SECOND INTERNATIONAL COLLOQUIUM ON SECURED TRANSACTIONS[1]

SECURITY INTERESTS IN INTELLECTUAL PROPERTY RIGHTS

UNCITRAL VIENNA 18-19 JANUARY 2007

SETTING THE STAGE: ECONOMIC BACKGROUND AND INTELLECTUAL PROPERTY FINANCING NEEDS AND PRACTICES

The Possible Interaction between the UNCITRAL Draft and European Proposals on Security Interests

Willem Grosheide

1. Preliminary Remarks

In the following presentation, some general observations will first be made (sub 2) with regards the establishment of an international instrument for the regulation of secured transactions. This is followed by a brief account of a recent study on the subject in the EU in view of further harmonisation of EU civil law (sub 3). Finally, some reflections are offered with regard to the interaction between the EU Study and the Legislative Guide, particularly with regard to intellectual property rights,

2. General Observations

Leaving aside the existing national differences in substantive intellectual property law, those differences related to the law of secured interests are generally seen as obstacles to worldwide cross-border trade in intellectual property rights.
In order to come to terms with these obstacles, one can think generally of various solutions in this respect. First one could opt for the complete worldwide harmonisation of the law of secured interests (possibly facilitated by a *unitary device* as codified in article 9 US Uniform Commercial Code). Secondly, one could mention the creation of a new international security right for cross-border transactions to be used next to the existing national security rights (introducing all sorts of fine-tuning questions). This may be optional, but would have to cover in particular third-party effects, *i.e.* the execution and insolvency creditors of both the debtor/grantor and the creditor/grantee of the security. Finally, one could attempt to make a statutory period of grace (*e.g.* three or four months) during which the security right retains the validity and the effect which it had under the law of its preceding location in another country. The harmonisation of choice of law rules within private international law seems to be difficult here since the core problem is the applicability of the *lex rei sitae* in this domain of secured interests. Finally, another possibility may

[1] Dr. F. W. Grosheide is professor of intellectual property law at the Center for Intellectual Property Law (CIER), Molengraaff Institute for Private Law, Utrecht University and practising law with Van Doorne in Amsterdam.

be the introduction of a generally recognised authority of a certain choice of law in this respect. Of course, all this can not be done without the establishment of an international legal instrument (*e.g.* a convention) or as in the EU a Regulation or a Directive.
With regard to any attempt at harmonisation a crucial issue will be the way in which to define what will be understood by an intellectual property right. Does such a right fall within the domain of property law in general or is it a special category thereof; is it a *sui generis* right? Will it be taken into account when designing the content of security rights regimes that intellectual property rights have specific qualities such as their temporal nature, their vulnerability to attacks on their validity, or the fact that they can be executed on a almost equal footing by right owners and their licensees? And what if the licensee violates its licensing agreement which forbids to give the licensed intellectual property rights as collateral in any security transaction, *e.g.* with a bank, enters into such a forbidden relationship?
A final observation must be devoted to the fact that the law of secured interests is a good example of what can be called a *mixtum compositum* of both contract law and property law, evidencing a decline in the significance of possession and the rise of contractual instruments coupled with title-based security rights (*e.g.* leasing, factoring). In this respect it is also noteworthy that, somewhat paradoxically, one sees, on the one hand, a tendency to enlarge the range of security rights and, on the other, a counter-tendency to diminish the powers of the secured party, especially in insolvency (*e.g.* the moratorium to enforce creditors' rights).

3. Study by Von Bar/Drobnig submitted to the EU

In a recent report by Christian von Bar and Ulrich Drobnig, *Study on Property Law and Non-Contractual Liability Law as they relate to Contract Law* (*SANCO B5-1000/02/000574*) submitted to the EU Commission, attention is paid to the interrelationship between contract law and property law in respect of secured transactions. In doing so, most of the general observations made in sub. 1 with regard to security rights in goods and services are in general taken into account. The study was made against the background of actual considerations about approximating or even harmonising the EU systems of contract law. The key issue is whether the unification or harmonisation of contract law may have an impact upon and interfere with existing property law. Having such an impact may primarily be expected upon the contractual (as distinct from statutory or judicial) transfer of ownership and the creation of security rights in movables and immovables. It is thought to be of crucial importance for doing business in the EU to reach at least a common understanding about how to answer questions on the borderline of particularly contract law and property law such as those related to secured transactions.
In doing so the study has as it main focus the problems which arise from the actual difference in the characterisation of the same questions of law in the EU member states. This is considered to be detrimental to the adequate functioning of the internal market. The respective questions have been elaborated in the form of questionnaires which have been addressed to professional organisations in the EU member states. However, the response to that questionnaires appeared to be very low.
Some of the study's findings are of special interest in view of the contents of the draft UNCITRAL Legislative Guide for secured transactions:

a businesses only rarely refrain from doing cross-border business within the EU due to anxieties about differences in law and consequential ignorance concerning the risks of liability which may be too great.

b businesses and the legal profession complain about, among other things, differences in the field of credit securities (particularly the retention of title in its different manifestations), and the loss of security by the mere fact of goods crossing a border is felt to be a big problem.

c great importance is given to freedom in the relevant choice of law rules.

d when it comes to identifying the subject-matter of property law it appears that despite differences between the legal systems of the member states both categorically and terminologically, there appears to be unanimity with respect to the result.

e if one takes the term *thing* as referring to the core concept of property law, it appears that the EU recognises both a narrow concept (Germany, Greece) and a broad concept (Austria, Belgium, England & Wales and Northern Ireland, France, Italy, The Netherlands, Portugal, Scotland, Spain, Sweden[S1]), the latter group regarding intellectual property rights (like receivables) as *biens* or *incorporeal moveable rights*, the broad concept being most clearly expressed in article 3:1 Dutch CC (*e.g. goed* = patrimonial right=asset).

f the broad concept as used in the Study, does not imply that all the rules which are applicable to these two forms of things are necessarily identical.

g. with regard to security interests the catalogued problems concentrate on the creation of rights *in rem* by contract, two approaches appearing to be followed:

g.1 rights *in rem* exist as soon as the contract is concluded, but in order to have third party effect (e.g. in relation to creditors of transferors or creditors of transferees) an additional act (e.g. the transfer of possession or entry in a register) is required.

g.2 rights *in rem* exist only after an additional act (such as the transfer of possession or entry in a register) is carried out.

It is important to note that the differences between the two approaches to creating security rights appear to have different effects:

a temporal effect: when is the security vested?

b validity effect: does the validity of the security right depend upon the validity of the underlying contract?

c accessorial effect: is the content of a proprietary security right dependant upon the content of the contractual right?

d enforcement effect: is the creditor competent to attack (*e.g.* rescind) the underlying contract first, or to invoke corresponding legal remedies (*e.g.* termination)?

4. Interaction between the EU Study and the UNCITRAL Draft

It is not a coincidence that UNCITRAL and the EU are both in the process of studying the legal facilitation of cross-border trade, since the same obstacles are encountered in the international arena as in the internal market. Given the fact that, legally speaking, the world is divided mainly along the lines of civil law systems and common law systems it does not come as a surprise that UNCITRAL drafts and the EU Study have to come to terms with the same existing differences in the national laws on secured transactions, and as a consequence thereof often arrive at the same sort of recommendations for overcoming these differences.

It is striking, however, that neither the authors of the EU Study nor the drafters of the Legislative Guide appear to have taken into account the fundamental reshaping of the economic order, in particular the developed world, over the last thirty years or so, from economies based on trade in goods and services into so-called knowledge economies based on exchange of products that are

either in themselves intellectual property rights or related to that kind of rights. This inaccuracy, however, is not easily repaired by including intellectual property rights in the final stage of drafting into the Legislative Guide, ranging them into the existing category of *intangible rights* , nor by categorising these rights as *incorporeal movable rights* or *patrimonial rights* as is done in the EU Study. For it may well be that the specific qualities of intellectual property rights, some of which are mentioned in sub 1, require special treatment when it comes to security transactions with regard to those rights and products and services related to those rights. In other words: it should have been made clear whether the existing legal regimes for establishing security rights in goods and services are without distinction concerning their specific qualities applicable to intellectual property rights.

Where does this all lead to with regard to security transactions in intellectual property rights?

Here the EU Study is not of much assistance since it only investigates the actual state of the law in the EU member states, suggesting some solutions for the indicated problems to which the existing differences in national law lead. Important in this respect, however, is the choice made by the EU Study for a broad concept of the notion of a thing, also covering intellectual property rights. This may be seen as an indication that under that study the general rules on security are considered equally applicable (at least in principle) to intellectual property rights. The Legislative Guide on the other hand introduces new rules which may well be in place for traditional goods and services, but may not be fine-tuned to intellectual property rights. Taking these observations into account the following reflections may be tentatively made in order to illustrate the specific problems that have to be solved with regards secured transactions in property rights.

Firstly, a special quality of intellectual property rights which make these rights different from goods and services, is that they can exist (and thus serve as collateral) on their own or be associated to other property such as goods and services. In practice, one will thus often see that a secured lender seeks financing based on the value of its inventory *c.a.* that involves associated intellectual property rights.

Secondly, and a further reason for concern, is the fact that these intellectual property rights may be owned either by the lender itself or licensed to it by a third party, either exclusively or non-exclusively. This of course decisively determines the competences of the lender with regard to the intellectual property rights.

Thirdly, things may become even more complicated if the license agreement under which the lender has become authorised to use the associated intellectual property right, knows of conditions which make the licensee dependent upon previous approval of the licensor (or simply forbids such a transaction to be done) in case of activities such as going for credit to a bank. If such a license agreement is in place, entering into a financing agreement by the licensee will give the licensor the right to terminate the license agreement forthwith leaving the lender empty-handed.

These examples illustrate that simply declaring the general rules for secured transactions to be applicable to intellectual property rights will lead to difficulties since the general rules do not take into account the specific aspects of transactions dealing with intellectual property rights as security interests.