# Grasping for Air: Revised Article 9 and Intellectual Property in an Electronic World

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## I. INTRODUCTION

The ongoing conflict between commercial and intellectual property laws presents a unique problem for Internet-based companies looking to utilize intellectual property rights as collateral. Furthermore, the confusion between the Uniform Commercial Code ("UCC") and federal intellectual property laws creates legal uncertainty, forcing attorneys to contend with both state and federal filing systems.[1] Due to

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[1] Paul J.N. Roy et al., *Security Interests in Technology Assets and Related Intellectual Property: Practical and Legal Considerations*, 16 COMPUTER LAW 3 (1999).

this confusion, the intellectual property assets of electronic commerce ("e-commerce") ventures are often "under-valued and under-utilized," even though these resources are likely to be a company's most valuable assets.[2] Bankruptcy can intensify these conflicts when e-commerce ventures leave intellectual property rights to a bankruptcy trustee or debtor in possession for dissemination.[3] This is demonstrated by the surge of Internet company[4] failures observed in the early part of this millennium.[5] The economic downturn left once "get-rich-quick" computer programmers "mitigating damages rather than adding new wings onto their homes"[6] and resulted in discord for venture capitalists, creditors, and licensors.[7]

Recognizing the new issues[8] presented by the emergence of e-commerce, the National Conference of Commissioners on the Uniform State Laws ("NCCUSL")[9] and the American Law Institute ("ALI")[10] established the Article 9 Drafting Committee ("Committee").[11] The Committee drafted an electronic friendly ("e-friendly") Article 9[12]—the UCC article that governs security interests in intellectual prop-

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[2] William J. Murphy, *Proposal for a Centralized and Integrated Registry for Security Interests in Intellectual Property*, 41 IDEA 297 (2002).

[3] *See* Madlyn Gleich Primoff & Erica G. Weinberger, *E-Commerce and Dot-Com Bankruptcies: Assumption, Assignment and Rejection of Executory Contracts, Including Intellectual Property Agreements, and Related Issues under Sections 365(C), 365(E) and 365(N) of the Bankruptcy Code*, 8 AM. BANKR. INST. L. REV. 307 (2000).

[4] Internet companies are commonly referred to as "dot-coms."

[5] Joshua Kaufman & Hoyun Kim, *Perfecting Security Interests in Intellectual Property*, LEGAL TIMES, May 22, 2000, at 24.

[6] *Id.*

[7] *Id.*

[8] Since Internet companies have little need for traditional property (such as multiple offices, factories, or storage facilities), these companies are highly dependent on intellectual property as a financing mechanism. Furthermore, Internet companies utilize various licenses and software programs that may be able to serve as collateral as well. Finally, these companies serve consumers on a global level, leading to some uncertainty on the proper status for filing an international security interest in the United States. Revised Article 9 recognizes these issues and has revamped the code to address these unique problems. *See infra* Part III; RUSSELL A. HAKES, THE ABCS OF THE UCC: (REVISED) ARTICLE 9 SECURED TRANSACTIONS (Amelia H. Boss ed., American Bar Association 2000).

[9] The NCCUSL is an unincorporated non-profit association of over 300 lawyers, judges, and law professors from all 50 states, the District of Columbia, Puerto Rico, and the Virgin Islands. The association's purpose is to create uniformity amongst state laws. Uniform Law Commissioners website, *at* http://www.nccusl.org/nccusl/DesktopDefault.aspx (last visited Oct. 29, 2003).

[10] ALI is a non-profit corporation founded in 1923 to promote social needs through the clarification and simplification of the law. American Law Institute website, *at* http://www.ali.org (last visited Oct. 29, 2003).

[11] THE NEW ARTICLE 9: UNIFORM COMMERCIAL CODE 17 (Corinne Cooper ed., American Bar Association 2000) [hereinafter NEW ARTICLE 9].

[12] *See infra* Part III for a detailed analysis of Revised Article 9.

erty—that would recognize the significance of intellectual property as collateral.[13] The Committee presented the revised Article 9 ("Revised Article 9")[14] to the fifty state legislatures in 1998.[15] The Committee requested that state legislatures consider and implement Revised Article 9 by July 1, 2001.[16] All fifty states enacted the Revised Article 9 provisions by the proposed deadline.[17]

Intellectual property assets are the most significant assets for e-commerce businesses.[18] These assets, described as intangible under Article 9,[19] are governed by both the UCC and federal intellectual property laws.[20] The co-existence of these varied statutes generates mass confusion among borrowers and lenders, who are uncertain of the proper law to follow when securing an interest in these assets.[21] The security provided to lenders is especially important because, when businesses fail, creditors look to claim rights in their collateral.[22] Without a guaranteed security in assets, lenders and venture capitalists are often unwilling to take risks on an e-commerce venture, especially in times of fiscal uncertainty.

One of the most confusing and crucial questions left unanswered by the uneasy coexistence of state and federal intellectual property laws is what is required to obtain a security interest[23] in a copy-

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[13] *Changes in Secured Financing Laws Will Affect Lenders Nationwide*, 37 No. 1 BANKR. CT. DEC. 7 (Jan. 9, 2001).

[14] All references herein to past and present Article 9 provisions will be distinguished by reference to "Former Article 9" or "Revised Article 9."

[15] Ben Carpenter, *Deposit Accounts under Revised UCC Article 9: What Bankers Need to Know*, A.B.A. BANKING J., June, 2001, at 70.

[16] Gerald T. McLaughlin & Neil B. Cohen, *Revised Article 9 is Here: Be Prepared*, 226 N.Y. L.J. 3 (July 2, 2001), at 3.

[17] *Id.*

[18] Raymond T. Nimmer, *Information Age in Law: New Frontiers in Property and Contract*, 68 N.Y. ST. B.J. 28 (May/June 1996). Nonetheless, lenders should not overlook the necessary tangible assets held by Internet companies. For example, lenders should obtain a security in computer disks, equipment, and other "tangible embodiments of intellectual property that are essential to using the intellectual property." Roy et al., *supra* note 1, at 6.

[19] Revised Article 9 defines "general intangible" as "any personal property, including things in action, other than accounts, chattel paper, commercial tort claims, deposit accounts, documents, goods, instruments, investment property, letter-of-credit rights, letters of credit, money, and oil, gas, or other minerals before extraction. The term includes payment intangibles and software." REV. U.C.C. § 9-102(42) (2001). Furthermore, the Official Comments to this section state that an example of a "general intangible" "[is] various categories of intellectual property . . . [a]s used in the definition of 'general intangible,' 'things in action' includes rights that arise under a license of intellectual property, including the right to exploit the intellectual property without liability for infringement." *Id.* at cmt. 5(d).

[20] *See* discussion *infra* at Parts IV and V.

[21] Murphy, *supra* note 2, at 297-98.

[22] RONALD MANN & JANE KAUFMAN WINN, E-COMMERCE 610 (Winter 2002 Draft).

[23] *See infra* Part III for a detailed discussion on security interests.

right.[24] Commentators suggest that much of the confusion over this question is a result of the decision in *In re Peregrine Entertainment Ltd.*,[25] the leading case on this issue.[26] In *Peregrine*, Judge Kozinski, a prominent judge on the U.S. Court of Appeals for the Ninth Circuit, held that the federal Copyright Act's filing provisions[27] preempt Article 9 of the UCC.[28] Commentators suggest, however, that *Peregrine* was wrongly decided.[29] In fact, Congress proposed legislation to reverse the decision.[30] The legislation, however, failed to become law, and soon after, commentary criticizing the decision subsided.[31] Nevertheless, in the wake of the e-commerce surge, this discussion needs to be revived, as Internet-based companies are highly dependent upon copyrights as their primary asset for financing.[32] Fortunately, the drafters of the UCC recalled the preemption problem when drafting an e-friendly Article 9 and attempted to persuade the federal legislature and courts to recognize that the Copyright Act should not preempt Revised Article 9.[33]

The focus of this Comment is on the tension that exists as a result of the *Peregrine* decision and the need to revise the mechanism for recording a security interest in copyrights. Since the securitization of trademarks and patents are both governed under the UCC, this Comment argues that copyrights should also be governed by the UCC. This Comment discusses Revised Article 9 and its interplay with bankruptcy law. Part II addresses the role of intellectual property[34] found in e-

[24] *See infra* Part V.

[25] Nat'l Peregrine, Inc. v. Capitol Fed. Sav. & Loan Ass'n of Denver, 116 B.R. 194 (Bankr. C.D. Cal. 1990) (hereinafter "*In re* Peregrine Entm't, Ltd.").

[26] *Id.*

[27] 17 U.S.C. § 205 (1996).

[28] *In re* Peregrine Entm't Ltd., 116 B.R. at 207-08.

[29] Robert H. Rothstein, *Paul Herald's "Resolving Priority Disputes in Intellectual Property Collateral": A Comment*, 1 J. INTELL. PROP. L. 167, 183 (1993).

[30] *See* Copyright Reform Act of 1993, H.R. 897 (Hughes), S. 373 (DeConcini), 103d Cong. § 1 (1993). When introducing this measure, Congressman Hughes of New Jersey stated that it was his intention to alleviate the "considerable amount of time and expense that is required in order to comply with the [*Peregrine*] decision." Steven Weinberger, *Perfection of Security Interests in Copyrights: The* Peregrine *Effect on Orion Pictures Plan of Reorganization*, 11 CARDOZO ARTS & ENT. L.J. 959, 960 (1993) (quoting 139 CONG. REC. E338 (daily ed. Feb. 16, 1993)). "Representative Hughes commented upon introducing the legislation that the *Peregrine* decision has 'turned a relatively simple business transaction into a nightmare for businesses and lenders.'" *Id.* at 960 n.7.

[31] *Id.*

[32] Nimmer, *supra* note 18.

[33] *See* NEW ARTICLE 9, *supra* note 11.

[34] This Comment focuses on copyrights, using trademarks and patents to form an analogy to the proper means of perfection. The author recognizes that domain names and trade secrets/data are essential assets for an e-commerce venture. Discussion of these assets, however, will be limited to notes 44 and 45.

commerce and the ability of creditors to secure an interest in these assets under Revised Article 9. Part III gives an overview of Revised Article 9, examining what will likely be required to perfect a security interest in a copyright under Revised Article 9. Part IV focuses on how most forms of intellectual property are secured in financial transactions. Part V analyzes how copyright is presently secured in financial transactions and explains why the UCC should become the sole vehicle for securing interests in copyrightable works. Ultimately, this Comment concludes that the changes in Revised Article 9 represent an improvement and that Revised Article 9 should serve as the primary vehicle for perfection of a security interest for all intellectual property assets, including copyrights. Further, this Comment advocates overturning *Peregrine* so that Congress can amend the Copyright Act in order to make it clear that the Copyright Act does not preempt Revised Article 9, thereby fostering the growth of e-commerce ventures that are highly reliant on copyright assets in obtaining financing. Such a system would simplify filing, create uniformity of notice for all parties, and foster investment and growth.

## II. INTELLECTUAL PROPERTY AND E-COMMERCE

Intellectual property law provides a mechanism to protect information created by individuals.[35] These laws seek to provide incentives, via creation of personal property rights, for individuals to create new information that can be used by the public.[36] They are based on English common law and originate from the Intellectual Property Clause of the United States Constitution.[37] Intellectual property laws are increasingly important today, as the creation of the Internet has provided a way for individuals to easily create and disseminate information.

Millions of people log on to the Internet everyday, and new websites continue to pop up.[38] The speed and efficiency of modern technology allows businesses to communicate instantaneously on a worldwide level.[39] High-speed communication makes e-commerce indispensable

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[35] PAUL GOLDSTEIN, COPYRIGHT, PATENT, TRADEMARKS AND RELATED STATE DOCTRINES 6 (Foundation Press, 4th ed. 1999).

[36] *Id.*

[37] *Id.* at 1-5; U.S. CONST. art. I, § 8, cl. 8.

[38] Francis G. Conrad, *Dot.Coms in Bankruptcy Valuations under Title 11 or www.snipehunt in the dark.noreorg/noassets.com*, 9 AM. BANKR. INST. L. REV. 417 (2001). Consumer use of the Internet exceeded the growth observed in any other medium. *Id.* at 417. "[T]he Internet achieved the 50 million users mark four times faster then the personal computer." *Id.*

[39] Amelia H. Boss & Jane Kaufman Winn, *The Emerging Law of Electronic Commerce*, 52 BUS. LAW. 1469, 1469 (1997).

in the current global marketplace.[40] In fact, reports show that virtual business environments resulted in a 2000 percent growth in Internet-enabled companies from 1997 to 2000.[41] As commerce on the Internet continues to expand, society places a newfound importance on information technology.[42] While intellectual property is not a new concept, e-commerce ventures spurred renewed interest in intellectual property assets and, consequently, intellectual property laws.[43]

Internet-based companies hold assets in copyrights, patents, trademarks, domain names,[44] and trade secrets.[45] Web pages used by Internet companies contain graphics, video clips, audio sound bites, text, and pictures that are entitled to copyright and, sometimes, trademark protection.[46] E-commerce entrepreneurs also utilize these assets as collateral to obtain the financing required to establish and maintain their presence on the Internet.[47]

The constant interactions among consumers on the Web, however, together with ever-evolving technological advances, make information technology assets in e-commerce, known as intellectual property, different from traditional property.[48] Due to the highly complex nature of

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[40] *Id.*

[41] Conrad, *supra* note 38, at 417.

[42] *See* Scott J. Driza, *Perfecting Security Interests in Intellectual Property*, 88 ILL. B.J. 162 (2000).

[43] I will use the terms "information technology" and "intellectual property" interchangeably to mean copyrights (including software), trademarks, patents, domain names, and trade secrets (including data).

[44] A new and interesting possible asset on the Internet is the domain name. Domain names, however, are beyond the scope of this article. For an excellent discussion on the use of domain names as a security interest, see Brent R. Cohen & Thomas D. Laue, *Acquiring and Enforcing Security Interests in Cyberspace Assets*, 10 J. BANKR. L. & PRAC. 423, 428 (2001); Adam Chase, *A Primer on Recent Domain Name Disputes*, 3 VA. J.L. & TECH. 3 (1998); Jonathan C. Krisko, *U.C.C. Revised Article 9: Can Domain Names Provide Security for New Economy Businesses?*, 79 N.C. L. REV. 1178, 1183 (2001).

[45] Trade secrets have traditionally provided a valuable commodity to businesses. Michael R. Levinson & Christopher E. Paetsch, *The Computer Fraud and Abuse Act: A Powerful New Way to Protect Information*, 19 NO. 9 COMPUTER & INTERNET LAW 11, 12 (2002). Trade secrets are beyond the scope of this article. However, for a thorough discussion on the use of trade secrets as security interests and the controversial debates surrounding sale of these secrets, which often include personal information about consumers, see Johanna Bennett, *It's My Life: Should You Own the Personal Information You Reveal Online?*, WALL ST. J., Oct. 29, 2001, at R9; Dan L. Nicewander, *General Intangibles Under Revised Article 9*, 54 CONSUMER FIN. L.Q. REP. 169, 170 (2000).

[46] Leonard T. Nuara & Howard P. Benard, *How Commerce Becomes E-Commerce*, 1156 PLI/CORP. 475, 483 (1999).

[47] Murphy, *supra* note 2, at 297-98.

[48] Roy et al., *supra* note 1, at 3. This mobility, especially in the case of software, creates problems for lenders who fail to file updated federal filings for subsequent generations of the information technology. *Id.* The federal system does not allow for open-ended filings. *Id.* Therefore, a lender must maintain amended filings as the asset evolves. *Id.* at 5.

the Internet, intellectual property assets are unusually mobile and more susceptible to change.[49] Presently, courts recognize that the federal laws governing trademarks and patents are not the proper mechanisms to govern security interests in those assets.[50] In contrast, according to *Peregrine*, federal laws are the proper mechanisms governing security interests in copyrights. Federal law concerning copyrights is a considerably murky area for businesses and lenders alike.[51] Revised Article 9 recognizes this confusion and suggests that federal copyright law be clarified in order to allow Internet companies greater flexibility in seeking perfection of an interest in information technology. Ultimately, this would protect investors and foster growth on the Internet.[52]

## III. INTELLECTUAL PROPERTY AND STATE LAW GOVERNANCE: ARTICLE 9 OF THE UCC

Revised Article 9 of the UCC, like Former Article 9, governs security interests in personal property.[53] Generally, both Revised and Former Article 9 apply to any contract that secures payment or other performance of an obligation through an interest in personal property.[54] This interest is called a "security interest,"[55] and the property used in these transactions is referred to as "collateral."[56] Article 9 "facilitate[s] financing by creating a comprehensive scheme for the regulation of security interests and by providing creditors with an efficient and streamlined method of perfecting security interests."[57] Intellectual

[49] *Id.* at 3.
[50] *See infra* Part IV.
[51] *See infra* Part V.
[52] *See* Murphy, *supra* note 2.
[53] NEW ARTICLE 9, *supra* note 11, at 18.
[54] *Id.*
[55] *Id.*; *see also* U.C.C. § 1-201(35) (2003).
[56] NEW ARTICLE 9, *supra* note 11, at 19; *see also* Rev. U.C.C. § 9-102(a)(12) (2001).
[57] Murphy, *supra* note 2, at 299.

property[58] is one the many types of personal property governed under Revised Article 9.[59]

### A. *Perfection under Article 9 of the UCC*

Perfection of a security interest occurs when a lender obtains control over collateral.[60] Control over collateral typically occurs by filing a UCC-1 financing statement in the appropriate state office.[61] Perfecting a security interest validates this interest against other creditors.[62] When creditors comply with Revised Article 9's perfection provisions, they are "generally protected against subsequent third party claims."[63] In a financial business deal, perfection may be the most essential com-

[58] It is essential to determine if assets are actually "property" before considering the use of intellectual property as collateral, because the UCC only applies to "personal property." Rev. U.C.C. § 9-101, cmt. 1 (2001). While these assets may be valuable to a company and are likely to be the most significant asset of an Internet company, it is unclear if intellectual property is truly property. Jonathan C. Lipson, *Financing Information Technologies: Fairness and Function*, 2001 WIS. L. REV. 1067, 1087 (2001). If information technology assets are not property, then no matter how valuable the assets, a debtor should not be able to grant a security interest in them since a security interest is, by definition, an "interest in personal property." Rev. U.C.C. § 9-109(a)(1) (2001). While it seems clear that copyrights and patents are property, the question is more amorphous for other forms of intellectual property such as trademarks, trade secrets, data and licenses. *See* 17 U.S.C. § 201(d)(1) (1976) ("The ownership of a copyright may be transferred . . . as personal property."); 35 U.S.C. § 261 (1952) ("[P]atents shall have the attributes of personal property."). It is ambiguous whether trademarks are actually property in and of themselves. Lipson, *supra* at 1087. Despite the ambiguity as to whether trademarks, trade secrets, or data are property, most courts have allowed security interests to attach to these assets. *See In re* Trimachi v. Together Dev. Corp., 255 B.R. 606 (Bankr. D. Mass. 2000) (trademarks can be security interests); *In re* Avalon Software Inc., 209 B.R. 517 (Bankr. D. Ariz. 1997) (trade secrets can be security interests); Joseph v. 1200 Valencia, Inc. (*In re* 199Z, Inc.), 137 B.R. 778 (Bankr. C.D. Cal. 1992) (trade secrets can be security interests); Levitz v. Arons Arcadia Ins. Agency (*In re* Levitz Ins. Agency), 152 B.R. 693, 697 (Bankr. D. Mass. 1992) (customer list defined as "general intangible" under Former Article 9); *In re* Chattanooga Choo-Choo Co., 98 B.R. 792 (Bankr. E.D. Tenn. 1989) (customer list defined as "general intangible" under Former Article 9); *In re* C.C. & Co., Inc., 86 B.R. 485 (Bankr. E.D. Va. 1988) (customer list defined as "general intangible" under Former Article 9); Creditors' Comm. v. Capital Bank (*In re* TR-3 Indus.), 41 B.R. 128 (Bankr. C.D. Cal. 1984) (customer list defined as "general intangible" under Former Article 9); *In re* Roman Cleanser Co., 43 B.R. 940 (Bankr. E.D. Mich. 1984) (trademarks are "general intangibles"); *In re* Emergency Beacon Corp., 23 UCC Rep. Serv. 766 (Bankr. S.D.N.Y. 1977) ("[P]atent rights, tradename, customer lists, books and records and [the] right to manufacture or sell emergency beacons and related electronic equipment were general intangibles within the meaning of [Former] § 9-106 [of the Uniform Commercial Code].").

[59] Rev. U.C.C. § 9-102(42) (2001).

[60] NEW ARTICLE 9, *supra* note 11, at 27.

[61] *Id.* Perfection can also occur when a lender takes physical possession of the collateral. *Id.* However, the nature of intellectual property is not conducive to a lender taking physical possession since this property is "intangible" by nature. *Id.*

[62] BLACK'S LAW DICTIONARY 523 (Pocket 2d ed. 2001).

[63] Murphy, *supra* note 2, at 299.

ponent of the entire transaction.[64] Lenders taking risks on e-commerce ventures demand that their investments be protected by collateral.[65] Absent proper filing for control of the collateral, the lender may find itself at the end of a long line of creditors on judgment day.[66]

Because priority is given to secured creditors under the United States Bankruptcy Code[67] ("Bankruptcy Code"), there is a critical link between secured collateral and judicial liens.[68] In order to ensure that collateral is secured, it must be properly filed. Proper filing requires compliance with Article 9 and is especially significant in the bankruptcy context.[69] The Bankruptcy Code requires the appointment of a trustee who acts as a "hypothetical judicial lien creditor."[70] Bankruptcy law allows a trustee or debtor in possession to avoid a security interest if the interest is unperfected when the company claims bankruptcy.[71] Hence, if the lender fails to properly perfect its interest in the intangible assets, it will find itself among many other unsecured creditors who are not likely to achieve full repayment.[72] This leaves the lender in a vulnerable position, unable to claim priority[73] over all other creditors.[74] Failing to properly perfect an interest under Revised Article 9 is enormously risky, because there is a possibility that after all of the secured creditors have been paid, there is nothing left in the bankruptcy estate, leaving the unsecured creditor "out to dry."[75] For example, if multiple parties hold a security interest in the same collateral, that one piece of collateral may be insufficient to meet the debts of all who have an interest in the collateral.[76] Therefore, in order to achieve priority over other lenders and have the ability to gain the full value owed, a creditor must "perfect" its security interest.[77]

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[64] Justin M. Vogel, *Perfecting Security Interests in Unregistered Copyrights: Preemption of the Federal Copyright Act and How Filing in Accordance with Article 9 Leads to the Creation of a Bankruptcy "Force Play,"* 10 AM. BANKR. INST. L. REV. 463, 466 (2002).

[65] *See* Ronald J. Mann, *Secured Credit and Software Financing*, 85 CORNELL L. REV. 134 (1999).

[66] *Id.*

[67] 11 U.S.C. § 101 (2003).

[68] 11 U.S.C. § 544 (2003).

[69] Vogel, *supra* note 64, at 463.

[70] 11 U.S.C. § 544(a)(1).

[71] Kaufman, *supra* note 5, at 24.

[72] *Id.*

[73] If a creditor properly secures an interest in the collateral, it will receive its amount owed before other lenders who do not have secured collateral. *Id.*

[74] *Id.*

[75] Vogel, *supra* note 64, at 466-67.

[76] William A. Dornbos, *Structuring, Financing, and Preserving Security Interests in Intellectual Property*, 113 BANKING L.J. 656, 657 (1996).

[77] *Id.*

Perfection under Revised Article 9 is straightforward.[78] Revised Article 9 merely requires the filing of a UCC-1 financing statement in the appropriate state office.[79] Determining where to file was a difficult task under Former Article 9, because the debtor's place of business was not clearly defined.[80] Under Former Article 9, a secured party filed a UCC-1 financing statement in the state where the collateral was located or, for intangibles, where the debtor was located.[81] A corporate debtor was located at its "place of business" or, for a multi-state firm, at its chief executive office.[82] Thus, those lending against a company's tangible assets frequently had to file in several states and monitor both acquisition and interstate movement of the assets.[83] As a result, those seeking perfection in collateral often found themselves filing in multiple jurisdictions in order to ensure that the interest was filed in any jurisdiction that could conceivably be seen as the debtor's chief executive office.[84]

Revised Article 9 renders the location of the debtor the relevant site for filing in most instances.[85] The new rules for determining where the debtor is located for purposes of filing are quite different under Revised Article 9. Section 307(e) of Revised Article 9 states that "a registered organization that is organized under the law of a State is located in that State."[86] Hence, for a debtor that is a corporation or other entity chartered by the state in which it is located, that state is the chartering or incorporating state.[87] If the debtor is not a corporation, the "chief executive office" test will still apply, requiring filing in the state where the organization's main office is located.[88] If the office is outside of the United States, the debtor is considered to be located in

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[78] The UCC typically allows a debtor to specify the goods by a class alone. Rev. U.C.C. § 9-108(b)(3) (2001). However, practitioners drafting agreements that wish to extend beyond the intangible asset itself to its proceeds and licenses must be more specific when filing. Rev. U.C.C. § 9-102(a)(1) (2001). Therefore, a creditor seeking to take advantage of the opportunity to obtain payment due under a license, for example, cannot merely file the collateral as general intangibles. In order to obtain the payments, the creditor must specify that this is an element of the agreement in the UCC–1 financing statement. Neil Cohen et al., *Bankruptcy in a Brave New E-World: Planning for the Day a Dot-Com Crashes*, 816 PLI/COMM 247, 257 (2001).

[79] Rev. U.C.C. § 9-310(a) (2001).

[80] Fmr. U.C.C. § 9-103(d) (1989).

[81] *Id.*

[82] *Id.*

[83] William C. Smith, *Article 9 Take 3*, 87 A.B.A. J. 52, 54 (2001).

[84] Cohen, *supra* note 78, at 256.

[85] Rev. U.C.C. § 9-307(e) (2001).

[86] *Id.*

[87] *Id.*

[88] Rev. U.C.C. § 9-307(b)(3) (2001).

the District of Columbia.[89] This new District of Columbia filing option is important to e-commerce vendors doing business on a global level.[90] While a diligent creditor's counsel should continue to investigate foreign law on filing and registration and comply with foreign requirements for perfection, the availability of perfection in the United States by filing a UCC-1 financing statement in the District of Columbia presents a welcome change for perfecting assets used as collateral in increasingly common offshore financing.[91]

### B. *Preemption*

The Supremacy Clause of the United States Constitution provides Congress with the ability to supersede state law in certain circumstances.[92] Recognizing that federal law is supreme, both Former and Revised Article 9 have specific provisions exempting assets governed by federal law.[93] Therefore, if a federal law controls registration of an asset, a UCC filing is unnecessary and ineffective to perfect that security interest.[94]

Revised Article 9 seeks to alleviate some of the conflict and confusion by suggesting that the courts and Congress allow fewer laws to preempt the UCC.[95] Although some practitioners argue that Revised Article 9 stifles the rights of intellectual property owners,[96] it actually expands opportunities for e-commerce by promoting the ability of individuals to create new and creative works in the electronic atmosphere.[97]

The language in Revised Article 9 was intentionally drafted narrowly to avoid federal preemption.[98] The Official Comments to Re-

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[89] Rev. U.C.C. § 9-307(c) (2001).

[90] *See* Barkley Clark, *Revised Article 9 of the UCC: Scope, Perfection, Priorities and Default*, 4 N.C. BANKING INST. 129 (2000).

[91] Smith, *supra* note 83, at 54 (quoting Sandra M. Rocks of the New York law firm of Clearly Gottlieb).

[92] U.S. CONST. art. VI, cl. 2.

[93] Rev. U.C.C. § 9-109(c)(1) (2001); Fmr. U.C.C. § 9-104(a) (1989).

[94] *Id.*

[95] Rev. U.C.C. § 9-109(c)(1) (2001).

[96] Lorin Brennan, *Financing Intellectual Property under Revised Article 9: National and International Conflicts*, 23 HASTINGS COMM. & ENT. L.J. 313, 328 (2001).

[97] *Id.* The author argues that Revised Article 9 bolsters the rights of secured lenders, which will, in turn, make lenders more comfortable about investing in e-commerce activities. Absent this sense of security, many lenders will forgo the option to finance e-commerce businesses—especially since they have seen the dot-coms' market shares collapsing. As a result, new and creative works that could have been created as part of an e-commerce venture will never achieve public exposure. *Id.*

[98] Rev. U.C.C. § 9-109(c)(1) (2001). "This article does not apply to the extent that: (1) a statute, regulation, or treaty of the United States preempts this article." *Id.*

vised Article 9 explain that Former Article 9 produced unintended results:

> Some (erroneously) read the former section to suggest that Article 9 sometimes deferred to federal law even when federal law did not preempt Article 9. Subsection (c)(1) recognizes explicitly that this Article defers to federal law only when and to the extent that it must—i.e., when federal law preempts it.[99]

This Official Comment, apparently written as a direct response to the *Peregrine* decision, expresses the drafters' desire to influence lawmakers and courts to place greater emphasis on the UCC, rather than individual federal laws that are not well-suited to regulate asset securitization.[100] Contrary to *Peregrine*, the Committee suggests that the Copyright Act does not run afoul of Revised Article 9.[101]

The *Peregrine* court, in contrast, held that even if a lender attempted to secure an interest in a library of copyrighted works by filing a security agreement and UCC-1 financing statements in the appropriate state offices, it did not have a secured interest in the assets because it failed to file the interest with the Copyright Office.[102] The court determined that a "transfer" under the Copyright Act included either a "mortgage" or "hypothecation of a copyright,"[103] which the court concluded encompassed the security interest at issue.[104] Ultimately, the court held that the Copyright Act completely preempted the UCC.[105]

This decision, however, has been highly criticized.[106] Such a broad reading of the Copyright Act may not have been the best interpretation. Revised Article 9 lends support for the proposition that the federal courts should revisit the *Peregrine* decision and make the UCC the sole vehicle for filing a security interest in a copyright. The result would be simplified filing for all creditors who seek to create rights in

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[99] Rev. U.C.C. § 9-109(c)(1), cmt. 8 (2001).

[100] Some predict that this new section may change the result seen with reference to the copyright law and relegate authority in a copyrightable work to the UCC rather than the federal copyright code. HAKES, *supra* note 8, at 64. Due to the newness of Revised Article 9 and the likely precaution of investors following the judicial decisions surrounding copyright filing, courts have yet to entertain a case that will test these new rules.

[101] William W. Chip, Note, *Transfers of Copyrights for Security under the New Copyright Act*, 88 YALE L.J. 125, 133 (1978) (stating that the Copyright Act "is far from comprehensive" as a security statute).

[102] *In re* Peregrine Entm't Ltd., 116 B.R. 194 (Bankr. C.D. Cal. 1990).

[103] *Id.* at 199; *see also* 17 U.S.C. § 205(d) (1976).

[104] *In re* Peregrine Entm't Ltd., 116 B.R. at 199.

[105] *Id.* (quoting CCNV v. Reid, 490 U.S. 730 (1989)).

[106] Rothstein, *supra* note 29.

an e-commerce vendor's copyrightable works.[107] This simplified filing would likely give lenders the added security they want and, therefore, lead to more flexible lending for e-commerce ventures looking to survive in this declining economy.

## IV. The Governance of Intellectual Property in Financial Transactions

### A. *The Trademark Model*

A trademark is a name, image, symbol, sound, or device used in the stream of commerce to identify a good or service.[108] Trademarks are governed under both state common law and federal law under the Lanham Act.[109] Trademarks allow consumers to identify a product or service with a particular name and the goodwill associated with that product or service.[110]

Trademarks are one of the most prominent assets on the Internet, because names and reputations are uniquely important on the Internet.[111] Many consumers searching for e-commerce retailers prefer to shop at established sites, in order to ensure that they will receive the products that they purchase over the Internet. Moreover, familiarity establishes a security that a consumer's credit card and personal information is not exposed to criminals.[112]

Creditors lending funds to e-commerce vendors against company trademarks must rely on Revised Article 9 to perfect a security in these assets.[113] Courts have concluded that perfection of a security interest in a federally registered trademark can only be achieved by filing a UCC-1 financing statement.[114] In the leading case in this area, *In re Roman Cleanser Co.*,[115] a creditor claimed that it had a security interest in the trademarks of the debtor.[116] The borrower, Roman Cleanser, granted the lender a security interest "in and to all of Roman

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[107] Moreover, the federal intellectual property laws—i.e., the Lanham Act and the Copyright Act—are not properly suited to provide the level of protection contemplated under the UCC.

[108] *See* 15 U.S.C. § 1127 (1946).

[109] 15 U.S.C. § 1051 et. seq. (1999); *see also* Murphy, *supra* note 2, at 311.

[110] *Id.*

[111] Danielle Weinberg Swartz, *The Limitations of Trademark Law In Addressing Domain Name Disputes*, 45 UCLA L. Rev. 1487, 1491-92 (1998).

[112] *See id.*

[113] *In re* Roman Cleanser Co., 43 B.R. 940 (Bankr. E.D. Mich. 1984), *aff'd*, 802 F.2d 207 (6th Cir. 1986); *In re* Together Dev. Corp., 227 B.R. 439 (Bankr. D. Mass. 1998).

[114] *Roman Cleanser Co.*, 43 B.R. at 940.

[115] *Id.*

[116] *Id.*

Cleanser's then owned and thereafter acquired goods, equipment, and general intangibles . . . ."[117] In 1984, Roman Cleanser filed for bankruptcy.[118] The bankruptcy trustee attempted to avoid the lender's security interest, arguing that in order to perfect a security interest in a federally registered trademark, a creditor must file with the United States Patent and Trademark Office ("PTO"). In *Roman Cleanser Co.*, the creditor filed a UCC-1 financing statement with the state, but not with the PTO.[119] The trustee argued that because there was no federal filing, perfection of the interest never occurred.[120] The Sixth Circuit disagreed, holding that the creditor perfected its interest properly via state filing.[121]

The court in *In re Together Development Corp.*[122] also found that state filing, rather than filing with the PTO under the federal Lanham Act, was required for securitization of trademark assets.[123] Because the lender only filed the security interest with the PTO, the interest was unperfected.[124] Therefore, the court held that the lender's security interest was "subordinate to the Debtor's rights as a lien creditor, and the Debtor may avoid that security interest."[125] The court further commented that the federal intellectual property laws "should be amended to place them in better harmony with the Code."[126]

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[117] *Id.*

[118] Roman originally filed a Chapter 11 petition that was later converted to a Chapter 7 liquidation. *Id.* at 942.

[119] *Roman Cleanser Co.*, 43 B.R. at 942.

[120] *Id.*

[121] *Id.* at 942-45. Apart from the court's holding regarding how to perfect a security interest in a trademark, the *Roman Cleanser* opinion is interesting in several other respects. First, the opinion suggests that use of the phrase "general intangibles" in the security agreement and financing statement will extend the security interest to intellectual property, such as trademarks, whether specifically described or not. Second, and similarly, the court seems to assume that the phrase "general intangibles" also extends to the goodwill associated with the trademark. *Id. Cf. In re* Specialty Foods of Pittsburgh, Inc., 8 U.C.C. Rep. Serv. 2d 491 (Bankr. W.D. Pa. 1989) (noting that a financing statement should articulate the interest that is held in general intangibles, namely trademarks, service marks, trade names, and goodwill of the debtor).

[122] *In re* Together Dev. Corp., 227 B.R. 439 (Bankr. D. Mass. 1998).

[123] *Id.*

[124] *Id.*

[125] *Id.* at 442.

[126] *Id.* The court in *In re 199Z, Inc.*, 137 B.R. 778 (Bankr. C.D. Cal. 1992), concurred, holding that the state commercial code governed, and therefore the proper filing location is with the state. The *199Z* court determined that the Lanham Act was insufficiently vague to apply to a security interest. *Id.* As the court stated, "had Congress intended that security interests in trademarks be perfected by filing with the Patent Office, it could have expressly provided for such a filing . . . ." *Id.* at 782. Since the Lanham Act did not specify an application to security interest filings, but limited itself to assignments, the state rather than the federal system provides the proper filing location. *Id.* Both the *199Z* court and the *Together*

The trademark model recognizes that Revised Article 9 establishes a comprehensive system equipped to handle security interests in intellectual property. Furthermore, trademarks are not the only form of intellectual property that utilizes Revised Article 9 in governing secured transactions.

### B. *The Patent Model*

The world of e-commerce is brimming with new and useful inventions protected under patent law.[127] Similar to copyrights, federal law exclusively governs patents. The federal authority for this governance is derived from the Intellectual Property Clause of the United States Constitution.[128] The Supreme Court has held that the Patent Act preempts conflicting state law.[129] Other courts, however, have held that the Patent Act does not preempt Article 9 of the UCC because there is no conflict.[130] The federal government grants patents to inven-

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*Dev.* court agreed that an assignment is not the same as a security interest, noting that a security interest is a future interest in intangible property, while an assignment is a complete transfer of the intangible property. *See In re 199Z, Inc.*, 137 BR at 778; *In re Together Dev.*, 227 B.R. at 439.

[127] Most significantly, several e-commerce entrepreneurs employed the business method patent to protect the novel way they do business on the Internet. Linda E. Alcorn, *Protecting Your Intellectual Property Assets: The Value of Business Method Patents*, 709 PLI/Pat 425, 432 (2002). "A business method is any new, non-obvious and useful process by which a company does business, whether or not the process is technical." *Id.* Recent decisions support this trend for the business method patent. In *State St. Bank & Trust Co. v. Signature Fin. Group, Inc.*, 149 F.3d 1368 (Fed. Cir. 1998), the Federal Circuit determined that patent protection could be granted to a computer data processing system. This decision represents a significant departure from traditional patent cases, because the court afforded patent protection to a business method that encompassed a mathematical algorithm. Lipson, *supra* note 58, at 1078-79. In *State St. Bank*, the court held that a data processing system used for implementing an investment structure could be subject to patent protection, despite its mathematical component. *State St. Bank*, 149 F.3d at 1368. This decision opened the door for e-commerce ventures to achieve patent protection for the mechanisms the ventures establish for engaging in commerce on the Internet. The holding in *AT&T Corp. v. Excel Communications, Inc.*, 172 F.3d 1352, 1358 (Fed. Cir. 1999), *cert. denied*, 528 U.S. 946 (1999), expanded the holding in *State St. Bank* to "methods." These decisions paved the way for the Federal Circuit to provide patent protection for Internet retailer Amazon.com's "one-click" method for placing orders over the internet. Amazon.com, Inc. v. Barnesandnoble.com, 239 F.3d 1343, 1347-49 (Fed. Cir. 2001).

[128] U.S. CONST. art. I, § 8, cl. 8. "To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries." *Id.*

[129] Bonito Boats, Inc. v. Thunder Craft Boats, Inc., 489 U.S. 141, 168 (1989); Compco Corp. v. Day-Brite Lighting, Inc., 376 U.S. 234, 237 (1964); Sears, Roebuck & Co. v. Stiffel Co., 376 U.S. 225, 231 (1964).

[130] *In re* Transp. Design, 48 B.R. 635, 638 (Bankr. S.D. Cal. 1985); Moldo v. Matsco, Inc. (*In re* Cybernetic Servs.), 252 F.3d 1039 (9th Cir. 2001); Lipson, *supra* note 58, at 1114 (2001).

tors for a term of twenty years.[131] Patent law exists "to protect the development of new technology and encourage its use."[132] Patents are granted to inventors as monopolies on the rights to make, use, and sell their inventions for a limited term, and they are exclusively federal in nature.[133] Patents are governed under Title 35 of the United States Code ("Patent Act").[134] Furthermore, all patent claims are litigated within the U.S. Court of Appeals for the Federal Circuit in Washington, D.C. ("Federal Circuit").[135] In fact, the Federal Circuit is commonly referred to as the Supreme Court of Patents.[136]

The bankruptcy court in *In re Transportation Design*[137] held that filing a UCC-1 financing statement was the proper mechanism to perfect a security interest in a patent.[138] The court stated that although the Patent Act did not sufficiently address the perfection of patents, the UCC filing system presented a comprehensive scheme to protect security rights in those assets.[139] The Ninth Circuit Court of Appeals, in *In re Cybernetic Services*,[140] later agreed with the bankruptcy court.[141] The court took a "pragmatic" approach in determining that the Patent Act fails to preempt a state commercial law under Article 9.[142] The *Cybernetic* court concluded that Article 9 is "a state commercial law that provide[s] a method for perfecting a security interest in a federally protected patent."[143] Hence, the court concluded that Article 9's filing system provided the proper mechanism to perfect a security interest.[144]

Again, the patent model shows that Revised Article 9 is the appropriate mechanism for governing intellectual property financial transactions involving the use of these assets as collateral. Nevertheless, although the courts have resolved that Revised Article 9 should be used for secured transactions involving trademarks and patents, they have not followed suit in dealing with copyrights.

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[131] Murphy, *supra* note 2, at 310.

[132] *In re Transp. Design*, 48 B.R. at 638 (citing Patent Act of 1836, ch. 357, § 11, 5 Stat. 117).

[133] 35 U.S.C. § 154(a)(1) (2003).

[134] 35 U.S.C. § 101-212 (2003).

[135] Matt Krantz, *Computer & Technology Patent Suits Try Patience of High-Tech Companies*, INVESTOR'S BUS. DAILY, Dec. 9, 1996, at A6.

[136] *Id.*

[137] 48 B.R. at 635.

[138] *Id.*

[139] *Id.* at 637.

[140] Moldo v. Matsco, Inc. (*In re* Cybernetic Servs.), 252 F.3d 1039 (9th Cir. 2001).

[141] *Id.* at 1044.

[142] *Id.* at 1046.

[143] *Id.*

[144] *Id.*

## V. THE CASE FOR COPYRIGHT TO BE SECURED UNDER REVISED ARTICLE 9

Copyrights are governed exclusively by federal law and protect original works of authorship.[145] The Copyright Act, however, does not require filing the actual work to obtain copyright protection; rather, this protection exists once the author/creator fixes the work in any tangible medium of expression.[146] The Copyright Act vests a "bundle of rights" in a copyright owner.[147] These exclusive rights include the right to reproduce, create derivative works, distribute, publicly perform, publicly display, and create digital transmissions of sound recordings.[148] These rights can be transferred as a "bundle" or separately.[149]

Copyright is one of the most essential assets to an e-commerce business, because it provides protection for all works fixed in a tangible medium, including software.[150] Therefore, it is critical for a careful lender to properly secure its interest in a borrower's copyright. Deter-

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[145] 17 U.S.C. § 102 (1976).

[146] Murphy, *supra* note 2, at 310.

[147] 17 U.S.C. § 106 (1976).

[148] 17 U.S.C. § 106 (1)-(6) (1976).

[149] *Id.*

[150] 17 U.S.C. § 117 (1998). Perhaps one of the most progressive changes in Revised Article 9 is that it specifically creates a method for lenders to acquire a security interest in software. Mary Jo Dively, *Intellectual Property as Collateral*, ALI-ABA Course Outline, SG023 ALI-ABA 235, 237 (Sept. 2001). In the growing e-commerce world, this is a necessary revision to keep up with the modern state of commerce. Cohen, *supra* note 84, at 254. Businesses attempting to maintain a presence on the Internet are dependent on software to keep their businesses moving. *Id.* An Internet presence requires the use of software to function on the Web. *Id.* Software programs allow e-commerce vendors to create and maintain web pages, to collect, store and retrieve data about their patrons and their inventory, and to generally complete commercial transactions on the Internet. *Id.*

These software programs are often some of the most valuable assets an e-business possesses. *Id.* at 256. An e-commerce retailer's unique programs to gather information or to better process customer orders can be an indispensable commodity providing significant value as collateral. *Id.* at 255. However, a lender holding an interest in an e-commerce company's unique software must be sure to become familiar with the software to determine whether the third party software is necessary to operate the software. Roy, *supra* note 1, at 4.

To generate income, e-commerce businesses often license advanced software programs in the ordinary course of business. This income-generating license may also be marketed as an asset when the e-commerce vendor is looking for a loan under the Revised Article 9. Rev. U.C.C. § 9-315(c) (2001). However, since the Revised Article 9 allows all proceeds to follow the perfected collateral, the license fees collected by third parties for an owner's software are proceeds of the software. Dively, *supra* at 237. In many cases this third party software—such as a run-time version of Java, Real Player, or Adobe Acrobat—will be commercially available, and thus does not create a problem for subsequent owners of the software. *Id.* If the third party software is not commercially available and the borrower's license to use that software is not transferable, however, the lender must obtain the ability to license the third party software for the collateral software to be useful or marketable. *Id.*

mining how to perfect an interest in a copyrightable work, however, is unclear.

Under Former Article 9, an internal conflict existed in determining whether the UCC or federal law should govern copyrights.[151] While the general step-back[152] provision within Former Article 9 seemed to suggest that the UCC should apply to copyrighted works, the filing step-back provision did not.[153] Revised Article 9 attempts to clarify this internal conflict by proposing that more assets should be governed under the UCC rather than under federal law.[154] Although section 311 of Revised Article 9 still gives priority to federal filing in some cases, the definition is narrowed to "a statute, regulation, or treaty of the United States whose requirements for a security interest's obtaining priority over the rights of a lien creditor with respect to the property."[155] With the Copyright Act in mind, section 311 attempts to avoid preemptive effect by utilizing narrow language, recommending that only federal laws that specifically discuss the priority rights of security interests should preempt the UCC.[156] This language, coupled with the UCC's "scope" provisions, states that "[t]his article does not apply to the extent that: a statute, regulation, or treaty of the United States preempts this article" and demonstrates the drafters' intention to make clear that the UCC will only be preempted by a federal scheme that specifically contemplates the securitization of assets.[157]

Although many commentators agree that this revised section may prompt courts to more narrowly interpret the federal laws that preempt the UCC and expand the scope of property covered by Revised Article 9, some skeptics argue that it will not change the registration proce-

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[151] Fmr. U.C.C. §§ 9-104, 9-302 (1989).

[152] The preemption sections of Former and Revised Article 9 are referred to as "step-back" provisions because they are sections that "step-back" from the UCC and defer to federal law. *See* NEW ARTICLE 9, *supra* note 11.

[153] In the "Transactions Excluded" section of the Former Article 9, also known as the "general step-back" provision, the Official Comment notes that

> [a]lthough the Federal Copyright Act contains provisions permitting the mortgage of a copyright and for the recording of an assignment of a copyright . . . such a statute would not seem to contain sufficient provisions regulating the rights of the parties and third parties to exclude security interests in copyrights from the provisions of this Article.

Fmr. U.C.C. § 9-104, cmt. 1 (1989). The filing step-back provision differed, however, stating in its Official Comments that the Copyright Act is an example of a statute that has a filing system sufficient to perfect a security interest, thereby making it impermissible to file under the UCC. Fmr. U.C.C. § 9-302, cmt. 1 (1989).

[154] Rev. U.C.C. § 9-109(c)(1) (2001); Rev. U.C.C. § 9-311 (2001).

[155] Rev. U.C.C. § 9-311(a)(1) (2001).

[156] *Id.*

[157] Rev. U.C.C. § 9-109(c)(1) (2001).

dures.[158] Skeptics argue that current case law, which holds that the Copyright Act completely preempts Former Article 9, will remain.[159] Revised Article 9 should bring new clarity to the issue and allow future courts to reconsider the holding in *Peregrine*, with the hopeful result of finding that the Copyright Act does not preempt Revised Article 9. A reconsideration of the current state of the law would allow copyright registrants to file exclusively under Revised Article 9, paralleling the process for all other forms of intellectual property.

Some courts have held that the federal Copyright Act preempts the UCC for the recordation of a registered copyright.[160] Under these cases, a creditor holding rights in a registered copyright must file the security agreement[161] in the United States Copyright Office ("Copyright Office") to perfect its interest and prevail over the rights of a judicial lien creditor.[162] *Peregrine*,[163] the seminal case in this area, involved a bankruptcy proceeding where the lender held a security interest in the debtor's "library of copyrights, distribution rights, and licenses to approximately 145 films, and accounts receivable arising from the licensing of these films to various programmers."[164] The lender bank gave the debtor a $6 million line of credit secured by the film library collection.[165] The lender attempted to secure its interest by filing a security agreement and UCC-1 financing statements.[166] The bank filed the UCC-1 financing statements in the appropriate state offices but failed to record its security interest in the Copyright Office.[167]

On January 30, 1989, Peregrine filed a voluntary petition for bankruptcy under Chapter 11. In April, using the strong-arm clause of the Bankruptcy Code,[168] Peregrine attempted to avoid the bank's security interest in the copyrighted works, claiming that failing to file with the Copyright Office left the interest unperfected.[169] The bankruptcy court

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[158] Lipson, *supra* note 58, at 1097.

[159] *Id.*; *see also In re* Peregrine Entm't Ltd., 116 B.R. 194 (Bankr. C.D. Cal. 1990).

[160] *In re* Peregrine Entm't Ltd., 116 B.R. at 194; *In re* Avalon Software, Inc., 209 B.R. 517, 522 (Bankr. D. Ariz. 1997).

[161] A security agreement is the contract entered into between the lender and borrower. *See* NEW ARTICLE 9, *supra* note 11.

[162] Paul A. Baumgarten, *Copyrights as Collateral: Perfection Finally Perfected After* Peregrine?, 71 U. DET. MERCY L. REV. 581 (1994).

[163] *In re* Peregrine Entm't Ltd., 116 B.R. at 194.

[164] *Id.* at 197.

[165] *Id.*

[166] *Id.*

[167] *Id.* at 198.

[168] Section 544 of the U.S. Bankruptcy Code is "commonly known as the 'strongarm clause,' [because] a trustee has the authority to avoid unperfected liens to the same extent as certain hypothetical ideal creditors." *In re* Rubia, 257 B.R. 324, 329 (10th Cir. 2001).

[169] *In re* Peregrine Entm't Ltd., 116 B.R. at 198.

disagreed.[170] On appeal, the court held that Peregrine's interest in the copyrights trumped the bank's security interest.[171] Judge Kozinski, sitting by designation, stated that the bank's failure to record its security interest in the Copyright Office prior to the bankruptcy filing left the interest unperfected and open to avoidance.[172] Thus, the court deemed that the bank's security interest, as to both the copyrighted works and the accounts receivable proceeds generated by the copyrights, was unperfected .[173]

The court concluded that a literal reading of the definition of "transfer" under the Copyright Act included either a "mortgage" or "hypothecation of a copyright."[174] The expansive language, the court held, encompassed the security interest at issue.[175] This language, coupled with the court's belief that copyright law "promote[s] national uniformity" and "avoid[s] the practical difficulties of determining and enforcing an author's rights under the differing laws in the separate courts of the various States," led the court to rule that the Copyright Act completely preempts the UCC.[176]

The decision in *Peregrine* has resulted in tremendous controversy.[177] The debate focuses primarily on the impracticality of the federal filing system and potential for dual filing.[178] First, although the court acknowledged in a footnote that federal filing of a variety of copyrights might be a cumbersome process, the court grossly understated the problems involved.[179] For example, a commercial lender who seeks to gain collateral in a borrower's copyright must file individual applications for each work and continue to update filings as new works are created.[180] Federal filing also places a burden on the lender, by requiring it to ensure that the borrower maintains registration of the copyright via the renewal process.[181] Conversely, filing only a UCC-1 financing statement merely necessitates that a lender specify that it is obtaining a security interest in the borrower's "general intangibles," re-

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[170] *Id.*

[171] *Id.* at 207.

[172] *Id.*

[173] *Id.*

[174] 17 U.S.C. § 205(d) (1976).

[175] *In re* Peregrine Entm't Ltd., 116 B.R. at 206.

[176] *Id.* at 199 (quoting CCNV v. Reid, 490 U.S. 730 (1989)).

[177] MANN, *supra* note 22, at 621.

[178] *Id.* at 610.

[179] *Id.*

[180] *Id.*

[181] *Id.*

quiring slightly more detail to explain any derivative rights the creditor may choose to possess.[182]

More significantly, the Copyright Act is not suited to deal with the complexities of modern commercial lending.[183] By simply perusing section 205 of the Copyright Act and Revised Article 9 of the UCC, one can observe how much detail is missing from the Copyright Act.[184] Section 205 takes up a few paragraphs, while Article 9 encompasses over 250 pages.[185] There are countless issues left unaddressed in the Copyright Act.[186] This absence of detail in relation to creating a security interest is justified, since the Copyright Act addresses copyright and not commercial transactions.[187] The Copyright Act does not address the plethora of issues involved in secured lending, such as royalty and linking agreements and various forms of content and data licenses.[188] This leaves a lender at the mercy of the UCC to ensure protection of these tangential rights.[189] Hence, utilization of the UCC for issues involving commercial lending would seem more appropriate than the Copyright Act.

Additionally, there is more uncertainty among the courts regarding perfection of a security interest in a copyrightable work when the copyright has not been registered.[190] In an Arizona case, *In re Avalon Software, Inc.*,[191] the court held that the Copyright Act completely preempted Article 9.[192] In this case, Avalon possessed an outstanding debt of $1.48 million, secured by both registered and unregistered copyrights.[193] The lender filed a UCC-1 financing statement in the proper state offices, but failed to file in the Copyright Office, claiming that filing in the federal office should only be required for registered copy-

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[182] *Id.*

[183] *Id.* at 621.

[184] *Id.*

[185] *Id.*

[186] 17 U.S.C. § 101-810 (1976).

[187] *See id.*

[188] *Id.* § 205.

[189] Marjorie Chertok & Warren E. Agin, *Restart.com: Identifying, Securing and Maximizing the Liquidation Value of Cyber-Assets in Bankruptcy Proceedings*, 8 AM. BANKR. INST. L. REV. 255, 269-270 (2000).

[190] HAKES, *supra* note 8, at 64. As explained within, copyright protection exists from the moment of fixation of a work in a tangible medium of expression; however, one may choose to register his copyrighted work with the Copyright Office in order to obtain increased rights in the work including the right to sue for copyright infringement and the ability to obtain treble damages. 17 U.S.C. § 412 (1976).

[191] 209 B.R. 517 (Bankr. D. Ariz. 1997).

[192] *Id.*

[193] *Id.*

righted works.[194] The court noted that "[t]he proper method . . . for a secured creditor to obtain a perfected security interest in either copyrighted or copyrightable property is to register that security interest with the United States Copyright Office."[195] The court aptly pointed out that registration "is not a condition of copyright protection" and that the Copyright Act applies to all copyrightable works.[196] Therefore, the court concluded that both registered and unregistered works must be filed in the Copyright Office.[197]

Other courts, however, have not followed this rule. In *In re AEG Acquisition Corp.*,[198] the debtor sought to invoke section 544(a)(1) of the Bankruptcy Code to avoid a security interest held by Zenith in three copyrighted works.[199] Only one of the three works was registered.[200] Zenith filed the security agreements but not the copyright registrations for two movies that were foreign works.[201] The court applied section 205(c) of the Copyright Act, which states,

> Recordation of a document in the Copyright Office gives all persons constructive notice of the facts stated in the recorded document, but only if—
> (1) the document, or material attached to it, specifically identifies the work to which it pertains so that, after the document is indexed by the Register of Copyrights, it would be revealed by a reasonable search under the title or registration number of the work; and (2) registration has been made for the work.[202]

The court explained the two-step process that must be followed to perfect a security interest in a copyright.[203] First, one must register the work with the Copyright Office.[204] Then, the lender must file the security interest with the Copyright Office.[205] Therefore, the court held that filing a security interest in the Copyright Office is only effective if the underlying registration is also recorded there.[206]

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194 *Id.*
195 *Id.* at 521.
196 *Id.* (quoting 17 U.S.C. § 408(a) (1976)).
197 *Id.* at 522.
198 127 B.R. 34 (Bankr. C.D. Cal. 1991).
199 *Id.*
200 *Id.*
201 *Id.*
202 17 U.S.C. § 205(c) (1976).
203 *AEG Acquisition Corp.*, 127 B.R. at 39-43.
204 *Id.*
205 *Id.*
206 *Id.* A more recent case agreed with the *AEG Acquisition Corp.* holding. In *In re World Auxiliary Power Co.*, the borrower used an unregistered copyrighted design as a security interest for a loan. *In re* World Auxiliary Power Co., 244 B.R. 149 (Bankr. N.D. Cal. 1999), *aff'd*, 303 F.3d 1120 (9th Cir. 2002). The lender bank filed a UCC-1 filing statement with the California Secretary of State, but it did not file the security agreement or the filing

Scholars explain this dichotomy between the courts as a distinction between "complete preemption" and "filing preemption."[207] The "complete preemption" theory dictates that the Copyright Act completely displaces Article 9 regarding both the copyright and the property closely related to the copyright.[208] On the other hand, the "filing preemption" theory maintains that the Copyright Act preempts only the filing rules of Article 9, leaving its other provisions such as creation, attachment, priority, and enforcement intact.[209]

*Peregrine*'s holding, that the bankruptcy trustee trumped the secured party as to both the copyrighted works and the proceeds of those works via royalty payments, is an example of complete preemption.[210] Similarly, the *Avalon* court's decision is an example of complete preemption, because the lender would be denied rights to both the security interest in the copyright, as well as all related property if the interest was not filed with the Copyright Office.[211] Conversely, the decision in *In re World Auxiliary Power*,[212] that a secured party is required to perfect its security interest in an unregistered copyright via a state UCC filing, is an example of filing preemption.[213]

*Peregrine* and like cases should be reexamined and overturned. In order to foster growth on the Internet and create a more simplified filing system, Congress should propose legislation to make it clear that section 205 of the Copyright Act was not intended to preempt Revised Article 9. This legislation would not only encourage more lenders to provide funding to borrowers who are highly dependent on copyrights

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statement with the Copyright Office. *Id.* at 150. Again, utilizing Bankruptcy Code § 544(a)(1), the debtor reasoned that the asset was unperfected because it had not been recorded with the Copyright Office. *Id.* The court refused to avoid the transfer. *Id.* The Court held that since the asset lacked federal copyright registration, filing a financing statement with the Copyright Office would be pointless. *Id.* at 151. Instead, the court reasoned that the only mechanism for obtaining a perfected security interest in an unregistered copyright was by filing a UCC-1 financing statement with the Secretary of State. *Id.* Since the lender followed this rule, the court determined the asset had been properly perfected, and therefore it was not avoidable. *Id.* Nonetheless, the court opined that the asset would be "vulnerable to invalidation if a copyright was later registered and a competing security interest in the copyright had been recorded in the Copyright Office." *Id.* at 154 n.11. This dictum led to the suggestion that "a prudent secured creditor would record its security agreement in the Copyright Office at the same time it filed its UCC-1 financing statement in the UCC Office." *Id.*

[207] Lipson, *supra* note 58, at 1108.

[208] *Id.*

[209] *Id.* at 1109.

[210] *Id.* at 1110.

[211] *Id.* at 1112.

[212] *In re* World Auxiliary Power Co., 244 B.R. 149 (Bankr. N.D. Cal. 1999), *aff'd*, 303 F.3d 1120 (9th Cir. 2002).

[213] Lipson, *supra* note 58, at 1112.

as collateral, but may also help jump-start the struggling e-commerce community. By fostering this lending to e-commerce ventures and thereby fostering growth on the Internet, Congress would be taking yet another step forward in its attempt to revive the United States' waning economy.

Although this Comment is not the first to propose such legislation, past proposals were not as timely. Congress did not have the impetus to pass this type of legislation in the past because most of the businesses affected were traditional "brick-and-mortar" companies that had multiple assets available to obtain financing; the e-commerce surge had not arrived. Furthermore, the yearly stages of e-commerce development did not require this change in the law, as venture capitalists in the robust economy were willing to take risks that were often highly profitable. Today, however, the state of the economy has declined, and the e-commerce ventures are struggling to obtain financing based on their limited assets. Hence, the resurrection of this topic is uniquely essential to ensure growth on the Internet.

## VI. CONCLUSION

All of the cases discussed within were decided prior to the enactment of Revised Article 9. Revised Article 9's new strict preemption clause advises federal courts and legislators to narrow the scope of federal laws that should preempt the Code.[214] Hence, heeding the advice established in Revised Article 9, courts should reject *Peregrine* and similarly decided cases,[215] and Congress should propose legislation stating that section 205 of the Copyright Act does not preempt Revised Article 9.

Revised Article 9 represents a significant step forward for e-commerce. Through careful drafting, Revised Article 9 should now allow e-commerce vendors to more easily and securely utilize their copyrights, software, trademarks, and domain names as security interests, allowing these vendors to gain the funding required to build meaningful ventures on the Internet. Revised Article 9 acknowledges that e-commerce is an important part of today's economy by making the expansions discussed previously, which are essential to the growth of commerce on the Internet. Furthermore, high-tech Internet companies are dependent on gaining access to capital through the collateralization of intellectual property.[216] As such, Revised Article 9 fosters invest-

[214] Rev. U.C.C. § 9-109(c)(1) (2001).
[215] Nicewander, *supra* note 45, at 170-71; HAKES, *supra* note 8, at 64.
[216] Dornbos, *supra* note 76, at 657.

ment in on-line corporations by allowing e-commerce businesses to grant a security interest in their copyrighted software or customer databases.[217]

The revision of the general step-back provision, suggesting a limitation of the statutes that should be preempted by Revised Article 9, is the most progressive provision of the UCC. This new provision, coupled with a heightened understanding of the Copyright Act via the proposed legislation discussed above, would open the door for the courts to overturn *Peregrine* and allow lenders to file a security interest in the proper state office rather than with the PTO. This revision may make it easier for lenders to secure an interest in intangible copyrights used as collateral. Because the UCC allows lenders to merely specify the class of goods and the derivative rights granted in those works in the financing statement, the lenders can be sure to capture all of the borrowers' copyrights. Conversely, filing with the Copyright Office requires individual filing for each work.[218] This cumbersome process lends itself to error. Furthermore, if a borrower fails to renew copyright registration or makes a derivative work, the lender will not have collateral in those works.[219]

Finally, as a practical matter, filing solely under the UCC actually promotes the goals of the Copyright Act when dealing with software. Because some courts have held that the state office is the proper location for the filing of unregistered copyrights,[220] some companies may choose not to register to allow lenders the ease of state filing. Many software programmers, already weary of others obtaining their valuable code, are likely to hesitate to register their copyrightable software. This fear, combined with the programmers' need to utilize the software as collateral for loans, may convince e-commerce ventures to forgo registration, which will allow lenders to file UCC-1 financing statements, rather than filing with the Copyright Office. If the UCC were the primary filing vehicle for all copyrights, regardless of whether or not the copyright is registered, more programmers would be willing to register their software, thereby creating the notice advocated in the Copyright Act.

Lenders should not be required to monitor thousands of intangibles to ensure registrations are filed and renewed. It is neither the

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[217] Rev. U.C.C. § 9-102(a), cmt. 5(d) (2001) (noting that general intangibles include all forms of personal property not otherwise included, i.e., software).

[218] 37 C.F.R. § 201.4 (2003).

[219] *See* Brennan, *supra* note 96.

[220] *In re* World Auxiliary Power Co., 244 B.R. 149 (Bankr. N.D. Cal. 1999), *aff'd*, 303 F.3d 1120 (9th Cir. 2002); *In re* AEG Acquisition Corp., 127 B.R. 34 (Bankr. C.D. Cal. 1991).

function nor the expertise of the lender to participate in intellectual property monitoring. A new copyright law in tandem with Revised Article 9 would allow for state filing alone, thus easing the process and ensuring that all versions of a work are incorporated in the security agreement. This added security would give lenders solace when offering funding to new or developing e-commerce vendors.

Scholars, practitioners, and students of the UCC await the Congress' and courts' response to several of these matters. Ultimately, with time, the legislature and judiciary will meaningfully fill in the various interstices and give enhanced understanding to Revised Article 9's comprehensive and laudable vision. With this new vision, we can anticipate an easier mechanism for protection of the new economy's most valuable assets.