



ARTICLE

Taxation of Trademark Transactions

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Abstract

In a global scenario like today, businesses want to have a lasting and long-term impact in the competitive market and for this, the trademark or brandmark plays a very significant role to help the consumer to identify the products. All the commercial brands use a mark which distinguishes their product from those of others. The provisions regarding trade marks are given under the Trade marks Act, 1999. A brand's goodwill is also associated with this brandmark or trademark. In this paper, the author deals with a set of circumstances where there is a transfer of this trademark and tax is imposed under the Income Tax Act upon this trade. The research is divided into three parts. The first part deals with the meaning and definition of 'trademark' and explains the methods which are used for the valuation of intangible assets such as trade mark. The methods dealt with here align themselves with different factors which play an important role in assessing the value of any non-physical/intangible asset. It mainly harmonises the various factors affecting the worth of the asset with the market forces. The second part describes how the provisions under the Income Tax Act will be applicable to the trade of trade mark and the discussion ranges from income tax provisions related to long-term capital assets to short-term capital assets and the formulas applicable therein while calculating tax applicable to assets under these categories. The last part deals with the modes of transfer of the trademark and computation of tax payable under different modes integrating the types of assets with the modes of transfer.

Keywords - Taxation, Trademark, Trade, Valuation, Capital Gains, Assignment and Licencing

I. INTRODUCTION

The term "Trademark" is defined under section 2(1)(zb) of the Trade Marks Act, 1999 as "*a mark capable of being represented graphically and capable of distinguishing the goods or services of one person from those of others and may include shape of goods, their packaging and combination of colours*". The Act further states that "*unless the context otherwise requires, any reference to trade mark shall include reference to collective mark and certification trademark.*"³⁶² Trademark is an exclusive right hold by the registered trademark owner and considered as an intangible asset of priceless nature. The exclusive right grants the monopoly right to the owner alone to use the mark for the goods and services attached to it. Trademark is considered as a priceless intangible asset of a high economic value as it creates goodwill for a business or organisation.

Trademark being one of the intellectual properties, bears the feature of being sold and the capacity lies with the registered trademark owner to transfer the same to a third-party, just like transfer of any tangible property. Therefore, it can be said that trademark can be transferred, sold, pledged, or assigned to an interested third-party but it is equally important that the value of the mark is decided accordingly.

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³⁶² Trade Marks Act, 1999, s 2(2)(a)

II. TRADEMARK VALUATION

The feature of trademark of being sold can only be utilised when the true value of the mark is ascertained. Trademark is an intangible asset according to International Glossary of Business Valuation Terms herein after referred as IGBVT. It is an inclusive definition which says that “*Intangible Assets are Non-physical assets such as franchises, trademarks, patents, copyrights, goodwill, equities, mineral rights, securities and contracts that grant rights and privileges, and have value for the owner.*”³⁶³ Further Accounting Standard 26 defines Intangible Asset as “*Identifiable non-pecuniary asset, without physical significance, held for use in the production or manufacturing or supply of goods or services, for the purpose of rent to others, or for administrative purposes.*” Since intangible assets lacks the physical feature, it can be classified in two categories as identifiable asset and unidentifiable asset. The identifiable asset includes intellectual properties like trademark, copyright, patent, customer relationship, and contracts. The legal rights are attached to identifiable assets and have the feature of being assigned or sold or transferred or licensed to a third-party. Therefore, it can be separated from the business without making any alteration to the ongoing business. This very nature of identifiable asset makes it a definite asset because the end of this asset is foreseeable either by a legal agreement or by the end of period assigned to exploit the intellectual property. In the latter category of intangible assets there is skilled management, work force and work place are included which provides enhancement to the enterprise and therefore it cannot be sold separately.³⁶⁴

There are mainly three primary approaches to decide the value of an intangible asset. The value of the asset differs on the fact that whether it is an integral part of the process in which the intangible asset is involved. Since trademarks associated with the goodwill of any organisation, holds important legal rights to the organisation, the approaches for the valuation of Trademarks will include Market Approach, Income Approach and Cost Approach.

Market Approach

As the name suggests, the valuation method under market approach analyse and compares the value of trademark having similar feature at the present market to arrive at a value of the trademark. The market approach includes many elements while considering the value of any intangible assets as:

- Sales comparison method based on actual sales.
- Comparable profit margin method from the comparison of different companies dealing with similar services or goods that have been licensed or sold or transferred through a different method.
- The relief from the royalty method based on the comparison of actual licenses.³⁶⁵

The value is calculated using a fake royalty rate that one may get by owning the object, and the market and income techniques are contrasted with the royalty strategy. Here, the ownership implies that the business need not to pay for the use of the asset.

The sales comparison method and relief from the royalty method is based on the comparable uncontrolled transaction method hereinafter referred to as CUT of an intangible asset. While

³⁶³ Glossary MLB, <<https://www.mlb.com/glossary>> accessed 18 March 2025

³⁶⁴ Valentiam Group, ‘Valuation of intangible assets: What are the top methods’(15 April 2021) <<https://www.valentiam.com/newsandinsights/intangible-assets-valuation-methods>> accessed 18 March 2025

³⁶⁵ Aaron M. Rotkowski and Robert F. Reilly, ‘Market approach methods for intangible asset property tax valuation’ (2014) Spring_2014, <https://willamette.com/insights_journal/14/spring_2014_1.pdf> accessed 21 March 2025

applying the CUT method, the analyst considers some of the basic elements of comparison. These are as follows:

- The legal rights attached to the intangible asset
- The industry to which the intangible asset currently belongs or to the industry in which it will be used
- The intangible asset's term and the remaining time left on the sale or licence deed
- The geographical or territorial characteristics of licence or sale

These elements are generally compared between the CUT intangible asset and the taxpayer intangible asset. In this approach the data used by the analyst is mainly the publicly traded data which represents a market capitalisation of the enterprise as a whole and not only the intangible assets.

Income Approach

This is the most common approach to determine the value of any intangible asset. This method comes into picture in a situation when the asset is income producing or generating a cashflow. By extrapolating the asset's future value throughout the span of the remaining duration based on the present value, an estimate cost is created using this approach. The most common methods under the income approach are Multi-Period Excess Earning, Avoided Loss of Income and Greenfield methods.

The Multi-Period Excess Earning Method (MPEEM) isolates the excess cash flows generated by a single intangible asset and the expenses are deducted for cash flow which is associated with other assets³⁶⁶. As a result, the fair market value is determined by applying a present value discount. The deductions which are made to the earning stream for the use of other asset is known as complimentary asset charge including payment for working capital, tangible asset, and other intangible asset.³⁶⁷ The method of MPEEM is applied only in the case when the cash flow from the primary asset can be separated from the overall cash flow of the firm. This method is frequently applicable to customer relationship, vendor relationship, Intellectual Property Right, computer software and Licences etc.³⁶⁸

The contribution of with and without method in income approach is that it determines the value of an asset by comparing two discounted cash flow models. In one model it is assumed that the present cash flows of the firm are only through the ownership of subject asset and in the other model it is assumed that there is no existence of the subject asset. In the latter model, the loss of the intangible asset may lead to a loss or increased expenses or reduction to revenue of the firm. By these two scenarios the value of subject asset is determined. This method is applicable in licensing agreement, non-competing agreement, and supply agreement.³⁶⁹

The greenfield method works on the presumption that the firm owns only one asset and that is the subject asset as the business is a start-up business. The valuation professional or analyst is

³⁶⁶ Antonella Puca and Mark L. Zyla, 'The Intangible Valuation Renaissance: Five Methods' (CFA Institute, 11 January 2019) <<https://blogs.cfainstitute.org/investor/2019/01/11/a-renaissance-in-intangible-valuation-five-methods/>> accessed 25 March 2025

³⁶⁷ Paul Vogt, 'The Power of Intangibles: Unravelling the Mystery of Asset Valuation with MPEEM' (PCE Companies, 18 January 2025) <<https://www.pcecompanies.com/resources/using-the-multi-period-excess-earnings-method-to-value-your-companys-primary-asset>> accessed 26 March 2025

³⁶⁸ Shockwave Corporation, 'Illustrative Example of Intangible Asset Valuation', OECD TP WP6, <<https://www.oecd.org/tax/transfer-pricing/47426115.pdf>> accessed 13 April 2025

³⁶⁹ E. Anastasio, 'Valuation of Intangible Assets' [2020] PL 3

required to contemplate cash flows which is needed to build the infrastructure required for the business. Therefore, the firm must make investment, either through the purchase of asset or through the incurred losses for the utilization of the intangible asset.³⁷⁰ At the end there is a discounted income to its present value using an appropriate discount rate. This method is generally applicable to non-primary income generating assets as licences and permits, rights, and franchise agreement.

Cost Approach

The cost approach method works under the doctrine of substitution. It determines the value of the intangible asset by assuming the amount required to replace the service provided by the subject asset by creating a new similar asset.³⁷¹ Therefore, the approach is only considered when the subject asset is replaceable and not in a situation when it is original, such as patents or trademark, which are registered for its novelty or uniqueness and not in a position to be recreated. The whole approach work on the idea that a prospective investor or buyer will not pay any extra cost than the cost required to produce the substitute asset. While calculating the value of an asset, the deterioration or perishing made to it, is deducted from the total amount but this is not done in the case of non-physical assets, as it does not gets deteriorated with time or due to overuse.³⁷² This approach is commonly applicable to licences, certification, internally generated software, and workforce.³⁷³

III. TRADEMARK AND TAXATION LAWS

According to Section 2(24) of the Income Tax Act, 1961, a person is liable to pay tax on the income for any estimated year at any rate or rates decide by the Central Act.³⁷⁴ Here, ‘income’³⁷⁵ includes profits and gains; dividend; or any capital gain taxable under Section 45 etc. The term ‘person’³⁷⁶ includes an individual; a Hindu undivided family (hereinafter referred to as HUF); a company or a firm; any association of persons or a body of individuals, immaterial of incorporation; a local authority; and every artificial juridical person.

According to sub section (3) of Section 45, the profits or gains arising from the conveying of any capital asset by one person to a firm, or other association of persons, or body of individuals (not being a company or a co-operative society), through capital contribution or otherwise, shall be chargeable to tax as his income of the previous year in which such transfer takes place and, for this purposes the full value of consideration is the amount recorded in the book of account of the organisation as received or accruing in that year i.e., the amount recorded in the balance sheet.³⁷⁷ Since intangible asset or properties like that of goodwill³⁷⁸, patent etc., are treated as capital asset under Section 2(14) of the Act, the transfer of the same can be contemplated as capital gain to

³⁷⁰ IBBI, <<https://schoolofvaluation.com/understand-valuation-of-intangible-assets-for-ibbi-exam/>> accessed 18 April 2025

³⁷¹ PK Chopra & Co., ‘Valuation on intangible assets’ (TaxGuru, 25 February 2021) <<https://taxguru.in/income-tax/valuation-intangible-assets.html>> accessed 20 April 2025

³⁷² CGMA, ‘Three approaches to valuing intangible assets’ (2012)

<<https://www.cgma.org/content/dam/cgma/resources/tools/downloadabledocuments/valuing-intangible-assets.pdf>> accessed 20 April 2025

³⁷³ Supra note 7

³⁷⁴ Income Tax Act 1995, s 4

³⁷⁵ Income Tax Act 1995, s 2(24)

³⁷⁶ Income Tax Act 1995, s 2(31)

³⁷⁷ Income Tax Act 1995, s 48

³⁷⁸ Devidas Vithaldas v C.I.T., 1972 Tax. L.R. 971 (S.C.)

the purchaser and hence taxable. This view is supported by the Supreme Court judgment in *S.C. Cambatta and Co. P. Limited vs Commissioner of Excess Profit Tax*³⁷⁹, where it was held that the payment for goodwill or patent right is a capital receipt and therefore the profit arising out of it will be subject to taxation as capital gains. Another judgment in this reference is *Commissioner of Income Tax vs Medieval World Publication Pvt Ltd*³⁸⁰, the High Court of Delhi here held that the profit resulting from the transfer of any form of intangible asset or properties, i.e., trademark, copyright, and patent, is in the nature of capital gains and not business income hence taxable.

TYPES OF CAPITAL ASSETS

a. Short-term Capital Assets –

In India, assets possessed by an individual or a company for a duration of less than 36 months are commonly referred to as short-term capital assets. These assets consist of, among other things, investments that are bought and sold quickly, such as stocks, bonds, mutual funds, and other financial assets. Short-term capital gains or losses are any earnings or losses that are incurred when a person or company auctions a short-term capital asset in India. Taxes on long-term capital gains are higher than those on short-term capital gains. Short-term capital gains on publicly traded stock shares and equity-oriented mutual funds will be subject to a 15% tax as of the upcoming fiscal year, 2021-2022, while non-equity assets are subject to the equivalent income tax slab rate for the taxpayer.

b. Long-term Capital Assets –

Stocks, bonds, mutual funds, and other kinds of long-term investments owned by an individual or business for more than 36 months are referred to as long-term capital assets. Any profits or losses incurred upon the sale of a long-term capital asset in India can be referred to as long-term capital gains or losses. Long-term capital gains are not charged as high of taxation as short-term capital gains. For any income or profits exceeding Rs. 1 lakh in the financial year 2021–2022, long-term capital gains on listed equity shares and equities-oriented mutual funds are taxed at 10%, whilst non-equity assets are subjected to a 20% after-indexation tax.

Transfer of Trademark

“Transfer”³⁸¹ in respect of capital asset according to Income Tax Act includes sale, exchange, or relinquishment of the asset; or Extinguishment of any right which subsist in the property³⁸² etc. This transfer does not include³⁸³ any distribution of capital asset in total or partial partition of HUF; or any conveying of capital asset by way of a gift or will; or any transfer from the primary company to its secondary company etc.

IV. MODES OF TRANSFER OF TRADEMARK

1. Assignment of trademark

A trademark or brandmark can be transferred through assignment or transmission. As per Section 2(1)(b), “Assignment means assignment in writing by act of parties concerned.” Similarly,

³⁷⁹ S.C. Cambatta and Co. P. Limited v Commissioner of Excess Profit Tax, 1968 68 ITR 463 Bom

³⁸⁰ Commissioner of Income Tax v M/S Mediworld Publications Pvt. Ltd., MANU/DE/1010/2011

³⁸¹ Income Tax Act 1995, s 2(47)

³⁸² James Anderson v C.I.T., (1960) 39 I.T.R. 123 (S.C.)

³⁸³ Income Tax Act 1995, s 47

*“transmission means transmission by operation of law, devolution on the personal representative of a deceased person and any other mode of transfer, not being assignment.”*³⁸⁴ Assignment can be defined as a process through which the owner’s right, interest and title in a trademark and a brandmark is transferred.³⁸⁵ Assignment can be done in different manners as in complete assignment where the complete rights are transferred to second party for the registered trademark and here the owner derives royalty after selling the trademark. If there is a partial assignment, the transfer will take place in a piecemeal fashion, meaning that only the rights to a subset of the agreed-upon goods and services will be transferred. Transfer of trademark with goodwill deals with the situation where the owner transfers the value associated with the trademark in addition with the rights of the trademark. Therefore, the transferee can use the same mark concerning the goods or services in which the transferor was indulged. Even if there is no goodwill involved in the assignment, the transferee is nevertheless prohibited from using the mark on products or services that the transferor is already utilising. Therefore, transmission and assignment refer to transfer of the long-term capital asset.

The computation of the capital gains can be done by calculating the total value of consideration received as a result of transfer while making the deduction in the expenditure incurred solely in connection with the transfer and the cost of acquisition of the intangible asset with addition to any improvement cost thereto.³⁸⁶ Generally "cost of any improvement" in case of acquisition by the assessee from the previous owner means the purchaser cost but according to section 55(1)(b) this cost in relation to a capital asset being goodwill of a business shall be taken to be nil. Therefore, the formula for computation of capital gains will be as follows:

Full value of consideration - expenditure incurred wholly and exclusively in connection with transfer of capital asset – indexed cost of acquisition

Further, the government has notified certain factors for consideration during computation of cost of acquisition and these includes:

- Year of acquisition and cost inflation index of that year
- Year of transfer and cost inflation index of that year

Therefore, the formula for computation of indexed cost of acquisition will be:

The cost inflation index of the particular year of transfer of the capital asset is multiplied by the entire cost of acquisition, and the product of these two is divided by the cost inflation index of the specific year of acquisition. This method is described below:

Step 1: Cost of acquisition × Cost inflation index of the year of transfer of capital asset

Step 2: Resultant of Step 1

$\frac{\text{Resultant of Step 1}}{\text{Cost inflation index of the year of acquisition}}$ ³⁸⁷

Generally, the long-term capital gains are taxed at 20% rate (including surcharge and cess as applicable) but in certain cases, the capital gains may be charged at 10% rate (including surcharge as applicable). This benefit is available only in the following cases:

³⁸⁴ Trade Marks Act 1999, s 2(1)(zc)

³⁸⁵ Trade Marks Act 1999, s 37

³⁸⁶ Income Tax Act 1995, s 48

³⁸⁷ Income Tax Department, Tax on long-term capital gains, page 6

- Where the long-term gains are arising out of the sale of listed securities as defined under Section 2(h) of the Securities Contract (Regulations) Act, 1956 and the amount exceeds Rs. 1,00,000;³⁸⁸
- Long-term capital gains resulting from the transfer of any security listed on an acknowledged Indian stock exchange, or any mutual fund or UTI unit; or zero coupons bonds.

2. *Licencing of Trademark:*

By licencing of trademark, it could possibly mean the permission granted by the proprietor or owner of the mark to the third person to use that mark with or without conditions or restrictions. According to the Trademarks Act of 1999, authorization is given to all registered users as well as to any third party with the registered proprietor's written approval³⁸⁹. The term 'permitted use'³⁹⁰ is defined as "*the use of trademark*

(i) *by any registered user of the trade mark in relation to goods or services—*

- a) with which he is connected during trade; and*
- b) in respect of which the trade mark remains registered for the time being; and*
- c) for which he is registered as registered user; and*
- d) which complies with any conditions or limitations to which the registration of registered user is subject; or*

(ii) *by a person other than the registered proprietor and registered user in relation to goods or services—*

- a) with which he is connected during trade; and*
- b) in respect of which the trade mark remains registered for the time being; and*
- c) by consent of such registered proprietor in a written agreement; and*
- d) which complies with any conditions or limitations to which such user is subject and to which the registration of the trade mark is subject"*

The income generated from the licencing of trademark can be subjected to tax under two heads:

- Profits and gains from business and profession (PGBP)
- Income from other sources (IoS)

The profits and gains arising out of any "business" and "profession," carried out by the taxpayer in that financial year will be computed under PGBP. Here, the term 'business' includes any "*trade and commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture.*"³⁹¹ Accordingly, when trademark is licenced to a person who is using it to derive profits from the business, then it is taxable to income tax under PGBP. The term 'profession' is "*involves the exercise of intellectual or technical equipment resulted from learning or service.*"³⁹² It further involves "*occupation requiring purely intellectual or manual skills*"³⁹³ of a person.

³⁸⁸ Income Tax Act 1995, s 112A

³⁸⁹ P. Narayan, Law of Trademark and Passing off (Fourth Edition, 2017) 431

³⁹⁰ Trade Marks Act 1999, s 2(1)(r)

³⁹¹ Income Tax Act 1995, s 37(1)

³⁹² CIT v Manmohan Das, [1996] 59 ITR 699 (SC)

³⁹³ Income Tax Act 1995, s 2(13)

The owner of the trademark earns royalty income in case of licencing. The expression ‘royalty’ means the consideration for conveying of any rights subsiding in the trademark; or the imparting of any information concerning the use of the trademark; or rendering of any services in common with the activities referred above. Here, the transferee not being a person or a HUF, is responsible to pay to the ‘resident’ person, any sum by way of royalty with a deduction at the rate of 10% of the total sum.³⁹⁴

According to Section 9(1)(vi) of IT Act, ‘income’ by way of royalty accrues, when it is “payable by—

- a) *the Government; or*
- b) *a resident, except in a case where the royalty is payable in respect of any right, or property or information used or services utilised for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India ; or*
- c) *a person who is a non-resident, where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India*”³⁹⁵

In contrast to the reported rate of 30% to 40%, depending on the kind of person, the royalty income will be taxed at 10% if the aforementioned requirements are met. Important to note: Certain circumstances, including (a) when the non-resident receives "royalty" income from the Indian Government or an Indian company under a contract signed with them after March 31, 2003; (b) when the non-resident conducts business in India through a "permanent establishment" in India or renders professional services from a fixed place of business located in India; and (c) when the non-resident receives "royalty" income from the Indian Government or an Indian company under a contract In this case, a particular method for taxing such "royalty" money is provided under the IT Act.

Another aspect of trademark taxation is Withholding Tax where a domestic licensee sends royalty to an overseas trademark licence holder. Therefore, if the transfer of the trademark involves a non-resident seller, the buyer is generally required to deduct tax at source (TDS) at the applicable rates. According on the specifics of the transaction and any relevant tax treaties between India and the seller's place of residency, the TDS rates may change. The standard TDS rate is 10% (plus any applicable surcharge and cess), and it applies to royalties that are taxable under the IT Act. However, a non-resident who gets royalties and is qualified to benefit from the double taxation avoidance agreement ("DTAA") is entitled to employ the more favourable provisions and rates between the IT Act and the DTAA between India and the non-resident's place of abode.³⁹⁶ But to avail the benefits of a tax treaty, the non-resident seller is typically required to obtain a Tax Residency Certificate (TRC) from the tax authorities of their home country. The TRC serves as proof of tax residency and is submitted to the buyer to support a lower withholding tax rate or claim an exemption under the tax treaty. Therefore, in this case the buyer is responsible

³⁹⁴ Income Tax Act 1995, s 9(1)(vi)

³⁹⁵ Id.

³⁹⁶ Seema Jhingan and Neha Yadav, ‘Withholding Tax Implications On Payment Of Royalty’ (mondaq, 14 August 2018)

<<https://www.mondaq.com/india/withholding-tax/727406/withholding-tax-implications-on-payment-of-royalty>> accessed 28 April 2025

for deducting the applicable TDS at the time of payment to the non-resident seller and depositing it with the Indian tax authorities within the prescribed timelines. Additionally, the buyer is required to file the necessary TDS returns and provide the non-resident seller with a TDS certificate as proof of tax deduction.

V. CONCLUSION

From the above discussion it is certain that profits or earnings received from the transfer of trademark by way of licencing or assignment will be subject to tax under the provisions and regulations given under Income Tax Act. The taxation of trademarks depends on whether the transfer results in a capital gain or a capital loss. If the transfer of a trademark results in a capital gain, it is taxable under the head "Capital Gains" in the Income Tax Act. The capital gains are classified as either short-term or long-term, depending on the holding period of the trademark. The cost of acquisition of the trademark is deducted from the sale consideration to calculate the capital gains. Additionally, the benefit of indexation (adjusting the cost for inflation) is available for long-term capital gains. The indexed cost of acquisition helps in reducing the taxable gains. In the author's view, this tax will help in economic stability of the nation as goodwill is considered as a capital asset and its transfer generates the capital gain. This capital gains and profits are taxable to strengthen the economy. Simultaneously, it is also important to note that tax laws can be complex and subject to change.