

Argentina Licensing Update

Practical aspects of licensing in Argentina; recent laws and tax regulations are discussed

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I shall analyze certain practical aspects which, according to my own experience, have complicated matters with regard to licensing in Argentina.

Before going into more detail, however, I wish to refer to two regulations which were passed in the last two years. I will also mention some aspects of the situation of the licensor as regards taxes.

REGULATIONS PASSED IN RECENT MONTHS

There are two recent regulations which were passed which I consider of sufficient importance to mention here. One is referred to the accepted royalty percentages in contracts between independent parties and the other is referred to acts requiring approval and registration.

Regulation 58/79 dated June 7, 1979

178 Royalty payment sums, agreed upon between independent parties, will not be objected to when not exceeding the amounts established in Article 10, Paragraph d. This article establishes which are the clauses that merit objection. Included are those clauses establishing royalty payments of more than 1 % in the licensing of trademarks when not including transfer of technology; 2 % in contracts covering technology for the automobile industry and 5 % in the remaining cases.

Before this regulation was passed, the Registry quite frequently objected to royalty payment percentages, even if they were not higher than the percentages mentioned above. This gave rise to the following alternative: the contract was redrafted including the percentage generally suggested by the Registry which led to its immediate approval and registration, or the percentage agreed upon by the parties to the contract was insisted on, leading to the subsequent delay and risk involved in taking this stand.

The regulation was passed based on the presumption that when the parties to a contract are independent, said parties have freely entered into the contract and that in view of the free will of said parties, the contract is legally binding when the royalty payment agreed upon does not exceed the percentages established by law.

Regulation 7/80 dated January 14, 1980

This regulation establishes which acts require approval and registration.

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proval and registration.

I would like to refer to the reasons why this regulation was passed, although its provisions are rather general and apply to all contracts.

Law 21.788 passed in April 1978, establishes the legal framework for risk contracts covering prospecting for and production of hydrocarbons. These risk contracts are entered into by state enterprises and private, local or foreign contractors.

Article 2 of said law establishes that the contractors are bound to providing the necessary technology for the performance of the operations within the area set out in the contract, at their own exclusive expense. Thus, we find that any contract includes an obligation which prima facie implies the provision of technology, even when said provision is merely an accessory object of the contract.

In many cases this contribution of technology or of technical services did not necessarily imply transferring knowledge to the beneficiary of the services. Many risk contracts did not actually cover the assignment of knowledge, the assimilation or acquisition of technology or of a right to the use of industrial property rights.

In view of the above, contractors were not sure if such contracts were governed also by the Law of License Agreements.

Regulation 7/80 thus states that Law 21.617 requires only contracts including training or teaching the license certain technology covered by the technical services rendered, to the registered. In those cases in which the technical services do not include transferring knowledge, even when the party rendering the services uses its own technology, the contract does not have to be approved and registered.

Having referred to the rulings, I will now proceed with the discussion of the reform of our legislation. The new law is replacing Law 21.617. Some amendments have been discussed privately and it is to these which I will now refer.

First, contracts entered into by parent corporations covering the natural and constant flow of technology provided as know-how, technical assistance, or by sending technicians, etc. would not require registration.

At present, transfer of technology carried out by informal means such as trips, by telephone or telex, etc., and not involving the payment of fees, does not require registration when performed by parent corporations. The scope of Article 5, which covers this aspect of matter, would be broadened to include the transfer of technology between parent and independent parties.

Royalty Payments

I have already referred briefly to Regulation 58/79 covering royalty payments. This includes contracts with royalty payments not greater than 1% covering licensing of trademarks and not including the provision of technology and not greater than 5% in the remaining cases, with those contracts which are automatically registered. You will notice that I did not refer to the 2% royalty payment for contracts related to the automobile industry. The bill in question eliminates this restriction, a reasonable step in view of the specific legal framework involved in this industrial sector, as this restriction was included in Law 21.617 because Law 19.135 which established it, was in force at the time the former was passed. The new legal framework in force for this particular industrial activity has eliminated the restriction and there was no point to including it in what can be considered a law of general rather than particular scope. The corresponding contracts, therefore, take into account the 5% established for the cases mentioned above.

I shall now refer to certain practical considerations which I shall divide in two groups. First, I shall mention the information and documentation which must be filed together with the application for registration of a contract. I will then refer to certain aspects and clauses that have been objected to by the Registry, or by the licensee or even by the licensor.

FORMAL REQUIREMENTS FOR FILING APPLICATIONS FOR APPROVAL OF CONTRACTS

- a. A request signed by either party to the contract or an attorney of either party, must be filed for the approval and registration of the contract.
- b. A form must be filled out stating certain information regarding the licensor and the licensee. The information requested regarding the licensor covers only the name and address. The licensee must furnish information regarding the corporate relationship existing between licensor and licensee, estimated payments to be made, estimated total sales of licensee, and whether the licensee received any other technology from abroad, whether covering the object of the contract or any other, prior to the execution of the contract.
- c. Original contract, in Spanish, and two copies.
- d. A list of the patents, trademarks and designs included in the contract, indicating date of issuance, expiration, registration number, and in the case of patents, the text of the main claim.
- e. Parties having their place of business abroad must have their signature attested by a notary public and the notary public's signature must be authenticated by the authorities of that country, the document then being legalized by the Argentine Consulate.
- f. The parties to the contract must establish legal addresses within the Republic of Argentina. I will refer to this particular point below.
- g. The licensor must expressly state that he is familiar with the provisions of Law 21.617.
- h. A description of the products and processes li-

censed, including technical characteristics must be furnished. It is advisable to include, whenever available, brochures, manuals or other printed matter describing the object of the license.

LEGAL OR CONTRACTUAL ASPECTS WHICH TEND TO COMPLICATE MATTERS

I now wish to refer to what could be considered the main object of this discussion: "A licensing case from Argentina". I shall refer to some aspects of this matter, which, from experience, require special consideration.

LICENSOR'S LIABILITY

There are basically two clearly defined aspects as regards the licensor's liability, whether to the licensee or to their parties.

The licensor's liability arises, first, on account of damages suffered by the licensee or third parties, resulting directly as a consequence of certain use when following the licensor's instructions, if they were provided. By damages is understood, not only consequential damages, but also loss of profits. In these cases, it has been acceptable for the licensor to limit his liability, either to a fixed amount or to a percentage of the royalties incurred in his favor.

The licensor's liability arises, secondly, on account of the infringement of industrial property rights of third parties by licensee. In these cases, clauses limiting or exempting the licensor's liability are unacceptable.

There is a logical distinction which must be made with regard to this last case. When the infringement of industrial property rights of third parties occurs outside the Republic of Argentina, I understand it is logical to allow the full exemption of liability, as the license is granted for a specific country, although including the possibility of exporting to third countries. It would be extremely risky for the licensor to agree to be held liable for infringements in countries which he was never interested in as markets, and for which he is therefore unaware of the existence of third party rights.

Accounting Information To Be Rendered By Licensee To Licensor

The licensee offers information, from information, from time to time, to the licensor with regard to the sales of the licensed products. This information is generally provided by means of reports sent directly to the licensor, who reserves the right to verify said information when he sees fit, whether directly through his own personnel or by means of independent professionals.

The licensee quite frequently objects to this procedure of verification or request for greater information to be supplied by him to the licensor. I wish to point out that this objection mentioned does not refer to provisions established in our legislation, but to an objection stated by one of the parties to the contract, in this case the licensee, at one point of the negotiation.

The reasons usually given for objecting to the mentioned verification procedures, refer to danger of said information being made known. We set aside the situation in which the licensor has

granted a nonexclusive license and that once the contract has been executed, the licensor competes either directly or indirectly by means of an associate, with the licensee. In these cases, there is no doubt and it is quite inevitable for the licensee's competitor to acquire information which is generally confidential. This is a risk run by the licensee when entering into a nonexclusive contract.

The objection is more understandable when, in the case of nonexclusive license agreements, the licensor does not compete directly or indirectly with the licensee, —as well as in the case of exclusive license agreements— and the information obtained by the licensor as a result of the examination of the licensee's accounting books reaches a competitor.

I believe it is logical and reasonable to take the necessary precautions so that this does not occur. It is therefore customary for the parties to agree that the licensor shall hold such information confidential and shall restrict such examinations of the licensee's accounting books to twice or three times a year.

Establishing a Legal Address in the Republic of Argentina

Article 17 of our Law 21.617 states that in order to request the approval and registration of contracts, the parties to said contracts must establish a legal address in the Republic of Argentina.

This particular requisite has been objected to by some licensors when the contract establishes that the jurisdiction or applicable law is not that of Argentina. They understand that after establishing in a clause of the contract that the applicable law is that of a certain country, the courts of said country being competent in the event of controversies, establishing a legal address in the Republic of Argentina would constitute an extension of the jurisdiction.

This requisite has also been objected to even in the event of agreeing to submit disputes to Argentine Law Courts, when a legal address has been established abroad for service of notices and payment of royalty fees. In these cases, the licensors hold that on establishing a legal address as required by Law 21.617, the licensee may be held to be complying with his obligations when paying the due sums at the locally established address, or when serving notice of any alteration in the contractual relationship at said legal address.

You will see from my following remarks that the licensor has nothing to fear when complying with the aforementioned requisite.

First, the law specifically states that on establishing legal address in this country, the party in question does so only in order to request the approval and registration of the contract. This statement implies that the legal address established is valid only for the Registry and not for the other party to the contract, and only for the actual filing of the request for approval and registration. Once this procedure has been completed, the legal address loses its validity. The establishment of said legal address does not necessarily have to appear in the wording of the contract and can be men-

tioned in a separate document.

It is important to add, moreover, that on establishing a legal address, it is possible to expressly state that such an address is established only in order to comply with the requirements provided in Article 17 of Law 21.617, the legal address established in the corresponding contract being valid in all other respects.

Deductions From The Sales Price

The royalty payments agreed upon in a contract must be calculated on the basis of the new value of sales, once a series of items established in Article 11 have been deducted. The actual list of deductions merely states certain examples of items to be deducted from the invoice value at the factory gate and no doubt there is no reason why the parties to the contract cannot agree to the deduction of other items from said price.

I have found that import duties on raw materials and other staples required for manufacturing the object of the licensed agreement have been a frequent subject of negotiation. The licensees requesting this deduction hold that if this item is not deducted from the sales price, the royalty fee will be calculated taking into account an item which, although a part of the final price of the product, is not under the licensee's control. The licensees also hold that by allowing this item to be included in the final price on which the royalty fee is calculated, the licensor is obtaining a benefit on a greater tax.

In some cases, the royalty fee has been reduced in a certain percentage, in order that the overall payment is similar to the original royalty fee minus the deduction of import duties.

I do not find this alternative advisable as it not only could have influence in agreements in other countries involving the licensor, when they included the benefit of more favorable clauses referring to this matter, but in the event that such duties are reduced or eliminated, the licensor would find his income from royalty fees reduced.

The economic policy set out by the present authorities, a policy which, according to statements made on several occasions, will continue long after the present authorities have concluded their term of office, foresees the systematic reduction in the duties charged for imported products, raw materials and staples.

In the event of adopting the alternative mentioned above, the individual royalty fees would be gradually reduced, notwithstanding an eventual increase in the overall sales which would then appear as an increase in the actual sums received by the licensor.

Conclusions May Differ

The conclusions which can be arrived at by some licensees are of course, rather different, when considering the same requirements. A certain raw material may not be available in the local market, if only because there is no local supplier. The licensee is thus forced to purchase such raw material abroad, and therefore, to pay the corre-

sponding import duties. On the other hand, several local suppliers may exist and, because of the particular situation of our economy, their prices may be somewhat higher than the prices existing on the international market. Leaving aside the possibility of dumping, it is quite obvious that the licensee who may deduct import duties from the price on which royalty fees will be calculated, will prefer to purchase his material abroad, because his final costs will be reduced since the royalty will only affect the FOB price of the raw material. If instead of importing, he buys the necessary raw materials on the local market, the final product price will be higher and consequently the royalty fee will also be higher.

We are considering two completely opposite situations which must be taken into account when discussing this particular requirement. The licensor will, no doubt, have to become familiar with and do the corresponding research covering the actual situation of the local market.

We cannot forget that at some point the item to be deducted be that of possible antidumping duties established by the corresponding authorities for the import of certain staples.

Thus, the most advisable position seems to be that if the licensor should accept the deduction of import duties, said duties be deducted from the ex-factory price and not by reducing the royalty fees.

Technology For Tenders

There are major works which have been planned by state enterprises and the state itself, which include the requirement that the successful bidder rely on technical assistance and/or technology provided by internationally known suppliers or sources. This requirement is established in the bid specs.

When a local concern cannot provide, of its own accord, such technical backing, and decides to submit a tender, it must necessarily seek out the required technical assistance and/or technology by entering into contracts with those who can provide it and are internationally known for their research and development activities.

In the event that such a concern is awarded the tender for the works, the contract will be extremely valuable to it and will, no doubt, be enforced as soon as possible.

Yet what happens if such a concern is not awarded the tender? Here we have a situation offering certain surprises for the supplier of technical assistance or technology as there will be no transfer of knowledge, simply because there is no works in which to apply it.

At this point the parties to the contract are faced with a situation which was not contemplated on entering into such a contract. Certain rights and obligations for the parties to the contract will have been created and yet it will be impossible for the parties to fulfill them.

In such cases, it is advisable both for the licensor as well as for the licensee to include a clause subjecting the contract to a suspensive condition, the future and uncertain event being in this case the awarding of the tender to the licensee. Thus, the

obligations cannot be executed and remain uncertain until the occurrence of said future and uncertain event.

The Registry has accepted subjecting the contract to such a suspensive condition and although Article 26 provides that performance of the contract must be initiated within a two-year term, the awarding of a tender to the licensee or to another party, i.e. the occurrence of the future and uncertain event which will create a legal relation, generally takes place within said term. In the event that it does not, the same Article 26 establishes that the contract can be registered once again, and no doubt the new registration will be acceptable to the Registry, particularly in view of the fact that the causes which prevented the contract from taking effect are beyond the control of both licensor and licensee.

Once the tender has been awarded to the licensee, the contract takes effect as regards the specific legislation ruling transfer of technology. At that point the rights and obligations of the parties to the contract are legally created, and any act prior to said awarding, and subject to the aforementioned suspensive condition, acquired full validity.

Renewal of Earlier Contracts

When the first law ruling transfer of technology came into force in 1971, many contracts existed which had been entered into before that date. These earlier contracts were registered automatically and were considered valid until December 31, 1973. Regulation 119/73 established a series of requisites to be complied with by the parties to these contracts in order to adjust them to the legal rules and regulations in force and their temporary validity was extended to December 31, 1974, once they had complied with said requisites.

Law 21.617 established that the validity of such temporary registration was extended until a regulation approving or rejecting a final registration was passed. We must point out that these extensions referred only to the validity of the registration, as if the contract as such had expired, the extensions could not provide for a greater duration than that agreed upon by the parties to the contract.

Regulation 211/77 was finally passed in view of the considerable number of cases included in the successive extensions and the impracticality of studying each particular case. This regulation established that the temporary registration became final if and when the specific conditions set out in said regulation were met. The final registration was valid until December 31, 1979.

Thus, we are faced with a considerable number of contracts signed prior to 1971 and whose validity expired four months ago. Many of these contracts have been renewed, and the parties to said contracts have requested the approval and registration of the renewals. In other cases, however, the approval and registration of renewals has not been requested and I shall refer to these particular cases at this point.

RENEWAL

In order to request the renewal of a contract

whose validity expired on December 31, 1979, it is necessary to comply with the following requisites:

a. File a duly arranged and orderly text of the contract. As you know, many agreements entered into before 1971 were subjected to a series of modifications, in view of the many regulations passed at a later date which required that certain conditions be met in order to allow the continued validity of the contracts. Compliance with these conditions frequently implied including new clauses, altering the prices agreed upon, reducing the obligations or covenants of the licensor, etc. This led to the existence of contracts with a series of modifications and amendments making it quite difficult to determine which exactly was the text of the contractual relationship in force between the parties.

b. Adjust the duly arranged and ordered text to the provisions established in Law 21.617. This should not offer any difficulties.

c. Indicate the actual flow of technology registered during the duration of the contract.

d. Indicate the new technology to be incorporated by means of the renewal requested.

TAXATION AND RELATED MATTERS

There are two types of taxes which are directly related to license agreements.

First, there is the stamp tax, which must be paid once the agreement has been approved. Second is the income tax which affects not the contract itself, but the royalty paid by the licensee to a licensor domiciled abroad, I shall consider each separately.

Stamp Duty

It is levied by the Federal Districts and the provinces on all license agreements. The actual rate in the Federal District is 1% of the estimated value of the agreement, and must be paid within

five days running from the date parties are notified of the approval.

Income Tax

The Income Tax Law assumes that 40% of the amounts paid to licensors domiciled abroad, is to be considered as net profit. Therefore, only said percentages is taxable to a flat 45%; provided the agreement has been approved and registered at the Registry of License Agreements. If the agreement has not been approved and registered, and therefore it has not complied with the provisions of Law 21.617, the flat 45% is payable on the total amount without any type of deduction.

The above means that if the total amount due is \$30,000 the income tax which will be deducted will be \$5,400. That is 18% of the total amount.

If it was agreed that royalties were to be paid free of tax, then in the same example in order to allow the licensor to receive \$30,000, we should increase said amount \$6,585 (21.95%). Therefore the 18% of \$36,585 would allow us to reach the sum due to licensor.

Related matters

There are other payments which have to be kept in mind:

(i) Tax on the purchase of foreign currency: this is a .6% due on all transactions involving the purchase of foreign currency, which must be made through banks or duly authorized brokers.

(ii) Official fees payable to the Registry of Technology of .15% of the estimate value of the agreement. This is paid to the Registry prior to obtaining the copies of the resolution of approval and of the agreement with the attestation of its recordal.

Finally, I wish to point out that Argentina has signed treaties which avoid double taxation with Sweden, West Germany, and Bolivia.