# IP RIGHTS AND LOAN FINANCING: EUROPEAN PERSPECTIVE

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# Introduction

Intangible assets, including intellectual property rights ("IP Rights") represent an important asset of the companies.

- IP Rights are relevant for IP Finance in the following transactions:
- IP Securitizations; in which vehicles are incorporated (“SPVs”) by IP Rights holders in order to borrow money from lenders secured by a portfolio of IP Rights as collateral. SPVs use the royalties from their portfolio of IP Rights to pay interests to lenders/investors (e.g. on the basis of underlying contracts such as licensing, franchising, merchandising agreements, etc.);
- IP SALE LEASE BACK; in which the IP Rights of the lessee are sold to the leasing company, that lease them back to the firm with the final option to buy back;
- IP LOANS; in which the lenders provide loans to borrowers secured by the IP Rights of the borrowers.
- IP Rights considered for IP Finance are:
- Formal IP Rights; such as patent and trademarks that are subject to a formal registration system;
- Informal IP Rights; such as copyright, which come into being when the subject-matter is created by the author and is fixed in some tangible form.

Formal IP Rights give a monopoly protection and, generally, they do not last as long as some Informal IP Rights (however, such as in the case of registered trademarks, they can be used indefinitely provided that the IP Right continued to being used).

# I - Due Diligence

- IP Rights need to be separately identified and valued.

- Business and legal due diligence on IP Rights is required by lenders in order to identify:
  - IP Rights value/quality/duration;
  - Titles over the IP Rights;
  - Any earlier conflicting right.

- In the context of taking security, lenders will normally focus on Formal IP Rights. However, lenders may find that Informal IP Rights are of significant commercial value to the companies.

## I - A. Public available registers can provide valuable information on Formal IP Rights

In national or international public registers (e.g. www.uibm.gov.it; www.patent.gov.uk; www.dpma.de; www.inpi.fr) lenders/advisors can identify not only the perimeter of the relevant IP Rights, but also verify information on:

- The registered owner and any chain of assignment relating to the Formal IP Rights;
- Duration of the Formal IP Rights;
- Fees due in order to maintain the effectiveness of registration of the Formal IP Rights;
- Any earlier security interest over the Formal IP Rights.

## I - B. There is a very limited due diligence that lenders/advisors can carry out on Informal IP Rights

Experience shows that there are often claims on the ownership of Informal IP Rights.

- There are not formalities for the creator to obtain the Informal IP Rights and, therefore, the relevant information cannot be verified in a public available register.
- The due diligence process will be focused on the contracts on the basis of which companies have obtained the use of the creative works in their business (e.g. copyright in the computer programs developed by IT companies).

# II - Taking Security over IP Rights

Lenders are interested to secure temporary control over the IP Rights in order to ensure:

- The right to dispose of the IP Rights collateral in the event of default of the debtor;
- The right to enforce (in order to acquire or sell) their IP Rights collateral against any other third party;
- A high-ranking of priority of their IP Rights collateral against any other creditor of the debtor.

General Applicable Rules:

- Securities over tangible assets, which belong to IP Rights (e.g. original pictures, paintings, etc.) are governed by the rules of tangible assets.
- Securities over intangible assets follow their own rules in order to ensure the security right of the guarantee.

# III - Applicable Law over the IP Rights

IP Rights are regulated by the law of the Country where the IP Rights are registered (for the Formal IP Rights) or used as first (for the Informal IP Rights) and any determination on how to secure the IP Rights depends on whether security has to be taken over a Formal or Informal IP Rights.

The protection is granted in the territory where the security over the IP Rights is registered.

## III - A. Security over Formal IP Rights

- Public registers operate a priority system granting to the first applicant a priority security right over Formal IP Rights:
- Formalities for creating the securities over the Formal IP Rights are regulated by the law of the Country in which the security needs to take effect;
- The Formal IP Rights remain vested in the company-borrower, which will continue to be responsible for the maintenance of the Formal IP Rights.
- Formalities in order to effect/create a security over the Formal IP Rights are comparable to the one that are traditionally provided for the immovable assets (real properties).

Some EU countries examples of securities registration:

- In Italy: Securities and special privileges over trademarks and patents are expressly allowed for monetary credits by articles 138 and 140 of the Italian Code on Intellectual Property (Legislative Decree no. 30/2005) and are effective upon registration with UIBM (Italian Registrar for Trademarks and Patents).
- In France: Pledges ("*nantissement*") over trademarks and patents are governed by Articles L 142-1 and following of the French Commercial Code and are effective, under L 143-17, upon registration with INPI (National Institute for Industrial Property).
- In Spain: Trademarks and patents as well as their registration requests can be given as security or be subject to other rights "*in rem*". The security is binding against third parties of good faith if it is duly registered in the Spanish Patent and Trademarks Register (Article 46 of Law 17/2001; Articles 74 and 79 of Law 11/1986).

## III - B. Security over Informal IP Rights

Since there is no register, lenders' interests may not be protected against any third party who later acquires the full right over the relevant intangible asset.

- **Common law based Countries** (UK, for example): Lenders seeking to take security over Informal IP Rights may set up floating or fixed charge over all assets of the company, including the Informal IP Rights, or set up a mortgage:
  - **Floating charges** crystallize all the assets of the debtor in case of its default, without preventing it to dispose of its assets until that time and it is recorded in the Companies House in order to be opposable to third parties;
  - **Floating and fixed charges** crystallize specific and defined assets of the debtor in case of its default, without preventing it to dispose of its assets until that time and it is recorded in the Companies House in order to be opposable to third parties;
  - **Mortgages** operate in order to provide security by a transfer of property rights. Therefore, the legal title to the secured Informal IP Right is transferred to the lender, while the company-borrower retains an equitable interest on the Informal IP Right (so-called "redemption equity").

- **Civil law based Countries** (Italy, France, Spain, for example): It is not allowed to take a security over the Informal IP Right itself, but on the rights deriving from such Informal IP Right (e.g. royalties).
  - In Italy, with regard to copyright, the national law (Articles 107 and 111 of the Italian Copyright Law) states that the holder of the rights to publish and use the masterpiece who is not directly the author can secure such rights to third parties, while the author cannot secure to third parties the rights to publish and use the masterpiece, but only the royalties from such rights.
  - In Spain, the author's exploitation rights over copyrights cannot be subject to any lien, except for its profits and products, which is considered as wages in relation to lien rules (Article 53, Royal Decree 1/1996).

- Special charges over Informal IP Rights: cinematographic works
  - In Italy: Security over cinematographic works can be filed with the special public register held by SIAE (the Italian organization of authors and publishers). The security operates towards third parties, but it cannot prevent any claim in relation to proprietary rights over the Informal IP Rights.
  - In France: L 123-1 and following of the French Cinema Code provides for the "*nantissement cinématographique*" (cinematographic charge), an *in rem* security right over the film and the relevant rights assigned by the author to the producer, to be filed with the local Cinema and Audiovisual.

# IV - The EC principles of IP Rights securities

## IV - A. Community Trade Marks ("CTMs")

- The CTM system coexists with domestic systems. The first EC Directive was adopted in 1988 (now replaced by EC Directive 2008/95) in order to align the respective laws of the Member States in this area.
- CTM is valid and enforceable across the European Union as a whole territory (27 Member States and any new Member State). CTMs may be used in only one part of the European Union, such as in a single Member State or in more Member States.

Registration of trademarks with the Office for Harmonization in the Internal Market based in Alicante, Spain ("**OHIM**") allows lenders/advisors to deal with:

- A single administrative centre to be checked;
- A single filing procedure to be carried on;
- A priority regime valid in all the Member States.
- The effects of CTMS are governed by the provisions of EC Council Regulation no. 207/2009 ("2009 EC Regulation"). Under consideration (11) of the 2009 EC Regulation:

"*A CTM is to be regarded as an object of property which exists separately from the undertakings whose goods or services are designated by it. Accordingly, it should be capable of being transferred, subject to the overriding need to prevent the public being misled as a result of the transfer.* ***It should also be capable of being charged as security in favour of a third party*** *and of being the subject matter of licenses*".

- **Article 19 of the 2009 EC Regulation** expressly provides for securities over CTMs:

  1. A CTM may, **independently of the undertaking**, be given as security or be the subject of rights *in rem*;
  2. Upon request of one of the parties, securities or rights *in rem* **shall be entered in the Register of Community trademarks** ("**Register**") and **published on the Community Trade Marks Bulletin** ("**Bulletin**").

- CTMs are regarded also as national trademarks registered in the Member State (Article 16 of 2009 EC Regulation):

  - Where the owner has his seat or his domicile on the relevant date; if this principle is not applicable
  - Where the owner has an establishment on the relevant date of filing; if this principle is not applicable
  - Where is the seat of the filing office.

- For any enforcement procedure, the courts and authorities of the relevant Member State are competent and the procedure may be entered in the Register and published on the Bulletin.

## IV - B. <u>European Patent</u>

- The European patent system is the aggregate of 27 national regimes, each of them with its own rules, law and costs.

- The only harmonized aspect of the European Patent ("**EP**") is the centralization of the granting procedure, which is administered by the European Patent Office with main office in Munich, Germany ("**EPO**") on the basis of international rules set up in Munich in 1973 (European Patent Convention; latest update in 2010, 14th edition) ("**Munich EP Convention**").

- The Munich EP Convention is governed by conventional international law and does not form part of the Community legal order, but all Member States gradually acceded to it.

- Once granted, EPs need to be filed with each national patent office of the Member State in which is requested protection.

- Once an EP has been granted, it becomes a national patent and is subject to the national rules of the Member States designated in the application.

- The regime of the priority filing is ensured by each Member State and the national patent offices. The same for the enforcement, which is granted by the national Courts.

- Transfers, licenses and other rights in respect of EP applications are registered centrally in the European Patent Register in accordance with Rules 22 to 24 of the European Patent Convention, but national regulations and requirements apply with regard to registration of transfers, licenses (excluding compulsory licenses) and other rights.

- Under the EP regime, EPs may be granted as security (see Article 71 of the European Patent Convention) and the relevant security needs to be filed with the EPO.

- National laws apply in relation to the effect and validity of the securities, including formalities in order to oppose the right to third party at local level (see Articles 74 of the European Patent Convention).

## IV – C. Forthcoming EC rules on Community Patents ("CPs")

- The idea of a Community Patent dates back to the 1960s and European Community is currently working on a single procedure for the granting of a single patent, under EC rules, with validity in all the European Union.
- With Decision of 10 March 2011, the EC Council it has authorized the enhancement of cooperation in the area of the creation of unitary patent protection (EC Council Decision 2011/167).
- The draft legal framework of CPs will be likely based on the same principles of CTMs, including the ones concerning securities.

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