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ALLIANCE OF INTERNATIONAL BUSINESS LAWYERS

Licenses under Insolvency

September 2013

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The Legal Situation in Germany

The effect of insolvency proceedings on licensing agreements has been a significant source of concern for related businesses in Germany. Presently, while license contracts are provided for under the German Patent, Trademark and Copyright Acts, there is no specific provision in these statutes for the treatment of license agreements in cases of insolvency. In the absence of any specific provision, the general provisions of the German Insolvency Code apply, resulting in conflict for license right holders and licensees in national licensing agreements. These conflicts arising from the Code's application are further exacerbated in cases involving the international grant of licenses and cross border insolvencies. Under the German Insolvency Code, if a mutual contract was not performed or not completely performed by the debtor or the other contract party at the date when the insolvency proceedings were opened, such a contract will be governed by § 103 of the Code. This section provides that the insolvency administrator may elect whether or not to perform on such a contract. Where the administrator chooses to reject the contract, the other party shall be only entitled to a non-performance claim as an insolvency creditor which generally results in a low and long awaited pay out.
The nature of license agreements is that they often involve continuing obligations from one or both parties such as an obligation to continue paying royalties or licensing fees by the licensee and the returning obligation of the licensor to honour the terms of the license agreement, which may include an exclusivity clause. The existence of these continuing obligations creates an incompletely performed "mutual contract".

In practice, under insolvency proceedings where the licensee is the debtor, he will seek to retain the rights to a profitable license so as to maintain a profitable source of revenue and recoup any investments made in the bid to exploit the license; understandably, where the licensor is the debtor and thus the intellectual property has been included in the insolvency estate, the administrator will often chose to only perform such license agreements which will produce the highest yield for the insolvency estate and reject the less profitable ones.

While this creates an obvious conflict in Germany for license agreements in national bankruptcies, the case is further complicated when it involves the international grant of licenses within cross border bankruptcy proceedings. The differences in the treatment of license agreements in insolvency proceedings under German and US law were highlighted in the popular *In re Qimonda* case. Here, the German company, Qimonda went into insolvency in Munich making its mutual contracts (referred to as executory contracts under US bankruptcy law) subject to the debtor's right to reject contracts under §103 of the German Insolvency Code. Upon Qimonda's application, the US court recognized the German insolvency proceedings but also applied 11 U.S.C §365, which grants licensees in an insolvency proceeding the right to retain their licenses under specified conditions. When the Qimonda administrators attempted to reject the performance of the patent licenses, the US licensees objected by asserting their rights to retain their licenses under §365 (n). Several motions and appeals later, the conflict arising from the differences in the treatment of licenses in German insolvency proceedings and those of other jurisdictions remains unresolved.

The question in Germany remains, how to balance the interests of debtors and creditors regarding license agreements in insolvency? The current practice in Germany indicates that relief may be found in the unlikely hands of the holder of a sub – license.

The decisions of the German Federal Supreme Court (*Bundesgerichtshof* – BGH) in the Take Five and M2Trade cases indicate that in certain circumstances, the sublicenses or (sub-sublicenses) would not be affected by the termination of the main license agreement **regardless of the reason for the termination or dissolution of the main license agreement.**

In these cases, the court relied on the principle of protection from succession "*Sukzessionsschutz*" in coming to its decisions. The Sukzessionsschutz principle applies for all types of intellectual property rights and generally functions to maintain and protect the position of a licensee (exclusive or non exclusive) even in the case of a transfer of ownership of the intellectual property right concerned. The court in Take Five and M2Trade considered a balancing of the interests of the license holder and that of the sub-licensee and held that the interest of the sub-licensee (e.g. recouping substantial financial investments) in continuing the licensee agreement outweighed that of the right holder in the termination of the main license agreement and the resulting sub- license.

These cases give judicial support to the position that where a license agreement permits the creation of sublicenses, these sublicenses can then survive the assignment and termination of the main license agreement. While this is a welcome development for sub – licensees, it creates a disturbing lack of control for the licensor regarding the exploitation of its intellectual property rights. Here, the main licensor does not replace the terminated main licensee in the sub-licensing relationship but may only require that the main licensee (sub-licensor) assign his claim for the licensee fees to the main licensor before claiming payment from the sub-licensee. Additionally, there is no specific provision for how and why these surviving sub –licenses can be terminated or even properly maintained, as the terminated main licensee has no real interest in the matter and the main licensor is not a legal party to the sub – licensing agreement.

License holders and parties entering into licensing agreements are advised to reassess their licensing models to clearly establish the terms of the license and contractually position themselves to take advantage of this recent development in German law. The implementation of strategic contract clauses such as excluding the grant of sub-licenses without prior consent of the licensor, specifying termination of any sub-licenses upon the termination of the main agreement and/or providing that all sub-licensing fees be directly paid to the main licensor upon termination of the main license will help to ensure that the license holder retains more control over the license relationship.

Hopefully, anticipated reform to the Code and new judicial decisions will address these lingering concerns and move to produce a fully functional and internationally compatible framework for the treatment of licenses in national and cross border insolvency proceedings.

The Legal Situation in Denmark

A special feature in Danish IPR legislation regarding insolvency is Section 62(1) of the Copyright Act which provides as follows: "The author's right to control his work shall not be subject to creditor proceedings, either when remaining with the author or when with any person who has acquired the copyright by virtue of marriage or inheritance."

This provision means that a creditor can not force a disclosure, reproduction, publication, public performance etc. of a copyright protected work in order to seek fulfillment in the income from such exploitation. This is also the case when it comes to bankruptcy. However, that important restriction is only applicable vis-à-vis the original authors; if the copyright owner (the licensor) is a company that has acquired the rights from the author, that company does not enjoy any special protection in case of a licensee's bankruptcy. The special rule only applies to exploitation of the work as such, not the sale of copies.

A classical court decision enlightens us on the possible consequences of Section 62(1) when copyright protected works have to be dealt with in a licensee's bankruptcy estate: In 1983, the Danish Supreme Court found that it did not constitute a copyright violation that a record company's estate sold already produced phonograms. Before the bankruptcy a licensing agreement was made between the rightholders (NCB) and the record company on the manufacture and distribution of phonograms with musical works. NCB was not – when NCB in connection with the bankruptcy terminated the license – able to prohibit the sale of

goods stored, i.e. the copies already manufactured. NCB's remuneration claim was considered as an unsecured claim in the bankruptcy proceedings.

When it comes to the copyright as such, and when the licensor is the original author, the estate is forced to deliver the copyright back to author by way of free transfer. Another possibility for the estate is to join or enter into the licensing agreement. This is a general possibility according to the Danish Bankruptcy Act (Section 55). This causes no special problems regarding copyright and patent licenses. However, under "special circumstances" Section 55 does not apply, and such special circumstances could, e.g., be certain personal or technical requirements; it is recommended to seek legal advice regarding the interpretation of the term "special circumstances".

Regarding transfer of a licensing agreement to a third party as part of a reconstruction treatment of an estate special copyright and patent problems occur. New rules regarding such transfers was enacted in the Danish Bankruptcy Act in 2011 (Section 14c). Such a transfer may not be possible regarding copyright and patent licenses because such licenses, as a general rule, can not be transferred to a third party, cf. Section 56(2) of the Danish Copyright Act and Section 43 of the Patent Act, unless a right to transfer is stipulated in the licensing contract. It has to be determined in a concrete interpretation, depending on the actual circumstances, in which cases an estate, despite the said provisions in the Copyright Act and Patent Act, may transfer such copyright or patent licenses to a third party.

The Alliuris Group – an international alliance of medium sized business law firms

Interview with Chairman Ulrich Herfurth, by Lawyer Monthly Magazine, August 2013

Firstly, what do you enjoy most about being Chairman of the Group?
It is really a pleasure to work with lawyers all over the world in such a friendly but professional atmosphere. Leading the group means taking responsibility for its progress and maintaining the professional quality of our members. It also requires creating a good atmosphere on the personal level. I am proud that in the ten years of existence of the ALLIURIS Group, there has been no major dispute among members regarding our strategy, approach or the collaboration as a whole.

What are the key issues you are currently aiming at?
ALLIURIS has nearly completed its global expansion, keeping in mind that the Group is not interested in being extremely large but we would rather retain a close knit and trusting relationship with each other. After the expansion into the major markets of India, China and Brazil, we are now completing the alliance with firms in the USA and Canada. On this basis we are now focusing on business development projects for the alliance and its members in order to utilize the valuable experience in the 'Automotive', 'Energy', 'IT', 'Life Science' and 'Finance' sectors held by the ALLIURIS firms.

What do you feel are some of the main achievements of the Group?
ALLIURIS has developed a number of legal services for corporate clients, namely for the incorporation of companies, claims management, distribution and license agreements, M&A and acquisition of real property, and – as a recent development – the LifeBook, a manual for company succession and emergency cases. Our London member firm has just brought in its specific know-how about the capital markets.

ALLIURIS' website states that the Group helps to cross borders; how does it do this?
ALLIURIS helps clients to cross borders by providing the right service and legal advice. An important benefit for a corporate client is not only having the close contact with his local law firm but additionally having easy access to experienced lawyers with international backgrounds in reputable law firms in the major markets in the world. It is an advantage that this network structure offers international solutions in similar conditions as for the national projects – ALLIURIS does not maintain big overhead and related costs that in the end have to be borne by the client. In that sense, ALLIURIS helps its members to cross borders because there is a solid landing point in the target country.

What are the benefits of belonging to a network such as this?
All ALLIURIS members benefit from the advantages of the network: They can support their clients in the increasing international business, they can gain new clients for international legal services because they have more know-how and connections in other jurisdictions, and they can receive new cases from other members in the network, depending on the direction the business globally flows.

Have there been any recent regulatory developments that have particularly interested you or affected your work?
The major regulatory developments have been achieved already 10-20 years ago, when lawyers and law firms were allowed to merge nationally and internationally. Today, lawyers have to face stronger competition by organisations who are not law firms - like associations, insurance companies, service providers etc. We will see whether the Anglo-Saxon system of external financing and ownership of law firms will also be accepted by other nations in Europe.

Are there any that you would like to see?
Today, the professional rules in several jurisdictions do not fully comply with each other. This could mean that a lawyer admitted in one country but practising in another could face a conflict of rules and obligations because of contradictory principles of client protection and public security (e.g. in the field of money laundry, criminal law etc.). The countries in the European Union should at least achieve a harmonised solution for such matters.

Is there anything else you would like to mention?
The future of law firms is not totally foreseeable. Certainly the concentration process will continue and many firms will be absorbed by bigger organisations. On the other hand small entities will survive, based on very specific know-how. We believe that medium-sized business law firms will remain to be a good counterpart for the decision makers in medium-sized companies who need a one stop shop but as well a personal, trusting relationship with their lawyers. This is totally in line with the strategy of ALLIURIS and its members: providing international skills in all major markets but staying down to earth and being a trustful partner for the client.

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The ALLIURIS GROUP is organised as an international association under Belgian Law with its seat in Brussels.

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