# Pitfall for buyers of Chinese trademarks

## Description

Here is the story:

A foreign investor wishes to buy a Chinese local brand in respect of certain products falling within Class A, and at the time of executing the trademark transfer agreement, the seller doesn't disclose that he has a very similar trademark in Class B products which are similar products with those in Class A. After partial payment of the sale price, the buyer tries to effect the title transfer of the trademark with trademark office in Beijing. It is later informed that because there is a similar trademark in similar products, the trademark transfer cannot go through unless the similar trademark is transferred to the buyer at the same time. Now the buyer turns back to the seller negotiating the sale of similar marks, which is always difficult to attain the goal at reasonable cost. The seller is of course ready to take advantage of the catch-22 situation on the part of the buyer.

The problem is not rare in practice and in some cases involving Sino-foreign joint venture projects, the trademark is the key asset both parties will spare no efforts to fight for.

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This problem stems from the provision of Chinese trademark law and regulations. Article of 42 of China Trademark Law provides in its second paragraph:

> where a registered trademark is being transferred, the similar mark(s) registered by the registrant on the same products and the identical or similar marks registered on the similar products shall be transferred all together.

At the same time, the Implementation Rules for China Trademark Law provides in its Article 32:

> where a registered trademark is being transferred, the same or similar mark(s) registered by the registrant on the same or similar products shall be transferred all together, failing which the trademark office shall extend a period for correction thereof; in case correction is not made upon expiration the said extended period, it shall be deemed that the application for transfer of the trademark is forsaken, and the trademark office shall give notice thereof in writing to the applicant.

Due to this rule, China trademark office will always reject the application for trademark transfer once it finds that a similar trademark is not being transferred together.

Here comes the question to the buyer: what shall I do now if the seller is not willing to transfer the similar trademarks on reasonable terms?

There is no easy and ready answer for the buyer as the courts are actually divided on how to treat the sale contract in which the similar marks are not drew along.

## I. What About the Validity of the Trademark Sale Contract

The question that shall be answered in the first place is whether the trademark sale contract is still valid given that it goes against the above-cited provision in China Trademark Law. There is a view to the effect that the provision is a compulsory one in violation of which the sale contract in point shall be void. However, the majority opinion is that the sale contract shall be maintained valid.

China Supreme Court has classified compulsory provisions under Chinese laws into two classes: administrative compulsory rules, and effectual compulsory rules (the latter referring to rules “directly impacting the validity of the contract in question”). This cited rule is provided *per se* to regulate the administrative conducts of the trade mark office, mandating the office to reject application for trademark transfer in breach of this rule, and the rule itself does not say the mark transfer contract will be void and instead, the implementation rule simply provides for an extended period for applicant to make up for the failure. So the direct consequence of violating this rule is that the trademark transfer will be stopped and in other words, the transfer contract cannot be performed or the purpose of the contract is frustrated.

So in essence, the rule is administrative in nature, and  it shall not affect or annul the trademark transfer contract altogether.

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## II. What Remedies the Buyer Have under Chinese Laws

Unless the seller is willing to sell the similar trademarks to the buyer, or the trademark assignment contract is well written allowing the buyer to drag along those similar trademarks with the current sale, the buyer is left with nothing but to terminate the contract and claim for damages to compensate for its loss pursuant to the terms of the assignment contract in question.

Under current Chinese laws, courts are very conservative to award huge damages to non-defaulting party to a contract. It is definitely a big challenge for the buyer to seek satisfactory compensation from Chinese courts.

Because of the barrier of similar trademarks standing in the way, it is unlikely that courts will enforce the trademark transfer contract against the decision made by the trademark office. There have been attempts by buyers to sue for real performance of the trademark assignment contract, but unsuccessful.

In another arbitration case, we see the buyer sue to have the similar marks removed off the register so as to pave the way for the trademark transfer which is indeed mistaken in understanding the laws.

## III.  Lesson Trademark Buyers Should Learn from Story

The pitfall described above must be bore in mind when buyers purchase registered trademarks in China. The best way and the only effective way to fend off the risk is to write your trademark transfer contract air-tight, giving sufficient attention to the possible problems arising related to the similar trademarks.

Not only does the contract need to contain representation, warranties or undertaking to the effect that the seller does not have and will not register similar trademarks at the time of execution of the trademark transfer contract and during the process of effecting title transfer in the trademark, but also

the contract shall have clauses explicitly affording remedies to the buyers once similar trademarks are found down the road  making sure the buyers can then enforce the contract.

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