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Benefits for both parties

While the legal framework governing trademark licensing in India has been liberalised, brand owners should remain vigilant when drafting their agreements

Licensing presents an opportunity for brand owners to leverage their trademarks to create an additional revenue stream without having to invest in infrastructure for manufacturing or marketing the product. In many cases, this means that the brand owner can reap the benefits of its brand's popularity to venture into territories where it may not have a core presence or competencies.

A multinational corporation can have a number of reasons for wanting to license its trademarks in an emerging economy such as India. They may include the following:

- There is an investment cap in a particular sector or industry. For instance, in the insurance sector in India, a foreign company can have a maximum shareholding of 26%. As a result, the foreign entity or multinational company must enter into a licence agreement with its joint venture partner to safeguard the ownership of its brands.
- The royalty payments to a multinational company on use of the brand name by a minority or major subsidiary can be repatriated without any foreign exchange restrictions by the government
- The rights holder wants to distribute or market its trademarked products without having to manufacture them itself locally.
- The rights holder wants to understand the market and local culture and preferences through a joint venture partner or distributor before making investments in manufacturing products locally.

Two initiatives from the Indian government helped to develop trademark licensing in India. First, the amendment of the Trademarks Act in 2003 changed the definition of 'permitted use' to include use of a brand name with the consent of the brand owner by any party, provided that this is through a written agreement. This means that use of the mark by a licensee will inure to the benefit of the licensor without having to record formally the licensor as a 'registered user' under the Trademark Act. Thus, such use by a licensee can also be used as a defence against a non-use cancellation action by a third party.

Second, in 2009 the Department of Industrial Policy and Promotion (a part of the Ministry of Commerce and Industry) allowed the automatic payment of royalties for use of a trademark or brand name without any restriction on the amount. This was a key liberalisation move to attract foreign investment. Previously, the maximum royalty payments allowed on the use of trademarks or brand names was 2% for exports and 1% for domestic sales where no technology transfer was involved.

Protection of licensor's rights

Even before the expansion of the definition of 'permitted use', the Indian courts recognised the rights of brand owners – in particular, in cases where the brand owner and its joint venture partner were in conflict, which resulted in the brand owner:

- asking the licensee to stop using the mark;
- challenging the licensee's rights on expiry of the term licence agreement; or
- terminating the licence on account of violation of any condition that formed part of the licence.

The following decisions show the courts' stand on this issue.

In *Baker Hughes Limited v Hiroo Khushalani*, the Delhi High Court noted that the permission to use the mark was granted under a collaboration agreement which stipulated that the joint venture company was entitled to use the brand owner's company name as long as the latter's shareholding did not fall below 40%. Therefore, use of the mark after that company's share in the joint venture's equity fell below 40% was improper and deserved to be restrained.

In *Fedders North American v Show Line*, the court observed that the plaintiff had authorised the defendant to use the trademark FEDDERS for a period of five years, by virtue of a licence agreement. The court held that after this period came to an end, use of the mark FEDDERS by the defendant was not in line with the rights available to the plaintiff as a registered proprietor of the mark. Accordingly, the court restrained the defendant from using the mark FEDDERS.

In *Velcro Industries BV v Velcro India Ltd*, Velcro Industries had entered into a collaboration agreement with its Indian directors to create Velcro India Ltd. Under the term of a trademark licence, later renewed, the defendant was permitted to use the name 'Velcro' as part of its trade name. Upon the expiry of the trademark agreement on September 30 1986, Velcro Industries requested that the defendant stop using the name and mark VELCRO; the defendant did not comply. The Bombay High Court found that after the licence had expired, the defendant had no right to use the VELCRO mark as part of its trade name. Accordingly, it restrained the defendant from using the VELCRO mark.

Key licence elements

One of the most relevant aspects of licensing involves quality control over use of the licensed mark by a third party and the extent of such control. The absence in the licensing agreement of quality control provisions can lead to mitigation of the distinctive value attached to a particular mark. As a result, not only may the goodwill and reputation of a mark deteriorate, as the goods so marketed may become substandard over a period of time, but the owner may also lose ownership of the mark. The courts have referred to such licensing agreements as 'naked licences'. To avoid such consequences, the quality control provisions should cover:

- a right of inspection of the premises where the goods are manufactured;
- a description of the types of process used by the licensee to manufacture the licensed goods;
- for services, details of personnel training and knowledge to offer such services to customers;
- managerial controls, including defining the nature of the relationship between the parties to the licence agreement;
- approval of marketing and advertising campaigns undertaken by the licensee;
- effective mechanisms for establishing after-sales services; and
- the appearance of the trademark on product packaging, including acknowledgement of the brand owner's rights in the trademark.

The other issues that a licence agreement should address are as follows;

- a list of the licensed merchandise and how it can be sold or distributed;
- the term and territory of the licence;
- the frequency and amount of the royalty payable by the licensee and tax issues;
- each party's termination rights, as well as their rights and obligations after termination;
- the parties' respective rights and obligations if they discover infringing use of the trademarks by a third party;
- how consumer complaints and product-related regulatory issues will be handled; and
- each party's indemnification and obligations. The licensor may typically want recognition of its exclusive rights in the brand name and trade dress, while the licensee may not be allowed to deal with a competitor's products or to sub-license.

Exclusive or non- exclusive licence

Neither the Trademark Act nor the Contract Act bars non-exclusive licences. Whether an exclusive or non-exclusive licence is the best option for a brand owner will depend on the business objective, market conditions and nature of the product. It will also depend on whether the licensee is financially capable of fully exploiting an exclusive licence. As an example, a brand of Disney's stature, which involves various characters – each with distinctive elements – will require entering into non-exclusive licences. At the same time, the onus on the brand owner to maintain quality control, audit the licensees' records and keep a check on use of the licensed brand is much higher in case of a non-exclusive licensee.

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Online sale

As the digital environment gains popularity with the growing young and urban population in India, brand owners should become familiar with the issues inherent to the online sale of products bearing licensed marks. A licence agreement should clearly set out, among other things:

- whether the licensee is permitted to set up an online store;
- the domain name to be used for such store; and
- who owns the data of customers visiting the store.

Thus, an agreement should take into account the current realities, including the language used in invoices and the terms and conditions of sale, whether they are on paper or online.

Licence recordation

Recordation of the licensee as a registered user is not mandatory as the definition of 'permitted use' has been widened to include use made by an unregistered licensee. However, such recordation, if at all desired, is possible only for registered marks. The licensing of unregistered marks is possible at common law, although some aspects will be governed by the terms and conditions entered by the parties through a written licence agreement.

Summary

Trademark licensing is a key commercial tool that enables rights holders to extend the reach of its brand through third-party use without assigning any legal ownership rights to such third party. Thus, a licence can benefit both the proprietor and the licensee. That said, to avoid any misunderstanding and ambiguity, the parties must be clear about their expectations, which in turn requires a well-drafted and negotiated agreement. It is also necessary to understand local tax issues on royalty payments and those surrounding quality control. WTR