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### Strategic Alliances: Emerging Trends in Future Corporate Business

Naresh Menghraj Gehi  
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**STRATEGIC ALLIANCES:  
EMERGING TRENDS IN FUTURE CORPORATE BUSINESS**

**Naresh Menghraj Gehi**

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STRATEGIC ALLIANCES:  
EMERGING TRENDS IN FUTURE CORPORATE BUSINESS

by

NARESH MENGHRAJ GEHI

BACHELORS OF LEGAL LAWS  
LL.B, UNIVERSITY OF BOMBAY, 1992

A Thesis Submitted to the Graduate Faculty  
of the University of Georgia in Partial Fulfillment  
of the  
Requirements for the Degree

Masters of Law

ATHENS, GEORGIA

1995

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STRATEGIC ALLIANCES:  
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by

NARESH MENGHRAJ GEHI

Approved:  Date 10/20/94  
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June 7, 1995  
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## ACKNOWLEDGEMENTS

It is a matter of great pleasure for me to have completed my thesis. I owe an enormous debt of gratitude to Dr. Rick Huszagh for being my major professor. I fall short of words to thank him for all the earnest cooperation which he has solicited in the preparation of my thesis. I specially thank Professor Samuel Davis who has been my major source of inspiration in the Law School. He has been extremely kind to offer his valuable suggestions in the preparation of my thesis. It was my pleasure to work with him. I thank Professor Gabriel Wilner for his moral support without which it would have been difficult for me to proceed. Last but not least, my special thanks to Sherri Mauldin, a great friend, for her indispensable support in computers.

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CHAPTER 1  
INTRODUCTION

This thesis describes the importance of strategic alliances in today's competitive world. It shall make the reader familiar with the concept of a strategic alliance and the benefits of entering into a strategic alliance. It shall further deal with the legal implications, various industries in which strategic alliances are dominant and the procedures for dealing with issues such as the intellectual property of the developed product.

A. Definition & Overview

An alliance is defined as the joining of forces of two or more entities in pursuit of a common opportunity or opportunities.<sup>1</sup> A strategic alliance is an arrangement for economic collaboration between firms at more or less, the same level of distribution, involving an exchange of critical skills aimed at extending or buffering the core

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<sup>1</sup> Douglas G. Sriver Strategic Alliances in the 1990's 12 Computer L. J. 264 1992 available in WESTLAW JLR File.

The author has used the word entities instead of companies or businesses because some parties to the alliance can be governmental agencies, universities or non business entities.

business strategy, technology or markets of partners.<sup>2</sup>

Reflecting a slightly different perspective, Jorde and Teece define a strategic alliance as a bilateral or multilateral relationship characterized by the commitment of two or more partner firms to a common goal.<sup>3</sup> An alliance is said to be strategic when it represents a strategic initiative of an entity or it otherwise provides essential support to a strategic initiative or objective of the entity.<sup>4</sup> Research indicates that the care and thought of the strategic alliance partners increases with the importance of the venture to the strategic objectives of the entity. Thus, when the parties enter into a long term alliance, the commitment of the parties becomes more and more strategic. Conversely, an alliance which is not strategic is said to be "tactical"<sup>5</sup>

In forming a strategic alliance time and management should be considered equally important as the financial aspects. Obviously, strategic alliance is a good means of

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<sup>2</sup> S. Achrol Ravi et al, The Environment of Marketing Channel Dyads, A Framework for Competitive Analysis 47 J.Mrktg. at 3. (1991).

<sup>3</sup> Thomas. M. Jorde & David. J. Teece, Acceptable cooperation Among Competitors in the Face of Growing International Competition 58 Antitrust L.J. 529. (1991).

<sup>4</sup> Douglas.G.Scriver, supra note 1.

<sup>5</sup> A tactical relationship is a good way of beginning a relationship with another corporation. This will make the parties aware of each others likes and dislikes, and subsequently the parties can engage into a strategic alliance.

gaining access to the capital of another company, especially in an instance where the other partner has excellence in technology, research and development facilities, etc. However, one corporation may have excellent distribution skills, but it may be deficient in manufacturing due to poor research and development facilities. Thus, a joint effort can enable the partners to overcome this barrier by combining their core competencies. The partners can produce mass amounts of goods together in a shorter time and can reap the benefits of the market before other competitors enter the market. Instead of one of the partners bearing the entire cost and risk associated in manufacturing the product, the costs for production, distribution can be shared between the partners.

Strategic Alliances have been variously described as coalitions, hybrid organizations, quasifirms and transorganizational systems.<sup>6</sup> They represent alternative modes of organization between market mediated exchange and internal hierarchy.<sup>7</sup> It is difficult for a single corporation to compete alone in an ever changing environment. The need for a strategic alliance arises because in the post industrial era, unusual forms of marketing organization which are ambidextrous and highly flexible will be needed to cope with complex and dynamic

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<sup>6</sup> Thorell & Hans B, Networks: Between Markets and Hierarchies 7 J. Strategic Mgmt. at 37. (1986).

<sup>7</sup> Id. at 38.

tasks environment.<sup>8</sup> Strategic Alliances are partnerships that work together to attain some strategic objective<sup>9</sup>

#### B. Difference Between Strategic Alliances and other Alliances

A joint venture has been the most visible form of a strategic alliance. It enjoys the control and coordination advantages of an internal hierarchy, but presents special problems of its own, eg. fusing of cultures, potential domain conflict with parent companies etc.<sup>10</sup> Strategic Alliances on the other hand go beyond normal market transactions but fall short of mergers.<sup>11</sup> A strategic alliance differs from other types of alliances as they are more informal, spontaneous partnerships that come together fast and break up fast.<sup>12</sup> A strategic alliance can be distinguished from entity joint ventures as they do not involve the formation of joint ownership of a legal separate firm which exploits the shared technology, rather the participating firms coordinate joint activity within limits

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<sup>8</sup> S. Achrol Ravi, Evolution of the Marketing Organization: New Forms for Turbulent Environments 55 J. Mrktg. at 77 (1991).

<sup>9</sup> K.R. Harrigan, Strategic Alliances & Partner Asymmetries Mgmt. Information Rev. at 53 (1987). (quoting Berg et al, Joint Venture Strategies and Corporate Innovation).

<sup>10</sup> Achrol Ravi et al, supra note 2 at 3.

<sup>11</sup> Id. at 3.

<sup>12</sup> Thomas. M. Jorde & David. J. Teece, supra note 3.

structured by a series of agreements.<sup>13</sup> Corporations prefer strategic alliances because reported success rates for interfirm ventures is low.<sup>14</sup> Strategic Alliances bring together partners that may be horizontally- or vertically related to each other, but need not be related to each other at all.<sup>15</sup> The partners will stay together as long as they need each other and their venture remains successful, unless the terms invoked by the bargaining agreements "divorce clause" are so egregious that they constitute an exit barrier that perpetuates a partnership long after its usefulness to at least one of the partners has expired.<sup>16</sup> Entering into a merger or a joint venture can restrict the market share of the companies.<sup>17</sup> A strategic alliance benefits the corporations to contribute their 'core competencies' and avoid expensive means of manufacturing which may involve high research and development costs. Strategic Alliances are more successful when partners are related in products, markets or technologies.<sup>18</sup> These ventures last longer between partners of similar cultures,

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<sup>13</sup> Jeffery Atik, Technology and Distribution as Organizational Elements Within International Strategic Alliances, U. Pa. Int'l Bus. L. at 274. (1993).

<sup>14</sup> K. R. Harrigan, supra note 9 at 53.

<sup>15</sup> Id. at 53.

<sup>16</sup> Id. at 54.

<sup>17</sup> Id.

<sup>18</sup> Id. at 70.

asset sizing and venturing experience levels.<sup>19</sup> Venturing firms should worry less about their partners traits and more about the competitive needs that their ventures are intended to address when managers use strategic alliances.<sup>20</sup>

In the case of merger of equals between two corporations, two corporations of approximately the same size join in a stock for stock transaction along with exchange ratio which is fixed on a market to market basis. In such ventures, one of the parties acts as an acquiror and will offer a modest premium to the market price for the target stock.<sup>21</sup> In contrast, strategic alliance is a bilateral type of relationship which is characterized by the commitment of two or more partners to reach a common goal and which entails the pooling of specialized assets and capabilities.<sup>22</sup> It can include technology swaps, joint research and development, co-development of a product and sharing of complimentary assets by the corporation.<sup>23</sup> Moreover, they are distinct from exchange transactions because in case of an exchange transaction the object of the transaction is supplied by the selling firm to the buying

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<sup>19</sup> Id. at 70.

<sup>20</sup> Id. at 70.

<sup>21</sup> Id. at 531.

<sup>22</sup> Id.

<sup>23</sup> One party may do the manufacturing and the other party may do the distribution for the a co-developed product.

firm in exchange for cash,<sup>24</sup> while a strategic alliance cannot have a one sided party which receives cash alone.

Strategic Alliances include consortia, and joint ventures. These alliances are an easy and effective way to organize for innovation, especially where an industry is found to be fragmented.

A strategic partner varies from a financial investor in that a strategic partner will invest more money for less ownership.<sup>25</sup> The investment may be for a longer time, depending on the nature of the project and the strategic partner brings with him other facilities to the project such as its research and development facilities as well as may provide distribution networks and manufacturing services.<sup>26</sup>

In essence, strategic alliances are good means of turning competitors into friendly associates. By cooperating with another entity, a corporation can reduce the cost of development, production testing, building a sales force etc.<sup>27</sup> It can help the partners to avoid taking loans from financial investors who charge high interest. "Strategic alliances at the growth stage are frequently characterized as joint ventures in which two corporations,

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<sup>24</sup> Id.

<sup>25</sup> A. David Sliver, Strategic Partnering: The Elements of Strategic Alliances McGraw Hill Pub. 15 (1993).

<sup>26</sup> Id. at 15.

<sup>27</sup> Id. at 15

one of which possesses a rapid growth track and the other with lots of assets agree to work cooperatively.<sup>28</sup>

### C. Benefits of a Strategic Alliance

The potential benefits of strategic alliance include:

1. Reduction of the capital costs on an individual party associated with entering into new product lines or expanding capacity for existing products.
2. Penetration of specific geographic markets, particularly when one of the partners is familiar with the geographic market or has local governmental or business contracts.
3. Reduction of research and development costs or other fixed costs in developing or marketing new products.
4. Gaining access to new or improved technology.
5. Acquiring a distribution network.
6. Acquiring a source of raw materials or other inputs.<sup>29</sup>

A strategic alliance is useful for a corporation which may have limited resources and technology. Such a drawback can be overcome by combining the resources of the other partner. The combination of resources and technology can reduce the investment and will be beneficial in spreading

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<sup>28</sup> Id.

<sup>29</sup> Blaine V. Fogg & Stephen F. Arcono; Strategic Partnerships and Alliances PLI 1993, available in WESTLAW, JLR File.

the risks. The best results in a strategic alliance can be achieved if the partners pursue the alliance in a horizontally related activity.<sup>30</sup> The goals of the partners should be clearly defined before entering into the alliance. For example, they may be designed specifically to help the corporation to keep abreast of the latest developments in science and technology, gain access to any geographic market and resources, and exercise control and share the risks. In particular, the alliance partners can enter into countries where it may not be possible for a company to enter into a particular geographic market due to regulations.<sup>31</sup>

#### D. Relationship Between the Strategic Partners

The successful performance of an alliance is dependant on the links between the partners and the joint activity.<sup>32</sup> The partners should have a complimentary strategic motive for the corporation. Researchers have found that a horizontally and closely related venture performs better than a venture that is vertically related in terms of venture success, survival and duration.<sup>33</sup> Specifically, such alliances have been found to be highly successful in the metal fabrication, petrochemicals, pharmaceutical and

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<sup>30</sup> Harrigan, supra note 9 at 70.

<sup>31</sup> Id.

<sup>32</sup> Harrigan K. R. supra note 9 at 54.

<sup>33</sup> Id. at 54.

programming (film) industry. In sum, the best benefits are derived where the partners are related in product, market and technology.<sup>34</sup>

The joint production of goods in a strategic alliance has the aspects of contract and property.<sup>35</sup> The contract aspect of this joint production relation will involve the efficient and timely transfer of technology and the duty of the other partner of the non - disclosure of the proprietary technology.<sup>36</sup>

The need to compete in global markets and especially the devalued dollar and U.S. stocks and asset values enhance the formation of strategic alliances which involve U.S. companies and other international corporations who intend to enter in the U.S. markets to do business.<sup>37</sup> In future, strategic alliances will be more important to corporations than mergers, outright acquisition and entity joint ventures to compete in global markets as the joint effort of the

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<sup>34</sup> Id.

<sup>35</sup> Jefferey Atik, supra note 14 at 278.

A firm from Japan produces a particular type of hair oil with property technology. This firm may enter into an alliance with another firm from Italy in which the firm from Japan transfers its technology to the Italian firm, enabling the firm to produce hair oil in Italy.

<sup>36</sup> Id.

<sup>37</sup> J. Michael Snell & Marc J. Segalman, New Deal Structures in the 1990's: Mergers of Equals and Strategic Alliances 731 PLI at 578 (1991).

alliance shall help the strategic partners in saving time and money.<sup>38</sup>

"Collaboration among competitors through strategic investments and through various business relationships, including informal cooperation, strategic networks, contractual networks, consortia and joint ventures can serve to reduce time costs and risks inherent in developing a technology or a new product, penetrating a new market and improving quality, and performance and customer service."<sup>39</sup>

E. Different Areas in Which Strategic Alliances are Emerging

A strategic alliance may be in the following areas:

1. Training, Knowledge and Exchange: In this type of a strategic alliance, one of the parties provides the necessary training and the other partner provides the essential knowledge which is needed in developing the product.<sup>40</sup>

2. Lead Sharing and Cross Referrals: One of the partners may be a good manufacturer but may be incapable of

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<sup>38</sup> Id. at 580.

<sup>39</sup> Id. at 580.

<sup>40</sup> Microsoft provides training and information concerning its products to many product developers in order to make their products accessible to IBM products.

providing an after sales and service facility. A cross referral strategic alliance can be entered with another party.

3. Teaming: Teaming is an arrangement where two or more of the providers of products or services work in a cooperative environment in order to pursue one or more joint or mutual opportunities.

4. Research and Development Agreements: The Research and development agreements can either be bilateral or it may involve three or more parties.<sup>41</sup>

Various types of agreements are entered by corporations which form strategic alliances. An agreement may be with respect to the joint development and manufacturing of a product. Similarly, an agreement may be entered where one of the parties markets the products of the other, whereby the other shall act as an agent of the other party.<sup>42</sup>

Corporations also enter into strategic alliances by means of cross licensing agreements. In this type of an agreement two or more companies license some or all of their

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<sup>41</sup> Id. Anderson consulting has a cost sharing contract with the air force. This contract is related to the development of knowledge based software program. Anderson is a founder sponsor of the institute of learning sciences at the Northwestern university. In this arrangement Anderson has been granted the right to commercialize the technology which results from the research at the institute and in return Anderson shall be funding the Air force for the development of the product.

<sup>42</sup> IBM has a large number of strategic alliances in this area.

technological know how which they possess to each other for use in each other's product or manufacturing process.<sup>43</sup>

The other forms of alliances include the traditional joint venture in which each of the parties contribute certain assets and share the profits and losses of the newly formed separate entity.<sup>44</sup>

A strategic alliance primarily relies on control and compromise rather than control and contract being its operative terms.<sup>45</sup>

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<sup>43</sup> Charles T. C. Compton, Cooperation, Collaboration, and coalition: A Perspective on the Types and Purposes Technology Joint Ventures 61 Antitrust L. J. at 864. (1993).

Seagate Technology Inc. and Quantum Corporation (two of the worlds largest disk drive manufacturers) made an announcement in July 1992 of entering into a worldwide patent cross licensing agreement. The chief executive of Seagate, Alan Shugart, stated that the intention of entering into such an agreement was to avoid future litigation with Quantum corporation. He further stated "I'm an American citizen and I can see that lawyers are screwing up the country and therefore my solution is to have a broad cross license agreement with a key competitor."

<sup>44</sup> The joint venture between Texas Instruments, Canon, and the Singapore Economic development Board to construct a 30,000 square foot semiconductor manufacturing facility in singapore at an estimated cost of \$330 million. Under this Joint venture agreement, Texas instruments and the Singapore agency shall each own 26 percent share of the company and Hewlett-Packard and Canon shall each have 24 percent. All the products which shall be manufactured shall be sold to Texas Instruments, which shall guarantee to sell to the other partners at a pro rata percentage of the products.

<sup>45</sup> Id. at 868.

An example is the series of joint ventures and co-development agreements announced between Apple and IBM in 1993.

## F. The Need for a Strategic Alliance

The innovation of new goods creates a demand in the market. The increasing demand of the goods leads to competition which in turn results in lowering the prices of goods. In today's everchanging business environment it is not possible for a single firm to do all of these activities alone especially for reasons of cost, competence and timeliness. The competitive situation has created a necessity for corporations to unite in order to be competitive and keep abreast of changing technology.

Formerly, most of the corporations were vertically integrated i.e. they manufactured literally each and every part of the product. Now due to the short term product life cycle and increasing competition it is extremely difficult and equally expensive for a corporation to be vertically integrated. These vertically integrated corporations are changing into virtually integrated which are linked up, down, and sideways with other corporations in a value chain which extends from research and development, production distribution, marketing etc. within a network of alliance and partnerships.<sup>46</sup>

"It is dumb to make everything just in order to prove you can. The key is to do something better than everyone else in the world."<sup>47</sup>

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<sup>46</sup> Id.

<sup>47</sup> Id.

Risk sharing becomes important especially when the next generation of technology requires investments of hundreds of million dollars and especially in instances where the risk standards are to be determined in future.<sup>48</sup>

A strategic alliance is helpful for newly emerging corporations in order to survive in the adolescent period. The union of the partners can also help them also by staying at the "bleeding edge" of the core technology.<sup>49</sup>

Strategic Alliances are a good means of establishing de facto standards by technology companies<sup>50</sup> who intend to establish their dominance in the market and makes their task easier to compete with another dominant corporation in the market.<sup>51</sup> Sharing of financial risks, need for

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<sup>48</sup> Id. at 870.

<sup>49</sup> Id. at 872.

<sup>50</sup> Creating a de facto standard requires the building of an entire infrastructure of suppliers, software developers, chip and component manufacturers, and distributors. The most important factor in creating a defacto standard is a customer base which is the sine qui non about not only the enterprises technological significance but also the long term survival.

<sup>51</sup> The Apple/IBM Motorola alliance announced in 1991 set defacto standards in the personal computer industry in 1993. Apple and IBM astonished the computer market by announcing a series of strategic alliances as both were intense competitors. Motorola was the third party to the arrangement.

Apple and IBM hope that the combination of three big names will help them to build customers and the necessary infrastructure to create a defacto standard. this alliance shall also include some small time corporations which shall bring their complimentary skills. In this alliance Groupe Bull is one of the small time corporations which shall bring its complimentary skills.

complimentary know how and technology and opportunities for quickly entering new markets are the key factors which motivate the formation of strategic alliances.<sup>52</sup> The importance of strategic alliances has also been realized in the multimedia industries. "Multimedia industries involve the convergence of various historically distinct industries, including computer software and hardware communications and entertainment and publishing.<sup>53</sup> These alliances help in the development of multimedia products as a single corporation in this industry may not possess the required expertise and know how in the field.<sup>54</sup>

The most common forms of alliances traditionally have been partnerships and formation of separate entities. A partnership has the advantages of a single level of taxation because of the "Pass through" nature. It is flexible in allocating losses and profits separately within its management structure. But a partnership has a disadvantage

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<sup>52</sup> William I. Schwartz, Legal Issues Raised by Strategic Alliances Involving Multimedia 10 Computer Law. 19 1993 available in WESTLAW, JLR File.

<sup>53</sup> Id.

<sup>54</sup> IBM, Apple and Silicon Graphics. Software Corporations such as Microsoft, Consumer electronic suppliers such as Sony, Matsushita, Video game corporations such Sega and Nintendo, entertainment and publishing corporations such as Paramount and Time Warner. Cable companies such as TCI, and Telephone and Telecommunication companies such as Bell Atlantic and AT&T.

of unlimited liability.<sup>55</sup> A separate entity is preferable where a project requires a long term commitment of management resources and significant investment.<sup>56</sup>

Advances in technology and specialization of products has made it increasingly difficult for a single corporation to satisfy the needs of the customers and keep pace with the changing market. There is specialization needed in literally every field today.<sup>57</sup> In order to survive and compete successfully it is necessary to be competitive and innovate goods at the proper time by manufacturing products which have a short term life cycle. To provide such short life cycle services is very difficult for a single corporation and thus it normally takes multiple providers to successfully achieve their objectives. With the development of technology and modern communication systems the expectations of the clients have also increased. The clients need products which satisfy their needs smoothly and efficiently. The clients keeps an interest in buying products which are reliable and can render a high level of performance.<sup>58</sup> This has imposed a compelling necessity on

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<sup>55</sup> Mark F. Radcliffe & J. Howard Clowes, Strategic Alliances and Intra-Industry Licenses 4 Computer Law. 21 (1991) available in WESTLAW, JLR File.

<sup>56</sup> Id.

<sup>57</sup> There are specialized computer programs for accounting, lawyers, shippers, doctors etc.

<sup>58</sup> Mark L. Gordon & Françoise Gilbert, Contracting for Systems Integration Transactions 12 Computer Law 13 1991 available in WESTLAW, JLR File.

the manufacturers to develop products which ratify the needs of their clients.

Before having a strategic alliance it is important for the partners to understand the needs and expectations of the client.<sup>59</sup> An agreement should be entered by the partners only if they feel that they possess the infrastructure to meet client requirements.

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<sup>59</sup> Id.

CHAPTER 2  
MANAGEMENT ISSUES

A. Control

A critical issue after the formation of a strategic alliance is the decision to be taken by the parties regarding the day to day management of the newly formed enterprise. These are very delicate issues as the success and failure of the alliance relies on it.<sup>60</sup> The lawyers should determine the strengths of the parties and accordingly hand the management to the appropriate partner. The agreement should define the rights and duties of the managers and the other employees.

The issues relating to policy should be addressed by means of a special vote. Critical issues should have a super majority vote or unanimity between the parties.<sup>61</sup> They should be decided by the board of directors. The board of directors should consist of equal number of directors of each of the parties.<sup>62</sup> The parties should express equal

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<sup>60</sup> Mark Radcliff supra note 55.

<sup>61</sup> An example in this area would be like change in the area of research, changes in the budget above a certain percentage. The requirement of a significant contribution of new capital by the parties, the admission of third parties to the alliance.

<sup>62</sup> Id.

concern over filling positions resulting from a vacancy and for minimum number of directors needed for a quorum.

B. Duties and Responsibilities of the Project Manager and Other Employees

The duties and responsibilities of the project manager should be determined. The contract should provide for the recruitment of adequate and well trained competent staff.<sup>63</sup> A substitution clause should be included for changes of non competent staff members. There should be special privileges given to experienced employees who are well trained and possess an indepth knowledge of the project,<sup>64</sup> since loss of such employees could hamper the smooth functioning of the project. There should also be a provision delineating the duties to be performed by each participant.

C. Handling of Disputes in a Strategic Alliance

As a strategic alliance includes complex transactions between the parties, disputes and other problems are likely to arise during the performance of the alliance.<sup>65</sup> The agreement should suggest different modes of dispute resolution between the parties. There should also be meetings between the parties at regular intervals to resolve

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<sup>63</sup> Mark Gordon & Francoise Gilbert, supra note 58.

<sup>64</sup> Id.

<sup>65</sup> Id.

disputes which may arise. The agenda of the these meetings should be to discuss the problems which have arisen after the last meeting and should suggest ways and means for resolution. If the parties are unable to reach a compromise then the matter should be forwarded to the management committee.

If the management committee fails to resolve the dispute then the parties should resort to arbitration. An equal number of arbitrators should be appointed by the parties and the decision of the arbitrators should be binding and final on the parties.<sup>66</sup>

#### D. Communication During the Performance of the Alliance

Problematic issues should be negotiated through intense communication, preferably face to face as people need to understand each other before they can trust each other.<sup>67</sup> Clear communications, spotting of issues for each other ahead of time, recognizing each others priorities and avoiding surprises are the foundations of mutual trust<sup>68</sup> which is essential to project completion.

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<sup>66</sup> I do not propose the courts as courts involve a lot of money and time.

<sup>67</sup> Udayan Gupta, Tough Economic Times can Make Strategic Bedfellows .... Alliances Between Firms Promote Competitive Strength, Wall St. J., Nov. 23, 1990 at B2.

<sup>68</sup> Id.

### E. Vertical and Horizontal Relationships

The structured relationship between the strategic partners can either be vertically or horizontally structured. In a vertical relationship between the parties, the responsibilities and the obligations flow directly to a party whereby one of the parties renders performance to the other party.<sup>69</sup> In horizontal relationships there is a group or teaming relationship between the parties. The parties agree that they have a joint interest in the venture.<sup>70</sup>

In the vertical relationship between the manufacturer and the client, the manufacturer renders performance to the client.<sup>71</sup> The involvement of the client is very limited in the project. In case of large projects, especially where a number of parties are involved the client should allocate his responsibility to the "Prime Manufacturer." The Prime Manufacturer shall be a person who shall have overall responsibility of owing performance on behalf of the other strategic partners to the client directly. He shall be held responsible to the client for any sort of problems which may arise during the project.<sup>72</sup>

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<sup>69</sup> Mark Gordon supra note 58.

<sup>70</sup> A vertical relationship can be between the client and one of the providers. There can also be a horizontal relationship between the client and one of the providers.

<sup>71</sup> Id.

<sup>72</sup> The prime manufacturer shall monitor the performance of the other members in the chain to ensure successful implementation of the alliance. He serves as a nexus between the client and the other strategic partners.

The coordination, development and implementation of the project should entirely rest on the prime manufacturer. He should act as a gateway between the client and the other manufacturers.<sup>73</sup> At uniform intervals the prime manufacturer should keep the client informed about the project. This will create a cooperative bond between the client and all the manufactures resulting in strengthening the relationship between the parties. The prime manufacturer should keep the client informed on the evolution of the project. He should see that the different components in the project operate uniformly and should ensure mutual cooperation between the other strategic partners.

Sometimes, the client will have to have a direct relationship with all the strategic partners especially when none of the partners wish to undertake the role of the prime manufacturer. In such relationships there shall be a number of vertical linkages between the client and the manufacturers.<sup>74</sup> It is possible for the client to have a number of vertical linkages with the different strategic partners but this is not feasible as it does not allocate overall responsibility in an event of failure of the project. Each partner shall assume responsibility to the extent of his share in the alliance. When there is a

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<sup>73</sup> Id.

<sup>74</sup> Id.

failure by one of the partners then the entire project can come to a standstill.

In a horizontal relationship between the client and the manufacturer the client pairs up with the strategic partners. In many instances the client does not possess the expertise which is necessary to develop the product but he has the entire information and understanding of his requirements. The client may have some expert personnel employed in his organization who can work with the alliance partners to develop the product. The client contributes his knowledge resource in the development of the product, but the strategic partners bring in other resources such as expertised technical staff, programmers, technicians etc who are able to fulfill the obligations of the client.<sup>75</sup> This type of arrangement is lucrative to both the client and the alliance partners since it reduces the manufacturing costs of the client to a great extent. It also benefits the strategic partners as they learn to innovate new products with the assistance of the client. This can serve as a source for future income for the strategic partners. Consequently, these factors provide an edge to horizontal relationships over vertical relationships.

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<sup>75</sup> Id.

#### F. Horizontal Structure Between the Providers

In the 1990's a number of strategic alliances have emerged between hardware and software computer developers.<sup>76</sup> In these relationships the strategic partners exchange information on important issues such as research and development of a new product. Compatible and easily marketable products can be developed with the cooperation and coordination of the other partners. Thus, the team effort of the partners enables them to have a leading edge over other competitors since the core competencies of each of the partners can be used to manufacture unique products with the advantage of the partners remaining a separate and independent identity.

It is not possible to say when a purely vertical or a horizontal relationship will be beneficial. The structure is totally dependant on the nature of the transaction and the requirements of the parties.<sup>77</sup> Once the type of structure has been determined then one can go ahead with the specifics which best suits the interest of the parties.

The real success of a strategic alliance can only be determined after the parties start working together towards a strategic objective. The allocation of responsibility should be on those people who are dedicated to the project. There should be uniform support from the senior management

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<sup>76</sup> Id

<sup>77</sup> Id

executives, entrepreneurs, managers etc. of the company. In order to ensure success there should be no communication gap between the parties. This shall increase the rapport and shall make the relationship healthy and also, will keep the interests of the parties synchronized.<sup>78</sup>

The flow of information should be properly balanced. This shall help to bring the problematic issues to the managements forefront at an earlier stage rather than keeping them in abeyance. The delay can lead to end in disruptive and contentious disputes.<sup>79</sup>

An effective dispute resolution process is an important factor in the formation of the alliance as "allowing surprises to occur and disputes to fester can jeopardize even the most economically successful venture."<sup>80</sup>

As a strategic alliance is a hybrid organization where the components are manufactured by different parties it is necessary that these parties share certain technical knowledge and trade secrets. Therefore, to achieve positive results it is essential to see that there is a free flow of information between the parties.<sup>81</sup> These factors require careful definition prior to the project's commencement, since it can alemiorate the problematic areas which may

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<sup>78</sup> Douglas Scriver supra note 1.

<sup>79</sup> Id

<sup>80</sup> Id

<sup>81</sup> Mark Gordon supra note 58.

hamper the smooth functioning of the alliance.<sup>82</sup> This is very important as a strategic alliance may involve several partners who have a different history and organization. Therefore it is necessary to ensure that the relationship between the parties is smooth and cordial. The parties should take all efforts to eliminate intimidating factors and should establish means to work together. Procedures should be developed to terminate employees who do not cooperate with the other team employees. Special consideration should be paid to issues such as allocation of responsibilities among the participants and the scope and extent of responsibility of each of the parties. The flow of information should be uniform. These sorts of responsibilities should be allocated to a team manager who should be responsible for the leadership and scheduling the project.<sup>83</sup>

#### G. Conclusion

The goal of the strategic partners should be to see that all the components which operate together are compatible and produce the required information within a stipulated time. This requires meticulous coordination. Strategic alliances have the ambidexterity for efficient management of business information needed to have a leading

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<sup>82</sup> Id

<sup>83</sup> Id

edge over others. Strategic alliances have evolved with the availability of an increasing number of choices and alternatives,<sup>84</sup> and the pressures of a number of small and less expensive competitors. For example, in the computer industry a number of small software firms have emerged all over the world that have their own niche and provide the customers with an array of software application programs which are developed for the computers and their clones.<sup>85</sup> For the non-niche market participants, a strategic alliance among partners can increase the production of compatible products, techniques and technologies. Such partners can be a client or provide products and services.<sup>86</sup> However, it is important to see that the link between the parties is properly established since a weak link can adversely affect the project efficiency and effectiveness.<sup>87</sup>

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<sup>84</sup> Id.

<sup>85</sup> Id.

<sup>86</sup> Such as manufacturers, distributors, developers and consultants.

<sup>87</sup> E.g., failure to meet deadlines, personal incompatibility, etc. Therefore it is necessary to figure out several means through which the relationship between the parties remains cordial.

CHAPTER 3  
INTERNATIONAL STRATEGIC ALLIANCES

A. Control of an International Strategic Alliance  
(hereafter "ISA")

Implementation of an effective ISA requires the partners to craft non-entity structures which can resolve operational and strategic control disputes as well as place limitations on the individual participant's unilateral discretion within the overall organizational design.<sup>88</sup> Thus, an ISA should be specified by means of a proper contract. Consideration should be given by the partners to factors such as which of the national laws would govern the contract in the event of a dispute between the parties as most of the ISA'S involve the joint development and production of goods.<sup>89</sup> The parties in an ISA can be bound to each other by means of the licensing of technology and/or the allocation of national distribution rights.<sup>90</sup> This enables the ISA partners to enhance cooperation and suppress the possibility of a breach of the contract.

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<sup>88</sup> Jefferey Atik supra note 13 at 276-277.

<sup>89</sup> Id. at 291-292.

<sup>90</sup> Id. at 294.

An ISA may be between a licensor firm which might have developed its own technology. The licensee firm may be willing to provide capital and the required infrastructure in the manufacturing of the product. It may also be ready to act as the distributor of the new product.

Since an ISA is a hybrid organization,<sup>91</sup> it can be superior to an individual firm in many respects. Oliver Williamson states that firms come into existence in order to reduce transaction costs. The distinguishing aspect of the strategic alliance in comparison to the firm is that in the former strategic partners retain their identities but they subject certain transactions to a quasi hierarchical governance structure.<sup>92</sup>

#### B. The Need for an International Strategic Alliance

One of the most remarkable developments in this decade is the globalization of markets<sup>93</sup> which has created new opportunities for those corporations who can be both productive and visionary. Globalization of markets involves interdependencies among the economies of the world.

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<sup>91</sup> Id. at 283.

<sup>92</sup> Id.

<sup>93</sup> S. Tramer Causvil, The Globalization of Law, Politics & Markets 1 Ind. J. Global Legal Stud. 83. 1993. available in WESTLAW, JLR File.

Manufacturing and innovation of products is necessary for corporations to compete, and succeed in the global market.

The five important considerations in global marketing are:

1. The fluid nature of manufacturing and sourcing activities.
2. Business activity flows freely to places best equipped to perform it most economically and efficiently.
3. Competition for customers and markets has intensified significantly.
4. Contemporary corporations move throughout the world trying to lay their foundations in various industries.
5. Technology spreads freely and rapidly between markets and players.
6. Borrowing and financing activity is worldwide as well.<sup>94</sup>

Essentially, the global market necessarily implies the survival of the fittest.

Global exchange has given rise to new opportunities, new sources of know how and production inputs, new ideas or partnerships which cause synergy and new ideas of competitive advantage. For corporations to operate successfully and efficiently in this market managers must understand the rules and regulations of all governments

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<sup>94</sup> Id.

involved. They also have to be aware of the cultural idiosyncracies of the markets where they intend to do business.<sup>95</sup>

ISAs challenge lawyers to contribute to the global competitiveness of corporations by having a better understanding of the business strategy performance relationship. This requires sensitive approaches to issues such as promotion, protection of assets, customer franchise, know how creativity and corporate culture.<sup>96</sup>

By entering into an ISA participating firms gain flexibility in terms of manufacturing and sourcing of products. This flexibility enables the corporations to respond appropriately to opportunities and fluctuations in national markets. While an ISA may take a long time to materialize, once it does it can be very lucrative for the parties. However, legal agreements and contracts are insufficient for maintaining cordial relationships among the parties which is a hallmark of success.<sup>97</sup> Loose and ambidexterious arrangements are key for healthy relationships between the parties. This requires that the lawyers monitoring these strategic partnerships act continually to ensure compatibility between the parties. In

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<sup>95</sup> The corporate managers and entrepreneurs have to develop knowledge of country to country differences and also have to understand the interplay of such factors.

<sup>96</sup> Id.

<sup>97</sup> Id.

the case of ISA, most of the legal arrangements between the parties are project based. Thus, the sensitive issues for the legal professionals normally involve patents, know how and intellectual property.

Corporations form an ISA primarily to share the risks and high costs which are associated with international business ventures. By pooling their resources and core competencies the partners can create synergistic alliances for research and development, design manufacturing or marketing.<sup>98</sup> Successful international companies thrive on the basis of such network of collaborations. The job of a lawyer in the age of collaborations is to assume a proactive role in defining the parameters of successful collaboration.<sup>99</sup> The legal professional should be well prepared to structure these ventures, disclose proprietary knowledge and establish means to resolve conflicts which may arise between the parties.<sup>100</sup> Corporations today are challenged in terms of product standardization, economies of scale in manufacturing and simultaneous new market entry.<sup>101</sup> This is extremely challenging environment for lawyers as it implies a more favorable environment for harmonization of product standards, advertising, regulations and legal

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<sup>98</sup> Id.

<sup>99</sup> Id.

<sup>100</sup> Id.

<sup>101</sup> Id.

processes.<sup>102</sup> The key to succeed lies in being able to constantly produce and remain economically stable. The intention of the strategic partners should be to achieve 'world class' status. New discoveries are attempted by corporations in order to respond to new technologies, shifting buyer needs, new segments in the industry, changing input costs, new regulations being imposed by the government.

A corporation which can innovate quickly and convert the goods into tangible products will have a competitive edge over the others in the market. Globalization of markets mandates efficiency not only in the process of creative discoveries but also in the process of taking the product to the market place.<sup>103</sup> The "early mover" advantages are very important in technology intensive areas. The costs, complexities and risks associated with business ventures drive companies towards "partering" collaboration with overseas distributors or agents, contract manufacturers, trading companies, freight forwarders, and even competitors.

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<sup>102</sup> In this area the lawyer can help in promoting the laws of trade and contract.

<sup>103</sup> Id.

## CHAPTER 4

### STRATEGIC ALLIANCES IN DIFFERENT INDUSTRIES

#### A. Computers

A number of strategic alliances have emerged in the computer industry.<sup>104</sup> Alliance building now is fundamental to the way U.S. electronic companies conduct business, some eight of the ten electronic companies now have alliances, and most CEO's, are planning or negotiating new ones.<sup>105</sup> The ultimate purpose of these is not only to develop or manufacture products, but to bring them to the market at the right time in order to reap the benefits. According to Cathrene Lewis, IRM's director of Application development "we view strategic alliances as absolutely critical to our success."<sup>106</sup> "We have computers - what we don't have in

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<sup>104</sup> The 1993 Annual report of Xilinx, Inc, a silicon valley corporation has pioneered itself as the worlds leading supplier of CMOS programmable logic and development software. The title page of the annual report proclaims "The theme of the years Annual report is Strategic alliances". This report further states that "Xilinx would have been unable to have a new market in the semiconductor industry and also, would have not been in a position to grow the company over 135 million dollars in revenue in a period of eight years if it had not entered into strategic alliances.

<sup>105</sup> T.C. Compton supra note 63 at 863.

<sup>106</sup> Id. at 864.

Europe is distributors."<sup>107</sup> Obviously, powerful players intend to develop niche markets and this will result in an increase of alliances in this industry.

Strategic Alliances assume special importance as the price of developing new software has been increasing and the channels for their distribution of goods become saturated.<sup>108</sup>

There is a greater degree of collaboration and integration between the parties in a strategic alliance in comparison to a standard licensing and distribution relationships. Strategic alliances also possess a more active approach by the parties in development, marketing and distribution of a product.<sup>109</sup>

The forms of such alliances range from second sourcing through an equity investment within an option to purchase the entire business of the other party.<sup>110</sup>

The most commonly involved themes in a strategic alliance are:

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<sup>107</sup> Richard L. Hudson, Britain's GEC Takes Pan-European Tack ... Fast Growth Strategy is Popular But Risky, Wall St. J., March 9, 1990 at A12.

<sup>108</sup> Mark Radcliff supra note 55.

<sup>109</sup> The following is the list of examples of investment and distribution agreements in a strategic alliance:

1. The investment and license between Adobe Systems Inc., and Apple Computer Inc.
2. The investment and distribution arrangement between Ardent computers corporation and Kutoba Limited.
3. The investment and distribution arrangements between Metaphor Computer Systems Inc. and IBM.

<sup>110</sup> Id.

1. Distribution of a product of one party by the other party.
2. Research and Development of a product by one party and marketing and distribution of the product by the other party.
3. Joint Development of the product by the parties and distribution of the product by both of the parties.
4. Corporate Planning: Where a senior party invests in the equity of one party and receives a license for some of the parties technology.<sup>111</sup>

Big corporate giants are seeking actively for small corporate partners.

"you know the interest is high when Intel corporation and IBM. companies that did not care for start ups ... began actively seeking out smaller strategic partners."<sup>112</sup>

Strategic Alliances foster innovation which can accelerate the manufacturing of goods as well as facilitate easy and effective access to new markets.<sup>113</sup> Conversely, small corporations also better understand the need for alliances and are learning how to avoid "giving the store

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<sup>111</sup> Id.

<sup>112</sup> Udayan Gupta supra note 67 at B2.

<sup>113</sup> Sony Corporation of America has several alliances with many small time corporations. According to Ron Sommer, President of Sony corporation "the more areas we want to cover, the more willing we have to be to have partners."

away" while getting growth financing and venture capital funds. By developing closer and intimate bonds with small corporations, big corporations are tapping into years of research and development.<sup>114</sup>

Strategic alliances in the computer sector is driving the entire computer industry towards the goal of complete compatibility of computer systems and more powerful applications through object oriented software and improvements in microprocessors. This will simplify the flow of business information between and within organizations, especially when paperless document technology is involved.

#### B. Strategic Alliances in the Biotechnology and Pharmaceutical Industry

Many strategic alliances have evolved between small, middle ranged and large corporations in the field of pharmaceutical and Biotechnology.<sup>115</sup> Infact, they are a

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<sup>114</sup> Dean Corley, Motorola Inc. manager of equipment R&D in Tempe, Arizona. Motorola used a computer system which was manufactured by Applied Intelligent Systems Inc. in order to inspect semiconductor chips. Mr Corley stated that they gained technology which would have been hardpressed for Motorola to gain on its own.

<sup>115</sup> Caremark International Inc. announced strategic alliances with three major pharmaceutical companies in order to have a competitive advantage in the pharmaceutical industry. Under this alliance Caremark shall work with the other drug companies with its own database to develop strategies in order to provide cost effective drug benefits to its customers. The other companies which are participating are Pfizer Inc. and Rhone Poulenc Inc. Caremark expects the arrangement to increase its 1994

dominant factor in this industry as corporations have realized that "it is cheaper than to make."<sup>116</sup> The cost of developing a drug is normally approximately two hundred and thirty one million,<sup>117</sup> but strategic alliances with smaller enterprises have materially reduced these costs.

"Small corporations are not only entrepreneurial but carry on their research in a swift, focused and decisive manner."<sup>118</sup> They also reach strategic decisions more rapidly compared to large firms. However, these gains from faster research and development aided by less bureaucracy depend upon proper negotiations which meld their respective strengths in a manner that satisfies the expectations of both parties. If not, the rations are likely to boycott an alliance when they discover the other side is not devoting proper time, commitment and resources which it may have indicated in the onset. This can result in corporations buying back their technologies.

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earnings by five cents to six cents a share. For 1993 the company has accrued profits of 77.7 million. In this arrangement the other drug companies shall have exclusive access to Caremarks prescription drug database. The alliance shall enable Caremark and other drug companies to study how different drug treatment regiments effect the health outcomes of patients and to develop protocols for the most effective use of drugs.

<sup>116</sup> Udayan Gupta supra note 67 at B2.

<sup>117</sup> Id.

<sup>118</sup> Id.

### C. Strategic Alliances in the Steel Industry

Despite a number of reforms there seems to be no improvement in the steel capacity utilization in the United States. The exit barriers, both financial and social, are extraordinarily high due to the concentration of steel employment in depressed areas where job security is especially valued and the steel workers unions have much political clout.<sup>119</sup> By forming strategic alliances and entering into technology swaps the steel companies can increase the production of their goods at a very low price and also can manufacture superior goods without additional investments.<sup>120</sup> In essence, strategic alliances in the steel industry are a smarter and profitable way to accomplish the industry's inevitable rationalization.<sup>121</sup>

Strategic alliances benefit the steel corporations in the following ways:

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<sup>119</sup> Eric G. Friberg & Marcel Genet, Forging Strategic Alliances in Steel, Wall. St. J., Feb. 7, 1985 at 30.

<sup>120</sup> With steel selling at two hundred to four hundred dollars a ton the investment cost for a new integrated plant which runs from one thousand five hundred to one thousand eight hundred a ton are too high.

<sup>121</sup> A recent example is the alliance between Brazil's Tabaroo plant which is jointly owned by Brazil's Curd, Japans Kawasaki, Italy's Fuisider and California steel. In this alliance slabs from Brazil shall be used to feed the fainting California plant which was formerly owned by Kaiser Steel. A lot of time and effort shall be saved as California Steel will not have to reopen the entire project and make huge investments in the former Kaiser facilities.

1. It lowers the prices of steel for heavy consumers of steel and auto makers.<sup>122</sup>
2. Increases the competitive strengths of the parties since there is greater supply continuity. In essence, financially sound and competitively strong suppliers can forge long term commitments to their customers and provide efficient services.
3. Fosters innovation.
4. Facilitates the passing of cost and quality improvements to end users.
5. Allows suppliers to devote more capital to new products.<sup>123</sup>

While alliances in the steel sector are somewhat risky and difficult in the beginning but can have many benefits in the long term.

#### D. Airline Industry

Strategic Alliances in the airline industry are a relatively recent phenomenon but are rapidly proliferating. They tend to focus mainly on joint marketing arrangements and the combining of tasks such as ticket processing and plane scheduling.<sup>124</sup>

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<sup>122</sup> Such as the construction industry, ship builders and the oil companies.

<sup>123</sup> Id.

<sup>124</sup> A proposed alliance between PWA, based in Colgany Alberta, and AMR Corp, parent of American Airlines.

CHAPTER 5  
LEGAL ISSUES

The legal issues raised by strategic alliances include questions of control as well as the nature and valuation of each party's contributions. The most important and sensitive issue in a strategic alliance is the protection of intellectual property.

A. Intellectual Property

Intellectual property has been described as the most acute and sensitive issue in strategic alliances. This relates to the ownership, licensing and control of the intellectual property rights.<sup>125</sup> Strategic Alliances frequently involve research and development by the newly formed strategic enterprise and the parties independently. These parties invest and contribute technology and many other resources. A successful strategic alliance should possess the assurance of global, perpetual royalty free or low costs rights to all the technology which is required for the activities of the partners.<sup>126</sup> The partners should own all the intellectual property which is developed after the

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<sup>125</sup> William Schwartz supra note 52.

<sup>126</sup> Id.

formation of the venture. This should be licensed in the name of the venture itself of all the intellectual property which has been developed by them jointly to carry out the day to day business of the enterprise.

A lot of attention should not be focussed on the ownership of patent, copyright etc. In fact, the strategic partners should concentrate more on what the business and technical staff have in mind when they think of "ownership" rights to use and commercialize the technology.<sup>127</sup>

If the parties can agree, then it shall be very easy for the lawyers to draft a combination of assignment and license provisions which shall satisfy the business objectives of the participants. The parties should also determine who shall be responsible for the protection of identifiable and patentable subject matter as well as for completing formalities with respect to copyright. The parties should take precautions for safeguarding patentable subject matter and should determine royalties and damages from infringes in the event of a material breach.

The intellectual property which relates to the business of the strategic alliance should belong to the entity only. There should be a focus on what intellectual property means in the context of a strategic alliance and the rights which

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<sup>127</sup> Id.

the participants want with respect to intellectual property.<sup>128</sup>

## B. Type of Entity

A number of issues are involved in dealing with the types of entities which are involved in constructing a strategic alliance. The most important are:

1. Tax: The strategic partners should be extremely careful in creating a partnership for tax purposes in what the parties otherwise intend as a contractual venture.

2. Security: The parties should take proper precautions to effectively safeguard each of their assets.

3. Securities Law: Securities issues can be implicated, both in terms of potential regulations as well as antitrust issues.

4. Human Resource and Personal Law: In these forms of transactions, difficult issues in these areas are likely to arise.

5. Cross Border Issues: The types of issues which may involve borders are transborder data flow and related data protection, foreign ownership restrictions, Technology Transfer Laws, customs regulations and export controls, tax treaties and other related issues, currency and foreign exchange issues, trade groupings and the other trends in

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<sup>128</sup> Id.

this area, political risks issues, government subsidies and other benefits.

6. Dispute Resolution: These are the most sensitive and delicate issues. These issues can be better addressed up front rather than when the issues arise resulting in straining the relationship between the parties.<sup>129</sup>

The role of a lawyer in assessing, structuring negotiating and implementing strategic alliances is to act as a facilitator, guide, architect, advisor, interpreter, technician and mechanic in support of the business people and their objectives.<sup>130</sup>

Creating a successful strategic alliance is like choosing a right partner for a marriage.<sup>131</sup> Therefore the selection of proper parties is the key factor while entering into a strategic alliance. As far as possible a strategic alliance should be between parties who possess a similar culture and personality. There should also be a proper balance of the contribution of the parties. The ultimate success of the venture is dependant upon the trust between the parties and their compatibility with each other.

The relationship between the parties should neither be too tight nor should it be extremely loose as this will

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<sup>129</sup> Douglas Scriver supra note 1.

<sup>130</sup> Id.

<sup>131</sup> Id.

enable the parties to loose focus on commitment.<sup>132</sup> The agreements and other incidental and ancillary documents should be well planned, negotiated and drafted. The agreement should clearly define the objective of the parties and the responsibilities and the role to be played by each of the strategic partners. The parties should also have an escalation and dispute resolution agreement.<sup>133</sup>

A proper planning and negotiating system shall help the parties to develop trust and confidence in each other. This would serve as a catalyst as it shall strengthen the relationship between the parties and avoid future disputes.

### C. The Role of the Lawyer

The challenge for the lawyer who forms a strategic alliance is to properly evaluate the strengths and desires of the parties. The lawyer must develop an understanding of the product, the development process and the third party agreements and relationships which are related to the development and distribution of the product.<sup>134</sup>

Accordingly, the lawyer must structure the relationship on the basis of clear legal principles and insist the parties consider the following steps:

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<sup>132</sup> Id.

<sup>133</sup> A mandatory internal escalation of disputes often has the beneficial effect of keeping issues of lower levels rather than escalating them to the point where they can be divisive "points of principle" separating the entities.

<sup>134</sup> Mark Radcliff supra note 55.

1. The parties should be clear over the objectives which they intend to achieve from the strategic alliance. A lawyer can be helpful in this regard, but he should be careful in understanding the objectives and limits of the clients.
2. An appropriate level of the management should be present while entering into a strategic alliance. This is very important as these alliances require the attention of senior level officers rather than those agreements which typically deal with the distribution or licensing agreements.
3. A pre-negotiation session should be held between the parties before the formation of a strategic alliance. This will enable the parties to know each's intentions, desires, likes, dislikes and goals which the parties intend to achieve.
4. As a strategic alliance will involve a joint effort by the parties, the parties should not have a win or loose attitude. The cooperation, integrity and mutual respect for each other is very important as the parties shall be working together for a long time. If the negotiations between the parties are properly established then the parties should view each other as partners and not as competitors or adversaries.<sup>135</sup> Before the

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<sup>135</sup> Id.

purchase the entity either through a bidding process or a buy or sell option.<sup>138</sup>

D. Legal Issues Involved in the Management of the Alliance

Especially in large projects the lawyer should suggest the parties recruit independent management which is not associated with any of the parties. Another simple remedy would be to have one party manage the entity under a management contract.<sup>139</sup>

The lawyer should consider the structure of the alliance and the effect it shall have on the managers. The corporate directors and managers will have a duty of loyalty towards the corporation and not towards the parties especially where the alliance is structured.<sup>140</sup> The profits of the parties should preferably be distributed by means of dividends. It can also be shared by means of royalties or through the sales of the product to the entity or through the royalties on the technology licenses.<sup>141</sup>

The lawyer should consider sensitive issues such as dissolution. The rights and liabilities of the parties

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<sup>138</sup> Id.

<sup>139</sup> Id.

<sup>140</sup> This duty might prove to be particularly awkward due to the corporate opportunity doctrine in which the officer or the director will have a duty to present the opportunity first to the "alliance corporation" instead of to the party whom he is employed with.

<sup>141</sup> Id.

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<sup>138</sup> Id.

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<sup>141</sup> Id.

should properly addressed in the event of dissolution. The attorney should take into consideration crucial issues such as the rights of each of the parties to the technology which has been developed and is owned by the entity. He should also consider the responsibilities of the parties such as paying off the entity's current and future obligations. If these issues are not dealt properly then the parties may find themselves to be the joint owners of the technology. This can inevitably lead to the disadvantage of joint ownership. In such an instance, the party which is ready to accept responsibility for the entity's liability should be made the owner of the technology and the other party should have perpetual, non exclusive and non transferable license to own the technology.

The party which has a major share in the alliance may require special voting provisions such as 3/4th majority instead of a simple majority especially in deciding issues such as mergers or sale of assets.<sup>142</sup> The agreement should clearly specify the rights of each of the parties in deciding such issues.

If one of the parties has a major investment in the alliance it may wish to have a representative on the other parties board of directors of the decisions of the other

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<sup>142</sup> Id.

party. A proper solution would be to have a voting agreement with the share holders.<sup>143</sup>

If any of the shareholders intend to sell the stock, the party which has a major share should be given preference to purchase its stock at the same price.

E. Legal Issues to be Considered by the Parties Before Entering into a Strategic Alliance

The strategic alliance should begin with a proposal from the client.<sup>144</sup> The client should determine his needs properly. He should inform the manufacturers of the time and money he is ready to contribute for the product. One of the manufacturers should assume the role of a prime manufacturer having the overall responsibility of the project.<sup>145</sup> The prime manufacturer should forward the proposal to the other manufacturers. Those manufacturers who express their willingness to join the project should forward their proposal which precisely indicates the duties and responsibilities which they are ready and willing to perform.<sup>146</sup> It is at this stage of the transaction a horizontal relationship shall be developed between the

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<sup>143</sup> Id.

<sup>144</sup> Mark Gordon supra note 58.

<sup>145</sup> Id.

<sup>146</sup> Such as technical requirements, pricing and other business conditions should be included by the manufacturers in their proposal to the prime manufacturer.

manufacturers on the basis of compatibility, performance and the capability of joining the project.<sup>147</sup> The agreement should then address pricing, payment terms, warranties and time factors.

There should be a clear understanding between the parties regarding the protection of intellectual property rights and confidential information which shall be circulated between the parties. Concern also should be expressed regarding the protection of intellectual property rights in the future.

In the field of computers, especially, the manufacturers may have to provide the client with proprietary information or other confidential information.<sup>148</sup> In order to protect and safeguard the interests of the manufacturers from exploitation of confidential information, appropriate confidentiality agreements, including restrictions should be entered between the parties.<sup>149</sup>

After the proposal is accepted by the client and the manufacturers, the parties should enter into a draft agreement.<sup>150</sup> The draft agreement is useful specially in

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<sup>147</sup> Id.

<sup>148</sup> Id.

<sup>149</sup> Both during and after any stage of the relationship should be executed by the parties who receive the access.

<sup>150</sup> This draft agreement should specify the relationship, purpose, role to be played by each party and the schedule of payments etc.

case of complex transactions since it enables the parties to resolve their differences. The parties can then have consistent expectations regarding the nature of the project and its terms and conditions.<sup>151</sup> The draft agreement should be comprised of the business, technical and legal points which have been discussed between the parties. In a horizontal structure between the client and the manufacturer, the draft agreement will focus on the products and services which will be developed and the role which will be played by all the parties to the alliance.<sup>152</sup> Only if these issues are amicably resolved should the parties enter into drafting a final and binding agreement.<sup>153</sup>

After the project is implemented, it is likely that the process and specifications may change.<sup>154</sup> These are more likely in case of long term projects.<sup>155</sup> These changes may be the result of recent developments in the technology, changes due to market fluctuations or due to the needs of the client. A special provision should be drafted for implementing these changes. There should also be a replacement provision for change of old technology by modern technology.

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<sup>151</sup> Id.

<sup>152</sup> Id.

<sup>153</sup> Id.

<sup>154</sup> Mark Gordon supra note 58.

<sup>155</sup> E.g., specification of the system, increase in the wages of the staff members and the price of the product.

After the manufacturers are ready with the system for installation at the clients premises, the client may wish to have a trial or demonstration session for testing the system for future use.<sup>156</sup> During the demonstration the client and his staff who are capable of evaluating the system should be present. In order to secure the interest of the manufacturers, the lawyers should draft a special clause to prevent the clients from bargaining since a refusal by the client after using the system for some time will undoubtedly pose major problems for the manufacturers. This clause should also provide for compensation to the manufacturers in an event of non acceptance of the system by the client. This clause should be unambiguous and should contain detailed acceptance criteria in order to minimize the possibility of dispute between the parties to the contract. The prime manufacturer should deal with these issues on behalf of the other manufacturers with the client.

The contract between the parties should include a provision for the warrantet of the system. This is very important especially in strategic alliances involving the manufacture of complex systems. The nature and duration of the warrantee should be specifically defined in the contract. In a horizontal setting between the manufacturers and the client, the prime manufacturer should be held

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<sup>156</sup> Mark Gordon supra note 58.

responsible for the warrantee of the entire project.<sup>157</sup> The period of warrantee should be specifically mentioned in the contract. The lawyers should see that the warrantee provision includes specific statements pertinent to the interoperability of the different parts of the system.<sup>158</sup>

The failure of one of the systems can have an adverse effect on the entire functioning of the project. The clients should be given an assurance of the interoperability of the system. A specific time limitation should be given to the prime manufacturer to remodify the defect. If the prime manufacturer fails to remedy the defect within the stipulated time then compensation should be provided to the client for the delay.<sup>159</sup> The defective component should be immediately repaired by the prime manufacturer. If it is found that the component does not perform properly then it should be replaced by a new system.<sup>160</sup>

Similarly, there might be certain systems or programs which might have been specifically manufactured by the prime manufacturer for the purpose of the client. The ownership and proprietary rights of these programs is very sensitive to the prime manufacturer. The terms and conditions of the ownership should be mentioned in the contract. To safeguard

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<sup>157</sup> Mark Gordon supra note 58.

<sup>158</sup> Id.

<sup>159</sup> Id.

<sup>160</sup> Id.

the interests of the manufacturers the client can be provided a license by the prime manufacturer for using these programs.<sup>161</sup> These contracts are very frequently found in strategic alliances where the client needs the system for his internal use. The client has a limited license and right to use the system of the manufacturer. The scope of the client's right is restricted to use the technology in that particular form only even if the intention of the client is to diversify in some other business.

There can also be a co-ownership between the manufacturer and the client.<sup>162</sup> In this type of a setting both of the parties enjoy complete ownership rights and can use the product in any manner irrespective of whether such type of use was contemplated by the parties.<sup>163</sup> In these relationships one of the parties mostly concentrates on the marketing of the product. The structure of the final product depends on the goals of the parties.

Sometimes, the client may have to reveal all of his confidential information to the manufacturers so that the manufacturer can develop the product to the expectations of the client. The information forwarded may be very sensitive such as mode of operations, nature of doing business, and

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<sup>161</sup> Id.

<sup>162</sup> Id.

<sup>163</sup> Id.

research and development.<sup>164</sup> The lawyer should draft appropriate provisions in this regard to safeguard the interests of the clients. Similarly, the manufacturers may possess instruments of open architecture as opposed to closed architecture. The agreement between the parties must provide for protection to all the parties. It should clearly define the nature of the confidential information to be protected and its usage. There should also be special agreements between the prime manufacturer and other sub manufacturers since in the manufacturing process the sub manufacturers may have to reveal their information to the prime manufacturer. In order to avoid the exploitation of the proprietary information of the sub manufacturers a separate agreement should be entered between the prime manufacturers and other manufacturers.<sup>165</sup> The client should pay a portion of the price at the time of delivery of the product and the rest of the money should be paid in installments during and after the acceptance period.<sup>166</sup>

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<sup>164</sup> Id.

<sup>165</sup> Id.

<sup>166</sup> Id.

F. The Different Types of Research and Development Agreements in a Strategic Alliance

A research and development agreement<sup>167</sup> may include the following areas:

1. Licensing Agreement: A legal permission is granted to utilize patents or proprietary technology for an up front fee or for royalties.

2. Cross Licensing agreements: This relationship involves two or more corporations which give legal permission to use each others patents or proprietary technology.

3. Technology Exchange: This may involve an exchange or a swap of proprietary technology. Money may or may not be involved in such transactions.

4. Visitation and Research Participation: The dispatch of researchers who visit, observe and participate in the research and development activities of the other partner firms.

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<sup>167</sup> A leading example of a strategic alliance in research and development is the alliance between Glaxo Inc, and Amylin Pharmaceutical Inc. In october 1991, Glaxo paid Amylin one million dollars and also loaned it an additional two million to develop and commercialize Amylin's blockage therapy which is intended to block the production of a pancreatic hormone to provide treatment for diabetics. Glaxo agreed to put 35 scientists to work on the research and development team and invest two hundred thousand dollars in Amylin's common stock. If Amylin develops the product then Glaxo shall possess the right to sell the product and pay royalty to Amylin Inc.

5. Personal Exchange: An ongoing and reciprocal program in which researchers from one company spend time working in another company.

6. Joint Development: Two corporations join with each other to develop a new product or technology.

7. Technology Acquisition Agreements: Investments are made in foreign companies to gain access to technology.<sup>168</sup>

#### G. The Different Types of Manufacturing Alliances in a Strategic Alliance

1. Original Equipment Manufacturing: In this type of relationship one company manufactures a product for another company which sticks its label on it and handles all aspects of business activities, including marketing and servicing as if it had manufactured the product.

2. Second Sourcing: It is an arrangement whereby one company is given the permission to manufacture a product which is designed and developed by another company as a second source supply for customers using the same specifications.

3. Fabrication Agreements: In this type of arrangement one company uses another company's fabrication facilities to manufacture products as the other partner

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<sup>168</sup> Committee on Japan office of Japan Affairs, U.S. Japan Strategic Alliances in the Semiconductor Industry: Technology Transfer, Competition, and Public Policy at 10. (1992).

lacks manufacturing facilities or intends to subcontract out the task of fabrication.

4. Assembly and Testing Agreements: The components and parts which are manufactured are sent elsewhere to another company where they are assembled and tested.

5. Procurement Agreements: A commitment is made by a party to purchase certain quantities of specified goods or services over a specified period of time.

6. Sales Agency Agreement: Exclusive or non exclusive rights to sell the partner's original product or products to which the value is added, in specified markets.

7. Servicing Contracts: The provision of follow up service in foreign markets which is very often tied to marketing arrangements.

8. General Purpose Tie Ups: This is an agreement on common or compatible technical standards which links devices and systems and users of different machines.<sup>169</sup>

#### H. The Antitrust Concern in Strategic Alliances

There has been a lot of ink spilt on the fear of antitrust regulations while corporations enter into strategic alliances. This is due to the imposition of stringent antitrust regulations. In order to facilitate cooperation between the corporations the government has passed "The National Cooperative Act of 1984" (NCRA). The

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<sup>169</sup> Id. at 10.

purpose of NCRA is to promote research and development of products by companies and to encourage innovation and stimulate trade.<sup>170</sup> Under this act those corporations which engage in joint research and development and are registered with the government, are free from being declared illegal. If a corporation is held liable for antitrust violations, the defendants become responsible for only actual rather than treble damages.<sup>171</sup> If the claim is found to be false, frivolous or mischievous then the parties can recover attorneys fees. Thus, the NCRA is a good step towards enhancing cooperation between companies. Unfortunately, it excludes production, marketing and joint research developments.<sup>172</sup>

Corporations have developed a number of misconceptions over the issue of Antitrust while entering into strategic alliances. It is misconception to state that strategic alliances shall decrease the competition. In fact, competition is more likely to be strengthened by alliances rather than weakened. In case of International Alliances, domestic competition will increase. Strategic alliances between two companies not competing today that give both

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<sup>170</sup> Maria Sendra, Strategic Alliances for the Innovation in the Global Market of the 1990's: A Comparative Study of the Relationship Between Innovation and the Patent/Antitrust Mechanisms of United States and the European Economic Community. 9 Int'l Tax & Bus. Law. at 387 (1992).

<sup>171</sup> Id.

<sup>172</sup> Id.

concerns access to more modern, productive facilities can lead only to lower costs and more aggressive competition.<sup>173</sup> And also, domestic alliances shall lead to more competition which shall result in giving better financial stability.

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<sup>173</sup> Eric G. Friberg & Marcel Genet supra note 119 at 30.

## CHAPTER 6

### CONCLUSION

The 1990's will encompass a rapid increase in strategic alliances as major corporations 'Petestroika' i.e. restructuring of costs. Currently, they seem to be the best means for decreasing transaction costs and an enhancing risk sharing. In essence, clustered relationships help parties to access the core competencies<sup>174</sup> of one another. For example, corporations enjoy especially good profits if their products are introduced into appropriate markets at an early stage. Through a joint research and development program under a strategic alliance products can be produced in large quantities in a short time to support such entry.

An alliance should last as long as it serves the purposes of the parties.<sup>175</sup> There should always be proper negotiations before its commencement. If the parties realize that serious injury may arise from its premature termination, they should not fully commit to it. However, there are great pressures on U.S. international corporations to enter such alliances, especially with Asian counterparts

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<sup>174</sup> Douglas. Scriver supra note 1.

<sup>175</sup> Udayan Gupta supra note 67 at B2.

This is entirely dependant on the project. it may involve a number of months, years, days etc.

to keep abreast of their other international competitors since by forging such alliances they can keep the other competitors busy in their own pond.<sup>176</sup> The joint efforts of U.S. and Asian companies also help the U.S. partner cope with production inadequacies since many Asian companies are strong where the U.S. companies are weak.<sup>177</sup> Moreover, the U.S. corporations can learn new and easy means for developing high tech products by making investments as well as acquire export platforms to other countries.<sup>178</sup> Thus, strategic alliances with clearly defined objectives shall be a hallmark in the future.

To be competitive internationally corporations must join networks of international coalitions and must also learn how to manage them.<sup>179</sup> Every corporation must develop a certain number of senior managers who combine know how of the other company with the ability to work with foreign partners who have different goals and a different culture.<sup>180</sup> It shall be an asset if senior managers are

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<sup>176</sup> William Taylor Stop Playing 'Catch Up' with the Japanese Wall St. J. March 3, 1992 at A12.

<sup>177</sup> Especially in the high quantity mass production of sophisticated consumer and industrial goods.

<sup>178</sup> AT&T has made surplus profits by collaborating with Korea's Goldstar in building Telecommunications switches, fibre optics and transmission equipment.

<sup>179</sup> Daniel A. Sharp, Manager's Journal: Combat Protectionism with Global Alliances, Wall St. J., June 1, 1987 at 35.

<sup>180</sup> Id.

trained to learn the native language of the foreign corporation. This fosters increased cultural empathy between the parties.

By being competitive globally through strategic alliances, a nation can preserve jobs and also contribute increased competitiveness at home. Researchers believe that American corporations have been more successful and competitive globally rather than at home.<sup>181</sup> By developing closer ties with various business and financial partners around the world, trade barriers can be alleviated and mutual trust enhanced. Ultimately, this will facilitate the new U.S. responsibility for "leadership" management of the world economy,<sup>182</sup> while improving the competitiveness of its corporations in world markets.

The future importance of International Strategic Alliances will depend upon major revisions in the structure of U.S. governance of its corporate citizens. Reforms in the following areas are especially important.

1. The Antitrust laws need to be relaxed to facilitate such collaborations.
2. The tax laws should be revised to encourage employees to work for new strategic partnerships.
3. Taxation of such alliances should be equitable and predictable.

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<sup>181</sup> Id.

<sup>182</sup> Id.

4. The national government should think along a horizontal dimension rather than a vertical dimension when making future decisions about taxation, antitrust, industrial, economic and other policies.<sup>183</sup>

Lawyers must play a critical role in shaping the efficiency and effectiveness of such alliances. They must work with the management professionals as a team in resolving critical issues<sup>184</sup> as well as guiding and shaping the future course of the alliance relationship, especially as regards global procurement and the coordination of manufacturing and marketing operations. In essence, the lawyer must be merged and joined in the prime activities of the alliance and they must learn better how to be progressive players.<sup>185</sup> High esteem will surely follow their successful efforts in this regard.

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<sup>183</sup> Id.

<sup>184</sup> S. Tramer Causvil supra note 93.

<sup>185</sup> Id.



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