

Trademark Licensing In China

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Practical drafting advice for preparing trademark licenses under Chinese law

A trademark license agreement, once concluded in accordance with China's law, is legally binding. The parties should perform all their obligations stipulated in the agreement. No party should arbitrarily alter or terminate the agreement. If a party fails to perform his obligations, or arbitrarily alters or terminates the agreement, the party will be liable to undertake the corresponding legal responsibilities. Therefore, how to draft a license agreement which could be carried out successfully becomes most important. For the performance of the agreement, the terms and conditions comprising the agreement between the parties must be specific and clear so that no misunderstanding and dispute will arise in respect of the terms and conditions. The parties should specifically and clearly indicate in the agreement their rights and obligations, the terms and conditions for the performance of the agreement, the conditions for termination of the agreement, liability for breach of agreement and resolution of disputes arising from the agreement.

Under China's trademark practice, a trademark license agreement should include, but not limited to, the following aspects, which should be expanded specifically and clearly in the agreement:

The Kind of Trademark License

The license agreement should indicate whether the licensee is exclusive or non-exclusive. The exclusive license, rarely used in China, refers to that in which the licensee permits only one licensee to use his trademark on certain goods in certain

territory. The licensee may not permit a third party to use the same trademark on the same goods in the same territory. The licensee also enjoys the prohibitory right to prevent other persons from using the trademark. But it is not clear whether the licensee also prohibits the licensee from using the trademark. Therefore, the license agreement should expressly indicate whether the license is also exclusive to the licensee.

Non-exclusive license means that the licensee permits more than one party to use the same trademark on the same goods in the same territory and the licensee himself also enjoys the right to use the trademark. The licensee has no right to prevent other parties from using the trademark.

Ownership of the Licensed Trademark

Trademark license refers to two important points — the ownership of a trademark and the right to use a trademark. What the licensee obtained from the trademark license agreement is the right to use the trademark, not the ownership of the trademark. The ownership belongs to the licensor. To confirm that, the agreement should include express provisions on ownership. The provisions should state that the licensee acknowledges the licensor's exclusive ownership, right and interest in and to the licensed trademark, and agrees that he will not at any time do or cause to be done any act or thing in any way impinging or interfering to impede any part of such ownership, right and interest in and to the licensed trademark. The licensee shall not in any manner represent that he has ownership in the licensed trademark. The goods and other materials should indicate that the licensed trademark is being used under

license, and/or equivalent wording to indicate precisely who is the proprietor of the trademark, and the licensee relationship between the parties.

A provision should expressly prohibit the licensee from including the licensed trademark in his company name or trading style. The agreement should also include that any goodwill or other benefit derived from the use of the licensed trademark shall inure solely to the benefit of the licensor.

Quality Control

The Trademark Law places emphasis on the quality of the goods. Article 26 provides that the licensee shall supervise the quality of the licensed goods, and the licensee shall guarantee the quality of the licensed goods. In accordance with the Trademark Law, the agreement should include specific and express provisions on quality control.

The provisions should state that the licensee shall guarantee that the licensed goods produced by him meet the quality standards formulated by the licensor. The licensee shall submit to the licensor on a regular basis representative samples of the licensed goods covered by the licensed trademark for inspection. The licensor or his servants or agents, may at reasonable times enter the licensee's premises where the licensed goods are produced and stored for sale for the purpose of inspecting the licensed goods and method of production. For such a purpose, the licensor may station a permanent inspector at the

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licensee's premises. In the event the licensed goods produced do not meet the quality standards, the licensee shall discontinue the production and distribution of such goods.

As to the unqualified goods which have been distributed, the licensee may claim for damages. Furthermore, to make the licensed goods enjoy good separation, the provision should indicate the main mission to the licensee for approval of specimens of labelling, packaging, materials, promotional or advertising materials dealing with the trademark.

Discontinuing Use at the Expiration of the Agreement

Provisions should indicate that at the expiration of the license agreement, the licensee shall discontinue all use of the licensed trademark on the goods, signs or advertisement, and any other indication of use of the licensed trademark. At such expiration, any and all right to use the licensed trademark granted to the licensee shall immediately be assigned and reverted to the licensor. The licensee furthermore shall make no claim whatsoever to the licensed trademark or against the use thereof by the licensee or his assignees and licensees.

Within the validity of the agreement, the licensee enjoys the right to use the licensed trademark. When the agreement expires, the licensee's right to use the licensed trademark will be forfeited. In the absence of the licensee's consent, the continuous use of the licensed trademark will become an infringement. However, it may be provided that the licensee may during the period of six months after such expiration sell any of the licensed goods that at that date are in stock and marked with the licensed trademark.

Assignment, Sub-License and Pledge

When the licensee obtained from the licensor agreement is the right to use the licensed trademark, but not the ownership of the licensed trademark. He is, therefore, not entitled to assign, sub-license and pledge the license agreement or any right or interest thereof. If the agreement

is assigned to a third party, whose productive condition is unknown to the licensee, the quality of the goods cannot be controlled, and the reputation of the licensed trademark will be damaged.

Royalties

If royalties are included in the agreement, provisions should indicate the time and amount of payments. Royalties may be paid quarterly or yearly. The amount of royalties may be a certain percentage of the net sales of the licensed goods. The Trademark Law and other laws or rules have no mention of the maximum and minimum of the percentage, which is decided by the parties. The provision should mention the definition of the net sales against to which the royalties are to be calculated. For calculation of royalties, the provision should also mention that the licensee shall keep faithful and complete records and books of the accounts containing the information, such as details of the production of the licensed goods, the amount of the stock of the licensed goods, the licensed sales of the licensed goods, etc.

Scope of Territory

A provision should be included specifying the territory of the license. Under the license agreement, the licensee is authorized to use the licensed trademark in the territory provided in the agreement, but he is not entitled to use the trademark beyond the scope of the territory provided in the agreement.

Liability to the Licensor's Trademark

In order to protect the licensed trademark and to prevent consumers' confusion as to the origin of the goods, the agreement should provide that the licensee shall not use a trademark that is similar or almost identical to the licensed trademark on the identical or similar goods. Violating this provision will constitute trademark infringement. Further the licensee shall not use the licensed trademark on similar or dissimilar goods, and shall not use the trademark by associating with his trademark, unless the licensor authorizes it.

Trademark Infringement

Regarding infringement, the license agreement should provide that proceedings for infringement of the trademark shall be taken at the discretion of the licensee and by the licensee. When the licensee becomes aware of any infringement or threatened infringement of the trademark, he shall immediately notify the licensee of the same and shall give particulars thereof and advise to the licensee to the best of his ability in relation to any act that the licensee may decide to take to protect the trademark. When the licensee decides to take action, the licensee shall provide full assistance.

The licensee enjoys only the right to use the trademark, but does not enjoy the prohibitory right to stop other persons from using the same trademark. Therefore, when he learns of any infringement of the trademark, he is not entitled to take action against the infringer. However, provision might be included that the action may be taken at the discretion of the licensee, in the name of the licensee.

Obligations of the Licensee

Under a license agreement in China, the rights and obligations of the licensee and licensee are closely related. A party who enjoys a right must perform his obligations. As to the licensee, his main obligations are to guarantee that the licensee can exercise his right to use the licensed trademark within the term of the agreement. In the absence of the licensee's consent, the licensee shall not assign, pledge or encumber the licensed trademark for the benefit of his creditors. The licensee shall not surrender the trademark, and shall never let the trademark expire. In case of an exclusive license, the licensee shall not grant the license to a third party. Furthermore, the licensee must guarantee that he has exclusive ownership to the licensed trademark, and no other person will make claim to the licensed trademark.

Termination of the License Agreement

Conditions for the termination of the license agreement should be

included in the agreement. The other party of the agreement is entitled to terminate the agreement on account of any of the following events:

1. One party is in default of the agreement, which default is incapable of cure or which default, being capable of cure, has not been cured within a specified number of days after receipt of written notice by the other party.

2. One party becomes insolvent, makes a general assignment for the benefit of creditors, or assigns to a third party. The assignment of one party has been passed to a third party for 90% or whatever percentage is required to pass control to the third party.

3. The licensee assigns, sub-licenses or pledges the license agreement.

4. The licensee fails to pay royalties in the extension period.

5. The licensee causes the use of the licensed trademark.

6. The licensee commits the infringement of the licensed trademark by using a trademark that is similar to the licensed trademark on the identical or similar goods.

7. The prevention of performance that goes beyond the control of the parties (i.e. force majeure or in a result of governmental action).

Liability for Breach of Agreement

Once an agreement is concluded, the parties should perform their obligations. If one fails to perform his obligations, he will be liable to undertake his legal obligations. China's Foreign Economic Contract Law, applicable to the trademark license agreement, provides that when a party fails to perform, or his performance does not conform to the agreed contractual obligations, the contract is breached, the other party is entitled to a claim for

damages or to ask the party in default to adopt reasonable remedial measures. If the losses suffered by the other party are not paid in full after the remedial measures are taken, the other party retains the right to claim for damages. With regards to the amount of damages that should be paid, the law provides that damages for breach of contract by a party consist of a sum equal to the loss suffered by the other party as a consequence of the breach. The parties may agree in a contract that a certain amount of liquidated damages shall be paid to the other party if one party violates the contractual obligations, and they may agree upon a method for calculating the damages arising over such a breach of contract. In case both parties are in breach of the contract, both parties shall bear the relevant losses in accordance with the obligations due to them. The law further provides that if a party fails to pay at the appointed time the amount agreed upon in the contract, the other party is entitled to payment of principle plus interest for the delay. The trademark license agreement should include damages for breach of agreement so that the agreement will be carried out successfully.

Resolution of Disputes Arising From an Agreement

When a trademark license agreement is signed, many disputes may arise from the performance of the agreement. Provisions on resolutions of disputes should be included. The Foreign Economic Contract Law stipulates that disputes arising over a contract ought to be settled, if possible, through consultation or mediation by a third party. In case the parties concerned are not willing or fail to go through consultations or mediation, they may sub-

mit to China's arbitration agency or other arbitration agency in accordance with the arbitration agreement reached afterward. China's arbitration agency is the Foreign Economic and Trade Arbitration Commission of the China Council for the Promotion of International Trade.

In cases in which an arbitration clause has not been stipulated in a contract or an arbitration agreement has not been made afterward, the parties may take their case to a people's court.

It is not mandatory under Chinese laws that arbitration be conducted in China. The parties may themselves decide whether the arbitration is conducted in China or in any other country. The Civil Procedure Law of China stipulates that the people's courts shall not take cognizance of cases of disputes if such disputes are covered in arbitration agreements between the disputing parties.

In the resolution of disputes arising from agreement, the problem of applicable law will be involved. In respect of the applicable law to the agreement, the Foreign Economic Contract Law stipulates as follows: The contracting parties may choose the law applicable to the settlement of disputes. In the absence of such election, the law of the country that has the closest connection with the contract applies. The equity or contractual joint venture contracts must be governed by the laws of China. In case no relevant provision is stipulated in the laws of China, international practice may apply. When determining the law of the country that is most closely connected with the contract, the law of the place in which the contract is concluded and the law of the place where the agreement is performed should be considered.