

Agreements should be phrased unambiguously

Possible risks and side effects of joint ventures

By Dr. Johannes Weisser

Tapping into the tremendous potential of the Indian market is much easier with a partner who has profound knowledge of the local market and is well connected there than going it alone.

Where such cooperation is carried on a purely contractual basis and no strategic know-how is involved, the risks associated with such type of cooperation is fairly limited and easy to manage. However, the Indian partner will sometimes ask not only for the supply of technology and know-how, but also for an equity participation in the Indian subsidiary. In this case we are talking about a joint venture. Such a form of cooperation can be quite advantageous for both sides, as is impressively illustrated by the report on the Indian joint venture entered into by Gehrlicher Solar AG, published in this issue of GermanyContact India, page 15 et seq. But in any case, joint ventures should be planned and managed very thoroughly because some bad surprises may lurk along the way. One German

company recently had such a painful experience.

The Enercon case

To date, India has, unlike other developing countries, not been a source of major concerns with regard to the protection of intellectual property rights (IPR). Indeed, this was a major advantage in attracting foreign direct investment. A case decided recently by an Indian patent authority has, however, cast some doubts on this assessment. What had happened?

Enercon GmbH, a German manufacturer of wind power generation equipment, holding a 56 percent majority interest in the joint venture Enercon India Ltd., was de facto expropriated by its Indian minority shareholder. The disputes between the partners who had initially worked together quite successfully, involve issues relating both to corporate and patent law. In addition, there is a dispute regarding the use of the Enercon name. All this resulted in Enercon having no more influence on the operations of the joint venture company irrespective of its majority interest. The dispute culminated in a series of applications filed by the joint venture company to have all patents held by Enercon in India declared invalid. Some of these applications were granted by the Intellectual Property Appellate Board (IPAB) in Chennai. According to some publications in Germany, the IPAB in its reasoning has allegedly stated, in addition to traditional reasons for voiding a patent such as lack of novelty or lack of inventive step that access to the Enercon technology would touch upon the interest of the nation and that this would prevail over the ownership interest of a private company to have its technology protected. Both lines of argument would appear to pose some problems here. However, two entirely different themes need to be distinguished.

Does India provide effective protection of IPR's?

On the one hand, there is the question why lack of novelty and inventive step

should exist only in India while these patents – according to Enercon – have been recognized in all other countries and even survived challenges to their validity elsewhere. Enercon is hoping for a convincing answer to this question from the High Court in Delhi where it has appealed against the decision of the IPAB.

On the other hand, and this is the much more crucial point, there might be the question of India's reliability as a trading partner if indeed, as claimed in the press, national interest had in fact been put above the interest of the patent holder by the IPAB. But is this really what the IPAB has decided? No such wording can be found in the decisions rendered by the IPAB, as these merely cite lack of novelty and inventive step to support the voiding of the patents. Since both elements are prerequisites for the granting of a patent, the lack of only one, albeit both elements would indeed justify the voiding of a patent in principle. It is only in an interim order issued by the IPAB in July 2010 where it is stated that in order to expedite the process of administering justice and to end the dispute between the parties which goes back to 2005 "such that these alternate sources of production of electrical energy can be tapped and utilized for the betterment of society and the public at large, either by way of upholding the patent grant or in the alternative, throwing open the same technology to the concerned industries to utilize the same in an expeditious and benevolent manner for the benefit of the industry and the public at large as well as the nation (emphasis added)." With this certainly somewhat elevated wording, the IPAB had at least initially left the door open in both directions.

Enercon cites circumstances that may cast some doubts

However, according to Enercon, there are a few other circumstances which might be regarded as suitable for casting some doubt on whether the proceedings before the IPAB were really fair. It remains to be seen whether the

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High Court in Delhi will address these issues and thus help to maintain the confidence of international investors in the effective protection of IPR's in India. Neither the Government of India nor businesses have an interest in any doubts being raised in this regard, in particular since Germany enjoys a high reputation as one of the most important sources for technology and know-how. All this is reinforced by the fact that India has in the past rightly claimed to be the "better China" in particular due to the effective protection of International Property Rights (IPR's).

Last but not least it must be borne in mind that one of the prerequisites for having the patents declared void was that the Indian partner was duly authorized to file such applications. This is a civil and corporate law issue which does not fall within the competence of the IPAB. The decision of the Company Law Board with regard to these issues is, however, still pending and it is doubtful whether this decision will be issued any time soon. This has not, however, prevented the IPAB from issuing its own decisions declaring the patents void, thus jumping ahead of the queue.

Legal framework for protecting IPR's must be used

This then raises the question as to what avenues are available to a foreign company to protect itself against such a "cold expropriation". In cases where the foreign partner contributes or licenses IPR's to a joint venture, a no-challenge clause may be considered whereby the licensee undertakes not to challenge the validity of the IPR's either directly or through affiliated enterprises. Furthermore, contractual penalties may be agreed in case of a breach of confidentiality and non-use obligations with regard to know-how which is not capable of legal protection. All such obligations should survive the termination of the agreement where possible. Such provisions have been standard clauses in international trade agreements for a long time and in principle offer sufficient protection.

Special attention is also to be devoted to the rules regarding the corporate governance of the joint venture. Thus, particular attention should be paid to the powers granted to the local management. This requires careful drafting and at least initially, some restraints, in particular with regard to the list of items requiring the consent of the foreign shareholder. Where the local management is granted special powers of attorney, these must be worded very carefully so that they

cannot be used later to the detriment of one shareholder. If there are signs of powers being abused, these must be withdrawn or curtailed immediately. This requires, however, that such information is received by the foreign shareholder in the first place. In order to ensure this, expats who have the necessary competences may be sent to work in the joint venture. This should also be agreed explicitly in the joint venture agreement.

And of course a joint venture agreement should also contain rules with regard to an orderly dissolution of the joint venture in case of a falling out among the partners. In particular call and put options with clearly defined valuation rules for the shares of the other partner are suitable mechanisms which may not avoid a conflict, but may help to solve it.

A prerequisite for all of the above mechanisms is, however, that courts are available to administer justice in an effective manner in case of a possible breach of contractual obligations. This also includes a speedy process of these cases.

Prospects for the future

Companies who are planning activities in India should check carefully whether and if so on what basis they enter into a joint venture in India. The most crucial point here is finding the right partner which requires a lot of care. Both the Indo-German Chamber of Commerce (IGCC) and the German diplomatic missions can offer support in this regard. Once a partner has been identified, due care and attention must be paid to the best possible protection with regard to the know-how involved, but also corporate governance rights with regard to the operation of the joint venture as well as clearly defined exit scenarios must be negotiated and agreed.

In addition, there is the hope that from the Indian side there will be a clear signal in appropriate form that considerations of national interest will not be used as an albeit supplementary reason to void patents and other IPR's held by a foreign entity. One opportunity to make such an unequivocal statement is now with the Delhi High Court. And provided that there is sufficient political will in this regard, this might even be cast into statute by way of an amendment of existing legislation. This would certainly be the most unequivocal signal to the international community that India is really serious about honouring its commitments with regard to the protection of IPR's which it has undertaken as a signatory of the TRIPS agreement.

What are IPRs?

Intellectual Property Rights (IPRs) are rights given to persons over the creation of their minds. They usually give the creator an exclusive right over the use of his or her creation for a certain period of time.

Intellectual property rights are customarily divided into two main areas:

Copyright and rights related to copyright

The rights of authors of literary and artistic work such as books and other writings, musical compositions, paintings, sculptures, computer programs and films are protected by copyright, for a minimum period of 50 years after the death of the author. Also protected through copyright and related rights are those of actors, singers and musicians, producers of sound recordings and broadcasting organizations. The main purpose of protection of copyright and related rights is to encourage and reward creative work.

Industrial property

These rights can usefully be divided into two main areas:

One area can be characterized as the protection of distinctive signs, in particular trademarks which distinguish the goods or services of one undertaking from those of others and geographical indications which identify a good as originating in a place where a given characteristic of the good is essentially attributable to its geographical origin.

The protection of such distinctive signs aims to stimulate and ensure fair competition and to protect consumers by enabling them to make informed choices between various goods and services. The protection may last indefinitely, provided the sign in question continues to be distinctive.

Other types of industrial property are protected primarily to stimulate innovation, design and the creation of technology. In this category fall inventions protected by patents, industrial designs and trade secrets.

The social purpose is to provide protection for the results of investment in the development of new technology, thus giving the incentive and means to finance research and development activities.

A functioning intellectual property regime should also facilitate the transfer of technology in the form of foreign direct investment, joint ventures and licensing. The protection is usually given for a finite term, typically 20 years in the case of patents. It should be noted that the exclusive rights given are generally subject to limitations and exceptions, aimed at fine-tuning the balance that has to be found between the legitimate interests of right holders and of users.

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