for every two years thereafter, the right to nominate the President (Managing Director) shall alternate between Foreign and Local.

iii. <u>Joint Chief Executives:</u>

The Joint Company shall have two chief executive offices, both of which shall carry the same authority and position, and which shall be occupied by two persons, each called a Joint President (Joint Managing Director). Both Foreign and Local shall nominate one Joint President (Joint Managing Director) each.

iv. <u>Functional Chief Executives:</u>

a. The Chief Executive Officer (President or Managing Director) of the Joint Company shall be a nominee of Local.

b. The [illegible] and [illegible] President ([illegible]) [illegible] [illegible] or [illegible] responsibilities [illegible] law of (Country [illegible]) [illegible] be to administer all the [illegible] subject to [illegible] hereof.

c. The Joint Company [illegible] office to be held [illegible] position is that of [illegible] Production (Executive Vice President [illegible]).

d. Without limiting the duties and [illegible] of the Chief Executive Officer [illegible] Section 2 hereof, the principal [illegible] or such Executive Vice President [illegible] (Executive Vice President [illegible]) [illegible] to superintend all technical aspects [illegible] production, including, without limiting the generality of the foregoing, the utilization of industrial property, technical data and [illegible] inputs, machinery and equipment; training of technicians; maintenance of machinery; and the performance of all other duties necessary to [illegible] the production standards required of the Joint Company.

In conformity [illegible] the [illegible] the Joint [illegible] applicable, the parties may wish to [illegible] the Joint [illegible] are [illegible] the [illegible] obligations of the [illegible] parties in this regard.

[illegible] shall [illegible] that as [illegible] business [illegible] officers and employees of the Joint Company shall be recruited locally in that country, [illegible] by [illegible] officers and employees of the Joint Company [illegible] of [illegible], recruited from outside that country, or recruited by foreign, shall, in addition to their normal responsibilities and duties as officers and employees of the Joint Company, be responsible for assisting to train individuals recruited locally in that country in all aspects of their offices or employments with a view to ensuring that as many of the offices of the Joint Company as possible shall be or become occupied by such locally-recruited individuals.

[illegible]

It must be determined how the [illegible] partners [illegible] appointment of [illegible] are [illegible] agree.

The establishment of the posts of the officers [illegible] Joint Company will have been provided for in the incorporating documents. In most [illegible] are appointed by the directors of the [illegible] jurisdictions, directors are considered [illegible] the company, and not of the interests of particular shareholders. Accordingly, neither the directors [illegible] shareholders who appoint them [illegible] enforceable contracts to limit directors' powers or to fetter their discretion, such as by stipulating for the appointment of particular officers.

There will be little difficulty in securing the appointment of nominees of particular partners to the various post when the partners are on good terms because the directors will cooperate to appoint the individuals agreed upon. Where the parties are in disagreement, however, the question becomes more difficult.

[illegible]
[illegible]:

Although, as [illegible], [illegible] agreement for the appointment of [illegible], it [illegible] nevertheless [illegible] provisions of the [illegible] for co-operation in the [illegible] of the [illegible].

[illegible] corporation [illegible] of the [illegible] special majority for [illegible] of officers, [illegible] special majority [illegible] the consent of [illegible] Director [illegible] of the [illegible].

[illegible]
[illegible]:

The [illegible] to the office of [illegible] Director, [illegible] to the office of Executive Vice-President - Production, and the nominee of (include here any other offices which are to be created and occupied by nominees of particular partners), and shall continue to do so from time to time throughout the term of this Agreement.

In the event that any of the above provisions shall be held by any court of competent jurisdiction to be invalid, the parties hereto agree to co-operate in the revision of these presents in order to ensure that the intent of this Agreement is carried out insofar as is legally possible.

CHAPTER FOUR

FINANCIAL POLICIES

FINANCIAL POLICIES

A. PROFIT POLICY:

PROBLEM: The Joint Company must decide on whether profits are to be retained or distributed to the partners.

COMMENTS: Some of the principal purposes for retaining profits are as follows:

1. for working capital;
2. for expansion of production and sales facilities;
3. for acquisitions;
4. to replace capital assets;
5. to retire debt;
6. to redeem capital stock;
7. to comply with local laws or the conditions of issuance of some of the capital stock of the Joint Company, requiring certain compulsory reserves, etc.;
8. foreign exchange controls preventing the expatriation of profits from the host country.

Some of the principal reasons for distributing profits are as follows:

1. The partners may wish to recover their capital investment;
2. The partners want to derive a profit;
3. It may be necessary to obviate taxes, if any, on undistributed earnings;

4. If either or both partners consolidates its balance sheet and profits and loss statements with those of the Joint Company, there may be less incentive for the distribution of profits, because [illegible] the earnings of each will reflect those of the Joint Company. This is especially true if either partner is a public company, the value of whose shares will often be determined by a [illegible] earnings multiple, or is undertaking acquisition on the basis of book value.

5. If the Joint Company seems to be in danger of going under, both partners will probably want to recover as much of their investment as possible by distributing what profits there might be.

6. If the taxes paid by the Joint Company on its profits and retained earnings are less than the taxes paid by each partner on distributed earnings, there may be an incentive to retain profits.

7. Generally, a confidence in the long term success of the Joint Company may inspire the partners to retain a greater percentage of earnings.

In general, it would appear that the greater the earnings that are retained by the Joint Company, the greater will be the economic advantages to the host country and to the long term success of the Joint Company. Accordingly, the partners should adopt financial policies which ensure the greatest possible retention of profits.

Mitigating against this approach will be the desire of one or both of the partners to receive a fair return on investment.

Some of the ways in which the partners, especially the foreign partner, can profit from the Joint Company are as follows:

1. Dividends
2. Interest
3. Royalties
4. Management fees
5. Fees for provision of technical data, information and know-how
6. Salaries paid to its personnel who are employed by the joint company
7. Through increases in its own net worth from consolidated accounting principles

POSSIBLE APPROACHES:

In the absence of prohibitions against distribution, the following approaches might be adopted to ensure the greatest possible retention of profits in the Joint Company.

1. Compulsory Reserves: The joint venture agreement might stipulate that compulsory reserves be established before dividends may be paid.

It is impossible within the scope of this study to suggest a compulsory reserve formula which should apply in all cases, but some possibilities are to express it:

(a) as an absolute amount;

(b) as a fixed percentage of profits;

(c) as a progressively increasing percentage of profits.

2. Prior Uses of Profits: Where the partners can foresee specific uses for profits, the joint venture agreement might specify that no profits may be distributed until such uses are satisfied.

3. Indication of Intention: Where the partners feel that either of the above two approaches might be too inflexible, joint venture agreements commonly stipulate that the parties recognize the desirability of retaining as much profits as possible in order to provide for the greatest possible growth for and the greatest financial viability of, the joint company.

POSSIBLE CLAUSES:

1. The parties hereto recognize that their own and the best interests of the Joint Company will be best served by taking all steps reasonable to ensure the expansion of the production facilities of the Joint Company, as rapidly as market conditions permit, and to this end, agree to retain sufficient earnings in the Joint Company before distributing profits to the shareholders, as may be reasonably required in the circumstances to provide for such expansion, and for the other requirements of conducting the affairs of the Joint Company according to sound business practices.

2. Before any profits of the Joint Company shall be distributed as dividends to the shareholders thereof, ____ percentage of each year's net after-tax profits shall be set aside to meet the capital and other requirements of the Joint Company.

AUDITORS AND BOOKS OF ACCOUNT

PROBLEM:

The Joint Company must adopt accounting procedures which will represent accurately its financial status.

COMMENTS:

In a wholly-owned operation, the books of account do not necessarily have to reflect the true worth of the company. They may be designed, for example, to minimize taxation by taking maximum allowable depreciation. They must also provide the directors with the requisite data for making sound business decisions.

In joint ventures, a further requirement is required; the books must satisfy the needs of the partners as well, in order that they can ascertain the true state of their investments. Where reserve funds are called for, the accounting methods must be consistently applied from year to year, and on a basis that is thoroughly understood by the partners.

POSSIBLE APPROACHES:

Most joint venture agreements provide firstly, that the auditors must be acceptable to all partners, and secondly, that they shall be an internationally recognized firm of auditors. This latter step is usually adopted because of the desire of the foreign partner to have auditors and accounting practice with which he is familiar, and also because of the frequently expressed complaint that it is difficult to find competent auditors in developing countries.

Where, however, competent local auditors can be found, the major advantages in utilizing them will be that their services are often more reasonably priced, and secondly, they may be more familiar with local administrative practices and have closer contacts with local officials, which can often obviate many difficulties.
Under the laws of many countries, the auditors are selected annually by the shareholders. The partners might stipulate on a firm of auditors in the joint venture agreement, or else provide for a special majority in the incorporating documents which will require the approval of all partners for their appointment.

POSSIBLE CLAUSES:

1. Proper books of account and other records shall be kept regarding all transactions entered into by the Joint Company, and shall be freely accessible to the partners at all reasonable times.

2. The auditors of the Joint Company shall be (name of a host country accounting firm).

3. The auditors of the Joint Company shall be appointed at the annual meeting of shareholders by unanimous vote (or by a special majority which is large enough to require the approval of all shareholders).

CHAPTER FIVE

MARKETING ARRANGEMENTS

[illegible]

A. [illegible]

PROBLEM: The Joint Company should not be prevented from having access to as large a market area as it is capable of supplying.

COMMENTS: A common complaint of local partners of joint ventures is that the foreign partner wants the Joint Company to supply only the host country market and perhaps those in a few neighbouring soft currency countries, while it services all of the profitable world markets from its wholly-owned facilities located elsewhere.

One of the top economic priorities of all developing countries is to establish export industries to earn foreign exchange. Accordingly, the Joint Company should aim at obtaining access to foreign markets, particularly [illegible] hard currency countries.

Four market regions the Joint Company may wish to exploit are as follows:

1. the host country
2. the country of the foreign partner
3. other specifically designated countries
4. the world

The principle non-economic factor mitigating against the Joint Company being able to exploit all markets of the world is that the licensing agreements obtained from the foreign partner and elsewhere will often impose a territorial [illegible]

restrictions on [illegible].

In negotiations [illegible] with the [illegible], the foreign partner will [illegible] able [illegible] the Joint [illegible] into and [illegible] with other or related [illegible] giving them the right to [illegible] property in other countries.

Accordingly, [illegible] host country [illegible] the following [illegible]

1. the industrial [illegible] patents, trademarks and trade names owned by or licensed to the foreign partner;

2. the licences [illegible] made by the foreign partner or licences to other parties, indicating:
   (a) the date of expiry of each;
   (b) the geographical area covered;
   (c) the conditions under which each may be terminated by the foreign partner or licensee;
   (d) the products and industrial property included in each such licence or sublicence;
   (e) the royalties payable under each;

M[illegible] [illegible] as is [illegible], th[illegible] to bar[illegible] the [illegible] the Joint Company.

In the case [illegible] parties [illegible] who [illegible] may be [illegible] expiry [illegible] the mon[illegible], [illegible] the Joint Company. [illegible] of not more than [illegible] years [illegible] make new [illegible] t[illegible] applicable to the [illegible] from time to time [illegible] it becomes [illegible] exploiting them.

A further [illegible] ... in the possible [illegible]olation [illegible] ... [illegible] of [illegible] ... [illegible] ... [illegible] ... [illegible] of [illegible] ... to [illegible] to [illegible] than [illegible] ... the fo[illegible] of [illegible] ... or [illegible] ... [illegible] in [illegible] ... [illegible] ... [illegible] ... of those operati[illegible] to the Joint [illegible].

B. [illegible]

[illegible]: Provision should be made for the [illegible] all the data and information available to the [illegible] partner for the promotion, advertising and sale of [illegible] products.

[illegible]: The cost of giving promotion [illegible] advertising [illegible] prepared may be very [illegible]. The Joint [illegible] therefore make [illegible] for obtaining as many of [illegible] materials as possible from the foreign partner.

The partners [illegible] agree that the cost to the Joint Company of such materials should be only the cost of printing and transportation of the materials [illegible]. [illegible] portion of the cost of creation need not be [illegible] because the foreign partner will have made [illegible] in any case, and it is to its advantage that the best possible marketing aids be used by the Joint Company. Where the foreign partner has extra marketing aids on hand, it is not unreasonable that they shall be [illegible] to the Joint Company free of charge. Provision should [illegible] be made for the right to use all new aids developed [illegible] the cause of the joint venture agreement.

POSSIBLE CLAUSE:

Foreign shall supply to the Joint Company free of charge all advertising and marketing aids which it now has or shall acquire during the term of this Agreement and which relate to the products produced or sold by the Joint Company. More specifically, but without limiting the generality of the foregoing, such advertising and marketing aids shall include brochures, pamphlets, catalogue sheets, labels, boxes, cartons, packaging, diagrams, manuals, designs, logos, pictures, descriptions, instructions, films, scripts, recordings, colour schemes and other data designed to explain assist or promote the sale, distribution, use, and servicing of the said products.

C. [illegible]

PROBLEM:

It is necessary for the Joint [illegible] to establish [illegible] marketing organization which can secure the fullest practicable penetration of both the local and foreign market areas.

[illegible]TS:

In most developing country joint ventures, the local [illegible] will be the primary market [illegible] of the Joint [illegible], and the local [illegible] will be [illegible] great [illegible].

The exploitation of [illegible] many [illegible] as [illegible] by the Joint Company should be the aim of every developing country joint venture. The development of [illegible] requires expertise and [illegible] which the foreign partner may be in a [illegible] to provide.

[illegible] MARKETING [illegible]ZATIONS:

Two basic ways in which the Joint Company's products can be sold in both local and foreign markets are

(1) directly to the ultimate consumer; and

(2) indirectly through intermediaries or middlemen.

1. <u>Direct Selling:</u> Some of the ways in which direct [illegible] might be organized are as follows:

   (a) <u>Salesmen:</u> The Joint Company might have its own salaried or commissioned salesmen who call upon customers on behalf of the Joint Company.

(b) Sales Subsidiary: For reasons of convenience, taxation, etc., it may be considered expedient to establish a [illegible] sales subsidiary of the Joint Company, either in the host country or abroad. In addition, the sales subsidiary might use wholly-owned subsidiaries of its own to conduct selling operations in [illegible] countries. Use of a sales subsidiary will [illegible] be the most practical [illegible] for large-scale international sales operations, [illegible] it may be [illegible] base [illegible] subsidiary in [illegible] haven jurisdiction.

(c) Branches: [illegible] international tax and other ramifications, [illegible] may be [illegible] branches in the foreign market areas. Another possibility [illegible] that the sales subsidiary conduct its operations through branches in some or all market areas.

(d) [illegible] Agents: [illegible] Joint Company may engage independent commission agents in each of the market areas to assume responsibility for selling the goods.

(e) Foreign Partner as Sales Agent: In some joint ventures the international sales operation of the foreign partner undertakes to sell the Joint Company's goods on a commission basis.

A major drawback to the Joint [illegible] its own direct [illegible], subsidiaries or [illegible] for [illegible] of [illegible], [illegible] cover the host country [illegible] commission agents on the [illegible] foreign partner [illegible] establish sales facilities [illegible]. [illegible] commission agents, however, [illegible] other manufacturers as well, [illegible] attention to securing the [illegible] for the Joint Company's [illegible] subject to little control [illegible].

Often, therefore, the use [illegible] foreign partner's existing [illegible] might represent an excellent means of achieving [illegible] penetration of foreign markets without capital [illegible] or the difficulty of recruiting a large international sales force. The commission charged for such services may also be less than would be charged by independent [illegible], since the foreign partner will participate to the extent of his equity in any savings accruing to the Joint Company.

3. In [illegible] direct sel[illegible]

(a) [illegible] company [illegible]

[illegible]

[illegible] the [illegible]

vo[illegible]me [illegible]

the [illegible]

[illegible]

[illegible] st[illegible] tribution pr[illegible] the retail market pri[illegible] increa[illegible] Joint Comp[illegible].

(b) Sales to [illegible] Partner: [illegible] partner is experienced in world marketing of the products, and the Joint Company [illegible] to such areas, [illegible] the foreign partner purchase the pr[illegible] from the Joint Company and then assume re[illegible] their ultimate sale.

The problem with [illegible], [illegible] any one firm [illegible] the output, [illegible] price and [illegible].

[illegible] As a general rule, the Joint Company w[illegible] achieve the widest [illegible] in foreign markets with the [illegible] by utilizing [illegible] directly to consumers, or [illegible] interested [illegible] who can then sell [illegible] the public. [illegible] may be independent agents in each market [illegible] the existing international sales organization [illegible] partner might be utilized.

After the Joint Company has achieved [illegible] penetration [illegible] this approach, and has the requisite capital, it might then consider the possibility of undertaking its own direct sales operations through its own [illegible] branches or subsidiaries. This stage will be reached when [illegible] cost of such direct sales including the necessary capital outlays, becomes less than the cost of commissions and other expenses of direct sales through independent agents, or of indirect sales, including the profit lost from selling through intermediaries.

D. [illegible]

PROBLEM: [illegible] facilities for [illegible]

COMMENT: [illegible] of the Joint [illegible] efforts [illegible] providing adequate [illegible] in the market areas.

Like the [illegible] organization, the Joint Company may find it most [illegible] to keep its [illegible] capital outlays for servicing facilities to a minimum.

POSSIBLE APPROACHES: It may be [illegible] operations, and [illegible] the form of selling organization may determine [illegible] servicing organization. Servicing will not necessarily present any difficulty [illegible] the sel[illegible] premises in the mar[illegible] facilities exist, however, [illegible] where, for example, [illegible] independent agents are used, the independent service arrangements may have to be made.

Servicing whether performed by related or independent agents, may require services in relation to installation, customer training and instruction, warranty work, and continuing maintenance and repairs. The Joint Company has a direct interest in assuring that all such operations are performed competently, expeditiously, and at a minimum cost, since they

all [illegible]

[illegible] difficult [illegible]

A [illegible] to [illegible] all re[illegible]

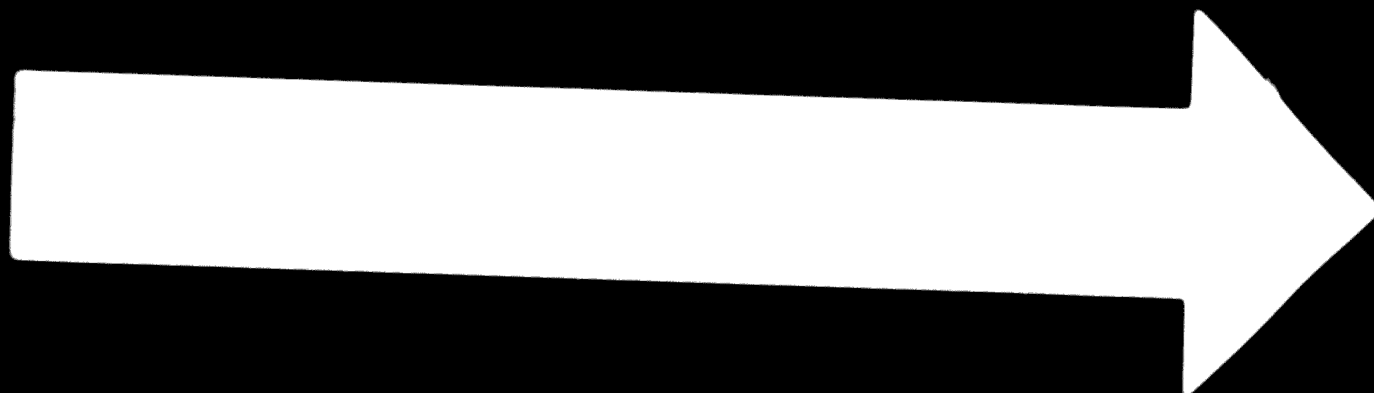
It [illegible] formed [illegible] may wish to [illegible] Some pos[illegible]

1. Establi[illegible]

2. Establish [illegible]

3. Declare that [illegible] profit, or at a low profit;

4. Make the authorized sales agencies non-exclusive for short terms only, [illegible]



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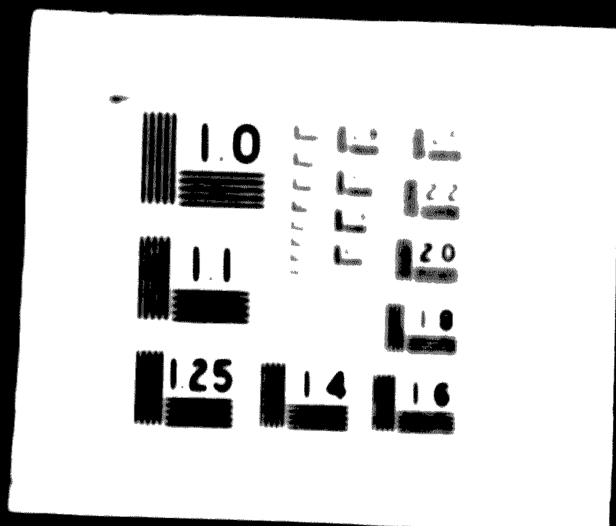


F. [illegible] TRADE MARK

[illegible]

1. PARTIES: The licen[illegible] will be the Joint Company and the licensee will be [illegible], [illegible] United States.

2. [illegible]: [illegible] mention that the li[illegible] has the right to license certain industrial property rights and that the licensee wishes to use them in respect of certain specified products.

3. DEFINITIONS: It is common to define items such as
   (a) the territory for which the rights are granted; and
   (b) the products on which the names and marks are to be used, i.e. the authorized products.

4. GRANT OF LICENCE:

The Joint Company will unity to assure that the license granted is an exclusive one for the territory.
In deciding upon the territory in which the Joint Company shall obtain the right to use the trade marks and trade names, the same considerations apply as with respect to the territory in which it obtains the right to manufacture and sell the authorized products from Foreign. Generally, the Joint Company will wish to obtain as large a territory as possible.

In some developing countries, it may be national policy to prohibit the use of foreign trade [illegible] trade in competition with locally produced goods. [illegible] the case, the partners will have to agree on new names and marks for the host country, but will [illegible] that products exported from the [illegible] the international marks and names with their existing goodwill.

[illegible]:

A. Foreign hereby grants to the Joint Company the right during the continuance and subject to the provisions of this Agreement to use each and every of the trade marks and trade names upon or in connection with the [illegible] products manufactured and/or assembled by or on behalf of the Joint Company within the territory and which comply with the relative standards, and the Joint Company agrees that it will use the trade marks and trade names upon or in connection with all authorised products so manufactured and/or assembled.

B. The right of the Joint Company to use the trade marks and trade names as aforesaid is an exclusive right for the whole of the territory.

REGISTRATION: To protect against unauthorised use of the trade marks and names by third parties, registration is usually required.

POSSIBLE CLAUSE:

Prior to the use by the Joint Company of any of the trade marks or trade names, Foreign and the Joint Company shall take all steps necessary to ensure that the said trade marks and trade names in this agreement, where necessary, are registered in all of the appropriate jurisdictions within the territory and shall take such other necessary steps as are required to prevent the unauthorized use by other parties of the said trade marks and trade names. Foreign and the Joint Company shall from time to time execute and do all such documents, acts and things as may be required to ensure that the Joint Company's use of the trade marks and trade names is in all respects in accordance with the law and practice of the various jurisdictions within the territory and is not injurious to Foreign's rights as proprietor of the trade marks and trade names.

6. **TERMINATION:**

The grant of licence may be made

(a) in perpetuity;

(b) for a fixed term in years; or

(c) for the duration of the joint venture; or

(d) for the duration of the patent licence agreement

In so far as the trade mark and trade name rights are worthwhile for the Joint Company to have, it will be advantageous for the grant to be for as long a period as possible.

Where the foreign partner is the licensor, [illegible] to tie the grant [illegible] the duration of [illegible] the joint venture. This [illegible] would [illegible] on the Joint Company, however, if the foreign partner decides to [illegible] after [illegible] money [illegible] expended to promote the products [illegible] withdrawal would mean a loss of [illegible] goodwill.

Accordingly, it is suggested that the Joint Company will generally be in a stronger position if the termination is independent of the duration of the foreign licensor's [illegible] participation in the Joint Venture.

As mentioned, it is not unreasonable that while the foreign licensor is a partner in the Joint Company that no royalties should be paid for the use of its trade marks and trade names. If such rights are to continue after withdrawal by the foreign partner, however, it is not unreasonable that royalties should be paid, and in such a case, the foreign partner should not object to granting such rights beyond the period of his participation in the joint venture.

If the alternative to tying the licence to the equity participation of the foreign partner is a fixed term agreement, the joint company will still suffer from the loss of goodwill upon being forced to give up use of the trade marks and trade names. The solution may be, therefore, for the Joint Company to become the owner rather than licensee of the trade marks and trade names it uses. This may be achieved in two ways, namely:

1. Assignment for the Foreign Partner:

   An arrangement may be made whereby trade marks and trade names are purchased by the Joint Company from the foreign partner. They may constitute part of the foreign partner's contribution to capital.

2. Adoption of New Marks and Names:

   Where the goodwill that use of the foreign partner's trade marks and trade names can bring to the joint company not significant, or may not be necessary to assist in either domestic or foreign sales or both, serious consideration may be given to the Joint Company establishing its own marks and names, so that all good-will generated will accrue to it, and will not be lost by expiry of time, withdrawal of the foreign partner, etc.

POSSIBLE CLAUSES:

1. The term of this Agreement shall be years, provided that notice of its intention not to renew this agreement be sent by Foreign to the Joint Company at least six months prior to the termination hereof. In the event that no such notice shall have been given, this Agreement shall continue for a further years, and thereafter until six months notice shall have been received by the Joint Company.

2. Notwithstanding the above provision, this Agreement shall terminate if the Joint Company shall become dissolved or enter into liquidation (whether voluntary or compulsory) or become subject to or submit to any

law for the relief of [illegible] or if a receiver shall be appointed [illegible] its assets or if any ex[illegible] the Joint Company.

7. **[illegible]:**

The Joint Com[illegible]y's op[illegible] more flexible if it h[illegible] the [illegible] to [illegible] its license rights and subl[illegible] to others.

POSSIBL[illegible]:

The Joint Company shall have the [illegible] to [illegible] the benefits to this Agreement, and to sublicense the rights to the trade names and trade [illegible], to such other parties and upon such terms and con[illegible] as it shall in its absolute discretion determine, provided however that it remains responsible to Foreign for its obligations hereunder and provided that such assignment or sublicence shall apply only to the designated territory.

8. **T[illegible] WHICH FOREIGN LICENSOR MAY WISH:**

(a) **Use of Trade Marks and Trade Names:**

It is customary for the foreign licensor to want clauses inserted in the licence agreement requiring the following undertakings of the licensee:

i. to comply with the legal requirements for affixing marks and names to the products;

ii. to notify the licensor of its manner of using the names and marks;

iii. to use only the authorised marks and names in association with the products;

iv. to not use the names and marks on any unauthorized product ; and

v. to not violate the territorial restriction placed on the use of the marks and names.

(b) <u>Inspection:</u>

To ensure that the goodwill associated with his marks and names is maintained, the licensor will generally want the following rights, namely:

i. to inspect the products bearing the names and marks;

ii. to test the products to ensure quality control;

iii. to investigate the marketing techniques relating to products bearing the marks and names; and

iv. to prohibit the sale of any non-complying product

(c) <u>Ownership:</u>

The licensor may wish the following affirmations by the licensee, namely:

i. that the use of the marks and names by the licensee does not derogate from the ownership thereof by the licensor; and

ii. that the licensee will deny or question the validity of the registrations of the marks or names;

(d) <u>Infringements:</u>

In case of or unauthorized use of the marks or names, the licensor will often require as follows:

i. that the licensor has the exclusive right to take

action against an infringer;

ii. that the licensee will assist in bringing any such action; and

iii. that the licensee will notify the licensor of any suspected infringements.

(e) Rights after Termination:

The licensor will often insist that clauses in respect of some or all of the following conditions come into effect upon termination of the license agreement:

i. the licensee will assist in cancelling any registrations there may be of the license agreement;

ii. the licensee will discontinue use of the marks and names;

iii. the licensee will return to the licensor at the latter's expense, or else destroy, again at the expense of the licensor, all advertising, stationery, containers, etc. bearing the marks and names; and

iv. the licensee will permit the licensor to purchase all inventories bearing the marks and names. The cost thereof should be the fair market value;

C. [illegible]

The follow[illegible] some possible [illegible] agency agreement, appointing [illegible] form or [illegible] as [illegible] agent, to sell the products [illegible] behalf [illegible] Joint Company.

I. DESIGNATION [illegible]

The [illegible] will have to decide whether the [illegible] an excl[illegible] for a specific territory, [illegible] the agent, [illegible] terms, such as lower commission [illegible] larger volume [illegible] possible. By a non-exclusive agency, [illegible] competition might be encouraged, resulting in increased sales [illegible]. One practice which might be followed is to designate a [illegible] agent for a particular region, but [illegible] verbally to not appoint another agent [illegible] performance becomes unacceptable. This [illegible] of competition may be sufficient to obviate the disadvantages of creating exclusive agencies, while at the same time, assuring their advantages to the Joint Company.

POSSIBLE CLAUSES:

The Joint Company hereby designates Foreign as a sales agent for the sale of the products in (territory) according to the terms and conditions hereinafter set forth.

The Joint Company reserves the right to sell directly to customers and to appoint another or other sales within (territory).

2. AGENT'S AUTHORITY: The concept of an agency is that the agent does not contract with the customers as a principal, but for and on behalf of the Joint Company.

POSSIBLE CLAUSE: Foreign shall have the authority to solicit and accept in the name of and on behalf of the Joint Company orders for the products at the prices and the other terms and conditions set forth in Schedule ... subject to approval from customers within the territory and to deliver the products so ordered to the said customers.

3. OBLIGATIONS OF AGENT: The Joint Company may wish to require certain undertakings of the agent in respect of use of its best selling efforts, advertising, non-competition, warranties, inventories, etc.

POSSIBLE CLAUSES:

(a) Best Efforts:

Foreign agrees to use its best efforts to promote the sale of the products in the territory and to maintain an adequate sales force and organization to do so effectively.

(b) Advertising:

Foreign agrees to advertise at its own expense in such manner and to such extent as effectively promote the sale of the products within the territory.

(c) Non-Competition:

Foreign agrees not to participate in, directly or indirectly, the manufacture sale or promotion of any other products that are similar to or competitive with the products, which are the subject matter of this agreement.

(d) Warrantees:

Foreign agrees that the only warrantees, guarantees, and

[illegible]

4. [illegible]: [illegible]

[illegible]: (a) [illegible] best eff[illegible] assist[illegible] products [illegible] will assist [illegible]

(b) Aids: The Joint [illegible] agrees to [illegible] to Foreign from time to time with samples of such promotional materials and other aids as it may deem appropriate, and shall have the right to approve any translations thereof or additional promotional materials and aids which Foreign may propose to use in the territory.

[illegible]: An agent may be [illegible] services, or else [illegible] performance. [illegible] of [illegible] remuneration, [illegible] great deal of [illegible] be necessary to [illegible] To ensure that the agent [illegible] rights, the commission [illegible] Joint Company [illegible]

POSSIBLE CLAUSE: The Joint Company shall [illegible] per cent of the F.O.B. factory [illegible] all products sold to customers [illegible] pursuant to orders solicited and [illegible] by [illegible] Such commissions shall be payable [illegible] customer for the products, and shall not be payable [illegible] the customer has made full payment therefore to the Joint Company.

RELEASE: There are many difficulties in ensuring that the [illegible] sold do not infringe industrial property rights of third parties and it is usual to include a release clause to protect the Joint Company in the event of an action against the agent.

POSSIBLE CLAUSE: No representation is made that the products or their use or sale do not infringe any patents, trade marks or trade names or other rights of third parties. Foreign agrees to release the Joint Company from and in respect of any and all claims by Foreign or by third parties for any such infringement.

7. [illegible]

[illegible]

POSSIBL[illegible]

[illegible] the Joint [illegible] in writing, to [illegible] of its intent [illegible] to terminate, until [illegible] export or import licenses, [illegible] to [illegible] its obligations [illegible] due in the ordinary course of business, or [illegible] of the obligations [illegible].

H. SOME POSSIBLE TERMS FOR A DISTRIBUTORSHIP AND SERVICING AGREEMENT.

Outlined below are some of the possible terms which might be inserted in a distributorship and servicing agreement, whereby the distributor purchases the products from the Joint Company for resale in its own name rather than in the name of and as agent for the Joint Company.

1. **GRANT OF RIGHTS:** As in an agency agreement, it may be most advantageous for the Joint Company not to grant exclusive distributorships for particular territories, but to give verbal assurance that they will remain exclusive if performance is good.

POSSIBLE CLAUSE: The Joint Company hereby grants to Foreign the right, but not the exclusive right, to serve as a distributor and service agent throughout the world of the products.

2. **OBLIGATIONS OF DISTRIBUTOR:** The following clauses contain some of the provisions which the Joint Company may wish to have included in the agreement.

POSSIBLE CLAUSE: Foreign hereby accepts the above grant of rights, and undertakes as follows:

(a) **Best Efforts**

To use its best efforts to promote, market and service the products throughout the world;

(b) **Organization**

To provide for and maintain at its sole expense a

sales and service organization adequate and competent to promote, sell and service the products effectively throughout the world;

(c) <u>Service Organization:</u>

to provide and maintain at its sole expense a service organization adequate and competent to provide technical advice to customers and prospective customers, and carry out installations, repairs and replacements of the products;

(d) <u>Inventory:</u>

to maintain an inventory of the products reasonably adequate to meet anticipated demand within each market region of the world;

(e) <u>Spare Parts:</u>

to maintain an inventory of spare and replacement parts, including all materials necessary to carry out all installation, servicing and repair operations;

(f) <u>Cooperation:</u>

to cooperate in all ways possible with the Joint Company to establish and maintain the standards and reputation of the products, to comply with all reasonable suggestions offered by the Joint Company which the Joint Company deems desirable for the stimulation of sales and the improvement of service operations, and to cooperate with such representatives of the Joint Company as the Joint Company may from time to time, at its option, send out for the purpose of supporting and promoting the efforts of Foreign

(g) <u>Advertising:</u>

to advertise, at its own expense, [illegible] to such extent as may reasonably be required to publicize the products within each market area of the world.

(h) <u>Reporting:</u>

at the request of the Joint Company, Foreign shall provide to the Joint Company a list including the names and addresses of all its customers, and the terms and conditions of all sales made to them, and of all servicing operations carried out by it, during the previous six month period.

(i) <u>Non-Competition:</u>

Foreign hereby agrees that it shall not undertake any other business, nor engage in the sale or servicing of any products other than those which are the subject of their Agreement, without the prior written consent of the Joint Company.

. OBLIGATIONS OF JOINT COMPANY:

It may be appropriate for the Joint Company to stipulate in a general fashion the obligations it has in dealing with the distributors. The following clauses may be appropriate.

<u>POSSIBLE CLAUSES:</u> The Joint Company hereby agrees and undertakes as follows:

(a) to use its best efforts to manufacture, deliver and sell to Foreign such products, spares and replacement parts as Foreign may, from time to time order; and

(b) to use its best efforts to provide Foreign with such advice and other assistance on matters relating to the marketing and servicing of the products as may reasonably be required to enable Foreign to effectively carry out its obligations hereunder, and to provide to Foreign as promptly as possible, samples of such sales promotion materials and order sales aids as the Joint Company may deem appropriate. The Joint Company shall have the right to approve any translations of these materials and aids before they are used anywhere in the world, as well as the right of prior approval of any additional sales promotion materials and sales aids which Foreign shall propose to use anywhere in the world.

4. GENERAL CONDITIONS: The following general conditions are often included in destributorship agreements to protect the manufacturer.

(a) No Agency: It is agreed that the relationship hereby established is solely that of buyer and seller, it being understood that Foreign is acting on its own account and is to have no authority to assume or create any obligation to make any representation, guaranty or warranty on behalf of the Joint Company with respect to any product or otherwise.

(b) Products: The Joint Company reserves the right to, at any time, add to or eliminate from its manufacturing operations any products, and to change any of the specifications thereof; provided, however, that any such addition, elimination or change shall not affect obligations created by any order of Foreign that shall have been accepted by the Joint Company prior to such addition, elimination or change.

(c) Orders: All orders by Foreign shall be in writing, and if made by telephone, telegraph, cable, telex, radio or otherwise, shall be confirmed in writing, and shall be subject to approval and acceptance in writing by the Joint Company, such approval and acceptance being effective when mailed, postage prepaid, to Foreign.

(d) <u>Suits:</u> In the event of any actual or threatened suit against Foreign or any of its customers by reason of the sale or use of the products, Foreign shall report the details thereof to the Joint Company, and the Joint Company shall furnish to Foreign such information it possesses which may assist Foreign or its customer in defending or determine dealing with the suit.

5. **CONDITIONS OF SALE:**

In establishing some of the legal conditions upon which the products are to be sold to the distributor, the following clauses might be considered:

All sales by the Joint Company to Foreign shall be subject to the following terms and conditions, and to such of the other terms of this Agreement as may be applicable:

(a) Passage of Title: All right title and interest in and to the products and parts purchased hereunder and risk of loss with respect thereto shall pass from the Joint Company to Foreign at the time and place of acceptance of the pr[illegible] the first international carrier handling [illegible].

(b) Warranty: The Joint Company shall replace free of charge or grant credit for the cost of putting in good working order, any products which are defective, provided that Foreign gives written notice of the defect within 90 days after receipt thereof by Foreign. The Joint Company reserves the right to inspect any products before replacing them, and will grant a credit to Foreign for the cost of freight for returning the same only if the product or products should prove to have been so defective that they could not have been put in good working order by Foreign at a reasonable cost, the reasonableness of which shall be determined by the Joint Company in its absolute discretion.

Except as provided herein, the Joint Company makes no warranty, express or implied, as to the products, and shall not be liable for any damage, whether direct, indirect or consequential, in connection with or resulting from the resale or use of the products.

No representation is made that the products or their use or sale by Foreign do not infringe any patents, trade marks or trade names or any other rights of third parties.

(e) <u>Price:</u> The prices at which Foreign shall purchase the products, including the replacement parts and spares, are those indicated in Schedule A hereto annexed. The Joint Company may change the said prices from time to time, and any such changes shall be effective   days following the date on which such changes may be posted by prepaid air mail addressed to Foreign.

6. RESALE AND SERVICING

Foreign shall be free to resell the products to customers throughout the world and perform its servicing obligations hereunder at whatever prices and on whatever other terms and conditions as Foreign shall deem appropriate.

7. TERMINATION.

Either party hereto may terminate this Agreement as of any date not less than days after its execution by giving at least months prior written notice of such intention to terminate to the other party, but no such notice shall be required for the Joint Company to terminate this Agreement in the event that Foreign shall fail to fulfil any of its obligations hereunder or shall fail to pay any amounts owing by it when due, or if the ability of Foreign to meet its financial commitments shall ever be in doubt.

CHAPTER SIX
PATENT LICENSING ARRANGEMENTS

For an industry in a developing country to manufacture a certain product, it may have to be either the owner or the licensee of the patent or patents relating thereto.

It is unusual for a developing country industry to own any patents, but it is almost universal practice for manufacturing joint ventures in developing countries to be licensees of foreign patents.

Patent license agreements generally take a standard form, except for the provision which relates to the royalties payable and the related technical information and know-how which is to be supplied. In the balance of this chapter, some of the standard terms appearing in a patent license agreement are outlined and the ones relating to royalties are discussed in detail. Related provisions with respect to technical information and know-how are discussed separately in the succeeding chapter.

Throughout these two chapters, it is assumed that the foreign partner in the joint venture is also the licensor of the patents but where the licensor is an independent party, many of the same considerations will be valid as well.

SOME POSSIBLE TERMS FOR A PATENT LICENSE AGREEMENT

The following are some of the clauses that one might expect to find in a license agreement for patents and related know-how, where only a relatively small quantity of know-how is required by the Joint Company.

A. **RECITALS:** The recitals generally outline the fact that the licensor (in this case assumed to be the foreign partner) is engaged in the manufacture of certain products pursuant to various patents of which it is the owner (or licensee), and that the licensee (in this case the Joint Company, which might also be a sublicensee) wishes to manufacture the same goods using the same products.

B. **DEFINITIONS:** It is common to set out definitions for terms such as

1. **Licensed Products**, meaning the products which the licensee is authorised to manufacture. The Joint Company should ensure that as wide a range of products as possible are included, and that any new products utilising the patents or any improvements developed by the licensor are also included.

2. Territory, including the geographical area in which the licensee is entitled to manufacture and sell the licensed products. As has been discussed, the Joint Company should generally attempt to secure as large a territory as possible.

3. Technical Information, including an enumeration of all the possible types of printed matter and data which might be necessary for the licensee to produce the licensed products.

C. GRANT OF LICENSE: In this clause, the license is granted to the licensee for the term of the agreement, the licensee is authorised to manufacture and sell the licensed products within the territory. The licensee should attempt to obtain an exclusive license for the territory.

D. QUALITY CONTROL: The licensee will generally have to covenant to maintain certain standards of quality required by the licensor, and the licensor will be given the right to inspect the licensed products to assure such standards.

E. INFRINGEMENT ACTIONS: The licensor will generally attempt to insert a clause in the license agreement stating that the licensor does not warrant that the patents do not infringe industrial property rights of third parties. The licensee should attempt to [illegible]

clause that in the event of infringement, the licensor will indemnify and save the licensee harmless, meaning that all the financial losses suffered therefrom by the licensee may be recouped from the licensor, and that the licensor will be responsible for defending any action brought.

7. **SALES TO LICENSEE:** It is common for the licensee to require a clause that if it needs any materials or supplies, the licensor will use its best efforts to have them supplied by itself, by its affiliates or by other parties.

8. **ASSIGNMENTS AND SUBLICENSES:** To permit the fullest possible exploitation of the patent rights, the licensee should attempt to secure the rights to assign the agreement and to sublicense other producers throughout the territory.

TERMINATION: The licensee may wish to terminate the obligation to pay royalties after either a definite period or the expiration of the patents being licensed. In this case, it might wish to obtain an option to continue the license until the expiration of the last patent or renewal thereof, or any time earlier by giving, for example, one year's notice.

RELATED KNOW-HOW: The following chapter outlines in considerable detail other provisions in respect of the supply by the licensor of technical data, information, assistance and know-how related to the patents licensed.

The provisions set forth below are not detailed, but may suffice where the Joint Company has existing production facilities, and the know-how it requires is not extensive.

POSSIBLE CLAUSES:

1. The Licensor shall make available to the Licensee without charge and as required by the Licensee, all such technical data and information as shall be necessary for the Licensee to manufacture, sell and service the licensed products and all products related thereto.

2. If the Licensee shall desire technical assistance in connection with the manufacture, sale, application or servicing of the licensed products and all products related thereto, the Licensor shall make available to the Licensee the services of trained personnel for and during such periods as the Licensee shall reasonably require.

3. Representatives of the Licensor and the Licensee shall from time to time consult with each other regarding research, production, sales, servicing, advertising and promotion pertaining to the manufacture and sale of the licensed products, and including all developments and improvements in respect thereof, and the Licensor shall do all such things as shall be necessary to supply all the technical data and information and technical assistance in respect thereof as the Licensee shall request in accordance with the terms of the two preceding paragraphs.

J. ROYALTIES

1. TYPES OF ROYALTIES: Royalties or fees paid for the use of industrial property may be in the form of (a) lump sum payments or (b) payments on a continuing basis.

A lump sum royalty is usually a payment to reimburse the foreign partner before any use is made of the industrial property, while continuing royalties depend upon the extent of the use made of the industrial property.

2. COMPUTATION OF ROYALTIES:

A. Lump Sum Royalties: Some possible considerations for determining or computing lump sum royalties are as follows:

i. the costs to the foreign partner of transferring the industrial property, including the related know-how, technical information and technical assistance to the Joint Company.

ii. the amount the foreign partner feels it should demand as a token of the good fa[illegible] of the licensee.

iii. the goodwill which the foreign partner feels might be attached to the right to use the industrial property in the particular region.

B. Continuing Royalties: Some ways in which continuing royalties may be computed or expressed are as follows:

i. as a fixed amount for each unit produced through utilising the industrial property;

ii. as a fixed amount for each unit sold;

iii. according to the gross selling price of each unit;

iv. according to the net selling price of each unit;

v. differential royalties for units sold abroad and units sold in the host country;

vi. minimum royalty requirements, often based as a rule of thumb, on half of the royalties which would otherwise derive from realization of the market projections.

vii. differential royalties based on the number of units produced or sold, usually varying inversely with the quantity.

viii. net royalties, after deduction of all taxes payable by either or both the foreign and the Joint Company to the host country in respect thereof.

COMMENTS:

A. Lump Sum Royalties:

Where the foreign licensor is also an equity partner in the Joint Company, the reasons for an initial lump sum royalty payment are substantially weakened; as an equity owner, the foreign partner will participate in the goodwill accruing to the Joint Company, will be in a position to assure the Joint Company's good faith, and will profit in proportion to his shareholdings to the extent that the Joint Company does not have to make the lump sum royalty payment.

Accordingly, it may be best that a lump sum royalty not be paid to the foreign licensor, but if one is necessary, then it should be kept low, and might be paid for in fully-paid shares rather than in cash. Generally, however, lump sum royalties are not recommended.

B. <u>Continuing Royalties:</u>

It is impossible to specify which base or bases for computing a continuing royalty will be best for industrial joint ventures in developing countries, but some of the following considerations might be kept in mind:

i. A royalty based on <u>net selling price</u> is probably better in most instances than one based on either production or gross selling price because it encourages the foreign partner to do everything possible to maximise the selling profits of the Joint Company, and does not burden the Joint Company with payments where goods are produced but not sold.

ii. Where one aim of the Joint Company is to encourage exports from the host country, and the foreign partner is either making export markets available, is assisting in the export sales, or both, a strong bargaining point for the Joint Company may be to pay <u>differential</u>

royalties for export sales. Higher royalties paid on the net selling price of exported products, as opposed to products sold in the host country market, may encourage more active cooperation by the foreign partner-licensor in developing foreign markets, and in securing the rights initially for the Joint Company to exploit such markets.

iii. Minimum royalty requirements may provide a certain measure of security to the foreign partner and prevent the Joint Company from "sitting on the product". As an equity participant in the joint venture, however nothing should be done which will enable the foreign partner to profit unreasonably at the expense of the Joint Company. Rather, the remuneration he receives should be a direct reflection of the Joint Company's success, for which he must be at least partly responsible, and minimum royalties are not, therefore, recommended.

iv. It is often common in licensing agreements to stipulate for progressively decreasing royalties based on the number of units produced or sold; the greater the number, the less the royalty. This practice may not be ideal for joint ventures where the foreign partner is the licensor, in so far as it may not encourage maximum efforts

at expansion after a certain sales or production level has been reached. In addition it may have the effect of assuring a minimum royalty.

v. Provision for net royalty payments, "free" of all host country taxes, is not recommended. For example, if a net royalty of $ 1.00 is stipulated, and the host country imposes a 15% withholding tax on all royalty payments to foreigners or non-residents, then the Joint Company would have to pay total royalties of approximately $ 1.18 to achieve that net royalty of $ 1.00. Assuming then that the foreign licensor is taxed at 50% on his royalty income in his own country, but can take advantage of a foreign tax credit provision (which is almost universal amongst developed countries), then he would receive 59 cents net after all taxes with 18 cents taxes of having been paid to the host country and 41 to his own country.

On the other hand, if a "gross" royalty rather than a "net" royalty of $ 1.00 is specified, the foreign partner will receive net after all taxes, 50 cents with 15 cents in taxes having been paid to the host country and 35 cents to his own.

To acquire a better picture of the overall effect of taxation, the equity of both partners remaining in the Joint Company after payment of the royalties must also be considered. On these

facts, the net overall economic benefits to the foreign partner-licensor with both a net and a gross royalty requirement of $ 1.00 are considered.

The following table outlines various income tax ramifications, and demonstrates the overall benefits to the foreign partner-licensor, including his equity remaining in the joint company after payment of the royalties.

The following assumptions are made in the table:

1. that the host country imposes firstly a 1% and secondly a 30% withholding tax on royalties;
2. that the host country imposes a 30% tax on profits of the Joint Company, and that royalties are a deductible expense;
3. that the foreign partner pays a 50% tax on profits in his home country; and
4. that the Joint Company is a 50/50 equity joint venture.

	Net [illegible] of 1.0		Gross Royalty of 1.0[illegible]	
1. Withholding tax rate	15%	30%	15%	30%
2. Total Revenue of [illegible]	1.18	1.43	1.18	1.43
3. Royalty pd. to [illegible]	1.18	1.43	1.00	1.00
4. Profit of Jt. Co.	0	0	.18	.43
5. Host Country [illegible]				
(a) [illegible]	[illegible]	.43	.15	.30
(b) 30% Profit [illegible]	0	0	.054	.129
(c) TOTAL	[illegible]	[illegible]	.204	.429
6. Foreign [illegible]				
Income of [illegible]				
(a) Royalty [illegible]	1.18	1.43	1.00	1.00
(b) Gross T[illegible] of [illegible]	[illegible]	.715	.50	.50
(c) Less [illegible]	.18	.43	.15	.30
[illegible]	[illegible]	.285	.35	.20
7. TOTAL [illegible]	[illegible]	.715	.554	.629
[illegible]ign's [illegible] equity in				
remaining [illegible] profit	0	0	.063	.151
9. Net Benefits to [illegible]				
(a) Total Royalty	1.18	1.43	1.00	1.00
(b) Plus equity remaining	0	0	.063	.151
(c) TOTAL	1.18	1.43	1.063	1.151
(d) Less total taxes	.59	.715	.554	.629
(e) NET BENEFIT	.59	.715	.509	.522

[illegible]

Where the [illegible] royalties [illegible] seen that the extra [illegible] for a net [illegible] an extra [illegible] withholding tax rate [illegible], the extra [illegible] in only a [illegible]. Accordingly, [illegible] increase in royalty [illegible] results in only a [illegible] increase in the net return to foreign [illegible] local partner with no equity in the joint company where the withholding tax rate is [illegible]. [illegible] is 30%, a [illegible] increase in royalty payments [illegible] only a 37% increase in the net return to foreign, [illegible] again, leaves no equity in the joint company for the local partner.

It can be seen, therefore, that providing for a net royalty of a specified amount does not result in proportionate benefits to the foreign partner, and the joint company suffers by having no retained profits, and the local partner by having no remaining equity. In addition, the host country does not gain extra taxes from payment of the higher royalty required unless the tax rate on profits is higher than the tax rate on royalties distributed abroad.

Accordingly, net royalty payments of a fixed amount are not recommended when the licensor is also the foreign partner in the developing country joint venture.

3. <u>PAYMENT OF ROYALTIES:</u>

Three issues arising in respect of the payment of royalties are: the currency in which the royalties are to be paid; whether they will be paid in the form of fully-paid shares or assets of the Joint Company; and the place where they are to be paid.

(a) <u>Currency:</u> The royalties may be paid in the host country currency, the currency of the licensor's home country, or the currency of some third country.

Where the Joint Company has export sales, it may be possible to pay the royalties out of the proceeds therefrom. This approach has the advantage of acting as an incentive to the foreign partner to aid in increasing the export sales of the Joint Company - i.e. if no export sales, it gets no royalties. On the other hand, it has the disadvantage of depriving the Joint Company and the host country of foreign exchange earnings, which may be especially valuable where they are in the form of hard currencies. It may therefore be most advantageous for the Joint Company and the host country if the royalty payments are made in the currency of the host country.

On the other hand, the foreign partner will generally want payment to be made in the hard

currency of his own home country or else in some other hard currency in a foreign tax base country. By this means, he can protect against devaluations and inflation in the host country.

If the foreign partner can not, therefore, be persuaded to accept royalty payments in host country currency, it is recommended that they be made out of the proceeds from export sales in terms of the local currency of each market area. By this means, royalties will be paid in both soft and hard currencies, and if the foreign partner wishes payment in his own home country currency, or a hard currency, his home country market, and/or hard currency countries will have to be made available to the Joint Company's products.

(b) Assets or Shares: Where initial lump sum royalties are to be paid to the Foreign partner, payment is often made in fully-paid shares of the Joint Company, thereby obviating an outlay of scarce funds. This approach might also be adopted for continuing royalties.

A further possibility is to provide for the payment of royalties with inventory of the Joint Company. In this way, a certain limited market is created for the products of the Joint Company, and the foreign partner can either keep such products or resell them. This approach, if feasible, may be ideal for developing country joint ventures because it creates a market for

a limited number of its products, as well as obviating the outlay of either foreign or local currency.

This approach may also present advantages to the foreign partner, perhaps avoiding the payment of host country withholding taxes on royalty payments and not creating any tax disadvantages in its home country or elsewhere because net resale proceeds after deduction of import duties if any, and transportation charges, will generally be no higher than the tax on royalty income.

(c) __Place:__ Often the place of payment of royalties will depend on the type of payment. It will probably be easiest for the Joint Company to make payment in the host country, but if royalties are paid out of export proceeds and the foreign partner is conducting the international selling operations, then royalties might be deducted from payments received in each of the foreign market areas.

ROYALTY [illegible]

1. In consideration of the granting of the license contained in this Agreement, the Joint Company hereby agrees to pay to Foreign within 60 days following the end of each calendar year, royalties equal to   per cent of the net sales prices of all licensed products manufactured and sold by the Joint Company during such year.

2. Licensed products sold by the Joint Company pursuant to the license herein granted shall be deemed to have been sold when paid for.

3. If the licensed products are returned or allowances made thereon after the royalty thereon shall have been paid, the Joint Company shall be entitled to take appropriate credit for such overpayment against royalties thereafter accruing.

4. Each payment to be made hereunder shall be made in (host country currency; or, the currency of the country in which the purchase of each of the licensed products is resident) at such place as Foreign may designate.

5. In lieu of payments as provided for in Clause 4 above, the Joint Company shall have the option of satisfying such obligation to pay by either

(a) issuing fully paid-up shares in the capital stock of the Joint Company to Foreign, in which case the shares shall

be [illegible] either their [illegible] of the Joint [illegible], at their par value, and shall [illegible]ed in sufficient multiples [illegible] satisfies but does not [illegible] payments due hereunder, [illegible] (currency); or

(b) by [illegible] F.O.B. (nearest point to produc[illegible] in host country) a suffi[illegible] of the licensed products set forth in Schedule [illegible] annexed so as to satisfy [illegible] the aggregate payments due hereunder, with any difference being [illegible] (currency) [illegible] value of said licensed [illegible] purposes of this clause shall be [illegible] cost of production [illegible] of the Joint Company, [illegible] per cent.

6. Any taxes, duties or imposts other than income or profits taxes assessed or imposed upon the sums due hereunder to Foreign pursuant to this Agreement, shall be borne and discharged by Foreign, and if so required by law, the Joint Company shall deduct them from any payments to be made to Foreign hereunder.

7. The Joint Company agrees to use its best efforts to obtain any necessary approval for this Agreement by authorities of (host country) or of any other country, countries or groups of countries in the territory, and to obtain the consent of any such authorities to the remittance of payments to Foreign under this Agreement in the event that such consent shall be necessary.

CHAPTER [illegible]

TECHNICAL INFORMATION, TECHNICAL ASSISTANCE AND KNOW-HOW

While a patent licence ensures the right to produce a certain product, it does not necessarily provide the licensee with the requisite know-how to produce such products. Accordingly, the patent licence must impose on the licensor the obligation of supplying the Joint Company with all of the technical data, information, assistance and know-how necessary to use the patent rights to produce the required products.

It is common practice for the patent licence agreement to contain provisions for the supply of all this related information and know-how. Where the licensee possesses a certain degree of manufacturing know-how, the technical assistance required may be very limited. In the case of manufacturing industries in developing countries, however, a great deal may be required, and the legal provisions might be very extensive, going even so far as to provide know-how for construction of the necessary production facilities.

When the know-how required is not too extensive, it is common to include all the know-how provisions in the patent license agreement, but where they are more extensive, it may be better legal practice to draft a separate technical assistance and know-how agreement. Separate agreements are also generally

utilized for all items not directly related to actual use of the patent rights, such as construction of the production facilities, the supply of technical advisors, and training assistance.

In this chapter, a number of specific areas in which technical information, technical assistance and know-how which might be required by the Joint Company are outlined, and possible legal clauses are suggested which might be utilized in the patent licensing agreement or in separate agreements.

A. PLANNING OF FACILITIES

PROBLEM:

It is necessary for the Joint Company to obtain plans and specifications for construction of the plant and production facilities.

ALTERNATIVES:

1. The Foreign partner might possess plans for the construction and layout of the plant and production facilities required by the Joint Company, or it may have an engineering and architectural staff which is capable of producing them.
2. It may be necessary for the Joint Company, with the assistance of the Foreign partner, to commission an independent firm of consulting engineers to design the production facilities.
3. A further possibility is for the Foreign partner to undertake to obtain the plans and specifications from independent sources, and make them available to the Joint Company.

CONCERNS:

Some of the main concerns of the Joint Company at this stage might be as follows:

1. to obtain the requisite plans at the lowest cost;
2. to ensure that the facilities are adequate to satisfy production requirements;
3. to ensure that the facilities are capable of expansion as sales potential increases;

4. to ensure that the facilities are of the latest, most modern, and most economical design and construction.

One of the best approaches for the Joint Company may be to require the foreign partner to provide all of the plans etc., permitting him to obtain them from whatever sources he might choose, including any plans which he might have on hand. Consulting engineers might be required to adapt existing plans to the new site, etc., but this will be less costly than starting afresh, and such savings be passed on to the Joint Company. Such savings may be reflected in a lower price or in lower royalties paid by the Joint Company. The Joint Company will be able to protect all of its previously cited interests through contractual undertakings by the foreign partner.

POSSIBLE CLAUSES:

1. Foreign shall furnish to the Joint Company detailed plans, specifications, blueprints and other data and information sufficient to enable a qualified contractor or contractors to construct production facilities at (address of site in host country)capable of producing (quantity) per year of (list products), which said production facilities shall be capable of being altered, added to or expanded in an economical fashion so as to increase the production of the above said

products or to adapt the facilities for the production of other related or similar products as the business exigencies of the Joint Company may from time to time require, and shall be of the latest, most modern, and most economical design, and shall be capable of producing the said products in the most efficient and economical fashion.

2. Foreign hereby warrants and guarantees that the said production facilities shall satisfy all of the above requirements.

B. CONSTRUCTION OF FACILITIES

PROBLEM: Efficient means of constructing the production facilities, while at the same time maximizing benefits to the host country, should be determined.

COMMENTS: Construction will usually involve two main phases: firstly, construction of the plant; and secondly, purchase, construction, assembly and installation of the required machinery and equipment. These two phases may be undertaken either separately, or together, and in the former case, the responsibiliti for each might be assumed by either the same or different parties.

Where the plant itself may be of standard specifications it might be practicable for the local partner to assume a major role in having it constructed according to the specifications agreed upon by the foreign partner or consulting engineer responsible for their design. This practicability may arise from the local partner's knowledge of local conditions, contractors and personnel. The greater expertise required in respect of the machinery and equipment may necessitate that the Foreign partner assumes the major role in this area. In both cases, however, the expertise of both partners will be of much benefit and their cooperation should be assured.

In all aspects of construction, the host country will benefit from obtaining as much of the materials and as many of the personnel locally. In addition, the Joint Company will benefit most by this approach because of the cheaper costs and the convenience of having local people who can do follow-up and repair work.

With his knowledge of local conditions, the local partner will be a good position to assist in obtaining a reliable contractor and subcontractors, as well as in carrying on liaison work with them to help overcome problems as they arise. It may therefore be advisable to stipulate that the local partner must either approve the contractor and/or subcontractors, or at least, that it is his obligation to assist in their selection. A provision may also be inserted that, wherever possible, contractors, subcontractors and workers are to be from the host country, and that all materials, price and quality being equal, should be obtained locally.

Another problem is to decide to whom the contractors should be legally responsible for construction according to the specifications. They might be primarily responsible to the Joint Company, to the foreign partner, or to the consulting engineer. In the latter two instances, such parties might in turn be made responsible to the Joint Company.

It is difficult to suggest that any one approach may be better than another, but if the contractor or consulting engineer is responsible to the foreign partner, and the foreign partner is responsible in turn to the Joint Company, the foreign partner with his expertise will be in a good position to assure that the production facilities conform to the requirements and the Joint Company will have ready recourse against the foreign partner to assure compliance.

One way to provide for construction of the production facilities is a "turn-key" contract where the production facilities are turned over to the Joint Company in complete working order. Another is for the Joint Company to undertake the construction through the hiring of the contractors and subcontractors on its own, and to satisfy itself, with the assistance of outside experts and/or experts from the foreign partner, that the facilities satisfy the requisite standards.

Regardless of what approach is adopted, it may be desirable that the Foreign partner be legally responsible to the Joint Company for assuring the completion of the production facilities according to the requisite standards and specifications, and the foreign partner can then be left relatively free to enter into what guarantees it might wish with the contractors and/or consulting engineers.

POSSIBLE CLAUSES:

With respect to the construction of the plant and the production facilities, Foreign and Local hereby agree as follows:

1. Foreign shall assume full responsibility to the Joint Company for assuring that the plant and production facilities conform to the required specifications and are capable of producing the required products.

2. In the construction of the plant and production facilities, Foreign and Local agree to use best effort to assure that as much of the materials, equipment and machinery as possible are obtained in (host country), provided there is no sacrifice in quality and the costs thereof are not greater than the cost of obtaining them from elsewhere, and to assure that as many of the contractors, subcontractors, workers and other personnel engaged therein are nationals or residents of (host country).

C. <u>SUPPLY OF MACHINERY AND EQUIPMENT</u>

POSSIBLE CLAUSES:

Foreign shall furnish to the Joint Company

1. Advice in connection with all phases of the design, layout and construction of the production facilities;

2. advice with respect to the specifications of equipment, placement of orders, and the awarding of contracts;

3. and shall review all plans, lay-outs, designs, bids and contracts for the supply of equipment and machinery.

D. INSTALLATION OF MACHINERY

POSSIBLE CLAUSES:

Foreign shall furnish to the Joint Company all the necessary technical assistance to assemble and install the equipment and machinery in the plant so that it will function in the manner required in the specifications.

E. MAINTENANCE OF FACILITIES

POSSIBLE CLAUSES:

Foreign shall furnish to the Joint Company all of the technical data information and assistance necessary to assure the effective operation and maintenance of the machinery and equipment including:

(a) a list of recommended plant spares;

(b) lubrication and maintenance manuals;

(c) detailed operating instructions;

(d) detailed manuals indicating the construction and assembly of each model and type of machinery and equipment; and

(e) instructions regarding start-up and shut-down.

F. OPERATION OF FACILITIES

Foreign shall furnish to the Joint Company technical assistance and advice on all aspects of plant operations including, but without limiting the generality of the foregoing,

(a) scheduling, material specifications and ordering, and production techniques relating to the manufacture of the products;

(b) quality control and production planning;

(c) methods, studies and other industrial engineering activities in connection with the organization, planning, training of personnel, and development of operating practices and procedures to obtain the most efficient use of the production facilities; and

(d) recommended safety procedures.

G. [illegible]

POSSIBLE CLAUSES:

1. The Joint Company shall not be required to accept the plant or production facilities [illegible] such time as it shall be [illegible] satisfied that the said production facilities are capable of producing the required products in the required quantities.

2. Accordingly, before such acceptance, representative samples of each type of product to be produced by the Joint Company shall be sent to (name of independent testing agency or firm; or to Foreign's main production plant) for testing to assure their compliance with the required standards and specifications and that they have been constructed in a good and workmanlike manner; and the Joint Company shall have been furnished with a guarantee and warranty of the satisfaction of such conditions.

H. FURTHER TECHNICAL INFORMATION

PROBLEM:

Because it is most unlikely that the Joint Company will have its own research and development facilities, it is necessary that it be able to take advantage of all new developments available to the foreign partner.

POSSIBLE CLAUSE:

Foreign shall during the term of this Agreement, provide to the Joint Company all technical information and assistance as shall be necessary to keep the Joint Company aware of, current with, and able to effectively utilize, the latest developments in technology applicable or relating to the manufacture sale or use of the products which are to be produced by the Joint Company.

1. **FURTHER PRODUCTS:**

PROBLEM:

If Foreign develops or becomes entitled to manufacture new products, the Joint Company should be given the right to manufacture them as well.

POSSIBLE CLAUSE:

1. Foreign hereby grants to the Joint Company the right of first refusal to acquire the rights to manufacture and sell anywhere in the world any products which are not covered by this agreement, and which Foreign shall have the right to grant.

2. If Foreign grants any other license for any of the products which are the subject matter of this agreement or are similar thereto to any other person upon terms more favourable than those granted herein to the Joint Company, then Foreign shall forthwith and from then on grant the same such favourable terms to the Joint Company, and the parties hereto agree to do all such things as shall be necessary, including the amendment of these presents, to accomplish such end.

J. [illegible]

PROBLEM:

It must be decided what the obligations of foreign shall be with respect to training the Joint Company personnel in the operation of the production facilities.

POSSIBLE APPROACHES:

Most joint venture agreements provide for training of the employees of the Joint Company by representatives of the foreign partner both in the host country, and at one or some of the foreign partner's existing plants. Representitives of the foreign partner who provide on-the-job training often do so by serving as full-time employees of the Joint Company.

COMMENTS:

The Joint Company will wish to obtain the best possible training for its employees at the lowest cost. Generally, it will be less expensive to have on the job training by employees or representatives of the foreign partner who serve as employees of the Joint Company. This approach may also serve to foster greater cooperation than providing on the job training through outsiders.

While the cost of sending employees to the foreign partner's plant for training and instruction may be very costly, it is usually

found to be worthwhile for a limited number of key technical employees, including foremen, supervisors and technical officers.

Training requirements will generally be heaviest prior to the start-up of production, and the Joint Company should assure that the foreign partner makes sufficient personnel available for training during this crucial period. It may also be the best time to send key employees to the foreign partner's plant for training. Advisors provided by the foreign partner for on-the-job supervision and training will generally stay on during start-up and the initial operating period. Thereafter, it may be found that the executive officer in charge of the technical aspects of the Joint Company, who will usually be the appointee of the foreign partner, will be able to provide the requisite additional training except, perhaps, when new models or products are to be produced by the Joint Company.

POSSIBLE CLAUSES:

Foreign hereby undertakes to provide training and technical assistance to the Joint Company upon the following terms and conditions, namely

1. (a) Prior to the start-up of production, Foreign agrees to accept for training up to (maximum number) operating employees of the Joint Company at its plant located

(site of Foreign's plant) for periods of at least months each.

(b) It is understood that the maximum number of such employees to be trained by Foreign at any one time shall be and that they shall be made familiar with all operational and technical aspects of production as relate to or are similar to the production operations to be undertaken by the Joint Company.

(c) The Joint Company shall have no obligation to pay for the costs of such training, other than to pay for their travelling expenses to and from (Foreign's country) and their salaries, if any.

(d) Foreign will use its best efforts to assist in arranging for immigration visas for such trainees, and in finding suitable living accomodations at reasonable prices for such trainees while they shall be in (Foreign's country).

2. For prior to the start up of production and during the initial operating period, which initial operating period shall not last longer than days, Foreign agrees to provide to the Joint Company:

(a) one qualified production supervisor, and
assistants, all of whom shall be graduate engineers, who , besides their responsibilities in respect of readying the plant and operating facilities for the start-up of production and the initial operating period, shall assume responsibility for training all the operating employees of the Joint Company in their operating functions;

(b) one qulified individual who will assist in the recruitment and hiring of the necessary employees and in the development of personnel and labour relations skills in the Joint Company;

(c) All expenses in respect of such individuals, including their salaries, travel expenses and living expenses while in (host country) shall be reimbursed to Foreign by the Joint Company, providing that such expenses, inclusive of all taxes but exclusive of travel to and from (host country), shall not exceed
per man per month.

(d) Local agrees to use its best efforts to arrange for their immigration visas into (host country) and suitable accomodation while they should be in (host country).

3. (a) The Joint Company shall be entitled, from time

to time, and if it shall consider necessary, to require Foreign to send to (host country) such personnel or individuals as it shall consider necessary to assist the Joint Company in finding solutions to any of its problems and in training employees of the Joint Company to cope with such problems.

(b) The Joint Company shall reimburse to Foreign the expenses of such employees for the period during which they shall be absent from their regular business duties with Foreign, including their travel to and from the (host country) by economy fare air passage, their salaries and their living expenses, provided the total of such expenses including all taxes but excluding the said air passage, shall not exceed   per man per month.

4. During such time as said personnel supplied by Foreign shall be rendering technical assistance and training to the Joint Company, they shall not be considered as employees of the Joint Company, for any purposes nor shall Foreign make any claim on behalf of such personnel arising from accident or any other cause.

K. SOME POSSIBLE TERMS OF AN ENGINEERING CONTRACT

1. RECITALS:

WHEREAS the Joint Company has been incorporated for the purpose of manufacturing (host country) the products listed in Schedule A hereto annexed under license from Foreign, and such other products as it may determine from time to time to manufacture;

WHEREAS the Joint Company requires engineering services of Foreign and the planning, process design, building, equipping, start up, and the initial operating period of a plant and production facilities to manufacture the aforementioned products;

AND WHEREAS Foreign is desirous of providing to the Joint Company the aforementioned engineering services;

NOW THEREFORE, in consideration of the premises and covenants herein contained, and the sum of $1 paid by the Joint Company to Foreign, the receipt of which Foreign doth hereby acknowledge, the PARTIES HERETO AGREE AS FOLLOWS:

2. PLANNING RESPONSIBILITIES OF FOREIGN:

Foreign hereby agrees to provide overall plans, including general building drawings, process designs, machinery foundations, the layout of machinery and equipment, and in cooperation with the Joint Company, shall be responsible for and generally see to the realization of the project on the basis of the above plans.

Foreign's planning and work-out documents shall consist of the following matters, namely:

(a) general plans for building and foundation

(b) layout of manufacturing plant

(c) plans concerning erection of machinery, tools, jigs and fixtures and testing equipment necessary for production

(d) generating plant and auxiliary equipment

(e) plant equipment and materials for water supply

(f) plant equipment and materials for electrical power and gas supply

(g) machine tools

(h) miscellaneous auxillary plant and equipment

(i) jigs, tools, and patterns

(j) office fittings and furniture

(k) erection and installation of plant equipment

(l) all wiring and plumbing required for the factory

3. <u>TENDERS AND ORDERS:</u>

Foreign shall render such assistance as shall be necessary to enable the Joint Company to invite tenders and word orders for the construction and completion of the plant and production facilities.

4. <u>TECHNICAL ASSISTANCE:</u>

Foreign shall make available the necessary personnel to the Joint Company to inspect all the work during progress as may be necessary and on delivery to the site, to supervise erection and installation, to inspect

on completion, and on [illegible] the Joint Company to issue such acceptance certification as may be necessary. Foreign shall also provide the necessary staff to ensure the necessary and required operations of the plant, which said staff shall be available to the Joint Company from the start of construction until the end of the initial operation period, which said initial operating period shall be at least   days after completion of the first production run of at least one of the licensed products.

5. GUARANTEE:

Foreign shall perform it's duties and functions under this agreement in such a manner as to ensure, and Foreign does hereby warrant and guarantee, that after the final production stage has been reached, the plant and production facilities shall be capable of producing at least (number) of (specify products) per year.

Foreign shall exercise a high standard of care and shall be liable for any negligence or failure to comply with the above production specifications. The liability of Foreign under this agreement for failure of the production facilities to achieve such standards shall consist of all losses of profits occasioned to the Joint Company to the failure of the said plant and production facilities to meet these required standards, plus the costs of altering the facilities so that they conform to such standards.

6. PROJECT ENGINEER.

Foreign will nominate and provide to the Joint Company a project engineer and such other supporting technicians as the Joint Company considers to be necessary to coordinate effectively and to control the execution of the work and to exercise general site supervision.

7. OBLIGATIONS OF JOINT COMPANY:

The obligations of the Joint Company hereunder shall be as follows:

(a) to pay all salaries and expenses for all personnel provided under this Agreement shall be borne by the Joint Company. Such personnel, their salaries and maximum expenses, including their costs of travel to and from the host country as are hereinafter set forth in Schedule B:

(b) to purchase land for the factory site, and have a geographical survey thereof performed;

(c) to undertake all steps necessary with local governmental authorities to ensure that the plant site is provided with adequate utilities, including rail and road transport, water, gas, electricity, and sewers and other waste disposal facilities;

(d) to undertake steps necessary, and to use its best efforts to arrange for transportation of all materials, machinery and equipment required for the plant including clearance through customs, and to pay for all transportation costs including freights, duties and insurance;

(e) to carry out in conjunction with Foreign negotiations with consultants and civil contractors for the building, based on Foreign's lay out drawings, specifications (such as loads, dimensions, etc.) and recommendations, and will in this connection with the assistance of Foreign, undertake the following:

(i) preparation of tender documents,

(ii) invitations to bidders,

(iii) selection of contractors,

(iv) execution of contract documents,

(v) issuance of orders for the commencement of work,

(vi) appointment of qualified engineers and technicians for supervision of work,

(vii) issuance of acceptance certificate as required,

(viii) and all such other work as is normally required of or performed by an owner.

CHAPTER EIGHT

PARTNERSHIP COMPATIBILITY A[illegible]

It appear[illegible] almost [illegible] recognized that the [illegible] not only [illegible] continu[illegible] of the partner [illegible], but to ensure that if the partnership should be dissolved, that the new partner, if any, will also be compatible.

If one partner w[illegible] or involuntarily from the joint venture, the remaining partner or partners will want to be able to acquire new partners of their own choosing.

Withdrawal by one partner can arise in a number of ways, some of which are:

1. the [illegible] to sell his share of the Joint Company;
2. death of an individual partner;
3. the winding, dissolution or liquidation of a corporate partner;
4. the bankruptcy or insolvency of a corporate or individual partner;
5. the desire of a partner to find another more compatible partner, or else to carry on the Joint Company alone.

A. [illegible]

[illegible]:

It is common in joint venture arrangements to stipulate that no share transfer may be made without the consent of the other partners.

[illegible]:

Both foreign and local agree that they will not sell, transfer, assign, mortgage, pledge or otherwise encumber or deal with any or all shares of the capital stock of the Joint Company without the prior written consent of the other, except as is hereinafter provided and provided that this provision shall not apply to transfer of shares to qualify Directors so long as the beneficial ownership of such shares is retained by foreign or local as the case may be.

B. BUY-SELL AGREEMENTS

Where one partner feels that the [illegible] joint ownership has broken down to the point where he [illegible] buy out the other [illegible] or be bought out himself, a buy-sell agreement [illegible] alternatives. Buy-sell agreements are frequently used in the case of 50/50 joint ventures where deadlocks arise which cannot be resolved. In [illegible], they are an instrument of last resort only, but do offer a reasonable means of [illegible] which [illegible] partner may buy out the other.

It provides basically that the partner wishing to take such steps, will make an offer to buy the other partner's shares upon specified terms. The offeree partner then may either accept the offer to purchase, or upon the same terms, may purchase the shares of the offeror partner at that same price.

Another version of the buy-sell agreement allows the initial offer to be one of sale, giving the offeree the right to either accept or to himself sell at that price.

The essence of both versions is that the offeror's terms must be fair, because the offeree partner is given the option of making the same deal at the same price.

Inequities may arise, however, where for instance, the local partner wishes to carry on as a partner, but cannot finance the purchase of the foreign partner's shares. This difficulty may be overcome by granting to the local partner in the buy-and-sell agreement, some or all of the payment privileges discussed below in relation to rights of first refusal.

[illegible]

1. CO[illegible]

1. Either [illegible] or [illegible] (hereinafter in this clause called the "offeror") shall have the right [illegible] [illegible] of [illegible] notice in writing (hereinafter called the "original notice") to the other to offer to sell to the other (hereinafter in this clause called the "offeree") [illegible] the offer[illegible] and terms to be specified in the original notice, provided, however, that [illegible] shall [illegible] on the "closing date", as hereinafter defined, and the balance shall be payable in no more than (number) annual installments and provided further that the original notice shall provide that the offeree shall have the right to elect to sell to the offeror all of the shares of the Joint Company then owned by the offeree at the price and upon the terms set forth in the original notice.

2. Within 90 days after receipt of the original notice the offeree shall advise the offeror by notice in writing (hereinafter called the "notice of election") whether the offeree accepts the offer of the offeror to sell all but not less than all of the outstanding shares of the Joint Company owned by the offeror or elects to sell to the offeror all of the outstanding shares of the Joint Company owned by the offeree.

action against an infringer;

ii. that the licensee will assist in bringing any such action; and

iii. that the licensee will notify the licensor of any suspected infringements.

(e) <u>Rights after Termination:</u>

The licensor will often insist that clauses in respect of some or all of the following conditions come into effect upon termination of the license agreement:

i. the licensee will assist in cancelling any registrations there may be of the license agreement;

ii. the licensee will discontinue use of the marks and names;

iii. the licensee will return to the licensor at the latter's expense, or else destroy, again at the expense of the licensor, all advertising, stationery, containers, etc. bearing the marks and names; and

iv. the licensee will permit the licensor to purchase all inventories bearing the marks and names. The cost thereof should be the fair market value;

3. If the offeree does not advise the offeror by notice in writing within the said period of 30 days as hereinbefore provided then the offeree shall be deemed to have accepted the offer of the offeror to sell all but not less than all of the shares of the Joint Company owned by the offeror, in accordance with the terms of the original notice.

4. The purchase and sale of the shares of the Joint Company resulting from the acceptance or deemed acceptance by the offeree of the offer of the offeror to sell contained in the original notice as aforesaid or the election by the offeree to sell to the offeror all but not less than all of the shares of the Joint Company owned by the offeree or the offeror, as the case may be as aforesaid, shall be completed on a date (hereinafter called the "closing date") no later than:

   (a) days after receipt by the offeror of the notice of election, or

   (b) if the offeree does not deliver a notice of election, as aforesaid, days after receipt of the original notice by the offeree, at which time the nominees of the party whose shares are to be sold (hereinafter called the "vendor") shall resign as directors, officers and employees of the Company and the other party who is purchasing the vendor's shares (hereinafter called the "purchaser") shall and will pay to the vendor

[illegible] forth [illegible]

[illegible]

(e) [illegible], the vendor [illegible] fail [illegible] refuse [illegible] shall [illegible] of the purchase price [illegible] thereof [illegible] [illegible] advisable in order to complete the transaction [illegible] irrevocably [illegible] attorney of the vendor for [illegible] in the name of and on behalf of the vendor to execute [illegible] deeds, transfers, conveyances, assignments, [illegible] which the vendor [illegible] herein contained.

(f) If, on the closing date, the purchaser shall fail or refuse to complete the transaction, the vendor shall have the right to purchase the purchaser's shares and on payment to the vendor of a share equal to 75 per cent of the purchase price, to execute and deliver all such transfers, resignations and other documents and instruments which may be necessary or advisable in order to complete the transaction and the purchaser is

hereby irrevocably appoints the attorney of the Vendor for and in the name of and on behalf of the Vendor to execute and do any deeds, transfers, assurances, assignments, assurances and things which the Vendor ought to execute and do [illegible].

(e) It is understood and agreed that neither party hereto shall make or assist in making any application to wind up the Joint Company after any such notice shall have been delivered pursuant to the provisions of this clause.

(ii) [illegible]

1. In th[illegible] event that either Forei[illegible] [illegible] Local shall at any time durin[illegible] [illegible] of th[illegible] agreement or w[illegible]thin one year aft[illegible] [illegible] of this agreement desire to sell [illegible] of (otherwise than for the purpose of [illegible] directors) any shares in the capital of th[illegible] Joint Company for the time being owned and controll[illegible] by such [illegible] (such party being referred to below as the "offeror") [illegible] the right to send a notic[illegible] in writing (referred to below as the "notice") to the other [illegible] (referred to below as the "offeree") which [illegible] effective shall be signed by the offeror and shall [illegible] the follow[illegible]:

   (a) The price of each share [illegible] the capital stock of the Joint Company;

   (b) [illegible] offer to buy all [illegible] the shares in the Joint Company owned or controlled by the offeree at the [illegible];

   (c) An offer t[illegible] sell all of [illegible] shares in the Joint Company owned or controlled by the offeror at the said price.

2. Upon receipt of such notice, the offeree shall be entitl[illegible] within days of receipt of this notice to accept either one of the offers contained in the notice, and the transaction shall be closed within days of the date of such acceptance. In the event the offeree does not accept either one of the said offers within the perio[illegible] of days aforesaid, then at the option of the offeror

to be exercised by the offeror within   days after the lapse of the last mentioned   day period, the offeree (referred to below as the "Vendor") shall be deemed to have accepted the offer of the offeror (referred to below as the "Purchaser") to purchase all of the shares in the capital stock of the Joint Company owned or controlled by the offeree and the transaction shall be closed within   days after the exercise of the said option.

Upon the date set for closing, the vendor shall sell and transfer and assign to the purchaser all of the shares the capital stock of the Joint Company owned or controlled by the vendor, shall cause its nominees to resign from the Board of Directors of the Joint Company and any office or employment that such nominees may have with the Joint Company and the purchaser shall and will pay to the vendor the purchase price as set forth in the notice in full by cash or by certified cheque; provided that if at the closing date the vendor should be indebted to the Joint Company in an amount recorded on the books of the Joint Company and verified by the auditor of the Joint Company, the purchaser shall have the right out of the said purchase price to pay, satisfy and discharge all or any portion of any such indebtedness and to receive and take credit against the purchase price for the amount or amounts so paid on account of the indebtedness.

If on the date fixed [illegible] the vendor shall neglect or refuse to complete the transaction, the purchaser shall have the right [illegible] (without prejudice to [illegible] other [illegible] remedies [illegible]) [illegible] of such [illegible] price (less any [illegible] to [illegible] indebtedness to the Joint Company) to the credit of the vendor in an account [illegible] the [illegible] of [illegible] with the [illegible] the Joint Company [illegible] behalf of and in the name of the vendor [illegible] complete the transaction as aforesaid and the vendor [illegible] and constitutes the purchaser [illegible] to any of such [illegible] complete the [illegible] and execute any and every document [illegible] behalf.

If a sale [illegible] clauses of this agreement shall [illegible] sale, until the sale of shares in the Joint Company shall have taken place, [illegible] party [illegible] shall do or cause or permit to be done anything [illegible] the ordinary course of business of the Joint Company.

(iii) **SHO[illegible]**

At any time after [illegible] , either party may offer in writing to sell to the other party all (but not part) of the shares of the Joint Company [illegible] offeror party and its Affiliated Corporations, at a specified price [illegible] terms and conditions as shall [illegible] offer. If the offeree party shall not [illegible] accepted [illegible] offer within [illegible] days after the [illegible] notice thereof, the [illegible] party shall have the right, exercisable [illegible] giving written notice to the other party within [illegible] days after the expiration of such [illegible] day period, to purchase all (but not part) of the shares of the Joint Company [illegible] by the offeree party and its Affiliated Corporations, at the price and on the terms and conditions specified [illegible] offeror's original offer of sale. The closing of [illegible] pursuant to this clause shall take place within [illegible] days after acceptance of the offer by the offeree or the giving of notice by the offeror of the exercise of its right of purchase hereunder, as the case may be.

C. RIGHT OF FIRST REFUSAL

Especially where one of the partners wishes to sell his shares, it is common for joint venture agreements to give a right of first refusal to purchase such shares to the other partner or partners. In jurisdictions where the Joint Company is permitted to purchase its own shares, the right of first refusal might also be given to the Joint Company.

The right of first refusal will depend upon the receipt by the selling partner of a *bona fide* offer to purchase by an outside party.

One problem inherent in a right of first refusal is in ascertaining the *bona fides* of the outsider's offer to purchase. It might therefore be made a condition precedent to the right of any partner to sell his shares to an outsider that any offer to purchase be presented in writing to the other partner.

Another possibility is that the offeree partner must offer to sell its shares to the other partner at a specified discount from the offer price and that the other partner be permitted to then complete the sale of those shares to the outsider at the full option price. This approach gives the other partner the option of either purchasing himself, or taking in a new partner and making a profit on the transaction. In adopting this approach, any

offer to purchase received by the selling partner will have to be made assignable and exerciseable by the successors and assignees of the offeree partner.

POSSIBLE CLAUSE:

In the event that Foreign shall receive a bona fide offer to purchase all but not less than all of the shares it owns in the capital stock of the Joint Company, then Foreign shall not be entitled to accept such offer without firstly, presenting to Local a certified copy of such offer, which said offer must be assignable to the Local partner, and secondly, presenting to Local an offer to purchase shares at a discount of per cent from the price in the original bona fide offer to Foreign.

D. OPTION AGREEMENT

The principal advantage of the local partner obtaining a option to purchase some or all of the shares of the shares of the foreign partner is that if the Joint Company is financially successful, the option may be exercised, whereas if it is a failure, there need not be any capital investment by the local partner. In addition, the option gives the local partner the right to a large future stake in a successful venture, without necessitating the initial need for raising capital and risking it in an untested venture.

It will be recalled that one form of possible joint venture arrangement was for the foreign partner to own 100 per cent of the shares of the Joint Company for a specified time period, after which the local partner would have the option to purchase some or all of the foreign partner's shares.

Many refinements on this theme are possible, and an option of the local partner to purchase some or all of the shares of the foreign partner may be utilised, whatever the percentage ownership of the foreign partner might be.

The three main problems in utilizing an option agreement are in deciding upon the timing, and in deciding upon the price, and in the local partner obtaining the necessary financing.

1. TIMING

PROBLEM:

The time at which the local partner is to purchase some or all of the foreign partner's shares must be determined.

COMMENTS:

The timing is important for two main reasons. Firstly, the Joint Company will suffer if the option is exercised too early, and full advantage of the foreign partner's contributions, such as technology, know-how, industrial property, managerial skills, technical assistance, training, and marketing assistance, has not accrued to the Joint Company.

Secondly, if the option is exercisable at a future specified date, the foreign partner may be encouraged to take either an extractive or blasé approach to the joint venture and his responsibilities to it.

The period before which the option becomes exerciseable must be long enough that the foreign partner is encouraged to maximize his contributions to it, especially in training the local partners to be able to carry it on above.

This means that the foreign partner must have been able to achieve a fair return on his investment before the option da[illegible] The financial returns to the foreign partner may be measured in terms of some or all of the following items, namely:

1. dividends;
2. lump-sum royalties;

3. continuing royalties;
4. management fees;
5. technical assistance and training fees;
6. salaries of personnel provided by it;
7. interest on loans to the Joint Company;
8. interest (dividends) on debt capital of the Joint Company;
9. capital receipts from sale of shares in the Joint Company;
10. increase in its own earnings or capital worth derived from participation in the joint venture which may be reflected in an increased value of its shares.

BLE APPROACHES:

To overcome the problem of the foreign partner adopting an extractive or blasé approach to the joint venture prior to and after the option date, some or all of the following approaches might be adopted to assure his continuing interest, namely:

1. pay continuing royalties based on sales;
2. pay continuing interest on loans or debt capital;
3. require that the option price be paid out of future profits of the joint company;
4. provide for a long term repayment, assuring that principal and interest obligations be subordinated to other obligations incurred in the ordinary course of business;
5. specify precisely the obligations of the foreign partner in the joint venture agreement, both before and after, but especially before, the option date;

6. require a cash deposit by the foreign partner in trust for the Joint Company or local partner, which will be treated as liquidated damages upon default, to assure the performance of its obligations;

7. provide for actual damages, over and above the forfeit deposit, occasioned by default of the foreign partner in its obligations;

2. OPTION PRICE

PROBLEM:

The option price at which the local partner is to purchase some or all of the foreign partner's shares will be determined.

APPROACHES:

Some possible approaches of determining the option price are as follows:

1. setting a predetermined price per share;
2. by a predetermined formula, such as
   (a) book value, or
   (b) a specified earnings multiple;
3. by a predetermined process, such as
   (a) evaluation by an independent third party such as a judge or firm of accountants,
   (b) arbitration, and
   (c) a combination of conciliation and arbitration
   (d) a court

COMMENTS:

1. Setting a predetermined price may be too arbitrary an approach for joint ventures, because it is not likely to reflect the real value of the shares. If it is too high at the option date, the local partner will be deprived of the right to exercise his option at a reasonable price; if too low, the foreign partner will become more and more disinterested in the affairs of the Joint Company as the option date approaches.

2. Utilizing some predetermined formula may also be too arbitrary. For example, the book value, as determined by

the books of the company, may be far less than actual value if maximum or accelerated depreciation has been taken. On the other hand, the plant may be obsolete at the option date. Furthermore, the book value might not in any way reflect the earning potential of the Joint Company.

If book value is used, it is common to exclude therefrom any valuation for any intangible assets, such as good will, and for intangible property rights such as patents, trade marks, trade names, and licences.

Using a formula such as a certain multiple of earnings per share may be reasonable, in so far as earnings reflect the actual value at the option date. But the predetermined earnings multiple may be either too low to reflect a rapidly growing company, or it may be too high if the Joint company's earnings are declining.

3. Use of a <u>predetermined process</u> for fixing the purchase price generally provides the greatest flexibility and ensures the reaching of a reasonable price.

The problem with utilizing one independent third party to determine the option price lies in finding a competent party who is acceptable to both partners. Generally, the outside party, if an individual, will not be a resident national, or if a firm, will not be conducting operations in either of the partner's countries or the host country. One solution

is to choose a [illegible] for ex[illegible], [illegible] some [illegible].
Another approach is to [illegible] the [illegible] determined by
a court of some third [illegible].

A common approach is to [illegible] the option price by
arbitration. [illegible] a single arbitrator,
it is often best to [illegible] of the partners [illegible]
one arbitrator, who must then agree on a third arbitrator.

A further approach is to [illegible] for [illegible] or
proceedings whereby the parties at first to [illegible] agree
on the price, upon [illegible] of which, the question goes to
arbitration. This [illegible] may be [illegible] best, since it
combines flexibility with the opportunity of [illegible]
a realistic valuation, and [illegible] arbitration, which,
like court proceedings, may be costly and time-consuming,
as only a last resort.

[illegible]

[illegible]: [illegible] especially [illegible] even [illegible] the [illegible] wish [illegible] a "shot-gun [illegible] to raise [illegible] other's shares.

POSSIBLE SOLUTION: [illegible]

1. [illegible] to the local [illegible] the outside [illegible] for any incompatibility which [illegible].

2. Require [illegible] of [illegible] for the withdrawing partner's [illegible], including a long term, low or no interest and a long grace period.

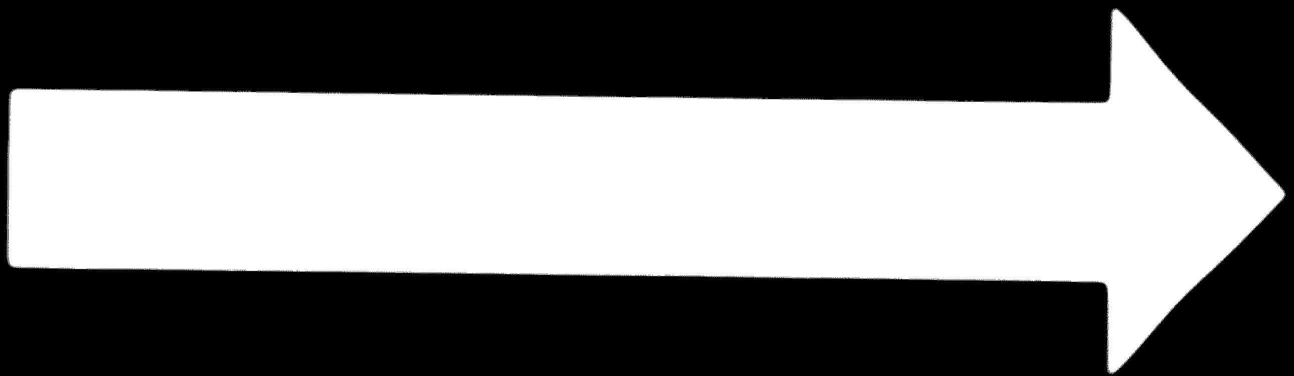
3. Require that dividends distributed to the foreign partner be in partial or full satisfaction of the local partner's payment obligations.

4. Require that the [illegible] out of [illegible] of the joint [illegible] form of dividends.

The latter [illegible] on his [illegible] permitting the [illegible] partner to [illegible] a [illegible] joint venture at a [illegible] required, without [illegible] the Joint Company [illegible].

The drawback to this [illegible] is that the lo[illegible] be [illegible] the shares with after-tax [illegible] the local laws, the Joint Company will have probably been taxed on its profits, and the [illegible] on the div[illegible] paid to it.

To overcome this problem, the tax authorities of the host country may be persuaded to permit special tax exemptions, such as exempting the local partner on dividends paid [illegible] which are utilized to purchase the foreign partner's shares. The exemption might even go further and apply to corporate profits distributed to the local partner for such a purpose.



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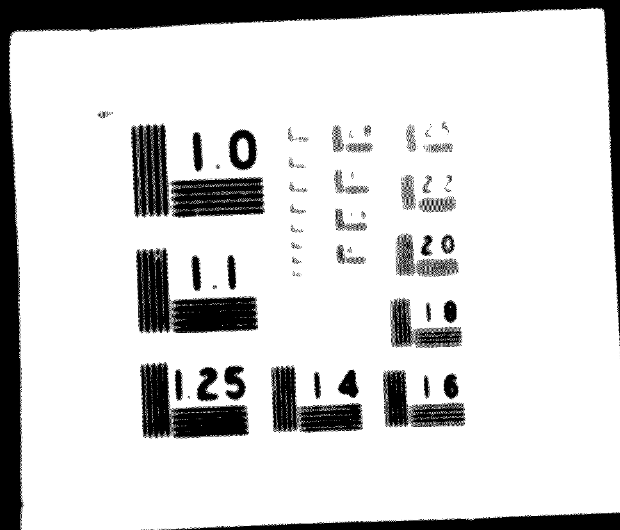


POSSIBLE OPTION AGREEMENT

This agreement made the day of , 19 , between Foreign Manufacturing Company Limited, a company incorporated under the laws of (jurisdiction of incorporation) having its principal office at (site of head office), (hereinafter called "Foreign" of the first part); and Developing Country Investments Limited, a company incorporated under the laws of (jurisdiction of incorporation) having its principal office at (site of head office), (hereinafter called "Local" of the second part).

IT IS AGREED THAT:

1. In consideration of one dollar and other good and valuable consideration, receipt which is hereby acknowledged, Foreign hereby grants to Local, and to any person or persons designated by Local, the full and exclusive right and option to purchase at the price hereinafter stipulated the shares of the capital stock of the Joint Company owned by Foreign, and all or any part of any additional shares of such stock hereafter required by Foreign, free and clear of any loan, charge or encumbrance, on the terms and conditions hereinafter stipulated.

2. This option may be exercised by Local at any time after (option date) by written notice to Foreign offering to purchase the number of shares set forth in such notice at a price which shall be the fair value of such shares at the date of such notice. In determining such fair value,

only the tangible assets of the Joint Company (excluding, without limitation, any value for good will, trade marks, patents, licenses, or other intangible property rights), together with any leasehold it owns will be taken into account. In the event that Foreign and Local shall not have agreed on such fair values within 20 days after the notice of exercise of the option, such fair value shall be determined by (internationally recognized accounting firm), accountants, having a principle place of business at .

3. Upon exercise of the option, the shares with respect to which the option has been exercised shall be transferred by Foreign to Local and the purchase price paid, except as provided below, within 30 days after notice of such exercise of the option or, in the event that the fair value shall be determined by (name of accounting firm) within 15 days after notice of their decision.

4. If an authorization by the Government of (host country) should be required for said transfer or payment, Local shall obtain such authorization and shall notify Foreign and the Joint Company thereof, and in such event the shares with respect which the option has been exercised shall be transferred and the purchase price paid within 15 days afte giving of such notice of authorization by Local.

5. The purchase price shall be paid to Foreign at a bank to be designated by Local in the notice of exercise of the option, against delivery to Local of a properly executed document of a transfer relating to the shares covered by this option.

6. This agreement shall be binding on the heirs, successors and assigns of each of the parties hereto. This agreement may be assigned by Local, and on any such assignment the assignee shall have all the rights, and be subject to all the obligations, of the grantee hereunder.

In witness whereof the parties hereto have caused this Agreement to be signed by proper signing officers and have hereto affixed their corporate seals.

E. SHARE CERTIFICATES

PROBLEM:

The partners must assure that shares cannot be transferred without the transferee being bound by all the terms and conditions contained in the joint venture agreement.

COMMENTS:

It may be possible under the law of some jurisdictions for a bona fide transferee for value who has no notice of the restrictions on transfer or other conditions in the joint venture agreement to acquire the shares in the joint company free of such restrictions and conditions and any other equities existing between the joint venture partners.

POSSIBLE SOLUTIONS:

Notice of the existing equities may be given in fact or constructively, such as by being contained in the incorporating documents of the Joint Company, where such documents are deemed to constitute notice of the provisions contained therein; or by being printed on the share certificates themselves.

Apart, therefore, from setting out the restrictions on transfer in the incorporating documents, it is a recommended safeguard that the incorporating documents specify that all share certificates are to be endorsed before issue, with the restrictions on transfer.

If such restrictions are too lengthy to be conveniently inserted thereon mentioning the existence of restrictions on transfer as are contained in the incorporating documents which are open to inspection by the public.

<u>POSSIBLE CLAUSE:</u>

The parties hereto agree that every share certificate of the Joint Company shall have noted on its face a statement to the effect that the shares represented by such certificate are issued in accordance with and pursuant to the provisions of this Agreement and further that no share in the capital stock of the Joint Company can in any way be assigned or transferred (save and except for directors' qualifying shares) without the assignee or transferee executing an agreement indicating that such assignee or transferee adheres to and agrees to be bound by, all of the provisions hereof.

2. CHANGES IN PARTNER'S IDENTITY

PROBLEM: The partners might wish to make provision to protect against changes in the ownership or identity of the other corporate partner or partners.

COMMENTS: The ownership continuity or [illegible] clauses above protect against changes in ownership of the shares of the joint company. This topic deals with protection against changes in the ownership or identity of the foreign corporate partner, which may be tantamount to the introduction of a new partner into the joint venture without the consent of the local partner. This may be felt necessary because the success of a joint venture often depends as noted upon the personal relationships between the partners.

Changes in the identity of the foreign corporate partner can occur through it being involved in an acquisition merger or reorganization whereby control passes to new owners.

Legally, the partner will still be bound by the joint venture agreement, but will be able to replace all of the individuals involved in the joint venture, destroying the personal relationships upon which the local partner has been relying for an efficient and harmonious working relationship. Furthermore, there may be many ways in which the new owner can subvert the spirit of the joint venture agreement, while

still fulfilling its obligations thereunder.

Another problem is that a change in ownership or control of the foreign partner can bring about business incompatibility, [illegible] the new owner may be competing with the Joint Company in a way [illegible] the former owner was not.

POSSIBLE [illegible]:

1. The joint venture agreement may specify that whenever the majority ownership or the effective control of the foreign partner should pass from its present to new owners that the joint venture agreement becomes voidable.

   This alternative may, however, deprive the Joint Company of certain continuing rights to licences, technical assistance, know-how, etc., which it may wish to have, but may be necessary where the new owner of the foreign partner is found to be wholly incompatible, such as, for instance, where it is carrying on business in the same area as the Joint Company with competing products.

2. Another possibility for protecting against the introduction of incompatible individuals into the Joint Company by a foreign partner under different control, is to provide that whenever the effective control of the foreign partner changes hands, all individuals appointed or supplied thereafter by the foreign partner to the Joint Company, including directors, officers, and technical assistants and advisors, must be approved by the local partner.

This [illegible] requires the foreign part[illegible] be [illegible], [illegible] will not be [illegible] to [illegible] Joint Company.

[illegible] [illegible] control of [illegible] persons [illegible], [illegible] all of the [illegible] of the Joint Company, [illegible] of whom it is the obligation of [illegible] to provide [illegible] Joint Company under the terms [illegible] Agreement, [illegible] first approved by [illegible] to accept or cause [illegible] to be accepted, [illegible] appointment of directors, officers, [illegible] other [illegible].

[illegible]

One of the most frequently expressed dissatisfactions with joint ventures is that disputes between the partners hamper the efficient business operations of the joint company.

Disputes may arise with respect to the validity, construction and performance of the joint venture agreements and the related documentation, including the determination of the rights of the parties *vis à vis* one another and the joint company. It is difficult, if not impossible, to draft a joint venture agreement in sufficient detail to cope with all eventualities and to regulate fully all aspects of the joint venture relationship. In addition, even the most carefully worded agreement will be subject to some ambiguities. Furthermore, changes in laws or economic or political conditions may require a restructuring of the joint venture arrangement.

It is essential, therefore, to provide procedures by which the equitable settlement of disputes can be expeditiously obtained.

POSSIBLE APPROACHES

Four approaches to the settlement of disputes are as follows:

1. informal agreement
2. conciliation
3. arbitration
4. court proceedings

A. INFORMAL AGREEMENT

It is axiomatic that the best approach is for the partners to settle disputes by mutual agreement, without recourse to more formalized procedures. While most disagreements will be resolved on the spot, it may be considered useful to insert a clause in the agreement providing for the co-operation of the parties to achieve this end.

POSSIBLE CO-OPERATION CLAUSE

The parties hereto ascribe to the principle that the expeditious and equitable settlement of disputes arising under this agreement is to their mutual advantage and is in the best interests of the Joint Company. To this end, they therefore agree to each use their best efforts to resolve all differences of opinion and to settle all disputes through co-operation and consultation.

1. [illegible]

[illegible] parties to [illegible], but if both are dealing in good faith, [illegible] attainable.

[illegible] CLAUSES

1. If in the opinion of any party to this agreement, any other party is in default in the performance of any obligation hereunder, and the parties are unable to agree upon a mutually satisfactory solution, the first party shall give the other party written notice specifying the respects in which a default is believed to exist and calling upon such other party to remedy that default. Unless the matter is disposed of by agreement within 30 days after the receipt of such notice or such longer period as may be agreed to by the parties, then the complaint may be referred to a Conciliation Committee under Clause 2 hereof. Any complaint which either party does not wish to refer to a Conciliation Committee, or which is not

determined by the final ruling of a Conciliation Committee may then be submitted by the first party to Arbitration as hereinafter provided.

2. The parties to a complaint arising under Clause 1 hereof may agree that the matter shall be referred to a mixed Conciliation Committee composed of four members, two nominated by each party, whose duty shall be to seek a friendly solution of the complaint. The Conciliation Committee, after having heard the representatives of the parties shall give a ruling within three months of the date on which the complaint was referred to it. The ruling in order to be binding, must be unanimous.

[illegible]

[illegible]

1. [illegible] proceedings are required, the parties may have to wait some time before a court hearing can be obtained.

2. The arbitration award can be quickly implemented, without the requirement, as in the case of court decisions, of awaiting appeals to higher courts.

3. The costs of arbitration will generally be less than the costs of court proceedings.

4. Arbitration procedures can be more flexible than those of courts, such as in respect of the times of sitting, the proper law to be applied, the introduction of evidence, and in ensuring that the arbitrator has personal expertise in the field of the dispute.

Three types of arbitration agreements are outlined hereafter as indications of some of the possible clauses which might be utilized by the parties. The recommendation is made as to which might be best, and will naturally depend on the requirements of the parties. It appears, however, that in most countries where arbitration is well developed, such as through the existence of codified arbitration rules, that shorter agreements incorporating the local law, or else the arbitration law of some foreign jurisdiction or body, are quite appropriate.

The comment has not been unfrequently made that once a dispute reaches the court or arbitration stage, the partnership arrangement has suffered a fundamental and perhaps irremedial breakdown. This is not a necessary consequence, however, and provided the partners derive mutual advantages from continued participation, the court or arbitration decision may provide a new foundation for co-operation and understanding.

A. Complex Agreement: Provision for Expert Arbitrator

1. (a) Arbitration in accordance with the provisions of this Clause shall be the sole method of determining any dispute between the parties to this Agreement arising out of, or relating to, the execution or interpretation of this Agreement, the determination of the

rights and obligations of the parties hereunder, or the operation of this Clause and which is neither resolved by mutual agreement or by Conciliation as referred to above.

(b) Arbitration proceedings shall be instituted by a notice in writing given by the complainant to the respondent.

(c) If the dispute relates to technical or accounting questions, it may by agreement between the parties be referred either to a single expert or to a body of three experts, of whom two shall be appointed by the parties (one by each) and the third shall be appointed by mutual consent of the said parties. If the parties do not agree upon the single or the third expert, the other party may request the Director of (name of an internationally recognized technological institution) when the question is a technical one, or the President of (name of an internationally recognised accounting institution) when the question relates to accounting, to appoint the single expert or the third expert.

(d) If during the proceedings before an expert or experts acting under Paragraphs (a), (b)

or (c) of this Clause, there arises in the opinion of the expert or experts or of either of the parties, a question of law (which expression shall include any question as to the interpretation of this joint venture agreement) the determination of which is necessary to a decision upon the technical or accounting question in issue, the question of law shall, if not determined by agreement between the parties, be submitted to arbitration under Paragraphs (e), (f), (g) and (h) of this Clause by the parties or either of them, either upon their own initiative or at the request of the expert or experts.

(e) If the parties do not agree that the dispute shall be referred to an expert or experts under Paragraphs (c) and (d) of this Clause, or if they do so agree but the appointments provided for are not made or a decision is not given within the time limited for the purpose, or if in the circumstances set out under Paragraph (d) of this Clause, either of the parties seeks the determination of a question of law, each of the parties shall appoint an arbitrator, and the two arbitrators before proceeding to arbitration shall appoint an umpire who shall be the President of the Arbitration Board.

If the two arbitrators cannot within days of the institution of the proceedings agree on the person of the umpire, the latter shall, if the parties do not otherwise agree, be appointed at the request of either party by the President of the International Court of Justice.

(f) If one of the parties does not appoint its arbitrator or does not advise the other party of the appointment made by it within days of the institution of proceedings, the other party shall have the right to apply to the President of the International Court of Justice to appoint a Sole Arbitrator.

(g) The appointment of an umpire or sole arbitrator under Paragraphs (a), (b) and (c) of this Clause shall be within the complete direction of the person authorised to make it, and the exercise of his discretion may not be questioned by either party. The person so appointed shall not be closely connected with or have been in the public service of, nor be a national of (jurisdiction of incorporation of the joint company), the nations in which the other parties to this Agreement are incorporated.

If the arbitration is referred to the Arbitration Board, the award may be given by the majority. The parties shall comply in good faith with the award of a sole arbitrator or of an Arbitration Board.

2. (a) If the party liable to execute the final award given in accordance with Clause 1 of this Agreement, fails to comply therewith within the time specified for such award for compliance or, if no time is therein specified within days after the communication thereof to the parties, the party in favour of which the award has been given, shall be entitled to seek the termination of this Agreement by a decision of the Arbitration Board or sole arbitrator made in accordance with Paragraph (b) of this Clause 2. Any such decision shall be without prejudice to any accruing rights and liabilities arising out of the operation of this Agreement prior to its termination hereunder, including such other rights, sums or damages as may have been awarded by the Arbitration Board or sole arbitrator.

(b) The power to make the decision provided for by Paragraph (a) of this Clause 4, shall only be exercisable subject to the conditions following, namely:

(i) the decision shall be made by the Arbitration Board or Sole Arbitrator who made the final award concerned;

(ii) if the Arbitration Board or Sole Arbitrator who made such award is for

any reason unable or unwilling to act, the question of termination for non-compliance with an award shall be referred to arbitration in accordance with Clause 1 hereof in the manner provided for determination of disputes;

(c) no decision terminating this Agreement shall be made unless the Arbitration Board or Sole Arbitrator shall have first prescribed a further period (not being less than days) for compliance with the award, and after the expiration of such further period shall have found that the award has not then been complied with.

B. Complex Agreement: Extensive Arbitration Rules

1. Any dispute arising under this Agreement which cannot be settled amicably shall be submitted to arbitration in accordance with the Arbitration Rules hereto following.

2. Arbitration Rules:

(a) Any dispute arising under this Agreement which cannot be settled amicably shall be referred to a single arbitrator for settlement by arbitration in accordance with these Rules.

(b) Any one or more parties to this Agreement wishing to have recourse to arbitration

(hereinafter referred to as "the Claimant") shall serve a statement of Claim together with a written request for arbitration on the other parties to this Agreement.

(c) (i) Any party to a disputed Agreement receiving such a Statement of Claim and request for arbitration, who wishes to take part in the arbitration proceedings shall, within 30 days of such receipt (or within such extended period as the Claimant may allow in writing), so notify the Claimant and serve on the Claimant a Case in Answer to the Statement of Claim.

(ii) A Case in Answer may rebut the Statement of Claim or, in so far as the nature of the Claim permits, support it.

(iii) A Case in Answer may contain a counter-claim and the Claimant may within 15 days of receipt of a Case in Answer (or within such extended period as the party serving the Case in Answer may allow in writing) waive a Case in Reply on the party serving the Case in Answer.

(d) Any party receiving a Statement of Claim and request for arbitration, who fails so to notify the Claimant and so to deliver a Case

in Answer within the aforesaid time limit of 30 days (or any extension thereof that the Claimant may allow in writing), shall not be entitled to take part in the arbitration proceedings but shall nevertheless accept and be bound by any award made in the course of those proceedings.

(e) (i) For the sake of convenience and with the object of minimising expense, the Claimant and every party serving a Case in Answer (hereinafter collectively referred to as "the parties to the proceedings") will endeavour (but will not be obliged) to agree pursuant to the following subclauses of this Rule upon the appointment as an arbitrator of a suitable person conversant with the law of (jurisdiction whose law is to govern) and upon any proceedings being conducted in (host country).

(ii) The Claimant shall propose in his request for arbitration the name of an arbitrator and the country or place where the arbitration proceedings will be conducted.

(iii) Every Case in Answer shall state whether the party serving the same accepts such proposals and may contain counter-proposals.

(iv) If the proposals made by the Claimant are accepted by all the other parties to the proceedings, the Claimant will appoint as arbitrator the person so proposed by him and the proceedings will be conducted in the country so proposed by him. But, if the Claimant's proposals are not accepted by all the other parties to the proceedings, the parties to the proceedings will by unanimous agreement, within the period of 15 days next following the expiry of the time limited in Rule (iii) for any party to serve a Case in Answer (or within such extended period as the parties to the proceedings may jointly agree), appoint the arbitrator and choose the country where the proceedings are to take place.

(v) If an arbitrator (whether appointed by the parties to the proceedings or otherwise) refuses to act or becomes incapable of acting or dies, then, within 30 days of such event, a new arbitrator will be appointed in his place by the parties to the proceedings by unanimous agreement.

(vi) If the parties to the proceedings are ever unable to reach unanimous agreement on any such appointment or choice as aforesaid within the time limit prescribed, the appointment or choice in question will be made at the request of any one or more of the parties to the proceedings by the President of the International Chamber of Commerce or, failing him, by the President of the International Court of Justice.

(vii) For the avoidance of doubt it is hereby declared that notwithstanding that any such appointment or choice is made by the President of the International Chamber of Commerce or the President of the International Court of Justice, the proceedings will nevertheless be regulated by and conducted in accordance with these Rules.

(f) The Claimant will be responsible for supplying the arbitrator with copies of the following:

(i) these Rules;

(ii) this Agreement;

(iii) the Statement of Claim;

(iv) every Case in Answer;

(v) any Case in Reply;

(vi) all other documents which the parties to

the proceedings or any of them wish to put in evidence.

(g) (i) The arbitrator will determine the time and place (being in the country or town chosen for the arbitration proceedings in accordance with Rule (v) of every hearing and will afford to each of the parties to the proceedings an opportunity for an oral hearing and the right to be represented by one or more lawyers. The arbitrator shall conduct the proceedings in private and, subject to the provisions of Rule (ix), shall deliver a signed copy of his award giving his reasons therefor to each of the parties to this Agreement within 60 days of his appointment.

(ii) Subject to these Rules, all matters relating to the competence and powers of the arbitrator or to procedure shall be governed by the law of the country where the proceedings are being conducted.

(h) (i) Every award shall be final and the parties to this Agreement shall carry out every award without delay (provided that the arbitrator shall have power to correct in any award any clerical mistake or error arising from any accidental slip or omission).

(ii) The parties to this Agreement waive their rights to any form of appeal against an award in so far as any such waiver may be valid.

(i) (i) The remuneration of the arbitrator shall be determined at the time of his appointment by the parties or person appointing him and the arbitrator shall be entitled to be paid his remuneration before delivery of any award.

(ii) The parties to the proceedings shall be jointly and severally liable to the arbitrator for the full amount of his remuneration but, as between themselves, they shall bear the amount of such remuneration in the first instance in equal shares (though without prejudice to any right of subsequent reimbursement arising by virtue of any direction or order with regard to costs given pursuant to Rule 11).

(j) The costs of any reference to arbitration shall be in the discretion of the arbitrator, who may direct to and by whom and what manner those costs or any part thereof shall be paid or borne, and may tax or settle the amount of such costs or any part thereof to be paid or borne.

(k) Every document sent by any party to a disputed Agreement to another such party may be sent by ordinary prepaid letter post but, where an airmail service is available, it will be sent by airmail post. Every document so sent will be deemed for the purposes of these Rules to have been served on the party to whom it was addressed on the fourth day after it was posted.

C. <u>Short Agreement</u>:

1. Any dispute, difference or question arising between Foreign and Local concerning the construction, meaning or effect of this agreement or any part hereof shall be referred to a single arbitrator if Foreign and Local agree upon one, and failing such agreement to a board of three (3) arbitrators, one to be appointed by Foreign, one to be appointed by Local, and one to be appointed by the two arbitrators so named by Foreign and Local.

2. If any party (herein called the "appointer") delivers a notice in writing to the other party hereto, appointing an arbitrator and requiring the other party hereto either to agree to such appointment or to name a second arbitrator, and if such other party shall refuse and neglect to deliver a written notice to the appointer within

ten (10) days of the receipt of the first mentioned notice either agreeing to such appointment or moving a second arbitrator, the appointor may make application to a judge of the Supreme Court of (host country) for the appointment of a second arbitrator, and the second arbitrator so appointed shall be deemed to be the arbitrator appointed by the other party.

3. If the two arbitrators are unable to agree upon the person to be named as the third arbitrator either of the said arbitrators may make application to a judge of the Supreme Court of (host country) for the appointment of the third arbitrator. The decision of the majority of the three arbitrators so appointed shall be final and binding on the parties hereto.

4. The provisions of the Arbitrations Act of (host country) shall apply to any such arbitration.

D. COURT PROCEEDINGS

For the reasons enumerated in the last section, the use of court proceedings to settle joint venture disputes may be found impracticable. It is especially important that disputes be resolved quickly, because the partners are forced "to live together", and the disruption caused by an unsettled dispute may make such cohabitation extremely difficult with a concomitant upsetting of the joint company's operations.

From experience, therefore, it is usually not recommended that disputes by joint venture partners with the joint company or with each other be left to determination by court proceedings.

E. GOVERNING LAW

PROBLEM

Where the partners do not agree upon the settling of all disputes by arbitration, but decide instead that each shall have normal recourse to courts of law, it must be determined which laws are to apply. In addition, where arbitration is chosen, it is customary to specify which law shall be applied to settle all questions of law.

POSSIBLE ALTERNATIVES

The proper law for determining all disputes arising out of the joint venture agreements, including interpretation of the agreements themselves may be the law of

1. the host country;
2. the foreign partner's country of incorporation;
3. some mutually acceptable third country or jurisdiction;
4. certain rules of international law.

COMMENTS

Because of his familiarity with the last country law, the local partner will usually desire that it apply. Since it is the law under which the Joint Company is incorporated, it is also the law which will most naturally apply in the absence of any provision to the contrary.

One problem which may arise in specifying that the host country law shall apply is that if the joint venture agreements are executed elsewhere, one of the partners is resident or incorporated there, and part of the performance is to take place there, a court of that jurisdiction might decide that it shall have competence to determine any questions according to its own law.

To obviate this possibility, even though it is remote, the joint venture agreement should specify precisely which laws are to apply and also all of the documents [illegible] be executed in the host country.

Where the laws of the host country are considered by both partners to be inadequate, and those of another jurisdiction are selected, it is best to choose arbitration for the settlement of all disputes, and to stipulate that any questions are to be decided according to the law of that other jurisdiction. In this way, the host country laws will not have a chance of application unless the courts assume jurisdiction contrary to the stipulation that all questions are to be decided by arbitration.

Besides providing that the laws of a third jurisdiction are to apply, a further possibility is to stipulate that some form of international law shall apply. This approach has been adopted in at least one large joint venture, and has certain advantages to offer in

multipartite joint ventures where the choice of the law of one of the partner's countries might appear too arbitrary.

POSSIBLE CLAUSES

1. All questions relating to the validity, construction or performance of this Agreement shall be governed by the laws of (host country).

2. This agreement shall take effect as a Deed made in (host country) on the date when it is executed by or on behalf of the last of the parties hereto executing the same, and shall be governed by and construed in all respects in accordance with the laws of (host country).

3. In view of the diverse nationalities of the parties to this Agreement, it shall be governed by and interpreted and applied in accordance with the principles of law common to (host country) and the several nations under which the other parties to this Agreement are incorporated, and in the absence of such common principles, then by and in accordance with principles of law recognised by civilised nations in general, including such of those principles as may be applied by international tribunals.

CHAPTER TEN

STANDARD CONTRACT PROVISIONS

In addition to all of the other provisions, the following are some clauses which it may be found helpful to insert in the joint venture and related agreements.

A. PARTIES

COMMENT:

The parties to a joint venture arrangement may be individuals, corporate bodies, governments or governmental agencies; the agreements may be bipartite or multipartite. In many instances, the local partner will be a governmental agency of the host developing country, such as an industrial development corporation whose shares are wholly -owned by the government. For convenience, it is assumed throughout this study that there are only two parties; the foreign partner being a developed country corporation, and the local partner being a developing country corporation. Where the identity of either of the parties would alter the suggested legal wording, such differences will be indicated.

POSSIBLE DESIGNATION OF PARTIES:

This AGREEMENT made the day of , 19 ,

BETWEEN

FOREIGN MANUFACTURING COMPANY LIMITED,
a company incorporated under the laws of (jurisdiction of incorporation) having its principal office at (situs of head office),

(hereinafter called "Foreign")

OF THE FIRST PART;

AND

DEVELOPING COUNTRY INVESTMENTS LIMITED,
a company incorporated under the laws of (jurisdiction of incorporation) having its principal office at (situs of head office),

(hereinafter called "Local")

OF THE SECOND PART.

B. RECITALS

COMMENTS:

In joint venture agreements, where it is impossible to foresee all contingencies, recitals can assist in indicating the nature of the relationship between the parties and some of the circumstances under which the agreement has been entered into. As such, they do not constitute the obligations or rights of the parties, but may be of assistance in interpreting the agreement.

Typical recitals may cover the following items.

1. identification of the parties, including the type of business and the geographical situs;
2. the intention to form a joint venture company;
3. reasons for entry into the joint venture arrangement;
4. nature of the business operations to be conducted by the joint venture company, and its geographical situs;
5. any other item peculiar to the establishment of the joint venture agreement which will serve to clarify the relationship of the parties.

POSSIBLE RECITALS:

WHEREAS Local (brief description of its business activities); and

WHEREAS Foreign manufactures (products) under certain patents in (country) and sells them under certain trade names and bearing certain trade marks in (geographical region); and

WHEREAS Foreign and Local desire to cause the above said products to be manufactured in (developing country), and thereby bring certain benefits to (developing country) including decreased imports, increased exports, employment, and a higher level of technical and industrial know-how; and

WHEREAS capital, industrial property, technical skills and know-how are required to produce (products) and market them in order to effect the said benefits; and

WHEREAS Foreign is in a position and is willing to supply such capital, industrial property, technical skills and know-how; and

WHEREAS Foreign and Local desire to form a corporation in (country of incorporation of joint venture company) to carry out the production of marketing, and to provide for certain arrangements relating to its operations and affairs; and

WHEREAS Foreign and Local intend that to these ends the provisions of this Agreement shall be carried out in a spirit of good faith and good will;

NOW THEREFORE, in consideration of the premises and covenants herein contained, and other good and valuable consideration flowing from each party to the other, the receipt whereof both parties by their execution of the Agreement do hereby acknowledge; the parties hereby agree as follows:

C. DEFINITIONS

COMMENTS:

It is common practice in legal agreements to set out definitions of words and phrases which will be frequently used. In joint venture agreements and the related legal documentation, definitions are usually indicated at the first of the agreement, and may cover the following items:

1. the products which the joint company is being licensed to produce by Foreign;
2. the components which may be supplied by Foreign;
3. spare parts for the manufacture of the licensed products or machinery to be used by the joint company;
4. the products which the joint company will manufacture;
5. the territory in which the joint company may sell the licensed products;
6. sub-contractors who may be authorized by the joint company to produce the licensed products;
7. date upon which the agreement becomes effective;
8. the technical information which Foreign is supplying to the joint company;
9. corporations which may be related to the parties and which the parties may agree to cause to be bound by certain provisions in the agreements;
10. aids to interpretation of the agreement;
11. any other frequently used phrases.

POSSIBLE DEFINITIONS:

1. "Licensed Products" means the devices and products described in schedule annexed hereto, together with all improvements and modifications thereof or developments with respect thereto. It shall also include any new products developed by Foreign (or by the licensor of the products to the joint company) subsequent to the date of this agreement whether or not related to the products describe in schedule above, and appropriate amendments to the said schedule shall be hereafter executed to incorporate any such new products.

2. "Components" means those components and parts of licensed products which the Licensor may from time to time agree in writing to permit the Licensee to manufacture or procure within the territory (which the Licensor utilizes in its business operations for the production of such licensed products anywhere in the world);

3. "Spare Parts" means replacement parts for Licensed Products or for any part thereof;

4. "Territory" means (geographical areas where Licensed Products are to be manufactured and where they are to be sold by the Licensee), each existing and internationally recognized at the date of this agreement;

5. "Authorized sub-contractor" means any company or other body incorpor[illegible] or person for the time being approved by Local for the purpose of manufacturing on behalf of the Licensee the Licensed Products and Com[illegible]

6. "Effective Date" means the date upon which the last of the agreements attached hereto as Schedules shall have been executed by the parties thereto, including the date on which the Joint Company, having been duly constituted under the laws of (jurisdiction of incorporation) shall have executed the last of the agreements attached hereto as schedules, and become bound thereby.

7. "Technical Information" means engineering, manufacturing and originating information relating to the manufacture and servicing of licensed products, including drawings, blue prints, design sheets, sales of material, material specifications, photographs, photostats and general data, and designs and specifications relating to manufacturing equipment, tools and fixtures, but includes, however, only such information as is (1) available to the Licensor and (2) applicable to the operations of the Licensee under this agreement.

8. "Controlled Corporation" A body corporate shall be determined to be controlled by one of the parties hereto if said party directly or indirectly holds or controls more than 25 per cent of the total votes conferred between issued sale capital of that body corporate (for this purpose excluding some of the total from steady body corporate any votes which are available only on the happening of specified contingency or upon specific business).

9. In this agreement, the singular shall include the plural and the masculine the feminine, except where the context otherwise requires.

10. "Start-up Period" means the period from the completion of construction of the production facilities until such time as the first of all types of products to be produced therein have been certified as being on specification, and the Joint Company is satisfied that the production facilities are capable of producing the agreed upon products in the agreed upon quantities.

11. "Initial Operating Period" means the (amount of time) immediately following the start-up period and during which period Foreign's obligation for supply of technical and training assistance to the Joint Company shall continue as hereafter specified.

D. NOTICE: Any notice required or permitted under the provisions of this Agreement shall be sufficiently given if

(a) delivered personally, in which case it shall be deemed to have been received at the time of delivery;

(b) sent by prepaid registered air mail, cable or telegram addressed as follows:

To Local at

To Foreign at

To the Joint Company at

or to such other addresses as may hereafter be furnished in writing by either party hereto to the other, and in the case of prepaid registered air mail shall be deemed conclusively to have been received on the fifth business day of the recipient following the date on which it is so mailed; and in the case of a cable or telegram, shall be deemed conclusively to have been received on the second business day of the recipient following the date on which it is so sent.

(c) sent by prepaid telex addressed as follows:

To Local at (telex address)

To foreign at (telex address)

To the Joint Company at (telex address)

in which case it shall be deemed conclusively to have been received on the first business day of the recipient following the date on which it is so sent.

For purpose of ascertaining the date of mailing or sending or receipt in the above provisions, all times shall calculated according to that of the time zone of the addressee or sender.

8. FORCE MAJEURE:

(a) Any failure or delay in the performance by either party hereto in its obligations under this agreement shall not constitute a breach hereof or give rise to any claims for damages if, and to the extent caused by occurences beyond the control of the party affected, including, but without limiting the generality of the foregoing, acts of governmental authority, acts of God, strikes or concerted acts of workmen, fires, floods, explosions, wars, riots, storms, earthquakes, accidents, acts of a public enemy, war, rebellion, insurrection, sabotage, epidemic, quarantine restrictions, shortages of labour, materials or supplies, failures by contractors or subcontractors, transportation embargoes, failures or delays in transportation, rules, regulations orders of directives of any government or any state, subdivision, agency or instrumentality thereof or the order of any court of competent jurisdiction.

(b) Without prejudice to any other remedies that may then be available to either of them, in the event of failure or delay arising out of or resulting from such causes, the parties will cooperate in an effort to agree upon the establishment of such alternative arrangements not subject to such failure or delays as will confer upon them benefits comparable in character and substantially equivalent in amount to those intended to be conferred by this Agreement, on terms and conditions not materially more burdensome to either party than those herein provided.

CO-OPERATION AND IMPLEMENTATION:

(a) Each of the parties hereto shall not at any time during the continuance hereof deal with any of the shares of the Joint Company owned by it whether by sale, pledge, gift or otherwise, in any manner inconsistent with the carrying out of its obligations hereunder.

(b) The parties hereto agree that they will at all times exercise all voting rights conferred on them by the shares in the capital of the Joint Company registered in their names or beneficially owned by them in such manner as to ensure that the provisions of this agreement are all complied with.

(c) If any of the terms or provisions of this agreement shall be declared illegal or unenforceable by any court of competent jurisdiction, then the parties hereto agree to do all things and cooperate in all ways open to them to obtain substantially the same results, or as much thereof as may be possible, including the amendment or alteration of these presents.

G. SOLE CONTRACT:

This Agreement constitutes the only agreement between the parties hereto and supersedes all prior agreements, expressed or implied, between the parties. This agreement and the terms and conditions of sale provided for herein may be modified only by written agreement by both parties.

[illegible]. LANGUAGE:

This Agreement shall be executed by the parties hereto in both (language of local partner or host country) version and a (language of foreign partner), each of which shall be binding on the parties, it being understood that and agreed that in the event of any discrepancy between the two said versions, the (language of local partner or host country) shall prevail.

APPENDIX

I. MERCK SHARP & DOHME OF INDIA LTD.

Merck Sharp & Dohme of India Ltd. is joint venture company located at Bhandup near Bombay, India, engaged in the manufacture of pharmaceutical chemicals. The 60 per cent interest is owned by Merck Sharp & Dohme Incorporated, a United States company whose net sales in 1967 were US$528,126,000 with net income of close to US$90,000,000. The 40 per cent partner is Tata Sons, Ltd., one of India's largest privately owned companies.

I. FORMATION OF JOINT COMPANY

Merck Sharp & Dohme Incorporated had been selling in India when in 1958, the Government announced pursuant to its Second Five Year Plan a policy of establishing a manufacturing capacity for basic drugs and pharmaceutical chemicals in India. Merck Sharp & Dohme Incorporated entered into negotiations with the Indian Government, and offered to supply technical assistance to a government corporation for a streptomycin plant in exchange for a low fee and formation of a 60/40 joint venture to manufacture vitamins and steroid hormones with a private concern. The government's counter offer was for a 50/50 joint venture with a government corporation but it finally approved the 60/40 joint venture with private interests, eventhough usual practice was to preclude majority foreign ownership of Indian Companies. It was abrogated in this instance because of other precedents, and because its primary goal was not to ensure control by nationals, but to create a broad capital market, educate the public and stimulate Indian entrepreneurs. Pursuant to the joint

arrangements, a temporary plant became operative in 1959 and the permanent one was opened in 1964, producing a full line of pharmaceutical chemicals.

II. FINANCING

The Join Company has an authori ed capital of 42 million rupees (approximately US$6 million), consisting of 4.2 million shares of 10 rupees each. The paid up capital is only 18 million rupees. No long term loan arrangements have been made but the Company has received extensive loans

through normal banking channels, and especially from the Punjab Bank.

III. MANAGEMENT

The Board of Directors of the Joint Company has nine members, composed of six Merck representatives and three Tata representatives. Merck has also assumed a dominant role in the day to day management, and there has been no interference by Tata; Merck has operated it basically as a wholly-owned foreign subsidiary. The Managing Director and Secretary are Indians, the Sales Manager is an Australian, and the Chief of Production is a British-American.

IV. TECHNICAL ASPECTS

Although it is the general policy of Merck to stipulate in its trademark and patent license agreements that the license becomes revocable upon a change in the ownership or control of the licensee, no such clause was contained in the license agreement to the Joint Company. Merck felt that its rights were adequately protected through majority ownership. Nor has any provision been

made for payment of royalties for its supply of technical assistance, patents, trademarks and know-how; Merck had felt originally that dividends alone would suffice.

V. MARKETING ARRANGEMENTS

In 1968 the Joint Company's sales were 50 million rupees. All sales by the Joint Company are made through a distributing firm called Voltas, which is owned by Tata Sons Ltd.; Volkart Brothers, a Swiss Company; several life insurance companies; the Unit Trust of India; and the general public; but Tata represents the dominant voice. Because of good results, Voltas has been left relatively free to conducts its business. The Joint Company has moderate exports, encouraged by a 15 per cent government cash rebate.

VI. MISCELLANEOUS

One of the major contributions of the Joint Company has been import substitution, and the Indian authorities seem content with the progress made by the Joint Company. No finished products are imported but certain materials and intermediates are purchased from Merck. Because of the importance of the pharmaceutical industry to India, it could easily have come under government ownership and it is unusual that the majority ownership should be in a foreign company. It is expected that if the company undertakes substantial expansion, the government would ask the management to make a public issue of shares, which would increase the Indian financial participation.

II. MOORE BUSINESS FORMS DE CENTRO AMERICA, S.A.

Moore Business Forms de Centro America, S.A. is an equity joint venture company that manufactures business forms in El Salvador. Forty-nine per cent of its equity capital is owned by Moore Corporation, Limited, a Canadian company with large international interests, and fifty-one per cent by Salvadorians.

I. FORMATION OF JOINT COMPANY

There were three principal contributing factors to the formation of the joint company. The first was the formation of the Central American Common Market and the progress it had made towards economic integration of the five member countries, offering local producers vastly expanded market opportunities. The second factor was the "nationalization" of Moore Business Forms de Cuba, S.A. in 1962, which had been seventy per cent owned by Moore Corp. The remaining shares were owned by Cubans who were forced to leave Cuba and their shares became forfeit to the Cuban government. Even with only a thirty per cent ownership, the Government dictated management of the company, leaving Moore Corp. no alternative but to sell its majority interest to the Cuban government. The method of compensation is still under discussion. This *de facto* expropriation left Moore Corp. without production facilities in Central America at a time when the CACM offered good economic prospects for continuing production; it also meant that the former employees who left Cuba were available for operations elsewhere. The third important factor in the Joint Company's formation was the associationentered into with Alex Dutriz, a Salvadorian

businessman with interests in newspapers and printing, and who agreed to become a local partner in the joint company. As a result of this association, Moore Corp. became the forty-nine per cent shareholder in the joint company through a series of arrangements commencing in December 1961 and ending in February 1965.

II. CAPITAL STRUCTURE

The authorized capital of the joint company is relatively small, being 200,000 Colones (US$80,000) consisting of 2,000 shares with nominative value of 100 Colones each. All of the shares are issued and fully paid; Moore Corp. owns 979, Mr. John Kirkpatrick, Chairman of the Board of the joint venture and Manager of the International Division of Moore Business Forms, Inc. owns 1 for the total of 980 shares, or forty-nine per cent. Moore restricted its ownership to forty-nine per cent so that the joint company could qualify under the Salvadorian Industrial Development Law for tax and other investment incentives, which apply only where Salvadorians own a majority of the shares. The remaining fifty-one per cent of the share capital is owned by Dutriz (about thirty-three per cent), Armando Criado, the former General Manager of Moore Business Forms de Cuba, S.A. and three other Salvadorian residents. The initial capital requirements of the company were fully met by subscriptions for shares and no debt financing was required. The cost of commencing operations was this law because the joint company rented the printing plant from Dutriz, and needed only to convert some of the presses and purchase a few others.

III. DIRECTION AND MANAGEMENT

There are five members on the Board of Directors. The Chairman is Mr. Kirkpatrick, and the others are Dutriz, Criado and two other Salvadorians. Mr. Kirkpatrick is the only non-resident of El Salvador. Moore Corp. is not concerned about being frozen out of the Board, eventhough there is no cumulative voting, nor in not being able to exercise the control it might wish, because it feels that through the ownership of the patents, tradenames, and as the sole supplier of the form dispensing machines, it is in an adequate position to safeguard its interests in the joint company.

The officers, and not the Board, plays the dominant role in the company's affairs. Dutriz is the President and Criado is Secretary and General Manager. Besides Criado, the Assistant General Manager, the Sales Manager and two of plant supervisors were formerly with Moore's Cuban operation. As General Manager, Criado is the chief executive officer in charge of the day to day operations. As of the End of 1967, the joint venture had 150 full time employees, none of whom were unionized.

IV. TECHNICAL ASPECTS

On the formation of the joint venture, Moore Business Forms, Inc., a wholly-owned United States subsidiary of the Moore Corp., entered into a technical assistance agreement with the Joint Company and licensed to it the use of the Moore trademarks and patents for the Central American Market Region. Moore Inc. receives a royalty calculated on the production levels.

Relatively little technical training and know-how had to be provided because Criado and the other top officers were familiar with Moore's techniques from the Cuban operation.

V. MARKETING ASPECTS

In its production, the Joint Company purchases paper competitively from Canada and the United States and small portions from Guatemala and Scandanavia. All of the handling and dispensing machines are imported from wholly-owned United States manufacturing subsidiaries of Moore Corp. Although these machines do not qualify for import duty exemptions, it is unlikely they will be produced locally because economies from the large production run of the American plants more than offset the applicable tariffs.

The CACM population is about 10,000,000 and Moore Corp. estimates that total sales will reach about US$2,000,000 per year. If access can be gained, however, to South American markets, and this figure can be greatly increased, but this matter depends largely upon progress made by LAFTA. The company employs its own direct sales force of salesmen but utilizes a sales agency agreement in respect of Panama.

VI. MISCELLANEOUS

The joint company plans to expand its production capacity by fifty per cent and is building a new plant in San Salvador. Financing for this plant will be provided through retained earnings and a secured, long term loan from a government-owned development agency, INSAFI.

Moore Business Forms de Central America, S.A. represents the first

experience of Moore Corporation, Limited as a partner in a joint venture in a developing country, and Moore Corp. is satisfied with its participation of forty-nine per cent. It feels that local participation promotes better relations with the government, employees and customers. Problems normally associated with joint control have not yet arisen because Moore enjoys an ultimate power control through the licensing agreement. In addition individuals and not the local government is the local partner. When tax holidays expire in 1975 the principal reason for Moore Corp. remaining the minority partner may no longer apply but it nevertheless contemplates no restructuring of the operations because of the continuing advantages from local participation.

III. CARLING BREWERY (HONG KONG) LIMITED

Carling Brewery Hong Kong Limited is a 50/50 Joint Venture whose equal owners are a large Canadian Brewery and a consortium of Hong Kong business men.

I. FORMATION

In 1962 the Hong Kong partners approached four North American brewing corporations to find a partner who would supply the required technology, know-how and financing to construct and operate a brewery in Hong Kong. They finally settled in the Canadian Company, and a joint venture agreement was negotiated. Under the agreement, the Joint Company was incorporated in 1964 under the name Associated Breweries Ltd. In 1965, this name was changed to include the word "Carling" because, roughly translated, that word means "good health" in the local language. In addition it was felt that the international goodwill associated with that name would assist marketing efforts.

II. CAPITAL STRUCTURE

The total capitalisation of the Company has not been made public to date, but the authorised share capital consists of 1,060,000 common voting shares for which each partner subscribed equally. The land was contributed by the local partners in return for paid-up shares. Additional money was raised from the Hong Kong and Shanghai Banking Corporation, and secured by fixed charges on the land, plant and equipment. By the above methods, sufficient capital was raised to construct a medium sized brewery with a net capacity of 60,000

Canadian barrels (1 million Imperial gallons) per year, with a peak monthly of 100,000 gallons.

III. DIRECTION AND MANAGEMENT

Equal control follows [illegible]; the Joint Company's Board of Directors has six members and the Articles of Association stipulate that each partner has the right to appoint three directors. The Chairman is specifically precluded from exercising a casting vote in the event of deadlock. The partners have divided the responsibility for day-to-day management along functional lines. The General Manager and Head Brewer is a former employee of the Canadian partner and two of the Hong Kong partners were appointed Joint Managing Directors. While the General Manager is the Chief Executive Officer of the Company, his expertise is restricted mainly to the technical aspects of production. The local Joint Managing Directors deal chiefly with marketing and personnel problems. By 1967 the General Manager was the only foreigner serving as an employee of the Joint Company. He serves also as one of the Canadian partner's nominee directors, and the two others commute from Canada to Hong Kong for board meetings.

IV. TECHNICAL ASPECTS

The Joint Venture agreements set out in considerable detail the responsibility of the Canadian partner for the supply of industrial property, technical assistance and know-how. The Canadian partner has assumed responsibility for supplying all of the know-how for construction of the brewery, including selection and placement of orders for all the machinery and equipment, plant

layout, and providing specifications for all items such as refrigeration, piping, electricity, waste disposal, etc. It also provided a project engineer at its own cost to assist with the construction for the period of 6 months. The Joint Company assumed responsibility for selection of the plant site, engagment of local architects and engineers, and construction of the plant and facilities according to the specifications provided by the Canadian partner.

V. MARKETING ARRANGEMENTS

The first beer was produced in November 1966 and is one of about 40 beers sold in Hong Kong. One of the biggest assets to its marketing campaign is the use of the "Carling" names which are licensed by a wholly owned subsidiary of the Canadian partner to the Joint Company. Five brand names and trademarks were licensed to the Joint Company in return for continuing royalties based on sales volume; the major brand that has been promoted with the assistance of local publicity agents is "Black Label" beer. The Joint Company covenanted to sell beer outside the Colony of Hong Kong.

VI. MISCELLANEOUS

Carling Brewery (Hong Kong) Limited is the first joint venture undertaken by the Canadian partner, and the Canadian partner admits that the joint venture is the only vehicle by which it would have entered the Far Eastern market, as previously, it had supplied the Far East from its United Kingdom or United States production facilities, but because of its unfamiliarity with the methods and procedures for conducting business in there, it would not have

made the direct investment without a local partner. In addition, it was necessary that the local partners be individuals with whom the Canadian partner felt it could easily carry on business. The Canadian partner is quite satisfied with its first Joint Venture and would be prepared to enter further joint ventures.

IV. BRAZILIAN LIGHT AND POWER COMPANY LIMITED

Since March 1966 Brazilian Light and Power Company Limited has become the minority partner in seven industrial joint ventures in Brazil.

I. FORMATION OF THE JOINT VENTURES

Brazilian Light was formed in 1912 as a Canadian company to act as a holding and management company for utility subsidiaries that were operating in Brazil from 1899 and on. It is Canada's largest foreign investment, and represents the largest aggregation of private international capital in Central and South America. Brazilian has had as many as 45,017 employees and is the biggest employer in Brazil.

Since its incorporation, Brazilian has at one time or another been engaged in electrical, traction, gas and ~~the~~ telephone utilities in Brazil. Its principal present-day operations, however, are its electrical utilities, and has divested itself of most of the traction, gas and telephone utilities because of ~~its~~ inability to obtain profitable concession agreements from governmental authorities.

Its last major divestment of a utility operation occurred in 1966 when Brazilian sold all of its telephone utilities to the federal government. Its telephone subsidiary had faced the same problems as were encountered in the traction and gas utilities; inadequate rates, inflation, increasing costs of operation and construction made the necessary capital outlays, and the possibility of obtaining long term financing impossible. Telephone services were accordingly highly inadequate and in 1964 there were only 862,648 tele-

phones in service but there were 578,000 unfilled applications. Proceedings commenced by President Goulart in 1962 culminated in expropriation proceedings under President Branco in 1966.

Compensation for the telephone utility was set at a price US$96,315,78[illegible], payable over a twenty year period with outstanding balances secured by a serial bond guaranteed by the federal government at six per cent. Of the total of more than $158,000,000 of principal and interest, which Brasilian will receive over the 20 years, it is obligated to reinvest $65,000,000 in Brasil.

II. REINVESTMENT PROGRAMME

The Government imposed certain reinvestment requirements in respect of the $65 million; the funds must be reinvested only in industrial, agricultural and financial undertakings. In addition, Brazilian has laid down its own guidelines which are as follows:

1. Investments should be in production activities contributing to the development of Brasil; export industries are specially attractive.

2. Investment should be to expand productive capacity and not to buy out existing partners.

3. Investment should be within the sale agreement guidelines, and not in public utilities, natural resources, real estate, entertainment, retail or wholesale trades.

4. Investment should be as a minority shareholder only.

5. No investments are to be made in a company that does not already possess the technical know-how necessary to carry out its operations, because Brazilian has no management or technical know-how outside of the utility field.

Brazilian has created two wholly-owned sub-subsidiaries to carry out the investment programme. Brazilian feels that it can contribute two things to the joint ventures in which it participates, capital and financial know-how. In particular, it seeks to tailor an accounting system for each joint venture company which will provide management with essential data. It has an investment supervisory team of six individuals, four of whom are accountants. This team negotiates the joint venture agreements, supervises the investments, and participates in the financial supervision of each joint company through serving on their boards.

The following are short descriptions of eight joint venture investments made by Brazilian up to the end of 1958.

1. FABRICA NACIONAL DE VAGOES S.A.: This company is engaged in the manufacture of railroad cars and accessories, truck chassis, frames and wheels, earthmoving equipment and farm implements. Brasilian owns twenty-five per cent of its capital consisting of common shares and Preference A and B shares. Brasilian's main contribution was capital required for expansion and it benefits from the six per cent dividends paid on the preference shares.

2. INDUSTRIAS ALIMENTICIAS CARLOS DE BRITTO: This company has become Brazil's second largest canning company, and Brazilian owns about twenty-eight per cent of its capital stock. It is a family-run company to which Brazilian's main contributions are more than $1,500,000 in capital and its introduction of financial and accounting controls. Brazilian receives a ten per cent dividend on its preference shares which constitute all of its capital holdings in the company.

3. EUCATEX S.A. - INDUSTRIA E COMMERCIO: Brazilian owns twenty per cent of the capital stock of this company which is engaged in the manufacture of wallboard, accoustical tiles and related building materials. Brazilian's capital contribution is approximately US$1 million for factory improvements, and it has helped to introduce fiscal and cost accounting techniques. As of 1966, it was the only one of Brazilian's joint ventures that had undertaken exports, and has paid a ten per cent dividend each year on its Preference B shares to Brazilian.

4. EMPRESA INDUSTRIAL GARCIA S.A.: This is a family operated company engaged in the spinning and weaving of textiles. Brazilian's contribution has been about $848,000 constitutes about twenty-six per cent of the capital, and combined with the holding of the General Manager, is sufficient to constitute

majority control of the company. Brazilian found that this company's biggest problem was inventory control and has introduced a new accounting system to cope with this problem by eliminating duplication and dead stock. Brazilian has received a regular dividend on its common shares.

5. FARLOC DO BRASIL S.A. - INDUSTRIA E COMERCIO: For $613,000, Brazilian acquired a 41.6 per cent of its capital stock of this company which is engaged in the production and sale of brake and radiator parts. Wagner Electric of the United States owns about 30.4 per cent and a Brazilian individual owns the remaining twenty-eight per cent. Even though it is the largest shareholder, Brazilian considers its holding as an investment rather than a means of exercising control. Although no dividends have been paid on its common shares, it expects good capital appreciation over the years.

6. BRINK'S S.A. - TRANSPORTES DE VALORES: This is a new company incorporated in 1966 of which Brazilian owns forty-nine per cent and Brink's Corporation Limited of the United States owns fifty-one per cent. Brazilian's total investment is $267,273. Brink's sought out Brazilian because it wanted a local partner who was familiar with the problems of conducting business in Brasil and who had risk capital. This joint company will be able to transport valuables for other companies in the Brazilian

group, and therefore represents a form of vertical integration. As of the end of 1967, no dividends had been declared.

7. CELFIBRAS-FIBRAS QUIMICAS DO BRASIL LIMITADA: Private Company was formed by Celanese Corporation of New York and Brazilian in 1966 to manufacture nylon yarn in Brazil. Celanese owns fifty-five per cent and Brasilian forty-five per cent, although it was agreed that no dividends would be paid for three years and thereafter they would be paid equally to each partner. The joint venture agreement also specifies that Celanese is to have the management powers over the company, which is acceptable to Brasilian because of its desire not to participate in the day to day management. First returns are not expected on this investment until 1972.

III. CONCLUSIONS

Brasilian may not be atypical of foreign investors operating public utilities in developing countries. Public utilities are usually first priorities for nationalization and because of rates and concession agreements, governments are in a strong economic position to force terms upon the foreign owner.

In its reinvestment programme Brasilian has not acted as a typical foreign partner in a joint venture in a developing country. Firstly its local Brasilian subsidiaries are the actual partners and in the Celfibras and Brink's ventures, the foreign investor looked upon

Brazilian as if it were a local partner. Secondly, Brazilian has been seeking investment opportunities for its blocked funds, rather than seeking out local partners for its own projects. Thirdly, Brazilian does not participate in the day-to-day management or bring technical expertise to any of the joint ventures. Fourthly, it has not adopted majority or controlling positions in any of the companies and in Peixe, does not even own any common shares. Fifthly, its main contributions have been capital and the introduction of sophisticated techniques and standards of accounting and fiscal control; no industrial property has been introduced. Sixthly, it has chosen to invest as a minority partner, even though no legal constraints or incentives had dictated this business decision.

Shareholders of Brazilian have benefitted from this course of action; income from the telephone sale proceeds was almost $3 million for the first 6 months of 1966, whereas operating losses from the telephone operation for the first half of 1965 had been more than $1.2 million. In addition, the quarterly dividend of twenty-five cents was resumed and the stock sold at an all-time high. At the same time, Brazil acquired ownership of its essential utility at a very reasonable price, and has stimulated industrial growth through the compulsory reinvestment.

V. MANNESMANN-SUMERBANK BORU ENDUSTRISI T.A.S.

Mannesmann-Sumerbank Boru Endustrisi T.A.S. is an equity joint venture company that manufactures steel pipe in Turkey. 57 per cent of the equity capital is owned by the Mannesmann Group, a group of German companies with world-wide interests in the mining, iron, and steel industries. The remaining 43 per cent is owned by Sumerbank, a Turkish state bank engaged in a wide variety of industrial banking transactions of many kinds, including development banking. It does not draw money from the capital market or from private financial institutions, but obtains its money from public sources and from the investments it holds.

1. FORMATION OF JOINT COMPANY:

Sumerbank approached Mannesmann in 1954, proposing construction of facilities for the manufacture of steel pipe in Turkey, the main purpose being to save foreign exchange. The factory was built by Turkish workers with mainly German materials according to German plans. Mannesmann was the most important supplier of machinery and equipment and its share of the capital was paid for entirely through the supply of machinery and equipment. The factory was built near the town of Izmit, situated on the Sea of Marmara about 100 kilometers from Istanbul and connected by highway and rail to Istanbul and Ankara.

The site, which belonged originally to Sumerbank, has access to good water supplies, labour and transportation of facilities. At the start of production, about 15,000 tons of from 1/2" to 2 1/2" pipe were produced and by 1967 capacity was up to about 100,000 tons per year with sizes of up to 40 inches.

II. CAPITAL ARRANGEMENTS:

The original equity capital was 5,600,000 TL, of which 3,200,000 was subscribed by Mannesmann. In return for machinery and equipment the capital was later increased to TL 35 million (about US$ 4 million), of which TL 20 million were contributed by the Mannesmann Group, again in the form of machinery and equipment. It is very difficult for the Joint Company to obtain long term financing from abroad, because the risk of devaluation precludes solicitation from foreign or international financial institutions nor would the Turkish Government permit borrowing on the Eurodollar market. It has received, however, one long term loan from the European Investment Bank in the cause of an indirect transaction through a Turkish Development Bank. Mannesmann has not made any loans to the Company and accordingly the bulk of the Joint Company's debt financing has been provided by Sumerbank. The legal reserves of the Company are about TL 11 million and free reserves about TL 24 million, equalling approximately the TL 35 million capital of the Company. This conservative procedure is favoured by the government and consequently the dividend policy of the Joint

Venture Company is also conservative.

III. DIRECTION AND MANAGEMENT

The joint company has five directors elected by general meeting of shareholders. Three members are representatives of Mannesmann group and two of the Sumer Bank. Mannesmann's representatives are two Germans and one Turk. The Board meets three times a year in either Turkey or Germany to determine general policy of the company, but does not participate in the day-to-day management. The President of the Board is one of the German members.

In its day to day affairs, the joint company is headed by two Managing Directors; a Turkish Managing Director in charge of commercial affairs, and a German Managing Director who co-operates with his Turkish counterpart and who is responsible for the technical aspects. These two Managing Directors are not Board members, but they constitute a type of executive committee, with one in no way subordinate to the other. Differences which arise may be referred to the Board. This arrangement has been found practicable and satisfactory.

In the late 1950's five Germans were employed by the Company consisting of the technical managing director and four foremen. Presently only the Technical Managing Director and one plant technician are Germans, both individuals work under a three year contract. The heads of the different service divisions work directly under the Turkish Managing Director and all administrative work must be done by Turkish nationals.

In 1968 the Company had 84 administrative employees and 508 workers.

IV. TECHNICAL ASPECTS

There is no technical assistance agreement between the Mannesmann Group and the Joint Company nor does Mannesmann receive any royalties because it is the policy of Mannesmann not to take royalties from any company in which it has majority participation. It communicates all technological developments to the company on a continuing basis, however, to ensure that the joint company is kept up to date.

The skelps and coils necessary for the production of steel tubes are themselves outputs of a steel factory, and had to be imported by the Joint Company during its first years of production from Mannesmann. Now, however, the skelps and coils are produced in Turkey by Karabuk Iron and Steel Works and Eregli Steel Works. Although the Joint Company is independent of imports, the price of skelps locally is up to 70 per cent higher than internationally, making for a very high priced finished product.

V. MARKETING ARRANGEMENTS

Most sales are carried out through independent selling agencies which buy from the Joint Company at net prices, paying 30 per cent in advance and 70 per cent upon sale. Because of the high price of its products the Company has very few exports. Recently, however, a few

hundred tons of steel pipes were exported to neighbouring countries, including Lebanon.

There is no external competition to the Joint Company since the imports of steel tubes have been banned. The Joint Company suffers inland competition however, from companies manufacturing steel tubes, plastic tubes and cement tubes.

VI. MISCELLANEOUS

One problem encountered by the Joint Company in its relationships with the Turkish government has been the policy of the Government to permit a capital increase only on condition that the Company undertakes to increase exports and that profit transfers out of the country be covered by foreign exchange earnings. To increase exports, however, would require selling at a loss, since the Turkish products cannot compete on the world market. Apart from this and similar difficulties, however, the relations between the two joint venture partners and between the Joint Company and the Government are considered quite satisfactory. Import substitution will continue to be the main contribution of the Joint Company to the Turkish Economy.

VI. VOLTAS

Voltas was formed in 1954 as a bilateral equity joint venture company in India, owned forty-five per cent by Volkart Brothers, a Swiss Company engaged in trading activities and fifty-five per cent by Tata Sons Limited, a large private Indian company. Voltas is India's largest and most versatile distributor. It has 6000 employees and deals in more than 650 major products.

I. FORMATION:

Volkart Bros. had been trading in India since 1851. After Independence in 1947, Volkart felt it was necessary to bring in more Indian capital and personnel to participate in the new scheme of economic development. In 1953, Volkart began negotiations with Tata for formation of a joint venture. Tata is India's largest industrial enterprise and controls about 10% of all Indian investment in industry. After formation of the joint company Volkart Brothers continued its own separate dealings in cotton, coffee, coconut fibres and other produce. Throughout the 1960's, Volkart merged its activities with the Indian company Patel, Cotton Company Limited in an arrangement approximating a 50/50 joint venture company called Patel-Volkart Limited.

II. CAPITAL STRUCTURE

Voltas has an authorized capital of 50 million rupees (US$6.6 million) of which 43.3 million rupees is issued and subscribed for.

At its conception, Voltas was owned 45% by Volkart and 55% by Tata. By 1968 Volkart owned 10%, Tata 13%; the Life Insurance Corporation and Unit Trust of India 2%, and the public owned 45%. It now has over 9,200 registered shareholders.

Voltas has obtained financing through the issue of debentures and from other sources. Foreign exchange loans have been obtained from the Industrial Credit and Investment Corporation of India Ltd., Continental Bank International of the United States, and the Commonwealth Development Finance Company Ltd. of the United Kingdom. As of October 1st, 1968 these loans totalled as high as 13.24 million ($1.77 million).

Volkart's participation in Voltas never proved as financially rewarding as had pursuit of its own activities, and Volkart was therefore interested in decreasing its equity participation and investing its capital elsewhere. This policy of divestment and foregoing of subscription rights coincided also with government policy of widening the ownership basis and encouraging capital market formation.

III. DIRECTION AND MANAGEMENT

The Chairman of the Board and Chief Executive Officer of Voltas is an Indian national who came to it from Tata, the Executive Directors for Sales and Engineering came from Volkart, and the General Manager in charge of manufacturing operations was recruited from outside. Since its formation more and more personnel and executives of the joint company have come from Tata and there are no longer any Swiss employed in Voltas.

As the Company has progressed it has assumed a larger degree of independence from its two founting partners, especially from Volkart. By informal agreement, Tata now decides all major policy issues, which is ideal because of Tata's great managerial financial and technical resources. Eventhough it owns [illegible] of the equity, and is the largest single shareholder, the Life Insurance Corporation and Unit Trust of India acts as a passive investor, and has given Voltas' Secretary a proxy for its shares. Voltas is happy to have its participation because of the prestige it lends to the joint venture.

IV. MARKETING ASPECTS

The Company's head office is in Bombay, with branches in Calcutta, Delhi, Madras, Bangalore and Lucknow. In the year 1967-68, [illegible] of the goods sold by the Company were manufactured in India, while 19% were imported. The percentage of imports is decreasing, but is nevertheless increasing in absolute terms. Because of a growing tendency for many manufacturers to sell directly to the public, thereby eliminating [illegible] such as Voltas, the Company is aware of the necessity for diversification. The primary emphasis of Voltas will still be on the distribution of engineering equipment including after-sales servicing for a number of manufacturers, but it has also undertaken the manufacture of certain items such as air conditioners, refrigeration equipment, water coolers, elect[illegible] overhead travelling cranes, hoists, fork-lift trucks, core drilling equipment and diamond drill bits. It also has entered joint ventures

with non-Indian partners for the manufacture of products such as machine tools, switchgear and allied electrical equipment. In addition, it has undertaken a number of turn-key construction projects. Voltas also intends to increase its manufacturing activities in the electronics and agricultural fields.

V. MISCELLANEOUS

Volta has attempted to comply with national objectives of increasing exports, but this has proven difficult both in respect of the goods it distributes and of those it manufactures; all these goods are manufactured under license and the foreign licensors have precluded their export. To help earn more foreign exchange, Voltas intends to increase its construction activities in other Asian countries.

Voltas is regarded by the Government of India as a good corporate citizen, and is in fact looked upon as a Tata Company. The broad ownership base dovetails with official plans to encourage development of Indian capital markets. In addition to its own activities, Voltas has helped to promote other joint ventures between foreign and local collaborators in India. It has also acted as the local partner in many Indian joint ventures undertaken with foreign partners, eventhough it is rare for a developing country joint venture to become the promoter of other joint ventures. In the future, Voltas will remain primarily a trading organization, but with increasing emphasis on the manufacture of products in which it deals.

VII. P.T. PHILIPS RALIN ELECTRONICS LTD.

P.T. Philips Ralin Electronics Ltd. is an equity joint venture company manufacturing electronic equipment in Indonesia. Sixty per cent of its capital is owned by Philips of Eindhoven, a leader in electronics throughout the world, and the remaining 40 per cent is owned by the government of Indonesia.

I. FORMATION

Philips was conducting business in Indonesia before the Second World War. The Japanese conquered the country in 1942, and Philips left, but returned in 1946 and continued manufacturing light bulbs, radio sets and transmitter equipment from imported components. Relations between the Netherlands and Indonesia deteriorated, however, and in 1957 the Philips property was taken under government custody, and Indonesian Directors were recruited from the rank and file of the company. From 1957 to 1967, Philips maintained a few unofficial contacts with the company by shipping it some parts and components; it also forewent its claims against the government. Nevertheless, very few Philips personnel remained, and production difficulties multiplied. Finally in 1967, the new regime recognized the necessity for economic recovery and for industrial Cooperation, and asked Philips to resume its activities in Indonesia.

A basic agreement was signed in November 30, 1967 between Philips and the Government under which the Joint Company received the maximum fiscal incentives permitted by the law. The Company has undertaken production

of radios, television sets, and light bulbs with greater local production of components to alleviate foreign exchange problems.

II. FINANCING

Philips has a 60 per cent share and the Government a 40 per cent share in the capital of 17.5 million guilders. The government paid for its share by contributing the fixed assets which had previously belonged to Philips before they were taken into custody. Philips contributed its share by introducing machinery and equipment. Whatever operating funds have been required have been obtained locally.

III. DIRECTION AND MANAGEMENT

Philips and the Government have an equal participation on the Board of Directors and on the Executive Board. The Executive Board consists of four members, two appointed by each party. During the first eight years of the Joint Venture the Chairman of the Executive Board is to be appointed by Philips, but he does not have a casting vote. The executive directors have an internal arrangement for the allocation of executive functions amongst themselves. In the event of a deadlock on the Executive Board the dispute would be referred to the Board of Directors. A deadlock there would be referred to a General Meeting of the shareholders, in which case Philips would have the majority vote. It is recognised, however, that for any dispute to go that far would signify the end of the joint venture.

In exercising the day-to-day management Philips holds the keycards because of its scientific know-how and because it appoints the General Manager.

It seeks, however, the active participation of the government, although it does not wish interference. Another key to Philips power is in the supply of integrated machinery; all of the existing machinery has come from Philips or other European firms and Philips could refuse to supply further competible machinery in the event of an irreconcilable conflict.

IV. TECHNICAL ASPECTS

At the time of creation of the joint venture arrangement, a technical assistance agreement was concluded between Philips and the Company. The Indonesian Government did not want the payment of royalties to Philips, but the latter insisted on them because even its wholly-owned subsidiaries pay royalties to Eindhoven. The Government agreed to this policy upon assurances that the Indonesian joint company would be treated on the same basis as all of Philips other enterprises. Accordingly, royalty transfers have been guaranteed by Indonesian Law.

V. MARKETING ARRANGEMENTS

Management's attention has been directed initially to the problems of production, and only recently has it turned to the question of sales. Philips continues to export a number of products to Indonesia, but the question of conflicts between such imports and the Company's production has not yet been discussed. On the other hand Philips has imposed no territorial restrictions on sales of the Company's products and supposingly, if they can become competitive on world markets, the joint company's products will be exported.

VI. MISCELLANEOUS

One of the most pressing problems to date has been personnel. The basic joint venture agreement created three different categories of personnel: those to be kept without change; personnel who were to be trained; and lastly, personnel who were to be dismissed. In 1967 the [illegible] employed [illegible], 600 of whom were redundant, but the Government was unwilling to classify them as dismissible. Outside of the government there would be very little employment and the government could not risk labor unrest. Accordingly the Company has been obligated to keep all these extra people on the payroll, and a long time will pass before they can be economically absorbed into the Joint Company. Over the long term, the economic and social structure of Indonesia is so uncertain and tenuous that it is impossible to predict what success the Company might enjoy. In any event, the creation of the joint venture was a positive step by the Government in so far as it has recognized the need for foreign know-how and technology, and was prepared to grant majority control and ownership to Philips to secure it. Philips, of course, had very little to lose in returning, since all of its capital investment had been taken under custody by the Government.

VIII. THE GROUP OF THE SOCIETE INDUSTRIELLE ET AGRICOLE DU NIARI (S.I.A.N.)

I. FORMATION

The Grands Moulins de Paris Group (G.M.P.) is a number of companies controlled by the Vilgrain family of France and is the largest supplier of flour in France. Beginning in 1950, G.M.P. joined with Compagnie Générale des Oléagineux Tropicaux (C.G.O.T.) to form the Société Industrielle et Agricole du Niari (S.I.A.N.) for the raising of peanuts and the production of peanut oil in the Niari Valley on the Kouilou River in the Congo. S.I.A.N. suffered an initial setback due mainly to inexperienced management. Political pressure prevented liquidation, and it was therefore decided to convert to sugar with financial backing from the Fonds d'Investissement des Territoires d'Outre-Mer (F.I.D.E.S.). The venture was again a failure, but with the infusion of new management from G.M.P. and financial support from the newly created Compagnie Fonciere pour l'Outre-Mer (COFIMER), which took equity positions in newly created African ventures, S.I.A.N. started to turn around. In 1958 production of sugar more than tripled over the previous year and success seemed certain.

COFIMER and G.M.P. decided on a policy of diversification and expansion for S.I.A.N. Diversification included the production of flour, soap, cattle fodder and other types of food products. Expansion involved investment in other francophone countries of Africa, with milling operations being by far the most important. African governments were anxious to participate as well because of the prestige attached to milling industries. S.I.A.N. thus entered

into joint ventures for [illegible] with the governments of Congo-Brazzaville, Chad, [illegible] the Ivory Coast, the Central Afr[illegible]. Before the outbreak of [illegible] a local partner for [illegible] restricted to the [illegible].

II. CAPITAL [illegible]

S.I.A.N. is a mixed [illegible]. Its equity capital is [illegible]. The capital is owned as follows:

40.5% Grands Moulins de Paris

19.5% Fonds d'Aide et de Coopération

8.0% Dutch interests

32.0% COFIMER and other French interest

When the holding was created the independent state of Congo did not exist but the French colonial administration supported the venture through the intermediary of the public fund F.I.D.E.S., which was a shareholder of S.I.A.N. After independence, F.I.D.E.S. was replaced by Fonds d'Aide et de Coopération. In the group of S.I.A.N. companies, S.I.A.N. itself is the only one in which the Government has no participation.

The principal subsidiary of S.I.A.N. is the Société [illegible] (SOSUNIAM) which is owned 38 percent by S.I.A.N., 24 percent by the Republic of the Congo, 12 percent by Dutch interests, and 26 percent by other French

interests including [illegible] S.I.A.N. [illegible], once directly and now indirectly through S.I.A.N.

G.N.P. and [illegible] S.I.A.N. joint ventures. This [illegible] business [illegible] reasons. Also, [illegible] S.I.A.N., [illegible] African company, [illegible] African countries [illegible] direct participation of [illegible] to participate directly in [illegible] new development. In establishing a new venture, S.I.A.N. [illegible] the numerous ways in which governments [illegible] the conduct of business. [illegible] capital contributions [illegible], [illegible], [illegible], etc. In addition [illegible] S.I.A.N. capital, more than [illegible] of all investments are financed [illegible] long-term loans, many of which are obtained in France.

IV. MANAGEMENT POLICIES

S.I.A.N. has chosen to own its plantations rather than obtain its goods through supply contracts with individual farmers, i.e. the [illegible] system. This plantation system has produced lower costs and assures its works of a certain fixed income. It places, however, the risk of crop failure directly upon the company, and requires much organizational expertise. The Governments [illegible] have [illegible] the land for the plantations have not objected to this system.

Both C.V.P. and [illegible] .I.A.[illegible] [illegible]
participation in any [illegible]
holding. They feel [illegible]
satisf[illegible] [illegible]
hand in t[illegible]
then have [illegible]
To [illegible]
it is [illegible] prac[illegible]
of [illegible] be [illegible]
be [illegible]
the government [illegible]

A[illegible] of the [illegible]
to nominating [illegible] [illegible]
could occur with [illegible]
with Africans in the [illegible]
Africans are [illegible]
training. [illegible]
of personnel [illegible]

V. [illegible]

S.I.A.V. [illegible] directly to the p[illegible] [illegible]
intermediaries, especially [illegible]
of debts.

The largest problem is the price of [illegible]
year agreement [illegible] into force in January [illegible]

second United Nations Sugar Conference held in Geneva will help to stabilize prices, and that the trade cooperation achieved through the Organisation Commune Africaine et Malgache (O.C.A.M.) can be continued.

S.I.A.N.'s initial purpose to supply the Congo and neighbouring countries with sugar and SOSUNIARI was supposed to supply the world market. SOSUNIARI's present capacity is 60,000 tons per year and will be increased to a 100,000 tons, thereby producing more than all of S.I.A.N.'s other ventures combined at a cost which is probably the lowest in the world. Because of world surpluses, however, the sugar can be sold profitably only in protected markets.

SOSUNIARI intends to conclude agreements with Algeria, the USSR and the USA, but continues to sell most of its produce in the O.C.A.M. countries. Some of its best prospects lie, however, in increased local consumption, which S.I.A.N. has found generally follows the establishment of local production.

VI. MISCELLANEOUS

Host governments benefit from S.I.A.N's investments in two ways, through dividends and taxes. As a condition of investment S.I.A.N. insists on a convention d'etablissement guaranteeing S.I.A.N. tariff or quota protection, foreign exchange licenses to import machinery and equipment, and the free transfer of interests and royalties abroad.

A continuing problem for S.I.A.N. is to avoid identification with any particular tribe or political party in Africa, but this is very difficult when the daily cooperation with African governments is required. The price of sugar is another problem which may be alleviated somewhat by international agreements by regional integrations such as O.C.A.M. and the increase in local consumption.

In spite of insistence on majority ownership and managerial control of all enterprises African Governments do not resent but actively seek the participation of S.I.A.N. The plantation system has not been criticised. The reason is that S.I.A.N. contributes substantially towards the development of host countries and provides them direct revenues through dividends and taxes.

IX. THE GHANA TEXTILE PRINTING COMPANY LTD.

The Ghana Textile Printing Company Ltd. is an equity joint venture company owned 51% by the Ghana Industrial Holding Corporation, and 49% by the Anglo-Dutch Textile Investigation Group (Adtig). It is engaged in the manufacture and sale of printed cotton textiles in Ghana.

1. FORMATION

During the 1940's, the United Africa Corporation (U.A.C.) became one of the largest general merchant enterprises in the world. It is the wholly-owned subsidiary of Unilever Limited, the large multinational British corporation. During the 1950's it began to seek out partners to produce as many of the goods in which it had traded, and by the late 1960's the group operated or had substantial interests in about seventy industrial enterprises, which employed about 40,000 workers in English speaking African countries.

In 1960, the Government of Ghana, Alexander Drew and Sons (an English Textile Company), and Dodwell (an English merchant company) concluded an agreement to establish a textile venture in Ghana. Drew and Dodwell were to act as advisors and the Government was to own all of the equity. At the same time, the Unilever was establishing a soap factory in Ghana through its wholly-owned subsidiary Lever Brothers Ghana Limited. An agreement was reached between Unilever and the Government of Ghana whereby the Government acquired 49 percent of the equity in Lever Brothers Ghana Limited, and in return, the foreign consortium Adtig in which Unilever played a leading role through its wholly-owned subsidiary, the United Africa Corporation, acquired

49 percent of the equity of the textile company.

In the meantime, the Government arranged for termination of the Drew and Dodwell contracts and by 1966, both the construction of plant and the share exchanges had been completed. A new Company called the Ghana Textile Printing Company Limited (G.T.P.) was formed to acquire the textile venture's assets and production started in March 1966. The result was therefore that Unilever owned 51% of Lever Brothers Ghana Limited and continued to manage it. The Adtig consortium owned 49% of G.T.P. and was in fact responsible for management of it. Of the 49% of the G.T.P. shares owned by Adtig, 35% are owned by the United Africa Corporation (U.A.C.), Unilever's wholly-owned subsidiary; 6% by the Calico Printers' Association, a British company; and 8% by Texo-Print, a Dutch company. Outside of Adtig, Calico and Texo-Print are active competitors.

II. CAPITAL STRUCTURE

The authorised capital of G.T.P. is 750,000 Ghanaian pounds. The Adtig members paid for their shares in hard currency and the Government paid for its portion through the contribution of the fixed assets which it had previously owned in the textile company. Both partners have also contributed loan capital to G.T.P. in proportion to their respective shareholdings. An expansion of the production facilities in 1968 required substantial loans from English sources.

III. DIRECTION AND MANAGEMENT

The Board of Directors has five members: three are nominated by

the Government and two by the Consortium. Adtig has the right to nominate the Managing Director, who up until now has always been a person from U.A.C. Although U.A.C. is dominant in Adtig, the Management is in very close co-operation with the Technical Manager and with Togo-Print and Calico. Although the Consortium in fact provides the management for G.T.P., it finds from time to time that the Governments majority ownership and position on the Board creates added management problems.

From a financial point of view, it has been the Company's policy to reinvest a major portion of its earnings, and this policy has been reinforced by the difficulties of obtaining foreign exchange for the expatriation of profits. The Company has also followed a policy of localising its operations. For instance, of the 350 persons employed by G.T.P., only 16 are not nationals of Ghana. No women are employed and all employees must be literate; all the workers belong to a union.

IV. PRODUCTION AN MARKETING

Adtig provides commercial and technical assistance to G.T.P. in return for which royalties are supposed to be paid. Because of foreign exchange difficulties, however, there had been problems in transferring these fees abroad. Most of the cotton cloth is imported for printing because of its lower cost, but a substantial portion is now being produced locally. Cotton goods produced in Africa are more costly than goods from the Far East. Accordingly, all of the company's production is protected against foreign competition by tariffs and the requirement for import licenses. Also, all

the produce is consumed locally. Sales are generally made through distributors, but some large retail stores buy direct.

V. MISCELLANEOUS

G.T.P. was granted a 5 year holiday from corporate taxes and import duties to encourage its establishment. The entry of the United Africa Corporation into this joint venture is unique, having depended on its 100 percent ownership of the soap factory. Having the Government as a partner often causes problems requiring greater patience for solution but all difficulties have been ironed out so far in a businesslike fashion and the prospects for the company and for the consortium are good. Foreign exchange continues to constitute a major problem of conducting business in Ghana, and service fees have not yet been remitted. In spite of governmental priorities, import financing would be almost impossible without credit insurance from the exporting countries. Also, the Government requires a six months credit before payment can be made.

X. COMPAÑIA CENTROAMERICANA DE PRODUCTOS LACTEOS S.A. (Prolacsa)

Prolacsa is an equity joint venture company in Nicaragua engaged in the production of powdered milk.

I. FORMATION

Nestle is a Swiss company and is one of the world's largest multinational corporations. It is engaged in the manufacture and sale of chocolates, milk products, prepared and frozen foods and instant beverages, and conducts business in more than 70 countries. In 19[illegible]8 Nestle was selling in Nicaragua through an independent agent, and the government contacted it proposing construction of a powdered milk factory. Nestle concluded a plant would be feasible if it could sell throughout all of the five member countries of Central American Common Market region, and if it received protection against low cost imports.

In 1962 the five member countries signed the Protocol of San José guaranteeing that powdered milk would not be imported into the CACM, and that it could circulate freely between the five countries without taxes being imposed. To prevent total monopoly prices, however, the Protocol states that when Central American production meets local needs, 1% of the requirements may be imported.

II. CAPITAL STRUCTURE

It was decided that the governmental agency the Instituto de Fomento Nacional (Infonac), would become a partner with Nestle and Infonac owning 1%

each to encourage as much Central American participation in the company as possible, it was agreed in 1966 that the capital of the country would be 10 million cordobas composed of 100,000 shares divided into five series, as follows:

Series A - 15% - owned by Nestle

Series B - 15% - owned by Infonac

Series C - 20% - owned by the Stock-breeders' Association of Nicaragua (1[illegible] and other Central American investors ([illegible]%)

Series D - 20% - owned by Central American investors

Series E - 30% - owned 16% by Nestle, 9% by Nicaraguan financial institution and [illegible]% by other Central American investors.

Prolacsa was incorporated on December 15, 1966. Nestle insisted that the [illegible]% reserved for Central American investors be divided equally amongst investors of the other four Central American countries. In the event of withdrawal there is no first refusal given to any shareholders but preemptive rights exist in respect of any capital increase. In 1967 the Inter-American Development Bank granted to Infonac a loan of US$1 million which Infonac in turn loaned to Prolacsa in cordobas, meaning that Prolacsa can pay off this loan in soft currency without risk of devaluation. This loan must be used only for imports of machinery and equipment and it was stipulated that at least $50,000 worth must be selected on a public tender basis.

III. DIRECTION AND MANAGEMENT

The Board of Prolacsa has five members and each of the five series of shares is entitled to select one director. Through the Series A and E shares,

Nestle has two seats, and Infonac has one seat through the Series B. The Stock-breeders' Association of Nicaragua, although it has a majority of the Series [illegible] shares, has agreed that it would elect a non-Nicaraguan Director, and this seat is presently held by a [illegible] financial institution. [illegible] ty of four, giving Nestle a _de facto_ veto power.

Since Nestle is responsible for controlling the technical aspects of production, Infonac has [illegible] allowing Nestle to control the day-to-day management as well. Nestle designates all major corporate officers, including the General Manager, two [illegible] Managers who deal with administration and production, the Laboratory Chief, and the Head Mechanic, but it is expected that this arrangement might be changed in the near future.

IV. TECHNICAL ASPECTS

The factory was built in [illegible] the interior of Nicaragua. Initial capacity will be about 4 million pounds of powdered milk a year and expansion of facilities will be necessary to reach the 10 million pounds required to meet the total expected consumption in the CACM. Two brands of powdered milk, one with 28% and the other with 26% fats are produced.

During the first negotiations, Infonac asked Nestle to license its trademarks to Prolacsa. Nestle was finally persuaded to do so on the basis that other imports would be restricted and it would no longer be able to

import Nestle brandname products int[illegible].

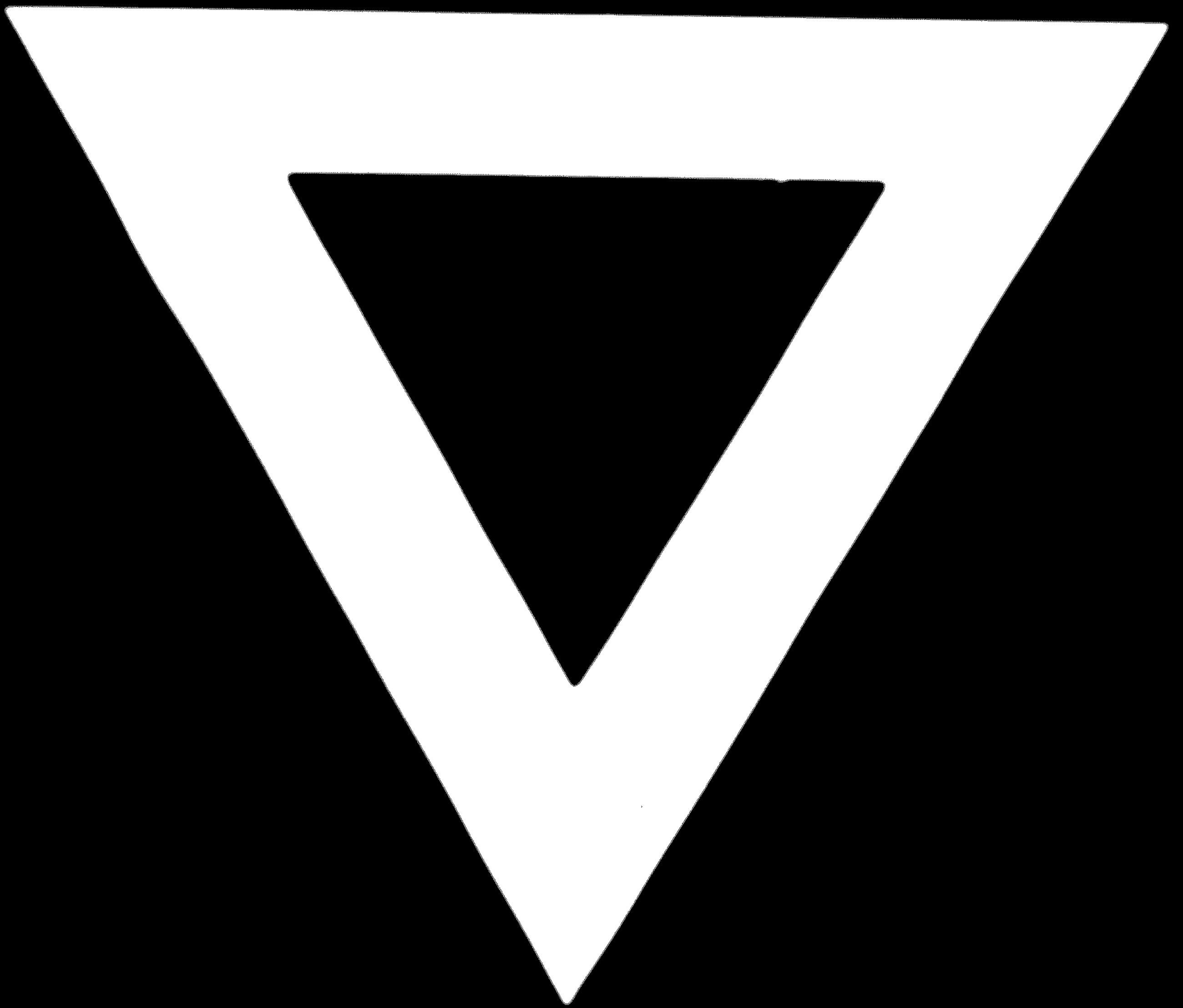
Nestle, of course, [illegible] to protect its brandnames, but its technical assistance [illegible] production. It has also [illegible] stock-breeders [illegible] their grazing, breeding and [illegible] assistance and trademarks [illegible] per pound of milk powder produced, [illegible] having been net pr[illegible]ted profits exceed a [illegible]. Royalty payments are to be made [illegible].

V. MARKETING [illegible]

It was not necessary for Prolacsa to [illegible] since Nestle already had a distribution [illegible] Guatemala, El Salvador, Costa Rica, Honduras and Nicaragua. Prolacsa therefore signed distribution agreements with the companies [illegible] in each of these countries and these organizations act as commissioned sales agents. Until production reaches CACM consumption levels, all foreign [illegible] will be precluded.

VI. MISCELLANEOUS

Most of Prolacsa's suppliers are individual stock-breeders and the government of Nicaragua has committed itself to establishing a road network to facilitate milk collection, the cost of which will be about 14 million. The government will also pay the estimated $5 million cost of helpint to improve breeding stock and grazings and milking methods,



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