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Changes in the Treatment of Trademark Royalties in EU Customs Law: The Example of 3D Printing*

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A careful comparison of the legal framework of trademark royalties for 3D printed objects such as lamps under the Community Customs Code and the Union Customs Code confirms that trademark royalties will become dutiable under the new EU Customs Law regime. The new regime achieves legal certainty, but at a price for importers.

I INTRODUCTION

The situation is as follows: a 3D printer produces trademark-protected lamps ('lamps') in the US.¹ The shape and the logo of the lamps are designed with computer-aided design technology in Hong Kong and saved as a model file that is sent to the 3D printer for production.² The manufacturer sells the lamps to an EU buyer ('importer') and grants the importer ('licensee') the right to resell the lamps on the condition that the licensee pays a trademark license fee ('trademark royalties'). Upon import into the EU, these lamps are subject to customs duties.³

This article evaluates whether trademark royalties must be included in the transaction value for customs valuation purposes. In other words, are trademark royalties for 3D printing dutiable under EU Customs Law? In order to answer that question, we will compare the Community Customs Code ('CCC' or 'current EU customs law regime') and its implementing provisions, which apply until 1 May 2016, with the Union Customs Code ('UCC' or 'new EU customs law regime') and the consolidated preliminary

draft of the UCC Implementing Act ('UCC Implementing Act'), which will apply as from 1 May 2016.⁴

Based on that comparison, we conclude that trademark royalties for 3D printed objects such as lamps will become dutiable under the UCC. This was not necessarily the case under the CCC.

2 A NOTE ON THE SCOPE

This article does not attempt to cover all possible situations in which sales or royalties agreements foresee the payment of royalties by the licensee. A case-by-case analysis would be necessary in that regard. This is because, under EU customs law, royalties cover payment for:

- the use of rights relating to the manufacture of imported goods, e.g., patents, designs, models and manufacturing know-how;
- the sale for exportation of imported goods, e.g., trademarks and registered designs; and

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* The views expressed in this article are exclusively those of the authors and do not necessarily reflect those of Sidley Austin LLP nor its partners. This article has been prepared for academic purposes only and does not constitute legal advice.

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¹ The 3D printed objects could also be T-shirts and dolls, to name but a few.

² M. Weinberg, *It Will Be Awesome If They Don't Screw It Up: 3D Printing, Intellectual Property, and the Fight Over the Next Great Disruptive Technology*, Pub. Knowledge (November 2010); R. Janssen, I. Blanckers, E. Moolenburgh & B. Posthumus, *TNO: the Impact of 3-D Printing on Supply Chain Management* (April 2014); I. Silverman, *3D Printing, Challenges for the Fashion Industry*, PLC Mag. (December 2013).

³ The CN code of the lamps is 9405 and a conventional rate of duty applies; 2.7%, 3.7% or 4.7% depending on the material.

⁴ On 13 Jan. 2014, the EU issued the Union Customs Code Implementing Act, which, if enacted in its current form, will make royalty payments of goods imported into the EU dutiable under EU customs law.

- the use or resale of imported goods, e.g., copyright and manufacturing processes inseparably embodied in the imported goods.⁵

In addition, while focusing our analysis on the CCC and the UCC, we will also refer to Article 8.1 sub c of the WTO Customs Valuation Agreement, and to Commentaries 11 and 25.1 of the World Customs Organization Technical Committee on Customs Valuation ('WCO Technical Committee').⁶

3 THE DUTIABILITY OF TRADEMARK ROYALTIES FOR 3D PRINTING UNDER EU CUSTOMS LAW

For the purposes of analysing the dutiability of trademark royalties, 3D printing is a good example because it is a technology advancing at astonishing speeds. 3D printing is a revolutionary process that deserves full attention.⁷ So, under which conditions are trademark royalties for 3D printed objects such as lamps dutiable under the CCC and the UCC?

3.1 The Dutiability of Trademark Royalties for 3D Printed Lamps under the Current EU Customs Law Regime

According to Articles 32(1)(c) and 32(5)(b) of the CCC and Article 157(2) of the CCC implementing provisions, trademark royalties must fulfil two cumulative conditions in order to be dutiable: first, trademark royalties must relate to imported lamps and, additionally, trademark royalties must constitute a condition of sale of the lamps.⁸

Concerning the first condition, the question is: why are trademark royalties paid in the first place? One answer can be found in Commentary 25.1 of the WCO Technical Committee, which states:

The most common circumstances in which a royalty or licence fee may be considered to relate to the goods being valued is when the imported goods incorporate the intellectual property and/or are manufactured using the intellectual property covered by the licence. For example, if the imported goods incorporate the trademark for which the royalty or licence fee is paid,

this would indicate that the fee relates to the imported goods.

In our example, trademark royalties are paid by the licensee because the imported lamps and the trademark covering the lamps are intertwined. More specifically, the payment of trademark royalties is considered to be related to the lamps when the lamps are resold to a third party. The tangible (lamps) cannot be purchased without the purchase of the intangible (trademark).

Concerning the second condition, the question is: would the manufacturer be prepared to sell the lamps without the payment of trademark royalties? This is the theory of 'separability'.⁹ No general answer can be provided to such a question. A careful review of all the facts surrounding the sale should be conducted.

In determining whether trademark royalties are a condition of sale of the lamps, one can take into account the text of the sales or royalties agreements:

- reference to royalties in the sales agreement;
- reference to the sale of the lamps in the royalties agreement;
- stated terms of the sales or royalties agreements;
- reference of termination of the sales agreement as a consequence of breaching the royalties agreement because the licensee does not pay the trademark royalties to the licensor.¹⁰

Nevertheless, according to Commentary 11 of the WCO Technical Committee, the terms of the sales or royalties agreements do not imply as such that the payment of trademark royalties is a condition of sale, especially if the importer has a genuine choice about whether to take the lamps with or without trademark. More than the wording of the sales and royalties agreements, it is the margin of discretion of the importer that should be examined. As a consequence, the determining factor is that the seller must have required the buyer to make that payment (leaving the importer no discretion).

The existence of this *requirement* can be proven in several ways. First, if the manufacturer or licensor explicitly make the sale of the lamps conditional on the payment of trademark royalties, then the payment is without any doubt *required* and thus a condition of sale. On the

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⁵ Article 157 of the CCCIP.

⁶ Commentary 11 of the Customs Code Committee (customs valuation section) on the application of Art. 32(1)(c) CCC in relation to royalties and license fees paid to a third party according to Art. 160 of Regulation (EEC) 2454/93; Commentary 25.1 of the Customs Code Committee about third-party royalties and license fees.

⁷ *The Shape of Things to Come: 3D Printing*, World Intell. Prop. Rev. (1 May 2013).

⁸ This provision is the implementation of Art. 8(1)(c) of the Agreement on Implementation of Art. VII of the General Agreement on Tariffs and Trade 1994 ('WTO Customs Valuation Agreement').

⁹ S. Sherman & H. Glashoff, *Customs Valuation: Commentary on the GATT Customs Valuation Code* 131 (Kluwer 1988).

¹⁰ M. Lux, D. Cannistra & M.A. Rodriguez Cuadros, *The Customs Treatment of Royalties and License Fees with Regard to Imported Goods*, 7 Global Trade & Cust. J. 127 (2012).

contrary, if the importer has the option to purchase the lamps without being required to pay the trademark royalties, then the royalty payment should not be considered as a condition of sale.

Second, if royalties are not paid to the manufacturer, but rather to a third party (e.g., a licensor that is not related to the manufacturer), *the manufacturer must require the importer to pay the trademark royalties* in order for them to be dutiable (included in the customs value). As a result, in this case, many royalties are not considered dutiable and are thus excluded from the customs value.

Third, if one member of a multinational group sells lamps to another member of the same group, and *requires* that member to pay trademark royalties, this also proves that the payment of trademark royalties is a condition of sale, compare Commentary 25.1 of the WCO Technical Committee.

Under the CCC, once the two above conditions are met, the trademark royalties must be added to the transaction value and they are dutiable as such. Under Article 8.1 sub c and 8.3 of the WTO Customs Valuation Agreement, the two conditions are supplemented by three additional ones:

- the royalties should be paid by the importer, either directly or indirectly;
- the royalties must not be already included in the transaction; and
- the adjustment of the transaction while including trademark royalties should be done on the basis of objective and quantifiable data.

3.2 The Dutiability of Trademark Royalties for 3D Printed Lamps under the New EU Customs Law Regime

According to Article 230-11 of the UCC Implementing Act, the trademark royalties must still fulfil the above two conditions from the CCC in order for the lamps to be dutiable. First, trademark royalties must be related to the lamps, particularly when the trademark transferred under the royalties agreement is embodied in the lamps. There may also be no evidence to the contrary. Second, trademark royalties must constitute a condition of sale for the imported lamps.

Under the UCC, this second condition is met in three different situations:

- (1) the manufacturer or person related to the manufacturer requires the importer to make this payment;

This provision wisely implements Commentary 11 of the WCO Technical Committee, defining trademark royalties as a condition of sale based on whether the seller has made payment of those royalties a *requirement* for the importer.

- (2) the payment by the importer is made to satisfy an obligation of the manufacturer, in accordance with contractual obligations;

The terms of the sales or royalties agreements still continue to be relevant factors for the examination of the condition of sale. But note that the provision refers to ‘contractual obligations’. This term is quite vague. It does not specify the party (manufacturer, licensor and licensee) or the type of agreement (sales or royalties agreement). This ‘contractual obligations’ term could thus be subject to debate and challenged by importers before national customs authorities.

- (3) the lamps cannot be sold to, or purchased by the importer without payment of the royalties to a licensor.

Here the UCC departs from the current EU customs law regime in a way that is particularly burdensome for importers: the ‘condition of sale’ determination has been broadened. In the absence of situations (1) and (2) above, which are applicable under the CCC, the ‘condition of sale’ condition can now be met simply if the importer cannot obtain the lamps without paying trademark royalties for them. There need not be a *requirement* imposed on the importer by the manufacturer to pay royalties. For instance, if the licensor is not related to the manufacturer and the importer, the trademark royalties will be dutiable. This means that trademark royalties will become dutiable and will be included in the transaction in nearly all situations. This clause can be qualified as catch-all. Even if this provision is still a draft, it is likely that the Member States will adopt it.

This provision has the advantage of enumerating three situations in which the condition of sale is considered as fulfilled. It guarantees legal certainty. Nevertheless, the special requirements for the inclusion of trademark royalties in the transaction value have been removed in the new EU customs law regime. Moreover, the range of application has been extended because only general conditions for an inclusion must be fulfilled.

4 CONCLUSION

To summarize, the trademark royalties for 3D printed objects such as lamps will become dutiable under the new EU customs law regime because the scope of the ‘condition of sale’ has been extended. For trademark royalties to be dutiable, the manufacturer does not need to require the importer to pay them. The simple fact that the importer must pay them if he wants to resell the lamps is now sufficient. If an importer of lamps wanted a national customs authority not to include trademark royalties in the transaction value of the lamps, it would now need to demonstrate that the payment of trademark royalties is not related to the lamps.

This highlights the fact that legal certainty can cost importers money. It also represents a missed opportunity to foster trade. Indeed, as a consequence of this change, the import of 3D products into the EU may well decrease. Probably, importers will avoid importing lamps. Instead, they will buy the 3D model file containing the shape and the logo of the lamps and 3D print the lamps in the EU. Such an approach means that the lamps will not

be subject to customs duties because of the lack of border control from customs authorities. The only trademark royalties paid by the importer would be for the upload of the 3D model file. Should this scenario unfold, the EU may want to review EU customs law, may need to be substantially reviewed in order to keep pace with the development of new technologies such as 3D printing.