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HONGFANGLAW LEGAL & IP

How to Make the Best Use of Your Licensing Agreement in China?

Jenny Liao & Eric Su

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As one of the leading focused practice, the team was founded with professionals dedicating to intellectual property practice for over 20 years since late 1990s.

We keep our commitment to clients and stakeholders as the top priority, and with the high standard service quality, we devote ourselves to the best tailor-made solutions to clients.

We are proud of practicing in IP industry, with our professionalism and passion.

“WE DO IP
RIGHT.”

ACQUISITION

PROTECTION

SOLUTION

We are focusing on legal solutions for intellectual property matters as our key practice, and assisting clients with other legal issues derivatively, mainly as below:

Trademark acquisition (incl. filing, opposition, invalidation, etc.)

Patent acquisition (incl. application and maintenance, etc.)

Domain name acquisition and arbitration

Administrative and criminal prosecution

Customs recordation and prosecution

Legal risk assessment and advice

Administrative and civil litigation

Licensing & transaction support

Contracts and advertisement

Copyright registration

Online delisting

Data-analyzing





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Tax Implication of Licensing Agreement

Jenny Liao

Senior Manager Corporate Accounting & Tax

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1. Introduction



Introduction - Royalties

General Definition

Royalties are fees paid in relation to the use of intellectual property, such as trademarks, patents, copyrights, and proprietary technology



Introduction - Royalties

China Customs Regulation	China Tax Law	
	Corporate Income Tax	Double Taxation Agreements
<p>“Royalties” shall mean fees paid by the buyer of imports to an intellectual property rights holder or persons duly authorized by the rights holder for licensing or transfer of patent rights, trademark rights, proprietary technologies, copyrights, distribution rights, or selling rights;</p>	<p>Income from royalties referred to derived by an enterprise through provision of the right of use of patent rights, non-patented technologies, trademark rights, copyright and any other concession rights.</p>	<p>Where the definition of royalties under a Double Taxation Agreement expressly includes the amounts collected for use of industrial, commercial and scientific, the provisions of royalties clauses under the Double Taxation Agreement shall apply to the relevant royalty income.</p>

Introduction - Royalties

General tax implications

- Foreign enterprises without establishments or places of business in China shall be subject to a unilateral concessionary rate of withholding tax of 10% on gross income from royalties; certain countries and regions apply relatively lower rates.
- Royalty remittances are also subject to 6% VAT.

Introduction - Royalties

General tax implications

- According to Customs, royalties are subject to the following duties if they are related to imported goods which are due to be sold in China:
 - A. Customs duty (tariff rate depends on the HS code and place of origin)
 - B. VAT (9% OR 13%) and/or consumption tax
- Royalties should be deductible for CIT purposes provided they are directly related to the FIE's business operations and charged at normal market rates

Introduction - Royalties

Withholding Tax Comparison of DTA Tax Rates under Royalty

Countries and Regions	Rate
USA DTA (1987)	10%
Germany DTA (2017)	10%
Luxemburg (1996)	10%
Hong Kong (2007)	7%
Singapore (2008)	10%

Introduction - Royalties

Example: Outbound Royalty Payment (Tax calculation)

RMB

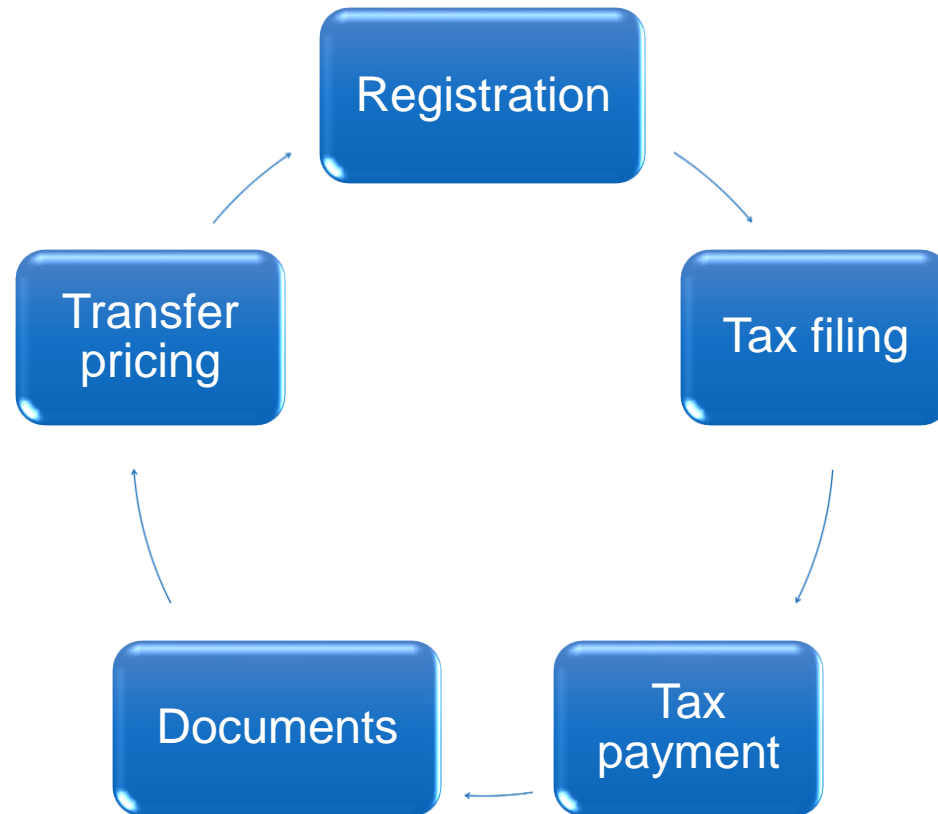
Item	Formula	Amount	Final %
Royalty Fee	(1)	1,000,000	100
Withholding Tax	(2) = (1) / (1+6%) * 10%	94,340	9.4
VAT	(3) = (1) / (1 + 6%) * 6%	56,604	5.7
Surtax –UCMT	(4) = (3) * 7%	3,962	0.4
Surtax – ES	(5) = (3) * 3%	1,698	0.2
Surtax - LES	(6) = (3) * 2%	1,132	0.1
Net Payment	(7) = (1)-(2) -(3) -(4)-(5) -(6)	842,264	84.2

2. Additional Tax Considerations



Additional Considerations

China Licensee's Obligation – withholding agent



Additional Considerations

**Beneficial
Owner**

Ownership

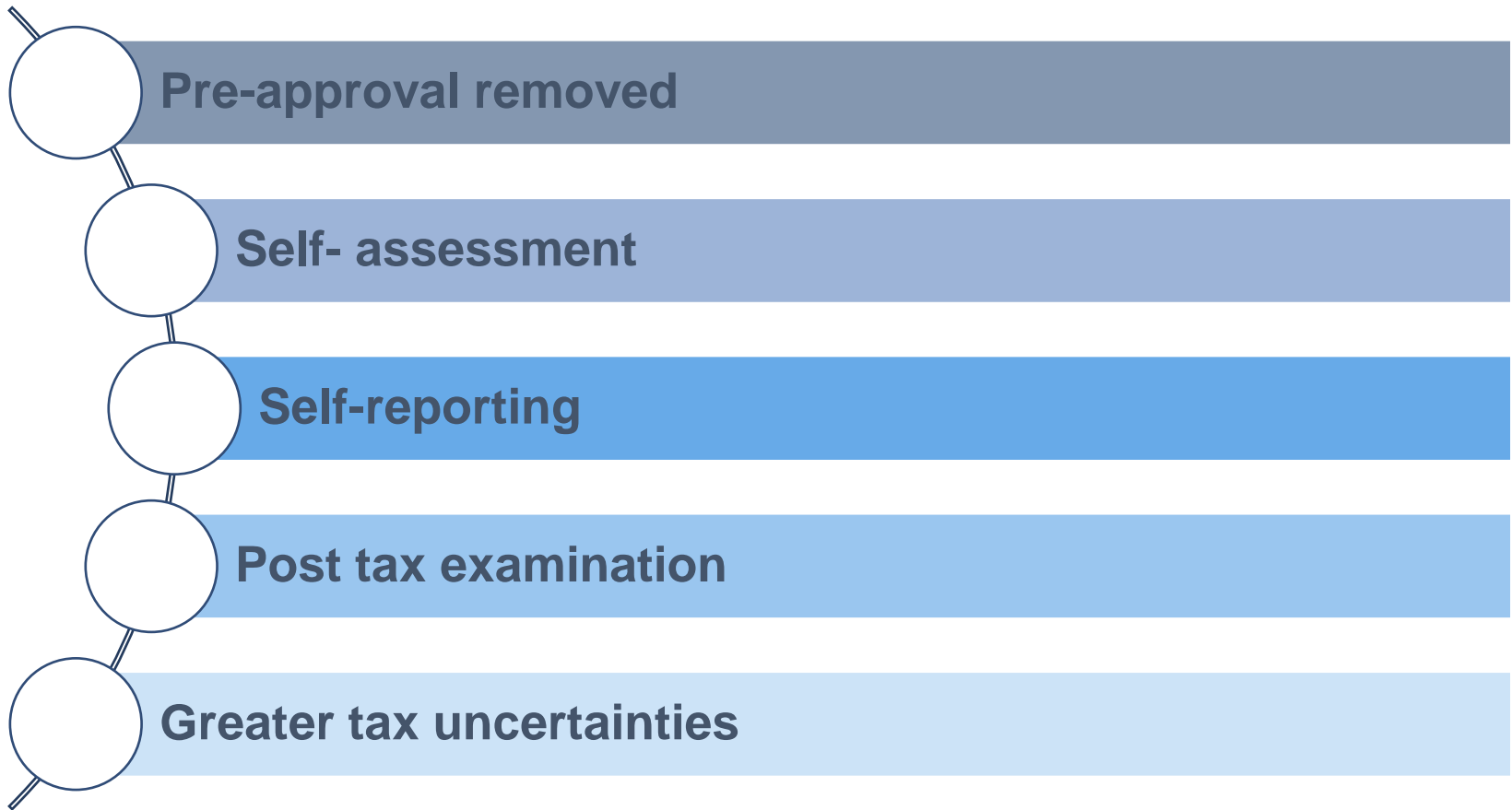
**Control over the income and the rights
and property**

Individual/company/organization

**Agents/conduit company not
applicable**

Additional Considerations

Simplified Process for Claiming Tax Treaty Benefits (China)





3. Procedures for Cross-border License Fee Payment

Procedure

Step 1

Contract registration

- If for importing of tech & know-how (incl. patent transfer, patent right transfer, patent licensing, know-how licensing, & technical service agreement), company must register at local commerce bureau and MOFCOM to obtain Technology Import License
- If for trademark licensing or transfer, company must register at trademark office

Step 2

Applying for DTA benefits

Step 3

Withholding tax filing: Complete withholding VAT and withholding CIT filings, respectively, within the mandated period

Step 4

Record-filing with tax bureau in charge if outbound payment is over USD \$50,000

Step 5

Bank payment

Similar to the service fee payment, the below document might be required by the bank to achieve the payment:

- Relevant contract; and,
- The invoices, the payment notice, or the other documents that can prove the rationality and authenticity of the transaction



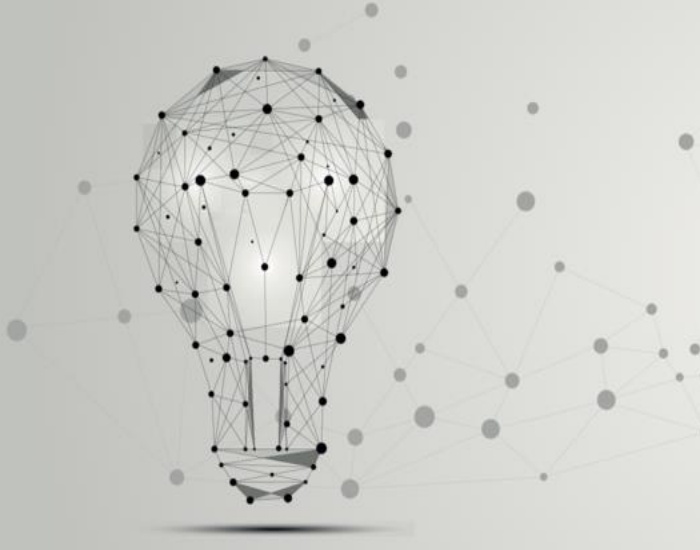
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Brand Licensing

Common Legal Issues of IPR Licensing



Speaker: Eric Su

Founding Partner of HongFangLaw

eric.su@hongfanglaw.com

Outline

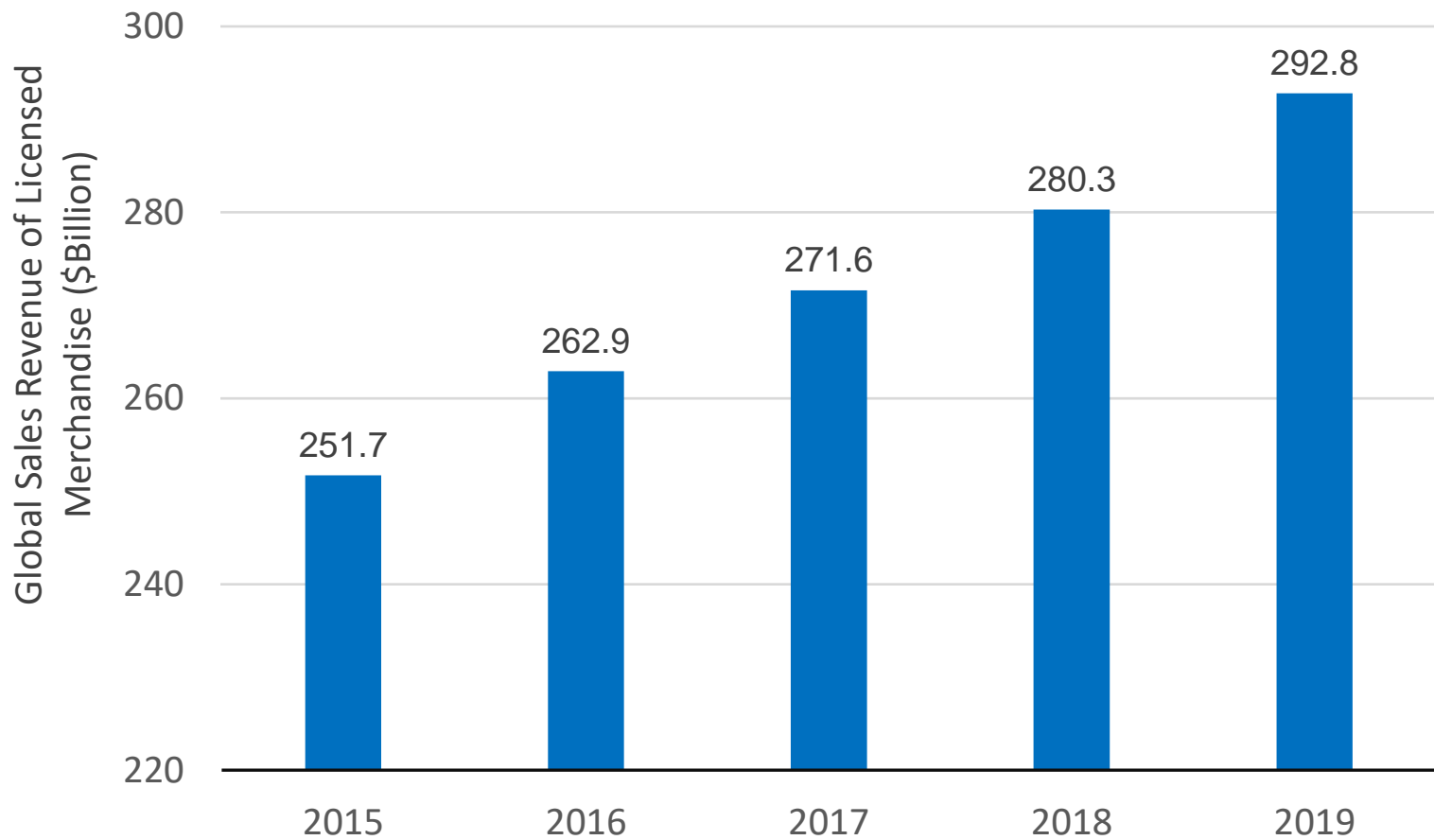
- *What is brand licensing*
- *Scope of license*
- *Knowledge of a licensee by licensor – How to select a licensee?*
- *Type of license*
- *Royalty and payment*
- *Default and penalty*
- *Duration, renewal, termination and recordal*
- *Application Law*
- *Supervision on the license*
- *Other commercial clauses and financial considerations*

➤ *What is Brand Licensing?*

Brand Licensing is a process of creating and managing contracts between the owner of a brand and a company or individual who wants to use the brand in association with a product, for an agreed period of time, within an agreed territory.

It is a way for brand owners to increase their current fan base and move into new businesses without major investment in new manufacturing processes. It is a smart, resource-effective way to grow both brand reach, impact and revenues quickly and profitably.

➤ *Global Sales Revenue of Licensed Merchandise*



➤ *Leading Global Licensors of 2020*

◆ **Disney** -- \$ 54.7 Billion  The WALT DISNEY Company

◆ **Meredith Corporation** -- \$26.5 Billion  meredith

◆ **Authentic Brands Group** -- \$12.3 Billion  AUTHENTIC BRANDS GROUP

◆ **Warner Meida** -- \$11 Billion 

◆ **Harbro** -- \$6.9 Billion 

◆ **Sanrio** -- \$4.4 Billion 

➤ *Scope of License*

The subject of the license could be a trademarked or copyrighted brand name, likeness, logo, graphic, saying, signature, character or a combination of several of different elements.

Be clear with what you wish to license in or license out:

- ◆ To manufacture
- ◆ To use
- ◆ To sell
- ◆ To distribute
- ◆ To make copies
- ◆ To display
- ◆ To make derivative works from it

➤ *Scope of License*

Strictly define the types of merchandise to be licensed and subdivide the major categories of licensed merchandise to maximize the commercial value

e.g. The commodity category of “kid's clothes” could be further subdivided into toddler boys clothes, toddler girls clothes, big boys clothes, big girls clothes, kid's sports wear, kid's shoes, kid's socks, etc.

e.g. The commodity category of “drinks” could be further subdivided into milks, carbonated drinks, juices, etc.

e.g. The commodity category of “ice-cream” could be further subdivided into strawberry ice cream, chocolate ice cream, vanilla ice cream.....

e.g. Derivative brands/Sub-brands license, PLAYBOY 1953, PLAYBOY GOLF, PLAYBOY ICON, PLAYBOY Bunny; JEEP ; JEEP SPIRIT; ...

➤ *Knowledge of a licensee by licensor – How to select a licensee?*

◆ **Type of Licensee**

1. The actual user of the licensed property
2. A shell legal entity (USA, Hong Kong -- fashion industry)

◆ **Due Diligence**

1. Licensee's business status and experience in the industry (Existing brands, enterprise scale, turnover, etc.)
2. Licensee's supply chain and distribution channels
3. Licensee's financial background such as credit guarantee
4. Licensee's legal structure, legal representative, shareholders, etc., and whether these legal representative and shareholders would like to make a personal guarantee.

➤ *Knowledge of a licensee by licensor – How to select a licensee?*

- ◆ Does the licensee manufacture the product by itself or entrust a third party to do so? -
- A letter of authorization shall be issued separately for the commissioned manufacturer.
- ◆ Commissioned manufacture or disguised sublicense? -- If the commissioned manufacturer also sells the licensed products itself, it shall be regarded as a sub-licensee
- ◆ Sublicense or label transaction? – whether or not the manufacturer purchases label from the licensee

I note in the fashion industry, most of the licensee or sub-licensee, even an online authorized store is enjoyed the right to find its own factory to manufacture the licensed products.

➤ *Type of License*

- ◆ **Exclusive License:** The permission of licensee to safeguard rights (in its own name) ; In an exclusive license, the licensor usually requires priority and low price in purchasing licensed merchandise;
- ◆ **Non-exclusive License:** Normally, the licensee will require the licensor not to authorize more than X number of licensees within the same scope of the license;
- ◆ **Sole License:** similar to an exclusive licensee except that the licensor also retains the right to use (very rare in practice);
- ◆ **Sub-license:** Licensee is allowed to grant subordinate license to third parties

➤ *Payment and Royalty*

- ◆ **Lump-Sum Payment**
- ◆ **Royalty Fee**
- ◆ **Minimum guarantee + royalty fee:** the licensor should have the auditing rights
- ◆ **Benefit-sharing:** e.g. If sales reach a certain amount in 3 years, the licensee acquires a portion of the ownership/using right of the licensed property
- ◆ **Deposits**

➤ *Default and Penalty*

The payment/royalty is usually paid 6 months/one year in advance, or a lump sum.

If the licensee fails to pay the fee in due course, the licensor shall send Notice of Default/Reminder Letter to the defaulted licensee immediately (notarized if possible). If the licensee is still unable to pay the balance, the licensor shall terminate the contracts accordingly and hold the breaching party liable.

➤ *Period, renewal, termination and recordal*

- **Period : 5+5**, the first three years are the investment period of a brand and it becomes profitable in the fourth and fifth years; Annual Authorization Letter
- **Renewal:** Renew the contract in advance; Be alert that the distributors/sub-licensees of licensee pre-emptively negotiate with the licensor.
- **Termination: Expiry of** Termination or Termination in advance for breaching of agreement? in which situations will the agreement be terminated? in which manner? how termination should be requested by a party? Inventory clearance?

➤ Recordal: Register the trademark license with CNIPA

国家知识产权局

地址:北京市西城区茶马南街1号 邮政编码:100055

<p>邮政编码: 610000</p> <p>四川省成都市武侯区星狮路511号503A</p> <p>成都卓阳</p>	<p>发文编号:</p> <p>SYXK20190000027965</p>
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商标使用许可备案通知书

成都卓阳:

你(单位)报送的第28800002号注册商标使用许可,我局予以备案。

备案号 20190000027965


许可人 成都卓阳生物科技有限公司

被许可人 成都卓阳生物科技有限公司

许可期限 2019年11月01日至2029年01月13日

许可使用商品/服务项目:

第3类: 1:洗发液;2:口香水;3:动物用化妆品;4:洁肤乳液;5:干花瓣和香料的芳香混合物;6:空气芳香剂;7:香料;8:化妆品;9:香精油;10:洗洁精



办理方式: 代理办理 商标代理机构: 四川正一知识产权代理有限公司 当前页/总页: 1/1

➤ *Application Law*

➤ **Application Law**

➤ **Dispute Resolution:** ADR? Court? Venue? –How to execute the judgment/arbitration decision.

13. **APPLICABLE LAW.** This Agreement shall be governed by and interpreted under the laws of the State of Illinois without regard to its conflicts of laws provisions. Licensee hereby submits to personal jurisdiction in Cook County, Illinois or any other court of competent jurisdiction chosen by Licensor. The parties hereto agree that any and all disputes arising out of or relating in any way to this Agreement shall be litigated only in courts sitting in Cook County, Illinois or any other court of competent jurisdiction chosen by Licensor.

第二十九条 适用法律与争议

29.1 管辖法律：本协议应受中国法律管辖，并依中国法律进行解释。

29.2 仲裁：

由本协议引起的或与之有关的任何争议、争执或权利主张，包括关于本协议的有效、无效、违约或终止的争议、争执或权利主张，都应当在上海国际经济贸易仲裁委员会通过仲裁解决。仲裁员人数应为三（3）人。仲裁程序中使用的语言应为中文。仲裁裁决应为终局且对双方均有约束力。

29.3 律师费用：败诉一方应支付胜诉一方因仲裁所产生的所有合理的律师费用和成本。

➤ *Supervision on the license*

➤ **Quality Control**

Quality control requires both a setting of standards of quality and the policing of those standards by the owner of the trademark or its representatives to ensure that standards are being complied with.

➤ **Reporting and Auditing**

The licensor normally requires the licensee to keep records and accounts of its sales so that the licensor may audit or check on the accuracy of calculation, which form the basis of royalty payment.

➤ **IP & Infringement**

Whether licensee and/or licensor are sued by a third party;
Whether a third party is infringing the licensor's trademark;
The licensee/affiliates/subsidiaries/shareholders/senior executives are forbidden to file the IP around the world;

➤ *Other commercial clauses and financial considerations*

◆ **Performance Requirements**

Many licensing agreements come with performance clauses, which allow for the agreement to be dissolved or penalties to be levied if the licensee doesn't live up to certain requirements.

◆ **Written Approval**

Design, quality, labels, factories, distributors, online stores, etc., shall be all approved in advance by the licensor.

◆ **Product Liability**

which entity will be legally responsible, should the use, consumption, storage or transportation of the product cause harm.

◆ **Confidentiality**

- Know-how
- Trade secrets
- Any information received as part of agreement



**STAY
WITH US.
THANK
YOU!**





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Q & A

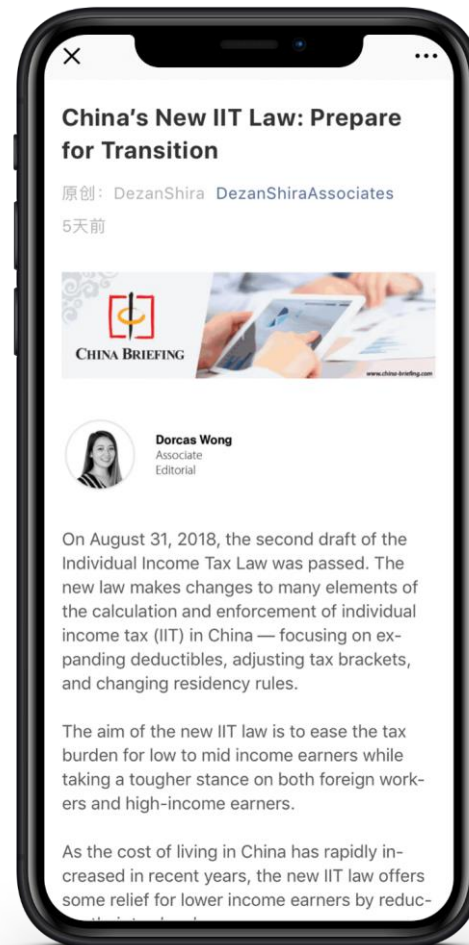


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