Key requirements for trademark licensing in Latin America and the Caribbean

When creating a regional licensing programme, understanding the nuances of the rules and regulations at jurisdictional level is key to success

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Global trademark licensing is fiendishly complex, with rules and practices varying in different countries. In-house counsel need to be both perceptive and strategic so as to act as translators for diverse market realities, ecosystems and legal systems, thus ensuring continuous and unified operations around the world.

Parties to a global trademark agreement generally seek advice on negotiations from attorneys in the United States or the European Union. The licensor and licensee to a cross-border transaction will then usually assign a single law to govern the licence agreement. Unsurprisingly, when a licence includes territories in Latin America and the Caribbean (a vast territory starting with Mexico in the north, continuing through Central America and encompassing South America and the Caribbean), the business deal becomes even more complex, as the selection of contract law and disputes venue will not necessarily supersede local laws. Most IP laws in Latin America and the Caribbean apply automatically if the licence involves a national contractual party or if it is to be carried out within the corresponding jurisdiction, with many of the legal provisions being mandatory.

This article focuses on key issues that commonly arise in trademark licensing in Latin America and the Caribbean and takes a country-by-country look at best practices, the rules and regulations on quality control standards, licence registration, royalties and distribution regulations across multiple jurisdictions. Paying close attention to these is critical for any foreign parties entering a negotiation or drafting an international trademark licence that involves a Latin America or Caribbean jurisdiction.

Quality control

Most international trademark licensing deals include quality control provisions. For example, in many other countries, if a trademark owner fails to carry out adequate control over the quality of the services or goods, the mark could be considered abandoned. Such provisions shield licensors by stipulating approval mechanisms and trademark usage guidelines, and monitoring the licensee's compliance provisions.

In Mexico, a quality control standard is explicitly laid out in the relevant law, which states that products and services sold or provided by the licensee must be identical to those of the licensor. In practice, a licence agreement should contain the know-how, trade secrets, technical confidential information and training to comply with this standard. If a party fails to honour the clause, the injured party may seek judicial relief and request the termination of the agreement for breach of contract. However, it is unclear whether relief would apply if such a clause is absent from the agreement. Following the 2010 amendments to the Mexican legal framework, there are now legal grounds to file a class action for consumer protection. Although not yet tested, there is a risk that the consumer protection watchdog or a group of active stakeholders could file a class action against both a licensor and a licensee for acting contrary to the public interest and failing to adopt suitable quality control measures to the detriment of consumers.

In Central America, the relevant law in Guatemala provides that a "summary of the quality control arrangements" should be included when registering a trademark licence. It also states that the licence may contain provisions that assure quality control measures for the owner. In a similar manner, Honduras establishes that a licence can be registered only if it contains clauses that ensure effective control of the quality of the products or services. Finally, in El Salvador, the relevant law provides that a trademark owner may prevent the sale of products of inconsistent quality in the Salvadoran market when those products were manufactured exclusively to be exported.

Guatemala, Honduras, Nicaragua and Costa Rica also establish that at the request of any party or *ex officio*, a judge (in Guatemala and Nicaragua) or the trademark office (in Honduras and Costa Rica) may prohibit a licensee from using a mark when, due to a lack of adequate quality control, it causes or may cause a likelihood of confusion, deception or damage to consumers. In Honduras, Nicaragua and Costa Rica such behaviour can result in the cancellation of the licence registration.

In other Latin America and Caribbean bloc countries, quality control is not statutorily regulated and all contractual terms and conditions are governed by the contract between parties. A good example of this would be Colombia, where the Andean Decision on Trademark Licensing does not specifically regulate the contents and minimum requirements of a licence. Further, Panama has no general provisions for this area, nor does it establish provisions that determine the nullity of the contract; therefore, the licence is exclusively subject to what the parties agree.

The relevant law in Uruguay provides no specific regulatory framework for quality control standards or procedure for trademarks licensed for product distribution. Thus, there are no precise measures, nor is it indicated how much control must be used to preserve a trademark in the context of a trademark licence agreement. Consequently, quality control in a trademark licence will depend on the parties' agreement and the nature of the agreement executed. Most likely, the parties will agree on the means for ensuring that a licensee's use of the trademark is consistent with the licensor's needs and demands, and – at the same time – that consumers receive the same quality of goods or services no matter where they are purchased or experienced. In connection with this, it is usual for the parties to set out a report and auditing obligation in the contract for stricter control over the quality of the marked products.

In this sense, it is quite common for trademark licences in Uruguay to be granted within the framework of other agreements (eg, franchise agreements or contracts that include licences over other IP rights). In this way, one of the main conditions of a franchise agreement is the concession of a trademark licence; in the context of franchising, the quality control is much stricter than in a standard trademark licence agreement.

On the other hand, Uruguayan law regulates certification or trademark guarantees. Such provisions state that trademarks are symbols that certify common characteristics (ie, qualities, components, nature, methodology implemented and other relevant aspects) between products and services provided by authorised parties and controlled by the certifying entity. In summary, the certifying entity approves that the product meets the required standard, quality or requirement in question and that such certification is evidenced to the customer through the use of a particular symbol or logo belonging to the company.

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Licence registration

In many Latin America and Caribbean jurisdictions, the trademark owner or licensee will need to formally register the trademark licence. Failing to do so can be devastating and could even lead to an opportunistic trademark extortion scenario. Several countries in Latin America and the Caribbean bloc allow marks to be recorded before they are used. Registering a licence creates legal certainty against third parties and, in some countries, a legal presumption of use.

By way of example, in Colombia, the registration of a licence with the Superintendency of Industry and Commerce (SIC) is not compulsory. However, the absence of registration before the competent national office means that the agreement lacks legal effect against third parties. In other words, for publicity purposes, the licence should be filed before the SIC, otherwise the agreement will have only inter-party effects. For registration purposes, short-form licence agreements are accepted by the local trademark office. It is key that when the relationship between licensor and licensee ends, the licence cancellation is recorded as well.

For registration purposes before the SIC, and following Andean regulation, the contract should consist of a private legal instrument executed by the parties, which identifies both the licensor and the licensee, and details the IP assets (trademarks and/or patents) to be licensed. Official fees are due at the time of recordal and are approximately $150 plus 19% VAT when trademarks are involved and $200 plus 19% VAT when patents are involved. This procedure can be expedited and carried out online. If no requirements or information requests are raised, the registration can be completed in less than a month; if the licence agreement is non-exclusive, several registrations can be made.

In Chile, while it is not compulsory to register a licence with the National Institute of Industrial Property (INAPI), unregistered licences have no legal effect and offer no protection against third parties. The contract should consist of the original private legal instrument signed by the relevant parties and should be filed along with the respective annotation form. This will then be analysed by INAPI examiners; if it complies with the necessary regulations, it will then be accepted for registration. Starting from the date that the application is accepted, the applicant will have 60 days in which to pay and provide proof of payment of 1 UTM (monthly tax unit). Once paid, the licence will be annotated in the margin of the trademark registration. INAPI reserves the right to require more information in case of reasonable doubts regarding the veracity of the content of the relevant documentation (the licensing contract). If the payment is not made or proof of payment is not provided within 60 days, the application for annotation will be deemed to have been abandoned.

In Central America, Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua and Panama, trademark licence agreement registration is not compulsory nor constitutive of rights, hence the legal force of the licence is unaffected if it is not registered. The registration is made only for the purposes of publicity and legal certainty.

In Mexico, it is not legally necessary to record a licence with the Mexican Trademark and Patent Office. However, it is advisable, as this allows enforcement actions against third parties and provides a legal presumption of use of the mark by the rights holder.

In respect to the Caribbean, more specifically, the Cayman Islands Intellectual Property Office, formerly the Cayman Islands Trademarks Registry, is the principal body regulating the registration and licensing of IP rights in the region, the largest volume of which comprises trademarks. IP protection, particularly trademark registration and licensing, is frequently relied upon in financing and security documentation, with financial institutions, companies and investors capitalising on the value that is intrinsic to a recognisable brand.

Royalties

Another key issue in international licensing agreements is the taxation of royalties. The payment of royalties is generally subject to the payment of income tax and the amount varies from country to country; further, taxes may apply in every jurisdiction. Additionally, when granting an exclusive licence, it is important to consider whether transfer pricing regulations apply, as some legislation may treat exclusive licensors and licensees as related parties, making them subject to these tax regulations.

In Colombia, if royalty payments are involved, specifically for the licensing of trademarks and patents, such agreements should be recorded before the Domestic Taxes and Customs Office in order to benefit from tax relief on royalty payments.

In Chile, the Income Law does not define what a royalty is. Rather, it describes the burden of withholding tax for each case and distinguishes between different tax rates. In this sense, royalty payments for the use, enjoyment and exploitation of trademarks are subject to a withholding of up to 30% with no deductions allowed. Also, and considering the privileged tax rate for royalties (usually the withholding is at a rate of 35%), the Chilean legislation has imposed a limit on the amount of accepted expenses due to royalty payments. This cap is up to 4% of the payer's gross revenues when payments are made to a related non-resident party. Nevertheless, this 4% limit does not apply if the royalty paid to the related party is subject to a tax rate equal to or greater than 30% in the relevant party's country of residence.

Distribution

Where trademark licences are related to distribution contracts, they may be affected by the specific conditions of the distribution contract, making it necessary to analyse the specific distribution provisions of every country. In most countries, distribution agreements are subject to mandatory provisions, some of which are highly protective of the distributor, meaning that the trademark licence provisions can be affected. For example, some distribution regulations presume the exclusivity of the distributor under specific circumstances and therefore affect the trademark licence if it is deemed to be an accessory.

In Colombia, a non-exclusive distributor, licensee, agent or franchisee may be appointed, which means that the holder of the trademark rights could appoint several distributors, agents and franchisees for the same territory. This is especially relevant as absolute exhaustion of rights is contemplated under the local regulation.

On the other hand, in Uruguay, the key issues in distribution agreements, particularly related to IP matters, are as follows:

- The legal right granted to the distributor to use the supplier's intellectual property, including brand names and trademarks, must be for the purposes of its sales and marketing efforts. Also, given the fact that the agreement will only be enforceable against third parties once it is registered before the Trademarks Office, it is recommended that the parties agree to proceed in this way.

- There are certain aspects regarding the scope of the distribution agreement that have gained certain relevance in distribution agreements in Uruguay. These include:
  - the territory in which the distribution is allowed (and connected to this, the territory in which the trademarks can be used under the trademark licence);
  - provisions that address the parties' post-termination obligations, such as how to deal with open or outstanding orders after termination, the return of inventory, buy-back or transfer of remaining stock, and any marketing or other obligations and rights that would survive the agreement's termination; and
  - clauses containing the exclusive right to sell the products (or not) within the defined territory. In connection with the exclusivity clause, Section 12 of the Trademark Act foresees the exhaustion of trademark rights, under which circulation of marked products, legitimately introduced in the market by the owner or by a duly authorised third party, cannot be impeded by other lawful users of those trademarks, as long as such products and their presentation, packaging and wrapping have suffered no substantial alteration, modification or damage.

Hence, it is common in Uruguay for distribution agreements to be fulfilled by both parties respecting such exclusivity. However, given that exhaustion of trademarks rights can be international and that a third party may legitimately and in good faith introduce the marked products in Uruguay through unofficial distribution channels (parallel imports), the exclusivity effect can be quite relative.

There is no special law governing distribution agreements in Chile. Under the Civil Code, the will of the parties will govern their relationship and the contract existing between them will act as the law. While oral agreements are enforceable in Chile, this will likely be more complicated than the enforcement of written agreements. In any case, the agreement will be enforceable provided that the plaintiff can prove its existence, its contents and that there has been a breach of the whole or of part of it.

Distribution agreements need not be registered in Chile. However, practice indicates that many distribution agreements contain additional contracts among their exhibits, which are considered to be part of them. This is the case with trademark licence agreements – again, the trademark licence must be registered with INAPI in order to be enforceable against third parties.

Moreover, Chilean law permits the appointment of a distributor to be non-exclusive, which means that the principal could appoint several distributors for the same territory. In this regard, organisations should note that parallel imports are permitted and specially provided for by the Industrial Property Law.

Where there is more than one non-exclusive distributor designated for the territory of Chile, distributors should be aware that there would also be a third party interested in importing legitimate goods produced by the principal into Chile. It is advisable that the distribution contract between the principal and the distributor refers to the fact that the principal has or will have the right to sell goods in the territory, by means of a subsidiary. Considering that the principal would also be interested in selling the goods online, either directly or through an intermediate party addressed abroad, the principal would be competing directly with the distributor. It is therefore advisable, but not mandatory, to include in the contract a clause regarding possible compensation for the distributor.

As a rule, it is not compulsory to register a trademark licence agreement in Latin America and the Caribbean region. However, without registration, agreements will have no legal effect

Comment

In-house counsel and licensors must consider local legislation requirements and issues on quality control, registration, royalties and distributions when negotiating and drafting cross-border licensing agreements in Latin America and the Caribbean bloc. The level of local requirements and flexibility varies from jurisdiction to jurisdiction. For example, the laws in Mexico, Guatemala, Honduras, Nicaragua and Costa Rica provide a stricter quality control standard, compared to Colombia, Chile, Uruguay, the Cayman Islands and Panama. As a rule, it is not compulsory to register a trademark licence agreement in Latin America and the Caribbean region. However, without registration, agreements will have no legal effect nor protection against third parties. When it comes to the taxation of royalties, in-house counsel must be aware that the licensee will generally have a withholding obligation at high rates. Parties should consider various tax treaties to reduce the tax rates. Finally, when licensing in Latin America and the Caribbean bloc, it is crucial to implement a strategy that contemplates the governing local laws and how they may affect the agreement. WTR

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