India

RNA Intellectual Property Attorneys

Opportunities abound in pro-liberalisation regime

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Generally speaking, brand owners can monetise their brand equity in two ways: by licensing the brand – that is, selling the right to commercially use or develop it to a third party – or by marketing and manufacturing the products under the brand name themselves. Both options have an impact on the level of investment necessary to roll out a venture.

Whether to licence is a decision to be taken when the brand has started to gain traction and the business is considering scaling up. For a multinational corporation, there may be a number of reasons to license its trademarks in an emerging economy such as India. For instance, there is a foreign investment cap in some sectors or industries (eg, a cap of 26% on foreign investment in the media sector). As a result, multinational corporations must enter into a licence agreement with a joint venture partner to safeguard the ownership of their brands. Alternatively, where a particular sector has recently opened up to foreign investment (eg, the defence sector), a joint venture partner or distributor can help the rights holder to understand the market and local preferences before it invests in manufacturing the products locally.

Licensing can also prove attractive where the royalty payments for use of the brand name by a minority or major subsidiary can be repatriated without any foreign exchange restrictions. Likewise, the rights holder may wish to distribute or market its trademarked products without having to manufacture them locally itself. Or it may have in mind a potential licensor with a proven track record for distributing products which also has the necessary infrastructure in place.

Licensing objectives

Goal setting in a licensing scenario is crucial. Businesses should clearly define the objectives of licensing in order to work out the terms. Some of the issues to consider include:

- the territory in which the licensee may use the trademark and whether this also extends to online sales;
- the duration of the licence;
- whether the licence is exclusive or non-exclusive;
- whether the licensee is permitted to sub-license;
- quality control over use of the licensed mark by the rights holder or licensor and the degree of such control;
- the specific merchandise to be licensed and how it can be sold or distributed;
- the frequency and amount of royalty payments by the licensee and tax issues;
- the termination rights of each party and their rights and obligations after termination;
- how consumer complaints and product-related regulatory issues will be handled; and
- indemnification clauses and the respective obligations of the licensor and licensee.

Quality control of licensed goods

A crucial aspect of licensing involves quality control over use of the licensed mark by the licensee and the degree of such control. The quality must be equal to the quality of the licensor's own goods and services. Exercising quality control can also be a good business practice for maintaining a high level of goodwill in the brand. As a part of the quality control process, licence agreements should provide for the following:

- a right of inspection of the premises where the goods are manufactured;
- a description of the processes used by the licensee to manufacture the licensed goods;
- details of how the trademark should appear on the product's packaging, including acknowledgement of the brand;
- 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 colour schemes and size of packaging, labels, signs, advertising and marketing materials, artwork, plans and other materials for approval.

Case law on quality control

In *Gujarat Bottling Company Ltd v Coca-Cola Company* (AIR 1995 SC 2372) it was held that the licensing of a trademark is governed by common law, which is also statutorily permissible, provided that the licensing does not cause confusion or deceive the public and does not destroy the mark's distinctiveness, and that a connection in the course of trade continues to exist between the goods and the rights holder.

Licensing issues in the online world

As the digital environment gains popularity with India's growing young and urban population, rights holders should stay abreast of the issues surrounding the online sale of products bearing licensed marks. A licence agreement should clearly specify, among other things, whether the licensee is permitted to sell online, the domain name to be used for such sales, if allowed, and who owns the data of customers visiting the website.

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

Royalty payments for use of brand names

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

Many multinationals have taken advantage of the newly liberalised regime; royalty payments have increased by 57.43% in the space of four years. Maruti Suzuki, Hindustan Unilever, Nestlé India, Bosch and ABB India have remitted the highest amount of royalties to their parent companies.

Royalties paid by Indian subsidiaries to foreign parent companies have also been attracting attention. Royalty payments have become the largest source of earnings for multinationals operating in India. For now, the government does not intend to change the rules or impose any caps on royalty payments, in order to maintain its liberal image and continue to attract foreign investment.

Protecting licensors' rights

The current definition of 'licensed use' or 'permitted use' refers to 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 the licensee having to be formally recorded as a 'registered user' under the Trademarks Act, 1999. Such use by a licensee can also be a defence against a non-use cancellation action by a third party. Even before the expansion of the definition of 'permitted use' in 2003, the Indian courts recognised the rights of brand owners – in particular, in cases where the licensor and licensee were in conflict which resulted in:

- the licensor asking the licensee to stop using the mark;
- the licensor challenging the licensee's rights on the expiry of the licence agreement; or
- the licensor terminating the licence as a result of violation of conditions that formed part of the licence.

In *Baker Hughes Limited v Hiroo Khushalani* the Delhi High Court noted that 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 the 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 had expired, use of the FEDDERS mark 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 terms of the trademark licence, later renewed, the defendant was permitted to use the name Velcro as part of its trade name. Upon the trademark agreement's expiry on September 30 1986, Velcro Industries requested that the defendant stop using the name and the VELCRO mark; 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.

Conclusion

Licensing is a potentially lucrative business model which provides rights holders with the opportunity to increase the geographical reach of their brands and to maximise their revenues. The Indian licensing regime is liberal both in terms of royalty payments and in that it imposes no obligation to record the licence, so long as both parties have set out their understanding or terms of agreement in writing. Success relies principally on the parties' mutual trust and the revenues involved. However, when things go wrong, the clarity of terms and established limits, as set out in the agreement, will be the key to dealing with any conflicts. **WTR**

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