
Tax centric interpretation of Intellectual Property

In an interesting case involving transfer of Intellectual property between two entities located outside India where the trademarks were owned by an Australian company but used in India, the Delhi High court in an Appeal from Authority of Advance Ruling (AAR) has held that such transaction is not taxable in India.

Facts of the case

The petitioner - CUB Pty. Limited (CUB), formerly known as Foster's Australia Limited entered into a brand license agreement (BLA) with Foster's India Limited by virtue of which Foster's India was licensed to use certain registered trademarks of the Petitioner in India. However, the ownership of marks remained with CUB.

CUB entered into a Sale Purchase Agreement (which was a composite agreement) with SAB Miller (SAB). The agreement apart from sale of shares included sale of a) trade marks (b) Foster's Brand Intellectual Property and (c) the grant of exclusive and perpetual licence in relation to Foster's Brewing Intellectual Property, confined to the territory of India. The termination of the BLA with Foster's India Limited and the execution of the Sale Purchase Agreement took place on the same day.

CUB sought an advance ruling from the Authority of Advance Rulings (AAR) on the following issue:

Whether the income arising out of the transfers made to SAB Miller was taxable in India?

According to Section 9(1)(i) of the Income Tax Act, income arising from the transfer of a capital asset situated in India is taxable in India.

Primary Issue for consideration

Whether the intellectual property rights that were sought to be transferred could be said to be situated in India? If yes, then whether the applicant could contend that the tax should be computed based on the consideration as per the independent valuation obtained by the applicant.

Contentions of the parties

CUB contended that the intellectual property rights could not be said to be situated in India due to the reasons given below:

1. No assignment of any proprietary interest in the trademarks took place. Moreover, the trademarks were originally adopted by CUB in Australia. Hence, the situs of those rights was clearly Australia.
2. If the contention that the grant of license results in transfer of the situs of the trademark to the licensee countries were to be accepted, it would result in multiple taxation.

3. The trade mark exists independent of its registration. The statute merely fortifies the common law. Thus, registrations in India cannot result in the trademarks being 'situated' in India
4. The location of a trademark is governed by the common law maxim of '*mobilia sequuntur personam*', according to which the personal property held by a person is governed by the same laws that govern that person. The maxim operates in absence of a contrary statutory provision. Since, the Income Tax Act has not provided for the situs of trademarks, the said maxim would be applicable.
5. Since, the BLA was terminated before the transactions listed in the Sale Purchase agreement could be completed. Thus, exclusive rights over trademarks vested back with the CUB situated in Melbourne, Australia.
6. Since, both the asset and the place of contract were outside India, therefore, the transaction could not be taxed under the Indian Income-tax Act.

Contentions of the Income Tax Department (ITD)

ITD contended that the capital asset was situated in India, therefore, the transaction was taxable in India. The contentions are outlined below:

1. When the Foster's brand was initially introduced in India, it had no value. However, when the petitioner sold the trademark and the brand intellectual property rights with respect to the territory of India, substantial proceeds were received by them from SAB. This clearly represents the value it had gained from its operations in India. Thus, the income accrued in India.
2. The termination of the BLA took place after the Sale Purchase Agreement was executed.
3. Since, the sale of shares was integrally connected to the transfer of intellectual property rights, the transaction came under the ambit of Section 9 (1)(i) of the Income Tax Act.
4. The question of apportionment of liability as was reasonably attributable to India did not arise since whole of business in India was transferred and the entire consideration had to be taxed in India only.
5. There was a fallacy in the maxim, '*mobilia sequuntur personam*' as it was not possible that every time the Parent company would change its location, the situs of the capital assets would also change.

Observations and decision of the Authority of Advance Rulings(AAR)

1. Once it is clear that the asset is situated in India, the place of execution of the contract is immaterial. Relying on Section 55(2) of the Income Tax Act, AAR pointed out that it is clear that the goodwill, trade-marks or brand name associated with a business and other incorporeal rights are treated as capital assets under the Act.

2. AAR rejected the Applicant's contention that the situs of the intellectual property was said to be present where the owner was domiciled.
3. Placing reliance on the various trade mark registrations and the BLA, wherein it was stated that the Foster's India had to take due efforts for promotion of the brand, the Authority observed Foster's brand had undoubtedly generated goodwill in Indian market which was nurtured in India by reason of efforts Foster's India. Thus, intellectual property belonging to the applicant had its "tangible presence" in India. Now, as a result of the transfer the property would be enjoyed by SAB Miller, instead of Foster's India. However, the situs of the assets did not shift.
4. As the BLA and the Sale Purchase Agreements were terminated and entered into simultaneously, the question of the rights reverting back did not arise.
5. AAR thus concluded that the situs of the assets was located in India.

CUB appealed the decision to the Delhi High Court

The High Court overturned the decision of the AAR and observed that the legislature did not provide for the determination of situs of intellectual property rights as it had done for shares. Thus, in absence of any specific provisions dealing with situs of intellectual property rights, the maxim , '*mobilis sequuntur personam*' would have to be followed until a change in the law was brought out by the legislature.

Our comment

While it is true that the trade mark exists independent of its registration, the statute merely fortifies the common law rights that exist independent of registration. However, use of a brand name locally and promotion efforts by a local subsidiary do enhance its value and therefore result in appreciation of capital asset in a specific jurisdiction. Further, a trademark can be divided and sold to different owners in each country. It can also be licensed and royalties earned by the proprietor are specific to the territory. This goes to show territorial nature of the trademark rights. Thus, to say situs of intellectual property is to be present where the owner was domiciled seems tax centric interpretation of the Intellectual property.

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