Intellectual property rights on insolvency: risks and remedies for a licensee

(2025) 3 CRI 76

1 June 2025

Corporate Rescue and Insolvency Journal > 2025 Volume 18 > Issue 3, June > Articles

Corporate Rescue and Insolvency

Features

Mike Knapper

Is a partner in the London intellectual property team at Norton Rose Fulbright LLP. He is Head of IP for the EMEA practice.

Email: mike.knapper@nortonrosefulbright.com

Matthew Thorn

Is a partner

Email: matthew.thorn@nortonrosefulbright.com;

Nicole McKenzie

Is a senior associate

Email: nicole.mckenzie@nortonrosefulbright.com

Helen Coverdale

Is a senior knowledge lawyer in the London restructuring team of Norton Rose Fulbright LLP

Email: helen.coverdale@nortonrosefulbright.com

* * * * * *

KEY POINTS

- Many businesses license intellectual property (IP) rights such as copyright from third parties. The licence will give the licensee a contractual right to use the licensor's IP rights and therefore avoid an infringement of the IP right. Complex issues regarding the protection and realisation of IP rights can arise where a licensor (ie the person or entity that owns the IP rights) gets into financial difficulties.

- Although the Insolvency Act 1986 does not provide for the automatic termination of IP licences on the commencement of insolvency proceedings, an insolvency practitioner has broad powers which include the ability to:

- transfer the licence;

- repudiate (ie decline to perform) the licence; and

- (in a liquidation) “disclaim” the licence.

- This article outlines the principal areas of risk for a licensee of IP rights when the licensor enters into an insolvency process. It also suggests steps that a licensee may take to protect itself in potential future insolvency proceedings of its licensor.

* * * * * *

INTRODUCTION

For many businesses, intellectual property (IP) represents an increasingly valuable asset class. Commercial exploitation of IP rights is typically manifested through the licensing of user rights, which could be in the form of a bespoke exclusive licence (eg of a patent) or a non-exclusive, mass market standard form copyright licence (eg a shrink-wrapped, end-user computer software agreement). An exclusive licence gives the holder a greater degree of control, while a non-exclusive licence is more permissive and allows for multiple parties to use the property.

Licensees should consider the risks posed by the licensor's potential future insolvency proceedings, including the powers of any subsequently appointed insolvency office holder.

INSOLVENCY PRACTITIONERS' POWER OF SALE

In general terms, the Insolvency Act 1986 (IA 1986) confers wide powers on insolvency office holders (being administrators, administrative receivers and liquidators) appointed in respect of corporate entities. A core function of insolvency office holders is to identify the company's assets, then realise and distribute the proceeds to the company's creditors in accordance with the statutory waterfall of payments on insolvency.

If preservation of the IP licence is not considered to be in the best interests of the insolvency estate and the IP rights are of value, the insolvency practitioner will likely seek to sell the IP rights to realise the value for the benefit of creditors. The insolvency practitioner has the power to sell the IP rights to a third-party purchaser, subject to any required consents from secured creditors (absent a court order).

IP rights may be included in the sale of all the assets of the relevant company in a pre-pack administration sale. If the IP has been licensed, the insolvency practitioner may liaise with the licensee – particularly where there is an exclusive licence – to explore whether the licensee wishes to purchase the IP rights, but this is not strictly required. The sale and purchase agreement will usually be drafted on the basis that any purchaser will purchase only such right, title and interest as the company may have in the relevant asset.

There is a risk that the licensor's IP rights are purportedly sold free from the licensee's rights. The position here would be the same as if the transfer was made when the company was not in insolvency proceedings. If the licence relates to a registered IP right (such as patents, trademarks and registered designs) and the licensee's rights are registered at the UK Intellectual Property Office, any third party will be on notice and thereby bound by the licence. However, if registration has not occurred – or is not available for the IPR in question (for example, in the case of a software licence or other licence of copyright) – a bona fide purchaser for value acting in good faith without notice of the licence may take the IP free of the licensee's rights. This principle is codified in some IP legislation, for example s 90(4) of the Copyright, Designs and Patents Act 1988. In other words, where a purchaser acquires IP rights without notice of a licensee's rights, the licence may fall away.

Licences commonly contain prohibitions or restrictions on assignment of the IPR by the licensor. If the licensor, acting by its insolvency office holder, breached such a provision, there may be a claim in breach of contract against the insolvent licensor, which would rank with other unsecured claims in the relevant proceedings (with likely a very limited recoverability).

The insolvency practitioner also will likely receive indemnities in the sale contract from the purchaser to protect the insolvency practitioner (and in some cases, the insolvent company as seller) from loss and/or third-party claims. This is a commercial risk for the purchaser which should be factored into the price paid.

-- ***(2025) 3 CRI 76 at 77***

In cases where the licensor has been dissolved and the IP rights of the licensor have been transferred to the Crown as *bona vacantia* assets, the licensee may wish to purchase the IP rights direct from the Crown. The Crown acts through the *Bona Vacantia* Department of the Government Legal Department. If it is unwilling to engage in a sale, it may be necessary to restore the licensor company to the register and appoint an insolvency practitioner to allow the licensee to purchase the IP rights from the insolvency practitioner instead. This will be subject to the usual requirements and time limits on restoration.

LIQUIDATOR'S RIGHT OF DISCLAIMER

If a liquidator (but not an administrator or administrative receiver, referred to here together as administrators) considers that that the licence is an “onerous or unprofitable” contract (for example, because the value of the licensed IP has increased such that the licence fee is no longer market value) they may seek to disclaim the contract under s 178 IA 1986. Disclaimer is achieved simply by serving notice on prescribed parties.

To be considered onerous, a contract must be more than simply unprofitable and generally there would need to be obligations to be performed or costs to be incurred by the insolvent licensor. Disclaimer presents a risk even when the licence is perpetual, irrevocable and fully paid up (ie the consideration was paid upfront), provided “it may give rise to a liability to pay money or perform any other onerous act”. This could include cases where the licensor is contractually required to maintain registered rights such as trademarks or patents that involve renewal fees.

Where a liquidator successfully disclaims a licence, the whole contract is disclaimed. For example, where there is an agreement that covers the licensing of software and provides for ongoing support and maintenance, the liquidator would not be able to disclaim the support and maintenance obligations alone. Moreover, a disclaimer only operates to determine the rights, interests and liabilities of the licensor company.

Where a liquidator disclaims an IP licence, any party with an “interest” in the disclaimed property (eg an exclusive licensee) can apply to the court to have the IP rights vested in it under s 181 of IA 1986. In practice, if the licensee offered the liquidator a fair sum (plus costs) to take an assignment of the underlying IP rights, the liquidator would generally be willing to sell such rights to the licensee, rather than disclaim it. This is because the liquidator's function is to realise assets to maximise funds in the insolvent estate. In administration, where there is no power to disclaim onerous property, the administrator may be open to a consensual assignment.

POSITION ON ADMINISTRATION

Unlike a liquidator, an administrator has no statutory right to disclaim onerous contracts. Instead, if a licensor (acting by its administrator) breaches its obligations under a licence, the licensee will have an unsecured claim for damages. Occasionally it may be possible to seek a court order for specific performance on the part of the insolvent licensor. However, such orders are rare.

There may be a potential claim against the administrator in the tort of inducing a breach of contract. The rule in *Said v Butt* [1920] 3 KB 497 is often relied upon by administrators as authority for the proposition that the administrator (as agent of the company) will not be personally liable for causing a breach of contract provided they were acting within their powers and in good faith. Note however that in the context of directors, the Supreme Court recently concluded that *Said v Butt* does not apply to tortious liability and civil wrongs "which do not depend on any contract or voluntary arrangement between the parties and where liability arises even if they are complete strangers to one another" including trademark infringement – see *Lifestyle Equities CV v Ahmed* [2024] UKSC 17.

PROTECTIONS FOR THE LICENSEE

At the time of granting a licence to use IP rights, the licensee should consider what protections it may obtain should the licensor subsequently enter into an insolvency process. These may include insolvency remote ownership structures and taking security over the IP. They also may include structuring perpetual, irrevocable, or long-term paid-up licences so that they contain minimal onerous obligations (for example, ensuring that software maintenance obligations are contained in a separate contract). Other considerations include:

(I) REGISTRATION

Where possible under the law, the licensee should register their rights as a licensee with the UK Intellectual Property Office. A licence that is registered in this way will be binding on any successor in title to the registered IP. If an insolvency practitioner purports to sell the registered IP to a third party where the licence is recorded on the public register (or the new owner has actual notice of the licence), the new owner would be bound by the terms of the licence.

The position in relation to IP rights in other countries which are licensed by an insolvent UK licensor would depend on the local rules around registration of such licences.

(II) RESTRICTION ON ASSIGNMENT

The licensee may negotiate a contractual restriction on the licensor assigning the IP rights to a third party. If such provision is breached, the licensee would have a remedy against the (insolvent) licensor for breach of contract, as noted above. As the licensee cannot sue a company in administration without the consent of the insolvency practitioner or leave of the court, the breach of contract would generally be dealt with as part of the insolvency process and rank as an unsecured claim. In practice, the licensee *may need to negotiate with the assignee and their rights in this regard will depend on the facts.*

(2025) 3 CRI 76 at 78

(III) AUTOMATIC ASSIGNMENT/OPTION TO PURCHASE

The contract may include an express provision, triggered by the insolvency of the licensor, for either:

(i) an automatic assignment of the licensed IP rights to the licensee; or

(ii) an option to acquire the IP rights from the licensor.

However, as noted above, any breach of contractual provisions by the insolvent company will rank only as an unsecured debt and therefore the prospect of any meaningful return in the insolvency is low.

A provision of this kind also would need to be considered and drafted carefully. Any purchase price would need to be set at an arm's length amount to avoid falling foul of the anti-☒deprivation principle: this is the principle that seeks to prevent creditors from contracting out of the statutory payment waterfall. For example, if the option to purchase is only exercisable on insolvency and at a nominal value, it likely would be ineffective.

(IV) ESCROW ARRANGEMENTS

Escrow arrangements are most commonly used in the context of software licences.

Traditional “on premises” software licence agreements – where the software is installed and used on the licensee's own computer system – often grant the licensee a right to demand that the source code be put into escrow, or to join an existing escrow agreement. The NCC single licensee software escrow agreement provides that upon the licensor's insolvency and other prescribed events (eg breach of contract by the licensor), the source code and other information deposited with the escrow agent will be released to the licensee, subject to duties of confidentiality and other obligations. Title in the source code generally remains with the licensor. While the licensee would usually be unable to transfer the source code and property to a third party, it permits the licensee to use the source code to enable it to continue benefitting from the licence it has paid for (eg using the source code to maintain the software).

As with an option to purchase, there is a risk that an insolvency practitioner may challenge an escrow agreement for offending the anti-deprivation principle. In practice, this is likely to be a challenge to the licensee's rights to use the source code on release rather than a challenge to the release of the source code itself. In a properly drafted escrow agreement, the escrow agent would have to release the escrowed material it holds to the licensee upon the occurrence of the defined escrow release event (eg the insolvency of the licensor) and there usually would be no contractual mechanism for the licensor or insolvency practitioner to challenge this release unless it disputed whether the release event had actually occurred.

A licensee may reduce this risk by:

(i) making the release events wider than insolvency and arising at an earlier stage;

(ii) ensuring that fair market value has been paid to the licensor for the right to access and use the source code;

(iii) not seeking a transfer of title to the source code on commencement of insolvency proceedings.

CONCLUSION

The insolvency of a licensor presents significant risks for a licensee of IP rights. However, contractual safeguards can be negotiated in advance to mitigate against such an event. Should insolvency occur, early action is key. The licensee will need to act quickly in order to benefit from the legal options available to them.

* * * * * *

FURTHER READING

- Lexis+: practice note: Protecting intellectual property rights in order to minimise risk on insolvency. https://shorturl.at/Bd7av

- Lexis+: practice note: Introduction to intellectual property rights on insolvency. https://rb.gy/oo2fnh

- On the edge: data protection law for insolvency practitioners (2017) 2 CRI 64. https://rb.gy/snjnam

* * * * * *
