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## **Report of Working Group VI (Security Interests) on the work of its fourteenth session**

**(Vienna, 20-24 October 2008)**

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## I. Introduction

1. At its fourteenth session (Vienna, 20-24 October 2008), Working Group VI (Security Interests) continued its work on the preparation of an annex to the UNCITRAL Legislative Guide on Secured Transactions<sup>1</sup> specific to security rights in intellectual property, pursuant to a decision taken by the United Nations Commission on International Trade Law at its fortieth session, in 2007.<sup>2</sup> The Commission's decision to undertake work on security rights in intellectual property was taken in response to the need to supplement its work on the Guide by providing specific guidance to States as to the appropriate coordination between secured transactions and intellectual property law.<sup>3</sup>

2. At its thirty-ninth session, in 2006, the Commission considered its future work on secured financing law. It was noted that intellectual property rights (e.g. copyrights, patents and trademarks) were becoming an extremely important source of credit and should not be excluded from a modern secured transactions law. In addition, it was noted that the recommendations of the draft Guide generally applied to security rights in intellectual property to the extent that they were not inconsistent with intellectual property law. Moreover, it was noted that, as the recommendations of the draft Guide had not been prepared with the special intellectual property law issues in mind, enacting States should consider making any necessary adjustments to the recommendations to address those issues.<sup>4</sup>

3. In order to provide more guidance to States, the suggestion was made that the Secretariat should prepare, in cooperation with international organizations with expertise in the fields of secured financing and intellectual property law and, in particular the World Intellectual Property Organization (WIPO), a note for submission to the Commission at its fortieth session, in 2007, discussing the possible scope of work that could be undertaken by the Commission as a supplement to the Guide. In addition, it was suggested that, in order to obtain expert advice and the input of the relevant industry, the Secretariat should organize expert group meetings and colloquiums as necessary.<sup>5</sup> After discussion, the Commission requested the Secretariat to prepare, in cooperation with relevant organizations and in particular WIPO, a note discussing the scope of future work by the Commission on intellectual property financing. 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.<sup>6</sup>

4. Pursuant to those requests, the Secretariat organized, in cooperation with 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.

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<sup>1</sup> To be subsequently issued as a United Nations sales publication.

<sup>2</sup> *Official Records of the General Assembly, Sixty-second Session, Supplement No. 17 (A/62/17)*, part I, para. 162.

<sup>3</sup> *Ibid.*, para. 157.

<sup>4</sup> *Ibid.*, *Sixty-first Session, Supplement No. 17 (A/61/17)*, paras. 81 and 82.

<sup>5</sup> *Ibid.*, para. 83.

<sup>6</sup> *Ibid.*, para. 86.

At the colloquium, several suggestions were made with respect to adjustments that would need to be made to the draft Guide to address issues specific to intellectual property financing.<sup>7</sup>

5. At the first part of its fortieth session (Vienna, 25 June-12 July 2007), the Commission considered a note by the Secretariat entitled “Possible future work on security rights in intellectual property” (A/CN.9/632). The note took into account the conclusions reached at the colloquium on security rights in intellectual property rights. In order to provide sufficient guidance to States as to the adjustments that they might need to make in their laws to avoid inconsistencies between secured financing and intellectual property law, the Commission decided to entrust Working Group VI with the preparation of an annex to the draft Guide specific to security rights in intellectual property rights.<sup>8</sup>

6. At the second part of its fortieth session (Vienna, 10-14 December 2007), the Commission finalized and adopted the Guide on the understanding that an annex to the Guide specific to security rights in intellectual property rights would subsequently be prepared.<sup>9</sup>

7. At its thirteenth session (New York, 19-23 May 2008), the Working Group considered a note by the Secretariat entitled “Security rights in intellectual property rights” (A/CN.9/WG.VI/WP.33 and Add.1). At that session, the Working Group requested the Secretariat to prepare a draft of the annex to the Guide on security rights in intellectual property reflecting the deliberations and decisions of the Working Group (see A/CN.9/649, para. 13). As the Working Group was not able to reach agreement as to whether certain matters related to the impact of insolvency on a security right in intellectual property (see A/CN.9/649, paras. 98-102) were sufficiently linked with secured transactions law so as to justify their discussion in the annex to the Guide, it decided to revisit those matters at a future meeting and to recommend that Working Group V (Insolvency Law) be requested to consider those matters (see A/CN.9/649, para. 103).

8. At its forty-first session (New York, 16 June-3 July 2008), the Commission noted with satisfaction the good progress achieved by Working Group VI. The Commission also noted the decision of the Working Group with respect to certain matters related to the impact of insolvency on a security right in intellectual property, and decided that Working Group V should be informed and should be invited to express any preliminary opinion at its next session. It was also decided that, should any remaining issue require joint consideration by the two working groups after that session, the Secretariat should have discretion to organize a joint discussion of the impact of insolvency on a security right in intellectual property when the two working groups meet back to back in early 2009.<sup>10</sup>

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<sup>7</sup> See <http://www.uncitral.org/uncitral/en/commission/colloquia/2secint.html>.

<sup>8</sup> *Official Records of the General Assembly, Sixty-second Session, Supplement No. 17 (A/62/17)*, part I, paras. 156, 157 and 162.

<sup>9</sup> *Ibid.*, part II, paras. 99 and 100.

<sup>10</sup> *Ibid.*, *Sixty-third Session, Supplement No. 17 (A/63/17)*, para. 326.

## II. Organization of the session

9. The Working Group, which was composed of all States members of the Commission, held its fourteenth session in Vienna from 20 to 24 October 2008. The session was attended by representatives of the following States members of the Working Group: Algeria, Australia, Austria, Bolivia, Bulgaria, Canada, China, Colombia, Czech Republic, El Salvador, Fiji, France, Germany, Greece, Guatemala, India, Iran (Islamic Republic of), Italy, Japan, Kenya, Lebanon, Malaysia, Mexico, Nigeria, Norway, Republic of Korea, Russian Federation, Senegal, Spain, Switzerland, Thailand, Uganda, United Kingdom of Great Britain and Northern Ireland, United States of America and Venezuela (Bolivarian Republic of).

10. The session was attended by observers from the following States: Angola, Argentina, Belgium, Burundi, Côte d'Ivoire, Croatia, Democratic Republic of the Congo, Dominican Republic, Indonesia, Jordan, Mali, Peru, Philippines, Qatar, Saudi Arabia, Slovakia, Slovenia, Tunisia, Turkey and Zambia.

11. The session was also attended by observers from the following international organizations:

(a) *United Nations system*: World Intellectual Property Organization (WIPO);

(b) *Intergovernmental organizations*: League of Arab States;

(c) *International non-governmental organizations invited by the Working Group*: American Bar Association, Association of Commercial Television in Europe, Center for International Legal Studies, Commercial Finance Association, European Company Lawyers Association, Forum for International Conciliation and Arbitration, Independent Film & Television Alliance, International Bar Association, International Federation of Phonographic Industry, International Swaps and Derivatives Association, International Trademark Association and the Association of European Trade Mark Owners (MARQUES).

12. The Working Group elected the following officers:

*Chairman*: Ms. Kathryn Sabo (Canada)

*Rapporteur*: Ms. Jitka Václavicková (Czech Republic)

13. The Working Group had before it the following documents:

(a) Annotated provisional agenda (A/CN.9/WG.VI/WP.34);

(b) Annex to the UNCITRAL Legislative Guide on Secured Transactions dealing with security rights in intellectual property: note by the Secretariat (A/CN.9/WG.VI/WP.35 and Add.1).

14. The Working Group adopted the following agenda:

1. Opening of the session and scheduling of meetings.
2. Election of officers.
3. Adoption of the agenda.
4. Security rights in intellectual property.

5. Other business.
6. Adoption of the report.

### **III. Deliberations and decisions**

15. The Working Group considered the draft annex to the UNCITRAL Legislative Guide on Secured Transactions dealing with security rights in intellectual property (A/CN.9/WG.VI/WP.35 and Add.1). The deliberations and decisions of the Working Group are set forth below in chapter IV; sections A-C refer to A/CN.9/WG.VI/WP.35, and sections D-K refer to A/CN.9/WG.VI/WP.35/Add.1. The Secretariat was requested to prepare a revised draft of the annex reflecting those deliberations and decisions.

## **IV. Security rights in intellectual property**

### **A. Introduction**

#### **1. Background**

16. It was widely felt that the discussion of the background of the project was appropriate and should be included in the annex to the Guide dealing with security rights in intellectual property.

#### **2. The interaction between secured transactions and intellectual property law under the Guide**

17. The Working Group noted with appreciation the sensitivity demonstrated in the draft annex with respect to the interaction of secured transactions and intellectual property law. In addition, the Working Group noted with appreciation the collaborative role of WIPO, reflecting the interest of WIPO member States in the issue. It was also noted that WIPO planned to organize an information meeting to raise awareness among its member States of the importance of intellectual property financing and the relevant work of UNCITRAL; and to distribute a questionnaire to its member States with a view to gathering information on their law on intellectual property financing and providing feedback to the Working Group.

18. While there was agreement as to the policy reflected in the discussion of the interaction between secured transactions and intellectual property law under the Guide, a number of comments and suggestions were made with regard to the exact formulation, including that:

(a) In paragraph 8, second sentence, reference should be made to the exact text of recommendation 4, subparagraph (b), of the Guide and, in the last sentence, the reference to national law should be separated from the reference to international agreements, as the exact scope of the term “intellectual property” was a matter for both national law and international treaties and the latter could not be interpreted differently by each contracting State;

(b) In paragraph 9, the point that intellectual property law might need to be reviewed where it dealt with issues relating to security rights in intellectual property

differently than secured transactions law should be made more clearly and, in the last sentence, reference should be made to the need to ensure the compatibility of secured transactions and intellectual property law rather than their integration.

19. Subject to the changes mentioned above, the Working Group approved the substance of the section of the draft annex dealing with the interaction between secured transactions and intellectual property law under the Guide.

### 3. Terminology

20. While there was agreement that some terms needed to be explained in the commentary of the draft annex, a number of comments and suggestions were made as to the exact formulation of that commentary, including that:

(a) With respect to paragraph 13, the term “law relating to intellectual property” could be defined along the following lines:

“As used in this Annex, ‘law relating to intellectual property’ means any law, regulation or common law rule that governs any aspect of a State’s intellectual property regime, including but not limited to laws and regulations that govern the creation, registration, maintenance, renewal, assignment, sale, transfer or licensing of any intellectual property rights, as well as all laws and regulations governing the granting and recording of security interests, liens, mortgages or other security devices involving intellectual property rights”;

(b) In paragraph 15, the second sentence should be revised to state that a licence created a right in property, the example should be clarified by reference to the treatment of an exclusive licensee as a rights holder in some legal systems and the last sentence should refer to the term “security right” as used in the Guide;

(c) In paragraph 18, reference should be made to the different types of asset that could be used as an encumbered asset (i.e. the rights of a rights holder, the rights of a licensor that was not a rights holder and the rights of a licensee);

(d) In paragraph 19, reference should be made to the term “competing claimant” as used in the Guide and the reference to infringers should be qualified, since only “alleged” infringers would argue that they had a valid claim and were thus true competing claimants;

(e) In paragraph 20, it should be clarified that the Guide provided that a secured creditor acquired a security right in, but not ownership of, an encumbered asset, primarily because of the need to protect the rights of the grantor/owner, and that treatment did not affect the rights of a secured creditor for purposes of intellectual property law.

21. In support of the proposed term “law relating to intellectual property”, it was stated that it would be useful to summarize for the reader the meaning of that term, which was essential to understanding the relationship between secured transactions law and intellectual property law under the Guide. However, it was also stated that the Guide already clarified that the term “law” included both statutory and non-statutory law and that the term “law relating to intellectual property” meant a body of law that was broader than intellectual property law, strictly speaking, but narrower than general contract or property law. It was observed that recommendation 4, subparagraph (b), of the Guide, followed by extensive

commentary, should be sufficient, including a discussion of intellectual property law unaffected by the Guide, general property law affected by the Guide and intellectual-property-specific law accorded preference under recommendation 4, subparagraph (b). In addition, it was pointed out that, in its current formulation, the term was excessively broad and would inadvertently cover general contract and property law. It was widely felt that the principle of deference to law relating to intellectual property law would apply only to situations where that law dealt with security rights in intellectual property. After discussion, the Working Group requested the Secretariat to narrow the scope of the term to law that governed specifically intellectual property rights and security rights in intellectual property rights.

22. In the light of the fact that the concept of “competing claimant” was discussed in the chapter on the third-party effectiveness of a security right, the Working Group deferred to a later point during the session its decision with respect to the suggestion concerning the reference to infringers mentioned above in paragraph 20 (d). Subject to the other changes mentioned above, the Working Group approved the substance of the section of the draft annex dealing with terminology.

#### **4. Examples of intellectual property financing practices**

23. While the examples of intellectual property financing practices mentioned in the draft annex were generally considered to be useful, a number of comments and suggestions were made, including that:

(a) In paragraph 22, the last sentence of paragraph 39 (a) should be included with an additional reference to applicable law;

(b) In paragraph 23, the different types of encumbered asset (i.e. rights of a rights holder, rights of a licensor that was not a rights holder and rights of a licensee) should be clarified and discussed in the relevant examples;

(c) Paragraph 25 should be deleted and, in line with the terminology used in the Guide, reference should be made to a security right in all assets of an enterprise rather than to an enterprise mortgage, while that type of transaction should not be presented as a third category, as it simply involved security rights in tangible and intangible assets, that is, reflected practices listed in the first or the second category discussed in paragraphs 23 and 24 respectively;

(d) The example in paragraph 27 should be revised to clarify that the issue was whether a person could grant a security right in rights under a licence agreement in the course of its business and whether, as a result, that security right extended to the royalties payable under that licence agreement;

(e) In paragraph 38, reference should be made to a “secured creditor” or a “prospective lender or other credit provider” rather than to the narrower term “prospective lender”;

(f) In paragraph 39 (a), the last sentence should be moved to paragraph 22, amended as mentioned in subparagraph (a) above, and the insolvency discussion in paragraphs 39 (b) and (c) should be expanded to reflect in some detail four rather than two scenarios (see para. 129 below);

(g) Paragraph 40 should be revised to clarify that a security right in all assets of a grantor was useful despite any limitations introduced by intellectual property law, since a security right might extend to the proceeds of an originally encumbered intellectual property right and, in any case, such a security right might be effective against the insolvency representative in case of the insolvency of the grantor;

(h) Paragraph 41 should be revised to clarify that an accurate appraisal of encumbered intellectual property did not necessarily maximize the value of credit available and that, as in the case of any other type of encumbered asset, where intellectual property was encumbered the secured creditor would normally engage in due diligence to ascertain the value of the encumbered intellectual property.

24. The suggestion to delete paragraph 25 was objected to. It was widely felt that it reflected a different practice and should be retained. At the same time, it was agreed that the examples falling under the first category could be recast as falling under different subcategories depending on the type of encumbered asset involved in each case. Subject to the other changes mentioned above, the Working Group approved the substance of the section of the draft annex dealing with examples of intellectual property financing practices.

## **5. Key objectives and fundamental policies**

25. With regard to the section of the draft annex dealing with key objectives and fundamental policies, a number of comments and suggestions were made, including that:

(a) In paragraph 43, reference should be made to the overall objective of the Guide not interfering with, rather than being aimed at achieving, the objectives of intellectual property law;

(b) In paragraph 44, last sentence, the point about the Guide not interfering with the objectives of intellectual property law should be strengthened;

(c) In paragraph 45, the first sentence should be deleted as the Guide did not address issues relating to diminished value or abandonment of intellectual property rights by the rights holder or the secured creditor and, in the last sentence, reference should be made to a licence in general rather than to a “personal licence”.

26. More specifically, it was suggested that paragraph 45 should be revised to read along the following lines:

“Similarly, this key objective of promoting secured credit, while not interfering with the objectives of intellectual property law, 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, it is important to note that the creation of a security right in intellectual property should not be misinterpreted as constituting an inadvertent abandonment of intellectual property (e.g. failure to use a trademark properly, to use it on all goods or services or to maintain adequate quality control may result in loss of value to, or even abandonment of, the intellectual property) by the rights holder or the secured creditor. In addition, in the case of goods or services associated with marks, secured transactions law should avoid causing consumer confusion as to the source of goods or services (e.g. where a secured creditor replaces the manufacturer’s name and

address on the goods with a sticker bearing the creditor's name and address or retains the trademark and sells the goods in a jurisdiction where the trademark is owned by a different person). Finally, secured transactions law should not provide that the purported creation of a security right in the rights of a licensee that are, as a matter of intellectual property law, not transferable except with the consent of the licensor results in the transfer of such rights without the consent of the rights holder.”

27. It was stated that the reason for the proposed changes was to clarify the important goal of preventing harm to intellectual property interests as a result of the existence of a secured credit regime and to emphasize that the recommendations of the Guide would not bring about such harm. It was suggested that the reference to the secured creditor in the second sentence should be deleted, as an intellectual property right could be abandoned only by the rights holder. In addition, it was suggested that, in the last sentence, reference should be made to “applicable” intellectual property law. In that connection, with respect to paragraph 44, it was suggested that the first sentence should be recast in order to avoid creating the impression that the encouragement of innovation was the only objective of intellectual property law.

28. Subject to the other changes mentioned above, the Working Group approved the substance of that section of the draft annex.

## **B. Scope of application and party autonomy**

### **1. Broad scope of application**

29. With regard to the section of the draft annex dealing with the broad scope of application, a number of comments and suggestions were made, including that:

(a) Paragraph 47 should be revised to provide that, in some circumstances (depending on the relevant rules), a security right could be created even in an asset that was non-transferable, even though that security right would not be enforceable;

(b) Paragraph 50 should be revised to clarify that a general security rights regime would render fictional assignments unnecessary, and a recommendation should be introduced to provide that, unless otherwise provided in intellectual property law, a secured creditor could agree as to who was entitled to take the necessary steps to protect the encumbered intellectual property right;

(c) Paragraph 51 should be revised to provide that States enacting the law recommended in the Guide might wish to review their intellectual property legislation with a view to replacing all the devices by way of which a security right was created in intellectual property (including fictional assignments) with a general security right;

(d) Paragraph 54 should emphasize further the point that the list of issues following paragraph 54 was a non-exclusive list;

(e) In paragraph 54, the list of issues under the heading “copyright” should be revised along the following lines:

“(i) The determination of who is the author or joint author;

“(ii) The duration of copyright protection;

“(iii) The economic rights granted under the law and limitations and exceptions to protection;

“(iv) 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);

“(v) The transferability of economic rights, the possibilities for terminating transfers and licences and other provisions regulating transfers or licences of rights;

“(vi) The scope and transferability of moral rights;

“(vii) Presumptions relating to the exercise and transfer of rights and limitations relating to who may exercise rights;

“(viii) Attribution of original ownership in the case of commissioned works and works created by an employee within the scope of employment;”

(f) The reference to the protection of a trademark on the basis of a first-to-use or first-to-register rule should be reviewed;

(g) Paragraph 63 should be revised to provide that ownership with respect to intellectual property was a matter of intellectual property law, that the legal nature of a transfer for security purposes as a security device was a matter of general property and secured transactions law and that the legal nature of a licence was a matter of intellectual property and contract law;

(h) Paragraph 64 should be revised to clarify that any rules of secured transactions law on enforcement would not apply to the extent that they were inconsistent with rules of law relating to intellectual property that dealt with the enforcement of security rights in intellectual property.

30. The suggestion mentioned in paragraph 29 (a) above was objected to. It was widely felt that a non-transferable asset could not be encumbered. The suggestion to introduce a recommendation as to who would be entitled to take the steps necessary to protect the encumbered intellectual property right if intellectual property law did not deal with the matter was also objected to. It was widely felt that that was a matter of intellectual property law. Subject to the other changes mentioned above, the Working Group approved the substance of that section of the draft annex.

## **2. Application of the principle of party autonomy to security rights in intellectual property**

31. The Working Group approved the substance of the section of the draft annex dealing with the application of the principle of party autonomy to security rights in intellectual property.

## **C. Creation of a security right in intellectual property**

### **1. The concepts of creation and third-party effectiveness**

32. The Working Group approved the substance of the section of the draft annex dealing with the concepts of creation and third-party effectiveness of a security right.

### **2. Unitary concept of a security right**

33. The Working Group approved the substance of the section of the draft annex dealing with the unitary concept of a security right.

### **3. Requirements for the creation of a security right in intellectual property**

34. With respect to paragraph 73, the suggestion was made that the text should refer to the registration of a security right in an intellectual property registry and that the last sentence should be deleted as it dealt with third-party effectiveness rather than creation issues. Subject to those changes, the Working Group approved the substance of the section of the draft annex dealing with requirements for the creation of a security right in intellectual property.

### **4. Rights of a grantor in the intellectual property to be encumbered**

35. With respect to paragraph 75, it was suggested that the last sentence should be deleted as it dealt with matters that were not particularly relevant in that context. It was also suggested that the heading should be changed to refer to rights “relating to intellectual property” as the term “rights in intellectual property” might be misunderstood as meaning only the rights of a rights holder. Subject to those changes, the Working Group approved the substance of the section of the draft annex dealing with rights of a grantor in the intellectual property to be encumbered.

### **5. Distinction between a secured creditor and a rights holder with respect to intellectual property**

36. With respect to paragraph 76, the suggestion was made that the text should be revised to clarify that the term “rights holder”, as used in the draft annex, was generally intended to denote an owner and that a secured creditor was not an owner for the purposes of secured transactions law, which would not affect there being a different treatment of a secured creditor for the purposes of intellectual property law. In that connection, it was agreed that the meaning given to the term “rights holder” in the draft annex did not affect its exact meaning under intellectual property law.

37. With respect to paragraph 77, the suggestion was made that it should be revised to read along the following lines:

“Under the enforcement chapter of the Guide, upon default of the grantor the secured party may dispose of the encumbered asset or may propose to retain it in satisfaction of the secured obligation (see recommendations 156 and 157). Under proper circumstances, the secured creditor may be the buyer at a disposition that it conducts (see recommendations 141 and 148). Thus, while the creation of a security right in intellectual property does not work a change

in ownership of the intellectual property and nothing in the Guide provides that it changes the rights holder of the intellectual property, enforcement of the security right will often result in the grantor's rights in the intellectual property being transferred (and, thus, the identity of the rights holder, as determined by intellectual property law, might change). In situations in which the enforcement of the security right in the intellectual property results in a disposition to the secured creditor or retention of the intellectual property in satisfaction of the secured obligation, ownership may, at that time, be transferred to the secured creditor."

38. Subject to the changes mentioned above, the Working Group approved the substance of the section of the draft annex dealing with the distinction between a secured creditor and a rights holder with respect to intellectual property.

## **6. Types of rights in intellectual property that may be subject to a security right**

39. It was suggested that the heading should be revised to read along the following lines: "Categories of encumbered assets in an intellectual property context".

40. With respect to paragraph 80, it was suggested that the text should clarify whether the right to sue infringers, which was incidental to the rights of the rights holder, could be used as security for credit separately from the other rights of the rights holder.

41. It was also suggested that examples of evaluation systems should be set out since, while evaluation of the rights of a rights holder was not a legal issue, it was an important prerequisite for the use of intellectual property rights as security for credit. In that connection, reference was made to work by WIPO and the International Organization for Standardization.

42. With respect to paragraph 82, it was suggested that the text should clarify that inalienability could flow from (a) a contract that was enforceable by law, (b) a legal rule independent of any contract or (c) situations in which a security right in an asset that was non-transferable extended to the proceeds of that asset.

43. With respect to paragraph 83, it was suggested that the value of the licensor's contractual rights other than the right to claim royalties should also be discussed.

44. With respect to paragraph 84, it was suggested that the text should make it clear that (a) while, for the purposes of secured transactions law, royalties would be treated in the same way as any other receivables, their possible treatment for other purposes as part of the intellectual property right from which they flowed would not be affected; (b) the recommendations of the Guide with regard to a security right in an asset extending into proceeds, its third-party effectiveness and priority would apply to royalties as proceeds of intellectual property; and (c) reference should be made to paragraph 85 to clarify that a licensee could raise against an assignee of the royalties most of the defences or rights of set-off that the licensee could raise against the licensor (see recommendation 120 of the Guide).

45. With respect to paragraph 87, last sentence, it was suggested that reference should be made to recommendation 24 of the Guide rather than to the Guide in general in order to avoid inadvertently giving the impression, for example, that the licensor controlled the flow of royalties even in situations where the licensee had created a security right in its inbound royalty payments or that the licensor would be

treated in the case of the insolvency of the licensee as a privileged rather than as an unsecured creditor.

46. With respect to paragraph 90, it was suggested that there was no need to refer to a licensee's right to claim royalties as, if the licensee had a right to claim royalties, it would do so as a sub-licensor and the discussion of the licensor's rights in previous paragraphs would be sufficient.

47. With respect to paragraph 94, while some doubt was expressed as to whether the second part of the recommendation contained therein should be retained, it was agreed that the recommendation was useful and should be retained subject to (a) clarifying the context with language along the following lines: "in the case of a security right in a tangible asset with respect to which intellectual property is used"; and (b) expanding the commentary to explain in particular the second part of the recommendation, but also the meaning of the words "to deal with the tangible assets".

48. Subject to the changes mentioned above, the Working Group approved the substance of the section of the draft annex dealing with types of rights in intellectual property that may be subject to a security right.

## **7. Security rights in future intellectual property**

49. With respect to paragraph 95, it was suggested that the text should clarify that recommendation 17 of the Guide applied to intellectual property except as provided in recommendation 4, subparagraph (b), of the Guide.

50. With respect to paragraph 96, it was suggested that the reference to statutory prohibitions resulting from the application of the *nemo dat* principle (i.e. that one cannot give more rights than oneself has) was unnecessary because it applied to all types of asset by virtue of the application of general property law principles.

51. With respect to paragraph 98, first sentence, it was suggested that the text should be aligned more closely with recommendation 4, subparagraph (b), of the Guide.

52. Subject to the changes mentioned above, the Working Group approved the substance of the section of the draft annex dealing with security rights in future intellectual property.

## **8. Legislative or contractual limitations on the transferability of intellectual property**

53. With respect to paragraph 100, it was suggested that the text should include reference to article 8 of the United Nations Convention on the Assignment of Receivables in International Trade<sup>11</sup> dealing with the effectiveness of an assignment of receivables. Subject to that change, the Working Group approved the substance of the section of the draft annex dealing with legislative or contractual limitations on the transferability of intellectual property.

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<sup>11</sup> United Nations publication, Sales No. E.04.V.14.

## **9. Acquisition financing and licence agreements**

54. With respect to paragraphs 101 and 102, it was agreed that the only point that should be retained was that a licence agreement was not a secured transaction. The Secretariat was requested to include that point in the appropriate place in the draft annex.

## **D. Effectiveness of a security right in intellectual property against third parties**

### **1. The concept of third-party effectiveness**

55. With respect to paragraphs 1 and 2, it was suggested that the text should be recast to deal with the concept of third-party effectiveness rather than with the question of how third-party effectiveness could be achieved, as that matter was dealt with in paragraphs 5 and 6. With respect to paragraph 2, it was suggested that the text should distinguish between situations in which a security right could be made effective against third parties through registration in the general security rights registry or in the relevant intellectual property registry and situations in which registration of a security right in the relevant intellectual property registry was exclusive. It was stated that in the latter situation, recommendation 4, subparagraph (b), would apply and would result in registration in the relevant intellectual property registry becoming the exclusive method of achieving third-party effectiveness of security rights in intellectual property.

56. With respect to paragraph 4, it was suggested that the text should be recast to discuss the notion of “third parties” and “third-party effectiveness” rather than the notions of “competing claimant” and “priority”. It was widely felt that, while infringers were third parties against whom a security right would be effective, they were not competing claimants, unless they had a legitimate claim and that claim was appropriately acknowledged. In that connection, it was stated that if an “alleged infringer” had a legitimate claim, the issue would be the rights of the grantor of the security right and the *nemo dat* principle, as, if the alleged infringer was a legitimate claimant, the grantor might not have had rights to encumber at the time of the creation of the security right.

57. Subject to the changes mentioned above, the Working Group approved the substance of the section of the draft annex dealing with the concept of third-party effectiveness.

### **2. Third-party effectiveness of security rights in intellectual property that are registrable in an intellectual property registry**

58. With respect to paragraph 5, it was suggested that the text should clarify that, if registration in a specialized registry did not have third-party effects, such a registry would not qualify as a specialized registry with respect to which the relevant recommendations of the Guide could apply. In that connection, it was observed that, even if registration of a security right in the relevant intellectual property registry had constitutive effects, the registry would still qualify as a specialized registry under the Guide at least to the extent that the security right registered therein would become effective against all parties.

59. With respect to paragraph 6, it was suggested that the text should clarify that the situations described therein were situations to which, under recommendation 4, subparagraph (b), of the Guide, law relating to intellectual property would apply.

60. With respect to paragraphs 8-11, it was suggested that the text should be recast to focus on third-party effectiveness rather than on priority issues.

61. With respect to paragraph 9, it was suggested that the text should clarify that the searchers would potentially be competing claimants with respect to encumbered intellectual property. It was also suggested that the reference to difficulties associated with dual searching should be toned down as dual searching was done in several jurisdictions without much difficulty.

62. Subject to the changes mentioned above, the Working Group approved the substance of the section of the draft annex dealing with third-party effectiveness of security rights in intellectual property that are registrable in an intellectual property registry.

### **3. Third-party effectiveness of security rights in intellectual property that are not registrable in an intellectual property registry**

63. It was suggested that reference should be made to registration of a notice with respect to a security right in a trade secret. It was stated that, for confidentiality reasons, security rights in trade secrets could not be registered in an intellectual property registry. It was also observed that, to the contrary, registration of a notice with respect to a security right in a trade secret was possible because of the limited amount of data disclosed in that notice. In that connection, the suggestion was also made that the draft annex should discuss the so-called “technology escrow arrangements”, under which, for example, a licensee could be given access to copyrighted software or trade secrets in the event the licensor discontinued support, maintenance or development of the licensed product. Subject to those changes, the Working Group approved the substance of the section of the draft annex dealing with third-party effectiveness of security rights in intellectual property that are not registrable in an intellectual property registry.

## **E. The registry system**

### **1. The general security rights registry**

64. The Working Group approved the substance of the section of the draft annex dealing with the general security rights registry.

### **2. Asset-specific intellectual property registries**

65. With respect to paragraph 18, it was suggested that reference should be added to other international registration regimes, such as the regimes under the Patent Law Treaty (Geneva, 2000) and European Council regulation No. 40/941 of 20 December 1993 on the Community trademark. It was stated that examples of international registry systems in which registration of security rights in intellectual property was possible would be useful for the completeness of the discussion on registration and coordination of registries. Subject to those changes, the Working

Group approved the substance of the section of the draft annex dealing with asset-specific intellectual property registries.

**3. Coordination of registries**

66. It was agreed that legislators should be invited to review their general security rights and intellectual property registration systems to ensure that they were compatible. It was also agreed that the text should cross-reference examples 2-5 set out in chapter I, section D, of the draft annex, since those examples dealt with the effects of registration in intellectual property registries and general security rights registries, as well as with the relationship between the two. Subject to those changes, the Working Group approved the substance of that section of the draft annex.

**4. Registration of notices about security rights in future intellectual property**

67. With respect to paragraph 21, it was suggested that the first sentence should refer to the registration of a “notice” about a security right in intellectual property.

68. With respect to paragraph 22, it was suggested that the text should discuss the possibility of recording security rights in intellectual property while the application for registration of intellectual property in the intellectual property registry was pending.

69. Subject to the changes mentioned above, the Working Group approved the substance of the section of the draft annex dealing with the registration of notices about security rights in future intellectual property.

**5. Dual registration or search**

70. With respect to paragraph 24, it was suggested that the text should include in the list of cases referring to exclusive registration in the general security rights registry for secured transactions purposes a fourth case dealing with situations in which registration of a security right in an intellectual property registry did not have third-party effects.

71. With respect to paragraph 25, it was suggested that the reference to the due diligence requirements applying “equally” to all types of movable assets should be toned down, since, while due diligence was in principle the same, its exact nature might to some extent depend on the exact type of asset involved in each case.

72. Subject to the changes mentioned above, the Working Group approved the substance of the section of the draft annex dealing with dual registration or search.

**6. Time of effectiveness of registration**

73. It was suggested that the section of the draft annex dealing with the time of effectiveness of registration should either be recast to deal only with third-party effectiveness issues, rather than with priority issues, or be moved to the section dealing with priority. It was stated that a question relating to the time of third-party effectiveness might arise because of a difference in the time of effectiveness of a registration in the general security rights registry and in the relevant intellectual property registry.

74. Subject to the recasting of the section to deal with the time of effectiveness of registration in the general security rights registry and in the relevant intellectual property registry rather than with priority issues, the Working Group approved the substance of that section of the draft annex.

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

75. With respect to paragraph 28, it was suggested that the third option should be further explained by reference to the fact that the secured creditor would not need to register an amendment identifying the new transferee and that the transferee would acquire the encumbered asset subject to the security right.

76. With respect to paragraph 30, it was suggested that the text should be recast to avoid inadvertently giving the impression that, with regard to security rights in intellectual property, the draft annex recommended that a State should take with respect to encumbered intellectual property a different decision from the decision made with respect to other types of encumbered asset as to the issues identified in recommendation 62 of the Guide.

77. However, the concern was expressed that, if the third option mentioned in paragraph 28 did not become the recommended approach with respect to security rights in intellectual property, a secured creditor would have to register amendments each time the encumbered intellectual property became the subject of an unauthorized transfer, licence or sub-licence, at the risk of losing its security right if it were not informed and had not acted promptly. In particular, with respect to licences and sub-licences, it was stated that, if the secured creditor had not authorized a licence and enforced its security right, enforcement would result in termination of the licence and any sub-licence, which would make all the “licensees” infringers. In that connection, it was observed that, as the Working Group had agreed, the third-party effectiveness of a security right in intellectual property against infringers should be left to intellectual property law.

78. In response, it was stated that, at least in the case of intellectual property with respect to which there was a specialized registry, the transferee would have to register the transfer and the secured creditor could be informed. It was also observed that recommendation 62 of the Guide applied only to transfers and that licences did not constitute transfers under the Guide. However, as the characterization of a licence was a matter of intellectual property law, it was pointed out that if a certain type of licence (e.g. an exclusive licence) was treated as a transfer under intellectual property law, that treatment under intellectual property law would result in the treatment of that licence as a transfer under the Guide as well. In that connection, it was mentioned that the general recommendations should apply to protect ordinary-course-of-business transfers or licences, and thus it would be up to each enacting State to choose one of the three alternatives discussed in paragraph 28 (see paras. 97-100 below).

79. Subject to the changes mentioned in paragraphs 75 and 76 above, the Working Group approved the substance of the section of the draft annex dealing with the impact of a transfer of encumbered intellectual property on the effectiveness of registration.

## 8. Registration of security rights in trademarks

80. The Working Group engaged in a discussion of the recommendations made by the International Trademark Association concerning the registration of security rights in marks (i.e. trademarks and service marks) with a view to determining their compatibility with the Guide.

81. It was stated that the recommendations made in paragraphs 32 (a), (b), (f) and (g), dealing with third-party effectiveness of a security right in a mark, were compatible with the Guide in that they promoted the objectives of transparency and registration in a specialized registry or a general security rights or other commercial registry. In response to a question, it was noted that the recommendations did not deal with priority, but left that matter to national law. It was agreed that that approach would be compatible with the Guide, the provisions of which, when enacted, would be national law.

82. It was also observed that the recommendation in paragraph 32 (c), providing that the creation of a security right in a mark did not result in a transfer of the mark or confer upon the secured creditor the right to use the mark, was also compatible with the Guide. In that connection, it was said that, in the case of enforcement, the secured creditor could sell, but not use, the mark. It was also pointed out, with respect to the recommendation in paragraph 32 (l), that if the secured creditor could not use the mark and the insolvency representative did not use it either, the mark could be lost. In response, it was stated that the secured creditor had a right, but no obligation, to maintain the mark, and the concept of the “excusable non-use” of a mark could result in the preservation of the mark in the case of non-use because of insolvency of the rights holder.

83. In addition, it was observed that the recommendation in paragraph 32 (d) was compatible with the Guide in that it set forth a default rule for the rights of the parties within the limits of the applicable law. As to the recommendation in paragraph 32 (e), it was said that the recommendation was compatible with the Guide to the extent it emphasized the importance of valuation of marks without suggesting any particular system of valuation. With respect to the recommendation in paragraph 32 (h), it was stated that the recommendation was compatible with the Guide in that it recommended the filing of a notice even in relation to mark registries. In response to a question, it was noted that the recommendations did not apply to marks that were not registrable. In response to another question, it was noted that the reference to “the date of the security right” was a reference to the effectiveness of the security right between the parties and not against third parties.

84. As to the recommendations in paragraphs 32 (i), (j) and (k), it was observed that the recommendations were compatible with the Guide in the sense that they provided for efficient enforcement mechanisms and registration of court judgements or administrative enforcement decisions. As to the recommendation in paragraph 32 (m), subject to approval by the appropriate Government authorities, it was stated that it was compatible with the recommendations of the Guide with respect to efficient registration procedures.

85. After discussion, the Working Group agreed that the recommendations on the registration of security rights in marks should be retained. As to the presentation of the recommendations, the Working Group agreed that, while paragraph 31 should be retained in the section of the draft annex dealing with registration of security rights

in trademarks, the recommendations in paragraph 32 should be placed in the relevant sections of the draft annex.

## **F. Priority of a security right in intellectual property**

### **1. The concept of priority**

86. With respect to paragraph 33, it was suggested that the statement about a second transferee obtaining a transfer from a rights holder that had already transferred its rights should be toned down as, in some States, a second transferee might be protected as a good-faith purchaser. Subject to that change, the Working Group approved the substance of the section of the draft annex dealing with the concept of priority.

### **2. Identification of competing claimants**

87. With respect to paragraph 34, it was suggested, that in the light of the previous discussion of the Working Group (see para. 20 (d) above), the reference to “infringers” should be deleted from the discussion of competing claimants. It was also suggested that, in the third sentence, the reference to the principle of deference to intellectual property law should be expressed in a separate sentence together with the idea that it would apply only where there was a different rule that applied “specifically” to security rights in intellectual property. It was also suggested that duplication should be avoided with the terminology section. Subject to those changes, the Working Group approved the substance of the section of the draft annex dealing with identification of competing claimants.

### **3. Relevance of knowledge of prior transfers or security rights**

88. With respect to paragraph 36, it was suggested that the word “generally” should be added before the word “irrelevant”. It was also suggested that, in the second sentence, the words “notice of it” should be replaced by the words “notice of the later-created security right”. In addition, it was suggested that the statement about deference to law relating to intellectual property should be deleted as knowledge-based priority rules did not apply specifically to intellectual property but to all assets in general. That suggestion was objected to on the grounds that that matter should be left to intellectual property law. After discussion, it was agreed that language should be added that qualified the application of the principle of deference to intellectual property law by reference to the existence of knowledge-based priority rules that were specific to intellectual property. Subject to those changes, the Working Group approved the substance of the section of the draft annex dealing with the relevance of knowledge of prior transfers or security rights.

### **4. Priority of a security right registered in an intellectual property registry**

89. With respect to paragraph 37, it was suggested that the text should clarify that the Guide referred to specialized registration systems only to the extent that they permitted registration of security rights and that such registration had third-party effects. With respect to paragraph 39, it was suggested that the paragraph might not be necessary, since, if no registration took place, a security right would not be effective against third parties and paragraph 40 would be sufficient. Subject to those

changes, the Working Group approved the substance of the section of the draft annex dealing with the priority of a security right registered in an intellectual property registry.

**5. Priority of a security right that is not registrable in an intellectual property registry**

90. With respect to paragraph 42, it was suggested that the text should refer to recommendation 13 of the Guide, pursuant to which the grantor ought to have rights in the asset to be encumbered or the power to encumber it for the secured creditor to acquire a security right. It was also suggested that reference should be made to intellectual property law in some States that allowed the acquisition of a security right by a person that had no knowledge that the grantor did not have rights in the asset to be encumbered. Subject to those changes, the Working Group approved the substance of the section of the draft annex dealing with the priority of a security right that is not registrable in an intellectual property registry.

**6. Rights of transferees of encumbered intellectual property**

91. The Working Group approved the substance of the section of the draft annex dealing with the rights of transferees of encumbered intellectual property.

**7. Rights of licensees in general**

92. Differing views were expressed as to whether a licensee of encumbered intellectual property could take a licence free of a security right that was created by a rights holder and was made effective against third parties before the granting of the licence. One view was that the licence needed to be authorized to do so by the secured creditor in the security agreement. Otherwise, the secured creditor could consider the granting of a licence an event of default and enforce its security right by collecting the royalties or selling the licence. Another view was that the secured creditor could be protected in two ways: it could register its security right in the encumbered intellectual property or it could agree with the grantor that the secured creditor would become the rights holder (i.e. become a transferee), if permitted under intellectual property law. In the former case, a subsequent licensee would take the licence subject to the security right with the result that, in the event of default, the secured creditor could enforce its security right and either collect the royalties owed under the licence agreement or sell the licence. In the latter case, any licence given by the grantor of the security right would be unauthorized and constitute an event of both default and infringement.

93. There was general agreement as to the principle that a licensee should take a licence in encumbered intellectual property subject to a security right that was created by the licensor and was effective against third parties at the time the licence was granted. In addition, there was general agreement that a licensee should take the licence free of the security right if the secured creditor had authorized the licence free of the security right. Differing views were expressed, however, as to whether an ordinary-course-of-business non-exclusive licensee should also take the licence free of the security right (see paras. 97-100 below).

94. With respect to paragraphs 45 and 46, it was suggested that the text should clarify that enforcement of a security right in licensed intellectual property that was

effective against third parties could result in the transfer of the licensed intellectual property and thus in the termination of the licence, rather than in the secured creditor being able to terminate a licence agreement to which it was not a party.

95. With respect to paragraph 46, it was suggested that the text should clarify that the mere fact that a rights holder created a security right in its intellectual property did not preclude the rights holder from granting licences. In addition, it was stated that, in order for a clause of the security agreement precluding the rights holder from granting any licences to have effects on third-party licensees, it would need to be registered. In response, it was noted that many intellectual property registries did not provide for registration of security rights, and the general security rights registry under the Guide was not set up in such a way as to accommodate registration of security agreements or various clauses of security agreements. It was also observed that whether or not a licence was authorized was a matter of intellectual property law.

96. Subject to the changes mentioned above and the discussion of the rights of ordinary-course-of-business non-exclusive licensees (see paras. 97-100 below), the Working Group approved the substance of the section of the draft annex dealing with the rights of licences in general.

#### **8. Rights of ordinary-course-of-business non-exclusive licensees**

97. Differing views were expressed as to whether an ordinary-course-of-business non-exclusive licensee would take the licence free of or subject to a security right that was created by the licensor and was effective against third parties at the time the licence was granted.

98. One view was that such a licensee should take the licence subject to the security right (meaning that, in case of default and enforcement, the licence would terminate unless other arrangements had been made with the secured creditor). It was stated that, in a number of jurisdictions, the concept of an “ordinary-course-of-business” transaction was unknown and difficult to apply. In addition, it was observed that the concept of an ordinary-course-of-business licence had no precedent in intellectual property law, making it difficult to distinguish an ordinary-course-of-business licence from a non-ordinary-course-of-business licence. The example was given of trademark licences, in respect of which that concept would be extremely problematic. Moreover, it was said that the ordinary-course-of-business concept did not give unauthorized licensees a valid defence. It was also pointed out that often licences were mixed, in that they included both exclusive and non-exclusive rights. It was also mentioned that use of those concepts was not necessary as current intellectual property law already addressed that issue in an appropriate manner by leaving it to the parties to the security agreement. In that connection, it was stated that if the secured creditor wanted the grantor to grant licences, it would authorize all licences or at least those that met certain criteria. In any case, licensees would conduct appropriate due diligence to determine whether a licence had been acquired free of a prior security right.

99. Another view was that an ordinary-course-of-business non-exclusive licensee should take the licence free of the security right (meaning that, in the event of default and enforcement, the licence could nonetheless continue). It was stated that the ordinary-course-of-business concept was a simple and practical concept that was

widely known and used. In addition, it was observed that the main purpose for the use of that concept was to protect everyday, legitimate transactions, such as the off-the-shelf purchase of copyrighted software. It was pointed out that, in such transactions, purchasers should not have to do a search in a registry or acquire the software subject to security rights created by the software developer or its distributors. In addition, it was observed that the ordinary-course-of-business concept had nothing to do with the relationship between the licensor and the licensee, and was in no way meant to suggest that the licensee would get a licence free of the terms and conditions of the licence agreement and the law applicable to it. Moreover, it was said that if the secured creditor wanted to discourage non-exclusive licences, it could, in its security agreement (or elsewhere), require the borrower (the licensor) to place in all of the non-exclusive licences a provision that the licence would terminate if the licensor's secured creditor enforced its security right. Similarly, if the licensor did not want its licensee to grant any sub-licences, it could include in the licence agreement a provision whereby the granting of a sub-licence by the licensee would be an event of default under the licence agreement that would entitle the licensor to terminate the licence. It was stated that nothing in the Guide would interfere with the enforcement of such provisions as between the secured creditor and its borrower, or as between the licensor and its licensee. It was observed that normally the secured creditor would have no interest in doing so, since the licensor would be in the business of granting non-exclusive licences, and the secured creditor would expect the borrower to use the fees paid under those licence agreements to pay the secured obligation.

100. After discussion, it was agreed that, in some cases (e.g. in the case of an off-the-shelf sale or licence of software), licensees should take the licence free of a security right created by the licensor. While willingness was expressed to formulate a recommendation that would bring about that result, possibly on the basis of concepts such as authorization or implied authorization, it was generally found to be difficult to formulate such a recommendation in the abstract without referring to specific examples. The Working Group thus requested the Secretariat to include in the next version of the draft annex examples indicating how intellectual property law addressed the relevant issue, and proposals for a possible recommendation to be included in the draft annex and for commentary referring the matter, in line with recommendation 4, subparagraph (b), of the Guide, to law that applied specifically to intellectual property.

**9. Priority of a security right granted by a licensor as against a security right granted by a licensee**

101. After discussion, the Working Group approved the substance of the section of the draft annex dealing with the priority of a security right granted by a licensor as against a security right granted by a licensee.

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

102. After discussion, the Working Group approved the substance of the section of the draft annex dealing with the priority of a security right in intellectual property as against the right of a judgement creditor.

## **11. Subordination**

103. After discussion, the Working Group approved the substance of the section of the draft annex dealing with subordination.

## **G. Rights and obligations of the parties to a security agreement relating to intellectual property**

### **1. Application of the principle of party autonomy**

104. After discussion, the Working Group approved the substance of the section of the draft annex dealing with the application of the principle of party autonomy.

### **2. Right of the secured creditor to pursue infringers or renew registrations**

105. Some doubt was expressed as to whether the section of the draft annex dealing with the right of the secured creditor to pursue infringers or renew registrations should be retained. In response, it was noted that, like the relevant chapter in the Guide, the section was intended to list some issues that the parties might wish to address in the security agreement and to provide some rules that would be applicable in the absence of contrary agreement of the parties and would reflect the normal expectations of the parties.

106. As to the content of that section, the view was expressed that the content should be broadened to deal in general with the management of the encumbered intellectual property. In that connection, it was stated that the section contained an indicative list of issues that the parties might wish to address without excluding other issues within the limits of party autonomy set by intellectual property law.

107. With respect to the recommendations contained in the note to paragraph 63, it was agreed that the first was appropriate in that it referred to the agreement of the parties and should thus be retained. As to the second recommendation, both support and criticism were expressed. In support, it was stated that the recommendation reflected the normal expectations of the parties. In opposition, it was observed that, in the absence of an agreement of the parties permitting the secured creditor to pursue infringers or renew registrations, such a recommendation was not appropriate. The Working Group thus decided that the second recommendation should be retained, but within square brackets, for further consideration at a future meeting.

108. Subject to the changes mentioned above, the Working Group approved the substance of that section of the draft annex.

## **H. Rights and obligations of third-party obligors in intellectual property financing transactions**

109. With respect to paragraph 64, it was suggested that the text should clarify that a licensee as the debtor of the royalties owed under the licence agreement had the rights and obligations of a third-party obligor. Subject to that change, the Working Group approved the substance of the section of the draft annex dealing with the

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

## **I. Enforcement of a security right in intellectual property**

### **1. Intersection of secured transactions law and intellectual property law**

110. With respect to paragraph 66, it was suggested that the text should clarify that the United Nations Assignment Convention and the Guide dealt with the assignment of receivables rather than receivables in general.

111. With respect to paragraph 67, it was suggested that the last sentence should clarify that the application of intellectual-property-specific enforcement rules in the general law of civil procedure would be preserved.

112. Subject to the changes mentioned above, the Working Group approved the substance of the section of the draft annex dealing with the intersection of secured transactions law and intellectual property law.

### **2. Enforcement of a security right in different types of intellectual property**

113. After discussion, the Working Group approved the substance of the section of the draft annex dealing with the enforcement of a security right in different types of intellectual property.

### **3. Taking “possession” of encumbered intellectual property**

114. With respect to paragraph 71, it was suggested that the text should include a cross reference to the definition of the term “possession” to clarify that actual possession was meant.

115. With respect to paragraph 72, it was suggested that, for consistency in terminology, reference should be made to a “transfer” rather than to a “sale” of encumbered intellectual property.

116. Subject to the changes mentioned above, the Working Group approved the substance of the section of the draft annex dealing with taking “possession” of encumbered intellectual property.

### **4. Disposition of encumbered intellectual property**

117. With respect to paragraph 73, it was suggested that, to clarify that the assignment of the encumbered intellectual property was the result of the enforcement process rather than of a right of the secured creditor as a rights holder, the words “to assign” should be replaced by the words “to effectuate the assignment”. Subject to that change, the Working Group approved the substance of the section of the draft annex dealing with the disposition of encumbered intellectual property.

### **5. Rights acquired through disposition of encumbered intellectual property**

118. With respect to paragraph 75, it was suggested that the statement in the last sentence that the secured creditor did not become a rights holder as a result of the

enforcement process should be toned down, as the secured creditor could acquire the encumbered intellectual property in the context of enforcement. Subject to that change, the Working Group approved the substance of the section of the draft annex dealing with the rights acquired through disposition of encumbered intellectual property.

**6. Proposal by the grantor to accept the encumbered intellectual property**

119. With respect to paragraph 78, fifth sentence, it was suggested that, to avoid giving the impression that registration was a mandatory requirement, the text should be revised to clarify that the secured creditor should register in order to enjoy the benefits resulting from registration. Subject to that change, the Working Group approved the substance of the section of the draft annex dealing with the proposal by the grantor to accept the encumbered intellectual property.

**7. Collection of royalties and licence fees**

120. With respect to paragraph 79, it was suggested that the text should clarify that the Guide incorporated the principles of the United Nations Assignment Convention with regard to assignments of receivables. Subject to that change, the Working Group approved the substance of the section of the draft annex dealing with the collection of royalties and licence fees.

**8. Licensor's other contractual rights**

121. After discussion, the Working Group approved the substance of the section of the draft annex dealing with a licensor's other contractual rights.

**9. Enforcement of security rights in tangible assets related to intellectual property**

122. With respect to paragraph 81, it was suggested that the text should clarify the exhaustion doctrine by referring to an "intellectual property right" rather than to "intellectual property", as it is the right that would be exhausted and not the property, and by a more specific reference to "first marketing or sale" rather than the general reference to "first use". Subject to those changes, the Working Group approved the substance of the section of the draft annex dealing with the enforcement of security rights in tangible assets related to intellectual property.

**10. Enforcement of a security right in a licensee's rights**

123. Subject to the making of the same change in paragraph 86 as in paragraph 78 (see para. 119 above), the Working Group approved the substance of the section of the draft annex dealing with the enforcement of a security right in a licensee's rights.

**J. Law applicable to a security right in intellectual property**

**1. Law applicable to proprietary matters**

124. It was agreed that alternative C in paragraph 97 should be deleted. It was widely felt that, by referring to the law of the State under whose authority the registry was maintained, alternative C would introduce uncertainty as to the law

applicable or, at least, increase the time and cost of a transaction, since a secured creditor would need to undertake a search to identify the relevant registry in which the intellectual property to be encumbered was registered.

125. It was widely felt that both alternative A and alternative B had advantages and disadvantages. In favour of alternative A, it was stated that the law of the State in which protection of the intellectual property was sought (*lex protectionis*) was the law applicable to ownership rights under intellectual property law. It was also stated that, by referring to the *lex protectionis*, alternative A would result in the application to a priority conflict between a transferee and a secured creditor of the same law that would apply to a priority conflict between two secured creditors. At the same time, it was observed that alternative A presented the disadvantage that a secured creditor would have to register in multiple jurisdictions, a result that was likely to increase the transaction cost. It was also observed that alternative A did not make reference to regional organizations that provided regional registration systems.

126. In favour of alternative B, it was observed that, by referring to the law of the grantor's location, the approach would result in the application of a single law to the creation, third-party effectiveness, priority and enforcement of a security right. It was stated that, to avoid referring a priority conflict between a transferee and a secured creditor to two different laws (i.e. to the *lex protectionis* and to the law of the grantor's location), alternative B referred that priority conflict to the *lex protectionis*. It was also observed that alternative B was useful in that other priority conflicts, including a priority conflict with the insolvency representative, would be referred to the law of the grantor's location, that is, the law of the assignor's centre of main interests (i.e. the real, rather than the statutory, seat). To avoid introducing to alternative B the problems of alternative C referred to above (see para. 124), the Working Group agreed that the bracketed text in alternative B should be deleted.

127. While the view was expressed that both alternatives might be retained in the final text of the annex, the Working Group agreed that every effort should be made to reach agreement on one recommendation, with the advantages and disadvantages of each alternative being discussed in the commentary. In order to facilitate future discussions, the Secretariat was requested to set out practical examples against which the alternatives could be tested, and to further develop in the commentary the comparative advantages and disadvantages of the two alternatives. The Working Group also agreed that cooperation with the Hague Conference on Private International Law and the European Commission would be particularly welcome and requested the Secretariat to continue its efforts to ensure such cooperation and coordination.

## **2. Law applicable to contractual matters**

128. After discussion, the Working Group approved the substance of the section of the draft annex dealing with the law applicable to contractual matters.

## K. The impact of insolvency on a security right in intellectual property

129. During the session, it was stated that the issues to be referred to Working Group V pursuant to the decision of the Commission<sup>12</sup> presented four possible scenarios (see para. 23 (f) above), depending on whether (a) it was the licensor or licensee that had granted a security right in its rights under the licence; and (b) it was the licensor or licensee with respect to whom insolvency proceedings had been instituted. The questions that might be raised with respect to the effects of an insolvency proceeding on the rights of the secured creditor in each of those scenarios were considered, together with possible answers (see annex to the present report). The questions were felt to address as well the effects of a continuation or rejection of the licence contract in the case of an insolvency proceeding of a party to the licence contract. Moreover, the questions assumed that the circumstances were such that, pursuant to recommendations 69-86 of the *UNCITRAL Legislative Guide on Insolvency Law*,<sup>13</sup> the insolvent debtor might choose to continue or to reject the licence contract. It was mentioned that the questions did not address other issues that might arise, such as the effect of a stay on proceeding, possible legal limitations on the ability of the licensee to assign its rights under the licence, the effect of anti-assignment provisions in the licence contract, ipso facto clauses, unsecured claims for damages upon rejection of the licence contract, or whether the licensee had “vested rights” that it retained following a rejection of the licence contract. It was observed that those issues were generally addressed in the *UNCITRAL Legislative Guide on Insolvency Law*.

130. It was suggested that Working Group VI should ask Working Group V to consider an additional issue concerning the rights of a licensee of intellectual property when insolvency proceedings were instituted with respect to the licensor.

131. In that connection, it was stated that when insolvency proceedings were instituted with respect to a licensor of intellectual property, the licensor or its insolvency representative was entitled to decide to reject the licence contract (see recommendations 69-86 of the *UNCITRAL Legislative Guide on Insolvency Law*). It was observed that, very often, rejection would deprive the licensee of the benefits of a favourable licence contract and, thus, not only adversely affect the licensee but also, if the licensee had granted a security right in its rights under the licence, adversely affect the rights of the licensee’s secured creditor. In addition, it was said that while, pursuant to recommendation 82 of the *UNCITRAL Legislative Guide on Insolvency Law*, the licensee might have an unsecured claim to damages as a result of the rejection, it was unlikely that such damages would be recovered in full; thus, the claim to damages might mitigate the adverse effect but would not eliminate it.

132. It was pointed out that one way in which the insolvency laws of some States addressed that issue was to allow the licensee of certain kinds of intellectual property to elect to continue using the intellectual property under the licence contract, even if the licensor or its insolvency representative rejected the licence contract. In such a case, the licensee was obliged to comply with all terms of the

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<sup>12</sup> *Official Records of the General Assembly, Sixty-third Session, Supplement No. 17 (A/63/17)*, para. 326.

<sup>13</sup> United Nations publication, Sales No. E.05.V.10.

licence contract, including the payment of royalties due under the licence contract. However, it was mentioned that the licensor's insolvency estate would be relieved from ongoing obligations with respect to the licence contract, such as providing improvements. As a result, it was argued, the only obligation imposed upon the licensor was the obligation to continue honouring the intellectual property licence, an obligation that did not impose upon the resources of the licensor. It was noted that that approach had the effect of balancing the interest of the insolvent licensor to escape a burdensome contract and the interest of the licensee to protect its investment in the licence. In providing some protection for the licensee's interest, that approach was also said to provide some protection for the secured creditor of the licensee.

133. It was suggested that the annex to the UNCITRAL Legislative Guide on Secured Transactions should point out that a State might wish to consider including in its law a provision such as the one discussed above that would permit the licensee to continue to enjoy its rights under the licence contract in the event that the licensor was in insolvency proceedings and rejected the licence.

134. It was observed that the provisions of the *UNCITRAL Legislative Guide on Insolvency Law* should be carefully reviewed to ensure that the matters not addressed in the questions considered at the session were sufficiently addressed in that Guide. It was widely felt that the matters addressed in those questions and in the preceding paragraphs required careful consideration, in particular because the efficiency of security rights depended on whether those rights could withstand the test of insolvency and because several States were currently considering revising their laws to address those matters.

135. It was also suggested that the draft annex should address additional issues. In support of that suggestion, it was stated that there were two sets of conflicting interests that might arise in the event of the insolvency of a licensor that had granted a security right over a licensed intellectual property right. It was observed that, on the one hand, the secured creditor might seek to sell as rapidly as possible the intellectual property right that was the object of the security right, and recover the amount owed to it from the proceeds of the sale of that right, especially when the stream of royalties was not certain or guaranteed (e.g. by means of an insurance policy).

136. On the other hand, the insolvency representative might oppose the immediate termination of the licence contract and consequent sale in the belief that the continuation of the performance of the licence contract could produce better results in maximizing the value of the encumbered intellectual property right.

137. In that context, it was mentioned that the law of some States established that the secured creditor had a right to request the insolvency representative or the insolvency court, if necessary, to set a legally binding deadline for the decision to continue or not the performance of the licence contract; and to schedule a special hearing before the insolvency court, to attempt mediation between the insolvency representative and the secured creditor in order to obtain further protection for the secured obligation.

138. It was pointed out that the result mentioned in paragraph 137 (b) above might be achieved in various different ways, including through the provision of insurance

for the future royalties arising from the licence contract or through the upfront payment of part of the secured obligation.

139. There was support in the Working Group for all the suggestions mentioned in paragraphs 129-138 above. It was widely felt that the suggestions should be referred to Working Group V and, subject to further consideration by both working groups, the result should be reflected in the next version of the draft annex.

140. The Working Group decided that the matters mentioned in paragraphs 129-138 above (which include those raised in the questions contained in the annex) should be referred to Working Group V and that, subject to further consideration by both working groups, the result should be reflected in the next version of the draft annex.

## V. Future work

141. Before concluding its session, the Working Group engaged in a discussion of its future work. In that connection, the Working Group discussed a suggestion that guidance should be given to secured creditors accepting intellectual property as security for credit, in particular in relation to licensing practices. It was widely felt that while some discussion could be usefully included in the draft annex, the matter was sufficiently important and broad to be considered as a new project. It was stated that such a project could be aimed at a guide that would provide guidance to parties to secured transactions and guidance on the impact of licensing practices. Examples of similar work mentioned included the current work of the Commission on the revision of the UNCITRAL Model Law on Procurement of Goods, Construction and Services, which could include guidance for users other than legislators and regulators (see A/CN.9/615, para. 14), as well as past work of the Commission on the *UNCITRAL Legal Guide on Drawing Up Contracts for the Construction of Industrial Works*.<sup>14</sup> The Working Group agreed that some brief discussion of the matter should be included in the next version of the draft annex. The Working Group also agreed that the matter should be considered in due course as part of a discussion of its future work.

142. As to its future work on the draft annex, the Working Group noted that its fifteenth session was scheduled to be held in New York from 27 April to 1 May 2009. As the thirty-sixth session of Working Group V was scheduled to be held in New York from 18 to 22 May 2009, it was noted that it would probably not be possible to hold in early 2009 a joint session of the two working groups to consider the impact of insolvency on a security right in intellectual property, as originally envisaged by the Commission at its forty-first session.<sup>15</sup> It was also noted that the sixteenth session of Working Group VI was tentatively scheduled to be held in Vienna from 7 to 11 December 2009, those dates being subject to confirmation by the Commission at its forty-second session (Vienna, 29 June-17 July 2009), while the thirty-seventh session of Working Group V was tentatively scheduled to be held in Vienna from 5 to 9 October 2009, those dates also being subject to confirmation by the Commission.

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<sup>14</sup> United Nations publication, Sales No. E.87.V.10.

<sup>15</sup> *Official Records of the General Assembly, Sixty-third Session, Supplement No. 17 (A/63/17)*, para. 326.

143. In that connection, the Working Group agreed that the sessions of the two working groups to be held in the second half of 2009 should be scheduled in a way that would make it possible to hold a joint session, should such a joint session prove to be necessary. It was widely felt that every effort should be made to conclude discussion on the impact of insolvency on a security right in intellectual property as soon as possible, so that the result of that discussion could be reflected in the draft annex by late 2009 or early 2010. In that connection, the Working Group felt that it should be able to complete its work on the draft annex at its sixteenth session (late 2009) or at its seventeenth session (early 2010) in order to submit the draft annex to the Commission for final approval and adoption at its forty-third session, in 2010.

## Annex

## Effects of an insolvency proceeding on the rights of a secured creditor in four different scenarios

<i>Licensor is insolvent</i>	<i>Licensee is insolvent</i>
<p><i>Licensor grants a security right in its rights under a licence contract (primarily the right to receive royalties)</i></p>	<p><i>Licensee is insolvent</i></p>
<p><b>Question:</b> What happens if the licensor or its insolvency administrator decides to continue the performance of the licence contract under the insolvency law (see recommendations 69-86 of the <i>UNCITRAL Legislative Guide on Insolvency Law</i>)?<sup>a</sup></p> <p><b>Answer:</b> The licensee continues to owe royalties under the licence contract and the secured creditor of the licensor continues to have a security right both in the licensor's right to royalties under the licence contract and in the proceeds of that right, in other words, any royalty payments that are paid.</p> <p><b>Question:</b> What happens if the licensor or its insolvency administrator rejects the licence contract under the insolvency law (see recommendations 69-86 of the <i>UNCITRAL Legislative Guide on Insolvency Law</i>)?</p> <p><b>Answer:</b> The licensee does not owe royalties under the licence contract 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 contract.</p>	<p><b>Question:</b> What happens if the licensee or its insolvency representative decides to continue the performance of the licence contract under the insolvency law (see recommendations 69-86 of the <i>UNCITRAL Legislative Guide on Insolvency Law</i>)?</p> <p><b>Answer:</b> The licensor continues to have a right to receive royalties under the licence contract 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 contract and in the proceeds of that right, in other words, any royalty payments that are made.</p> <p><b>Question:</b> What happens if the licensee or its insolvency administrator rejects the licence contract under the insolvency law (see recommendations 69-86 of the <i>UNCITRAL Legislative Guide on Insolvency Law</i>)?</p> <p><b>Answer:</b> The licensee does not continue to owe royalties under the licence contract 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 contract.</p>
<p><i>Licensee grants a security right in its rights under a licence contract (primarily the right to use the intellectual property)</i></p>	<p><i>Licensee is insolvent</i></p>
<p><b>Question:</b> What happens if the licensor decides to continue the performance of the licence contract under the insolvency law (see recommendations 69-86 of the <i>UNCITRAL Legislative Guide on Insolvency Law</i>)?</p> <p><b>Answer:</b> The licensee continues to have rights under the licence contract and the secured creditor of the licensee continues to have a security right in those rights under the licence contract.</p> <p><b>Question:</b> What happens if the licensor or its insolvency administrator rejects the licence contract under the insolvency law (see recommendations 69-86 of the <i>UNCITRAL Legislative Guide on Insolvency Law</i>)?</p> <p><b>Answer:</b> The licensee does not have rights under the licence contract 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.</p>	<p><b>Question:</b> What happens if the licensee decides to continue the performance of the licence contract under the insolvency law (see recommendations 69-86 of the <i>UNCITRAL Legislative Guide on Insolvency Law</i>)?</p> <p><b>Answer:</b> The licensee continues to have rights under the licence contract and the secured creditor of the licensee continues to have a security right in those rights under the licence contract.</p> <p><b>Question:</b> What happens if the licensee or its insolvency administrator rejects the licence contract under the insolvency law (see recommendations 69-86 of the <i>UNCITRAL Legislative Guide on Insolvency Law</i>)?</p> <p><b>Answer:</b> The licensee does not have rights under the licence contract with respect to periods after rejection, but retains 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.</p>

<sup>a</sup>United Nations publication, Sales No. E.05.V.10.