

QUERY : WHAT IS THE MAXIMUM LIMIT OF REMITTANCE WHICH MAY BE REMITTED BY AN INDIAN RESIDENT TO RESIDENT OUTSIDE INDIA FOR ITS IPR ASSIGNMENT FOR USE IN INDIA

Statutes Involved :

1. Foreign Exchange Management Act, 1999
2. Foreign Exchange Management (current account transactions) Rules, 2000; **(The Rules)**
3. Foreign Exchange Management Act (FEMA), 1999 – Current Account Transactions Liberalisation RBI/2004/74 A.P. (DIR Series) Circular No.76 February 24, 2004 **(Notification 1)**
4. Foreign Exchange Management Act (FEMA), 1999 – Current Account Transactions – Liberalisation, RBI/2006-07/190, A.P. (DIR Series) Circular No. 14 November 28, 2006 **(Notification 2)**
5. Press Note 6 of 1992 issued by Ministry of Commerce and Industry **(PN 1)**
6. Press Note 1 of 1995 issued by Ministry of Commerce and Industry **(PN 2)**
7. Press Note 4 of 1996 issued by Ministry of Commerce and Industry **(PN 3)**
8. Press Note 18 of 1997 issued by Ministry of Commerce and Industry **(PN 4)**
9. Press Note 18 of 1998 issued by Ministry of Commerce and Industry **(PN 5)**
10. Press Note 9 of 2000 issued by Ministry of Commerce and Industry **(PN 6)**
11. Press Note 1 of 2001 issued by Ministry of Commerce and Industry **(PN 7)**
12. Press Note 2 of 2003 issued by Ministry of Commerce and Industry **(PN 8)**
13. Press Note 1 of 2005 issued by Ministry of Commerce and Industry **(PN 9)**

Explanation :

1. The FEMA or RBI or the Government of India nowhere defines what could be termed as royalty in respect of transactions under FEMA.
 - a. Interpretation of “Royalty” can be taken from the ruling of Apex Court in the ***State Of H.P. And Ors vs Gujarat Ambuja Cement Ltd. And Anr on 18 July, 2005*** wherein the Court considered its earlier view on interpretation of “royalty” in the case of ***“State of Orissa and Ors. v. Titaghur Paper Mills Co. Ltd. and Anr. [1985] Supp SCC 280”***, it was, inter alia, observed by this Court as follows:

"102. Royalty is not a term used in legal parlance for the price of goods sold. 'Royalty' is defined in Jowitt's Dictionary of English Law, Fifth Edition, Vol. 2, page 1595 as follows: Royalty, a payment reserved by the grantor of a patent, lease of a mine or similar right, and payable proportionately to the use made of the right

by the grantee. It is usually a payment of money, but may be a Payment in kind, that is, of part of the produce of the exercise of the right. Royalty also means a payment which is made to an author or composer by a publisher in respect of each copy of his work which is sold, or to an inventor in respect of each article sold under the patent”.

b. Also, the tax treaty between India and U.k. defines royalty as Definition of “Royalties” in a typical Indian Treaty e.g. Article 13(3) of India-UK Treaty:-

“(a) payments of any kind received as a consideration for the use of, or the right to use, *any copyright of a literary, artistic or scientific work*, including cinematograph films or work on films, tape or other means of reproduction of for use in connection with radio or television broadcasting, any patent, trade mark, design or model, plan, *secret formula or process*, or for information concerning industrial, commercial or scientific experience; and

(b) payments of any kind received as consideration for the use of, or the right to use, any industrial, commercial or scientific equipment, other than income derived by an enterprise of a Contracting State from the operation of ships or aircraft in international traffic”

c. The interpretation includes under its ambit all the intellectual properties under which the payment is made for its use. It does not include outright purchase of IPRs.

2. Chief Provisions issued by the Government of India

i. Trade Mark/ Brand Name :

a. Vide PN 1, use and purchase of trademark/ brand of foreign resident was allowed by the resident India. Prior to the same, an Indian entity could not have used the trade mark/ brand name of nor resident.

b. Vide PN 6, Trade Mark or Brand Name may be used or purchased, without a technology transfer, by an Indian Resident by an assignment or otherwise from a resident outside India under the automatic route with a condition that royalty may be paid only up to the extent of 2 % of export and 1 % of domestic sales.

c. PN 7 provides the procedure as to the calculation of royalty incase use or purchase of trade mark or brand name without technology transfer. It is as follows :

“Royalty on brand name/trade mark shall be paid as a percentage of net sales, viz., gross sales less agents’/dealers’ commission, transport cost, including ocean freight, insurance, duties, taxes and other charges, and cost of raw materials, parts, components imported from the foreign licensor or its subsidiary/affiliated company.”

ii. Royalty of IPRs under Technology Transfer vide technical collaboration agreement

- a. Vide Press Note issued in 1991, Royalty of any IPR with technology transfer is permitted under the automatic route provided the payment of royalty does not exceed 5% on local sales and 8% on exports and lump-sum payment does not exceed US\$2 million (initially it was USD 1 million which was raised up to 2 USD vide PN 3).
- b. Initially there was a time-duration of seven years from the date of commencement of commercial production or ten years from the date of agreement, whichever is earlier, for payment of royalty in case of foreign technology collaboration in case the Indian company is not a wholly owned subsidiary of the foreign company. But vide PN 8, the said restriction was done away with and now no time restriction has been imposed on Indian companies and no condition of foreign equity falls on the Indian company or royalty payment.
- c. Payment mode : Vide PN 4, the Government provided a mode of calculating the royalty as follows :
 - i. The royalty will be calculated on the basis of the net ex-factory sale price of the product exclusive of excise duties minus the cost of the standard bought-out components and landed cost of imported loaf components irrespective of the source of procurement, including ocean freight, insurance, custom duties etc The payment of royalty will be restricted to the licensed capacity plus 25% in excess thereof for such items requiring industrial licensed. In case of production in excess of the quantum, prior approval of Government will have to be obtained regarding the terms of payment of royalty in respect of such excess production.
 - ii. The royalty would not be payable beyond the period of the agreement, if the orders had not been executed during the period of agreement. However, where the order has been booked during the period of agreement, but executed after the period of agreement, royalty would be payable only after the Chartered Accountant Certifies that the orders in fact have been firmly booked and execution began during the period

of agreement and the technical assistance was available on a continuing basis even after the period of agreement.

iii. The lumpsum shall be paid in three installments detailed below unless otherwise stipulated in the approval letter - First 1/3rd after the agreement is filed with Reserve Bank of India, Authorised Foreign Exchange Dealer; Second 1/3rd on delivery of technical documentation; Third and final 1/3rd on commencement of commercial production of four years after the agreement is filed with RBI/Authorised Foreign Exchange Dealer, whichever is earlier. The lumpsum can be paid in more than three installments subject to completion of the activities as specified above.

iii. Hotel Industry:

Vide Press note 18 of 1991, separate guidelines had been issued in respect of hotel industry for automatic approval of foreign technical collaboration. Again in the PN 2, the same were got amended which is as follows:

(i) Technical and Consultancy Services including Fees for Architect, Design, Supervision, etc. -Upto 3% of the capital cost of the project (less cost of land and finance).

(ii) Financing and Marketing/Publicity Support Fee: Upto 3% of net turnover (Net turnover is gross receipts less credit card charges, travel agents' commission, sales tax, statutory payments, etc.)

(iii) Management Fees (including incentive Fee): Upto 10% of gross operating profit.

(iv) The above norms are applicable provided, the collaboration is proposed with companies running/ managing hotel (s) with at least 500 rooms.

iv. Previous ventures or Tie ups

a. Vide PN 5, it was instructed that if any previous joint venture or tie up has been held in terms of technology collaboration or trade mark/brand name, the said non resident can not enter into any kind of similar or allied collaboration without prior approval of the FIPB.

b. Again vide PN 9, the Government amended the earlier provisions which reads as follows :

i) Prior approval of the Government would be required only in cases where the foreign investor has an existing joint venture or technology transfer/trademark agreement in the 'same' field. The onus to provide requisite justification as also proof to the satisfaction of the Government that the new proposal would or would not in any way jeopardize the interests of the existing joint venture or technology/ trademark partner or other stakeholders would lie equally on the foreign investor/ technology supplier and the Indian partner.

Even in cases where the foreign investor has a joint venture or technology transfer/ trademark agreement in the 'same' field prior approval of the Government will not be required in the following cases:

- (a)** Investments to be made by Venture Capital Funds registered with the Security and Exchange Board of India (SEBI); or
- (b)** where in the existing joint-venture investment by either of the parties is less than 3%; or
- (c)** where the existing venture/ collaboration is defunct or sick. In so far as joint ventures to be entered into after the date of this Press Note are concerned, the joint venture agreement may embody a 'conflict of interest' clause to safeguard the interests of joint venture partners in the event of one of the partners desiring to set up another joint venture or a wholly owned subsidiary in the 'same' field of economic activity. These guidelines would come into force with immediate effect.

3. Provisions issued by RBI following the Press Notes issued by the Government of India

i. Remittance of royalty for IPR falls under Current Account Transaction under FEMA.

The rules for the same have been prescribed under the Rules.

- a. Article 8 of the Schedule II says that Remittances under technical collaboration agreements where payment of royalty exceeds 5% on local sales and 8% on exports and lump-sum payment exceeds US\$2 million, prior approval of Ministry of Commerce & Industry is necessary in this regard.
- b. Again Article 16 of the Schedule III says that Remittances for use and / or purchase of trade mark / franchise in India needs prior approval of RBI. But it is pertinent to note that by a **Notification No 2** RBI has done away with this condition and now no permission is required for getting into purchase or use of trade mark or franchise.

Conclusion :

At present the royalty against IPR along with technology transfer can be remitted up to 8 % of export and 5 % of domestic sale without any time limitation of time wherein the lump sum amount does not exceed USD 2 ml under automatic route and if it exceeds the limit, approval from Ministry of Industry and Commerce is to be compulsorily taken.

In case of use or purchase of trademark or brand name without technology transfer, under automatic approval, the royalty against the same is permitted up to 2 % of export and 1 % of domestic sale subject to maximum ceiling of USD 2 ml as the permissible limit of remittance under current account transaction is USD 2 ml.