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2016 – Study Question (General)

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Security interests over intellectual property

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I. Current law and practice

You are reminded that **IPRs** refers to patents, trademarks and registered designs only.
If more than one type of security interest is available under your Group's current law, please answer the questions for each type of security interest, as applicable.

Availability of security rights

1) Does your Group's current law provide for the possibility of creating security interests over IPRs?

yes

Please explain:

It is possible to create security rights over IPRs. In Luxembourg, the appropriate term would be "security rights" (*sûretés réelles*) as Luxembourg law does not know the substance over form approach used in the context of "security interests".

The following legal mechanisms can be used for that purpose:

- the pledge (*gage*) (as further explained below);
- the fiduciary contract (*contrat fiduciaire*) (as further explained below); and
- the pledge over a business universality (*gage sur fonds de commerce*) (as further explained below).

If yes, please answer Questions 2) to 14) inclusive before proceeding to question 15) and following.
If no, please proceed directly to question 15).

- 2) Are the available types of security interests defined by specific provisions relating to security interests over IPRs or by general commercial law principles (e.g. specific provisions in your Group's patent legislation rather than general commercial provisions that are applicable to tangible personal property as well as to patents)?

yes

Please explain:

Certain legal texts specifically applicable to IPRs make reference to the concept of pledge. However, such security rights are not regulated in further detail by those legal texts (other than in the case of patents). Therefore, the general commercial provisions apply to security rights over IPRs.

- 3) Under your Group's current law, what types of security interests are available for IPRs? In addressing the questions in sub-paragraphs a) to c) below, please specify briefly the main characteristics and differences of the available types of security interests.

- a) Does your law provide for security interests which are characterized by the full assignment of the underlying IPR to the security taker? For example, an assignment of the IPR for the purpose of security or authorization to dispose/use fully in the event of default.

yes

Please explain:

The types of security rights available for IPRs are (1) the pledge (*gage*), (2) the fiduciary transfer (*contrat fiduciaire*) and (3) the pledge over business universality (*gage sur fonds de commerce*).

The Pledge

The most classical security right in the context of IPR is the pledge (*gage*). The pledge is governed either by the Luxembourg Civil Code or the Commercial Code, the distinction between the two being the nature of the secured debt (i.e. civil or commercial, depending on whether the debtor is a private individual or a company). A pledge in IPRs does not as such encumber the proceeds from exploiting the IPRs (such as license fees, equitable remunerations, royalties or other compensation). Such proceeds may however be captured by a pledge agreement governed by the Luxembourg Act of 5 August 2005 on financial collateral arrangements, as amended.

A pledge is created by way of delivery (*dépossession*) of IPRs in respect of which the pledge is granted. Delivery can be actual or constructive. When pledging intangible movables (such as IPRs), delivery is usually deemed to take place by means of a notification or registration. In order to be effective against third parties (perfection), a pledge over IPRs must be registered with the Benelux Office of Intellectual Property (for Benelux trademarks and designs), the EU IPO (for EU trademarks and designs), the European Patent Office (for European patent applications) or the national patent registers (for national patent applications and granted patents). Such registrations will satisfy the above mentioned delivery requirement.

Any security right with respect to future IPRs will in principle be considered as a promise to pledge (*promesse de gage*). However, the Luxembourg Act of 20 July 1992 modifying the regime on invention patents (the "**Patent Act**") expressly provides for the possibility to pledge a patent application.

Title Transfer

A security right over an IPR may also be granted by way of title transfer by way of security (*transfert de propriété à titre de garantie*) to a licensed fiduciary (*fiduciaire*) under a fiduciary contract. In such a case, the ownership vests with a licensed fiduciary under the Act of 27 July 2003 ratifying the Hague Convention of 1 July 1985 relating to trust and its recognition and regulating fiduciary contracts (the

"**Trusts and Fiduciary Contracts Act**"). Following a title transfer, the licensed fiduciary holds the IPRs in its own name for the account of the secured beneficiaries. IPR collateral must be kept segregated from the licensed fiduciary's personal property or any other fiduciary property it may hold for the benefit of any other beneficiaries. The title transfer for security purposes to a licensed fiduciary is made by private agreement without any third party notification or any mandatory public registration which allows the fiduciary security right to remain entirely undisclosed.

Business Universality

A security provider may also grant security rights over IPRs in the context of a pledge over a going concern/business universality (*gage sur fonds de commerce*). The pledge is made public by its inscription to the mortgages register (*bureau de la conservation des hypothèques*). Due to high costs and burdensome administrative formalities, such pledge is not commonly put in place.

An outright assignment/title transfer of the IPR for security purposes is possible through a fiduciary contract (as mentioned above). Following an event of default, the transferred assets will vest with the fiduciary. In case of discharge of the secured obligations, the transferred assets will be returned to the security provider.

In cases not involving a licensed fiduciary, it is not possible under the Commercial Code or the Civil Code to transfer title for security purposes, given that these texts prevent a security taker from appropriating the pledged IPRs upon default (*pacte comissoire*). Enforcement of a civil pledge over IPRs will be made by judicial attribution or public auction upon the occurrence of a payment default and after a summons to pay (*mise en demeure*). Enforcement of a commercial pledge will be made through a public auction after a notified summons to pay (*mise en demeure*), it being understood that the modalities of the auction will be determined by a judge.

An exception applies in connection with patents. The Patent Act provides that enforcement of a pledge over patents will be made through an executory attachment (*saisie-exécution*). Upon an executory title (*titre exécutoire*) being granted to the security taker, the security taker will be allowed to seize the patent or the patent application and then sell the patent through a public auction. The forced sale (*vente forcée*) will then need to be inscribed in the patent register.

- b) Does your law provide for security interests that authorize the security taker to realize the security interest only in the event of default? For example, a pledge over an IPR that authorizes the pledgee to liquidate the pledged IPR in the event of default (but not to otherwise dispose of the IPR).

yes

Please explain:

Yes. It is possible to realize the pledge over IPRs upon the occurrence of a payment default; i.e. debt must be due and payable and subject to acceleration. In this case, the IPR may be realized either by way of sale (in case of a commercial pledge) or by way of judicial attribution (in case of a civil pledge) (see 2.(a) above).

- c) Does your law provide for security interests that authorize the security taker to use the underlying IPR? For example, *usus fructus* rights that authorize the creditor to use and/or realize proceeds from the exercise of the IPR only during the term of encumbrance. Is any right to use the encumbered IPR conditional upon default of the security provider?

no

Please explain:

It is in principle not possible under the statutory regime for a security taker to use the underlying IPR. However, based on general commercial and civil law principles, it is possible to provide for such right of use under the contract creating the security right. In case of express contractual provision, it would be possible for the creditor to use the underlying IPR even absent an event of default.

Under a fiduciary contract, the fiduciary will be able to use the encumbered IPR prior to default. The law does not include express provisions in this respect. It is understood that identical assets must be available for retransfer once the security right is terminated and title is transferred back to the security provider.

- 4) If more than one type of security interest is available under your Group's current law, what types are commonly used for IPRs? Please also specify if certain types of security interests are exclusively used for certain types of IPRs in your country. For example, patents may commonly be encumbered with pledges, while trademarks may commonly be assigned to the security taker.

In practice, the security right used in Luxembourg when seeking to encumber IPRs is the pledge (*gage*).

Effects of security interests

- 5) Is the security provider restricted in their right to use their IPR after providing a security interest over that IPR? For example, in respect of their right to grant licenses, or the right to use the protected subject matter. Please answer for each available type of security interest.

yes

Please explain:

In terms of terminology, we should clearly distinguish between a right "to use", i.e. the right to continue to exercise rights inherent to the IPR and the right "of use" (in financial collateral parlance) which means the right to transfer (assign, repledge, rehypothecate) the IPR as such. In terms of right "to use", the answer is yes, and the pledgor may in principle still use the IPR over which security has been taken. However, a pledgor is restricted in its right to use its IPR since it cannot contractually use the IPR for a different purpose than what has been agreed with the security taker. Similarly, the Patent Act expressly provides that the use of an invention by the holder of the patent application or patent is still possible despite the pledge over the patent.

A security provider using a fiduciary contract will be restricted in its right to use the IPR because the IPR has been delivered to the fiduciary.

- 6) May encumbered IPRs be assigned to third parties by the security provider?

yes

Please explain:

Yes. It is possible in principle for a security provider to assign the pledged IPRs, subject however to contractual arrangements to the contrary. However, the assignee will only obtain a flawed title because the assigned IPR will be pledged to the benefit of the security taker (please see 7.(b)).

For invention patents, the Patent Act provides that the inscription of a pledge renders void any subsequent assignment or pledge IPR without the consent of the security taker.

7) If yes:

a) under what conditions may an IPR be assigned (e.g. obligation to obtain consent from the security taker, public notification or registration)?

Such possibility depends largely on what has been agreed contractually. Only the Patent Act explicitly provides that inscription of a pledge renders void any subsequent assignment or pledge of IPR without the consent of the security taker

b) does the IPR remain encumbered with the original security interest for the benefit of the security taker?

yes

Please explain:

The assigned IPR will not be assigned free of charge, i.e. the assigned IPR will remain encumbered by the pledge existing to the benefit of the security taker (*droit de suite*).

8) What are the rights of the security taker before default (e.g. entitlement to damages, injunctions against infringers, or license fees)?

In principle, a pledge does not confer any particular rights to the security taker before default. However, according to legal doctrine, it is possible to provide otherwise contractually and grant such rights in accordance with general civil law principles.

9) Who of the security provider or the security taker is responsible for maintenance and defence of the IPR provided as collateral?

As owner of the IPR, the security provider remains in principle responsible for the maintenance and defence of the IPR (subject to contractual arrangements). Additional covenants may be stipulated in the pledge agreement to this effect in order to protect the IPR.

10) What are the legal consequences if the underlying IPR expires or is revoked? For example, the security right lapses simultaneously; the creditor has a compensation claim against the security provider.

Upon expiry of the encumbered IPR, the pledge will extinguish. For the sake of clarity, the security taker should apply for discharge of the registration of the security right. The Benelux Convention on Intellectual Property provides for a mechanism avoiding the discharge of the IPR's registration.

Registration may only be discharged upon a joint request from both the IPR holder and the security taker.

It is possible to contractually provide that the security taker will be financially compensated in case the IPR lapses.

11) Can any of these effects of security interests over IPRs before default be modified by contractual provisions between the parties? If so, which effects?

no

Please explain:

Many effects of security rights over IPRs can be modified contractually as between the parties, as long as they are not contrary to public policy (*ordre public*). It is unlikely that effects concerning proprietary effects, effectiveness against third parties and priorities are subject to contractual freedom.

Applicable law

12) Does your Group's current law provide for conflicts of laws as to the availability and effect of security interests over IPR portfolios containing foreign as well as national IPRs?

no

Please explain:

13) Which national law applies as to creation, perfection and effect of security interests over foreign IPRs? For example, where a US patent is provided as collateral in respect of a financial transaction in Europe.

The creation of security rights over foreign IPRs is governed by the law chosen by the parties in accordance with Regulation (EC) No 593/2008 on the law applicable to contractual obligations (Rome I). Proprietary effects, effectiveness as against third parties and rules of priority are subject to general conflict of laws principles.

General conflict of laws rules regarding movable assets likely apply with regards to effectiveness as against third parties and the effect of foreign IPRs (including priority rules). As such, the *situs* rule (*lex rei sitae*) requires that the law of the place where IPRs are located applies. There are no express rules clarifying the location of IPRs, however it likely refers to the jurisdiction for which protection is sought, i.e. the state where the IPR is registered.

14) Can a choice of law provision in a security interest agreement over IPRs overrule the applicable law as to availability and effect?

no

Please explain:

No. Security rights are understood to operate within a closed system of property rights and preferential

rights (*numerus clausus*) as a result of which it is not possible to agree on property rights and effects of security rights that are not enumerated or dealt with by statute.

Additional question

15) Regardless of your Group's current law relating to security interests over IPRs, is it possible to create a solely contractual regime for security interests over IPRs (i.e. beside the types of security interests defined by law) that is enforceable between the contracting parties?

no

Please explain:

No. It is not possible under Luxembourg law to create a solely contractual regime for formal property or security rights (*droits réels*) by agreement besides the types of security rights defined by law.

II. Policy considerations and proposals for improvements of the current law

16) Is your Group's current law regarding security interests over IPRs sufficient to provide certainty and predictability to the parties?

yes

Please explain:

Partially. The law should regulate security rights over IPRs in a more comprehensive manner and define applicable rules balancing the divergent interests of debtors, creditors and third parties. Conflict of laws rules governing the effectiveness against third parties and priorities of different classes of creditors remain a source of concern.

17) Under your Group's current law, is there an appropriate balance between the rights between security takers and security providers? For example:

a) are there situations in which the rights of security takers should be limited or extended (e.g. if assignment of an encumbered IPR is possible by the security provider without involvement of the security taker)?

no

Please explain:

This is not expressly addressed under current laws and needs to be addressed taking into account other areas of secured transactions law, such as the Act of 5 August 2005 on financial collateral arrangements, as amended (see also our answer to question 5).

b) are there situations in which the rights of security providers should be limited or extended (e.g. if the security taker is authorized to dispose of existing licenses without involvement of the security provider)?

no

Please explain:

This is not expressly addressed under current laws and needs to be addressed taking into account other areas of secured transaction law such as the Act of 5 August 2005 on financial collateral arrangements, as amended (see also question 5).

18) Are there any aspects of these laws that could be improved? Are there any other changes to your Group's current law that would promote transactions involving IPRs as collateral? If yes, please briefly explain.

yes

Please explain:

Yes. The law should pursue a wider codification objective that clearly spells out all rules for each type of IPR used akin to approaches undertaken in the area of financial collateral arrangements and international fora such as UNCITRAL (assignment of receivables in international trade) and by Unidroit in the area of international interests in mobile equipment and the corresponding protocols.

III. Proposals for harmonisation

19) Does your Group consider that harmonization of laws concerning security interests over IPRs is desirable?

yes

If yes, please respond to the following questions without regard to your Group's current law. Even if no, please address the following questions to the extent your Group considers your Group's laws could be improved.

Security system regarding IPRs

20) Should there be specific provisions regulating security interests over IPRs (i.e. separate from security interests over tangible property) generally?

yes

Please explain:

21) If no, should there be general commercial law principles that also apply to IPRs? If not, why?

22) What types of security interests should be available as minimum standard in all countries?

The formal qualification of security rights should not matter, where the arrangement provides credit support and secures the payment or the performance of an obligation. If the "pledge" (as adjusted to balance the interests of the different parties in a comprehensive manner) is the type of security right used, such concept should be sufficient.

23) Should the law be applied differently depending on the type of IPR? For example, should patents be encumbered exclusively with pledges, should trademarks be assigned to the security taker for the purpose of security?

no

Please explain:

No. What matters is predictability and the protection given to the security taker, balancing and reflecting the interests of all participating parties with sufficient flexibility. At enforcement, there should be no substantial difference between assignment and a security right once the security taker is limited to his interest.

Effect of security interests

24) Should the security provider be restricted in their right to use their IPR after providing a security interest over that IPR (e.g. in respect of their right to grant licenses, or to use the protected subject matter)? If so, how?

no

Please explain:

No. These questions should be left to contractual freedom reflecting the interests of the security taker in each particular case.

25) Should the security provider be able to assign encumbered IPRs to third parties?

yes

Please explain:

Yes. Please refer to our answer to question 6. The taking of security over an IPR should not be an excessive hurdle to the activity of the security provider.

26) What should the rights of the security taker be before default (e.g. entitlement to damages, injunctions against infringers, or license fees)?

A determination of rights of the security taker prior to default should be possible through appropriate provisions made in the security agreement.

27) Should the security provider or the security taker be responsible for maintenance and defence of the IPR provided as collateral?

yes

Please explain:

It seems more appropriate that the security provider, as the owner (*propriétaire*) of the IPR, defends the IPR. Please refer to question 9.

28) What should the legal consequences be if the underlying IPR expires or is revoked (e.g. the security right lapses simultaneously; creditor gains a compensation claim against security provider)?

Expiration of the underlying IPR is a risk that should in the end be borne by the security taker, unless such expiration is due to the negligence or any positive action by the security provider. Covenants can be inserted in the pledge agreement so that the security provider undertakes to do anything it can to maintain and protect the encumbered IPR.

29) Should it be possible to modify these effects of security interests over IPRs before default by contractual provisions?

yes

Please explain:

Yes. As much flexibility as possible should be given to the parties.

Applicable law

30) Which law should apply as to the availability and the effects of security interests where a foreign IPR is provided as collateral? Why?

Contractual freedom should allow the parties to choose the governing law of the security agreement with respect of their mutual obligations (but excluding proprietary effects, third parties effects and questions relating the priority of different classes of creditors).

The law regarding availability and effects of security rights should allow identical rules to govern a broader package of intangible collateral, including IPRs and receivables in order to lower the cost of secured lending. It is doubtful if a choice of law for proprietary effects and the realization of pledges can achieve the necessary certainty and predictability for all market participants, particularly in the context of different classes of secured creditors and their priorities. For purposes of legal certainty, predictability and coherence, one of the two following laws could be considered to govern security rights, when *in rem* rights (*droits réels*) over IPRs are concerned:

- according to the situs rule (*lex rei sitae*), the law of the country where the IPR is registered (see also Regulation (EU) No 2015/848 on insolvency proceedings);
- for reasons of economic efficiency, certainty and predictability, the law of the habitual residence of the security provider could also govern security rights over the IPR in accordance with international standards in receivables financing (see also the corresponding reference to the law of the assignor in the Act of 22 March 2004 on securitization, as amended), provided that such country enables a registration of security rights.

What matters is the transparency of a complete record of the entitlements to use and exploit IPRs.

31) Should a choice of law provision in a security interest agreement over IPRs overrule the applicable law? If yes, why?

no

Please explain:

No. The availability and effects of security rights should be governed by a law that is clearly predictable for all relevant parties, such as the law of the habitual residence of the security provider.

Additional considerations and proposals

32) To the extent not already stated above, please propose any other standards your Group considers would be appropriate to harmonize laws relating to security interests over IPRs.

Principles elaborated in various international fora should be taken into account, i.e. the UNCITRAL IP Supplement, the Convention on International Interests in Mobile Equipment and the UNCITRAL Receivables Convention as well as Principles of Conflict of laws in Intellectual Property prepared by the European Max Planck Group on conflict of laws in Intellectual Property.

33) Please comment on any additional issues concerning any aspect of security interests over IPRs you consider relevant to this Study Question.

Please indicate which industry sector views are included in part “**III. Proposals for harmonization**” of this form:

Summary