

UNCITRAL Legislative Guide on Secured Transactions

Supplement on Security Rights in Intellectual Property



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UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW

UNCITRAL Legislative Guide on Secured Transactions

Supplement on Security Rights in
Intellectual Property



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Preface

The *UNCITRAL Legislative Guide on Secured Transactions: Supplement on Security Rights in Intellectual Property* was prepared by the United Nations Commission on International Trade Law (UNCITRAL).¹

At its thirty-ninth session, in 2006, the Commission considered and approved in principle the substance of the recommendations of the *Guide*. It also considered its future work on secured financing law. Noting that the recommendations of the *Guide* generally applied to security rights in intellectual property rights, the Commission requested the Secretariat to prepare, in cooperation with relevant organizations and in particular the World Intellectual Property Organization (WIPO), a note for submission to the Commission at its fortieth session, in 2007, discussing the scope of future work on intellectual property financing in a supplement (initially called annex) to the *Guide*. The Commission also requested the Secretariat to organize a colloquium on intellectual property financing ensuring to the maximum extent possible the participation of relevant international organizations and experts from various regions of the world.²

Pursuant to that decision of the Commission, the Secretariat organized, with the cooperation of WIPO, a colloquium on security rights in intellectual property rights (Vienna, 18 and 19 January 2007). The colloquium was attended by experts on secured financing and intellectual property law, including representatives of Governments and national and international, governmental and non-governmental organizations. At the colloquium, several suggestions were made with respect to adjustments that would need to be made to the *Guide* to address issues specific to intellectual property financing.³

At the first part of its fortieth session, in June 2007, the Commission considered a note by the Secretariat entitled “Possible future work on security rights in intellectual property” (A/CN.9/632),⁴ which took into account the conclusions reached at the colloquium. In order to provide sufficient guidance to States

¹See www.uncitral.org.

²*Official Records of the General Assembly, Sixty-first Session, Supplement No. 17 (A/61/17)*, paras. 81, 82 and 86, available from www.uncitral.org/uncitral/en/commission/sessions/39th.html.

³See www.uncitral.org/uncitral/en/commission/colloquia_security.html.

⁴Available from www.uncitral.org/uncitral/en/commission/sessions/40th.html.

as to the adjustments that they might need to make in their laws to avoid inconsistencies between secured financing law and law relating to intellectual property, the Commission decided to entrust Working Group VI (Security Interests) with the preparation of a supplement to the *Guide* specific to security rights in intellectual property rights.⁵ At its resumed fortieth session, in December 2007, the Commission finalized and adopted the *Guide* on the understanding that a supplement to the *Guide* specific to security rights in intellectual property rights would subsequently be prepared.⁶

The work of Working Group VI was carried out at five one-week sessions, the final session being held in February 2010.⁷ At its fourteenth, fifteenth and sixteenth sessions, the Working Group referred certain insolvency-related matters to Working Group V (Insolvency Law),⁸ which Working Group V considered at its thirty-fifth, thirty-sixth and thirty-eighth sessions.⁹ In addition, the Working Group cooperated with WIPO and other intellectual property organizations from the public and the private sector, which attended its meetings as observers, to ensure that the *Supplement* would be sufficiently coordinated with law relating to intellectual property. Moreover, the Working Group cooperated closely with the Permanent Bureau of the Hague Conference on Private International Law in the preparation of chapter X of the *Supplement*, on the law applicable to a security right in intellectual property.¹⁰

At its forty-third session, held in New York from 21 June to 9 July 2010, the Commission considered and on 29 June 2010 adopted the *Supplement* by consensus (see annex II.A).¹¹ Subsequently, the General Assembly adopted

⁵*Official Records of the General Assembly, Sixty-second Session, Supplement No. 17 (A/62/17 (Part I))*, paras. 156, 157 and 162, available from www.uncitral.org/uncitral/en/commission/sessions/40th.html.

⁶*Ibid.*, (A/62/17 (Part II)), paras. 99 and 100. The *Guide* (United Nations publication, Sales No. E.09.V.12) is available from www.uncitral.org/pdf/english/texts/security-lg/e/09-82670_Ebook-Guide_09-04-10English.pdf.

⁷The reports of the Working Group on its work at those five sessions are contained in documents A/CN.9/649, A/CN.9/667, A/CN.9/670, A/CN.9/685 and A/CN.9/689. At those sessions, the Working Group considered A/CN.9/WG.VI/WP.33 and Add.1, A/CN.9/WG.VI/WP.35 and Add.1, A/CN.9/WG.VI/WP.37 and Add.1-4, A/CN.9/WG.VI/WP.39 and Add.1-7, and A/CN.9/WG.VI/WP.42 and Add.1-7. The working papers and reports on the work of Working Group VI (Security Interests) are available from www.uncitral.org/uncitral/en/commission/working_groups/6Security_Interests.html.

⁸A/CN.9/667, paras. 129-140; A/CN.9/670, paras. 116-122; and A/CN.9/685, para. 95. The working papers and reports of Working Group V (Insolvency Law) are available from www.uncitral.org/uncitral/en/commission/working_groups/5Insolvency.html.

⁹A/CN.9/666, paras. 112-117; A/CN.9/WG.V/WP.87; A/CN.9/671, paras. 125-127; and A/CN.9/691, paras. 94-98, also available from www.uncitral.org/uncitral/en/commission/working_groups/5Insolvency.html.

¹⁰At its sixteenth session, the Working Group considered a proposal by the Permanent Bureau of the Hague Conference (A/CN.9/WG.VI/WP.40, available from www.uncitral.org/uncitral/en/commission/working_groups/6Security_Interests.html).

¹¹The draft of the *Supplement* considered by the Commission is contained in documents A/CN.9/700 and Add.1-7, available from www.uncitral.org/uncitral/en/commission/sessions/43rd.html. For the report of the Commission on that draft, see *Official Records of the General Assembly, Sixty-fifth Session, Supplement No. 17 (A/65/17)*, paras. 192-227.

resolution 65/23 of 6 December 2010 (see annex II.B), in which it expressed its appreciation to UNCITRAL for the completion and adoption of the *Supplement*; requested the Secretary-General to disseminate broadly the text of the *Supplement*; recommended that all States give favourable consideration to the *Supplement* when revising or adopting their relevant legislation; and also recommended that all States continue to consider becoming party to the United Nations Convention on the Assignment of Receivables in International Trade (2001)¹² and implementing the recommendations of the *Guide*.

¹²United Nations publication, Sales No. E.04.V.14, available from www.uncitral.org/uncitral/en/uncitral_texts/payments/2001Convention_receivables.html.

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Introduction

A. Purpose of the *Supplement*

1. The overall objective of the *UNCITRAL Legislative Guide on Secured Transactions* (the *Guide*) is to promote low-cost credit by enhancing the availability of secured credit (see recommendation 1, subpara. (a)). In line with this objective, the *Supplement on Security Rights in Intellectual Property* (the *Supplement*) is intended to make credit more available and at a lower cost to intellectual property owners and other intellectual property rights holders, thus enhancing the value of intellectual property rights as security for credit. The *Supplement*, however, seeks to achieve that objective without interfering with fundamental policies of law relating to intellectual property (see paras. 46-52 below) by: (a) explaining how the recommendations of the *Guide* would apply in an intellectual property context; and (b) making, in a small number of cases, asset-specific recommendations with respect to security rights in intellectual property.¹

B. The interaction between secured transactions law and law relating to intellectual property

2. With only limited exceptions, the law recommended in the *Guide* applies to security rights in all types of movable asset, including intellectual property (see the *Guide*, recommendations 2 and 4-7). However, with respect to intellectual property, the law recommended in the *Guide* does not apply insofar as its provisions are inconsistent with national law or international agreements, to which the State enacting the law is a party, relating to intellectual property (see recommendation 4, subpara. (b)).

¹The *Supplement* must, therefore, be read together with the *Guide*. For easy reference, the *Supplement* follows the order in which the issues are discussed in the *Guide* (that is, introduction with purpose, terminology, examples and key objectives and fundamental policies, scope, creation of a security right, etc.). In each section, the *Supplement* summarizes briefly the general considerations of the *Guide* and then goes on to discuss how they apply to an intellectual property context.

3. Recommendation 4, subparagraph (b), sets out the basic principle with respect to the interaction of secured transactions law and such national law or international agreements relating to intellectual property. The meaning given to the term “intellectual property” is intended to ensure consistency of the *Guide* with laws and treaties relating to intellectual property. As used in the *Guide*, the term “intellectual property” means any asset considered to be intellectual property under law relating to intellectual property (see the term “intellectual property” in the introduction to the *Guide*, sect. B, para. 20). In addition, references in the *Guide* to “intellectual property” are to be understood as references to “intellectual property rights” (see paras. 18-20 below). The term “law relating to intellectual property” is used in the *Supplement* to refer to national law or law flowing from international agreements, to which a State is a party, relating to intellectual property that governs specifically security rights in intellectual property. Thus, the term is not used to refer to law that generally governs security rights in various types of asset and that may happen to govern security rights in intellectual property (see para. 22 below). In addition, the term includes both statutory and case law and is broader than the term “intellectual property law”, but narrower than general contract or property law. The scope of recommendation 4, subparagraph (b), will, consequently, be broader or narrower, depending on how a State defines the scope of intellectual property. It is understood that a State will do so in compliance with its international obligations flowing from intellectual property law treaties (such as various conventions administered by the World Intellectual Property Organization (WIPO) or the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS Agreement)),² as provided in those treaties.

4. The purpose of recommendation 4, subparagraph (b), is to ensure that, when States adopt the recommendations of the *Guide*, they do not inadvertently change basic rules of law relating to intellectual property. As issues relating to the existence, validity and content of a grantor’s intellectual property rights are matters which the *Guide* does not address (see paras. 60-73 below), the occasions for possible conflict in regimes on these issues are limited (as to the interaction of secured transactions law and law relating to intellectual property with respect to the enforcement of a security right in intellectual property, see paras. 229-232 below). Nevertheless, in matters relating to the creation, third-party effectiveness, priority, enforcement of and law applicable to a security right in intellectual property, it is possible that in some States the two regimes will provide for different rules. Where

²See *Legal Instruments Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, done at Marrakesh on 15 April 1994* (GATT secretariat publication, Sales No. GATT/1994-7).

this is the case, recommendation 4, subparagraph (b), preserves the intellectual-property-specific rule against being overridden inadvertently as a result of adoption by a State of the law recommended in the *Guide*.

5. It bears noting, however, that, in some States, rules of law relating to intellectual property (dealing with security rights in intellectual property) relate only to forms of secured transactions that are not unique to intellectual property and that will no longer be available once a State adopts the law recommended in the *Guide* (for example, pledges, mortgages and transfers or trusts of intellectual property for security purposes). For this reason, States that adopt the law recommended in the *Guide* may also wish to review their law relating to intellectual property to coordinate it with the secured transactions law recommended in the *Guide*. In that connection, States enacting the law recommended in the *Guide* will have to ensure that their secured transactions law reflects in particular the functional, integrated and comprehensive approach recommended in the *Guide* (see chap. I, paras. 101-112), without modifying the basic policies and objectives of their law relating to intellectual property.

6. The *Supplement* is intended to provide guidance to States with respect to such a functional, integrated and comprehensive secured transactions and intellectual property law system. Building on the commentary and the recommendations of the *Guide*, the *Supplement* discusses how the commentary and recommendations of the *Guide* apply where the encumbered asset consists of intellectual property and, where necessary, adds new commentary and recommendations. As is the case with the other asset-specific commentary and recommendations, the intellectual-property-specific commentary and recommendations modify or supplement the general commentary and recommendations of the *Guide*. Accordingly, subject to contrary provisions of law relating to intellectual property and any asset-specific commentary and recommendations of the *Supplement*, a security right in intellectual property may be created, be made effective against third parties, have priority, be enforced and be made subject to applicable law as provided in the general recommendations of the *Guide*.

7. A State enacting the law recommended in the *Guide* with a view to making credit more available and at lower cost to owners of assets such as tangible assets and receivables will most likely wish to make the benefits of such modernization available also to the owners of intellectual property, thereby enhancing the value of the intellectual property as security for credit. This may have an impact on law relating to intellectual property. While it is not the purpose of the *Supplement* to make any recommendations for changes to a State's law relating to intellectual property, as already mentioned, it may have an impact on that law. The *Supplement* discusses this impact and, occasionally, includes in the commentary modest suggestions for the

consideration of enacting States (the expression used is “States might” or “States may wish to consider ...”, rather than “States should”). These suggestions are based on the premise that, by enacting secured transactions laws of the type recommended in the *Guide*, States have made a policy decision to modernize their secured transactions law. The suggestions seek, therefore, to point out where this modernization might lead States to consider how best to coordinate their secured transactions law with their law relating to intellectual property. Thus, recommendation 4, subparagraph (b), is intended to foreclose only inadvertent change to law relating to intellectual property, not all change after careful consideration by a State enacting the law recommended in the *Guide*.

C. Terminology

8. States that adopt the law recommended in the *Guide* may wish to review their law relating to intellectual property and coordinate the terminology used in that law with the terminology used in the law recommended in the *Guide*.

(a) *Acquisition security right*

9. As used in the *Guide*, the term “acquisition security right” means a security right in a tangible asset (other than a negotiable instrument or negotiable document) that secures the obligation to pay any unpaid portion of the purchase price of the asset or an obligation incurred or credit otherwise provided to enable the grantor to acquire the asset. An acquisition security right need not be denominated as such. Under the unitary approach, the term includes a right that is a retention-of-title right or a financial lease right (see the term “acquisition security right” in the introduction to the *Guide*, sect. B, para. 20). For the purposes of the *Supplement*, the term includes a security right in intellectual property or a licence of intellectual property, provided that the security right secures the obligation to pay any unpaid portion of the acquisition price of the encumbered intellectual property or licence or an obligation incurred or credit otherwise provided to enable the grantor to acquire the encumbered intellectual property or licence.

(b) *Competing claimant*

10. In secured transactions law, the concept of a “competing claimant” is used to identify parties other than the secured creditor in a specific security

agreement that might claim a right in an encumbered asset or the proceeds from its disposition (see the term “competing claimant” in the introduction to the *Guide*, sect. B, para. 20). Thus, the *Guide* uses the term “competing claimant” in the sense of a claimant that competes with a secured creditor (that is, the claimant is another secured creditor with a security right in the same asset, another creditor of the grantor that has a right in the same asset, the insolvency representative in the insolvency of the grantor, a buyer or other transferee, or a lessee or licensee of the same asset). The term “competing claimant” is essential for the application in particular of the priority rules recommended in the *Guide*, such as, for example, the rule in recommendation 76, under which a secured creditor with a security right in receivables that registered a notice of its security right in the general security rights registry has priority over another secured creditor that acquired a security right in the same receivables from the same grantor before the other secured creditor but failed to register a notice of its security right.

11. In law relating to intellectual property, however, the notion of a “competing claimant” is not used and priority conflicts typically refer to conflicts among intellectual property transferees and licensees, even if no conflict with a secured creditor is involved (infringers are not competing claimants and, if an alleged infringer proves that it has a legitimate claim, it is a transferee or licensee of the encumbered asset and not an infringer). Secured transactions law does not interfere with the resolution of such conflicts that do not involve a secured creditor (a term that includes a transferee in a transfer for security purposes that is treated in the *Guide* as a secured creditor). Thus, a conflict between two outright transferees would not be covered by the *Guide*. However, a conflict between a transferee for security purposes of intellectual property rights and an outright transferee of the same intellectual property rights would, subject to the limitation of recommendation 4, subparagraph (b), be covered by the *Guide* (see recommendations 78 and 79).

(c) *Consumer goods*

12. The *Guide* uses the term “consumer goods” to refer to goods that a grantor uses or intends to use for personal, family or household purposes (see the term “consumer goods” in the introduction to the *Guide*, sect. B, para. 20). In the *Supplement*, for the purpose of applying the recommendations of the *Guide* relating to acquisition security rights in tangible assets to acquisition security rights in intellectual property, the term includes intellectual property or a licence of intellectual property used or intended by the grantor to be used for personal, family or household purposes.

(d) *Encumbered asset*

13. The *Guide* uses the term “encumbered asset” to denote an asset that is subject to a security right (see the term “encumbered asset” in the introduction to the *Guide*, sect. B, para. 20). While the *Guide* refers by convention to a security right in an “encumbered asset”, what is really encumbered and meant is “whatever right the grantor has in an asset and intends to encumber”.

14. The *Guide* also uses various terms to denote the particular type of intellectual property right that may be used as an encumbered asset without interfering with the nature, the content or the legal consequences of such terms for purposes of law relating to intellectual property, as well as contract and property law. These types of intellectual property right that may be used as security for credit include the rights of an intellectual property owner (“owner”), the rights of an assignee or successor in title to an owner, the rights of a licensor or licensee under a licence agreement and the rights in intellectual property used with respect to a tangible asset, provided that the intellectual property right is described as an encumbered asset in the security agreement. The owner, licensor or licensee may encumber all or part of its rights, if they are transferable under law relating to intellectual property.

15. Under law relating to intellectual property, the rights of an intellectual property owner generally include the right to prevent unauthorized use of its intellectual property, the right to renew registrations, the right to pursue infringers and the right to transfer and grant licences of its intellectual property. For example, in the case of a patent, the patent owner has exclusive rights to prevent certain acts, such as making, using or selling the patented product without the patent owner’s authorization.

16. Typically, under law relating to intellectual property and contract law, the rights of a licensor and a licensee depend on the terms of the licence agreement (in the case of a contractual licence), law (in the case of compulsory or statutory licence) or the legal consequences of specific conduct (in the case of an implied licence). In addition, normally, the rights of a licensor include the right to claim payment of royalties and to terminate the licence agreement. Similarly, the rights of a licensee include the authorization given to the licensee to use the licensed intellectual property in accordance with the terms of the licence agreement and possibly the right to enter into sub-licence agreements and the right to obtain payment of sub-royalties (see the term “licence”, paras. 23-25 below). Finally, the rights of a grantor of a security right in a tangible asset with respect to which intellectual property is used are described in the agreement between the secured creditor and the grantor (owner, licensor or licensee of the relevant intellectual property) in line with secured transactions law and law relating to intellectual property.

(e) *Grantor*

17. The *Guide* uses the term “grantor” to denote the person creating a security right to secure either its own obligation or that of another person (see the term “grantor” in the introduction to the *Guide*, sect. B, para. 20). As already mentioned (see para. 14), in a secured transaction relating to intellectual property, the encumbered asset may be the rights of the intellectual property owner, the rights of a licensor (including the right to the payment of royalties) or the rights of a licensee to use or exploit the licensed intellectual property, to grant sub-licences and to claim the payment of sub-royalties. Thus, depending on the kind of intellectual property that is encumbered, the term “grantor” will refer to an owner, a licensor or a licensee (although, unlike an owner, a licensor or a licensee may not necessarily enjoy exclusive rights as this term is understood under law relating to intellectual property). Finally, as is the case with any secured transaction relating to other types of movable asset, the term “grantor” may reflect a third party granting a security right in its intellectual property to secure the obligation owed by a debtor to a secured creditor.

(f) *Intellectual property*

18. As used in the *Guide* (see the term “intellectual property” in the introduction to the *Guide*, sect. B, para. 20), the term “intellectual property” means copyrights, trademarks, patents, service marks, trade secrets and designs and any other asset considered to be intellectual property under the domestic law of the enacting State or under an international agreement to which the enacting State is a party (such as, for example, neighbouring, allied or related rights³ or plant varieties). Furthermore, references in the *Guide* to “intellectual property” are to be understood as references to “intellectual property rights”, such as the rights of an intellectual property owner, licensor or licensee. The commentary to the *Guide* explains that the meaning given to the term “intellectual property” in the *Guide* is intended to ensure consistency of the *Guide* with law relating to intellectual property, while at the same time respecting the right of a State enacting

³Closely related to “copyright” are “neighbouring rights”, also called allied or related rights. These are rights that are said to be “in the neighbourhood” of copyright. The term typically covers the rights of performers, producers of phonograms and broadcasting organizations, but in some countries it can also include the rights of film producers or rights in photographs. Sometimes these are called *diritti connessi* (“connected rights”) or *verwandte Schutzrechte* (“related rights”) or *droits voisins* (“neighbouring rights”), but the common term is the English “neighbouring rights”. Internationally, neighbouring rights are generally protected under the International Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organizations, done at Rome on 26 October 1961. Additional protections are accorded to certain performers and phonogram producers in the WIPO Performances and Phonograms Treaty, adopted in Geneva on 20 December 1996.

the recommendations of the *Guide* to align the definition with its own law, whether national law or law flowing from treaties. An enacting State may add to the list mentioned above or remove from it types of intellectual property so that it conforms to national law.⁴ As a result, the *Guide* treats as “intellectual property”, for the purposes of the *Guide*, whatever an enacting State considers to be intellectual property in conformity with its national law and in compliance with its international obligations.

19. For purposes of secured transactions law, the intellectual property right itself is distinct from the rights to payment that flow from it, such as the right to payment of royalties, for example, from the exercise of broadcasting rights. Under the *Guide* rights to payment are characterized as “receivables” and could be an original encumbered asset, if described as such in the security agreement, or proceeds of intellectual property, if the original encumbered asset is intellectual property. However, this treatment of these rights to payment in the *Guide* does not preclude a different treatment for purposes of law relating to intellectual property. For example, for the purposes of law relating to intellectual property, a right of a licensor to payment of equitable remuneration might be treated as part of the intellectual property right of the licensor (for the treatment of receivables under secured transactions law and law relating to intellectual property, see paras. 97-105 below).

20. It is also important to note that a licence agreement relating to intellectual property is not a secured transaction and a licence with a right to terminate the licence agreement is not a security right. Thus, secured transactions law does not affect the rights and obligations of a licensor or a licensee under a licence agreement. For example, the owner’s, licensor’s or licensee’s ability to limit the transferability of its intellectual property rights remains unaffected. In any case, it should be noted that, while the question whether an intellectual property owner may grant a licence is a matter of law relating to intellectual property, the question whether the owner and its secured creditor may agree between them that the owner may not grant a licence is a matter of secured transactions law addressed in the *Supplement* (see para. 222 below).

(g) *Inventory*

21. As used in the *Guide*, the term “inventory” means tangible assets held for sale or lease in the ordinary course of a grantor’s business, as well as raw and semi-processed materials (work-in-process) (see the term “inventory” in the introduction to the *Guide*, sect. B, para. 20). For the purposes of the

⁴See footnote 24 to the introduction to the *Guide*.

Supplement, the term includes intellectual property or a licence of intellectual property held by the grantor for sale or licence in the ordinary course of the grantor's business.

(h) *Law and law relating to intellectual property*

22. As already mentioned (see para. 3), the commentary of the *Guide* also clarifies that references to the term "law" throughout the *Guide* include both statutory and non-statutory law. In addition, the commentary to the *Guide* clarifies that the expression "law relating to intellectual property" (see recommendation 4, subpara. (b)) is broader than intellectual property law (dealing, for example, directly with patents, trademarks or copyrights) but narrower than general contract or property law (see the *Guide*, introduction, para. 19, and chap. I, paras. 33-36). In particular, the expression "law relating to intellectual property" means national law or law flowing from international agreements, to which a State is a party, relating to intellectual property that governs specifically security rights in intellectual property, and not law that generally governs security rights in various types of asset and, as a result, may govern security rights in intellectual property. An example of a "law relating to intellectual property" might be law that applies specifically to pledges or mortgages of copyrights in software, assuming that it is part of the law relating to intellectual property and is not simply the application of a State's general law of pledges or mortgages in an intellectual property context.

(i) *Licence*

23. The *Guide* also uses the term "licence" (which includes a sub-licence) as a general concept, while recognizing that, under law relating to intellectual property, a distinction may often be drawn: (a) between contractual licences (whether express or implied) and compulsory or statutory licences, in which a licence is not the result of an agreement; (b) between a licence agreement and the licence that is granted by the agreement (for example, the authorization to use or exploit the licensed intellectual property); and (c) between exclusive licences (which, under law relating to intellectual property in some States, may be treated as transfers) and non-exclusive licences. In addition, under the *Guide*, a licence agreement does not in itself create a security right and a licence with a right to terminate the licence agreement is not a security right (see para. 20 above).

24. However, the exact meaning of these terms is left to law relating to intellectual property, as well as to contract and other law that may be

applicable (such as the Joint Recommendation concerning Trademark Licences, adopted by the Assembly of the Paris Union and the General Assembly of WIPO (2000),⁵ and the Singapore Treaty on the Law of Trademarks (2006)).⁶ In particular, a security right in rights under a licence agreement does not affect the terms and conditions of the licence agreement (in the same way that a security right in a sales receivable does not affect the terms and conditions of the sales contract). This means, inter alia, that the secured creditor does not acquire more rights than its grantor (see the *Guide*, recommendation 13). For example, the *Guide* does not interfere with the limits or terms of a licence agreement that may refer to the description of the specific intellectual property, the authorized or restricted uses, geographical area of use and the duration of use. As a result, an exclusive licence to exercise the “theatrical rights” in film A in country X for “10 years starting 1 January 2008” may be given and it will be different from an exclusive licence to exercise the “video rights” in film A in country Y for “10 years starting 1 January 2008”. Either way, the creation of a security right in the rights of a party to the licence agreement does not affect its terms and conditions.

25. In addition, the *Guide* does not affect in any way the particular characterization of rights under a licence agreement given by law relating to intellectual property. For example, the *Guide* does not affect the nature of rights created under an exclusive licence agreement as rights in rem or the nature of an exclusive licence as a transfer, as is the case under some laws relating to intellectual property. Moreover, the *Guide* does not affect any limitations included in the licence agreement as to the transferability of licensed rights (see paras. 52, 107, 158, 159, 187, 196 and 197 below).

(j) *Owner*

26. The *Guide* does not explain the term “owner” of an encumbered asset, whether that asset is intellectual property or not. This is a matter of the relevant property law. Accordingly, the *Guide* uses the term “intellectual property owner” referring to the meaning of this term under law relating to intellectual property, generally denoting the person that is entitled to enforce the exclusive rights flowing from intellectual property or its transferee, that is, the creator, author or inventor or their successor in title (as to whether a secured creditor may exercise the rights of an intellectual property owner, see paras. 29, 30, 87, 88 and 222 below).

⁵Available from www.wipo.int/about-ip/en/development_iplaw/pdf/pub835.pdf.

⁶Available from www.wipo.int/treaties/en/ip/singapore/singapore_treaty.html.

(k) *Receivable and assignment*

27. The term “receivable” is used in the *Guide* (see the term “receivable” in the introduction to the *Guide*, sect. B, para. 20) and in the United Nations Convention on the Assignment of Receivables in International Trade (the “United Nations Assignment Convention”; see article 2)⁷ to reflect a right to payment of a monetary obligation. Thus, for the purposes of the *Guide*, the term includes the right of a licensor (that may be an owner or not) or a licensee/sub-licensor to obtain payment of licence royalties (without affecting the terms and conditions of the licence agreement, such as an agreement between the licensor and the licensee that the licensee will not create a security right in its right to payment of sub-royalties). The exact meaning and scope of licence royalties are subject to the terms and conditions of the licence agreement relating to the payment of royalties, such as that payments are to be staggered or that there might be percentage payments depending on market conditions or sales figures (for a discussion of the term “secured creditor”, which includes an assignee of receivables, see paras. 29 and 30 below; for a discussion of the distinction between a secured creditor and an intellectual property owner, see paras. 87 and 88 below).

28. The term “assignment” is used in the *Guide* with respect to receivables to denote not only outright assignments but also assignments for security purposes (treated in the *Guide* as secured transactions) and transactions creating a security right in a receivable. To avoid creating the impression that the recommendations of the *Guide* relating to assignments of receivables apply also to “assignments” of intellectual property (as the term “assignment” is used in law relating to intellectual property), the term “transfer” (rather than the term “assignment”) is used in the *Supplement* to denote the transfer of the rights of an intellectual property owner. While the law recommended in the *Guide* applies to all types of assignment of receivables, it does not apply to outright transfers of any right other than a receivable (see the *Guide*, recommendations 2, subpara. (d), and 3; see also paras. 57-59 below). It should also be noted that, while what is a “transfer” or a “licence” is left to the relevant property or contract law, the term “transfer” is not used in the *Guide* to denote a licence agreement (see paras. 158 and 159 below).

(l) *Secured creditor*

29. The *Guide* recognizes that a security agreement creates a security right, that is, a limited property right, not an ownership right, in an encumbered asset, provided that the grantor has the right or power to create a security

⁷United Nations publication, Sales No. E.04.V.14.

right in the asset (see recommendation 13). Thus, in the *Guide*, the term “secured creditor” (which includes a transferee by way of security) is used to denote a person that has a security right and not an outright transferee or an owner (although, for convenience of reference, the term includes an outright assignee of receivables; see the term “secured creditor” in the introduction to the *Guide*, sect. B, para. 20). In other words, a secured creditor that acquires a security right under the *Guide* does not thereby acquire ownership. This approach protects the grantor/owner that retains ownership and often possession or control of the encumbered asset, while at the same time securing the secured creditor if the grantor or other debtor defaults on the payment of the secured obligation. In any case, secured creditors normally do not wish to accept the responsibilities and costs of ownership, and the *Guide* does not require a secured creditor to do so. This means, for example, that, even after the creation of a security right, the owner of the encumbered asset may exercise all its rights as an owner (subject to any limitations it may have agreed to with the secured creditor). It should also be noted that, even when the secured creditor disposes of the encumbered asset by enforcing its security right after default, the secured creditor does not necessarily become an owner. In this case, the secured creditor is merely exercising its right to dispose of the encumbered asset and the transferee acquires the rights of the grantor free of security rights with a lower priority than that of the security right being enforced (see paras. 237 and 238 below; see also the *Guide*, recommendation 149 and chap. VIII, paras. 57-59). Only where, after default, the secured creditor exercises the remedy of proposing to acquire the grantor’s ownership rights in the encumbered asset in total or partial satisfaction of the secured obligation (in the absence of any objection by the grantor, the debtor and any other affected person; see the *Guide*, recommendations 157 and 158), or acquires the grantor’s ownership rights by purchasing the asset at a sale in the context of an enforcement, will the secured creditor ever become the owner of the asset.

30. For the purposes of secured transactions law, this characterization of a security agreement and the rights of a secured creditor applies also to situations where the encumbered asset is intellectual property. However, the *Guide* does not affect different characterizations under law relating to intellectual property with respect to matters specific to intellectual property. Under law relating to intellectual property, a security agreement may be characterized as a transfer of the intellectual property rights of an owner, licensor or licensee and the secured creditor may have the rights of an owner, licensor or licensee, such as the right to preserve the encumbered intellectual property and thus to deal with authorities, grant licences or pursue infringers. So, for example, nothing in secured

transactions law prevents a secured creditor from agreeing with the grantor/owner, licensor or licensee to become an owner, licensor or licensee of the encumbered intellectual property (see the *Guide*, recommendation 10, and para. 222 below). If the agreement does or is intended to secure the performance of an obligation and law relating to intellectual property permits a secured creditor to become an owner, licensor or licensee, the term “secured creditor” may denote an owner, licensor or licensee to the extent permitted under law relating to intellectual property. In such a case, secured transactions law will apply with respect to issues normally addressed in that law, such as the creation, third-party effectiveness, priority, enforcement of and law applicable to a security right (subject to the limitation of recommendation 4, subpara. (b)); and law relating to intellectual property will apply with respect to issues that are normally addressed in that law, such as dealing with state authorities, granting licences or pursuing infringers (for the distinction between a secured creditor and an owner with respect to intellectual property, see also paras. 87 and 88 below).

(m) *Security right*

31. The *Guide* uses the term “security right” to refer to all types of property right in a movable asset that are created by agreement to secure payment or other performance of an obligation, irrespective of how they are denominated (see the term “security right” in the introduction to the *Guide*, sect. B, para. 20, and recommendations 2, subpara. (d), and 8). Thus, the term “security right” would cover the right of a pledgee or mortgagee of intellectual property, as well as of a transferee in a transfer for security purposes.

(n) *Transfer*

32. While the *Guide* uses the term “outright transfer” to denote transfer of ownership (see the *Guide*, chap. I, para. 25), the exact meaning of this term is a matter of property law. The *Guide* also uses the term “transfer for security purposes” to refer to a transaction that is in name only a transfer but functionally a secured transaction. In view of the functional, integrated and comprehensive approach it takes to secured transactions (see recommendations 2, subpara. (d), and 8), for the purposes of secured transactions law, the *Guide* treats a transfer for security purposes as a secured transaction. To the extent that a different characterization of a transfer for security purposes in other law would apply to all assets, this is not an issue with respect to which the *Guide* would defer to law relating

to intellectual property (see the *Guide*, recommendation 4, subpara. (b), and paras. 2-7 above). However, this approach does not affect a different characterization of a transfer other than an outright transfer for the purposes of law relating to intellectual property. For example, under law relating to intellectual property, the expression “transfer other than an outright transfer” may denote the granting of rights from a licensor to a licensee where the licensor retains some control over the use of the intellectual property (for a discussion of outright transfers of intellectual property, see paras. 57-59 below).

D. Valuation of intellectual property to be encumbered

33. The valuation of assets to be encumbered is an issue that all prudent grantors and secured creditors have to address irrespective of the type of asset to be encumbered. However, valuation of intellectual property may be harder at least to the extent that it raises the issue whether intellectual property is an asset that may be exploited economically to generate income. For example, once a patent is created, the question arises whether it has any commercial application and, if so, what would be the amount of income that could be generated from the sales of any patented product.

34. Secured transactions law cannot answer this question. Still, insofar as it affects the use of intellectual property as security for credit, some of the complexities involved in appraising the value of intellectual property need to be understood and addressed. For example, one issue is that, although the appraisal must take into account the value of the intellectual property and the expected cash flow, there are no universally accepted formulae for making this calculation. However, because of the increasing importance of intellectual property as security for credit, in some States, lenders and borrowers are often able to seek guidance from independent appraisers of intellectual property. In addition, parties in some States may be able to rely on valuation methodologies developed by national institutions, such as bank associations. Moreover, parties may be able to rely on training for valuation of intellectual property in general or for the purpose of licence agreements in particular provided by international organizations such as WIPO. Parties may also be able to rely on standards for the valuation of intellectual property as assets that can be used as security for credit developed by other international organizations, such as the Organisation for Economic Co-operation and Development.

E. Examples of financing practices relating to intellectual property

35. Secured transactions relating to intellectual property can usefully be divided into two broad categories. The first category consists of transactions in which the intellectual property rights themselves serve as security for the credit (that is, the rights of an owner, the rights of a licensor or the rights of a licensee). In these transactions, the provider of credit is granted a security right in patents, trademarks, copyrights or other intellectual property rights of the borrower. Examples 1-4 below each involve such a situation. In example 1, the encumbered assets are the rights of an owner. In examples 2 and 3, the encumbered assets are the rights of a licensor and, in example 4, the encumbered assets are the rights of a licensee.

36. The second category of transaction involves financing transactions that involve intellectual property in combination with other movable assets, such as equipment, inventory or receivables. An illustration of this type of transaction is found in example 5, which involves a credit facility to a manufacturer, secured by a security right covering substantially all of the manufacturer's assets, including its intellectual property rights.

37. Each of the examples illustrates how owners, licensors and licensees of intellectual property can use these assets as security for credit. In each case, a prudent prospective lender will engage in due diligence to ascertain the nature and extent of the rights of the owners, licensors and licensees of the intellectual property involved and to evaluate the extent to which the proposed financing would or would not interfere with such rights. The ability of a lender to address these issues in a satisfactory manner, obtaining consents and other agreements where necessary from the owners of the intellectual property, will affect the lender's willingness to extend the requested credit and the cost of such credit. Each of these categories of transaction not only involves different types (or combinations) of encumbered asset, but also presents different legal issues for a prospective lender or other credit provider.⁸

⁸Some of these questions might be addressed in asset-specific intellectual property legislation. For example, article 19 of the Council Regulation (EC) No. 207/2009 of 26 February 2009 on the Community trademark provides that a security right may be created in a community trademark and, at the request of one of the parties, such a right may be registered in the Community trademark registry.

*Example 1**Rights of an owner in a portfolio of patents and patent applications*

38. Company A, a pharmaceutical company that is constantly developing new drugs, wishes to obtain a revolving line of credit from bank A secured in part by company A's portfolio of existing and future drug patents and patent applications. Company A provides bank A with a list of all of its existing patents and patent applications, as well as their chain of title. Bank A evaluates which patents and patent applications it will include in the "borrowing base" (that is, the pool of patents and patent applications to which bank A will agree to attribute value for borrowing purposes), and at what value they will be included. In connection therewith, bank A obtains an appraisal of the patents and patent applications from an independent appraiser of intellectual property. Bank A then obtains a security right in the portfolio of patents and patent applications and registers a notice of its security right in the appropriate national patent registry (assuming that the applicable law provides for registration of security rights in the patents registry). When company A obtains a new patent, it provides its chain of title and valuation to bank A for inclusion in the borrowing base. Bank A evaluates the information, determines how much additional credit it will extend based on the new patent and adjusts the borrowing base. Bank A then makes appropriate registrations in the general security rights registry or in the patent registry (as appropriate under the relevant law) reflecting its security right in the new patent.

*Example 2**Rights of a licensor in royalties from the licence of visual art*

39. Company B, a publisher of comic books, licenses its copyrighted characters to a wide array of manufacturers of clothing, toys, interactive software and accessories. The licensor's standard form of licence agreement requires licensees to report sales, and pay royalties on such sales, on a quarterly basis. Company B wishes to borrow money from bank B secured by the anticipated stream of royalty payments arising under these licence agreements. Company B provides bank B with a list of the licences, the credit profile of the licensees and the status of each licence agreement. Bank B then requires company B to obtain an "estoppel certificate" from each licensee verifying the existence of the licence, the absence of default and the amount due, and confirming the licensee's agreement to pay future royalties to the appropriate party (for example, company B, bank B or an escrow account) until further notice.

*Example 3**Rights of a licensor in royalties from the licence of a motion picture*

40. Company C, a motion picture company, wishes to produce a motion picture. Company C sets up a separate company to undertake the production and hire the individual writers, producers, directors and actors. The production company obtains a loan from bank C secured by the copyright, service contracts and all revenues to be earned from the exploitation of the motion picture in the future. The production company then enters into licence agreements with distributors in multiple countries who agree to pay “advance guarantees” against royalties upon completion and delivery of the picture. For each licence, production company C, bank C and the distributor/licensee enter into an “acknowledgement and assignment” agreement under which the licensee acknowledges the paramount security right of bank C and the assignment of its royalty payments to bank C, while bank C agrees that, in case of enforcement of its security right in the licensor’s rights, it will not terminate the licence as long as the licensee makes payments and otherwise abides by the terms of the licence agreement.

*Example 4**Authorization of a licensee to use or exploit licensed software*

41. Company D is a developer of sophisticated software used in various architectural applications. In addition to certain software components created by the company’s in-house software engineers (which the company licenses to its customers), company D also incorporates into its products software components that it licenses from third parties (and then sub-licenses to its customers). Company D wishes to borrow money from bank D secured by a security right in its rights as licensee of intellectual property from third parties, that is, its right to use and incorporate into its software some software components that it licenses from third parties (with the consent of the licensor if the licence agreement provides that the rights of company D are non-transferable). For evidence, the software developer can provide bank D with a copy of its software components licence agreement to determine whether company D may grant a security right.

Example 5

Security right in all assets of an enterprise

42. Company E, a manufacturer and distributor of cosmetics, wishes to obtain a credit facility to provide ongoing working capital for its business. Bank E is considering extending this facility, provided that the facility is secured by a so-called “enterprise mortgage”, “floating charge” or all-asset-security right granting to the bank a security right in substantially all of company E’s existing and future assets, including all existing and future intellectual property rights that it owns or licenses from third parties.

Security rights in tangible assets with respect to which intellectual property is used

43. Apart from the transactions mentioned above, there are transactions in which assets other than intellectual property, such as inventory or equipment, serve as security for credit, while the value of these assets is based to some extent upon the intellectual property with which they are associated. This category of transactions, illustrated by examples 6 and 7 below, involves security rights in tangible assets. As discussed in the *Supplement* (see paras. 108-112 below), a security right in a tangible asset does not automatically extend to the intellectual property used with respect to that asset, unless otherwise agreed by the parties. Thus, if a secured creditor wishes to take a security right in such intellectual property, the intellectual property has to be described in the security agreement as part of the encumbered asset.

Example 6

Rights of a manufacturer of trademarked inventory

44. Company F, a manufacturer of designer jeans and other high-fashion clothing, wishes to borrow money from bank F secured in part by company F’s inventory of finished products. Many of the items manufactured by company F bear well-known trademarks licensed from third parties under licence agreements that give company F the right to manufacture and sell the products. Company F provides bank F with its trademark licence agreements evidencing its right to use the trademarks and to grant a security right in the trademarked inventory, as well as its obligations to the trademark owners. Bank F extends credit to company F against the value of the inventory.

Example 7

Rights of a distributor of trademarked inventory

45. Company G, one of company F's distributors (see example 6), wishes to borrow money from bank G secured in part by its inventory of designer jeans and other clothing that it purchases from company F, a significant portion of which bears well-known trademarks licensed by company F from third parties. Company G provides bank G with invoices from company F evidencing that it acquired the jeans in an authorized sale or copies of the agreements with company F evidencing that the jeans distributed by company G are genuine and that company G has the right to create a security right in those jeans. Bank G extends credit to company G against the value of the inventory.

F. Key objectives and fundamental policies

46. As already mentioned (see para. 1), the overall objective of the *Guide* is to promote secured credit. In order to achieve this general objective, the *Guide* formulates and discusses several additional objectives, including the objectives of predictability and transparency (see the introduction to the *Guide*, paras. 43-59). The *Guide* also rests on and reflects several fundamental policies. These policies include providing for comprehensiveness in the scope of secured transactions laws, the integrated and functional approach to secured transactions (under which all transactions performing security functions, however denominated, are considered to be security devices) and the possibility of granting a security right in future assets (see the introduction to the *Guide*, paras. 60-72).

47. These key objectives and fundamental policies are equally relevant to secured transactions relating to intellectual property. Accordingly, the overall objective of the *Guide* with respect to intellectual property is to promote secured credit for businesses that own or have the right to use intellectual property, by permitting them to use rights pertaining to intellectual property as encumbered assets, without interfering with the legitimate rights of the owners, licensors and licensees of intellectual property under law relating to intellectual property, as well as under contract or general property law. Similarly, all the objectives and fundamental policies mentioned above apply

to secured transactions in which the encumbered asset is or includes intellectual property. For example, the *Guide* is designed:

(a) To allow persons with rights in intellectual property to use intellectual property as security for credit (see the *Guide*, key objective 1, subpara. (a));

(b) To allow persons with rights in intellectual property to use the full value of their assets to obtain credit (see key objective 1, subpara. (b));

(c) To enable persons with rights in intellectual property to create a security right in such rights in a simple and efficient manner (see key objective 1, subpara. (c));

(d) To allow parties to secured transactions relating to intellectual property maximum flexibility to negotiate the terms of their security agreement (see key objective 1, subpara. (i));

(e) To enable interested parties to determine the existence of security rights in intellectual property in a clear and predictable way (see key objective 1, subpara. (f));

(f) To enable secured creditors to determine the priority of their security rights in intellectual property in a clear and predictable way (see key objective 1, subpara. (g)); and

(g) To facilitate efficient enforcement of security rights in intellectual property (see key objective 1, subpara. (h)).

48. The general policy objectives of law relating to intellectual property include the objectives to prevent unauthorized use of intellectual property and to protect the value of intellectual property and thus to encourage further innovation and creativity. To accomplish this general policy objective, law relating to intellectual property accords certain exclusive rights to intellectual property owners. To ensure that the key objectives of secured transactions law will be achieved in a way that does not interfere with the objectives of law relating to intellectual property and thus provide mechanisms to fund the development and dissemination of new works, the *Guide* states a general principle for dealing with the interaction of secured transactions law and law relating to intellectual property. The principle is set out in recommendation 4, subparagraph (b) (see paras. 2-7 above and paras. 60-73 below).

49. At this stage, it is sufficient to note that the regime elaborated upon in the *Guide* does not, in itself, in any way define the content of any intellectual property right, describe the scope of the rights that an owner, licensor or licensee may exercise or impede their rights to preserve the value of their intellectual property rights by preventing their unauthorized use. Thus, the

key objective of promoting secured credit with respect to intellectual property will be achieved in a way that does not interfere with the objectives of law relating to intellectual property to prevent unauthorized use of intellectual property, to protect the value of intellectual property and thus to encourage further innovation and creativity.

50. Similarly, this key objective of promoting secured credit without interfering with the objectives of law relating to intellectual property means that neither the existence of the secured credit regime nor the creation of a security right in intellectual property should diminish the value of intellectual property. Thus, for example, the creation of a security right in intellectual property should not be misinterpreted as constituting an inadvertent abandonment of intellectual property by the owner/grantor; and failure by the owner/grantor or the secured creditor to use a trademark properly, to use it on all products or services or to maintain adequate quality control may result in loss of value to, or even abandonment of, the intellectual property.

51. In addition, in the case of products or services associated with marks, these key objectives mean that secured transactions law should avoid causing consumer confusion as to the source of products or services. For example, when enforcing a security right, a secured creditor should not be entitled to remove the manufacturer's mark from the encumbered assets or replace it with another mark (whether confusingly similar or not) and sell the encumbered assets.

52. Finally, these key objectives mean that secured transactions law should not override contractual limitations set forth in a license agreement. For example, if the license agreement provides that the rights of a licensee are non-transferable without the consent of the licensor, no enforceable security right in the license may be created without the consent of the licensor.

I. Scope of application and party autonomy

A. Broad scope of application

53. The law recommended in the *Guide* applies to security rights in all types of movable asset, including intellectual property (for the meaning of the term “intellectual property”, see paras. 18-20 above). Under the law recommended in the *Guide*, a legal or natural person may create or acquire a security right, and a security right may secure any type of obligation (see recommendation 2). The law recommended in the *Guide* applies to all transactions serving security purposes, regardless of the form of the transaction or the terminology used by the parties (see the *Guide*, recommendations 2, subpara. (d), and 8). The *Supplement* has an equally broad scope with respect to security rights in intellectual property.

1. Encumbered assets covered

54. The characterization of different types of intellectual property and the question of whether each type of intellectual property is transferable and may thus be encumbered are matters of law relating to intellectual property. However, the *Guide* and the *Supplement* are based on the general assumption that a security right may be created in any type of intellectual property, such as a patent, a trademark or a copyright. The *Guide* and the *Supplement* are also based on the assumption that the encumbered asset may be any of the various exclusive rights of an owner, the rights of a licensor, the rights of a licensee or the rights in intellectual property used with respect to a tangible asset.

55. However, there is an important limitation to the scope of the *Guide* and the *Supplement*. In line with general rules of property law, for a security right to be created in an asset, including intellectual property, the asset has to be transferable under property law, including law relating to intellectual property. For example, in many States, under law relating

to intellectual property, only the economic rights under a copyright may be transferred (and thus encumbered), but not the moral rights of an author. The law recommended in the *Guide* does not affect such limitations. More specifically, the law recommended in the *Guide* does not override provisions of any other law (including law relating to intellectual property) to the extent that they limit the creation or enforcement of a security right in or the transferability of specific types of asset, including intellectual property (see the *Guide*, recommendation 18). The only exception to this rule relates to statutory limitations to the assignability of future receivables and receivables assigned in bulk or in part (on the sole ground that they are future receivables or receivables assigned in bulk or in part; see para. 99 below), which would be removed or overridden by a rule or law enacting the relevant recommendation of the *Guide* (see the *Guide*, recommendation 23; see also paras. 102-104 and 120 below).

2. *Transactions covered*

56. As already mentioned (see para. 53), the law recommended in the *Guide* applies to all transactions serving security purposes, regardless of how they are denominated by the parties or by law relating to intellectual property. In other words, even if law relating to intellectual property characterizes a transfer of intellectual property to a creditor for security purposes as a conditional transfer or even as an “outright” transfer, the law recommended in the *Guide* treats this transaction as giving rise to a security right and thus applies to it as long as it serves security purposes (see recommendations 2, subpara. (d), and 8).

3. *Outright transfers of intellectual property*

57. To some extent, the law recommended in the *Guide* applies to an outright transfer (that is, a transfer of ownership) of a receivable (see recommendation 3). As the law recommended in the *Guide* treats royalties payable by the licensee of intellectual property to its licensor as receivables of the licensor (see the term “receivable” in the introduction to the *Guide*, sect. B, para. 20), it applies, to some extent, to the outright transfer of the right to the payment of royalties (without affecting the terms and conditions of the licence agreement, such as an agreement between the licensor and the licensee that the licensee will not create a

security right in its right to payment of sub-royalties). The inclusion of outright transfers of receivables in the scope of the law recommended in the *Guide* reflects the fact that such transfers are usually seen as financing transactions and are often difficult in practice to distinguish from loans against the receivables. However, simply because certain recommendations of the *Guide* would generally apply to outright transfers of receivables, this does not mean that the law re-characterizes an outright transfer of a receivable as a secured transaction. An important reason for not re-characterizing outright transfers of receivables as secured transactions is to avoid negatively affecting important receivables financing practices, such as factoring (for outright transfers of receivables, see the *Guide*, chap. I, paras. 25-31; for an example of a factoring transaction, see the introduction to the *Guide*, paras. 31-34).

58. The law recommended in the *Guide* also applies to transfers of all movable assets for security purposes, which it treats as transactions giving rise to a security right (see recommendations 2, subpara. (d), and 8). Thus, if a State enacts the recommendations of the *Guide*, a transfer of intellectual property (whether of full title or rights limited in scope, time or territory) for security purposes would be treated as a secured transaction. This approach of the law recommended in the *Guide* is based on the principle that, in determining whether a transaction is a secured transaction or not, substance prevails over form. Accordingly, parties will be able to create a security right in intellectual property simply by using the methods provided in the law recommended in the *Guide* without the need to adopt other formalities of a “transfer”. This result will not affect licensing practices as, under the law recommended in the *Guide*, a licence agreement does not in itself create a security right and a licence with the right to terminate the licence agreement is not a security right (see paras. 23-25 above).

59. The law recommended in the *Guide* does not apply to outright transfers of any movable asset other than receivables, including intellectual property (the term “assignment” is used in the *Guide* only with respect to receivables to avoid any implication that the recommendations that apply to the assignment of receivables apply more generally to security rights in intellectual property; see the introduction to the *Guide*, footnote 24; see also paras. 27 and 28 above). The law recommended in the *Guide* may, however, affect the rights of an outright transferee of an encumbered asset to the extent that there is a priority conflict between the rights of that transferee and the rights of a secured creditor with a security right in the asset. The reason for the exclusion of outright transfers of any movable asset other than receivables, including intellectual property, from the scope of the *Guide* is that they are normally subject to and sufficiently covered by other law, including law relating to intellectual property.

4. *Limitations in scope*

60. The *Guide* is based on the assumption that, in order to facilitate access to financing based on intellectual property, States enacting the recommendations of the *Guide* will include rules on security rights in intellectual property in their modern secured transactions regime. Accordingly, States enacting the recommendations of the *Guide* may wish to review their laws relating to intellectual property with a view to replacing all devices by way of which a security right in intellectual property may be created (including pledges, mortgages and conditional transfers) with the general concept of a security right. However, the *Guide* also recognizes that this must be done in a manner that is consistent with the policies and infrastructure of law relating to intellectual property of each enacting State.

61. The potential points of interaction between secured transactions law and law relating to intellectual property are dealt with in detail in the introduction (see paras. 2-7 above) and in various chapters of the *Supplement* (see, for example, paras. 229-232 below). As noted, the basic principle is set forth in recommendation 4, subparagraph (b), which provides that the law recommended in the *Guide* does not apply to “intellectual property in so far as the provisions of the law are inconsistent with national law or international agreements, to which the State (enacting the law recommended in the *Guide*) is a party, relating to intellectual property”. To provide a context for this more detailed discussion of the implications of recommendation 4, subparagraph (b), it is helpful at this point to delineate: (a) issues that are clearly the province of law relating to intellectual property and are not intended to be affected in any way by the *Guide*; and (b) issues on which a rule of the law recommended in the *Guide* may be pre-empted or supplemented by a rule of the law relating to intellectual property that regulates the same issue in a different manner from the *Guide*.

(a) Distinction between intellectual property rights and security rights in intellectual property rights

62. The law recommended in the *Guide* addresses only legal issues unique to secured transactions law as opposed to issues relating to the nature and legal attributes of the asset that is the object of the security right. The latter are the exclusive province of the body of property law that applies to the particular asset (with the partial unique exception of receivables to the extent that certain aspects of outright transfers of receivables are also covered in the law recommended in the *Guide*).

63. In the context of intellectual property financing, it follows that the law recommended in the *Guide* does not affect and does not purport to affect

issues relating to the existence, validity, enforceability and content of a grantor's intellectual property rights. These issues are determined solely by law relating to intellectual property. The secured creditor will need to pay attention to those rules in order to assess the existence and quality of the assets to be encumbered, but this would be the case with any type of encumbered asset (for example, whether a right to payment of funds credited to a bank account exists, its exact content and enforceability are matters for law other than secured transactions law). What follows is an indicative, non-exhaustive list of issues that may be addressed by law relating to intellectual property relevant to that assessment. Law relating to intellectual property may also deal with issues not included in the following list.

Copyright

- (a) The determination of who is the author, joint author or right holder;
- (b) The duration of copyright protection;
- (c) The economic rights granted under the law and limitations on and exceptions to protection;
- (d) The nature of the protected subject matter (expression embodied in the work, as opposed to the idea behind it, and the dividing line between them);
- (e) The transferability of economic rights as a matter of law and the right to grant a licence;
- (f) The possibility of terminating a transfer or licence of copyright, or otherwise regulating a transfer or licence;
- (g) The scope and non-transferability of moral rights;
- (h) Presumptions relating to the exercise and transfer of rights and limitations relating to who may exercise rights; and
- (i) Attribution of original ownership in the case of commissioned works and works created by an employee within the scope of employment.

Neighbouring (allied or related) rights

- (a) The meaning and extent of neighbouring rights, including whether a State may recognize certain neighbouring rights within copyright or other law;
- (b) The persons entitled to claim neighbouring rights;

- (c) The type of protected expression;
- (d) The relationship between holders of neighbouring rights and holders of copyright;
- (e) The extent of exclusive rights or rights of equitable remuneration with respect to neighbouring rights;
- (f) Any connecting factors or formalities for protection, such as fixation, publication or notice;
- (g) Any limitations and exceptions to protection for neighbouring rights;
- (h) The duration of protection for neighbouring rights;
- (i) The transferability of any neighbouring rights as a matter of law and the right to grant licences;
- (j) The possibility of terminating a transfer or licence of neighbouring rights, or otherwise regulating a transfer or licence; and
- (k) The scope, duration and non-transferability of any related moral rights.

Patents

- (a) The determination of who is the patent owner or co-owner;
- (b) The validity of a patent;
- (c) The limitations on and exceptions to protection;
- (d) Scope and duration of protection;
- (e) The grounds for invalidity challenges (obviousness or lack of novelty);
- (f) Whether certain prior publication is excluded from prior art and thus may not preclude patentability;
- (g) Whether protection is granted to a person who first invented the invention or to a person who first filed an application; and
- (h) The transferability of a patent and the right to grant a licence in a patent.

Trademarks and service marks

- (a) The determination of who is the first user or the owner of the mark;
- (b) Whether protection of the mark is granted to a person that uses the mark first or to a person that files an application first and whether protection

is granted to a subsequently registered mark if it conflicts with a previously registered mark;

(c) Whether *ex ante* use is a prerequisite to registration in a mark registry or whether the right is secured by initial registration and maintained by later use;

(d) The basis of protection of the right (distinctiveness);

(e) The basis for losing protection (holder's failure to ensure that the mark retains its association with the owner's products in the marketplace), as in the case of:

(i) Licensing without the licensor directly or indirectly controlling the quality or character of the products or services associated with the mark (so called "naked licensing"); and

(ii) Altering the mark so its appearance does not match the mark as registered; and

(f) Whether the mark may be transferred with or without goodwill.

(b) Areas of potential overlap between secured transactions law and law relating to intellectual property

64. The issues just addressed do not create any necessity for deference to law relating to intellectual property, since the law recommended in the *Guide* does not purport to address these issues. In other words, they are not issues where the principle of recommendation 4, subparagraph (b), has any application. The deference issue arises when the law relating to intellectual property of the State enacting the law recommended in the *Guide* provides an intellectual-property-specific rule on an issue falling within the scope of the law recommended in the *Guide*, namely, an issue relating to the creation, third-party effectiveness, priority, enforcement of or law applicable to a security right in intellectual property (see paras. 2-7 above).

65. The precise scope and implications of deference to law relating to intellectual property cannot be stated in the abstract since there is great variation among States on the extent to which intellectual-property-specific rules have been established, and indeed even within the same State depending on which category of intellectual property is at issue. In addition, the harmonization and modernization of the secured financing law achieved through the law recommended in the *Guide* has its limitations, since that law addresses issues of secured transactions law only and, under certain conditions, defers to law relating to intellectual property (see the *Guide*, recommendation 4, subpara. (b)). Another fact that limits the impact of the law recommended in the *Guide* is that law relating to intellectual property

in the various States does not address all secured transactions law issues in a comprehensive or coordinated way. For this reason, optimal results can only be obtained if the harmonization and modernization of secured transactions law achieved through the law recommended in the *Guide* is accompanied by a review of law relating to intellectual property to ensure compatibility and coordination with the secured transactions law recommended in the *Guide*. The examples set forth below illustrate some typically encountered patterns.

Example 1

66. In some States where security rights are created by a transfer of title to the encumbered asset, a security right may not be created in a trademark. The reason is a concern that the secured creditor's title would impair the quality control required of the trademark holder. Adoption of the law recommended in the *Guide* by such a State would make transfers of title unnecessary to create a security right in a trademark and eliminate the rationale for this prohibition, since the grantor retains ownership of the encumbered trademark under the concept of security right of the law recommended in the *Guide*. Whether the secured creditor may become the owner, licensor or licensee of rights in the trademark for the purposes of law relating to intellectual property is a different matter (for purposes of secured transactions law, a secured creditor does not become the owner, licensor or licensee; see paras. 8, 29 and 30 above, as well as paras. 87 and 88 below). Nonetheless, adoption of the law recommended in the *Guide* would not automatically eliminate the prohibition, because, to the extent that it is inconsistent with law relating to intellectual property, the law recommended in the *Guide* defers to that law. As a result, a specific amendment to the relevant law relating to intellectual property may be needed to harmonize it with the law recommended in the *Guide*.

Example 2

67. In some States, only transfers of intellectual property (whether outright or for security purposes) may be registered in a specialized intellectual property registry and such registration is mandatory for the effectiveness of a transfer. In other States, a security right in intellectual property may also be registered and such registration has constitutive or third-party effects. In view of the principle of deference to law relating to intellectual property embodied in recommendation 4, subparagraph (b), adoption of the law

recommended in the *Guide* would not affect the operation of such a rule and such specialized registration will continue to be required. However, deference to law relating to intellectual property will not always be sufficient to address the issue of coordination between the general security rights registry and intellectual property registries (see paras. 135-140 below) or the question whether a security right may be created in and a notice may refer to a future intellectual property right (see paras. 113-118 and 141-143 below).

Example 3

68. In some States, law relating to intellectual property provides for registration of both outright transfers and security rights in various intellectual property registries, but registration is not a mandatory precondition to effectiveness. However, registration has priority consequences in that rights arising from an unregistered transaction can be subject to rights arising from a registered transaction. In the case of such a State, recommendation 4, subparagraph (b), would preserve that rule of law relating to intellectual property of the State and, accordingly, a secured creditor desiring optimal protection may need to register both a notice of its security right in the general security rights registry and the security agreement or a notice thereof in the relevant intellectual property registry (although, if the intellectual property registry permits registration of security rights, registration there would be sufficient for all purposes). This is because: (a) registration in that State's general security rights registry is a necessary prerequisite to third-party effectiveness under secured transactions law (unless law relating to intellectual property allows registration of a security right in the relevant intellectual property registry to achieve third-party effectiveness); and (b) registration in the intellectual property registry will be necessary to protect the secured creditor against the risk of finding its security right affected by the rights of a competing transferee or secured creditor registered in the intellectual property registry pursuant to the priority rules of law relating to intellectual property.

69. In some States, registration of transfers and security rights in the relevant intellectual property registry provides protection only against a prior unregistered transfer or security right and only if the person with the registered right took its rights without notice of the prior unregistered right (the law recommended in the *Guide* would defer to this rule as it is a rule of law relating to intellectual property rather than a general rule of secured transactions law present throughout the State's legal system; see recommendation 4, subpara. (b)). In those States, adoption of the law

recommended in the *Guide* will raise the further question as to whether registration of a notice of a security right in intellectual property in the general security rights registry constitutes constructive notice to a subsequent transferee or secured creditor that registers its transfer or security right in the intellectual property registry. If so, under the law of such a State, it would be unnecessary for a secured creditor that has registered a notice of its security right in the general security rights registry to also register a document or notice thereof in the intellectual property registry in order to prevail as against subsequent transferees and secured creditors. Otherwise, under the law of that State, registration of a document or notice of the security right in the intellectual property registry may be required to gain priority over subsequent transferees and secured creditors. States enacting the recommendations of the *Guide* and the *Supplement* may wish to address this question.

Example 4

70. As a matter of law relating to intellectual property, some States provide for registration in the relevant intellectual property registry of a document or notice of a transfer of, but not of a security right in, intellectual property. In such situations, registration has priority consequences only as between transferees and not as between a transferee and a secured creditor. In States that adopt this approach, a secured creditor will need to ensure that a document or notice of all transfers of intellectual property to its grantor is duly registered in the intellectual property registry so as to avoid the risk of the grantor's title being defeated by the subsequently registered rights of a transferee. Likewise, the secured creditor will need to ensure that a document or notice of a transfer for security purposes made to it by the grantor is duly registered in the intellectual property registry in order to avoid the risk that the rights of a subsequent transferee of the grantor will defeat the rights arising from the security transfer in favour of the secured creditor. In all other respects, however, the secured creditor's rights will be determined by the secured transactions regime.

Example 5

71. As a matter of law relating to intellectual property, in some States registration of a document or notice of a transfer and a security right in an intellectual property registry is purely permissive and intended only to facilitate identification of the current owner. Failure to register neither invalidates the transaction nor affects its priority (although it might create evidentiary

presumptions). In States that adopt this approach, the position is essentially the same as when no specialized registry exists at all. Where these issues are dealt with by law relating to intellectual property, the law recommended in the *Guide* defers to it. Where, however, these issues are left to be determined by general property law, no issue of deference arises since the pre-*Guide* rules were derived not from the law relating to intellectual property but rather from property law generally. Thus, adoption of the law recommended in the *Guide* will replace the existing rules on creation, third-party effectiveness, priority, enforcement and law applicable to security rights in intellectual property. The old rules on these issues will continue to apply to outright transfers of intellectual property since the law recommended in the *Guide* only covers security rights in intellectual property. Consequently, the secured creditor will need to verify whether a purported transfer is actually an outright transfer or a disguised secured transaction (that is, a transaction that, although not called a secured transaction by the parties, serves security purposes). However, this type of risk management is no different from that necessary for any other type of encumbered asset for which a specialized registry does not exist.

Example 6

72. The question of who is the intellectual property owner in a chain of transferees of intellectual property is a matter of law relating to intellectual property. At the same time, the question of whether a transfer is an outright transfer or a transfer for security purposes is a matter of general property and secured transactions law. Finally, the rights and obligations flowing from a licence agreement is a matter of law relating to intellectual property and contract law. If a State adopts the law recommended in the *Guide*, transfers for security purposes will be treated as secured transactions.

Example 7

73. If law relating to intellectual property has specialized rules governing specifically the enforcement of a security right in intellectual property, these rules will prevail over the enforcement regime recommended in the *Guide*. However, if there is no specific rule of law relating to intellectual property on the matter and the enforcement of security rights in intellectual property is a matter left to general civil procedure law, the enforcement regime for security rights recommended in the *Guide* would take precedence. Similarly, if there is no specific rule of law relating to intellectual property on extrajudicial enforcement, the relevant regime recommended in the *Guide* on extrajudicial enforcement of security rights would apply (see paras. 229-232 below).

B. Application of the principle of party autonomy to security rights in intellectual property

74. The law recommended in the *Guide* generally recognizes the principle of party autonomy, although it does set forth a number of exceptions (see recommendations 10 and 111-113). This principle applies equally to security rights in intellectual property to the extent that law relating to intellectual property does not limit party autonomy (see para. 222 below). It should be noted that recommendations 111-113 apply only to tangible assets, as they refer to possession, a notion which in the *Guide* means “actual” possession and thus is not applicable to intangible assets (see the term “possession” in the introduction of the *Guide*, sect. B, para. 20).

75. An example of the application of the principle of party autonomy in secured transactions relating to intellectual property would be the following: if not prohibited by law relating to intellectual property, under secured transactions law, a grantor and a secured creditor may agree that the secured creditor may acquire certain rights of an owner, licensor or licensee and thus become an owner, licensor or licensee entitled to deal with public authorities (for example, to register or renew registrations), as well as to pursue infringers, make further transfers or grant licences. This agreement could take the form of a special clause in the security agreement or a separate agreement between the grantor and the secured creditor, since, under the *Guide*, a secured creditor does not, by the mere fact of obtaining a security right, become an owner, licensor or licensee (see paras. 26, 29 and 30 above and paras. 87 and 88 below).

76. Another example of the application of the principle of party autonomy would be the following: if not prohibited by law relating to intellectual property, under secured transactions law, a grantor and a secured creditor may agree that damages for infringement, as well as for lost profits and devaluation of the encumbered intellectual property, are included in the original encumbered assets. In the absence of such an agreement, such damages may still be treated as proceeds under the law recommended in the *Guide*, provided that that treatment is not inconsistent with law relating to intellectual property (see recommendation 4, subpara. (b)). However, the right to pursue infringement claims (as opposed to the right to the payment of damages for infringement) is a different matter. Typically, under law relating to intellectual property, this right cannot be used as security for credit. In addition, under the law recommended in the *Guide*, this right would not constitute proceeds as it would not fall under the scope of “whatever is received in respect of encumbered assets” (see the term “proceeds” in the introduction to the *Guide*, sect. B, para. 20).

II. Creation of a security right in intellectual property

A. The concepts of creation and third-party effectiveness

77. With respect to all types of encumbered asset (including intellectual property), the law recommended in the *Guide* draws a distinction between the creation of a security right (its effectiveness as between the parties) and its effectiveness against third parties, providing distinct requirements to achieve each of these outcomes. In effect, this means that the requirements for the creation of a security right can be kept to a minimum, while any additional requirements are aimed at addressing the rights of third parties. The main reason for this distinction is to achieve three of the key objectives of the law recommended in the *Guide*, namely, to establish a security right in a simple and efficient way, to enhance certainty and transparency, and to establish clear priority rules (see the *Guide*, recommendation 1, subparas. (c), (f) and (g)).

78. Under the law recommended in the *Guide*, a security right in intellectual property may be created by written agreement between the grantor and the secured creditor (see the *Guide*, recommendation 13, and paras. 82-85 below). For the security right to be effective against third parties, under the general rule recommended in the *Guide*, an additional step is required (see recommendation 29; for exceptions, see recommendations 34, subpara. (b), 39-41, and 43-45). For most intangible assets, this step is registration of a notice about the possible existence of the security right in a public registry, which also establishes an objective criterion for determining priority between a secured creditor and a competing claimant (see the *Guide*, recommendations 32 and 33; for the term “competing claimant”, see paras. 10 and 11 above). Accordingly, if a security right has been created in accordance with the requirements set forth in the law recommended in the *Guide*, the security right is effective between the grantor and the secured creditor even if the additional steps necessary to make the security right effective against third parties have not yet been taken (see recommendation 30). As a result, the secured creditor may enforce the security right in accordance with the enforcement procedures set forth in chapter VIII of the law recommended in the *Guide*, subject to the rights of competing claimants in accordance with the priority rules set forth in chapter V.

79. This distinction between creation and effectiveness against third parties applies equally to security rights in intellectual property. Thus, under the law recommended in the *Guide*, a security right in intellectual property can be effective between the grantor and the secured creditor even if it is not effective against third parties. In some States, law relating to intellectual property draws such a distinction. In other States, however, such a distinction is not drawn in law relating to intellectual property, which provides that the same actions are required for both the creation of a security right and its effectiveness against third parties. In such a case, as required by recommendation 4, subparagraph (b), the law recommended in the *Guide* defers to that law. To ensure better coordination between secured transactions law and law relating to intellectual property, States enacting the law recommended in the *Guide* may wish to consider reviewing their law relating to intellectual property. Such a review should make it possible for States to determine whether: (a) the fact that law relating to intellectual property does not draw a distinction between creation and third-party effectiveness of a security right in intellectual property serves specific policy objectives of law relating to intellectual property (rather than other law, such as general property law, contract law or secured transactions law) and should be retained; or (b) the distinction should be introduced in law relating to intellectual property so as to harmonize it with the relevant approach of the law recommended in the *Guide*.

B. Functional, integrated and unitary concept of a security right

80. To the extent that law relating to intellectual property permits the creation of a security right in intellectual property, it may do so by referring to outright or conditional transfers of intellectual property, mortgages, pledges, trusts or similar terms. The *Guide* uses the term “security right” to refer to property rights in movable assets that are created by agreement and secure payment or other performance of an obligation, regardless of whether the parties have denominated it as a security right (thus, transfers for security purposes are covered as security devices; see the term “security right” in the introduction to the *Guide*, sect. B, para. 20). This approach is referred to as the “functional, integrated and comprehensive approach” to secured transactions (see the *Guide*, chap. I, paras. 101-112, and recommendation 8). The *Guide* contemplates, by exception, that States may adopt a non-unitary approach in the limited context of acquisition financing and may retain transactions denominated as retention of title or financial lease of tangible assets (see the *Guide*, chap. IX).

81. A similar approach may be followed with respect to: (a) conditional transfers of an intellectual property right or of a licence of an intellectual property right in which the transferor is the secured creditor and the transfer of the intellectual property right or of the licence does not take place until the transferee pays any unpaid portion of the purchase price or meets any obligation incurred or repays any credit provided to enable the transferee to acquire the intellectual property right or the licence; (b) outright transfers of an intellectual property right or of a licence in which the transferee obtains the intellectual property right or the licence on credit and creates a security right in favour of the transferor to secure any unpaid portion of the purchase price or any obligation incurred or credit provided to enable the transferee to acquire the intellectual property or the licence; (c) retention-of-title transactions with respect to an intellectual property right or a licence in which the seller is the secured creditor and the buyer does not obtain the intellectual property right or the licence until the buyer pays any unpaid portion of the purchase price or meets any obligation incurred or repays any credit provided to enable the buyer to acquire the intellectual property right or the licence; or (d) financial lease kind of transactions with respect to an intellectual property right or a licence in which the lessor is the secured creditor and the lessee may exploit the intellectual property right or the license only as long as the lessee pays lease instalments or meets any obligation incurred or repays any credit provided to enable the lessee to acquire the right to exploit the intellectual property right or the licence (see the term “acquisition security right” in the introduction to the *Guide*, sect. B, para. 20; see also chap. IX below). Thus, States enacting the law recommended in the *Guide* may wish to review their law relating to intellectual property with a view to: (a) replacing all terms used to refer to the right of a secured creditor with the term “security right”; or (b) providing that, whatever the term used, rights performing security functions are treated in the same way and that such a way is not inconsistent with the treatment of security rights in the law recommended in the *Guide*.

C. Requirements for the creation of a security right in intellectual property

82. As already mentioned (see para. 78), under the law recommended in the *Guide*, the creation of a security right in an intangible asset requires a written document, which by itself or in conjunction with the course of conduct between the parties evidences the agreement of the parties to create a security right. In addition, the grantor must have rights in the asset to be encumbered or the power to encumber it either at the time of the conclusion

of the security agreement or thereafter. The agreement must reflect the intent of the parties to create a security right, identify the secured creditor and the grantor, and describe the secured obligation and the encumbered assets in a manner that reasonably allows their identification (see the *Guide*, recommendations 13-15). No additional step is required for the creation of a security right in an intangible asset. The additional steps (for example, registration of a notice in a general security rights registry) required for third-party effectiveness of that security right are not required for the security right to be created and thus be effective as between the grantor and the secured creditor.

83. However, law relating to intellectual property in many States imposes different requirements for the creation of a security right in intellectual property (which may take the form, for example, of a transfer for security purposes, a mortgage or pledge of intellectual property). For example, registration of a document or notice of a security right in intellectual property in the relevant intellectual property registry may be required for the creation of the security right. In addition, under law relating to intellectual property, the intellectual property to be encumbered may need to be described specifically in a security agreement (see para. 84 below). Similarly, as some intellectual property registries in these States index registered transactions by the specific intellectual property to which they relate, and not by the grantor's name or other identifier, registration of a document that merely states "all intellectual property of the grantor" would not be possible in these States and this would not create a security right (see para. 142 below). It would instead be necessary to identify each intellectual property right in the security agreement or in any other document to be registered in the intellectual property registry for the purposes of creating the security right.

84. Specific identification of the encumbered intellectual property right will often be necessary with respect to various types of intellectual property right such as, for example, a patent or a copyright. This may be so because, under law relating to intellectual property, an intellectual property right is often conceptualized as comprising a bundle of rights and, unless the parties intended to encumber all those rights, they may need to describe the assets to be encumbered specifically in the security agreement. In such a case, law relating to intellectual property may require a specific description for certainty as to the assets that are subject to a security right. Under such an approach, the intellectual property owner may use other concrete rights not covered by that specific description to obtain credit from another credit provider. It should also be noted that the nature of an intellectual property right as a bundle of rights allows the parties to encumber rights either as a bundle of rights or as separate rights, if they wish. Thus, if the parties wish to describe the encumbered intellectual property rights in a specific way,

they are always entitled to do so and will probably do so in most cases; but this should not deprive the parties of the right to describe the encumbered intellectual property rights in a general way, unless otherwise required by law relating to intellectual property.

85. The standard to be met with regard to the description of the encumbered assets in the security agreement under the law recommended in the *Guide* is sufficiently flexible to accommodate all different situations in that it refers to a description of the encumbered assets “in a manner that reasonably allows their identification” (see recommendation 14, subpara. (d)); the same standard applies to the notice to be registered (see para. 141, below and the *Guide*, recommendation 63). Thus, this standard could vary depending on what is a reasonable description under the relevant law and practice with respect to the particular encumbered asset. Furthermore, in all these situations, under the principle embodied in recommendation 4, subparagraph (b), the law recommended in the *Guide* would apply only in so far as it is not inconsistent with law relating to intellectual property. States enacting the law recommended in the *Guide* may wish to consider reviewing their laws relating to intellectual property to determine whether the different concepts and requirements with respect to the creation of security rights in intellectual property serve specific policy objectives of law relating to intellectual property and should be retained or whether they should be harmonized with the relevant concepts and requirements of the law recommended in the *Guide*.

D. Rights of a grantor with respect to the intellectual property to be encumbered

86. As already mentioned (see para. 82), a grantor of a security right must have rights in the asset to be encumbered or the power to encumber it at the time of the security agreement or at a later time (see the *Guide*, recommendation 13). This is a principle of secured transactions law that applies equally to intellectual property. A grantor may encumber its full rights or only limited rights. So, an intellectual property owner, licensor or licensee may encumber its full rights or rights limited in time, scope or territory. In addition, a grantor may encumber its assets only to the extent that the assets are transferable under general property law (the law recommended in the *Guide* does not affect such limitations; see the *Guide*, recommendation 18, and paras. 119 and 120 below). This principle also applies to secured transactions relating to intellectual property. So, an owner, licensor or licensee may only encumber its rights to the extent that those rights are transferable under law relating to intellectual property.

E. Distinction between a secured creditor and an owner with respect to intellectual property

87. For the purposes of the law recommended in the *Guide*, the secured creditor does not become an owner, licensor or licensee (depending on the rights of the grantor) on the sole ground that it acquired a security right in intellectual property. This may also be the case though under law relating to intellectual property (see the terms “owner” and “secured creditor”, paras. 26, 29 and 30 above). However, the exercise of the secured creditor’s rights upon default of the grantor will often result in the grantor’s encumbered intellectual property rights being transferred and, thus, the identity of the owner, licensor or licensee (depending on the rights of the grantor), as determined by law relating to intellectual property, might change. This may happen in situations in which the enforcement of the security right in the intellectual property results in acquisition of the encumbered intellectual property by the secured creditor in a disposition (see paras. 237 and 238 below and the *Guide*, recommendations 142 and 148) or in an acquisition of the encumbered intellectual property by the secured creditor in total or partial satisfaction of the secured obligation (see para. 242 below and the *Guide*, recommendations 156-159).

88. In any case, the question of who is the owner, licensor or licensee with respect to intellectual property and whether the parties may determine it for themselves is a matter of law relating to intellectual property. As already mentioned (see para. 87), under law relating to intellectual property, a secured creditor may at times be treated as an owner, licensor or licensee. Should law relating to intellectual property so provide, the secured creditor could, for example, renew registrations or pursue infringers or agree with the owner, licensor or licensee that the secured creditor will become the owner, licensor or licensee (see paras. 223-226 below).

F. Types of encumbered asset in an intellectual property context

89. Under the law recommended in the *Guide*, a security right may be created not only in the rights of an intellectual property owner but also in the rights of a licensor or licensee under a licence agreement (see the term “encumbered asset”, paras. 13-16, 54 and 55 above). In addition, although a security right in a tangible asset with respect to which intellectual property is used (for example, designer watches or clothes bearing a trademark) does not extend to the intellectual property (see paras. 108-112 below), such a

security right may have an impact on the intellectual property used with respect to the tangible asset to the extent the secured creditor may enforce its security right in the tangible asset (see paras. 245-248 below). As already mentioned (see paras. 82-85), under the law recommended in the *Guide*, the intellectual property to be encumbered needs to be described in the security agreement in a manner that reasonably allows its identification and this standard is sufficiently flexible to accommodate any requirements of law relating to intellectual property for a specific description of intellectual property to be encumbered (see the *Guide*, recommendation 14, subpara. (d)).

90. It should be noted that the law recommended in the *Guide* does not override any provisions of law relating to intellectual property (or other law) that limit the creation or enforcement of a security right or the transferability of an intellectual property (or other) asset (see recommendation 18). In addition, the law recommended in the *Guide* does not affect contractual limitations to the transferability of intellectual property rights (recommendation 23 deals only with contractual limitations on the assignability of receivables). As a result of these two recommendations, if, under law relating to intellectual property, a security right may not be created or enforced in an intellectual property right or if that intellectual property right is non-transferable by law or contract, the law recommended in the *Guide* will not interfere with these limitations (see paras. 119 and 120 below). The law recommended in the *Guide*, however, does override legal limitations to the assignability of future receivables or of receivables assigned in bulk or in part on the sole ground that they are future receivables or are assigned in bulk or in part (see recommendation 23). In addition, under certain conditions, the law recommended in the *Guide* affects contractual limitations to the assignability of receivables (without affecting the different treatment of receivables for purposes of law relating to intellectual property; see the *Guide*, recommendation 24, and paras. 102-105 below). As a result, to the extent that the law recommended in the *Guide* is enacted by a State, these legal or contractual limitations to the assignability of such receivables will no longer apply.

1. Rights of an owner

91. The law recommended in the *Guide* applies to secured transactions in which the encumbered assets are the rights of an intellectual property owner (see paras. 13-16, 54 and 55 above). Typically, the essence of the rights of an owner is the right to enjoy its intellectual property, the right to prevent unauthorized use of its intellectual property and to pursue infringers, the

right to register intellectual property and renew registrations, the right to authorize others to use or exploit the intellectual property and the right to collect royalties (for the owner's rights to preserve the encumbered intellectual property by pursuing infringers and renewing registrations, see paras. 93-95 below).

92. If, under law relating to intellectual property, these rights are transferable, the owner may encumber all or some of them with a security right under the law recommended in the *Guide*, which will apply to such a security right subject to recommendation 4, subparagraph (b). In such a case, all these rights would constitute the original encumbered assets (any rights to the payment of royalties would be proceeds of the owner's rights, unless included in the description of the encumbered assets in the security agreement). If these rights may not be transferred under law relating to intellectual property, they may not be encumbered by a security right under the law recommended in the *Guide*, since, as already mentioned (see para. 90), the law recommended in the *Guide* does not affect legal provisions that limit the creation or enforcement of a security right, or the transferability of assets, with the exception of provisions relating to the assignability of future receivables and receivables assigned in bulk (see the *Guide*, recommendation 18, and paras. 98-101 below).

93. Whether the right of an owner to preserve its intellectual property (for example, by pursuing infringers and obtaining an injunction and/or monetary compensation) may be transferred separately from the other rights of the owner is a matter of law relating to intellectual property. Typically, under law relating to intellectual property, the right to pursue infringers is part of the owner's rights and cannot be transferred separately from the owner's rights. However, the grantor as an owner and the secured creditor, under secured transactions law, may agree that the secured creditor may acquire this right, if acquisition of such a right by the secured creditor is not prohibited by law relating to intellectual property (see paras. 74-76 above and paras. 223-226 below).

94. In addition, unless prohibited by law relating to intellectual property, the grantor as an owner and the secured creditor may agree that the benefits from the exercise of the right of the grantor to pursue infringers (such as the right to the payment of damages arising from an infringement once exercised) are included in the original encumbered intellectual property. Thus, in cases where law relating to intellectual property treats such benefits as a movable asset that may be transferred separately from the owner's rights, the question of whether a security right may be created in those benefits would be a matter of secured transactions law (subject to the limitation introduced by recommendation 4, subpara. (b)).

95. For example, if, before or after the creation of a security right in the rights of an intellectual property owner, an infringement has been committed, and after the creation of such a security right, the owner has sued infringers and infringers have paid compensation to the owner, the secured creditor may be able to claim the compensation paid either as proceeds of the original encumbered intellectual property or as an original encumbered asset if properly so described in the security agreement. If the compensation has not been paid at the time of creation of the security right, but is paid later after default of the grantor (owner), the secured creditor could also be able to claim the compensation paid either as proceeds of the original encumbered intellectual property or, if appropriately so described in the security agreement, as an original encumbered asset. To the contrary, under law relating to intellectual property, the right to pursue infringers would normally not constitute proceeds of the original encumbered intellectual property or an original encumbered asset (see para. 93 above). However, if the grantor (owner) has filed a suit against an infringer and the lawsuit is still pending at the time of enforcement of the security right, a person that acquired the grantor's rights in the encumbered intellectual property in the context of enforcement of the security right should be able to take over the lawsuit and obtain any compensation granted (again, if permitted under law relating to intellectual property).

96. Similar considerations apply to the question of whether the right to deal with authorities at the various stages of the registration process (for example, the right to file an application for the registration of intellectual property, the right to register intellectual property or the right to renew a registration of intellectual property) or the right to grant licences may be transferred, and thus be part of the encumbered intellectual property. Whether the right to deal with authorities or to grant licences may be transferred or is an inalienable right of the owner is a matter of law relating to intellectual property. Whether it is part of the encumbered rights of the owner is a matter of the description of the encumbered asset in the security agreement, assuming that it may be transferred under law relating to intellectual property.

2. *Rights of a licensor*

97. Under the law recommended in the *Guide*, a security right may be created in a licensor's rights under a licence agreement (see paras. 13-16, 54 and 55 above). If a licensor is an owner, it can create a security right in (all or part of) its rights as mentioned above (see paras. 91-96 above).

If a licensor is not an owner but a licensee that grants a sub-licence, typically, it may create a security right in its right to the payment of royalties owed by sub-licensees under the sub-licence agreement. In such a case where the grantor creating a security right in sub-royalties is a licensor but not the intellectual property owner, the sub-royalties would be the original encumbered assets; where the grantor creating a security right in the intellectual property itself is the intellectual property owner, the sub-royalties would be proceeds of the original encumbered intellectual property, unless the sub-royalties were included in the description of the original encumbered assets in the security agreement (for the licensee's rights, see paras. 106 and 107 below). Such a licensor may also create a security right in other contractual rights of value that the licensor might have under the licence agreement and the relevant law. These other contractual rights might include, for example: (a) the licensor's right to compel the licensee to advertise the licensed intellectual property or product with respect to which the intellectual property is used; (b) the licensor's right to compel the licensee to market the licensed intellectual property only in a particular manner; and (c) the licensor's right to terminate the licence agreement as a result of breach by the licensee.

98. Following the approach taken in most legal systems and reflected in the United Nations Assignment Convention (see art. 2), the law recommended in the *Guide* treats rights to the payment of royalties arising from the licence of intellectual property as receivables (see the term "receivable" in the introduction to the *Guide*, sect. B, para. 20). This means that the general discussion and recommendations dealing with security rights, as modified by the receivables-specific discussion and recommendations of the *Guide*, apply to rights to the payment of royalties. Thus, under the law recommended in the *Guide*, statutory prohibitions that relate to the assignment of future receivables or receivables assigned in bulk or in part on the sole ground that they are future receivables or receivables that are assigned in bulk or in part are rendered unenforceable (see the *Guide*, recommendation 23). However, other statutory prohibitions or limitations are not affected (see recommendation 18). In addition, a licensee could raise against an assignee of the licensor's right to the payment of royalties all defences or rights of set-off arising from the licence agreement or any other agreement that was part of the same transaction (see recommendation 120).

99. In this context, it is important to note that the statutory prohibitions rendered unenforceable by the *Guide* refer to future receivables only as future receivables, or receivables assigned in bulk or in part. They do not affect legal prohibitions based on the nature of receivables, for example, as wages or royalties that may by law be payable directly only to authors or collecting societies. Many countries have "author-protective" or similar

legislation that designates a certain portion of income earned from exploitation of the intellectual property rights as “equitable remuneration” or the like that must be paid to authors or other entitled parties or their collecting societies. These laws often make such payment rights expressly non-assignable. The *Guide*’s recommendations with respect to legal limitations on the assignment of receivables do not apply to these or other similar legal limitations.

100. Furthermore, it is important to note that the treatment of the right to the payment of royalties as receivables for the purposes of the secured transactions law recommended in the *Guide* does not affect the different treatment of this right to the payment of royalties for the purposes of law relating to intellectual property.

101. Finally, it is equally important to note that the treatment of rights to receive payment of royalties in the same way as any other receivable does not affect the terms and conditions of the licence agreement relating to the payment of royalties, such as that payments are to be staggered or that there might be percentage payments depending on market conditions or sales figures (for the principle of respecting licence agreements under the law recommended in the *Guide*, see paras. 23-25 above, as well as paras. 107, 158, 159, 187, 191 and 192 below).

102. Under the law recommended in the *Guide*, if a licence agreement, under which royalties are payable, includes a contractual provision that restricts the ability of the licensor to assign the right to the payment of royalties to a third party (“assignee”), an assignment of the right to the payment of royalties by the licensor is nonetheless effective and the licensee cannot terminate the licence agreement on the sole ground of the assignment by the licensor of the right to the payment of royalties (see the *Guide*, recommendation 24). However, under the law recommended in the *Guide*, the rights of a licensee (as a debtor of the assigned receivables) are not affected except as otherwise provided in the secured transactions law recommended in the *Guide* (see recommendation 117, subpara. (a)). Specifically, the licensee is entitled to raise against the assignee all defences or rights of set-off arising from the licence agreement or any other agreement that was part of the same transaction (see recommendation 120, subpara. (a)). In addition, the law recommended in the *Guide* does not affect any liability that the licensor (or sub-licensor) may have under other law for breach of the anti-assignment agreement (see recommendation 24). As the term “licence” includes a sub-licence (see para. 23 above), the same principles apply to a provision in a sub-licence agreement under which a sub-licensee restricts the ability of its sub-licensor to assign the right to the payment of the sub-royalties due from the sub-licensee to the sub-licensor.

103. It is important to note that recommendation 24 applies only to receivables, and not to intellectual property rights. This means that it does not apply to an agreement between a licensor and a licensee according to which the licensee does not have the right to grant sub-licences (such an agreement would be one way for the licensor to control by agreement the licensed intellectual property, who can use it and the flow of royalty payments). It is equally important to note that recommendation 24 applies only to an agreement between a creditor of a receivable and the debtor of the receivable that the receivable owed to the creditor by the debtor may not be assigned. It does not apply to an agreement between a creditor of a receivable and the debtor of the receivable that the debtor may not assign receivables that may be owed to the debtor by third parties. Thus, recommendation 24 does not apply to an agreement between a licensor and a licensee that prohibits the licensee from assigning its right to payment of sub-royalties from third-party sub-licensees. Such an agreement would be another way for the licensor to control by agreement the flow of royalty payments and may exist, for example, where the licensor and the licensee agree that sub-royalties will be used by the licensee to further develop the licensed intellectual property. As a result, recommendation 24 does not affect the right of the licensor to negotiate the licence agreement with the licensee so as to control by agreement who can use the intellectual property or the flow of royalty payments from the licensee and sub-licensees. Breach of such licence agreements by the licensee would only make the licensee liable for damages and would not invalidate a security right created by the licensee in its right to the payment of sub-royalties. However, if the licence agreement is terminated by the licensor as a result of breach by the licensee, the latter would have no licence to sub-license and earn sub-royalties and its secured creditor would be deprived of its encumbered asset.

104. In addition, recommendation 24 does not apply to an agreement between a licensor and a licensee that the licensor will terminate the licence agreement if the licensee violates the agreement not to assign the right to the payment of royalties payable to the licensee by sub-licensees (such an agreement would be another way for the licensor to control by agreement the flow of royalty payments). In this context, it should be noted that the right of the licensor to terminate the licence agreement if the licensee breaches this agreement gives the sub-licensees a strong incentive to make sure that the licensor will receive payment. Moreover, recommendation 24 does not affect the right of the licensor: (a) to agree with the licensee that part of the licensee's royalties (representing a source for the payment of the royalties the licensee owes to the licensor) be paid by sub-licensees to an account in the name of the licensor; or (b) to obtain a security right in the licensee's right to the payment of royalties by sub-

licensees, register a notice in that regard in the general security rights registry (or the relevant intellectual property registry) and thus potentially obtain a security right with priority over the licensee's other creditors (subject to the recommendations of the *Guide* for obtaining third-party effectiveness and priority of security rights; see paras. 213-218 below).

105. Under the law recommended in the *Guide*, a secured creditor with a security right in a receivable has the benefit of a security right in intellectual property securing payment of the receivable (see recommendation 25). However, this does not mean that legal limitations on the transferability of intellectual property rights are set aside (see recommendation 18). Similarly, this does not mean that contractual limitations on the transferability of intellectual property rights are affected, as recommendation 24 applies to assignment of receivables and not to transfers of intellectual property rights.

3. Rights of a licensee

106. Under an intellectual property licence agreement and the law governing it, a licensee may have the right to grant sub-licences and to receive as a sub-licensor the payment of any royalties flowing from a sub-licence agreement. The discussion above with respect to the rights of a licensor (see paras. 97-105) would apply equally to the rights of a licensee as to those of a sub-licensor.

107. Typically, a licensee is authorized to use or exploit the licensed intellectual property in line with the terms and conditions of the licence agreement. Some laws relating to intellectual property provide that the licensee may not create a security right in its authorization to use or exploit the licensed intellectual property without the licensor's consent (although in many States an exception may arise where the licensee sells its business as a going concern). The reason is that it is important for the licensor to retain control over the licensed intellectual property and who can use it. If such control cannot be exercised, the value of the licensed intellectual property may be materially impaired or lost completely. If, however, the rights of a licensee under a licence agreement are transferable and the licensee creates a security right in them, the secured creditor will take a security right in the licensee's rights subject to the terms and conditions of the licence agreement. If the licence is transferable and the licensee transfers it, the transferee will take the licence subject to the terms and conditions of the licence agreement. The law recommended in the *Guide* does not affect these licensing practices.

4. *Tangible assets with respect to which intellectual property is used*

108. Intellectual property may be used with respect to a tangible asset. For example: (a) a tangible asset may be manufactured according to a patented process or through the exercise of patented rights; (b) jeans may bear a trademark and cars or other items may include a copy of copyrighted software or design rights; (c) a compact disc may contain a software programme; or (d) a heat pump may contain a patented component.

109. Where intellectual property is used in connection with a tangible asset, two different types of asset are involved. One is the intellectual property; another is the tangible asset. These assets are separate. Law relating to intellectual property allows an intellectual property owner to control many but not all uses of the tangible asset. For example, law relating to copyright allows an author to prevent unauthorized duplication of a book, but typically not to prevent an authorized bookstore that bought the book in an authorized sale to re-sell it or the end-buyer to make notes in the margin while reading. In essence, a security right in a tangible asset does not extend to the intellectual property used with respect to a tangible asset, and a security right in intellectual property does not extend to the tangible asset with respect to which the intellectual property is used. The *Supplement* recommends this approach (see recommendation 243 below).

110. However, under the law recommended in the *Guide*, the parties to the security agreement may always agree that a security right is created both in a tangible asset and in intellectual property used with respect to that asset (see recommendation 10). For example, a security right may be taken in inventory of trademarked jeans and in the trademark, giving the right to the secured creditor in the case of default of the grantor to sell both the encumbered trademarked jeans and the right to produce other jeans bearing the encumbered trademark. In such a case, where the manufacturer/grantor is the trademark owner, the encumbered assets are the owner's rights. Where the manufacturer/grantor is a licensee, the encumbered assets are the licensee's rights under the licence agreement (see paras. 43-45 above).

111. The exact extent of the security right depends on the description of the encumbered asset in the security agreement. As already noted (see paras. 82-85 above), a description of the encumbered assets "in a manner that reasonably allows their identification" is sufficiently flexible to accommodate all different situations (see the *Guide*, recommendation 14, subpara. (d)), as it sets a standard that could vary depending on what is a reasonable description under the relevant law and practice. It would thus seem that a general description

of the encumbered tangible asset would be in line with the principles of the *Guide* and the reasonable expectations of the parties. At the same time, key principles of law relating to intellectual property with respect to a specific description of intellectual property to be encumbered in a security agreement would be accommodated by the law recommended in the *Guide*. In any case, if, under the law recommended in the *Guide*, a general description of the encumbered intellectual property would be sufficient, while under law relating to intellectual property a specific description would be necessary, the latter requirement would apply to encumbered intellectual property under recommendation 4, subparagraph (b), of the *Guide*.

112. As already mentioned (see paras. 109 and 110), a security right in a tangible asset, with respect to which intellectual property is used, does not extend to the intellectual property (unless otherwise agreed), but it does encumber the tangible asset itself, including those characteristics of the asset that use the intellectual property (for example, the security right applies to a television set as a functioning television set). Thus, a security right in such an asset does not give the secured creditor the right to manufacture additional assets using the intellectual property. Upon default, however, the secured creditor with a security right in the tangible asset could exercise the remedies recognized under secured transactions law, provided that such exercise of remedies did not interfere with rights existing under law relating to intellectual property. It may be that, under applicable law relating to intellectual property, the “exhaustion doctrine” (or similar concepts) might apply and permit the enforcement of the security right (for a discussion of enforcement issues, see paras. 245-248 below).

G. Security rights in future intellectual property

113. The law recommended in the *Guide* provides that a person may grant a security right in a future asset, namely an asset created or acquired by the grantor after the creation of a security right (see recommendation 17). Like any other rule recommended in the *Guide*, this rule too applies to intellectual property, except in so far as it is inconsistent with law relating to intellectual property (see recommendation 4, subpara. (b)). Accordingly, under the law recommended in the *Guide*, a security right can be created in future intellectual property (as to legal limitations in that regard, see the *Guide*, recommendation 18, as well as paras. 119 and 120 below). This approach is justified by the commercial utility in allowing a security right to extend to future intellectual property.

114. Many laws relating to intellectual property follow the same approach, allowing intellectual property owners to obtain financing useful in the development of new works, provided that their value can be reasonably estimated in advance. For example, it is usually possible to create a security right in a copyrighted motion picture or software (the security right is created when the copyrighted work is created; see para. 40 above). In some States, a security right may be created in a patent application before the patent right is granted (typically, after the patent right is granted, it is considered as having been created at the time of the application).

115. However, in certain cases, law relating to intellectual property may limit the transferability of various types of future intellectual property to achieve specific policy goals. For example, in some cases, a transfer of rights in new media or technological uses that are unknown at the time of the transfer may not be effective in view of the need to protect authors from undue commitments. In other cases, transfers of future rights may be subject to a statutory right of cancellation after a certain period. In other cases, the notion of “future intellectual property” may include rights that have been created and that may be registered but that are not yet registered. Statutory prohibitions may also take the form of a requirement for a specific description of intellectual property.

116. Other limitations on the use of future intellectual property as security for credit may be the result of the meaning of the concepts of “improvements”, “updates”, “adaptations” or other changes to intellectual property under law relating to intellectual property. Such “other changes” in relation to copyrighted content can be, for example, changes regarding the quality of the content or the form of its delivery, such as the re-mastering or the digital conversion of a sound recording or new forms of electronic delivery of a sound recording that might lead to new, yet to be invented forms or uses, whether dependent or independent of any physical carrier.

117. The secured creditor should understand how these concepts are interpreted under law relating to intellectual property and how they may affect the concept of “ownership”, which is essential in the creation of a security right in intellectual property. For example, this determination is of particular relevance in the case of copyrighted software. In some States, a security right in a version of copyrighted software that exists at the time of the financing may extend automatically to modifications made to that version following the financing. However, typically law relating to intellectual property treats such future improvements as separate assets and not as integral parts of existing intellectual property. Thus, if future intellectual property rights may be encumbered, a prudent secured creditor that wishes to ensure that improvements are encumbered should describe the encumbered

asset in the security agreement in a manner that ensures that improvements are directly encumbered (see para. 241 below). If future intellectual property rights may not be encumbered, improvements may not be encumbered either and the law recommended in the *Guide* does not affect any such limitations (see recommendation 18).

118. If law relating to intellectual property limits the transferability of future intellectual property, the law recommended in the *Guide* does not apply to this matter in so far as it is inconsistent with law relating to intellectual property (see recommendation 4, subpara. (b)). Otherwise, the law recommended in the *Guide* applies and permits the creation of a security right in future assets (see recommendation 17). States enacting the law recommended in the *Guide* may wish to review their law relating to intellectual property with a view to establishing whether the benefits from these limitations (for example, the protection of the owner from undue commitments) outweigh the benefits from the use of such assets as security for credit (for example, the financing of research and development activities).

H. Legal or contractual limitations on the transferability of intellectual property

119. Specific rules of law relating to intellectual property may limit the ability of an intellectual property owner, licensor or licensee to create a security right in certain types of intellectual property. In many States, only the economic rights of an author are transferable; the moral rights are not transferable. In addition, legislation in many States provides that an author's right to receive equitable remuneration may not be transferable. Moreover, in many States, trademarks are not transferable without their associated goodwill. Finally, as is the case with assets other than intellectual property, an asset may not be encumbered by a person if that person does not have rights in the asset or the power to encumber it (see the *Guide*, recommendation 13, and the *nemo dat (quod non habet)* principle).⁹ The law recommended in the *Guide* respects all these limitations on the transferability of intellectual property (see recommendation 18).

120. The only legal limitations on the transferability of certain assets that the law recommended in the *Guide* may affect and remove are the legal

⁹Also known as the principle of *nemo plus juris ad alium transferre potest quam ipse habet* (no person can transfer to another a greater right than he has).

limitations on the transferability of future receivables, receivables assigned in bulk and parts of or undivided interests in receivables, as well as contractual limitations on the assignment of receivables arising from the sale or licence of intellectual property rights (see arts. 8 and 9 of the United Nations Assignment Convention and the *Guide*, recommendations 23-25). In addition, the law recommended in the *Guide* may affect and render ineffective contractual limitations, but only with respect to receivables (not intellectual property) and only in a certain context, that is, in an agreement between the creditor of a receivable and the debtor of that receivable (see paras. 102-104 above).

Recommendation 243¹⁰

Security rights in tangible assets with respect to which intellectual property is used

The law should provide that, in the case of a tangible asset with respect to which intellectual property is used, a security right in the tangible asset does not extend to the intellectual property and a security right in the intellectual property does not extend to the tangible asset.

¹⁰If it could be included in the *Guide*, this recommendation would be placed in chapter II, Creation of a security right, as recommendation 28 bis.

III. Effectiveness of a security right in intellectual property against third parties

A. The concept of third-party effectiveness

121. As already noted (see paras. 77-79), the law recommended in the *Guide* distinguishes between the creation of a security right (effectiveness of the security right as between the parties) and its effectiveness against third parties. This distinction applies equally to security rights in intellectual property. However, to the extent that law relating to intellectual property makes no such distinction and this is an intellectual-property-specific approach, the law recommended in the *Guide* would defer to that law (see recommendation 4, subpara. (b)).

122. In addition, in some States, the creation and third-party effectiveness of a security right in intellectual property are governed by the same rules that apply to a security right in other types of intangible asset. In other States, however, law relating to intellectual property may provide for particular methods in which a security right in some types of intellectual property may be created and made effective against third parties. The rules often differ for security rights in intellectual property that are subject to a specialized registration system (such as patents, trademarks and, in some States, copyrights) and security rights in intellectual property that are not subject to such registration (such as trade secrets, industrial designs and, in some States, copyrights). These matters are addressed in sections B and C below.

123. In the law recommended in the *Guide*, the concept of “effectiveness against third parties” refers to whether a security right in an encumbered asset as a property right is effective against parties other than the grantor and the secured creditor that have at that time or may acquire in the future a security or other right in that encumbered asset. Such third parties (“competing claimants”) include creditors of the grantor, the insolvency representative in the insolvency of the grantor, as well as transferees, lessees and licensees of the encumbered asset (see paras. 10 and 11 above). In law relating to intellectual property, by contrast, the phrase “third-party effectiveness” is often used to refer to the effectiveness of exclusive rights associated with ownership or rights of a licensor or licensee in intellectual property, rather

than to the effectiveness of a security right. These two sorts of reference should not be confused. While effectiveness of a security right in intellectual property as against third parties is a matter of secured transactions law, effectiveness of exclusive rights associated with ownership rights or rights of a licensor or licensee against transferees of those rights is a matter of law relating to intellectual property. In this context, it should be noted that, for purposes of secured transactions law, infringers are not competing claimants. Thus, the law recommended in the *Guide* does not apply to a “conflict” between the rights of a secured creditor and those of a purported infringer. In addition, if, for example, the purported infringer asserts as a defence against a secured creditor that the purported infringer is a transferee or a licensee of the encumbered intellectual property, the question of whether the purported infringer is in fact an infringer is to be determined in accordance with the law relating to intellectual property. Thereafter, if the purported infringer is proven to be a transferee or licensee (not an infringer) and a priority conflict arises between its rights and the rights of a secured creditor, the law recommended in the *Guide* applies to that priority conflict (see paras. 184-212 below).

B. Third-party effectiveness of security rights in intellectual property that are registered in an intellectual property registry

124. Under the law recommended in the *Guide*, security rights in intangible assets may be made effective against third parties by registration of a notice in the general security rights registry or of a document or notice in a specialized registry, if any. The law recommended in the *Guide* is based on the assumption that where a State maintains a specialized registry, it will permit registration of a document or notice of a security right as a method of achieving third-party effectiveness of the security right (see the *Guide*, recommendations 32, 34, subpara. (a) (ii), and 38, subpara. (a), and paras. 132-134 below).

125. Registration in an intellectual property registry differs from State to State in many respects, including: (a) whether transfers, licences or also security rights may be registered; (b) whether rights in patents, trademarks, copyrights or other types of intellectual property may be registered; (c) whether a document, a summary of a document or notice need be registered; and (d) what the legal consequences of registration are. In some cases, the answers to all these questions are not easy to obtain even in one and the same legal system.

126. For example, under law relating to intellectual property, in some States, a security right is not created or made effective against third parties unless and until a document or notice of it is registered in the relevant intellectual property registry. In other States, law relating to intellectual property provides that a security right is created and, at the same time, becomes effective against third parties when the security agreement is entered into between the parties, even without registration. In these cases, registration in the relevant intellectual property registry allows certain third parties (typically, transferees that are not aware that the asset is encumbered, that is, “good-faith transferees”) to invoke a priority rule, according to which a registered security right takes precedence over an unregistered prior security right, but the unregistered security right still remains effective against other third parties. In still other States, under law relating to intellectual property, a security right is created when the security agreement is entered into between the parties, but registration in the relevant intellectual property registry is necessary to make the security right effective against third parties, for example, by way of an evidentiary rule that prohibits evidence of unregistered security rights. In still other States, under law relating to intellectual property, the registration system does not readily accommodate registration of documents or notices of security rights, and creation and third-party effectiveness of security rights must be achieved outside the intellectual property registration system. Finally, in some States that distinguish between creation and third-party effectiveness, law relating to intellectual property provides that it is possible to achieve third-party effectiveness of a security right by using either the intellectual property registry or an available general security rights registry. If any of these methods existing under law relating to intellectual property is intended to be the exclusive method of obtaining effectiveness of a security right against third parties, in accordance with recommendation 4, subparagraph (b), it takes precedence over any of the methods provided in the law recommended in the *Guide*.

127. The *Guide* recommends a general security rights registry (see the *Guide*, chap. IV). In addition, where specialized registries exist that permit registration of a document or notice of a security right as a method of achieving third-party effectiveness of the security right, the *Guide* avoids undermining them. The *Guide* achieves that result by accepting registration in such a specialized registry as a method of achieving third-party effectiveness of a security right and attributing priority results to such a registration (see recommendations 38, 77 and 78). As this matter is beyond the scope of secured transactions law and, in any case, would require additional effort and expense by States, the *Guide* does not recommend that States that currently do not have a specialized registry for certain types of intellectual property create such a registry in order to permit the registration

of a document or notice of a security right in intellectual property. For the same reason, the *Guide* does not recommend that States that currently do not permit the registration of a document or notice of a security right in an intellectual property registry amend their laws to permit such registration. Finally, to avoid duplication of effort and expense, the *Guide* does not recommend a rule that requires registration of a document or notice of a security right in both the relevant intellectual property registry and in the general security rights registry. However, if States enacting the recommendations of the *Guide* have specialized intellectual property registries and wish to use them for registration of security rights in intellectual property, making use of the options offered in recommendation 38 of the *Guide*, they may wish to review their law relating to intellectual property and consider whether to permit the registration of notices of security rights with third-party effects in such already existing intellectual property registries. States that do not have specialized intellectual property registries or have such registries but do not wish to use them for registration of security rights in intellectual property, may always use the general security rights registry for registration of notices of security rights in all types of movable asset, including intellectual property.

C. Third-party effectiveness of security rights in intellectual property that are not registered in an intellectual property registry

128. As already mentioned (see para. 124), under the law recommended in the *Guide*, a security right in intellectual property may become effective against third parties by registration of a notice in the general security rights registry (see the *Guide*, recommendation 32). This is possible even if the encumbered intellectual property right may not be registered in an intellectual property registry (as is typically the case, for example, with copyrights, industrial designs or trade secrets). The same rule would apply in cases where a document or notice of a security right in intellectual property may be registered in an intellectual property registry but is not actually registered. In these cases, registration of a notice in the general security rights registry is sufficient and the legal consequence of registration is to make the security right effective against third parties (see the *Guide*, recommendations 29, 32, 33 and 38). However, in the particular case where law relating to intellectual property provides that a security right in intellectual property may be made effective against third parties only by registration in an intellectual property registry, a security right cannot be made effective against third parties by registration in the general security rights registry (see the *Guide*, recommendation 4, subpara. (b)).

129. As also already mentioned (see paras. 125 and 126), there are different approaches in law relating to intellectual property to the question of registration of a document or notice of a security right in intellectual property. In some States (often those whose secured transactions law derives from non-possessory pledge concepts), either no rights at all may be registered, at least, in some types of intellectual property or only outright transfers of intellectual property may be registered. This means that a security right in such intellectual property cannot be made effective against third parties by registration in an intellectual property registry. In other States (often those whose secured transactions law utilizes mortgage concepts), a security right in intellectual property is treated as another type of (outright or conditional) transfer and is, therefore, created and made effective against third parties to the same extent as any other transfer. Consequently, in those States, a document or notice of a title-based security right must often be registered in the relevant intellectual property registry in order for it to be created and made effective against third parties, but a non-title-based security right cannot be so registered. In some of those States, such registration has third-party effects. Finally, in a few States, there are additional requirements. These commonly include payment of a stamp duty or other transaction tax, or a requirement to give notice to an administrative body such as a national authors' association or collecting society. States enacting the law recommended in the *Guide* may wish to harmonize their secured transactions laws and their laws relating to intellectual property by: (a) replacing all existing security devices with an integrated notion of a security right or, at least, subjecting title-based security rights to the same rules that are applicable to security rights (see paras. 80 and 81 above); and (b) permitting the registration of a notice of a security right in intellectual property in the relevant intellectual property registry (at least for intellectual property rights that may already be registered therein) as a method of achieving third-party effectiveness.

IV. The registry system

A. The general security rights registry

130. As already noted (see para. 127), the *Guide* recommends that States establish a general security rights registry (see recommendations 54-75). In general, the purpose of the registry system recommended in the *Guide* is: (a) to provide an efficient method for making a security right in existing or future assets effective against third parties; (b) to establish an effective point of reference for priority rules based on the time of registration; and (c) to provide an objective source of information for third parties dealing with a grantor's assets as to whether the assets may already be encumbered by a security right (see the purpose section of the recommendations in chapter IV of the *Guide* on the registry system). Under this approach, registration is accomplished through registration of a notice of a security right, as opposed to registration of the security agreement or other document (see recommendation 54, subpara. (b)). The notice need only provide basic information concerning the security right, that is: (a) the name or other identifier of the grantor and the secured creditor or its representative, as well as their addresses; (b) a description of the encumbered asset; (c) the duration of registration; and (d) a statement of the maximum amount for which the security right may be enforced, if so provided in a State enacting the law recommended in the *Guide* (see recommendation 57).

131. The law recommended in the *Guide* provides precise rules for identifying the grantor of the security right, whether an individual or a legal person. This matter is important because notices are indexed and can be retrieved by searchers according to the name or other identifier of the grantor (see recommendations 54, subpara. (h), and 58-61). In addition, the law recommended in the *Guide* contains a number of rules to simplify the operation and use of the registry. For example, the law recommended in the *Guide* provides that, to the extent possible, the registry should be electronic and permit registration and searching by electronic means (see recommendation 54, subpara. (j)). Moreover, the law recommended in the *Guide* provides that fees for registration and searching, if any, should be set at a level no higher than necessary to permit cost recovery (see recommendation 54, subpara. (i)).

B. Asset-specific intellectual property registries

132. As already mentioned (see paras. 124-127), many States maintain national registries for registering (or recording) transactions (such as transfers) relating to intellectual property. In some of those registries, security rights in intellectual property may also be initially filed (that is, an application for registration may be submitted) and then actually registered. However, while patent and trademark registries exist in most States, not all provide for the registration of a document or notice of a security right in a patent or a trademark. In addition, in some States, the registration of a notice (whether of a security right or some other right) does not produce third-party effects. Moreover, a number of States have similar registries for copyrights, but the practice is not universal.

133. While some States have notice-based intellectual property registries, a larger number of States use recording act structures or “document registration” systems. In those systems, it is necessary to record the entire instrument of transfer or, in some cases, a memorandum describing the essential terms of the transfer. The reason for requiring registration of the transaction document or a memorandum stating the essential terms of the transaction is the need for transparency. Thus, it is essential for a transfer instrument or memorandum to identify the specific right being transferred in order to give effective notice to searchers and to allow efficient utilization of assets. In addition, intellectual property registries sometimes index registrations by the specific intellectual property and not by the grantor’s name or other identifier. This is because the central focus is on the intellectual property itself, which may have multiple co-owners or co-authors and may be subject to multiple changes in ownership as transfers are made. A more modern approach is to simplify the registration process by registering a limited amount of information (such as the names of the parties and a general description of the encumbered assets). For example, the registration requirements for trademarks are simplified by the Trademark Law Treaty (1994),¹¹ the Singapore Treaty on the Law of Trademarks (2006) and the Council Regulation (EC) No. 207/2009 of 26 February 2009 on the Community Trademark. Similarly, the Patent Law Treaty (Geneva, 2000)¹² simplifies registration requirements for patents.

134. In addition to national registries, there are a number of international intellectual property registries and registration in these registries is subject to relatively modern treaties or other international legislative texts that simplify the registration process, for example, the Madrid Agreement Concerning the International Registration of Marks (1891),¹³ the Protocol to

¹¹ Available from www.wipo.int/treaties/en/ip/tlt/.

¹² Available from www.wipo.int/treaties/en/ip/plt/.

¹³ Available from www.wipo.int/treaties/en/registration/madrid/.

which (1989) provides for the possibility to record a restriction of the holder's right of disposition in an international application or registration form.¹⁴ In addition, under the Community trademark regulation (see para. 133 above), a statement may be registered referring not only to ownership but also to a security right with third-party effects. Another example is the treaty on the International Registration of Audiovisual Works (the Film Register Treaty, (1989)), under the auspices of WIPO. The Film Register Treaty created an international registry that permits the registration of statements concerning audiovisual works and rights in such works, including, in particular, rights relating to their exploitation (the records of the diplomatic conference indicate that statements concerning security rights were also contemplated). Registration in this international registry creates an evidentiary presumption of validity for registered statements. This international registry allows two types of application: (a) a work-related application which identifies an existing or future work at least by title or titles; and (b) a person-related application which identifies one or more existing or future works by the natural person or legal entity that makes or owns, or is expected to make or own, each work. The international registry maintains an electronic database that allows cross-indexing between the different types of registration.

C. Coordination of registries

135. As already mentioned (see paras. 124 and 125), the *Guide* neither recommends the creation of a specialized registration system (for intellectual property or for any other type of asset), if one does not exist, nor interferes with existing specialized registration systems. However, where, under law relating to intellectual property, a document or notice of a security right in intellectual property may be registered in an intellectual property registry and, at the same time, under the law recommended in the *Guide*, that security right may also be registered in the general security rights registry, there is a need to address the issue of coordination between these two registries. In order to avoid interfering with law relating to intellectual property, the law recommended in the *Guide* addresses it through the general deference to law relating to intellectual property (see recommendation 4, subpara. (b)) and appropriate priority rules (see recommendations 77 and 78).

136. Thus, the law recommended in the *Guide* does not address or purport to address the question whether a security right in intellectual property may be registered in an intellectual property registry, the requirements for such

¹⁴See Form MM19 at www.wipo.int/madrid/en/forms.

registration (for example, document or notice registration) or its legal consequences (for example, effectiveness or presumption of effectiveness against all parties or only against third parties). Even if an intellectual property registry does not provide for the registration of security rights, provides for the registration of a document rather than a notice thereof or, having provided for such registration, does not give registration third-party effects, the *Guide* provides no recommendation to the contrary and takes the specialized registration system, if any, as is.

137. However, the *Guide* does make recommendations concerning the registration of a notice of a security right in intellectual property in the general security rights registry. For this reason, to the extent that the law recommended in the *Guide* addresses the effects of registration of security rights in an intellectual property registry in a way that would be inconsistent with the effects given to such registration by the law relating to intellectual property, the law recommended in the *Guide* defers to that law (see recommendation 4, subpara. (b)). By contrast, if the law recommended in the *Guide* does not address these issues at all or addresses them in a manner that is consistent with the law relating to intellectual property, then the issue of deference to law relating to intellectual property will not arise and thus the law recommended in the *Guide* will apply, giving such specialized registration third-party effects.

138. In addition, the *Guide* addresses the issue of coordination between a specialized registry (including an intellectual property registry) and the general security rights registry recommended in the *Guide* through appropriate priority rules. In order to preserve the reliability of intellectual property (and other specialized) registries (in particular, in cases where law relating to intellectual property provides no rule for determining priority), the law recommended in the *Guide* provides that a security right in intellectual property, a document or notice of which is registered in the relevant intellectual property registry (see para. 124 above), has priority over a security right in the same intellectual property, a notice of which is registered in the general security rights registry (see the *Guide*, recommendation 77, subpara. (a)). For the same reason, the law recommended in the *Guide* provides that a transferee of intellectual property acquires it, in principle, free of a previously created security right in that property, unless a document or notice of the security right is registered in the intellectual property registry (see recommendations 78 and 79). Under recommendation 4, subparagraph (b), this rule would apply only if it was not inconsistent with a rule of law relating to intellectual property (see paras. 184-187 below).

139. If States enacting the recommendations of the *Guide* have specialized intellectual property registries and wish to use them for registration of a

security right in intellectual property, making use of the possibilities offered in recommendation 38 of the *Guide*, they may wish to consider ways aimed at coordinating their existing intellectual property registries with the general security rights registry recommended in the *Guide*. For example, States may wish to consider permitting the registration of a notice of a security right in intellectual property in an intellectual property registry. In addition, States may wish to consider whether asset-based intellectual property registries should also have a debtor-based index (and general security rights registries should have an asset-based index). Moreover, States may wish to consider requiring the intellectual property registry to transmit a copy of each notice (or summary of a document) registered in that registry to the general security rights registry (and vice versa). Coordination of registries in this way would be easier, simpler, quicker and less expensive in an electronic registration system rather than in a paper-based registration system. Finally, it should be noted that the issue of coordination between a specialized registry and a general security rights registry would arise even if the specialized registry were an international or regional registry.

140. An alternative to a system permitting the forwarding of copies of notices from one registry to the other might be a system implementing a common gateway to both the general security rights registry and to various specialized registries. Such a common gateway would enable registrants to enter the notice simultaneously in both registries. Several steps would have to be taken in order to ensure the efficiency and effectiveness of a common gateway, including that: (a) a simple notice should be enough; (b) the notice should include the identifiers of both the grantor and the secured creditor (or its representative) and an asset-specific description of the encumbered assets; (c) searches in both registries should be possible with a single request; and (d) both grantor-based and asset-based indexes should be maintained with cross references in each registry to the other registry (see the *Guide*, chap III, paras. 80-82).

D. Registration of notices of security rights in future intellectual property

141. An essential feature of the general security rights registry recommended in the *Guide* is that a notice of a security right can refer to future assets of the grantor. This means that the security right can cover assets to be later produced or acquired by the grantor (see the *Guide*, recommendation 17) and the notice may cover assets described in a manner that reasonably allows their identification (see the *Guide*, recommendation 63, and paras. 82-85 and 113-118 above).

Thus, if the encumbered assets are described in the security agreement as all existing and future inventory, the notice may also describe the inventory in the same manner. Since priority is determined by date of registration, the priority of a security right extends to future inventory (see the *Guide*, recommendation 99). This approach greatly facilitates revolving credit arrangements, since a lender extending new credit under such a facility knows that it can maintain its priority position in new assets that are included in the borrowing base.

142. Existing intellectual property registries in many States, however, do not readily accommodate registration of rights in future intellectual property. As transfers of or security rights in intellectual property are indexed against each specific intellectual property right, they can only be effectively registered after the intellectual property is first registered in the intellectual property registry. This means that a blanket registration of a security right in future intellectual property in an intellectual property registry would not be feasible and a new registration of a security right would be required each time new intellectual property is created or acquired.

143. If, under law relating to intellectual property, an intellectual property right may not be created, acquired, transferred or encumbered before the intellectual property right is actually registered in an intellectual property registry, the law recommended in the *Guide* does not interfere with that prohibition and does not make the creation of a security right in such future intellectual property possible. However, if the creation of a security right in future intellectual property is not prohibited under law relating to intellectual property (as is the case, for example, with a patent or trademark while the application for its registration in the patent or trademark registry is pending), a security right in future intellectual property could be created and made effective against third parties under the law recommended in the *Guide* (see recommendations 17 and 68). States enacting the recommendations of the *Guide* may wish to consider reviewing their law relating to intellectual property to determine whether a notice of a security right may refer to future intellectual property and, if it does not, to consider permitting the registration of a security right in future intellectual property.

E. Dual registration or search

144. As already mentioned (see para. 138), the law recommended in the *Guide* gives priority, as a matter of secured transactions law, to rights with respect to which a registration is made in an intellectual property registry

and defers to any rules of law relating to intellectual property governing the registry with respect to the details of registration of a document or notice of a security right. As also noted above, this means that the law recommended in the *Guide* often obviates the need for dual registration or search. In particular, registration only in the general security rights registry would seem to be necessary and useful for secured transactions purposes: (a) where the encumbered asset is a type of intellectual property with respect to which no registration system exists under law relating to intellectual property (for example, copyrights or trade secrets in many States); (b) where the encumbered asset is a type of intellectual property with respect to which ownership rights may be registered in an intellectual property registry, but not a document or notice of a security right; and (c) where a document or notice of security right in intellectual property may be registered in an intellectual property registry, but such registration has effects that are inconsistent with third-party effects. On the other hand, registration in the relevant intellectual property registry may be preferable, for example: (a) where the encumbered asset is a type of intellectual property for which a registration system exists and allows registration of a document or notice of a security right (for example, patents or trademarks in many States); and (b) where the secured creditor needs to ensure priority over other secured creditors or transferees under the relevant law relating to intellectual property.

145. Before credit is extended or committed pursuant to a security agreement, a secured creditor exercising normal due diligence will typically conduct a search to determine whether there are prior competing claimants whose rights have priority over the proposed security right. As a first step, the secured creditor will search the chain of title to identify prior transfers and to determine whether the grantor actually has rights in the intellectual property or other movable assets to be encumbered so that the security right can become effective in the first instance. For types of intellectual property as to which ownership transfers must be recorded in a specialized registry in order to be effective against third parties, this chain of title search will be easier than for types of encumbered asset for which no such registry exists (the general security rights registry does not record title). As a next step, the secured creditor will search to determine whether any prior party in the chain of title has granted a security right that might have priority over the proposed security right. If there are no such security rights, the secured creditor will be able to reliably extend or commit credit on the basis of that intellectual property as long as it takes the steps necessary under the law recommended in the *Guide* to achieve third-party effectiveness. Finally, in cases where a secured creditor has registered a document or notice of its security right in the relevant intellectual property registry, the secured creditor has a right to rely on that registration and on the priority attributed to that

registration under the law recommended in the *Guide* (see recommendations 78 and 79). In such cases, a potential third-party creditor may need to search only in the relevant intellectual property registry. In other cases, a potential third-party creditor may need to search in both the relevant intellectual property registry (for ownership transfers) and in the general security rights registry (for security rights that may not be registered in the relevant intellectual property registry).

146. Under the law recommended in the *Guide*, it is envisaged that the general security rights registry will be electronic and will accept registration of notices of possible security rights with third-party effects at a nominal cost (based on cost recovery), if any, for registration and searching (see recommendation 54, subpara. (i)). This means that, in States that enact the recommendations of the *Guide*, registration and searching in the general security rights registry is likely to be simple, quick and inexpensive. However, under law relating to intellectual property, registries may not necessarily be fully electronic (although an increasing number of intellectual property registries allow online searching for a small or no fee). In addition, the document evidencing a transaction or a summary thereof may need to be registered (instead of a notice). Moreover, the document registered may have to be checked by the registry staff at least to the extent that the legal consequence of registration may be conclusive or presumptive evidence of the existence of a right in intellectual property.

147. Thus, to the extent that a document evidencing a transaction has to be registered in order to create a security right in intellectual property, the cost of registration in an intellectual property registry may reasonably be assumed to be higher than the cost of registration of a simple notice of a security right in the general security rights registry for the purpose of achieving third-party effectiveness. Similarly, unless the document registry is fully electronic and has also a grantor-based index, the cost and time of searching in such a document registry for intellectual property rights of a certain grantor may be reasonably assumed to be more time-consuming and costly than searching in an electronic notice-based general security rights registry. However, the types of intellectual property registry vary widely from State to State. Modern intellectual property registries (national, regional or international) tend to permit the online registration of a notice of a security right, for a nominal fee, with third-party effects and are organized in a way that also permits searching in a time- and cost-efficient way. Thus, registration and searching in such registries is also likely to be simple, quick and inexpensive. In addition, the time and cost required for registration and searching in the relevant intellectual property registry may be justified since such registration would provide more information (for example, because of the specific description of the encumbered assets and the information about transfers)

and probably more certain information (for example, because registration may constitute or be deemed to provide firm evidence as to the existence of a right).

148. The differences in cost of registration and searching may be illustrated by the following examples. For convenience, the examples assume that only the law of a single State applies, that the State has enacted the law recommended in the *Guide* and that (where applicable) the State also has an intellectual property registry that accepts registration of security rights in intellectual property with results that are consistent with those envisaged in the *Guide*.

149. A grantor that is the initial owner of a single intellectual property right creates a security right in that intellectual property right. Whether registration is made in the general security rights registry or in the relevant intellectual property registry, the secured creditor needs to register only one notice in order for the security right to be effective against third parties (unless the secured creditor prefers to register also in the relevant intellectual property registry, if any, because of the priority rules recommended in the *Guide*). A searcher that wants to extend credit on the basis of the encumbered intellectual property right will mainly need to search in the relevant intellectual property registry. The reason for this result is that by registering in that registry the searcher's security right would gain priority even over a security right, a notice of which was registered earlier in the general security rights registry. It should be noted, however, that, if the intellectual property registration system requires registration of a document, the registrar may have to check the document to ensure that it can be registered. These requirements may affect the time- and cost-efficiency of the registration process. While the notice-based registration system of the general security rights registry has the advantage of providing greater confidentiality and simplicity than a document-based registration system of the intellectual property registry, it has the disadvantage that it may not provide a searcher as much information as a document-based registration system.

150. A grantor that is the initial owner of 10 intellectual property rights creates a security right in all 10 rights. If registration is made in the general security rights registry, the secured creditor needs to register only one notice, listing the grantor's name and indicating the intellectual property rights as encumbered assets. As in this example the grantor is assumed to be the initial owner, a secured creditor need only be concerned about competing transfers made only by the grantor and not by any prior party in the chain of title. Thus, a searcher needs to conduct only one search in the general security rights registry against the name or other identifier of the grantor to find competing security rights.

151. However, a searcher will also need to conduct a separate search against each of the 10 intellectual property rights in the intellectual property registry to determine if there are other competing claimants such as outright transferees. If there is a specialized registry in which security rights in the intellectual property may be registered and the secured creditor, cognizant of the priority advantages of registration in such a registry, decides to search that registry and register its security right there, the secured creditor may need to register a document or notice for each intellectual property right separately, although in some cases it may be possible to register a single document or notice that identifies some or all of the encumbered intellectual property (for example, if all the intellectual property rights are patents). In such cases, a searcher needs to conduct a search in the intellectual property registry against each of the 10 intellectual property rights to find both prior security rights and other competing claimants.

152. In the example just mentioned (see paras. 150 and 151), if the grantor is not the initial owner but a transferee in a chain of transferees and each of the 10 intellectual property rights has 10 prior owners, registration in the general security rights registry may still be more efficient than registration in an intellectual property registry. A secured creditor would only need to register one notice in the general security rights registry against the grantor, but, in any relevant intellectual property registry, the secured creditor would need to register a document or notice against each of the 10 intellectual property rights. However, with respect to searching, if a security right remains effective against transferees without the need for an amendment notice to be registered in the general security rights registry (see paras. 158-166 and recommendation 244 below), then a searcher would have to conduct 10 searches outside the security rights registry to identify the prior owners of each intellectual property right and then conduct a search of each prior owner in the general security rights registry to discover whether there are prior competing security rights, that is 100 searches (10 prior owners multiplied by 10 intellectual property rights) in the general security rights registry to identify all prior security rights. However, if a security right is registered in an intellectual property registry, if any, the secured creditor need only conduct 10 searches, that is, one for each intellectual property right, since the search in the intellectual property registry will disclose both prior competing security rights and other competing claimants. Thus, as to searching with respect to multiple intellectual property rights that have had many previous owners, it would seem that searching in the intellectual property registry, if any, would be more time- and cost-efficient.

153. The examples mentioned above indicate that, while the general security rights registry in the *Guide* may better accommodate intellectual property financing in some contexts, this may not always be the case and would depend

on the circumstances of each case (see also paras. 158-166 below). They also indicate that, in view of the priority of a security right registered in an intellectual property registry and the need for the secured creditor to establish that the grantor has rights in the intellectual property to be encumbered, a registration or search may need to take place in the intellectual property registry in most cases (where registration of a security right in an intellectual property registry is possible).

154. The law applicable to third-party effectiveness and priority will also have an impact on the time- and cost-efficiency of registration. If the law applicable to these matters is the law of the State in which the encumbered intellectual property is protected, in the case of a portfolio of intellectual property rights, registration and searching will involve the registries of several States. The result would be different if third-party effectiveness and priority were to be governed by the law of the State in which the grantor is located (unless the grantor moves to another State or the encumbered intellectual property right is transferred from a person in one State to a person in another State, in which the law of more than one State will be involved; see the *Guide*, recommendations 45, 219 and 220). However, in any case, the main cause of the difference would be the applicable law and not the type of registration. Therefore, this matter is discussed in chapter X, on the law applicable to a security right in intellectual property.

F. Time of effectiveness of registration

155. Under the law recommended in the *Guide*, registration of a notice of a security right becomes effective against third parties when the information in the notice is entered into the registry records and becomes available to searchers (see recommendation 70). Where the registry is electronic, registration of a notice will become effective immediately upon registration. However, where the registry is paper-based, registration of a notice will become effective some time after registration.

156. Under law relating to intellectual property, specialized registration systems may have different rules with respect to the time of effectiveness of registration of a security right. For example, under law relating to patents and trademarks in many States, third-party effectiveness of a registered security or other right in a patent or a trademark dates back to the date of filing (that is, submission to the registry of an application for registration). Such an approach is useful where the registry takes time to actually register the security right in the patent or trademark, but may mislead a searcher as to whether specific intellectual property is encumbered.

157. As already mentioned (see paras. 135-140), the law recommended in the *Guide* deals with coordination issues by giving priority to a security right evidenced by a document or notice registered in a specialized registry (or a notation made on a title certificate) irrespective of the time of registration (see recommendations 77 and 78). Thus, the difference in the approach as to the time of effectiveness of registration may not cause any problems in determining the priority of a security right in intellectual property registered in the relevant intellectual property registry.

G. Impact of a transfer of encumbered intellectual property on the effectiveness of registration

158. The *Guide* recommends that the secured transactions law address the impact of a transfer of an encumbered asset on the effectiveness of registration of a notice in the general security rights registry (see recommendation 62). This recommendation is equally applicable to security rights in intellectual property made effective against third parties by registration of a notice in the general security rights registry. However, this recommendation is not relevant if:

(a) The transferee of an encumbered asset acquires it free of the security right, as is the case, for example, where the transfer is authorized by the secured creditor free of the security right (see recommendation 80);

(b) A document or notice of the security right has been registered in an intellectual property (or other specialized) registry;

(c) The grantor has transferred all its rights in an asset before granting a security right in that asset (in such situations, under the *Guide*, no security right is created; see recommendation 13); or

(d) There is no transfer of ownership, but only a licence in intellectual property.

159. With respect to subparagraph (a) in the preceding paragraph, it should be noted that, if the secured creditor did not authorize a licence (that is, if the licensee did not acquire the asset free of the security right) and enforced its security right, enforcement would amount to termination of the licence and any sub-licence, which would make all the “licensees” infringers upon completion of enforcement of the security right. With respect to subparagraph (d), it should be noted that recommendation 62 might apply to a licence, if, under law relating to intellectual property, it is treated as a transfer of ownership (while, under the *Guide*, a licence is not a transfer, the exact

meaning of the term “licence”, including the question whether an exclusive licence is to be treated as a transfer, is a matter of law relating to intellectual property; see paras. 23-25 above and para. 187 below).

160. The commentary of the *Guide* discusses three ways in which an enacting State may wish to address the matter (see the *Guide*, chap. IV, paras. 78-80). One way is to provide that, where the encumbered asset is transferred and the transferee does not acquire it free of the security right, the secured creditor must register an amendment notice identifying the transferee within a certain specified period after the transfer. If the secured creditor fails to do so, the original registration continues to be effective in principle. However, the security right is subordinated to intervening secured creditors and transferees whose rights arise after the transfer of the encumbered asset and before the amendment notice is registered. A second way in which enacting States may wish to address this issue is to provide that the grace period for the registration of an amendment notice is triggered only once the secured creditor acquires actual knowledge of the transfer of the encumbered asset by the grantor. A third way is to provide that a transfer of an encumbered asset has no impact on the effectiveness of registration of a security right.

161. If an enacting State adopts the third approach, a secured creditor of the transferor need not register a new notice of its security right identifying the transferee. In such a case, the original registration of a notice of security right in the asset now owned by the transferee would remain effective. However, transferees down in the chain of transferees might not readily be able to discover, through a search in the general security rights registry, a security right granted by any person other than their immediate transferor. In such cases, they would still have to search the chain of title and status of an encumbered asset outside the general security rights registry. On the other hand, if an enacting State adopts the first or the second approach discussed above, a secured creditor will have to register an amendment notice identifying the transferee. In such a case, the secured creditor will have the burden of monitoring the status of the encumbered asset (to a different degree, depending on whether the first or the second approach is followed). At the same time, however, transferees down the chain of title will readily be able to identify a security right granted by a person other than their immediate transferor.

162. States enacting the law recommended in the *Guide* will have to consider the relative advantages and disadvantages of the different approaches mentioned above and, in particular, their impact on rights in intellectual property. For example, under the first approach, a secured creditor extending credit against the entire copyright in a film would need to make continuous registrations against tiers of licensees and sub-licensees (if the relevant law relating to copyrights treated such an exclusive licence as a transfer that

may be registered) to maintain its priority against them or their own secured creditors. This would be a significant burden on such lenders and might discourage the extension of credit based upon such assets. On the other hand, such an approach would make it easier for a lender to a sub-licensee to find a security right created by its sub-licensor by a simple search only against the identifier of the sub-licensor. Here, the trade-off is between the relative costs of monitoring and multiple registrations by the lender to the “upstream” party as against the costs of conducting a search of the entire chain of title for security rights created by the “downstream” party. In this regard, it should be noted that typically under law relating to intellectual property a prior transfer retains its priority over later transfers without the need for an additional registration in the name of a transferee of an encumbered asset.

163. As already mentioned (see para. 161), if a State does not follow the third option, a secured creditor would have to register an amendment notice in the general security rights registry each time the encumbered intellectual property became the subject of an unauthorized transfer, licence or sub-licence (if licences are treated as transfers under the relevant law relating to intellectual property), at the risk of losing its priority if it was not informed about the transfer or was informed but had not acted promptly. The following examples may highlight the need for such an approach (see recommendation 244 below).

164. If a grantor of a security right in an intellectual property right is not the initial owner but the tenth in a series of 10 successive transferees and if a secured creditor need not register an amendment notice in the name of each transferee of the encumbered intellectual property right, the secured creditor need only register one notice in a general security rights registry. However, a searcher would have to conduct 10 searches outside the general security rights registry to identify each owner and then search the general security rights registry for each of the 10 prior owners to determine if there are any prior security rights granted by any of the owners.

165. If, however, the law requires the registration of a new notice each time the encumbered intellectual property is transferred, the secured creditor must register one notice against its grantor and one for each of the 10 prior owners. This may require that the secured creditor make a substantial effort to monitor not only the actions of its grantor, but also transferees (and licensees, if a licence is treated as a transfer).

166. These examples indicate that, if the law requires the secured creditor to register an amendment notice each time the encumbered intellectual property is transferred or licensed (to the extent an exclusive licence is

treated as a transfer under law relating to intellectual property), intellectual property financing would be discouraged or become more expensive. This is the reason why the *Supplement* recommends a different approach from that recommended in the *Guide* (see the *Guide*, recommendation 62). According to this approach, the registration of a notice of a security right in intellectual property in the general security rights registry would remain effective notwithstanding a transfer of the encumbered intellectual property. As a result, the secured creditor would not have to register an amendment notice indicating the name of the transferee of the encumbered intellectual property (see recommendation 244 below).

H. Registration of security rights in trademarks

167. The International Trademark Association (INTA) issued a series of principles with respect to the registration of security rights in trademarks and service marks (collectively referred to as “marks”) as “best practice” to be followed whenever and wherever possible.¹⁵ More specifically, INTA endorsed harmonization recommendations regarding the registration of security rights in trademarks, recognizing that intellectual property rights, including marks, are a major and growing factor in commercial lending transactions; lack of consistency in the registration of security rights in marks fosters commercial uncertainty and also poses a risk that a mark owner may forfeit or otherwise endanger its mark-related rights; many States have no recording mechanisms (or have insufficient mechanisms) for the registration of security rights in marks; many States apply different and conflicting criteria for determining what can and will be recorded; and international initiatives on security rights in intellectual property rights by organizations such as UNCITRAL will have broad implications for the way secured financing laws are implemented to deal with registration and other aspects of trademark security rights, especially in developing countries. It should be noted that the principles do not address issues relating to the registration of security rights in marks that may not be registered in a trademark office, leaving those issues to domestic secured transactions law (including the law recommended in the *Guide*). In addition, the principles address third-party effectiveness issues but do not set out priority rules, leaving them to domestic secured transactions law (including the law recommended in the *Guide*).

¹⁵See www.inta.org/index.php?option=com_content&task=view&id=1517&Itemid.

168. The main principles of such best practice are the following:

(a) A security right in a mark covered by a pending application or registration should be registrable in the national trademark office;

(b) For purposes of giving notice of a security right, registration in the applicable national trademark office or in any applicable commercial registry is recommended, with free public accessibility, preferably through electronic means;

(c) The grant of a security right in a mark should not have the effect of a transfer of legal or equitable title to the mark that is subject to the security right and should not confer upon the secured creditor a right to use the mark;

(d) The security agreement creating the security right should clearly set forth provisions acceptable under local law enabling the renewal of the marks by the secured creditor, if necessary to preserve the mark registration;

(e) Valuation of marks for purposes of security rights should be made in any manner that is appropriate and permitted under local law and no particular system or method of valuation is preferred or recommended;

(f) Registration of security rights in the local trademark office should suffice for purposes of perfecting a security right in a mark; at the same time, registration of a security right in any other place allowed under local law, such as a commercial registry, should also suffice;

(g) If local law requires that a security right be registered in a place other than the local trademark office in order to be perfected, such as in a commercial registry, dual registration of the security right should not be prohibited;

(h) Formalities in connection with registration of a security right and the amount of any government fees should be kept to a minimum; a document evidencing: (i) existence of a security right; (ii) the parties involved; (iii) the mark(s) involved by application and/or registration number; (iv) a brief description of the nature of the security right; and (v) the effective date of the security right, should suffice for purposes of making a security right effective against third parties;

(i) Regardless of the procedure, enforcement of a security right through foreclosure, after a judgement, administrative decision or other triggering event, should not be an unduly burdensome process;

(j) The applicable trademark office should promptly record the entry of any judgement or adverse administrative or other decision against its records and take whatever administrative action is necessary; the filing of a certified copy of the judgement or decision should be sufficient;

(k) In the event that enforcement is triggered by means other than a judgement or administrative decision, local law should provide for a simple mechanism enabling the holder of the security right to achieve registration, with free public accessibility, preferably through electronic means;

(l) In cases where the mark owner is bankrupt or otherwise unable to maintain the marks that are subject to a security right, absent specific contract provisions, the holder of the security right (or the administrator or executor, as the case may be) should be permitted to maintain the marks, provided that nothing shall confer upon the secured creditor the right to use the marks; and

(m) The relevant government agency or office should promptly record the filing of documentation reflecting release of the security right in its records, with free public accessibility, preferably through electronic means.

169. Principles (a), (b), (f) and (g) set forth in paragraph 168 above, dealing with third-party effectiveness of a security right in a mark, are compatible with the law recommended in the *Guide* in that they promote the objectives of certainty and transparency (see recommendation 1, subpara. (f)).

170. Principle (c) set forth in paragraph 168 above, providing that the creation of a security right in a mark does not result in a transfer of the mark or confer upon the secured creditor the right to use the mark, is also compatible with the law recommended in the *Guide*. It should be noted that, under the law recommended in the *Guide*, the secured creditor has a right, but no obligation, to preserve an encumbered intangible asset (such an obligation is foreseen only for tangible assets; see recommendation 111). If, in the case of the owner's insolvency, neither the owner nor the insolvency representative nor the secured creditor takes the necessary steps to preserve the encumbered mark, the mark may still be preserved under law relating to intellectual property (for example, under the doctrine of the "excusable non-use" of a mark).

171. In addition, principle (d) set forth in paragraph 168 above is compatible with the law recommended in the *Guide* in that it sets forth a default rule for the rights of the parties within the limits of the applicable law. Principle (e) is also compatible with the law recommended in the *Guide* to the extent it emphasizes the importance of valuation of marks without suggesting any particular system of valuation. Principle (h) is also compatible with the law recommended in the *Guide* in that it recommends notice filing even in relation to mark registries. It should be noted that the reference to "the effective date of the security right" is a reference to the time of effectiveness of the security right between the parties and not against third parties.

172. Moreover, principles (i), (j) and (k) set forth in paragraph 168 above are compatible with the law recommended in the *Guide* in the sense that they provide for efficient enforcement mechanisms and registration of court judgements or administrative enforcement decisions. Finally, principle (m), which is subject to approval by the appropriate government authorities, is compatible with the law recommended in the *Guide* with respect to efficient registration procedures.

Recommendation 244¹⁶

Impact of a transfer of encumbered intellectual property on the effectiveness of the registration

The law should provide that the registration of a notice of a security right in intellectual property in the general security rights registry remains effective notwithstanding a transfer of the encumbered intellectual property.

¹⁶If it could be included in the *Guide*, this recommendation would be placed in chapter IV, The registry system, as recommendation 62 bis.

V. Priority of a security right in intellectual property

A. The concept of priority

173. As used in the *Guide*, the concept of priority of a security right as against competing claimants refers to the question of whether the secured creditor may derive the economic benefit of its security right in an encumbered asset in preference to a competing claimant (see the term “priority” in the introduction to the *Guide*, sect. B, para. 20; see also the term “competing claimant”, paras. 10 and 11 above, as well as paras. 175 and 176 below). It should also be noted that a conflict between two persons, neither of whom is a secured creditor, is not a priority conflict under the law recommended in the *Guide*.

174. By contrast, in law relating to intellectual property, the concept of priority of an intellectual property right may relate to notions of exclusive rights. In most States, once intellectual property is transferred by the owner, a second transfer by the same person will normally transfer no rights to the second transferee (except if the first transferee does not comply with statutory registration requirements or the second transferee is a good faith purchaser; for the relevance of knowledge of prior transfers, see paras. 177 and 178 below). Similarly, if both the first and the second transferee create a security right in their intellectual property rights, there may be no priority conflict under the law recommended in the *Guide* to the extent the second transferee does not have any intellectual property right in which to create a security right. In such a case, the issue of priority in the sense that this term is used in the *Guide* does not arise. Accordingly, the law recommended in the *Guide* would not apply and this matter would be left to law relating to intellectual property, which would typically resolve it by reference to the *nemo dat* principle and principles about good faith acquisition of assets. It should be noted that, under the law recommended in the *Guide*, a party that does not have rights in or the power to encumber an asset at the time of the conclusion of the security agreement, or does not acquire such rights or power later, may not create a security right in the asset (see recommendation 13).

B. Identification of competing claimants

175. The *Guide* uses the term “competing claimant” to refer to another secured creditor with a security right in the same asset (which includes a transferee in a transfer by way of security), an outright transferee, lessee or licensee of the encumbered asset, a judgement creditor with a right in the encumbered asset and an insolvency representative in the insolvency of the grantor (see the term “competing claimant”, paras. 10 and 11 above). In particular, the law recommended in the *Guide* applies to priority conflicts: (a) between security rights, notices of which are registered in the general security rights registry (see the *Guide*, recommendation 76, subpara. (a)); (b) between a security right, a notice of which is registered in the general security rights registry, and a security right, a document or notice of which is registered in the relevant intellectual property registry (see recommendation 77, subpara. (a)); (c) between security rights, documents or notices of which are registered in the relevant intellectual property registry (see recommendation 77, subpara. (b)); (d) between the rights of a transferee or licensee of intellectual property and a security right in that intellectual property, a document or notice of which may be registered in an intellectual property registry (see recommendation 78); (e) between the rights of a transferee or licensee of intellectual property and a security right in that intellectual property, a document or notice of which may not be registered in an intellectual property registry (see recommendations 79-81); and (f) between two security rights that are both effective against third parties, one of which is created by the grantor and the other is created by the transferee, lessee or licensee of the encumbered asset. The last conflict is addressed in the sense that the transferee, lessee or licensee takes the asset subject to the security right created by the grantor (see recommendations 79 and 82) and the secured creditor of the transferee, lessee or licensee takes no more rights than the transferee, lessee or licensee had (see recommendation 31).

176. In an intellectual property context, the notion of “conflicting transferees” is used instead and it includes transferees and licensees competing with each other. If no conflict with a security right in intellectual property (which includes the right of a transferee by way of security) is involved, the law recommended in the *Guide* does not apply and the matter is left to law relating to intellectual property. If a conflict with such a security right is involved, the law recommended in the *Guide* does not apply in so far as its provisions are inconsistent with the enacting State’s law relating to intellectual property (see recommendation 4, subpara. (b)). Furthermore, the law recommended in the *Guide* does not apply to a conflict between a transferee of an encumbered asset that acquired the asset from a secured creditor enforcing its security right and another secured creditor that later

received a right in the same asset from the same grantor (that no longer had any rights in the encumbered asset). This is not a priority conflict under the law recommended in the *Guide*, but it may well be a conflict addressed by law relating to intellectual property.

C. Relevance of knowledge of prior transfers or security rights

177. Under the law recommended in the *Guide*, knowledge of the existence of a prior security right on the part of a competing claimant is generally irrelevant for determining priority (see recommendation 93; however, knowledge that a transfer violates the rights of a secured creditor may be relevant; see recommendation 81, subpara. (a)). Thus, a later created but earlier registered security right has priority over an earlier created but later registered security right, even if the holder of the later created security right had knowledge of the existence of the earlier created security right (see recommendation 76, subpara. (a)).

178. By contrast, in many States, law relating to intellectual property provides that a later conflicting transfer or security right may only gain priority if it is registered first and taken without knowledge of a prior conflicting transfer. The deference to law relating to intellectual property under recommendation 4, subparagraph (b), should preserve these knowledge-based priority rules to the extent they apply specifically to security rights in intellectual property.

D. Priority of security rights in intellectual property that are not registered in an intellectual property registry

179. As already mentioned, if law relating to intellectual property has priority rules dealing with the priority of security rights in intellectual property that apply specifically to intellectual property and the priority rules of the law recommended in the *Guide* are inconsistent with those rules, the law recommended in the *Guide* does not apply (see recommendation 4, subpara. (b)). However, if law relating to intellectual property does not have such rules or the priority rules of the law recommended in the *Guide* are consistent with such rules, the priority rules of the law recommended in the *Guide* apply.

180. Under the law recommended in the *Guide*, priority between security rights granted by the same grantor in the same encumbered asset that were made effective against third parties by registration in the general security rights registry is determined by the order of registration of a notice in that registry (see recommendation 76, subpara. (a)). This rule applies if a document or notice of a security right may not be registered or is not registered in a specialized registry. If such a document or notice may be registered and is registered in a specialized registry, different rules apply (see the *Guide*, recommendation 77, and paras. 181-183 below). In addition, if a security right is granted by a different grantor (for example, a transferee of the initial grantor), different rules apply (see the *Guide*, recommendations 79-83, and paras. 184-201 below). All these rules apply equally to security rights in intellectual property.

E. Priority of security rights in intellectual property that are registered in an intellectual property registry

181. The *Guide* recommends that a security right in an asset that is made effective against third parties by registration in a specialized registry (see recommendation 38) has priority over a security right in the same asset that is made effective against third parties by another method (see recommendation 77, subpara. (a)). It also recommends that a security right in an asset that is made effective against third parties by registration in a specialized registry has priority over a security right in the same asset that was subsequently registered in the specialized registry (see recommendation 77, subpara. (b)). In addition, the *Guide* recommends that, if an encumbered asset is transferred, leased or licensed and, at the time of the transfer, lease or licence, the security right has been made effective against third parties by registration in a specialized registry, the transferee, lessee or licensee takes its rights subject to the security right. If such a security right has not been registered in a specialized registry, a transferee, lessee or licensee of an encumbered asset takes the asset free of the security right, even if a notice of the security right was registered in the general security rights registry (see recommendation 78). These rules are subject to certain exceptions (see paras. 184-212 below, as well as the *Guide*, recommendations 79-81). In addition, if a transferee, lessee or licensee of an encumbered asset acquires its rights in the asset free of a security right, any person that subsequently acquires rights in the asset acquires its rights free of the security right (see the *Guide*, recommendations 31 and 82).

182. These recommendations are equally applicable to security rights in intellectual property. Thus, if there is a conflict between two security rights

in intellectual property, one of which is the subject of a notice registered in the general security rights registry and the other is the subject of a document or notice registered in the relevant intellectual property registry, the law recommended in the *Guide* applies and gives priority to the latter security right (see recommendation 77, subpara. (a)). If there is a conflict between security rights registered in the relevant intellectual property registry, the right registered first has priority (see recommendation 77, subpara. (b)). If there is a conflict between the rights of a transferee of intellectual property and a security right which, at the time of the transfer, may be and is registered in the relevant intellectual property registry, the transferee takes the encumbered intellectual property subject to the security right. However, if a security right in intellectual property may be registered but is not registered in the relevant intellectual property registry, the transferee or licensee of the encumbered intellectual property takes the encumbered intellectual property free of the security right, even if the security right was registered in the general security rights registry (see recommendation 78). In some States, under law relating to intellectual property, a secured creditor may have priority in this case, if the transferee is not a good-faith purchaser. Following recommendation 4, subparagraph (b), the law recommended in the *Guide* would defer to that rule if it applied specifically to intellectual property. Finally, if a transferee acquires a right in encumbered intellectual property subject to a security right, any person (for example, a secured creditor of the transferee) that subsequently acquires a right in the intellectual property from the transferee also takes its right subject to the security right (see recommendations 31 and 82).

183. For example, if A creates a security right in a patent in favour of B, which registers a notice of its security right in the general security rights registry, and then A transfers title to the patent to C, which registers a document or notice of its transfer in the patent registry, under recommendation 78 of the *Guide*, C would take the patent free of the security right of B. If A, instead of making a transfer, creates a second security right in favour of C and C registers a document or notice of the security right in the patent registry, under recommendation 77, subparagraph (a), of the *Guide*, C would prevail. In either case, as registration of a document or notice in the patent registry gives superior rights, under the law recommended in the *Guide*, third-party searchers could rely on a search in that registry and would not need to search in the general security rights registry. In all these examples, the questions of who is a transferee and what are the requirements for a transfer are matters of law relating to intellectual property. It should also be noted that registration in the intellectual property registry would normally refer only to a security right in intellectual property and not to a security right in tangible assets with respect to which intellectual property is used.

F. Rights of transferees of encumbered intellectual property

184. Under the law recommended in the *Guide*, a transferee of an encumbered asset (including intellectual property) normally takes the asset subject to a security right that was effective against third parties at the time of the transfer. There are two exceptions to this rule (see recommendation 79). The first exception arises where the secured creditor authorizes the sale or other disposition free of the security right (see recommendation 80, subpara. (a)). The second exception relates to a transfer in the ordinary course of the seller's business where the buyer has no knowledge that the sale or other disposition violates the rights of the secured creditor under the security agreement (see recommendation 81, subpara. (a)). If a security right may be registered (whether registered or not) in an intellectual property registry, as already mentioned (see paras. 181-183), a different rule applies (see the *Guide*, recommendation 78).

185. Recommendation 79 applies equally to security rights in intellectual property that may not be registered in an intellectual property registry and recommendation 78 applies to security rights in intellectual property that may be registered (whether registered or not) in an intellectual property registry. Thus, if a notice in respect of a security right is registered in the general security rights registry, a transferee or licensee of intellectual property will take the encumbered intellectual property subject to the security right, unless one of the exceptions set out in recommendations 80-82 applies (with respect to recommendation 81, subpara. (c), see paras. 188-212 below). These recommendations do not apply, under recommendation 4, subparagraph (b), if they are inconsistent with the priority rules of the law relating to intellectual property that apply specifically to intellectual property.

186. The preceding analysis deals with a priority conflict between a security right and the rights of a subsequent transferee. The situation is different where intellectual property is transferred before the creation of a security right, as no priority conflict arises here under the law recommended in the *Guide*. In this case, as a result of the *nemo dat* principle, the secured creditor will have no security right in the intellectual property at all. As already mentioned, the *Guide* does not interfere with the application of the *nemo dat* principle. To the contrary, this approach is reflected in the general rule in the law recommended in the *Guide* that a grantor can create a security right only in an asset in which the grantor has rights or the power to create a security right (see recommendation 13). This rule would be displaced though by a rule of law relating to intellectual property giving

priority to a secured creditor that took a security right in intellectual property without knowledge of a prior transfer of the intellectual property by the grantor (see the *Guide*, recommendation 4, subpara. (b)).

187. It is also important to note that, as already mentioned (see paras. 23-25, 158 and 159), under the *Guide*, a licence of intellectual property is not a transfer of the licensed intellectual property. Thus, the rules of the law recommended in the *Guide* that apply to transfers of encumbered assets do not apply to licences. However, the law recommended in the *Guide* would defer to law relating to intellectual property treating certain licences (in particular, exclusive licences) as transfers (see recommendation 4, subpara. (b)).

G. Rights of licensees in general

188. Intellectual property is routinely licensed. In such cases, the retained rights of a licensor, such as the ownership right, rights associated with ownership and the rights of a licensor under a licence agreement (such as the right to grant further licences or to obtain payment of royalties), may be used by the licensor as security for credit. Similarly, the licensor's authorization for the licensee to use or exploit the intellectual property or the licensee's right to grant sub-licences and obtain payment of sub-royalties (in both cases according to the terms of the licence agreement) may be used by the licensee as security for credit (as to the types of encumbered asset in an intellectual property context, see paras. 89-112 above).

189. Typically, under secured transactions law, including the law recommended in the *Guide*, a secured creditor does not become an owner of the encumbered asset, unless, upon default, the secured creditor enforces its security right and acquires the asset in an enforcement sale or in satisfaction of the secured obligation (see paras. 29, 30, 87 and 88 above, as well as paras. 237, 238 and 242 below). The question whether the intellectual property owner that has created a security right in its intellectual property is still the owner for purposes of law relating to intellectual property and may, for example, grant a licence in the encumbered intellectual property is a matter to be determined by law relating to intellectual property. Under general principles of law relating to intellectual property (with which the law recommended in the *Guide* is consistent), the grantor who is no longer the owner (or is not entitled to exercise the rights of the owner) may not grant a licence in its encumbered intellectual property if, under law relating to intellectual property, the secured creditor becomes the owner

(or may exercise the rights of an owner) of the intellectual property with authority to grant licences while the security right is in place (see para. 222 below). In this situation, a licence granted by the original owner would be an unauthorized licence under law relating to intellectual property and the licensee would obtain nothing based on the *nemo dat* principle. It also follows that, because the secured creditor only obtains a security right in the rights that the grantor has, in this situation there is no asset which the security right of the secured creditor of the licensee can encumber (see the *Guide*, recommendation 13).

190. If the owner, after creating a security right in its intellectual property, remains the owner but its ability to grant licences is limited by agreement with the secured creditor (to the extent such agreement is permitted under law relating to intellectual property), the owner may theoretically grant a licence, but the granting of a licence by the owner in breach of its agreement with the secured creditor would be an event of default. As a result, the owner's secured creditor could enforce its security right and, exercising the rights of the owner, sell the licensed intellectual property or grant another licence free of the pre-existing licence (and any security right granted by the licensee), as that licensee would normally have taken its licence subject to the security right of the owner's secured creditor (see the *Guide*, recommendations 79 and 161-163). Alternatively, the owner's secured creditor could enforce its security right upon default by collecting the royalties payment of which is owed by the licensee to the owner as licensor. If the encumbered asset is the owner's intellectual property rights, the secured creditor may collect the royalties as proceeds of the encumbered asset (see recommendations 19, 39, 40, 100 and 168). If the encumbered asset is the right of the owner as licensor to the payment of royalties, the secured creditor may collect the royalties as the original encumbered asset. In either case, the secured creditor may collect royalties even before default, but only if there is an agreement to that effect between the owner and its secured creditor (see recommendation 168). In any case, if the licensee took the licensed intellectual property free of the security right created by the owner in the intellectual property, the licensee could retain its licence and the secured creditor could only seek to collect the royalties owed by the licensee to the owner (see recommendations 80, subpara. (b), and 245).

191. If the licensee also creates a security right in its rights under the licence agreement (for example, the right to use or exploit the licensed intellectual property), that security right would be in a different asset (that is, not in the owner's rights). The reason for this result is that the licensee would have taken its rights under the licence agreement subject to the security right created by the owner (see the *Guide*, recommendation 79) and the licensee could not have given to its secured creditor more rights

than the licensee had (based on the *nemo dat* principle). So, if the secured creditor of the owner enforced its security right and disposed of the encumbered intellectual property free of the licence, the licence would terminate upon that disposition and the asset encumbered by the licensee would cease to exist. Likewise, whether or not the owner had created a security right to one of its creditors, if the licensee defaults on the licence agreement, the owner as licensor can terminate it to the extent permitted under law relating to intellectual property and the licensee's secured creditor would be again left without an asset encumbered by its security right.

192. As already mentioned (see paras. 23-25, 158, 159 and 187), the rights of the licensor and the licensee under the licence agreement and the law relating to intellectual property would remain unaffected by secured transactions law. So, if the licensee defaulted on the licence agreement, the licensor could exercise any available right to terminate it and the licensee's secured creditor would again be left without security. Similarly, secured transactions law would not affect an agreement between the licensor and the licensee prohibiting the licensee from granting sub-licences or assigning to the licensor the licensee's rights to the payment of royalties owed by sub-licensees to the licensee as sub-licensor (see paras. 102-104 above).

H. Rights of certain licensees

193. As already mentioned (see para. 184), as a matter of secured transactions law, there are two exceptions to the rule recommended in the *Guide* that a licensee of encumbered intellectual property takes the licence subject to a pre-existing security right (see recommendation 79).

194. The first exception arises where the secured creditor authorizes the granting of a licence by the licensor free of the security right (see recommendation 80, subpara. (b)). Thus, under the law recommended in the *Guide*, in the case of the grantor's default, the secured creditor could collect any royalties owed by the licensee to the grantor as licensor, but not sell the licensed intellectual property free of the rights of the existing licensee or grant another licence with the effect of interfering with the rights of the existing licensee as long as the licensee performs the terms of the licence agreement.

195. The second exception to the principle embodied in recommendation 79 is that a licensee that takes a non-exclusive licence in the ordinary course of business of the licensor without knowledge that the licence violated the

rights of the secured creditor in the licensed intellectual property, takes its rights under the licence agreement unaffected by a security right previously granted by the licensor (see the *Guide*, recommendation 81, subpara. (c), which applies to intangible assets generally, but only if a security right has been created and made effective against third parties before conclusion of a licence agreement). The result of this rule is that, in the case of enforcement of the security right in the licensed intellectual property by the secured creditor of the licensor under the enforcement rules of the law recommended in the *Guide*, the secured creditor could collect any royalties owed by the licensee to the licensor, but not sell the licensed intellectual property free of the rights of the existing licensee or grant another licence with the effect of interfering with the rights of the existing licensee as long as the licensee performs the terms of the licence agreement. This rule is intended to protect everyday, legitimate transactions, such as off-the-shelf purchases of copyrighted software with end-user licence agreements, by limiting the enforcement remedies of a secured creditor under the enforcement rules of the law recommended in the *Guide*. In such transactions, the essence of the protection meant here is that purchasers should not have to do a search in a registry or acquire the copyrighted software subject to security rights created by the software developer or its distributors.

196. Recommendation 81, subparagraph (c), is based on the assumption that the grantor retains ownership of the encumbered intellectual property. This means that recommendation 81, subparagraph (c), does not apply if, under law relating to intellectual property, the grantor is no longer authorized to grant a licence because it has transferred its rights as an owner to the secured creditor (which is not the effect of secured transactions law). In addition, recommendation 81, subparagraph (c), does not affect the relationship between the licensor and the licensee and does not mean that the licensee would obtain a licence free of the terms and conditions of the licence agreement and the law applicable to it (for example, free of a clause in the licence agreement that the licence will terminate upon default); nor does it affect limitations in the licence agreement on the licensee entering into sub-licence agreements. Moreover, this recommendation and the *Guide* as a whole do not interfere with the enforcement of provisions as between the secured creditor and the grantor/licensor (or between the licensor and its licensee) that the grantor/licensor place in all of the non-exclusive ordinary course-of-business licences a provision that the licence will terminate if the licensor's secured creditor enforces its security right.

197. The secured creditor may elect to avoid extending any credit to the grantor until it has an opportunity to review and approve the terms and conditions of any licence or sub-licence agreement entered into by the grantor. For example, the secured creditor may include terms in the security

agreement to ensure that expected royalties are paid up front, to provide for termination of any licence agreement in the case of non-payment of royalties and to prohibit the assignment of any royalties or sub-royalties. In addition, if the secured creditor of the grantor/licensor does not want to encourage non-exclusive licences, it can, in its security agreement (or elsewhere), require the grantor/licensor to place in all of the non-exclusive licences a provision that the licence will terminate if the licensor's secured creditor enforces its security right. Similarly, if the grantor/licensor does not want its licensee to grant any sub-licences, it can include in the licence agreement a provision that the granting of a sub-licence by the licensee is an event of default under the licence agreement that would entitle the licensor to terminate the licence. Nothing in the *Guide* would interfere with the enforcement of such provisions as between the secured creditor and the grantor (or as between the licensor and its licensee). Ordinarily, the secured creditor will have no interest in doing that, since the grantor/licensor (and any licensee) is in the business of granting non-exclusive licences and the secured creditor expects the grantor/licensor to use the fees paid under those licence agreements to pay the secured obligation.

198. From the discussion above it becomes clear that the scope of application of recommendation 81, subparagraph (c), is very limited for a number of reasons. Firstly, secured creditors often have no interest in limiting the ability of an owner/grantor to grant licences in its intellectual property and collect royalties. As a matter of fact, a secured creditor is in many cases interested in permitting licensing so that the owner/grantor may repay the secured obligation. Secondly, by its wording, recommendation 81, subparagraph (c), applies only where there is a non-exclusive licence, one that includes a legitimate “off-the-shelf” purchase of licences of mainly copyrighted software used with respect to equipment and only where the licensee had no knowledge that the licence violated the rights of the secured creditor under the security agreement.

199. In addition, the impact of the application of recommendation 81, subparagraph (c), is very limited. The effectiveness, priority and enforceability of the security right against competing claimants (other than the specific licensee) under secured transactions law are not affected. At the same time, if the secured creditor has other rights under law relating to intellectual property law (for example, the rights of an owner), these rights are not affected by recommendation 81, subparagraph (c). The extent of such rights or remedies is a matter of law relating to intellectual property.

200. However, as the concept of “ordinary course of business” is a concept of commercial law and is not drawn from law relating to intellectual property law, it may create confusion in an intellectual property financing context. Typically, law relating to intellectual property does not distinguish in this respect between exclusive and non-exclusive licences and focuses rather on the

issue whether a licence has been authorized or not. Accordingly, if a licence has been authorized (that is, the grantor of a security right has, under law relating to intellectual property, a right to grant licences in its encumbered intellectual property), the secured creditor of the licensee takes its right in the licence free of a security right created by the licensor.

201. To the contrary, if a licence has not been authorized, the licensee takes the licence subject to a security right created by the licensor. To the extent that a State has such a rule in its law relating to intellectual property, recommendation 81, subparagraph (c), would not apply (see the *Guide*, recommendation 4, subpara. (b)). As a result, unless the secured creditor authorized the grantor to grant licences unaffected by the security right (which will typically be the case as the grantor will rely on its royalty income to pay the secured obligation), the licensee would take the licence subject to the security right. Thus, if the grantor defaults, the secured creditor would be able to enforce its security right in the licensed intellectual property and sell or license it free of the licence. In addition, a person obtaining a security right from the licensee will not obtain an effective security right as the licensee would not have received an authorized licence and would have no right in which to create a security right.

202. If law relating to intellectual property does not address this matter at all or addresses it consistently with the way in which it is addressed in recommendation 81, subparagraph (c), recommendation 81, subparagraph (c), will apply in the limited cases and with the limited impact described above (see the *Guide*, recommendation 4, subpara. (b)).

203. However, in order to avoid any possible inconsistency between the law recommended in the *Guide* and law relating to intellectual property, a different approach could be followed (see recommendation 245 below). Under this approach, recommendation 81, subparagraph (c), would generally apply to rights of a secured creditor under the law recommended in the *Guide* (without affecting the effectiveness of a security right in licensed intellectual property, its priority as against a competing claimant other than a non-exclusive licensee or the enforcement remedies of the secured creditor under secured transactions law that do not affect the rights of the licensee). However, recommendation 81, subparagraph (c), would not affect the rights of a secured creditor if the secured creditor was treated as an owner under law relating to intellectual property (for example, as already mentioned, the law recommended in the *Guide* does not affect any right that the licensor may have to terminate the licence for non-compliance of the licensee with the licence agreement; see paras. 23-25 and 196).

204. It should be noted that, like any other approach recommended in the *Guide* with respect to security rights in intellectual property, this approach also would be subject to recommendation 4, subparagraph (b). In addition, it should be noted that: (a) references in the *Guide* and the *Supplement* to a security right in a priority context refer to a security right that is effective against third parties (otherwise no priority dispute can arise under the *Guide*); and (b) references in the *Guide* and the *Supplement* to an intellectual property licence refer to a licence granted by a person that is authorized to grant a licence in that intellectual property under the law relating to intellectual property.

205. The following examples are designed to clarify the situations to which this approach would apply and the impact of its application. In each example, it should be assumed that: (a) O owns intellectual property; (b) O creates a security right in the intellectual property in favour of SC; (c) SC's security right is effective against third parties either in accordance with the recommendations of the *Guide* or, if the law recommended in the *Guide* does not apply, in accordance with recommendation 4, subparagraph (b), under the law relating to intellectual property; and (d) SC has not agreed, in the security agreement or otherwise, that any licensee of O will enjoy its rights in the encumbered and licensed intellectual property free of SC's security right.

206. After SC takes the steps necessary to make its security right effective against third parties, O, who is in the business of granting non-exclusive licences of the intellectual property on substantially the same terms to any person who agrees to perform in accordance with such terms, offers to license the intellectual property to L. L enters into a licence agreement with O on those terms. O defaults on the obligation secured by the security right and SC sets out to enforce its security right. The right of L to use the intellectual property is protected by recommendation 81, subparagraph (c), and recommendation 245 below against enforcement by SC of its security right. However, SC still has whatever rights it may have against L under law relating to intellectual property and contract law.

207. After SC takes the steps necessary to make its security right effective against third parties, O grants a licence in the intellectual property to L. The licence agreement provides that L may grant sub-licences in the intellectual property only for educational markets. L grants a sub-licence in a commercial market to SL. O defaults on the obligation secured by the security right, and SC sets out to enforce its security right. If, under the law relating to intellectual property, the sub-licence to SL is not authorized, the right of SL to use the intellectual property is not protected by recommendation 81, subparagraph (c), or recommendation 245 below against enforcement by SC of its security right.

208. After SC takes the steps necessary to make its security right effective against third parties, O grants a licence in the intellectual property to L. The licence agreement provides that L has exclusive rights to use the intellectual property in State Z. O defaults on the obligation secured by the security right, and SC sets out to enforce its security right. The right of L to use the intellectual property is not protected by recommendation 81, subparagraph (c), or recommendation 245 below against enforcement by SC of its security right because the licence is exclusive.

209. After SC takes the steps necessary to make its security right effective against third parties, O, who is in the business of granting non-exclusive licences of the intellectual property on substantially the same terms to any person who agrees to perform in accordance with such terms, offers to license the intellectual property to L on such terms. L declines to enter into a licence agreement with O on those terms. Instead, O grants a licence in the intellectual property to L, pursuant to which L has substantially greater rights in the intellectual property than under the licences generally offered to others. O defaults on the obligation secured by the security right, and SC sets out to enforce its security right. The right of L to use the intellectual property is not protected by recommendation 81, subparagraph (c), or recommendation 245 below against enforcement by SC of its security right because the licence is not on substantially the same terms as other licences of the same intellectual property.

210. Before O and L enter into the licence agreement, L discovers the notice filed to make SC's security right effective against third parties and, accordingly, asks to see a copy of the security agreement relating to that notice. The security agreement is furnished to L by O. Upon reading the security agreement, L discovers that the licence to it would violate the rights of SC. Nonetheless, L enters into the licence agreement with O. O defaults on the obligation secured by the security right, and SC sets out to enforce its security right. The right of L to use the intellectual property is not protected by recommendation 81, subparagraph (c), or recommendation 245 below against enforcement by SC of its security right because L had knowledge that the licence agreement would violate SC's rights.

211. However, if O does not furnish a copy of the security agreement to L and, as a result, although L knows of the existence of the security right, L does not know that the licence would violate the rights of SC, the right of L to use the intellectual property is protected by recommendations 81, subparagraph (c), and 245 against enforcement by SC of its security right.

212. After SC takes the steps to make its security right effective against third parties, O offers to license the intellectual property but only to parties

who have experience in using this type of intellectual property. O grants a licence to L, who has that experience. O defaults on the obligation secured by the security right, and SC sets out to enforce its security right. The right of L to use the intellectual property is not protected by recommendation 81, subparagraph (c), or recommendation 245 below against enforcement by SC of its security right because O did not make a licence of the intellectual property available on substantially the same terms to any person who agreed to perform the obligations of the licensee under the licence agreement in accordance with such terms.

I. Priority of a security right in intellectual property granted by a licensor as against a security right granted by a licensee

213. Under the law recommended in the *Guide*, with limited exceptions (see the *Guide*, recommendations 80, subpara. (b), and 81, subpara. (c), and recommendation 245 below), a licensee takes its rights subject to a security right previously created by the licensor in its rights and made effective against third parties (see the *Guide*, recommendation 79). As already explained (see paras. 22 and 23), this means that, upon default, the secured creditor may enforce its security right and sell or license the grantor's rights in the intellectual property. If the licensee also grants a security right in its rights as a sub-licensor against the sub-licensee, no priority conflict arises under the law recommended in the *Guide* between the two security rights because they encumber different assets. The licensor's secured creditor has a security right in the licensor's right to the payment of the royalties owed to the licensor by the licensee under the licence agreement, while the licensee's secured creditor has a security right in any sub-royalties due to the licensee (as sub-licensor) by a sub-licensee under a sub-licence agreement.

214. However, a security right in sub-royalties created by a licensee as a sub-licensor can have an impact on the licensee's ability to pay royalties to the licensor if the licensee is in default with respect to its obligations to its secured creditor inasmuch as that secured creditor may seek to collect the sub-royalties itself. In addition, if the licensee, in payment of royalties owed by the licensee to the licensor, assigns to the licensor the right to the payment of a percentage of the sub-royalties that the licensee will obtain as a sub-licensor from sub-licensees, then a priority conflict may arise between a secured creditor of the licensor and a secured creditor of the licensee under the law recommended in the *Guide*. In such a case, if the assignment of the

right to payment of sub-royalties takes place before a security right is created and made effective against third parties by the licensee, the licensee does not have a right in the right to payment of the assigned sub-royalties at the time it creates a security right and thus a secured creditor of the licensee takes its security right in the right to payment of sub-royalties subject to the security right of the licensor's secured creditor. If, however, the assignment of the right to payment of sub-royalties by the licensee to the licensor takes place after a security right is created and made effective by the licensee in its right to payment of sub-royalties, the licensor takes its rights to payment of sub-royalties subject to the security right of the licensee's secured creditor and thus the licensor's secured creditor takes its security right also subject to the security right of the licensee's secured creditor (see the *Guide*, recommendations 13 and 31).

215. The following example may be useful in illustrating the problem. A creates a security right in all its future assets or rights to the payment of royalties in favour of secured creditor SC1. A then takes an intellectual property licence from licensor B and, in payment of royalties owed to B, licensee A assigns to licensor B the right to payment of a percentage of the sub-royalties payable to licensee A as a sub-licensor. Licensor B creates and makes effective against third parties a security right in these rights to the payment of royalties in favour of secured creditor SC2. Licensee A's secured creditor SC1 will prevail as licensor B took the assignment of the sub-royalties subject to the security right of licensee A's secured creditor SC1 and licensor B's secured creditor SC2 can have no greater rights than licensor B.

216. In this regard, it should be noted that the licensor has, under the law recommended in the *Guide*, numerous ways to protect itself in this circumstance. For example, the licensor can protect its rights by: (a) ensuring that its secured creditor registers first a notice of its security right in the general security rights registry; (b) ensuring that its secured creditor registers first a document or notice in the relevant intellectual property registry; (c) requiring the secured creditor of the licensee to enter into a subordination agreement with the licensor's secured creditor before granting a licence; (d) prohibiting the licensee from granting a security right in its right to the payment of sub-royalties; (e) terminating the licence in cases where the licensee created a security right in its sub-royalties in breach of such a prohibition; or (f) prior to the licensee as sub-licensor granting a security right in its right to the payment of sub-royalties to its secured creditor, granting a security right in its right to payment of a percentage of the sub-royalties and agreeing that any sub-licensee pay its sub-royalties directly to an account of the licensor. The *Guide* does not interfere with any agreements of this kind between licensor and licensee, if they are effective

under law relating to intellectual property and contract law. In addition, the licensor could insist that the licensee grant to the licensor a security right in its right to the payment of sub-royalties and take as a secured creditor the steps just mentioned.

217. However, these steps may protect the licensor to a certain extent only, because, for example: (a) rights in the encumbered intellectual property may not be subject to registration in an intellectual property registry; or (b) it may not be commercially practicable for the licensor to prohibit sub-licensing, terminate the licence agreement or obtain a subordination agreement. In addition, the priority of a security right created by the licensor as against another security right created by the licensee in its right to the payment of sub-royalties would be subject to the general rules explained above (see para. 213).

218. It should be noted that a secured creditor financing the acquisition of an intellectual property right or an intellectual property licence may have the special priority status of an acquisition secured creditor (see chap. IX below). However, this priority status will be relevant only if there is a priority dispute between security rights created by the same grantor in the same asset. Thus, this priority status does not apply to a priority dispute between a security right created by a licensor and a security right created by a licensee.

J. Priority of a security right in intellectual property as against the right of a judgement creditor

219. The *Guide* recommends that a security right that was made effective against third parties before a judgement creditor obtained rights in the encumbered asset have priority as against the right of the judgement creditor. However, if an unsecured creditor obtained a judgement against the grantor and took the steps necessary under the law governing the enforcement of judgements to acquire rights in the encumbered assets before the security right became effective against third parties, the right of the judgement creditor has priority (see the *Guide*, recommendation 84).

220. This recommendation applies equally to security rights in intellectual property (subject to the principle embodied in recommendation 4, subpara. (b)). In such a case, under law relating to intellectual property, the judgement creditor may have to obtain a transfer of the intellectual property and a document or notice thereof may have to be registered in an intellectual

property registry in order for the judgement creditor to obtain priority. If this transfer takes place before a security right was made effective against third parties, both under the law recommended in the *Guide* (see recommendation 13) and law relating to intellectual property (in accordance with the *nemo dat* principle), the transferee of encumbered intellectual property will take the encumbered intellectual property free of the security right.

K. Subordination

221. The law recommended in the *Guide* recognizes the principle of subordination (see recommendation 94). The essence of this principle is that, as long as the rights of third parties are not affected, competing claimants may alter by agreement the priority of their competing claims in an encumbered asset. The principle applies equally to security rights in intellectual property.

Recommendation 245¹⁷

Priority of rights of certain licensees of intellectual property

The law should provide that the rule in recommendation 81, subparagraph (c), applies to the rights of a secured creditor under this law and does not affect the rights the secured creditor may have under the law relating to intellectual property.

¹⁷If it could be included in the *Guide*, this recommendation would be placed in chapter V, Priority of a security right, as recommendation 81 bis. As an asset-specific recommendation, this recommendation would replace general recommendation 81, subparagraph (c), to the extent that it applies to the priority of the rights of a non-exclusive licensee of intellectual property as against the rights of a secured creditor of the licensor.

VI. Rights and obligations of the parties to a security agreement relating to intellectual property

A. Application of the principle of party autonomy

222. With few exceptions, the law recommended in the *Guide* generally recognizes the freedom of the parties to the security agreement to tailor their agreement so as to meet their practical needs (see recommendation 10). The principle of party autonomy applies equally to security rights in intellectual property, subject to any limitations specifically introduced by law relating to intellectual property (see the *Guide*, recommendation 4, subpara. (b)). For example, unless otherwise provided by law relating to intellectual property, an owner/grantor and its secured creditor may agree between themselves that: (a) the secured creditor may exercise some of the rights of the owner/grantor (for example, to deal with authorities, renew registrations or pursue infringers; see para. 75 above); (b) the owner/grantor may not grant licences (in particular exclusive licences) without the consent of the secured creditor; or (c) the secured creditor may collect royalties owed to the owner/grantor as a licensor even before default on the part of the owner/grantor.

B. Preservation of the encumbered intellectual property

223. Under the law recommended in the *Guide*, the party in possession of an encumbered asset has the obligation to take reasonable steps to preserve it (see recommendation 111). Similar rules apply to intellectual property. For example, the grantor has an obligation to deal with authorities, pursue infringers and renew registrations. In some States, law relating to patents provides that the owner/grantor may not revoke or limit the encumbered patent without the consent of the secured creditor.

224. In addition, under the law recommended in the *Guide*, a secured creditor is free to agree with an owner/grantor, in the security agreement or in a separate agreement, that the secured creditor would be entitled to take steps to preserve the encumbered asset (see recommendation 10). With respect to intellectual property, this could include dealing with

authorities, renewing registrations or pursuing infringers, even before default, provided that this is not prohibited by law relating to intellectual property (see recommendation 4, subpara. (b)). If the owner/grantor failed to exercise these rights in a timely fashion, the encumbered intellectual property could lose its value, a result that could negatively affect the use of intellectual property as security for credit. Thus, it would appear appropriate to apply the general approach in the *Guide*, allowing the grantor and secured creditor to agree on steps the secured creditor might take to preserve the encumbered asset, to intellectual property as well (to the extent not prohibited by the law relating to intellectual property). This approach would not interfere with the rights of the owner/grantor as its consent would be necessary. Similarly, this approach would not interfere with law relating to intellectual property because such an agreement would be ineffective, if it were concluded in violation of law relating to intellectual property. States enacting the recommendations of the *Guide* may wish to consider their law relating to intellectual property so as to determine whether such agreements should be permitted, as this would facilitate the use of intellectual property as security for credit.

225. Moreover, under the law recommended in the *Guide*, the secured creditor should be able to request the owner/grantor to allow the secured creditor to preserve the value of the encumbered intellectual property, for example, by dealing with authorities, renewing registrations or pursuing infringers (see recommendation 10), unless prohibited by law relating to intellectual property (see recommendation 4, subpara. (b)). Otherwise, the value of the encumbered intellectual property could diminish and such a result could negatively affect the use of intellectual property as security for credit.

226. If the owner/grantor accepted this request (or the secured creditor was authorized by agreement with the owner/grantor to take steps to preserve the encumbered intellectual property), the secured creditor would be entitled to exercise those rights with the explicit consent of the owner/grantor; if the owner/grantor did not respond, the secured creditor would be entitled to exercise those rights with the implicit consent of the owner/grantor; and, if the owner/grantor rejected the request, the secured creditor would not be entitled to exercise those rights. In addition, if the owner/grantor failed to pursue infringers or renew registrations, the secured creditor could consider that that failure constituted an event of default as described in the security agreement and could enforce its security right in the encumbered intellectual property. Again, these results would not interfere with law relating to intellectual property as recommendation 4, subparagraph (b), would defer to that law in case of any inconsistency.

Recommendation 246¹⁸

Right of the secured creditor to preserve the encumbered intellectual property

The law should provide that the grantor and the secured creditor may agree that the secured creditor is entitled to take steps to preserve the encumbered intellectual property.

¹⁸If it could be included in the *Guide*, this recommendation would be placed in chapter VI, Rights and obligations of the parties to a security agreement, as recommendation 116 bis.

VII. Rights and obligations of third-party obligors in intellectual property financing transactions

227. Where a licensor assigns to its assignee (whether an outright assignee or a secured creditor, see the terms “assignee”, “assignment” and “secured creditor” in the introduction to the *Guide*, sect. B, para. 20) its claim against a licensee for the payment of royalties under a licence agreement, the licensee (as the debtor of the assigned receivable) would be a third-party obligor under the *Guide* and its rights and obligations would be the rights and obligations of a debtor of a receivable. Similarly, where a licensee assigns to its assignee its claim against a sub-licensee for the payment of sub-royalties under a sub-licence agreement, the sub-licensee would be a third-party obligor with respect to the licensee’s assignee in the sense of the *Guide*.

228. As a result, for example, in a claim by an assignee of a licensor’s right to the payment of royalties, a licensee as a debtor of the assigned receivable may raise against the licensor’s assignee all defences and rights of set-off arising from the licence agreement or any other agreement, which are part of the same transaction and of which the licensee could avail itself as if the assignment had not been made and such claim had been made by the licensor. In addition, the licensee may raise against such an assignee any other right of set-off, provided that that right was available to the licensee at the time notification of the assignment was received by the licensee. However, any defences or rights of set-off that may be available to the licensee under law other than secured transactions law for breach of an agreement between the licensor and the licensee that the licensor will not assign its rights to the payment of royalties are not available to the licensee against the licensor’s assignee (see the *Guide*, recommendation 120). As such, the exercise of a right of set-off is not subject to the priority rules in the *Guide*. This recommendation also is subject to the principle of deference to law relating to intellectual property embodied in recommendation 4, subparagraph (b).

VIII. Enforcement of a security right in intellectual property

A. Interaction of secured transactions law and law relating to intellectual property

229. States typically do not provide for specific enforcement remedies for security rights in intellectual property in their laws relating to intellectual property. The general law of secured transactions normally applies to the enforcement of security rights in intellectual property. To the extent that law relating to intellectual property in some States actually does address the enforcement of security rights in different types of intellectual property, it typically engrafts existing secured transactions enforcement regimes onto the regime governing intellectual property. As a consequence, States that enact the *Guide's* recommendations will normally be substituting the *Guide's* recommended enforcement regime for the prior enforcement regime derived from, for example, a civil code and code of civil procedure, the common law of floating and fixed charges, a mortgage act or some other general law of enforcement, as the case may be.

230. The approach of the *Guide* to the enforcement of security rights applies not only to intellectual property (for example, a patent, a copyright or a trademark), but also to other rights that are derived from these types of intellectual property. Hence, consistently with the United Nations Assignment Convention, assets, such as rights to the payment of royalties and other licence fees, are treated as receivables and are subject to the enforcement regime recommended in the *Guide* for assignments (that is, outright transfers, security transfers and security rights) of receivables (see paras. 97-105 above). Likewise, a licensor's or sub-licensor's other contractual rights as against a licensee or sub-licensee will also be governed by a State's general law of obligations and security rights in those contractual rights will be enforced under a State's general secured transactions law. And again, a licensee's or sub-licensee's rights of use are treated in the same way as a lessee's or purchaser's rights and are governed by a State's general law of obligations, except as regards questions of registration (where specifically mentioned in law relating to intellectual property).

231. On occasion, States incorporate special procedural controls on the enforcement of security rights in intellectual property into law relating to intellectual property. In addition, the general procedural norms of secured transactions law in a State may be given a specific content in the context of enforcement of security rights in intellectual property. So, for example, the determination of what is commercially reasonable where the encumbered asset is intellectual property may depend on law and practice relating to intellectual property. This standard of commercial reasonableness may well vary from State to State, as well as from one intellectual property regime to another. The *Guide* recognizes this procedural variation and, in so far as any procedural rules apply specifically to security rights in intellectual property and impose greater obligations on parties than those of the enforcement regime set out in the recommendations of the *Guide*, they will, under the principle set forth in recommendation 4, subparagraph (b), displace the general recommendations of the *Guide*. If these procedural rules apply to security rights in assets other than intellectual property as well, they will be displaced by the recommendations of the *Guide* in States that enact them.

232. As for substantive enforcement rights of secured creditors, once a State adopts the recommendations of the *Guide*, there is no reason to develop different or unusual remedial principles to govern enforcement of security rights in intellectual property. The *Guide* merely recommends a more efficient, transparent and effective enforcement regime for a secured creditor's rights, without in any way limiting the rights that the owner of intellectual property may exercise to protect its rights against infringement or to collect royalties from a licensee or sub-licensee. As already pointed out (see para. 86), the secured creditor generally cannot acquire security in more rights than the rights with which the grantor is vested at the time of the conclusion of the security agreement or when the grantor acquires rights in the encumbered asset or the power to encumber it (see the *Guide*, recommendation 13).

B. Enforcement of a security right relating to different types of intellectual property

233. The *Guide* recommends a detailed regime governing the enforcement of security rights relating to different types of encumbered asset. Its basic assumption is that enforcement remedies must be tailored to ensure the most effective and efficient enforcement while ensuring appropriate protection of the rights of the grantor and third parties. This assumption and approach recommended in the *Guide* should apply equally to the enforcement of security rights in the various categories of intellectual property. Currently, the law of

most States recognizes a wide variety of rights relating to intellectual property, including:

- (a) The intellectual property in itself;
- (b) Receivables arising under a licence agreement;
- (c) The licensor's other contractual rights under a licence agreement;
- (d) The licensee's rights under a licence agreement; and
- (e) The owner's, licensor's and licensee's rights in tangible assets with respect to which intellectual property is used.

234. The enforcement regime recommended in the *Guide*, and applicable to each of these different rights in intellectual property, will be discussed separately in the following sections.

C. Taking possession of documents necessary for the enforcement of a security right in intellectual property

235. The right of the secured creditor to take possession of the encumbered asset as set forth in recommendations 146 and 147 of the *Guide* is normally not relevant if the encumbered asset is an intangible asset such as intellectual property (as the term "possession", as defined in the *Guide*, means actual possession; see the introduction to the *Guide*, sect. B, para. 20). These two recommendations deal only with the taking of possession of tangible assets. However, according to the general principle of extrajudicial enforcement, the secured creditor should be entitled to take possession of any documents necessary for the enforcement of its security right where the encumbered asset is intellectual property, whether or not those documents were specifically mentioned as encumbered assets in the security agreement. Such a right will normally be provided for in the security agreement.

236. It may be thought that, where a secured creditor takes possession of a tangible asset, which is produced using intellectual property or in which intellectual property is included, the secured creditor is also taking possession of the encumbered intellectual property. This is not the case. It is important to identify properly the asset encumbered by the security right. Even though many tangible assets, whether equipment or inventory, may be produced through the application of intellectual property such as a patent, the security right is in the tangible asset and does not, in absence of specific language in the security agreement purporting to encumber the intellectual property itself, encumber the intellectual property used to produce the asset.

The use referred to here means use consistent with the authorization of the owner or other licensor; if the use is unauthorized, the products are unauthorized and the secured creditor may be an infringer. So, for example, the secured creditor may take possession of a tangible asset, such as a compact disc or a digital video disc, and may exercise its enforcement remedies against the discs under the law recommended in the *Guide*. In cases where the secured creditor also wishes to obtain a security right in the intellectual property itself (including, to the extent the grantor has the right to sell or otherwise dispose of, or license the intellectual property, the right to sell or otherwise dispose of, or license it), it would be necessary for the secured creditor to specifically describe such intellectual property as encumbered assets in the security agreement with the grantor (see paras. 108-112 above, and the *Guide*, recommendation 243).

D. Disposition of encumbered intellectual property

237. Under the law recommended in the *Guide*, upon the grantor's default, the secured creditor has the right to dispose of or grant a licence in the encumbered intellectual property (but always within the limits of the rights of the grantor; see recommendation 148). As a result, if the grantor is the owner, the secured creditor should, in principle, have the right to sell (assign) or otherwise dispose of, or license the encumbered intellectual property. However, if the grantor had previously granted an exclusive licence to a third party free of the security right for a certain jurisdiction and time period, upon default, the secured creditor would be unable to grant another licence covering the same use within the same geographical and time limits of the licence, as the grantor had no such right at the time the secured creditor acquired its security right (*nemo dat*). However, the secured creditor may be able to grant another licence outside the geographical or time limits of the exclusive licence previously granted by the grantor.

238. In the above-mentioned situation, under the law recommended in the *Guide*, simply by exercising its enforcement rights, the enforcing secured creditor does not acquire the intellectual property against which the security right is being enforced. Instead, the secured creditor disposes of the encumbered intellectual property (by assigning or licensing it) in the name of the grantor. Under law relating to intellectual property, until the assignee or licensee (as the case may be) that acquires the rights upon a disposition by the enforcing secured creditor registers a notice (or other document) of its rights in the relevant registry (assuming the rights in question may be registered), the grantor will appear on the registry as the owner of the relevant intellectual property.

E. Rights acquired through disposition of encumbered intellectual property

239. Under the law recommended in the *Guide*, rights in intellectual property acquired through judicial disposition would be regulated by the relevant law applicable to the enforcement of court judgements (see recommendation 160). In the case of an extrajudicial disposition in line with the law recommended in the *Guide*, the first point to note is that the transferee or licensee takes its rights directly from the grantor. The secured creditor that chooses to enforce its rights in this manner does not become the owner merely as a result of this enforcement process, unless the secured creditor acquires the encumbered intellectual property in total or partial satisfaction of the secured obligation or at an enforcement sale (see recommendations 148 and 156).

240. The second point is that the transferee or licensee could only take such rights as were actually encumbered by the enforcing secured creditor's security right. Under the law recommended in the *Guide*, the transferee or licensee would take the intellectual property free of the security right of the enforcing secured creditor and any lower-ranking security rights, but subject to any higher-ranking security rights. Similarly, a good-faith transferee or licensee that acquired a right in intellectual property pursuant to an extrajudicial disposition that is inconsistent with the law recommended in the *Guide* would take the intellectual property free of the security right of the enforcing secured creditor and any lower-ranking security rights (see recommendations 161-163).

241. Under the law recommended in the *Guide*, a security right in a tangible asset extends to and may be enforced against attachments to that asset (see recommendations 21 and 166). To ensure that the security right also covers assets produced or manufactured by the grantor from encumbered assets, the security agreement normally provides expressly that the security right extends to such manufactured assets. Where the encumbered asset is intellectual property, it is important to determine whether the asset that is disposed of to the transferee or licensee is simply the intellectual property as it existed at the time the security right became effective against third parties or whether it also includes any subsequent improvement to it (for example, an enhancement of a patent or an adaptation of copyrighted work). Generally, laws relating to intellectual property treat such improvements ("updates", "adaptations" or "enhancements") as separate assets and not as integral parts of existing intellectual property. As a result, a prudent secured creditor that wishes to ensure that improvements are encumbered with the security right should describe the encumbered asset in the security agreement in a manner that ensures that improvements are directly encumbered by the security right (see paras. 116 and 117 above).

F. Proposal by the secured creditor to acquire the encumbered intellectual property

242. Under the enforcement regime recommended in the *Guide*, the secured creditor has the right to propose to the grantor that it acquire the grantor's rights in total or partial satisfaction of the secured obligation. If the grantor is the owner of intellectual property, the secured creditor could itself become the owner in the way prescribed by law relating to intellectual property, provided that the grantor and any other interested party (such as the debtor, any other person owing performance of the secured obligation or any person with rights in the encumbered asset) do not object (see the *Guide*, recommendations 156-159). Should the owner have licensed its intellectual property to a licensee that acquired its rights under the licence agreement free of the rights of the enforcing secured creditor, when the secured creditor acquires the intellectual property from the grantor, it acquires that right subject to the prior-ranking licence in accordance with the *nemo dat* principle. Once a secured creditor becomes the owner of intellectual property, its rights and obligations are regulated by the relevant law relating to intellectual property. In particular, the secured creditor may need to register a notice or document confirming that it acquired the intellectual property to enjoy the rights of an owner or to obtain any relevant priority. Finally, the secured creditor that acquires the encumbered intellectual property in total or partial satisfaction of the secured obligation would take the intellectual property free of any lower-ranking security rights, but subject to any higher-ranking security rights (see recommendation 161).

G. Collection of royalties and other licence fees

243. Under the enforcement regime recommended in the *Guide*, where the encumbered asset is the right to receive payment of royalties and other fees under a licence agreement, the secured creditor should be entitled to enforce the security right by simply collecting the royalties and other licence fees upon default and notification to the person that owes the royalties or fees (see recommendation 168). In all these situations, the right to the payment of royalties and other licence fees is, for the purposes of secured transactions laws, a receivable (see paras. 98-105 above). Thus, the rights and obligations of the parties will be governed by the principles pertaining to receivables that are set forth in the United Nations Assignment Convention and the regime recommended in the *Guide* for receivables. Once again, the secured creditor that has taken a security right in the right to the payment of present and future royalties is entitled to enforce only such rights to the payment of royalties (including rights to the payment of future royalties under existing licenses)

as were vested in the grantor (licensor) at the time of the conclusion of the security agreement or when the grantor acquired rights in the encumbered receivable or the power to encumber it (see the *Guide*, recommendation 13). In addition, subject to any contrary provision of law relating to intellectual property (see recommendation 4, subpara. (b)), the secured creditor's rights to collect royalties includes the right to collect or otherwise enforce any personal or property right that secures payment of the royalties (see recommendation 169).

H. Licensor's other contractual rights

244. In addition to the right to collect royalties, the licensor will normally include a number of other contractual rights in its agreement with the licensee (see para. 97 above). These may include, for example, the licensor's right to terminate the licence agreement if the licensee, in violation of an agreement not to grant any sub-licence or to create a security right in its rights under the licence agreement, grants such a sub-licence or creates such a security right. Where the licensor creates a security right only in its right to collect royalties, these rights will remain vested in the licensor. However, if the secured creditor also wishes to obtain a security right in these other rights of the licensor, they would have to be included in the description of the encumbered assets in the security agreement. In any case, if the secured creditor enforces its security right in the licensor's rights under a licence agreement and takes the encumbered intellectual property, as a matter of contract law, the secured creditor will be bound by the terms and conditions of the licence agreement.

I. Enforcement of security rights in tangible assets with respect to which intellectual property is used

245. In principle, except where the so-called "exhaustion doctrine" applies, the intellectual property owner has the right to control the manner and place in which the encumbered tangible assets with respect to which intellectual property is used (in line with the authorization of the owner), are sold. That is, in the event that the relevant intellectual property right has not been exhausted, the secured creditor should be able to dispose of the tangible assets only upon default and only if there is an authorization from the intellectual property owner (it is assumed that the security agreement does not encumber the intellectual property right itself; see paras. 108-112 and recommendation 243 above).

246. As there is no universal understanding of the “exhaustion doctrine” (often referred to as “exhaustion of rights” or “first-sale doctrine”), the *Supplement* makes reference to the doctrine not as a universal concept, but as it is actually understood in each State. Nonetheless, where the exhaustion doctrine applies under law relating to intellectual property, the basic idea is that an intellectual property owner will lose or “exhaust” certain rights when specific conditions are met, such as the first marketing or sale of the product embodying the intellectual property. For example, the ability of a trademark owner to control further sales of a product bearing its trademark is generally “exhausted” following the initial sale of that product. This doctrine serves to protect a person that resells that product from infringement liability. However, it is important to note that such protection extends only to the point where the products have not been altered so as to be materially different from those originating from the trademark owner or other authorized producer. In addition, the exhaustion doctrine does not apply if a licensee produces products bearing the licensed trademark without complying with the terms and conditions of the licence agreement (for example, as to quality or quantity).

247. In situations where a product is produced with the use of intellectual property that has been licensed to a licensee and that licensee attempts to create a security right in that product, under law relating to intellectual property, the licence agreement may provide that: (a) the licensee cannot create a security right in that product; and (b) a secured creditor may only enforce its security right in a manner agreed to by the licensor. In both these cases, the licence agreement will typically provide that the licensor may revoke the licence if the licensee acts as grantor or secured creditor in a manner that is contrary to the limitations contained in the licence agreement. As a consequence, in order to enforce effectively its security right in the product, in the absence of prior agreement between the secured creditor and the owner/licensor, the secured creditor would: (a) need to obtain the consent of the owner/licensor; or (b) rely on the relevant law relating to intellectual property and the operation of the exhaustion doctrine.

248. In cases where the secured creditor also wished to obtain a security right in the intellectual property itself (including, to the extent the grantor has the right to sell or license the intellectual property, the right to sell or license it), it would be necessary for the secured creditor to specifically refer to such intellectual property as an encumbered asset in the security agreement. Here, the encumbered asset is not the product produced using the intellectual property, but rather the intellectual property itself (or the licence to manufacture tangible assets using the intellectual property). A prudent secured creditor will normally seek to take a security right in

such intellectual property so as to be able to enforce its security right and sell or license the intellectual property to ensure that the licensee will be able to continue the production of any partially completed products.

J. Enforcement of a security right in a licensee's rights

249. In the discussion above, the grantor of the security right has been assumed to be the owner of the relevant intellectual property. The encumbered asset is one or more of the following rights: (a) the intellectual property itself; (b) the right of the owner/licensor to receive payment of royalties and other licence fees; or (c) the right of the owner/licensor to enforce other contractual terms relating to the intellectual property. Only in the discussion of security rights in tangible assets produced with the use of intellectual property (see paras. 245-248 above) were the rights of the owner/licensor and the rights of the licensee discussed together. However, most of the issues addressed in sections C-H of this chapter also are relevant in situations where the encumbered asset is not the intellectual property itself but the rights of a licensee (or sub-licensee) arising from a licence agreement (see paras. 106 and 107 above). In cases where the encumbered asset is merely a licence, the secured creditor obviously may only enforce its security right against the licensee's rights and may do so only in a manner that is consistent with the terms of the licence agreement.

250. In situations where the grantor is a licensee, upon the grantor's default, the secured creditor will have the right to enforce its security right in the licensee's rights under the licence agreement and to dispose of the licence to a transferee, provided that the licensor consents or the licence is transferable, which is rarely the case. Likewise, the enforcing secured creditor may grant a sub-licence, provided that the licensor consents or the grantor/licensee had, under the terms of the licence agreement, the right to grant sub-licences. In situations where the secured creditor proposes to a grantor/licensee to acquire the licence in total or partial satisfaction of the secured obligation and neither the grantor nor any other interested party (such as the debtor, any other person owing performance of the secured obligation or any person with rights in the encumbered asset; see the *Guide*, recommendations 156-158) object (and the licence agreement does not prohibit the transfer of the licence), the secured creditor becomes vested with the licence according to the terms of the licence agreement between the licensee and the licensor. Assuming that registration of licences is possible under law relating to intellectual

property, registration of the licence by the licensee/secured creditor that acquires the licence in total or partial satisfaction of the secured obligation may be a condition of the effectiveness of the licensee's rights or may simply serve information purposes.

251. Where the encumbered asset is the sub-licensor's right to the payment of royalties under a sub-licence agreement, the regime recommended in the *Guide* treats the asset as a receivable. This means that the secured creditor of the licensee/sub-licensor may collect the royalties to the extent that these were vested in the grantor/sub-licensor at the time when the security right in the receivable is enforced. In the case where creation by the licensee/sub-licensor of a security right in its right to payment of royalties owed by its sub-licensee constitutes a breach of an initial or intervening licence agreement, the licensor would retain all its contractual rights under the licence agreement, including the right to terminate that agreement, and the secured creditor of the licensee/sub-licensor would also retain its right to collect sub-royalties, at least, as long as the licensor did not terminate the licence agreement.

252. Where the encumbered asset is another contractual right stipulated in the sub-licence agreement, the secured creditor may enforce its security right in this contractual right as if it were any other encumbered asset. The fact that the licensor may have revoked the licence for the future or may have itself claimed a prior right to receive payment of sub-royalties, has no direct bearing on the right of the secured creditor to enforce these other contractual rights set out in the licence agreement.

253. The rights acquired by a transferee or sub-licensee of the encumbered licensee's rights upon disposition by the secured creditor or by a secured creditor that acquires the licensee's rights in total or partial satisfaction of the secured obligation may be significantly limited by the terms and conditions of the licence agreement. For example, a non-exclusive licensee cannot exercise its rights in the intellectual property against another non-exclusive licensee or against an infringer of the intellectual property. Only the licensor (or the owner) may do so, although, in some States, exclusive licensees may join the licensor as a party to the proceedings or even pursue infringers on their own. In addition, depending upon the terms and conditions of the licence agreement and the description of the encumbered asset in the security agreement, a transferee of the licence may not have access to information such as a source code. In order to ensure the effectiveness of the licence being transferred or sub-licensed, the security agreement will have to include such rights within the description of the assets encumbered by the grantor/licensee, to the extent that the licence agreement and relevant law permits it to encumber these rights as well.

IX. Acquisition financing in an intellectual property context

A. Introduction

254. Historically and in contemporary commercial and legal practice, many States have enacted a special regime to govern acquisition financing with respect to tangible assets. In accordance with these widespread practices, the discussion of acquisition financing in the *Guide* focuses on tangible assets such as consumer goods, equipment and inventory. The *Guide* does not make recommendations with respect to acquisition financing of other types of tangible asset such as negotiable instruments and negotiable documents. In addition, the *Guide* does not recommend that a special regime be established for acquisition financing with respect to intangible assets. Moreover, the *Guide* does not address explicitly the question whether a security right, and in particular an acquisition security right in a tangible asset with respect to which software is used, extends to the software (an intangible asset). However, the *Supplement* makes clear that a security right of any type in a tangible asset does not automatically extend to intellectual property used with respect to that asset, unless otherwise agreed by the parties (see paras. 108-112 and recommendation 243 above).

255. In particular, the *Guide* leaves open the question whether, in a modern credit economy, it would be useful to permit the creation of acquisition security rights in favour of lenders that finance the acquisition (but not the original creation) of intellectual property. Such an approach would provide general parity in the treatment of tangible assets and intellectual property rights. Given the significant differences in legal regimes governing intellectual property and other types of asset, if such an approach were adopted, the principles of the *Guide* on acquisition financing with respect to tangible assets could not simply be transposed to the intellectual property context. They would have to be adapted, as discussed in sections B and C below, to apply with respect to intellectual property.

B. Unitary approach

256. The basic idea of providing a special regime of acquisition financing for intellectual property is not unknown. For example, in some legal systems, a creditor may obtain an acquisition security right in copyrighted software, but only if: (a) the security right accompanies an acquisition security right in a tangible asset; (b) the software is acquired by the grantor in a transaction integrated with the transaction in which the grantor acquired the tangible asset; and (c) the grantor acquires the software for the principal purpose of using the software in the tangible asset. In other legal systems, it is possible for a secured creditor to obtain an acquisition security right in intangible assets (including intellectual property, whether or not the intellectual property is used in connection with tangible assets). In yet other legal systems, where the general law as set forth, for example, in a civil code does not contain the concept of an acquisition security right, a similar result may be achieved through a reservation of title, a financial lease or a hypothec securing the sales price of a movable asset. In each of these cases, the transaction may relate to an intangible asset, including an intellectual property right, although this is not common. Finally, in yet other legal systems, it is possible to use a “mortgage” or “fixed charge” to secure the payment obligation of the purchaser of intellectual property and, in such cases, the “mortgage” or “fixed charge” may prevail over a pre-existing “floating charge” (for a discussion of fixed and floating charges, see the *Guide*, chap. II, para. 67).

257. The rules on acquisition financing in the law recommended in the *Guide* are meant to rationalize and streamline different legal techniques by which creditors may obtain an acquisition security right in a tangible asset. Achieving general parity in regimes governing tangible assets and intellectual property rights would require a number of basic adjustments to the law recommended in the *Guide*. More specifically, it would be necessary to:

(a) To provide explicitly that acquisition security rights can exist in intellectual property, as well as in a tangible asset;

(b) To provide that States could adopt either a unitary or a non-unitary approach to acquisition financing;

(c) To eliminate any references to possession and delivery of the encumbered asset; and

(d) To develop appropriate distinctions between the acquisition financing of the intellectual property right itself and the acquisition financing of a licence or sub-licence of that intellectual property right.

258. In addition to these general adjustments, a number of more specific adjustments would be required. These adjustments would relate to: (a) the

third-party effectiveness and priority of an acquisition security right in intellectual property; (b) the priority of a security right registered in an intellectual property registry; and (c) the priority of a security right in proceeds of encumbered intellectual property. These specific adjustments are considered below in turn.

1. *Third-party effectiveness and priority of an acquisition security right in intellectual property*

259. In the chapter on acquisition financing, the *Guide* distinguishes between three different types of tangible asset, namely, consumer goods, inventory and assets other than inventory or consumer goods (such as equipment). The law recommended in the *Guide* provides that an acquisition security right in consumer goods (that is, goods used or intended to be used by the grantor for personal, family or household purposes; see the introduction to the *Guide*, sect. B, para. 20) is automatically effective against third parties upon its creation (that is, is effective against third parties without the need for registration) and has priority against a competing non-acquisition security right (see the *Guide*, recommendation 179).

260. The law recommended in the *Guide* offers alternatives for obtaining third-party effectiveness in relation to inventory and equipment. Under the first alternative, an acquisition security right in tangible assets other than consumer goods or inventory (that is, equipment) would have priority over a competing non-acquisition security right granted in the same asset by the same grantor, provided that the acquisition secured creditor retained possession of the asset or a notice of the acquisition security right was registered in the general security rights registry within a short period of time after the grantor obtained possession of the asset (see the *Guide*, recommendation 180, alternative A, subpara. (a)). A different rule would apply with respect to security rights in inventory (that is, in assets held by the grantor for sale, lease or licence in the ordinary course of the grantor's business; see the introduction to the *Guide*, sect. B, para. 20). In this situation, an acquisition secured creditor must have retained possession of the asset or registration of a notice in the general security rights registry would have to occur before delivery of the inventory to the grantor and secured creditors with earlier registered non-acquisition security rights would have to be notified of the acquisition secured creditor's intention to claim an acquisition security right, once again before delivery of the inventory to the grantor (see the *Guide*, recommendation 180, alternative A, subpara. (b)). By contrast, under a second alternative, no distinction would be drawn between inventory

and assets other than consumer goods or inventory. Under this alternative, the rule applicable under the first alternative to assets other than inventory would apply to all types of asset other than consumer goods (see recommendation 180, alternative B).

261. To adapt the law recommended in the *Guide* to intellectual property rights, the following adjustments would be necessary. In cases in which the intellectual property that is subject to an acquisition security right is used or intended to be used by the grantor for personal, family or household purposes, the acquisition security right would be treated according to the same rules as those that govern an acquisition security right in consumer goods. In cases in which the intellectual property that is subject to an acquisition security right is held by the grantor for sale or licence in the ordinary course of the grantor's business, the acquisition security right would be treated according to the same rules as those that govern an acquisition security right in inventory. And in cases in which the intellectual property that is subject to an acquisition security right is not held by the grantor for sale or licence in the ordinary course of the grantor's business or for personal, family or household purposes, the acquisition security right would be treated according to the same rules as those that govern an acquisition security right in tangible assets other than inventory or consumer goods. In adapting the law recommended in the *Guide* to intellectual property rights, the expression "sale, lease or license" should also be adapted to fit an intellectual property context in a manner that would be consistent with law relating to intellectual property. For example, if under law relating to intellectual property intellectual property is not properly the subject of a "sale", the term "sale" should be understood as meaning an "assignment" of intellectual property. Similarly, if under law relating to intellectual property intellectual property is not properly the subject of a "lease", this term should be understood as meaning a "licence" of intellectual property.

262. As intellectual property may be held for multiple purposes, reference should always be made to the primary (or predominant) purpose for which the relevant intellectual property is held by a person. The same criterion should be used for determining whether a transaction was in the ordinary course of business, rather than whether the transaction was based on standard terms agreed upon without negotiation. As a result, if intellectual property is held by the grantor primarily for sale or licence, a transaction relating to such intellectual property would typically be a transaction in the grantor's ordinary course of business.

263. If these adjustments were made, the rules relating to third-party effectiveness and priority of acquisition security rights in intellectual property would be as follows. In cases where the intellectual property right is acquired

for personal, family or household purposes, the acquisition security right would be automatically effective against third parties upon its creation (that is, effective against third parties without the need for registration) and would have priority against a competing non-acquisition security right (transposing recommendation 179). In cases involving inventory and equipment, it would be necessary to transpose both alternatives set out in the *Guide*. Under alternative A, an acquisition security right in intellectual property or a licence for use in the licensee's business and not for licensing or sub-licensing respectively would have priority over another security right granted in the same asset by the same grantor, provided that a notice of the acquisition security right was registered in the general security rights registry within a short period of time after the grantor acquired the intellectual property or licence (transposing recommendation 180, alternative A, subpara. (a)). Also under this alternative, an acquisition security right in intellectual property or a licence not held by the grantor for use in its business but meant for licensing or sub-licensing respectively would have priority over another security right granted in the same asset by the same grantor, provided that a notice of the acquisition security right was registered in the general security rights registry prior to the license being granted and secured creditors with earlier registered non-acquisition security rights were notified of the acquisition secured creditor's intention to claim an acquisition security right also prior to the license being granted (transposing recommendation 180, alternative A, subpara. (b)). Under alternative B, the regime governing intellectual property rights held for use in the grantor's business and not for licensing or sub-licensing would apply for all types of intellectual property or licences (transposing recommendation 180, alternative B).

2. *Priority of an acquisition security right registered in an intellectual property registry*

264. As a general rule, the law recommended by the *Guide* does not seek to modify any rules set out in other law that are applicable to specialized registries whether in relation to third-party effectiveness (see recommendations 34, 38 and 42) or priority (see recommendations 77 and 78). This policy is also adopted in the chapter on acquisition financing (see recommendation 181). Two consequences follow. Firstly, the special priority status granted to an acquisition security right over prior registered non-acquisition security rights refers only to security rights registered in the general security rights registry and not to security rights registered in specialized registries. Secondly, the general priority afforded by other law to security rights registered in specialized registries is maintained by the law recommended

in the *Guide*, regardless of whether the security right is or is not an acquisition security right. Thus, if the priority rules of the specialized registration regime provide for priority based exclusively on the time of registration, an acquisition security right in intellectual property registered in an intellectual property registry would not have priority over an earlier-registered security right registered in the intellectual property registry. Similarly, if the priority rules of the specialized registration regime afford priority to a later-registered acquisition security right, that priority would not be affected by the law recommended in the *Guide*.

265. The approach recommended in the *Guide* is justified by the need to avoid interfering with specialized registration regimes. However, it does not facilitate acquisition financing to the extent the priority rules of an intellectual property registration regime do not provide for a special priority status for acquisition security rights in intellectual property. As already mentioned (see para. 129), States enacting the recommendations of the *Guide* may wish to review their law relating to intellectual property with a view to determining whether the registration of notices of security rights in an intellectual property registry should be permitted. States may also wish to consider extending the special priority status of an acquisition security right to an acquisition security right registered in an appropriate manner in an intellectual property registry.

266. The following example may be useful in clarifying why such a regime might merit consideration. State A that has enacted the recommendations of the *Guide* also decides to permit registration of notices of security rights in intellectual property (even future intellectual property) in the relevant intellectual property registry as a method of achieving third-party effectiveness. A bank has extended credit to the grantor, and this credit is secured by a security right in all present and future intellectual property rights of the grantor. The bank has made that right effective against third parties by registering in the specialized registry. The security right in each future item of intellectual property is not effective against third parties until the grantor acquires that item. Nonetheless, under the general priority principles recommended in the *Guide*, which the State would presumably adopt if it were to permit registration of notices of security rights in future intellectual property, priority dates from the date of registration (see recommendation 76).

267. The grantor then wants to acquire a particular item of intellectual property on credit. The seller is willing to sell on credit only if it is granted a security right in the item to secure the remaining payment obligation. Under the rules of the law recommended in the *Guide* and in particular in view of recommendation 4, subparagraph (b), there is no way that the seller

can achieve the status of an acquisition financier with a special priority over already registered non-acquisition security rights unless the law relating to intellectual property so provides. That is to say, even if the seller wishing to achieve the special priority status of an acquisition financier follows all the steps necessary to claim such a right and registers a notice, a security right, a notice or document of which was registered in a specialized registry will always have priority over a security right, a notice of which was registered in the general registry (see the *Guide*, recommendation 77). Thus, if the specialized registration regime permits the registration of security rights in intellectual property but does not at the same time provide for a special priority status of acquisition financiers, a security right in present and future intellectual property registered first in the relevant intellectual property registry will have priority over the rights of an acquisition financier that takes a security right in the intellectual property being sold, registering a notice in the general security rights registry. Such a seller would have to rely on a transaction by which it retained title to the intellectual property right in question, provided that law relating to intellectual property recognized that approach (see paras. 280-283 below). The same situation could occur where: (a) the grantor seeks to acquire an exclusive licence, which is treated as a transfer of the intellectual property itself; (b) a licensor would be willing to grant a non-exclusive licence on credit if it is granted additional protection beyond that which it would get by simply terminating the licence agreement; (c) a licensee, as a sub-licensor, is willing to grant a non-exclusive sub-licence only if it can acquire a security right in the rights of a sub-licensee and any rights to payment of sub-royalties payable to the sub-licensee by a sub-sub-licensee; and (d) the acquisition financing is provided not by the owner as transferor or as licensor, nor by the licensee as sub-licensor, but by a third-party lender.

268. In many situations, however, if a transferor or licensor of intellectual property that is subject to specialized registration finances the acquisition of the intellectual property by the transferee or of the licence by the licensee, it can obtain the benefits of an acquisition secured creditor. This result follows in cases where the intellectual property registration regime permits the registration of security rights in general but does not permit the registration of security rights in future intellectual property. In such cases, a secured creditor of a transferee or licensee can register only after the registration of the transfer or licence. For example, at the same time A registers a transfer or licence to B on credit, A registers a notice with respect to a security right in the intellectual property to secure any outstanding payment obligation. Owing to the different operation of the specialized registration regimes (asset-specific registration), the general financier of B can only register after the transfer or licence to B is registered. Thus, A will necessarily obtain its security right before the general financier of B and

will in effect have functionally the same priority status as an acquisition financier. In other words, in these cases, the fact that an equivalent rule to that of recommendation 181 does not apply to the intellectual property register will not prevent the seller or licensor from obtaining priority. However, this result will only benefit the transferor or licensor financing the acquisition of the intellectual property by the transferee or of the licence by the licensee, and will not automatically permit a lender that finances the transferee or the licensee to obtain priority. That acquisition financier could only obtain first priority if it were the first secured creditor to register a notice with respect to its security right in the specialized registry after the transfer or license had itself been registered.

3. *Priority of an acquisition security right in proceeds of encumbered intellectual property*

269. A key feature of the acquisition financing regime recommended in the *Guide* relates to the treatment of acquisition security rights in proceeds of encumbered assets. The general rule in the law recommended by the *Guide* is that the priority of a security right in proceeds should follow that of the security right in the original encumbered assets (see recommendations 76 and 100). By contrast, the priority of a security right in proceeds of an asset that was subject to an acquisition security right does not automatically follow the priority of the acquisition security right in the initial encumbered asset. Once again, a distinction is drawn between consumer goods, inventory and assets other than inventory or consumer goods, such as equipment (see recommendation 185). As in the case of the original encumbered asset, the *Guide* offers alternatives.

270. Under alternative A, a security right in proceeds of tangible assets other than inventory or consumer goods has the same priority as the acquisition security right itself (see the *Guide*, recommendation 185, alternative A, subpara. (a)). However, a security right in proceeds of inventory only has the priority of an acquisition security right in inventory if the proceeds are not in the form of receivables, negotiable instruments, rights to payment of funds credited to a bank account or rights to receive proceeds under an independent undertaking (see recommendation 185, alternative A, subpara. (b)). Under alternative B, the security right in proceeds of the original encumbered asset has only the priority of a non-acquisition security right (see recommendation 185, alternative B). The consequence is that, when either of the alternatives of recommendation 185 is transposed to acquisition security rights in intellectual property, the revenue stream

generated by the licensing or sub-licensing of an intellectual property right continues to be encumbered with the security right. An additional consequence is that the security right in the royalties will not have the special priority of an acquisition security right.

271. It might be argued that this direct transposition is not optimal in the case of acquisition security rights in intellectual property. For example, intellectual property owners and licensors typically rely on their rights to payment of royalties to develop new ideas protected by intellectual property rights. Additionally, if the rights of secured creditors with an all-asset security right in rights of licensees always had priority over the rights of secured creditors with a security right in rights of intellectual property owners or licensors, owners or licensors would not be able to effectively use their rights to payment of royalties as security for credit. By contrast, it might also be argued that intellectual property owners and licensors could achieve an equivalent result by ensuring that they or their secured creditors: (a) obtained a security right in or an outright assignment of a right to payment of a percentage of the sub-royalties payable to the licensee as a sub-licensor by sub-licensees and registered a notice thereof in the relevant intellectual property registry before any registration in that registry by a secured creditor of the licensee; (b) obtained a security right in or an outright assignment of a right to payment of a percentage of the sub-royalties payable to the licensee as a sub-licensor by sub-licensees and registered first a notice thereof in the general security rights registry; or (c) obtained a subordination agreement from the secured creditor of the licensee.

272. As the objective of transposing the recommendations of the *Guide* to the intellectual property context is to ensure a parity of treatment between acquisition security rights in tangible assets and acquisition security rights in intellectual property, it is preferable to retain the same outcome in both cases. This would be particularly important where a grantor created a security right over all its present and future tangible and intangible assets. As a result, the *Supplement* recommends that the rules recommended in the *Guide* with respect to security rights in proceeds of original encumbered tangible assets subject to an acquisition security right be transposed without further modification into the regime governing acquisition financing of intellectual property (see recommendation 247 below). This result achieves an appropriate balance between the needs of the licensor to collect royalties and the needs of the financier extending credit to the licensee based on the licensee's rights to the payment of sub-royalties. For example, upon the licensee's default in the payment of royalties, the licensor will normally have the right to terminate the licence agreement and recover the licensed intellectual property. If the licensee's secured creditor (whose security right in the rights to payment of royalties as proceeds of intellectual property will have priority over the

security right of the licensor's secured creditor) wants to be able to obtain benefits from the licensed intellectual property, the secured creditor will need to cure the default, paying past due and even future royalties. Alternatively, if the licensee's secured creditor does not want to do so, it may be able to retain the royalties already collected, but would be unable to collect future royalties if the licensor terminates the licence agreement. This means that, from the licensor's perspective, the essential risk relates to royalties collected by the licensee or its secured creditor but not paid to the licensor. The licensor may address this risk by contractual terms relating to the timing of accounting and payments.

4. Examples illustrating how the acquisition financing recommendations of the Guide could apply in an intellectual property context

273. The following examples may be useful in clarifying how the recommendations of the *Guide* could apply in an intellectual property context. In all these examples, the owner or a later secured creditor financing the acquisition of intellectual property or a licence in intellectual property has an acquisition security right with special priority over a non-acquisition security right under the conditions described in the examples.

(a) Acquisition security right in intellectual property securing the purchase price of the intellectual property used in the grantor's business

274. B creates a security right in all of its present and future movable assets (including intellectual property) in favour of SC, who takes the actions necessary to make that security right effective against third parties. Subsequently, B acquires a patent from O to be used in B's business. Pursuant to the agreement between B and O, B agrees to pay the purchase price to O over time and B grants O a security right in the patent to secure B's obligation to pay the purchase price. O makes that security right effective against third parties within a short period of time such as 20 or 30 days after B obtains the patent. O's security right is an acquisition security right and has priority over the security right of SC (see recommendation 180, alternative A, subpara. (a), or alternative B, subpara. (b)). Whether the priority of O's security right extends to proceeds of the patent in the form of receivables, negotiable instruments, rights to payment of funds credited to a bank account or rights to receive proceeds under an independent undertaking depends on which version of recommendation 185 a State enacts. Under alternative A, the priority of O's security right carries over into the proceeds (see recommendation 185, alternative A, subpara. (a),

as transposed). Under alternative B, O's security right in the proceeds would have only the priority of a non-acquisition security right (see recommendation 185, alternative B, as transposed).

(b) Acquisition security right in intellectual property securing the purchase price of the intellectual property held by the grantor for sale or licence

275. B creates a security right in all of its present and future movable assets (including intellectual property) in favour of SC1, who takes the actions necessary to make the security right effective against third parties. Subsequently, B acquires a patent from O for the purpose of licensing it to third parties in the ordinary course of B's business. B obtains the money necessary to pay the purchase price to O by borrowing money from SC2, to whom B grants a security right in the patent to secure B's repayment obligation. Before B obtains the patent, SC2: (a) takes the actions necessary to make its security right effective against third parties; and (b) notifies SC1 that SC2 has an acquisition security right. SC2's security right is an acquisition security right and has priority over the security right of SC1 (see recommendation 180, alternative A, subpara. (b), and alternative B, subpara. (b), as transposed). The priority of SC2's security right does not extend to proceeds of the patent in the form of receivables, negotiable instruments and rights to payment of funds credited to a bank account or rights to receive proceeds under an independent undertaking, although it does extend to other types of proceeds (see recommendation 185, alternative A, subpara. (b), and alternative B, as transposed).

(c) Acquisition security right in an intellectual property licence securing the purchase price of the licence used in the grantor's business

276. B has created a security right in all of its present and future movable assets (including intellectual property) in favour of SC, who has taken the actions necessary for that security right to be effective against third parties. Subsequently, B obtains a licence from O to use a patent owned by O in B's business. B agrees to pay the licence fee to O over time and grants O a security right in B's rights as licensee to secure B's payment obligation. O makes that security right effective against third parties within a short period of time (such as 20 or 30 days) after B obtains the licence. O's security right in B's rights under the licence agreement is an acquisition security right and has priority over the security right of SC (see recommendation 180, alternative A, subpara. (a), and alternative B, subpara. (b), as transposed). Whether the priority of O's security right extends to proceeds of B's rights as licensee in the form of receivables, negotiable instruments and rights to payment of funds credited to

a bank account or rights to receive proceeds under an independent undertaking depends on which version of recommendation 185 a State enacts. Under alternative A, the priority of O's security right carries over to the receivables (see recommendation 185, alternative A, subpara. (a), as transposed). Under alternative B, O's security right in the receivables would have only the priority of a non-acquisition security right (see recommendation 185, alternative B, as transposed). It should be noted that O's rights pursuant to its security right are separate from and subject to different requirements than are O's rights under the licence agreement to terminate the licence agreement upon B's default in its obligations under the licence agreement.

(d) Acquisition security right in an intellectual property licence securing the purchase price of the licence held by the grantor for sale or licence

277. B grants a security right in all of its present and future movable assets (including intellectual property) to SC1, who takes the actions necessary to make the security right effective against third parties. Subsequently, B obtains a licence from O, the patent owner, for the purpose of sub-licensing the patent to third parties in the ordinary course of B's business. B obtains the money necessary to pay its licence fee by borrowing money from SC2, to whom B grants a security right in B's rights as licensee to secure B's repayment obligation. Before B obtains the licence, SC2: (a) takes the actions necessary to make its security right effective against third parties; and (b) notifies SC1 that SC2 will have an acquisition security right. SC2's security right is an acquisition security right and has priority over the security right of SC1 (see recommendation 180, alternative A, subpara. (b), and alternative B, subpara. (b), as transposed). The priority of SC2's security right does not extend to proceeds of the licence in the form of receivables, negotiable instruments and rights to payment of funds credited to a bank account, although it does extend to other types of proceeds (see recommendation 185, alternative A, subpara. (b), and alternative B, as transposed).

(e) Acquisition security right in an intellectual property licence securing the purchase price of the licence used in the grantor's business and held by the grantor for sale or licence

278. Software Company B acquires the intellectual property rights for an operating system for personal computers in a transaction pursuant to which it grants a security right in the operating system to SC to secure B's obligation to pay the purchase price. B acquires the intellectual property for the operating system so as to offer a licence of that operating system to any person who is willing to pay the licence fee and agree to comply with the terms of the licence

agreement. B will also utilize the operating system on the personal computers owned by B. Because the predominant use of the operating system by B is to hold it for sale or license to others, the rules that apply to acquisition security rights in inventory apply to SC's acquisition security right.

279. Manufacturer B acquires a patent for a piece of manufacturing equipment in a transaction pursuant to which it grants a security right in the patent to SC to secure B's obligation to pay the purchase price. B will use the patent in its own business and will not generally offer it for licence to others. However, B grants licences to use the patent to two of its subsidiaries. Because it is not the predominant use of the patent by B to hold it for sale or licence to others, the rules that apply to acquisition security rights in assets other than inventory or consumer goods apply to SC's acquisition security right.

C. Non-unitary approach

280. Section B of this chapter addresses the issue of intellectual property acquisition financing on the hypothesis that a State adopts the "unitary approach" to acquisition financing as provided in recommendations 178-186 of the *Guide*. It is based on the assumption that, if a State adopts the unitary approach to acquisition financing of tangible assets, it would also adopt the unitary approach to acquisition financing of intellectual property. To do otherwise would risk creating unnecessary confusion in relation to the creation, third-party effectiveness, priority and enforcement of acquisition security rights.

281. For the same reasons, if a State adopts the "non-unitary approach" to acquisition financing of tangible assets, it is reasonable to assume that the State would also adopt the non-unitary approach to acquisition financing of intellectual property. The non-unitary approach to acquisition financing of intellectual property rights might be reflected, for example, by contractual terms providing for a conditional transfer (which, under law relating to intellectual property, may include a conditional exclusive licence), a retention-of-title right, a financial lease right or a similar transaction with respect to an intellectual property right. Under the non-unitary approach, in addition, it is possible for an owner or for a third-party financier such as a bank to take an acquisition security right of the type available under the unitary approach.

282. Each of these acquisition financing transactions can be adapted relatively easily to the financing of intellectual property rights. Unlike the case with the unitary approach, however, it is not possible to directly transpose the recommendations governing retention-of-title rights and financial lease rights

to situations where the licensee is acquiring a non-exclusive licence. In these situations, there is no particular right that is being retained by the licensor in addition to its continuing right as owner (subject to the terms of the licence agreement). The normal remedy for the licensor in such cases is simply to revoke the licence. By contrast, a non-licensor acquisition financier (for example, a bank that finances acquisition of the licence by the licensee) would take an ordinary acquisition security right in the licensee's rights.

283. In drafting provisions to enact a non-unitary regime for acquisition financing, States would have to take into account two considerations. Firstly, in order to ensure the same functional outcomes as would result were the unitary approach to be adopted, States will have to address all the issues covered by the recommendation relating to the unitary approach as set forth in this chapter (see recommendation 247 below). Secondly, specific provisions of the law to be enacted would have to be adjusted in the same manner that, for tangible assets, recommendations 192-194 and recommendation 199 of the *Guide* (non-unitary approach) were adjusted to mirror recommendations 180 and 185 of the *Guide* (unitary approach) respectively. In other words, to achieve a non-unitary regime for acquisition financing of intellectual property rights, States would need to provide detailed rules to address issues of third-party effectiveness and the transformation of a transferor's ownership right, retention-of-title or similar right into a security right in the proceeds of the intellectual property that was transferred or title in which was retained (for a discussion of these adjustments in the case of the *Guide*'s non-unitary approach to acquisition financing, see the *Guide*, chap. IX).

Recommendation 247¹⁹

Application of acquisition security right provisions to security rights in intellectual property

The law should provide that the provisions on an acquisition security right in a tangible asset also apply to an acquisition security right in intellectual property or a licence of intellectual property. For the purpose of applying these provisions:

- (a) Intellectual property or a licence of intellectual property:
 - (i) Held by the grantor for sale or licence in the ordinary course of the grantor's business is treated as inventory; and

¹⁹If it could be included in the *Guide*, this recommendation would be placed in chapter IX, Acquisition financing, as recommendation 186 bis.

- (ii) Used or intended to be used by the grantor for personal, family or household purposes is treated as consumer goods; and
- (b) Any reference to:
- (i) Possession of the encumbered asset by the secured creditor does not apply;
 - (ii) The time of possession of the encumbered asset by the grantor refers to the time the grantor acquires the encumbered intellectual property or licence of intellectual property; and
 - (iii) The time of the delivery of the encumbered asset to the grantor refers to the time the grantor acquires the encumbered intellectual property or licence of intellectual property.

X. Law applicable to a security right in intellectual property

A. Law applicable to property matters

1. Purpose and scope

284. Generally, the conflict-of-laws rules recommended in the *Guide* deal with the law applicable to the creation, effectiveness against third parties, priority as against the rights of competing claimants and enforcement of a security right. They also determine the territorial scope of the substantive law rules recommended in the *Guide*, that is, if and when the substantive law rules of the State enacting the law recommended in the *Guide* apply (see the *Guide*, chap. X, paras. 1-9).

285. Chapter X of the *Guide* does not define the security rights to which the conflict-of-laws rules recommended in the *Guide* apply. Normally, the characterization of a right as a security right for conflict-of-laws purposes reflects the substantive secured transactions law in a State. However, the *Guide* recommends that a State that enacts the law recommended in the *Guide* following a non-unitary approach to acquisition financing apply the conflict-of-laws rules governing security rights to retention-of-title rights or financial leases (see recommendation 201). Similarly, as most of the substantive law rules of the law recommended in the *Guide* that apply to security rights in receivables apply also to outright assignments, the *Guide* recommends that such a State apply the conflict-of-laws rules governing assignments of receivables for security purposes to outright assignments of receivables (see the term “security right” in the introduction to the *Guide*, sect. B, para. 20, and recommendations 3 and 208).

286. In principle, a court or other authority will use its own law whenever it is required to characterize an issue for the purpose of selecting the appropriate conflict-of-laws rule. As the conflict-of-laws rules recommended in the *Guide* have been prepared to reflect the substantive law rules recommended in the *Guide*, a State that enacts both the substantive law and the conflict-of-laws rules recommended in the *Guide* will have no difficulty in applying either. If, however, a State does not enact the substantive law rules recommended in

the *Guide*, it may find it difficult to apply the conflict-of-laws rules recommended in the *Guide*. This may be so if a State treats creation and third-party effectiveness as one issue, while the conflict-of-laws rules recommended in the *Guide* would treat them as two separate issues and refer them to the laws of different States. It should be noted that, following the approach followed in most States, the *Guide* draws a distinction between the agreement creating a security right as a property right (referred to a specific law; see recommendations 203 and 208) and the mutual rights and obligations of the parties flowing from such an agreement as contractual rights (typically referred to the law chosen by the parties; see recommendation 216).

287. In any case, the question whether an asset (including intellectual property) may be transferred or encumbered is a preliminary issue to be addressed before the creation of a security right and is not addressed by the conflict-of-laws rules recommended in the *Guide*. Thus, to the extent that other conflict-of-laws rules refer issues of transferability of intellectual property rights, for example, to the law of the State in which the intellectual property is protected (*lex loci protectionis* or *lex protectionis*), the *Guide* does not affect them. This is so not because the law recommended in the *Guide* defers to law relating to intellectual property, but because the law recommended in the *Guide* does not address these issues. Following the same approach, the substantive law rules recommended in the *Guide* do not override statutory limitations to transferability (see recommendation 18).

288. When the conflict-of-laws rules recommended in the *Guide* refer a matter relating to security rights to the law of a particular State, the reference is to the entire body of law in effect in that State with the exception of its conflict-of-laws rules to avoid renvoi (see recommendation 221). This body of law includes not only statutory and non-statutory law (see the introduction to the *Guide*, para. 19) and the law in effect in particular territorial units of a multi-unit State (see recommendations 224-227), but also legal rules in effect in that State flowing from treaties, conventions and other international obligations. Thus, for example, if a conflict-of-laws rule refers a matter relating to security rights in intellectual property to the law of a State in which the law for that matter has been promulgated by a regional economic integration organization, the reference to the law of that State includes the rules of law promulgated by the regional economic integration organization.²⁰ The same applies to relevant rules promulgated by international organizations, such as WIPO.

²⁰For example, under article 16 of Council Regulation (EC) No. 207/2009 on the Community Trademark (see footnote 8 above), articles 17-24 apply. The law of the country where the proprietor has his seat or establishment (if inside the European Union) or the law of the seat of the Office (Spain) applies only if these articles have no specific rule.

289. It should also be noted that, whatever the applicable law may be, its application will be subject to: (a) the public policy and mandatory rules of the forum (see the *Guide*, recommendations 222); and (b) in the case of the grantor's insolvency, the impact of the application of the law of the State in which the insolvency proceedings are commenced with respect to certain insolvency-related matters (*lex fori concursus*; see recommendation 223). Finally, it should be noted that, like all the other rules recommended in the *Guide*, the conflict-of-laws rules as well do not apply in so far as they are inconsistent with national law or international agreements, to which the State is a party, relating to intellectual property, if any (see recommendation 4, subpara. (b)).

2. *The approach recommended in the Guide with respect to security rights in intangible assets*

290. Under the law recommended in the *Guide*, the law applicable to the creation, third-party effectiveness, priority and enforcement of a security right in an intangible asset is the law of the State of the grantor's location (see recommendations 208 and 218, subpara. (b)). Following the approach followed in many States, the *Guide* has asset-specific recommendations for security rights in certain types of intangible asset, such as rights to funds credited to a bank account (see recommendations 209-212), but not for security rights in intellectual property. Thus, if a State enacts the conflict-of-laws rules recommended in the *Guide*, without an asset-specific rule for intellectual property, the law of the State in which the grantor is located would apply to the creation, third-party effectiveness, priority and enforcement of a security right in intellectual property. The location of the grantor is defined as its place of business and, in the case of places of business in more than one State, its central administration, that is, the real, rather than the statutory, seat of the grantor (see recommendation 219). As already mentioned (see para. 289), recommendation 4, subparagraph (b), would also apply and, to the extent that the conflict-of-laws rules recommended in the *Guide* would be inconsistent with those of the law relating to intellectual property that applied specifically to intellectual property, the conflict-of-laws rules of the law relating to intellectual property would apply.

291. The principal advantage of an approach based on the law of the State in which the grantor is located is that it leads to the application of a single law to the creation, third-party effectiveness, priority and enforcement of a security right. So, for example, a secured creditor that wishes to obtain a security right in all present and future intangible assets (including both

intellectual property and other assets) of a grantor could obtain the security right, make it effective against third parties, ascertain its priority and have it enforced by referring to the law of a single State, even if the assets have connections with several States. In particular, both registration and searching costs with respect to security rights would in most cases be reduced, as a secured creditor would need to register and a searcher would need to search only in the State in which the grantor was located. This result would reduce transaction costs and enhance certainty and would thus potentially have a beneficial impact on the availability and the cost of credit.

292. Another particularly important advantage of an approach based on the law of the State in which the grantor is located and the definition of “location” as the place of central administration (see para. 290 above) is that that law is also the law of the State in which the main insolvency proceeding with respect to the grantor is likely to be administered (as to the meaning of a “main proceeding”, see, for example, articles 2, subpara. (b), and 16, para. 3, of the UNCITRAL Model Law on Cross-Border Insolvency).²¹ As a result, the law applicable to the creation, third party effectiveness, priority and enforcement of a security right and the law applicable to, for example, stay of individual actions, avoidance of certain transactions, treatment of secured creditors and ranking of claims are likely to be the law of one and the same State. It should be noted that, while in some cases the statutory seat may be easier to determine than the real seat, referring to the statutory seat might lead to the applicable conflict-of-laws rule being set aside for reasons of public policy or mandatory law (see the *Guide*, recommendation 222), if the statutory seat and the place of central administration of the grantor are not in the same State. This would be the case if the law of the State of the statutory seat has provisions on the priority of a security right that are inconsistent with the insolvency law of the State in which insolvency proceedings will be opened (*lex fori concursus*). For the reasons mentioned below (see paras. 305 and 306), an approach based only on the law of the State in which the grantor is located would not be appropriate for security rights in intellectual property.

293. However, if the grantor is a transferee that has taken the asset from the initial or intermediate owner located in a State other than the State of the grantor’s location, the secured creditor would have to search in the security rights registry (and possibly in the relevant intellectual property registry, if any) of any such other State. It should be noted that, in such a case, if the initial or intermediate owner had itself granted a security right that was subject to the law of the location of the initial or intermediate owner, under the law recommended in the *Guide*, the applicable law would be the law of the State

²¹United Nations publication, Sales No. E.99.V.3.

in which the grantor was located at the time a priority conflict arose (see recommendations 208 and 220, subpara. (b)). Under the law recommended in the *Guide*, except in certain prescribed situations, each transferee of an encumbered asset would take the asset subject to a pre-existing security right. As a result, each transferee would take the asset subject to a security right created by a prior owner (see recommendations 79-82).

294. It should be noted that where the grantor moves from one State to another State that has enacted the law recommended in the *Guide*, additional rules apply, if the law of the State of the grantor's new location is the applicable law. According to these rules, if the grantor moves to a State that has enacted the law recommended in the *Guide*, a security right remains effective against third parties for a short period of time without any action on the part of the secured creditor and thereafter only if the third-party effectiveness requirements of the State of the grantor's new location are met (see the *Guide*, recommendation 45).

295. For example, intellectual property owner A, located in State X, creates a security right in favour of secured creditor SC1 in a copyright protected in State Y, moves to State Y, which has enacted the law recommended in the *Guide* and creates another security in the copyright in favour of secured creditor SC2 in State Y. If State Y has enacted a rule referring priority as between secured creditors to the law of the State of the grantor's location (see the *Guide*, recommendation 208) and each security right has been made effective against third parties under the law of State under which it was created, the security right of SC1 has priority over the security right of SC2 for a short period of time without any action on the part of SC1 and thereafter only if SC1 meets the third-party effectiveness requirements of State Y. This result is the result of a rule based on recommendation 45 and not of a conflict-of-laws rule. If A, instead of moving to State Y, transfers the copyright to transferee B in State Y, whether transferee B obtains the copyright subject to the security right of SC1 will be determined in accordance with the law of the State of the grantor's location. Similarly, whether secured creditor SC2 takes its security right subject to the security right of SC1 will be determined in accordance with the law of the State of the grantor's location.

296. It should also be noted that, under the law recommended in the *Guide*, the relevant time for determining the location of the grantor for creation issues is the time of the putative creation of a security right and for third-party effectiveness and for priority issues it is the time when the issue arises (see recommendation 220). As a result, under the approach based on the law of the State of the grantor's location rule recommended in the *Guide* and to the extent that rule would apply to security rights in intellectual property assets, the creation of the security right of SC1 would be subject to the law

of State X and the creation of the security right of SC2 would be subject to the law of State Y. Whether transferee B and its secured creditor SC2 would take the intellectual property asset subject to the security right of SC1 would, after a short period of time (see the *Guide*, recommendation 45), be governed by the law of State Y.

3. *The law of the State of protection (lex protectionis)*

297. Although international conventions designed to protect intellectual property do not expressly address the law applicable to issues arising with respect to security rights in intellectual property, they generally adopt the principle of territoriality. Thus, in States parties to these conventions, the law applicable to ownership and issues of protection of intellectual property rights (such as the comparative rights of an intellectual property owner in one State as against a licensee or an infringer in another State) is the *lex protectionis*. It should be noted that, with respect to types of intellectual property that are subject to registration in a national, regional or international intellectual property registry (for example, patents and trademarks), the *lex protectionis* is the law of the State (including the rules promulgated by regional or international organizations) under whose authority the registry is maintained.

298. The view is expressed²² that the principle of national treatment embodied in international conventions protecting intellectual property implicitly imposes a universal rule in favour of the *lex protectionis* for determining the law applicable not only to ownership of intellectual property but also to issues arising with respect to security rights in intellectual property. In accordance with that view, it is asserted that provisions such as article 2, paragraph 1, of the Paris Convention for the Protection of Industrial Property (1883),²³ article 5, paragraph 2, of the Berne Convention for the Protection of Literary and Artistic Works (1886)²⁴ and article 3, paragraph 1, of the TRIPS Agreement lead to the conclusion that the appropriate connecting factor is the place of protection of the relevant intellectual property right.²⁵ In other words, according to this view, States parties to any of these international conventions are required to apply the *lex protectionis* to issues arising with respect to security rights in intellectual property.

²²See the report of Working Group VI (Security Interests) on the work of its sixteenth session (A/CN.9/685, para. 90).

²³Available from www.wipo.int/treaties/en/ip/paris/trtdocs_wo020.html.

²⁴Available from www.wipo.int/treaties/en/ip/berne/trtdocs_wo001.html.

²⁵These instruments may contain certain exceptions that are not considered relevant to this discussion.

299. As a result of this view, in order for a secured creditor to be able to obtain an effective and enforceable security right in an intellectual property right in a State in which the intellectual property right exists, the secured creditor would have to fulfil the requirements of that State. So, the principal advantage of an approach based on the *lex protectionis* is that, in recognition of the principle of territoriality adopted in international conventions for the protection of intellectual property, its application would result in the same law applying to both security rights and ownership rights in intellectual property. It should be noted that, under this approach, the *lex protectionis* determines the property right aspects of a security right. It does not necessarily apply to purely contractual matters between the grantor and secured creditor that may be subject to the law governing a contract (*lex contractus*; see section B of this chapter below).

300. However, there are also inefficiencies to an approach based on the *lex protectionis* as the law applicable to security rights in intellectual property. In many transactions, registration in registries located in several States would have to take place. This will be the case, in particular with: (a) transactions in which a portfolio of intellectual property rights protected under the laws of various States is used as security for credit, (b) transactions in which the encumbered assets are not limited to intellectual property that is used and protected under the law of a single State and (c) transactions in which all assets of a grantor are encumbered. As discussed further below, such a result is likely to add to the cost and complexity of an intellectual property financing transaction by increasing registration and search costs. In addition, if the grantor is not located in the State under whose law the encumbered intellectual property is protected and an insolvency proceeding with respect to the grantor is commenced in the State in which it is located, referring issues relating to a security right to the law of the protecting State might lead to the conflict-of-laws rule being set aside as contrary to public policy or mandatory law considerations of the *lex fori concursus* (see the *Guide*, recommendation 222). Thus, providing for a *lex protectionis* approach may unnecessarily deprive secured creditors of the choice of following the law of the State of the grantor's location or registering in the general security rights registry and thus saving transaction costs.

4. Other approaches

301. The view mentioned above (see paras. 297 and 298), attributing an extensive effect to international intellectual property conventions with respect to the determination of the law applicable to issues relating to security rights

in intellectual property, is not universally accepted. In addition, there is very little precedent on the application of the *lex protectionis* to such issues. Even assuming that these international conventions could impose conflict-of-laws rules, it would still be questionable whether the scope of application of those rules would cover all property effects contemplated by the *Supplement*, that is, the creation, effectiveness against third parties, priority as against the rights of competing claimants and enforcement of a security right in intellectual property.

302. Accordingly, even if one accepts the extensive effect of international intellectual property conventions described above (see paras. 297 and 298), it would still be necessary or useful for States to adopt conflict-of-laws rules applicable to issues arising with respect to security rights in intellectual property. Such rules would, at the very least, perform a gap-filling function with regard to any possible conflict-of-laws consequences resulting from existing international intellectual property conventions.

303. In view of the above-mentioned considerations, to combine consistency with the law applicable to ownership rights and the benefits of the application of a single law for security rights issues, the *lex protectionis* approach could be combined with the law of the grantor's location approach. As long as there was clarity as to which law was applicable to each issue, some issues could be referred to the law of the grantor's location, while other issues could be referred to the *lex protectionis*. Paragraphs 304-316 below provide examples of such hybrid approaches.

304. For example, the approaches based on the law of the State of the grantor's location and the *lex protectionis* could be combined in the following way. The law of the State of the grantor's location would apply in principle to the creation, third-party effectiveness, priority and enforcement of a security right in intellectual property. However, the third-party effectiveness and priority of a security right as against the rights of an outright transferee or licensee of intellectual property would be governed by the *lex protectionis*. This rule would apply irrespective of whether or not the *lex protectionis* provided for registration of a security right in intellectual property in an intellectual property registry. Under this first hybrid approach, a secured creditor would need to establish its right under the *lex protectionis* only in instances where a competition with an outright transferee or licensee was a concern. In the typical case where the insolvency of the grantor is the main concern (because the grantor cannot pay all its creditors), it would be sufficient for the secured creditor to rely on the law of the State in which the grantor is located, as would be the case for other types of intangible asset (such as receivables).

305. In States that follow such an approach with respect to security rights in intellectual property, it results in lowering transaction costs mainly for two reasons. Firstly, a secured creditor may always register under the *lex protectionis* and in the relevant intellectual property registry. Secondly, where the main concerns of a secured creditor are the insolvency of the grantor and a dispute with another secured creditor or a judgement creditor, the secured creditor may only need to meet the third-party effectiveness requirements of the State in which the grantor is located (for example, to register a notice only in the general security rights registry in the State in which the grantor is located). In such a case, a secured creditor may be prepared to take the risk of not registering under the *lex protectionis* in the intellectual property registry of the State in which the intellectual property is protected, which would protect the secured creditor against the risk of fraud by the grantor, as it would not lend if it feared fraud.

306. However, this first “hybrid” approach also has disadvantages. If the secured creditor needs to ensure its priority as against all competing claimants, it would have to meet the requirements of the law that typically governs ownership in intellectual property, that is, the *lex loci protectionis*. This would be the case in particular with respect to priority as against: (a) a transferee of intellectual property; (b) an exclusive licensee of intellectual property where an exclusive licence is treated as a transfer; and (c) a secured creditor that under law relating to intellectual property is treated as an owner or may exercise the rights of an owner (see paras. 30, 87, 88 and 222 above). Such a result could have a negative impact on the availability and the cost of credit. In addition, if the law of the State in which the grantor is located is not the law of the protecting State, the security right may not be effective and enforceable under the law of the protecting State, unless that State has adopted a conflict-of-laws rule referring to the grantor’s location. Moreover, as already mentioned (see para. 290), even in States in which a security right is subject to the law of the State in which the grantor is located, the *lex protectionis* may be applicable by virtue of recommendation 4, subparagraph (b). It should also be noted that, in particular if a security right may be registered in an intellectual property registry, the applicable law of the State of the grantor’s location may be set aside as fundamentally contrary to the public policy and the internationally mandatory rules of the forum (see the *Guide*, recommendation 222).

307. Other combinations of the two approaches might also be possible. Under a second hybrid approach, issues arising with respect to a security right in intellectual property that is subject to registration in an intellectual property registry (whether national, regional or international) may be referred to the law of the State under whose authority the registry is maintained (this approach is followed in the *Guide* with respect to security rights in tangible

assets that are subject to specialized registration; see recommendation 205). An exception could be made for issues relating to enforcement that, for reasons of cost- and time-efficiency, could be referred to the law of the State in which the grantor was located. At the same time, issues arising with respect to a security right in intellectual property that is not subject to such registration may be referred to the law of the State in which the grantor is located. Again, an exception could be made for the third-party effectiveness and priority of a security right in intellectual property that could be referred to the *lex protectionis*.

308. The main advantage of this approach is that it takes into account the existence of national, regional or international intellectual property registries and the potential reluctance of States that have such registries to adopt a conflict-of-laws rule that would disregard the existence of those registries. To the extent that legislation of regional or international organizations provides for registration of rights in intellectual property, member States of these organizations would find it difficult to adopt a rule that runs counter to regional or international legislation. For example, member States of the European Union may not be in a position to adopt a rule that failed to take into account that, under article 16 of the Council Regulation (EC) No. 207/2009 on the Community Trademark, community trademarks are subject primarily to articles 17-24 of the Regulation and only if these provisions have no specific rule will the law of the State where the proprietor has his seat or establishment (if inside the European Union) or the law of the seat of the Office (Spain) apply.

309. This second hybrid approach also has disadvantages. To the extent that rights in some types of intellectual property are capable of being registered in an intellectual property registry (for example, patents and trademarks), while other types are not (copyrights), it results in a different conflict-of-laws treatment of security rights in the various type of intellectual property. In addition, to the extent that this approach is based on the *lex protectionis*, it draws unnecessary distinctions, as the *lex protectionis* should apply to all types of intellectual property whether or not the *lex protectionis* provides for the registration of certain intellectual property rights. Moreover, to the extent that the second part of such an approach is identical with the first hybrid approach discussed above, but with a more limited scope of application, it would have all of its advantages and disadvantages (para. 306 above). Furthermore, such an approach may add cost and complexity to outright transfers of intellectual property rights that are not subject to such registration under the *lex protectionis*. This is so because an outright transferee of such an intellectual property right would have to investigate the law of the State of the grantor's location to ensure that the transfer was not subject to a prior security right.

310. Moreover, referring priority and enforcement to two different laws may add complexity in the determination of the applicable law. For example: (a) an issue may be characterized in a State as an issue of priority and in another State as an issue of enforcement; and (b) priority may affect enforcement issues such as who has the right to take over enforcement, distribution of proceeds from a sale, rights acquired by a transferee in an extrajudicial sale. To avoid these problems, with respect to security rights in intangibles, the *Guide* recommends as the law applicable to enforcement the law applicable to priority (see recommendation 218, subpara. (b)). Finally, this approach would require an investigation of the *lex protectionis* of all States concerned to ascertain whether those States permit registration of a security right in intellectual property in an intellectual property registry. For example, the law applicable to a security right in copyright would depend on whether the copyright may be registered in a copyright registry or not.

311. Another possible combination of the two approaches (the third hybrid approach) might be to refer the creation and enforcement of a security right to the law of the State of the grantor's location, unless the parties agreed to refer the law of the protecting State. Under such an approach, the third-party effectiveness and priority of a security right could be referred to the law of the State of the grantor's location, with the exception of the third-party effectiveness and priority of a security right as against the rights of a transferee, licensee or another secured creditor. This approach would: (a) allow a limited extent of party autonomy with respect to creation and enforcement of a security right; (b) refer third-party effectiveness and priority of a security right mainly to the law of the protecting State; and (c) refer the third-party effectiveness and priority of a security right as against an insolvency representative to the law of the State of the grantor's location.

312. This approach too would have disadvantages. To the extent that creation and third-party effectiveness are referred to two different laws, only States that treat these two issues as distinct issues (in other words, follow the approach recommended in the *Guide*) could apply such a rule. Thus, such a rule would have limited application until wide adoption of a law that would be consistent with the law recommended in the *Guide*. In addition, referring any issue other than the mutual rights and obligations of the parties to party autonomy just with respect to security rights in intellectual property would be a departure from the approach followed in the *Guide* (see recommendation 10, which does not permit party autonomy for any applicable law issue other than the mutual rights and obligations of the parties) and from conflict-of-laws principles of many States that do not permit party autonomy in the determination of the law applicable to property rights issues.

313. Moreover, as already mentioned (see para. 308), referring third-party effectiveness and priority to two different laws depending on the identity of the competing claimant might result in all secured creditors seeking to meet the third-party effectiveness requirements of both laws in order to ensure priority against all possible competing claimants, unless States adopt the substantive law recommendations of the *Guide*. Furthermore, unless States adopt the substantive law recommendations of the *Guide*, referring priority and enforcement to two different laws might result in inconsistencies, as one law would apply to priority in one State and another law could apply to priority in another State in which a priority issue is rather characterized as an enforcement issue. It should also be noted that referring priority and enforcement to two different laws might create circular priority problems.

314. Yet another combination of the law of the grantor's location and the *lex protectionis* might be the following: the *lex protectionis* could apply to the creation, third-party effectiveness and priority of a security right in intellectual property. However, a secured creditor could also effectively create a security right under the law of the State of the grantor's location. In addition, a secured creditor could rely on that law to achieve the effectiveness of a security right as against judgement creditors and the grantor's insolvency representative. Moreover, the law of the State of the grantor's location could govern the enforcement of such a security right. This is the recommended approach (see recommendation 248 below).

315. This hybrid approach would increase the advantages of a hybrid approach and decrease its disadvantages. The importance of the *lex protectionis* would be properly recognized. At the same time, the possibility for a secured creditor to create and enforce a security right under a single law would result in significant practical benefits, in particular for transactions involving a portfolio of intellectual property protected in different States or a portfolio of various tangible and intangible assets, including intellectual property, located (or protected) in various States. The same benefits would result from the possibility for a secured creditor to make a security right effective as against judgement creditors and the grantor's insolvency representative under a single law. Problems that may arise from the fact that the creation and third-party effectiveness as against certain competing claimants would be referred to the laws of different States could be avoided if a State adopted the substantive law recommendations of the *Guide* or described the issues covered in a neutral way that would be consistent with its own substantive law. Problems arising from the fact that priority and enforcement would be referred to the laws of different States could also be avoided through the use in the legislative text enacting this approach of neutral language consistent with the substantive law of the enacting State. In addition, the fact that a secured creditor would also be permitted to make

its security right effective against judgement creditors and the grantor's insolvency representative under the law of the grantor's location would not give rise to circular priority problems because the *lex protectionis* would recognize such effectiveness against those potential competing claimants. Moreover, the *lex protectionis* would always apply to priority disputes with other competing claimants (for example, another secured creditor or a transferee).

316. Furthermore, the advantage of possibly referring creation to the law of a single State would outweigh any disadvantage inherent in allowing the parties a choice between the *lex protectionis* and the law of the State of the grantor's location with respect to that matter. It should also be noted that such a rule would not affect third parties as the creation of a security right relates only to its effectiveness between the parties to the security agreement. Finally, it should be noted that, under the recommended approach, if a security right encumbers intellectual property protected in States A, B and C, the security right would be effective in all such States against the grantor's insolvency representative if such effectiveness has been achieved under the law of the State of the grantor's location. However, if the secured creditor has made its security right effective only under the law of State A (and State A is not the State of the grantor's location), its security right will not be effective in States B and C against the grantor's insolvency representative.

317. The advantages and disadvantages of the approaches mentioned above (see paras. 290-316) may be illustrated with the examples discussed below (see paras. 318-337), dealing separately with creation, third-party effectiveness, priority and enforcement issues.

5. Examples for a comparative analysis of the various approaches

(a) Creation issues

318. Intellectual property owner A, located in State X, owns a portfolio of copyrights in and protected under the laws of State X (in which security rights in copyright are not capable of being registered in an intellectual property registry), and a portfolio of patents and trademarks in and protected under the laws of State Y. Pursuant to a single security agreement, A creates a security right in both portfolios in favour of SC1 located in State Y. A then creates a security right in the same patent and trademark portfolio in favour of SC2 also located in State Y.

319. Under the *lex protectionis* approach A and SC1 would have to meet the creation requirements of State X with respect to the copyright portfolio protected under the law of State X and the requirements of State Y with respect to patent and trademark portfolio protected under the law of State Y. If they fail to do so, the security agreement will achieve only part of its intended purpose; for example, it may create a security right under the law of State X, but fail to create a security right under the law of State Y. Under the first hybrid approach that combines the law of the State of the grantor's location and the *lex protectionis* (see para. 304 above), A and SC1 would need to meet the requirements of State X for the creation of its security right in both the copyright portfolio and the patent and trademark portfolio (that is, for the security right to be effective between grantor A and secured creditor SC1).

320. Under the second hybrid approach, which distinguishes between security rights in intellectual property rights that may be registered in an intellectual property registry and those that may not be registered in such a registry (see para. 309 above), creation issues with respect to the security right in the copyright portfolio would still be referred to the law of State X (as the State of the grantor's location, although with respect to the copyright portfolio it is also the protecting State); and creation issues with respect to the security right in the patent and trademark portfolio would be referred to the law of State Y (assuming that rights in patents and trademarks may be registered in specialized registries in that State).

321. Under the third hybrid approach, which permits limited party autonomy with respect to the law applicable to the creation of a security right in intellectual property (see para. 311 above), the law of State X would apply, unless the parties chose in the security agreement the law of State Y. To the extent that both States distinguish between creation and third-party effectiveness and attribute to creation effects only as between the parties, this approach would not create problems. Otherwise, this approach could result in uncertainty as to the law applicable to creation issues. It should be noted that, if creation is distinct from third-party effectiveness and is referred by A and SC1 to the law of State X and by A and SC2 to the law of State Y, no major problem would arise as long as the priority conflict between SC1 and SC2 is referred to one law, in this example, to the law of State Y.

322. Where A and SC1 have chosen the law of the State of the grantor's location (State X) and A and SC2 have chosen the law of the State in which the intellectual property is protected (State Y), while the only difference between the laws of States X and Y with respect to the creation of a security right lies in the fact that, for example, State X, which has not enacted the recommendations of the *Guide*, requires more formalities in a security

agreement than does State Y, which has enacted the rules recommended in the *Guide*, this difficulty can be overcome by preparing the security agreement so that it satisfies the requirements of the more stringent law (although this could result in additional costs for the transaction). However, when States X and Y have inconsistent requirements with respect to formalities, this approach will not suffice to overcome this problem. Similarly, where the security agreement contemplates multiple present and future intellectual property rights as encumbered assets, difficulties may arise that could not be overcome. This is so in particular when a State has enacted the rules recommended in the *Guide* (allowing a single security agreement to create security rights in multiple present and future assets), while another State does not allow a security agreement to create a security right in assets not yet in existence or not yet owned by the grantor, or does not allow multiple assets to be encumbered in one and the same agreement.

323. Under the recommended approach (see recommendation 248 below), SC1 could create its security right in the copyright portfolio under the law of State X and in the patent and trademark portfolio under the law of State Y (in both cases, the protecting State). However, SC1 would have the option of also effectively creating its security right in the portfolio of patents, trademarks and copyrights under the law of State X (law of the State of the grantor's location).

(b) *Third-party effectiveness issues*

324. In the same example (see para. 318 above), in order to make its security right effective against third parties, under the *lex protectionis* approach, SC1 would need to meet the third-party effectiveness requirements of State X to make its security right in the copyright portfolio effective against third parties and the requirements of State Y to make its security right in the patent and trademark portfolio effective against third parties. This would possibly necessitate the registration of multiple notices with respect to the security right in the relevant registries of those States. In addition, potential creditors would have to search in all those registries. This means that potential creditors of A would need search the relevant registry in State X to find the security right in favour of SC1 in the copyright portfolio and the relevant registry in State Y to find the security right in favour of SC1 and SC2 in the patent and trademark portfolio. This situation could be further complicated by the fact that some of those States might utilize the general security rights registry for such notices, other States might provide the option of utilizing an intellectual property registry and still other States might utilize an intellectual property registry, if registration in such a registry is mandatory under law relating to

intellectual property (see recommendation 4, subpara. (b)). This disadvantage would be alleviated if there were an international registry in which notices of security rights, the third-party effectiveness of which was governed by the law of different States, could be registered.

325. However, under the first hybrid approach, it would be sufficient for SC1 to meet the third-party effectiveness requirements of State X. Any potential creditors of A would need to search only in the relevant registry in State X to find any security right created by A in its copyright portfolio in State X or in its patent and trademark portfolio in State Y (although a transferee or licensee need only search in the patent and trademark registry in State Y, as a conflict of priority with a transferee or licensee is under the first hybrid approach governed by the *lex protectionis*). Under the second hybrid approach, SC1 would need to meet the third-party effectiveness requirements of State X with respect to the security right in the copyright portfolio and the third-party effectiveness of State Y with respect to the security right in the patent and trademark portfolio. Under the third hybrid approach, SC1 and SC2 would have to meet the third-party effectiveness requirements of both States X and Y to ensure the effectiveness of their security rights against all possible competing claimants other than judgement creditors and the grantor's insolvency representative (with respect to which the law of State X would apply). Under the recommended approach (see recommendation 248 below), SC1 should generally meet the third-party effectiveness requirements of the law of State X for the copyright portfolio and the law of State Y for the patent and trademark portfolio (in both cases, the protecting State). However, to protect its right as against judgement creditors and the grantor's insolvency representative, SC1 would have the option of meeting only the requirements of the law of State X (the law of the State of the grantor's location).

(c) *Priority issues*

326. In the same example (see para. 318 above), if A creates another security right in its patent and trademark portfolios protected in State Y in favour of SC2, there will be a priority conflict between the security rights of SC1 and SC2 in the patents and trademarks protected in State Y. Under the *lex protectionis* approach, this priority conflict would be governed by the laws of State Y. The law of State Y would govern this priority conflict also under the approach referring priority of a security right in intellectual property that may be registered in an intellectual property registry to the law of the State under whose authority the registry is maintained.

327. Another example will illustrate how the *lex protectionis* approach will apply in the case of multiple transfers in a chain of title, where the transferor and each of the transferees create security rights. A, located in State X, owns a patent in State X. Owner A grants a security right in a patent to secured creditor SC1. A then transfers the patent to B, located in State Y, who creates a security right in favour of SC2. Whether transferee B obtains the patent subject to the security right of SC1 will be determined in accordance with the *lex protectionis*, that is, the law of State X, which happens to be also the law of the grantor's location. Whether secured creditor SC2 takes its security right in the patent from transferee B subject to the security right of SC1 will also be determined in accordance with the *lex protectionis* (normally, under the *nemo dat* principle, SC2 will acquire no more rights than B had).

328. Under the first hybrid approach, this priority conflict would be governed by the law of State X, in which the grantor is located. Under the second hybrid approach, the law of State Y would apply to the security right in the patent and trademark portfolio (registered in State Y) and the law of State X (the law of the State in which the grantor is located) would apply to the priority of the security right in the copyright portfolio. To modify the example slightly, if the copyright portfolio also includes copyrights protected in various States (in addition to State X) in which registration of a copyright and a security right in a copyright may be possible, under the second hybrid approach, the law of all those various States would apply to the priority of a security right in these copyrights.

329. Under the third hybrid approach, circular priority problems could arise. If grantor A became insolvent and insolvency proceedings were instituted in State X, under this approach, priority as between SC1 and SC2 would be governed by the law of State Y, while priority as between the insolvency representative (on one hand) and SC1 and SC2 (on the other hand) would be governed by the law of State X. If: (a) under the law of State X, the insolvency representative has priority over SC1 but not over SC2 and (b) under the law of State Y, SC1 has priority over SC2, then: the right of SC1 has priority over the right of SC2 (under the law of State Y), the right of insolvency representative has priority over the right of SC1 (under the law of State X), and the right of SC2 has priority over the right of the insolvency representative (under the law of State X). The result would be circular priority, as the right of SC1 prevails over the right of SC2 whose right prevails over the right of the insolvency representative whose right prevails over the right of SC1.

330. Under the recommended approach (see recommendation 248 below), the law of State Y (the protecting State) would govern the priority between SC1 and SC2. Circular priority problems would not arise under the

recommended approach because the rights of SC1 and SC2 will be effective against the insolvency representative in State Y (whose law will apply to a dispute between SC1 and SC2) whether such effectiveness has been achieved in State X or State Y. This is so under the recommended approach because a secured creditor has the option to make its right effective against the insolvency representative either under the law of the State of the grantor's location (State X) or the law of the protecting State (State Y). If the secured creditor opts for the law of the State of the grantor's location, its security right will also become effective against the insolvency representative in the protecting State.

331. It should be noted, however, that circular priority problems may arise even within one and the same State. However, in the situation described in the preceding paragraph, the circular priority problem arises under the third hybrid approach as a result of referring third-party effectiveness and priority to two different laws depending on the identity of the competing claimant. It should also be noted that, at the substantive law level, there are solutions to such circular priority problems. In the example mentioned, one solution could be to provide that the right of SC2 would have priority if under insolvency law the right of SC1 is not recognized as effective against third parties if a notice of it was not registered in State X. Another way to resolve this problem may be the following: the right of SC2 would have priority over the right of the insolvency representative, but SC2 would have to turn over the proceeds to SC1, because, as between SC1 and SC2, SC1 would have priority.

(d) Enforcement issues

332. In the same example (see para. 318 above), if A does business in States X, Y and Z and uses a particular patent under the law of each of those States, those patent rights may well have greater value taken together than they do separately because they operate collectively. Thus, if A creates a security right in those patents, SC1 would likely prefer to dispose of them together upon A's default because such a disposition would likely yield greater proceeds (thus also benefitting A). Yet this is likely to be difficult or impossible if States X, Y and Z have different rules for disposition of encumbered intellectual property rights. If State X allows only a judicial disposition of an encumbered asset, while States Y and Z allow a non-judicial disposition, disposition of the patent rights in a single transaction might be impossible. Even if all of the relevant States allow non-judicial disposition, the differences in required procedures may make a disposition of the rights in a single transaction inefficient at best.

333. Moreover, enforcement of a security right is not a single event; rather it is a series of actions. So, upon A's default, SC1, located in State Y, may notify A, located in State X, that it will enforce its security right in its patent rights protected under the laws of States X, Y and Z. SC1 may then advertise the disposition of the patent right in States X, Y and Z; indeed, it may advertise the disposition worldwide by means of the Internet. SC1 may then identify a buyer located in State Z, who buys the encumbered asset pursuant to a contract governed by the laws of State X.

334. Under an approach based on the *lex protectionis* or the law of the State under whose authority the registry is maintained, SC1 would need to enforce its security right in the patent protected in State X in accordance with the law of State X, its security right in the patent protected in State Y in accordance with the law of State Y and its security right in the patent protected in State Z in accordance with the law of State Z. Under the first hybrid approach, enforcement of the security right in the patent would be governed by the law of the State in which grantor A is located. It should be noted that, no matter which approach is followed, if SC1 sells the encumbered patents, in order to be fully protected, the transferee will have to register its rights in the patent registry of each State in which the relevant patent is registered and protected, that is, States X, Y and Z.

335. It should also be noted that, where A, located in State X, creates a security right in a patent registered in the national patent office in State Y and then A becomes insolvent, the law applicable to the creation, third-party effectiveness, priority and enforcement of the security right will be the law of State X or Y, depending on whether an approach based on the law of the grantor's location or an approach based on the *lex protectionis* is followed in the forum. Under the law recommended in the *Guide*, the application of any of these laws is subject to the *lex fori concursus* with respect to issues such as avoidance, treatment of secured creditors, ranking of claims or distribution of proceeds (see recommendation 223). Where the insolvency proceeding is opened in State X in which the grantor is located, the *lex fori concursus* and the law of the grantor's location will be the law of one and the same jurisdiction. Where the insolvency proceeding is opened in another State, where, for example, the grantor has assets, that may not be the case.

336. Under the third hybrid approach, problems could arise if enforcement and priority are referred to different laws. For example, if enforcement is referred by A and SC1 to the law of State X (the law of the State of the grantor's location) and by A and SC2 to the law of State Y (the protecting State) and both A and B initiate enforcement proceedings,

one law might apply to the remedies exercised by A and another law might apply to the remedies exercised by B. For instance, having the laws of States X and Y apply to procedural enforcement issues (for example, time periods for notices, or which of the two enforcing secured creditors had priority and could take over enforcement, or else distribution of proceeds) could result in uncertainty and inconsistencies. This would be particularly problematic if the law of State X allowed an extra-judicial sale of the encumbered asset while the law of State Y prohibited it (and which one of the two secured creditors sold the asset may have an impact on whether the transferees acquired the encumbered asset free or subject to the security right).

337. Under the recommended approach (see recommendation 248 below), the law of State X (the State of the grantor's location) would govern enforcement of the security right in both the copyright and the patent and trademark portfolios. This approach would provide significant practical benefits. As already mentioned, any problems with referring priority to a different law could be avoided through the use in the legislative text enacting the recommendation of neutral language consistent with the substantive law of the enacting State.

B. Law applicable to contractual matters

338. Under the law recommended in the *Guide*, the law applicable to the mutual rights and obligations of the grantor and the secured creditor arising from their security agreement (the contractual aspects of the security agreement) is left to party autonomy. In the absence of a choice of law by the parties, the law applicable to these matters is the law governing the security agreement as determined by the conflict-of-laws rules generally applicable to contractual obligations (see the *Guide*, chap. X, para. 61, and recommendation 216).

339. In view of the wide acceptability of the application of the principle of party autonomy to contractual matters,²⁶ the same rule should apply to the mutual rights and obligations of the grantor and the secured creditor in the case of a security right in intellectual property.

²⁶ See www.hcch.net/upload/wop/genaff_concl09e.pdf on the development of a future instrument on the choice of law in international contracts by the Hague Conference on Private International Law.

Recommendation 248²⁷

Law applicable to a security right in intellectual property

The law should provide that:

(a) The law applicable to the creation, effectiveness against third parties and priority of a security right in intellectual property is the law of the State in which the intellectual property is protected;

(b) A security right in intellectual property may also be created under the law of the State in which the grantor is located and may also be made effective under that law against third parties other than another secured creditor, a transferee or a licensee; and

(c) The law applicable to the enforcement of a security right in intellectual property is the law of the State in which the grantor is located.

²⁷If it could be included in the *Guide*, this recommendation would be placed in chapter X, Conflict of laws, as recommendation 214 bis.

XI. Transition

340. Under the law recommended in the *Guide*, the law should set out the date as of which it will come into force (the “effective date”) and specify the extent to which, after the effective date, the new law applies to security rights that existed before the effective date (see the *Guide*, chap. XI, paras. 1-3, and recommendation 228).

341. The different approaches to establishing an effective date as set out in the *Guide* offer States different possibilities for doing so. Whichever is selected, however, will provide a clear mechanism for determining when the law or its various parts will come into force (see the *Guide*, chap. XI, paras. 4-6). Neither the *Guide* nor the *Supplement* recommends that the effective date of the provisions of the law relating to security rights in intellectual property be different from the effective date of other provisions of the law. Thus, the approaches discussed in chapter XI of the *Guide* can be applied without modification to determine the date at which the provisions with respect to security rights in intellectual property will come into force. The only additional considerations are the following: (a) the entire law recommended in the *Guide* must come into force either at the time or before the provisions relating to security rights in intellectual property come into force; and (b) the provisions with respect to intellectual property rights must come into force as a whole. In other words, States may defer the coming into force of the provisions relating to security rights in intellectual property until a date after the general law has come into force, but when they decide to proclaim in force the provisions relating to security rights in intellectual property, they must do so in a manner that ensures that all these provisions come into force at the same time.

342. The *Guide* also contains recommendations relating to the protection of rights acquired before the effective date of the new law. The general principle is that the new law applies even to security rights that exist at the effective date. Consequently, if registration of a notice of a security right in the general security rights registry or in the relevant intellectual property registry becomes newly possible, States will have to provide for a grace period to enable notices of these security rights to be registered (thereby protecting both third-party effectiveness and priority as it existed under prior law). This principle and its implications are elaborated upon in the *Guide* (see the *Guide*, chap. XI, paras. 20-26).

343. A particular transition issue arises in relation to enforcement, that is, whether enforcement proceedings that had commenced prior to the effective date of the new law would have to be abandoned and recommenced under the new law. To avoid this result, the law recommended in the *Guide* provides that, once enforcement proceedings have been commenced in a court or binding arbitral tribunal, they may continue under prior law. However, it is possible for the enforcing secured creditor to abandon proceedings under prior law and recommence enforcement under the new law, in particular if the new law recommended in the *Guide* provides secured creditors with remedies not available under prior law (see the *Guide*, chap. XI, paras. 27-33). This principle should be equally applicable to enforcement proceedings commenced in respect of security rights in intellectual property.

344. Because the recommendations of the *Guide* relating to security rights in intellectual property offer financing and transactional opportunities that have not heretofore existed in many States, it might be thought that special provisions to govern transition to the new law would be required. The above review suggests, however, that the basic transition principles set out in the law recommended in the *Guide* can be applied without modification to the regime of security rights in intellectual property as recommended in the *Supplement*. No additional recommendations are needed for this purpose.

XII. The impact of insolvency of a licensor or licensee of intellectual property on a security right in that party's rights under a licence agreement

A. General

345. A licensor or a licensee of intellectual property under a licence agreement may create a security right in its rights under the licence agreement. If the grantor is the licensor, typically its secured creditor will have a security right in the licensor's right to receive royalties from the licensee as well as the right to enforce non monetary terms of the licence agreement and the right to terminate the licence agreement upon breach. If the licensee is the grantor, typically its secured creditor will have a security right in the licensee's right to use or exploit the licensed intellectual property subject to the terms of the licence agreement, but not a security right in the intellectual property itself. The secured creditor may then take the steps necessary to make that security right effective against third parties (see the *Guide*, recommendation 29).

346. Insolvency law, subject to avoidance actions, will typically respect the effectiveness of such a security right (see the *UNCITRAL Legislative Guide on Insolvency Law*,²⁸ recommendation 88). Similarly, insolvency law, subject to any limited and clearly stated exceptions, will respect the priority of a security right that is effective against third parties (see the *Guide on Secured Transactions*, recommendations 238 and 239). However, if the licensor or the licensee becomes subject to insolvency proceedings, there may be an effect on the rights of the parties to the licence agreement that will have an impact on a security right granted by the licensor or the licensee. In the case of a chain of licence and sub-licence agreements, the insolvency of any party in the chain will have an impact on several other parties in the chain and their secured creditors. For example, an insolvency of a party in the middle of the chain will affect the licence of subsequent sub-licensees and sub-licensors, but will not have any legal

²⁸United Nations publication, Sales No. E.05.V.10, available at www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf.

effect on previous ones. The terms of a licence agreement may provide for different results (for example, automatic termination of all licences upon the insolvency of any licensee up or down in the chain from the insolvent licensee), but these results will be subject to limitations under insolvency law (for example, rendering unenforceable automatic termination clauses).

347. Outside of insolvency, there may be statutory or contractual limitations on the ability of the licensor and the licensee to grant and enforce a security right in a right to the payment of royalties. Secured transactions law will typically not affect statutory limitations, other than mainly those relating to a future receivable, or a receivable assigned in bulk or in part on the sole ground that it is a future receivable, or a receivable assigned in bulk or in part (see the *Guide*, recommendation 23). Secured transactions law may affect contractual limitations (see the *Guide*, recommendations 18, 24 and 25). What effect, if any, an insolvency proceeding may have on those limitations on the assignment of receivables independent of secured transactions law is a matter of insolvency law (see the *Insolvency Guide*, recommendations 83-85).

348. The *Insolvency Guide* contains extensive recommendations concerning the impact of insolvency proceedings on contracts with respect to which both the debtor and its counterparty have not fully performed their obligations under the contract (see the *Insolvency Guide*, recommendations 69-86). A licence agreement could be such a contract, if it has not been fully performed by both parties and the term of the licence agreement has not been completed (so that there is remaining performance by the licensor). However, a licence agreement is not such a contract, if it has been fully performed by the licensee through an advance payment of the entire amount of the royalties owed by the licensee to the licensor, as may be the case in the event of an exclusive licence agreement and the absence of any ongoing obligations of the licensor. The insolvent debtor could be the licensor (owing the licensee the right to use or exploit the licensed intellectual property in line with the terms and conditions of the licence agreement) or the licensee (owing payment of royalties and the obligation to use or exploit the licensed intellectual property in accordance with the licence agreement).

349. The *Insolvency Guide* recommends that any contractual clauses that automatically terminate and accelerate a contract upon an application for commencement, or commencement, of insolvency proceedings or upon the appointment of an insolvency representative should be unenforceable as against the insolvency representative and the debtor (see the *Insolvency Guide*, recommendation 70). The *Insolvency Guide*

also recommends that the insolvency law should specify the contracts that are exempt from the operation of this recommendation, such as financial contracts, or are subject to special rules, such as labour contracts (see the *Insolvency Guide*, recommendation 71).

350. The commentary to the *Insolvency Guide* explains the perceived advantages and disadvantages of such clauses, the types of contract that may be appropriate to be exempted and the inherent tension between promoting the debtor's survival, which may require the preservation of contracts, and introducing provisions that override contractual clauses. The possible application of such provisions to intellectual property is addressed in the commentary at part two, chapter II, paragraph 115, of the *Insolvency Guide*. In particular, the commentary to the *Insolvency Guide* states that some laws uphold these clauses in some circumstances and explains the reasons for this approach. These reasons include the need for creators of intellectual property to be able to control the use of that property and the effect on a counterparty's business of termination of a contract, especially one with respect to an intangible (see the *Insolvency Guide*, part two, chap. II, para. 115). For example, automatic termination and acceleration clauses contained in intellectual property licence agreements may be upheld as the insolvency of the licensee may have a negative impact not only on the licensor's rights but also on the intellectual property right itself. This is the case, for example, where the insolvency of a licensee of a trademark used on products may affect the market value of the trademark and the trademarked products. In any case, clauses included in intellectual property licence agreements that provide, for example, that a licence terminates after X years or upon material breach such as failure of the licensee to upgrade or market the licensed products on time (that is, where the event that triggers the automatic termination is not insolvency) are not affected (see the *Insolvency Guide*, footnote 39 to recommendation 72).

351. The commentary of the *Insolvency Guide* also states that other laws override these clauses and explains the relevant reasons (see the *Insolvency Guide*, part two, chap. II, paras. 116 and 117). The commentary further explains that, although some insolvency laws do permit these types of clause to be overridden if insolvency proceedings are commenced, this approach has not yet become a general feature of insolvency laws. In this regard, the commentary speaks of an inherent tension between promoting the debtor's survival, which may require the preservation of contracts, and affecting commercial dealings by creating a variety of exceptions to general contract rules. The commentary concludes by expressing the desirability that an insolvency law permit such clauses to be overridden (see part two, chap. II, para. 118).

352. Under the recommendations of the *Insolvency Guide*, the insolvency representative may continue or reject a licence agreement as a whole, if it has not been fully performed by both parties (see the *Insolvency Guide*, recommendations 72 and 73). In the case of one licence agreement, continuation or rejection of the licence agreement by the insolvency representative of one party will affect the rights of the other party. In the case of a chain of licence and sub-licence agreements, continuation or rejection of a licence agreement will affect the rights of all subsequent parties in the chain. Finally, in the case of cross-licensing agreements (where a licensor grants a licence, the licensee then further develops the licence and grants a licence in the further developed licensed product to the licensor), continuation or rejection of a licence agreement will affect each party both in its capacity as licensor and licensee.

353. If the insolvency representative chooses to continue a licence agreement that has not been fully performed by both parties and as to which the insolvent debtor (licensor or licensee) is in breach, the breach must be cured, the non-breaching counterparty must be substantially returned to the economic position that it was in before the breach and the insolvency representative must be able to perform the licence agreement (see the *Insolvency Guide*, recommendation 79). In this case, the insolvency proceedings will have no impact on the legal status of a security right granted by the licensor or the licensee. However, if the insolvency representative chooses to reject the licence agreement, there will be an impact on a security right granted by the licensor or the licensee (for a full understanding of the treatment of contracts in the case of insolvency, see the *Insolvency Guide*, part two, chap. II, sect. E).

B. Insolvency of the licensor

354. If the licensor's insolvency representative decides to continue a licence agreement, there will be no impact on a security right granted by the licensor or the licensee. If the licensor is the insolvent debtor and has granted a security right in its rights under the licence agreement, and the licensor's insolvency representative decides to continue the licence agreement, the licence agreement will remain in place, the licensee will continue to owe royalties under the licence agreement and the licensor's secured creditor will continue to have a security right in those royalty payments. In this case of the licensor's insolvency, if the licensee has granted a security right in its rights under the licence agreement, the licensor will continue to owe the licensee unimpeded use of the licensed intellectual property under the licence agreement and the licensee's secured creditor will continue to have a security right in the licensee's rights under that agreement.

355. However, if the licensor's insolvency representative decides to reject the licence agreement, there will be an impact on a security right granted by the licensor or the licensee. If the licensor has granted a security right in its rights under the licence agreement, the licence agreement will no longer be effective, the licensee will no longer owe royalties under the licence agreement and thus there will be no royalties for the licensor's secured creditor to be able to apply to satisfy the secured obligation. In this case of the licensor's insolvency, if the licensee has granted a security right in its rights under the licence agreement, the licensee will no longer have the authority to use the licensed intellectual property and its secured creditor will lose its security right in the encumbered asset (that is, the licensee's authority to use or exploit the licensed intellectual property).

356. As a practical matter, a secured creditor with a security right in a licensor's rights under a licence agreement may protect itself from the consequences of a rejection of the licence agreement by the licensor's insolvency representative. Such a secured creditor may, for example, protect itself by obtaining and making effective against third parties (in addition to a security right in the licensor's rights under the licence agreement, that is, principally the royalties) a security right in the licensed intellectual property itself. Then, if the insolvency representative of the licensor rejects the licence agreement, the secured creditor of the licensor (subject to the stay and any other limitations imposed by insolvency law on the enforcement of a security right in insolvency proceedings) can enforce its security right in the licensed intellectual property by disposing of it or by entering into a new licence agreement with a new licensee similar to the licence that had been rejected and thus re-establishing the royalty stream (see the *Guide on Secured Transactions*, recommendation 149). The funds received from the disposition of the encumbered intellectual property or the royalties received pursuant to this new licence agreement would then be distributed to the secured creditor pursuant to recommendations 152-155. As a practical matter, however, this arrangement would be worthwhile only for significant licence agreements.

357. Similarly, a secured creditor with a security right in a licensee's rights under a licence agreement may seek to protect itself from the consequences of a rejection of the licence agreement by the licensor's insolvency representative by, for example, declining to make the secured loan unless the licensee obtains and makes effective against third parties a security right in the licensed intellectual property to secure the licensee's rights under the licence agreement. Then, if the insolvency representative of the licensor rejects the licence agreement, the licensee (subject to the stay and any other limitations imposed by insolvency law on the enforcement of security rights in insolvency proceedings) can enforce the security right in the licensed intellectual property itself by disposing of it

or by entering into a new licence agreement with a new licensor and the rights thereby obtained would be proceeds in which the secured creditor would have a security right. As a practical matter, this arrangement too would be worthwhile only for significant licence agreements.

358. As already mentioned, if at least one party has fully performed its obligations with respect to a licence agreement, the licence agreement is not subject to the recommendations of the *Insolvency Guide* concerning treatment of contracts. Where neither the licensor nor the licensee has fully performed its obligations under the licence agreement, however, the licence agreement would be subject to rejection under those recommendations. To protect long-term investments of licensees and in recognition of the fact that a licensee may depend on the use of rights under a licence agreement, some States have adopted rules that give additional protection to a licensee (and, in effect, its secured creditor) in the case of a licence agreement that would otherwise be subject to rejection in the insolvency of the licensor. Such protection is particularly important where there is a chain of licence and sub-licence agreements and thus several parties may be affected by the insolvency of one party in the chain.

359. For example, some States give a licensee the right to continue to use or exploit the licensed intellectual property, following the rejection of the licence agreement by the licensor's insolvency representative, as long as the licensee continues to pay royalties to the estate as provided in the licence agreement and otherwise continues to perform the licence agreement. The only obligation imposed upon the licensor's estate as a result of this rule is the obligation to continue honouring the terms and conditions of the licence agreement, an obligation that does not impose upon the resources of the licensor's estate. This approach has the effect of balancing the interest of the insolvent licensor to escape affirmative burdens under the licence agreement and the interest of the licensee to protect its investment in the licensed intellectual property.

360. In other States, licence agreements may not be subject to rejection under insolvency law because: (a) a rule that excludes the leases of immovable property from insolvency rules on rejection of contracts in the case of the lessor's insolvency applies by analogy to licence agreements in the licensor's insolvency; (b) licence agreements relating to exclusive licences create property rights (rights in rem) that are not subject to rejection (but may be subject to avoidance); (c) licence agreements are not regarded as contracts that have not been fully performed by both parties as the licensor has already performed its obligations by granting the licence; or (d) they are registered in the relevant intellectual property registry. In these States, the licensee may be able to retain the licence as long as it pays the royalties owed under the licence agreement.

361. In yet other States, licence agreements may be rejected, subject to the application of the so-called “abstraction principle”. Under this principle, the licence does not depend on the effectiveness of the underlying licence agreement. Thus, the licensee may retain the right to use or exploit the licensed intellectual property, even if a licence agreement has been rejected by the licensor’s insolvency representative. However, the licensor’s insolvency representative has a claim for the withdrawal of the licence based on the principle of unjust enrichment. Until such withdrawal, the licensee has to pay for the use of the licensed intellectual property on the basis of the principle of unjust enrichment an amount equal to the royalties owed under the licence agreement that was rejected.

362. It should be noted that the *Insolvency Guide* provides (see part two, chap. II, para. 143) that exceptions to the power to reject may also be appropriate in the case of labour agreements, agreements where the debtor is a lessor or franchisor or a licensor of intellectual property and termination of the agreement would end or seriously affect the business of the counterparty, in particular where the advantage to the debtor may be relatively minor, and contracts with government, such as licensing agreements and procurement contracts. To protect long-term investments and expectations of licensees and their creditors from the ability of the licensor’s insolvency representative in effect to renegotiate licence agreements existing at the commencement of insolvency proceedings, States may wish to consider adopting rules similar to those described in the preceding paragraphs. Any such rules would have to take account of the general rules of insolvency law and the overall effect on the insolvency estate, as well as law relating to intellectual property. States may also wish to consider to what extent the commercial practices described in paragraphs 356 and 357 above would provide adequate practical solutions.

C. Insolvency of the licensee

363. If the licensee is the insolvent debtor and has granted a security right in its rights under the licence agreement and the licensee’s insolvency representative decides to continue the licence agreement, the licence agreement will remain in place, the licensee will continue to have its rights under the licence agreement to use or exploit the licensed intellectual property (in accordance with the terms and conditions of the licence agreement) and the licensee’s secured creditor will continue to have a security right in those rights. In this case, if the licensor has granted a

security right in its rights to the payment of royalties under the licence agreement, the licensor's secured creditor will continue to have a security right in the licensor's right to the payment of royalties.

364. In cases in which the licensee's insolvency representative decides to reject the licence agreement, however, and the licensee has granted a security right in its rights under the licence agreement, the licence agreement will no longer be effective, the licensee will no longer have a right to use or exploit the licensed intellectual property and the licensee's secured creditor will not be able to use the value of the licensee's rights under the licence agreement to satisfy the secured obligation. In this case too, if the licensor has granted a security right in its right to the payment of royalties under the licence agreement, the licensor will lose its right to the payment of royalties and its secured creditor will lose its encumbered asset.

365. A secured creditor with a security right in a licensor's or licensee's rights under a licence agreement may seek to protect itself from the consequences of a rejection of the licence agreement by the licensee's insolvency representative by adopting comparable measures as described above (see paras. 356 and 357 above).

366. In the case of the insolvency of the licensee, it is important to ensure that the licensor either receive its royalties and the licensee otherwise performs the licence agreement, or that the licensor has a right to terminate the licence agreement. Insolvency law rules, such as those relating to curing any default of the licence agreement in the event that the licence agreement is continued (see para. 353 above), are essential. In addition, in situations where the insolvent licensee had granted a security right in its rights to the payment of sub-royalties, those sub-royalties will likely be a source of funds for the licensee to pay the royalties that it owes to the licensor. If the licensee's secured creditor claims all the sub-royalties and the licensee does not have another source for payment of royalties to the licensor, it is essential that the licensor have a right to terminate the licence to protect its rights.

D. Summary

367. The following table summarizes the impact of the insolvency of a licensor or licensee on a security right in that party's rights under a licence agreement.

Licensor grants a security right in its rights under a licence agreement (primarily the right to receive royalties)

Question:

What happens if the licensor or its insolvency representative decides to continue the performance of the licence agreement under the insolvency law (see the *Insolvency Guide*, recommendations 69-86)?

Answer:

The licensee continues to owe royalties under the licence agreement and the secured creditor of the licensor continues to have a security right both in the licensor's right to royalties under the licence agreement and in the proceeds of that right, in other words, any royalty payments that are made.

Question:

What happens if the licensor or its insolvency representative rejects the licence agreement under the insolvency law (see the *Insolvency Guide*, recommendations 69-86)?

Answer:

The licensee does not owe royalties under the licence agreement with respect to periods after rejection, but still owes any unpaid royalties for periods before rejection; the secured creditor of the licensor thus has a security right in the right to collect such royalties for periods prior to the rejection and in the royalties paid for those periods, but has no security right in rights to any future royalties because there will be no future royalties under the rejected agreement.

Question:

What happens if the licensee or its insolvency representative decides to continue the performance of the licence agreement under the insolvency law (see the *Insolvency Guide*, recommendations 69-86)?

Answer:

The licensor continues to have a right to receive royalties under the licence agreement and thus the secured creditor of the licensor continues to have a security right both in the licensor's right to royalties under the licence agreement and in the proceeds of that right, in other words, any royalty payments that are made.

Question:

What happens if the licensee or its insolvency representative rejects the licence agreement under the insolvency law (see the *Insolvency Guide*, recommendations 69-86)?

Answer:

The licensee does not continue to owe royalties under the licence agreement with respect to periods after rejection, but still owes any unpaid royalties for periods before rejection; the secured creditor of the licensor thus has a security right in the right to collect such royalties for periods prior to the rejection and in the royalties paid for those periods, but has no security right in rights to any future royalties because there will be no future royalties under the rejected agreement.

Question:

Licensee grants a security right in its rights under a licence agreement (primarily the right to use the intellectual property)

What happens if the licensor decides to continue the performance of the licence agreement under the insolvency law (see the *Insolvency Guide*, recommendations 69-86)?

Answer:

The licensee continues to have rights under the licence agreement and the secured creditor of the licensee continues to have a security right in those rights under the licence agreement.

Question:

What happens if the licensor or its insolvency representative rejects the licence agreement under the insolvency law (see the *Insolvency Guide*, recommendations 69-86)?

Answer:

The licensee does not have rights under the licence agreement with respect to periods after rejection, but retains any rights it may still have with respect to periods before rejection; the secured creditor of the licensee continues to have a security right in those rights of the licensee with respect to periods before rejection.

Question:

What happens if the licensee decides to continue the performance of the licence agreement under the insolvency law (see the *Insolvency Guide*, recommendations 69-86)?

Answer:

The licensee continues to have rights under the licence agreement and the secured creditor of the licensee continues to have a security right in those rights under the licence agreement.

Question:

What happens if the licensee or its insolvency representative rejects the licence agreement under the insolvency law (see the *Insolvency Guide*, recommendations 69-86)?

Answer:

The licensee does not have rights under the licence agreement with respect to periods after rejection, but retains any rights it may still have with respect to periods before rejection; the secured creditor of the licensee continues to have a security right in those rights of the licensee with respect to periods before rejection.

Annex I

Terminology and recommendations of the *UNCITRAL Legislative Guide on Secured Transactions: Supplement on Security Rights in Intellectual Property*

A. Terminology^a

“Acquisition security right” includes a security right in intellectual property or a licence of intellectual property, provided that the security right secures the obligation to pay any unpaid portion of the acquisition price of the encumbered asset or an obligation incurred or credit otherwise provided to enable the grantor to acquire the encumbered asset.

“Consumer goods” includes intellectual property or a licence of intellectual property used or intended to be used by the grantor for personal, family or household purposes.

“Inventory” includes intellectual property or a licence of intellectual property held by the grantor for sale or licence in the ordinary course of the grantor’s business.

B. Recommendations 243-248

Security rights in tangible assets with respect to which intellectual property is used^b

243. The law should provide that, in the case of a tangible asset with respect to which intellectual property is used, a security right in the tangible asset

^aIf it could be included in the *Guide*, this text would be placed in the relevant terms in section B, Terminology and interpretation.

^bIf it could be included in the *Guide*, this recommendation would be placed in chapter II, Creation of a security right, as recommendation 28 bis.

does not extend to the intellectual property and a security right in the intellectual property does not extend to the tangible asset.

Impact of a transfer of encumbered intellectual property on the effectiveness of the registration^c

244. The law should provide that the registration of a notice of a security right in intellectual property in the general security rights registry remains effective notwithstanding a transfer of the encumbered intellectual property.

Priority of rights of certain licensees of intellectual property^d

245. The law should provide that the rule in recommendation 81, subparagraph (c), applies to the rights of a secured creditor under this law and does not affect the rights the secured creditor may have under the law relating to intellectual property.

Right of the secured creditor to preserve the encumbered intellectual property^e

246. The law should provide that that the grantor and the secured creditor may agree that the secured creditor is entitled to take steps to preserve the encumbered intellectual property.

Application of acquisition security right provisions to security rights in intellectual property^f

247. The law should provide that the provisions on an acquisition security right in a tangible asset also apply to an acquisition security right in intellectual property or a licence of intellectual property. For the purpose of applying these provisions:

- (a) Intellectual property or a licence of intellectual property:
 - (i) Held by the grantor for sale or licence in the ordinary course of the grantor's business is treated as inventory; and

^cIf it could be included in the *Guide*, this recommendation would be placed in chapter IV, The registry system, as recommendation 62 bis

^dIf it could be included in the *Guide*, this recommendation would be placed in chapter V, Priority of a security right, as recommendation 81 bis. As an asset-specific recommendation, this recommendation would replace the general recommendation 81, subpara. (c), to the extent that it applies to the priority of the rights of a non-exclusive licensee of intellectual property as against the rights of a secured creditor of the licensor.

^eIf it could be included in the *Guide*, this recommendation would be placed in chapter VI, Rights and obligations of the parties to a security agreement, as recommendation 116 bis.

^fIf it could be included in the *Guide*, this recommendation would be placed in chapter IX, Acquisition financing, as recommendation 186 bis.

- (ii) Used or intended to be used by the grantor for personal, family or household purposes is treated as consumer goods; and
- (b) Any reference to:
 - (i) Possession of the encumbered asset by the secured creditor does not apply;
 - (ii) The time of possession of the encumbered asset by the grantor refers to the time the grantor acquires the encumbered intellectual property or licence of intellectual property; and
 - (iii) The time of the delivery of the encumbered asset to the grantor refers to the time the grantor acquires the encumbered intellectual property or licence of intellectual property.

Law applicable to a security right in intellectual property⁸

248. The law should provide that:

(a) The law applicable to the creation, effectiveness against third parties and priority of a security right in intellectual property is the law of the State in which the intellectual property is protected;

(b) A security right in intellectual property may also be created under the law of the State in which the grantor is located and may also be made effective under that law against third parties other than another secured creditor, a transferee or a licensee; and

(c) The law applicable to the enforcement of a security right in intellectual property is the law of the State in which the grantor is located.

⁸If it could be included in the *Guide*, this recommendation would be placed in chapter X, Conflict of laws, as recommendation 214 bis.

Annex II

Decision of the United Nations Commission on International Trade Law and General Assembly resolution 65/23

A. Decision of the Commission

1. At its 914th meeting, on 29 June 2010, the Commission adopted the following decision:

The United Nations Commission on International Trade Law,

Recognizing the importance of efficient secured transactions regimes in promoting access to secured credit,

Recognizing also the need to make secured credit more available and at lower cost to intellectual property owners and other intellectual property right holders, and thus the need to enhance the value of intellectual property rights as security for credit,

Noting that the *UNCITRAL Legislative Guide on Secured Transactions* generally applies to security rights in intellectual property, without inadvertently interfering with the basic rules and objectives of law relating to intellectual property,

Taking into account the need to address the interaction between secured transactions law and law relating to intellectual property at both national and international levels,

Recognizing that States would need guidance as to how the recommendations of the *UNCITRAL Legislative Guide on Secured Transactions* would apply in an intellectual property context and as to the adjustments that need to be made in their laws to avoid inconsistencies between secured transactions law and law relating to intellectual property,

Noting further the importance of balancing the interests of all stakeholders, including grantors, whether they are owners, licensors or licensees of intellectual property, and secured creditors,

Noting with satisfaction that the Supplement to the *UNCITRAL Legislative Guide on Secured Transactions* dealing with security rights in intellectual property is consistent with the *UNCITRAL Legislative Guide on Insolvency Law*^a with regard to the treatment of the impact of insolvency of a licensor or licensee of intellectual property on a security right in that party's rights under a licence agreement,

Expressing its appreciation to international intergovernmental and non-governmental organizations active in the fields of secured transactions law and law relating to intellectual property, in particular, the World Intellectual Property Organization and the Hague Conference on Private International Law, for their participation in and support for the development of the Supplement to the *UNCITRAL Legislative Guide on Secured Transactions* dealing with security rights in intellectual property,

Expressing its appreciation to the participants of Working Group VI (Security Interests), as well as to the Secretariat, for their contribution to the development of the Supplement to the *UNCITRAL Legislative Guide on Secured Transactions* dealing with security rights in intellectual property,

1. *Adopts* the Supplement under the title “UNCITRAL Legislative Guide on Secured Transactions: Supplement on Security Rights in Intellectual Property”, consisting of the text contained in documents A/CN.9/700 and Add.1-7, with the amendments adopted by the Commission at its forty-third session, and authorizes the Secretariat to edit and finalize the text of the Supplement pursuant to the deliberations of the Commission at that session;

2. *Requests* the Secretary-General to disseminate broadly the text of the Supplement to the *UNCITRAL Legislative Guide on Secured Transactions* dealing with security rights in intellectual property, transmitting it to Governments and other interested bodies, in both the fields of secured financing and intellectual property;

^aUnited Nations publication, Sales No. E.05.V.10.

3. *Recommends* that all States utilize the Supplement to the *UNCITRAL Legislative Guide on Secured Transactions* dealing with security rights in intellectual property, to assess the economic efficiency of their secured transactions regimes as well as their intellectual property regimes and give favourable consideration to the Supplement when revising or adopting legislation relevant to secured transactions and intellectual property, and invites States that have used the *Guide* and the Supplement to advise the Commission accordingly.

B. General Assembly resolution 65/23

2. At its 57th plenary meeting, on 6 December 2010, the General Assembly adopted, on the basis of the report of the Sixth Committee A/65/465, draft resolution III, the following resolution:

UNCITRAL Legislative Guide on Secured Transactions: Supplement on Security Rights in Intellectual Property

The General Assembly,

Recognizing the importance to all States of efficient secured transactions regimes in promoting access to secured credit,

Recognizing also the need to make secured credit more available and at lower cost to intellectual property owners and other intellectual property right holders, and thus the need to enhance the value of intellectual property rights as security for credit,

Noting that the *UNCITRAL Legislative Guide on Secured Transactions*^a generally applies to security rights in intellectual property, without inadvertently interfering with the basic rules and objectives of law relating to intellectual property,

Taking into account the need to address the interaction between secured transactions law and law relating to intellectual property at both the national and the international levels,

Recognizing that States would need guidance as to how the recommendations contained in the *UNCITRAL Legislative Guide on Secured Transactions* would apply in an intellectual property context

^aUnited Nations publication, Sales No. E.09.V.12.

and as to the adjustments that need to be made to their laws to avoid inconsistencies between secured transactions law and law relating to intellectual property,

Noting the importance of balancing the interests of all stakeholders, including grantors, whether they are owners, licensors or licensees of intellectual property, and secured creditors,

Expressing its appreciation to intergovernmental and international non-governmental organizations active in the fields of secured financing and intellectual property, in particular the World Intellectual Property Organization and the Hague Conference on Private International Law, for their participation in and support for the development of the UNCITRAL Legislative Guide on Secured Transactions: Supplement on Security Rights in Intellectual Property,^b

1. *Expresses its appreciation* to the United Nations Commission on International Trade Law for the completion and adoption of the UNCITRAL Legislative Guide on Secured Transactions: Supplement on Security Rights in Intellectual Property;^b

2. *Requests* the Secretary-General to disseminate broadly, including through electronic means, the text of the Supplement and to transmit it to Governments and other interested bodies;

3. *Recommends* that all States utilize the Supplement to assess the economic efficiency of their intellectual property financing and give favourable consideration to the Supplement when revising or adopting their relevant legislation, and invites States that have done so to advise the Commission accordingly;

4. *Also recommends* that all States continue to consider becoming parties to the United Nations Convention on the Assignment of Receivables in International Trade^c and implementing the recommendations contained in the *UNCITRAL Legislative Guide on Secured Transactions*.^a

*57th plenary meeting
6 December 2010*

^bSee *Official Records of the General Assembly, Sixty-fifth Session, Supplement No. 17 (A/65/17)*, ch. IV.

^cResolution 56/81, annex.

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