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Intellectual Property Financing: Security Interests in Domain Names and Web Contents

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INTELLECTUAL PROPERTY FINANCING: SECURITY INTERESTS IN DOMAIN NAMES AND WEB CONTENTS

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I. INTRODUCTION

Intellectual property has become an increasingly valuable corporate asset. Not surprisingly, many companies use intellectual property for security purposes in commercial financing schemes. The recent revision of Article 9 of the Uniform Commercial Code (UCC) was drafted with a comprehensive understanding of how intellectual property has been used generally in commercial transactions and as collateral in secured transactions.¹ The revised Article 9 aims to facilitate more financing schemes secured by intangible assets in electronic com-

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1. See Steven O. Weise, *The Financing of Intellectual Property Under Revised UCC Article 9*, 74 CHI.-KENT L. REV. 1077, 78–79 (1999) (explaining the reviewing process conducted by the Drafting Committee for Revised Article 9 on intellectual property).

merce.² Given the growth of borderless, electronic commerce, new intellectual property assets such as domain names and web contents are often the primary assets of online companies.³ If these assets are secured for purposes of obtaining financing for online companies, both the lender (creditor/investor) and the online company (debtor) should understand the nature of the assets and how a security interest in the assets is perfected. Most importantly, from the lender's side, having a perfected security interest will provide the lender priority in the intangible assets over the bankruptcy trustee in the event the online company is insolvent. From the online company's side, it is important to understand how the securing of intellectual property is achieved and what impact it may have on the company's daily operation.

II. UNDERSTANDING THE NATURE OF THE NEW CYBERASSETS— DOMAIN NAMES AND WEB CONTENT

Domain names are first-come, first-served.⁴ They serve dual functions: as Internet addresses and as source identifiers.⁵ Many online companies use their brands or trademarks as domain names. Internet users who search for a product, a service, or a company often employ two methods of searching.⁶ If the user knows the domain name, she will enter the domain name directly at the URL. If the user does not know the domain name, she will employ one of the search engines,

2. An example of how the revised Article 9 facilitates financing schemes secured by intangible assets is the new U.C.C. § 9-408 (2001). U.C.C. § 9-408 makes ineffective any attempt to restrict the assignment of general intangible. This result allows the creation, attachment, and perfection of a security interest in general intangibles. Consequently, this enhances the debtor's ability to obtain financing. See U.C.C. § 9-408 & cmt. 2.

3. See A. Michele Dickerson, *From Jeans to Genes: The Evolving Nature of Property of the Estate*, 15 BANKR. DEV. J. 285, 299-300 (1999) (noting the nature of intangible assets of online companies).

4. See generally *Brookfield Communications, Inc. v. W. Coast Entm't Corp.*, 174 F.3d 1036, 1044, 50 USPQ2d 1545, 1549 (9th Cir. 1999) (explaining the domain name assigning system). The Ninth Circuit noted that:

[t]o obtain a domain name, an individual or entity files an application with Network Solutions listing the domain name the applicant wants. Because each web page must have a unique domain name, Network Solutions checks to see whether the requested domain name has already been assigned to someone else. If so, the applicant must choose a different domain name. Other than requiring an applicant to make certain representations, Network Solutions does not make an independent determination about a registrant's right to use a particular domain name.

Id. (citation omitted); *Lockheed Martin Corp. v. Network Solutions, Inc.*, 985 F. Supp. 949, 953, 44 USPQ2d 1865, 1868-69 (C.D. Cal. 1997) (explaining Network Solutions's role in the domain naming system), *aff'd*, 194 F.3d 980, 52 USPQ2d 1481 (9th Cir. 1999).

5. See *Sallen v. Corinthians Licenciamentos LTDA*, 273 F.3d 14, 19, 60 USPQ2d 1941, 1944-45 (1st Cir. 2001) (explaining the function of domain names).

6. See *Brookfield*, 174 F.3d at 1044, 50 USPQ2d at 1549.

guessing the name of the source and entering a word or phrase. The search engine will conduct a search in the URLs and metatags and provide the user with a result.⁷

Because domain names generally comprise words or phrases, domain name owners look to trademark law for protection of their domain names.⁸ To ascertain whether a domain name is a protectable trademark, the domain name must be used in commerce as a source identifier. The domain name must be arbitrary, fanciful, or suggestive. If a domain name is descriptive of the goods or services, it must acquire secondary meaning through use and advertising in order for it to receive trademark protection. If a domain name is generic, it is not protected under trademark law.⁹

Ironically, some domain names that are not protectable under trademark law are highly valued in electronic commerce. These generic domain names command large sums in the secondary market.¹⁰ For example, business.com was purchased by a company for \$7.5 million¹¹ and loans.com for \$3.0 million.¹² Obviously, an online company having valuable domain names as corporate assets needs to know the value of its domain name and how it can use the domain name in commercial financing.¹³

In addition to domain names, many online companies have web contents as their most valuable assets. Web contents are divided into two categories: copyrightable contents and non-copyrightable contents. Copyrightable content includes music, literary text, software, graphics, and sounds.¹⁴ Such content should be registered with the

7. *Id.* at 1044, 50 USPQ2d at 1549–50 (stating that under the first search method employed by web users who often assume that the domain name of a particular company will be the company name followed by .com and under the second method, the web user will guess key words to input into a search engine).

8. See generally Xuan-Thao Nguyen, *Shifting the Paradigm in E-commerce: Move Over Inherently Distinctive Trademarks – the E-brand, I-brand and Generic Domain Names Ascending to Power?*, 50 AM. U. L. REV. 937 (2000) (analyzing legal protection for generic domain names under both trademark and unfair competition law).

9. *Id.* at 958–72.

10. See generally GreatDomains.com for auctions of domain names in the secondary market. GREATDOMAINS.COM at <http://www.greatdomains.com> (last visited Mar. 6, 2002).

11. Greg Johnson, *The Costly Game for Net Names: In the Dot-com World, Recognition is Everything*, L.A. TIMES, Apr. 10, 2000, at A1 (reporting the purchase of business.com).

12. See Cynthia Flash, *Are They Cybersquatters or Cyberentrepreneurs?* CMP Techwire, July 20, 2000 (reporting that Bank of America purchased loans.com for \$3.0 million).

13. See Francis G. Conrad, *Dot.coms in Bankruptcy Valuations Under Title 11 or WWW.snipehunt in The Dark.Noreorg/Noassets.com*, 9 AM. BANKR. L. REV. 417 (2001) (discussing valuation of domain names).

14. See generally *A & M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004 (9th Cir. 2001) (discussing contributory copyright infringement of online music); *Playboy Enters., Inc. v. Webworld, Inc.*, 991 F. Supp. 543 (N.D. Tex. 1997) (upholding claim for

Copyright Office.¹⁵ Copyright law provides copyright protection during the life of the author and for seventy years thereafter.¹⁶ If the content is a work for hire, the copyright term is 95 years from the year of its first publication or 120 years from the year of its creation, whichever expires first.¹⁷

Non-copyrightable content includes information, facts, and data. Such content does not enjoy copyright protection.¹⁸ The compilation of the non-copyrightable content that satisfies the originality test is protected under copyright law, though the protection is very thin.¹⁹ Many online companies own mostly non-copyrightable content. The non-copyrightable contents are valuable to such companies as they expend significant resources to create the contents.²⁰

When an online company uses its copyrightable and non-copyrightable web contents as collateral to secure a debt, payment, or performance of an obligation, Article 9 of the UCC governs the secured transaction.²¹

III. UNDERSTANDING SECURITY INTERESTS IN DOMAIN NAMES AND WEB CONTENTS

Under Article 9 of the UCC, domain names and web contents are classified as "general intangibles." General intangible is a catch-all classification of property "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."²² The term "gen-

copyright infringement for reproducing images on a website without authorization), *aff'd*, 168 F.3d 486 (5th Cir. 1999).

15. See 17 U.S.C. § 412 (2000) (stating that copyright registration is a prerequisite to infringement suit and certain remedies).

16. *Id.* § 302(a).

17. *Id.* § 302(c).

18. See *generally* Feist Publ'ns, Inc. v. Rural Tel. Serv. Co., 499 U.S. 340, 345-49 (1991) (explaining why factual information is not copyrightable due to the lack of originality).

19. *Id.* at 349 ("[T]he copyright in a factual compilation is thin.").

20. Internet companies like eBay rely on non-copyrightable content as their assets. eBay brought copyright infringement actions against other Internet companies for copying its content, but could not prevail because the content was non-copyrightable. eBay then successfully asserted a claim for trespass to online chattels. See *eBay v. Bidder's Edge, Inc.*, 100 F. Supp. 2d 1058 (N.D. Cal. 2000). See *generally* Allison Roarty, Note, *Link Liability: The Argument for Inline Links and Frames as Infringements of the Copyright Display Right*, 68 *FORDHAM L. REV.* 1011, 1036-58 (1999) (discussing the law of misappropriation and how it can be applied to curb theft of time-sensitive web contents).

21. U.C.C. § 9-109(a)(1) (2001) ("[Article 9] applies to a transaction, regardless of its form, that creates a security interest in personal property or fixtures by contract."); *id.* § 1-201(37) ("Security interest" means an interest in personal property or fixtures which secures payment or performance of an obligation.").

22. *Id.* § 9-102(42).

eral intangible” also includes payment intangibles and software.²³ The Official Comment 5(d) to the definition of “general intangible” indicates that the definition includes “various categories of intellectual property.”²⁴

A security interest in domain names and web contents is distinguishable from an assignment of ownership in the domain names and web contents.²⁵ An assignment is an absolute transfer of the entire right in the domain names and web contents.²⁶ The grant of a security interest in the domain name and web contents is less than a transfer of the entire rights; it is an agreement to assign the domain names and web contents in the event of default by the debtor.²⁷

A lender who provides finance to a debtor and takes a security interest in the debtor’s new cyberassets should know that its security interest in the cyberassets is not enforceable against the debtor and other third parties unless three requirements are satisfied.²⁸ First, the debtor must have rights in the cyberassets or power to transfer rights in the cyberassets. Second, the lender provides value (financing, loan, credit line) to the debtor. Third, the debtor authenticates a written security agreement that describes the cyberasset collateral. When all three requirements are fulfilled, the lender’s security interest in the cyberasset collateral becomes “attached.”²⁹

Next, to protect its attached security interests against the rest of the world, the lender must “perfect” it by employing an appropriate method of perfection.³⁰ The most common method of perfection is filing the financing statement covering the domain names and web contents collateral in an appropriate office.³¹

23. *Id.*

24. *Id.* § 9-102(42) & cmt. 5(d).

25. *Trimarchi v. Together Dev. Corp.*, 255 B.R. 606, 610–11 (Bankr. D. Mass. 2000); *Roman Cleanser Co. v. Nat’l Acceptance Co. of Am. (In re Roman Cleanser Co.)*, 43 B.R. 940, 944, 225 USPQ 140, 142 (Bankr. E.D. Mich. 1984) (analyzing the difference between a security interest and an assignment of ownership), *aff’d*, 802 F.2d 207, 231 USPQ 301 (6th Cir. 1986).

26. *See Acme Valve & Fitting Co. v. Wayne*, 386 F. Supp. 1162, 1165, 183 USPQ 629, 631 (S.D. Tex. 1974) (“In order for a transfer of rights in a trademark to constitute a sale or assignment, thereby vesting title to the trademark in a party, the transfer must be absolute and must relate to the entire rights in the trademark.”); *Li’l Red Barn, Inc. v. Red Barn Sys., Inc.*, 322 F. Supp. 98, 107 (N.D. Ind. 1970) (“[T]he rule is well established that a mere agreement for the future assignment of a trademark is not an assignment of either the mark itself or the goodwill attached to it.”), *aff’d per curiam*, No. 18062, 71-1012, 1972 WL 18062, 174 USPQ 193 (7th Cir. June 2, 1972).

27. *Roman Cleanser*, 43 B.R. at 944, 225 USPQ at 142 (analyzing difference between security interest and assignment).

28. U.C.C. § 9-203(b).

29. *Id.* § 9-203(a), (b).

30. *Id.* §§ 9-302 to 9-314 (providing different methods of perfecting security interests in different types of collateral).

31. U.C.C. § 9-310(a) (providing perfection by filing).

The financing statement must contain the identity of the debtor, the secured party (the lender), and an indication of the collateral property.³² Because domain names and web contents are in the catch-all definition of “general intangibles,” a mere indication of “general intangibles” on the financing statement suffices.³³ Moreover, Article 9 now allows a super-generic statement in the financing statement for indication of the encumbered collateral property.³⁴

The financing statement covering general intangibles is generally filed in the office of the Secretary of State where the debtor is located.³⁵ In some cases, a federal statute expressly preempts state law as to recording of security interest in a type of collateral.³⁶ Compliance with the federal statute will achieve perfection of security interest in the collateral.³⁷ However, a question arises as to where a financing statement covering domain names and web contents should be filed for perfection purpose.

IV. PERFECTING SECURITY INTERESTS IN DOMAIN NAMES

Currently, no court has addressed the issue of security interests in domain names. Further, there is no federal statute that governs the assignment of domain names and/or recording security interests in domain names. Most likely, state UCC law governs security interests in domain names.

Some domain names serve as source identifiers, functioning like trademarks. It would be instructive to look to case law on security

32. *Id.* § 9-502(a) (listing the contents of financing statement); *id.* § 9-504 (2001) (providing the standard for indication of collateral in the financing statement).

33. *Id.* § 9-504 cmt. 2 (allowing super generic description of the collateral such as “all assets other than automobiles” is sufficient for purpose of a financing statement).

34. *See* 17 U.S.C. § 1201(a)–(f) (2000).

35. U.C.C. § 9-501 (providing central filing office for financing statements covering all collateral, except timber to be cut, as-extracted collateral and fixture); *id.* § 9-301(1) (providing single jurisdiction choice of law of the debtor’s location); § 9-307 (providing rules to ascertain where a debtor is deemed to locate for Article 9 purposes).

36. *Id.* § 9-311(a)(1) & cmt. 2. The Official Comment provides:

Subsection (a)(1) exempts from the filing provisions of this Article transactions as to which a system of filing – state or federal – has been established under federal law. Subsection (b) makes clear that when such a system exists, perfection of a relevant security interest can be achieved only through compliance with that system.

An example of the type of federal statute referred to in subsection (a)(1) is 49 U.S.C. §§ 44107-11, for civil aircraft of the United States . . .

Subsection (a)(1) provides explicitly that the filing requirement of this Article defers only to federal statutes, regulations or treaties whose requirements for a security interest’s obtaining priority over the rights of a lien creditor preempt Section § 9-310(a). The provision eschews reference to the term “perfection,” inasmuch as Section § 9-308 specifies the meaning of that term and a preemptive rule may use other terminology.

Id.

37. *See id.*

interest in trademarks for guidance. Courts have held that the Lanham Act's registration provision does not preempt UCC filing requirements for the perfection of a security interest in a trademark.³⁸ Indeed, the text of 15 U.S.C. § 1060 or § 10 of the Lanham Act requires the recording of assignments of trademarks if the assignee wants the assignment not voided as against a subsequent purchaser for value and without notice.³⁹ 15 U.S.C. § 1060 provides:

An assignment shall be void against any subsequent purchaser for valuable consideration without notice, unless the prescribed information reporting the assignment is recorded in the Patent and Trademark Office within 3 months after the date of the assignment or prior to the assignment. The Patent and Trademark Office shall maintain a record of information on assignments, in such form as may be prescribed by the Director.⁴⁰

Consequently, Article 9 of the UCC governs the manner of perfecting security interests in trademarks. A financing statement indicating the trademark collateral filed with the applicable state office, often the office of the Secretary of State, is necessary to perfect the security interest in the trademark collateral. Thus, according to the courts, there is no justification for federal preemption and dual filings in both state office and the United States Trademark Office.⁴¹

For example, in *Trimarchi v. Together Development Corp.*, the debtor granted a security interest in its trademark to a creditor.⁴² The creditor filed a financing statement with the United States Patent and Trademark Office, not with the Secretary of State of Connecticut, where the debtor's principal place of business was located.⁴³ The debtor later filed a voluntary petition for reorganization under Chapter 11 of the United States Bankruptcy Code. The bankruptcy court ordered the debtor to sell substantially all of its assets, including its trademarks.⁴⁴ The creditor objected to the sale of the trademark, claiming a security interest.⁴⁵ The bankruptcy court ruled that the creditor failed to perfect its security interest in the trademark and thus was not entitled to any lien of the proceeds of the sale of the debtor's

38. *Trimarchi v. Together Dev. Corp.*, 255 B.R. 606, 612 (Bankr. D. Mass. 2000); *Roman Cleanser Co. v. Nat'l Acceptance Co. of Am. (In re Roman Cleanser Co.)*, 43 B.R. 940, 225 USPQ 140 (Bankr. E.D. Mich. 1984), *aff'd*, 802 F.2d 207, 231 USPQ 301 (6th Cir. 1986).

39. *Trimarchi*, 255 B.R. at 608 (citing 15 U.S.C. § 1060).

40. 15 U.S.C. § 1060(a) (2000).

41. See *Trimarchi*, 255 B.R. at 608; *Roman Cleanser*, 43 B.R. at 945, 225 USPQ at 143.

42. *In re Together Dev. Corp.*, 227 B.R. 439, 439-40 (Bankr. D. Mass. 1998), *aff'd sub nom. Trimarchi v. Together Dev. Corp.*, 255 B.R. 606 (Bankr. D. Mass. 2000).

43. *Id.* at 440.

44. *Id.* at 439.

45. *Trimarchi*, 255 B.R. at 607.

assets.⁴⁶ The creditor appealed the bankruptcy court's decision to the district court.

The creditor argued that as with copyrights, trademarks are intangible and lack identifiable *situs*.⁴⁷ Thus, the efficiency of a single recordation scheme for trademarks compels federal preemption under the Lanham Act.⁴⁸ Consequently, perfection of security interests in trademarks is with the Trademark Office.⁴⁹ The district court rejected the creditor's argument upon a careful analysis of Article 9 of the UCC, the Lanham Act, case law, and general policy considerations.⁵⁰

The *Trimarchi* court observed that federal preemption of the UCC perfection schemes will only occur when relevant federal statutes specifically and systematically provide for the filing of "all security interests" in a given form of property.⁵¹ The court noted that "a federal intellectual property registration or certificate of title, such as a certificate of federal trademark registration, reveals the name of the registrant and identifies the property but does not provide a list of lien holders."⁵² Thus, national registration alone, without any federal system for the recordation of security interests,

would leave the holder of a security interest with no means of recording or perfecting that interest. Absent a reliable means of verifying the status of their collateral, secured lenders would be more reluctant to extend credit. Such a result would be inconsistent with the stated purpose of Article 9 of providing a "simple and unified structure" for secured transactions.⁵³

The court held that the Lanham Act does not preempt the UCC's filing requirements and that the perfection of a security interest in a trademark is governed by Article 9. Moreover, the court also noted that "in 1988 the Senate passed a bill, among other things, that would have created a federal filing of security interests in trademarks and brought both the recordation and priority of security interests in trademarks into conformity with the counterpart copyright provisions."⁵⁴ "The portion of the bill related to security interests was not enacted, however, and thus, . . . 'the U.C.C. continues to govern security interests in trademarks.'"⁵⁵

The court concluded that the creditor failed to file the financing statement in accordance with state UCC law and therefore did not

46. *Together Dev. Corp.*, 227 B.R. at 442.

47. *Trimarchi*, 255 B.R. at 609.

48. *Id.*

49. *Id.*

50. *Id.* at 610-12.

51. *Id.* at 612.

52. *Id.*

53. *Id.* (quoting U.C.C. § 9-101 cmt. (1962)).

54. *Id.* at 611 (citing S. 1883, 100th Cong. (1988)).

55. *Id.* (quoting Stuart M. Rilback, *Intellectual Property Licenses; The Impact of Bankruptcy*, 576 PLI/PAT 199, 215 n.95 (1999)).

perfect its security interest in the trademark. Accordingly, the court dismissed the creditor's bankruptcy appeal.⁵⁶

The *Trimarchi* ruling is consistent with precedents established in this area.⁵⁷ In *Roman Cleanser Co. v. National Acceptance Co.*,⁵⁸ a creditor moved to intervene in an adversary proceeding, asserting that it had a perfected and senior security interest in trademarks which were sold by the trustee and as to which another creditor claimed ownership. Specifically, Roman Cleanser executed a loan and security agreement granting creditor NAC a security interest "in and to all of Roman Cleanser's then owned and thereafter acquired goods, equipment, and general intangibles and the proceeds thereof as collateral for the payment of all indebtedness and liabilities then existing or thereafter arising of Roman Cleanser to NAC."⁵⁹ NAC filed a financing statement with the Michigan Secretary of State pursuant to the Michigan UCC.⁶⁰

Five years later, the debtor entered into a sale agreement wherein it sold all equipment to Patterson, and Patterson executed a certain loan to the debtor. The agreement also provided "[i]n the event of default by Roman, Patterson will be entitled to and Roman grants to Patterson an exclusive perpetual license entitling Patterson to sell chemical products under all Roman owned trademarks."⁶¹ Subsequently, Roman filed a petition for bankruptcy. Patterson claimed that it was the owner of the debtor Roman's trademarks by virtue of the debtor's default under the agreement between Patterson and Roman. The trustee sold the trademarks to a buyer. After the sale, NAC filed a motion to intervene, contending that it had a perfected security interest in the trademarks and its security interest was senior to Patterson's ownership claim and the trustee's right.⁶²

The trustee contended that to perfect a security interest in a federally registered trademark a creditor must file a conditional assignment with the PTO, and because NAC failed to do so, its security interest was not perfected.⁶³

The court distinguished between assignment of trademarks and security interest in trademarks. "Since a security interest in a trademark is not equivalent to an assignment, the filing of a security interest is

56. *Id.* at 612.

57. See *Roman Cleanser Co. v. Nat'l Acceptance Co. of Am.* (*In re Roman Cleanser Co.*) 43 B.R. 940, 225 USPQ 140 (Bankr. E.D. Mich. 1984), *aff'd*, 802 F.2d 207, 231 USPQ 301 (6th Cir. 1986); *Creditors' Comm. of TR-3 Indus., Inc. v. Capital Bank* (*In re TR-3 Indus.*), 41 B.R. 128, 131 (Bankr. C.D. Cal. 1984).

58. 43 B.R. at 942, 225 USPQ at 141.

59. *Id.* at 941, 225 USPQ at 141 (quoting NAC's Statement of Position). Author's note: general intangibles include trademarks, copyrights and patents.

60. *Id.* at 941, 225 USPQ at 141.

61. *Id.* at 941, 225 USPQ at 140-41 (quoting the purchase agreement between Patterson and Roman Cleanser).

62. *Id.* at 942, 225 USPQ at 141.

63. *Id.* at 942, 225 USPQ at 141.

not covered by the Lanham Act.”⁶⁴ Accordingly, perfecting a security interest in trademarks is governed by Article 9 of the UCC. NAC perfected its security interest in the trademarks in accordance with Michigan law.⁶⁵

The trustee also contended that NAC’s security interest should be voided as unenforceable because “to have a valid and enforceable security in a trademark, the secured party must also have a corresponding interest in the machinery and equipment necessary to produce the products to which the marks attach.”⁶⁶ The trustee asserted that because NAC had released the security interest it had in the machinery and equipment, its security interest in the trademark was rendered unenforceable. The court rejected the trustee’s contention for lack of merit.

In summary, though the Lanham Act governs federal trademarks, there is no federal preemption for perfection of security interests in trademarks. State regulations, through the adoption of Article 9 of the UCC, control the perfection of security interests in trademarks. Consequently, if a domain name is qualified for protection as a valid trademark, perfection of security interest in the domain name is achieved by filing the financing statement. The financing statement must provide an indication of the domain name collateral (classified as “general intangible”) with the office of the Secretary of State where the online company is incorporated or has its chief executive office.⁶⁷ In the cases where the domain names are not protectable trademarks, Article 9 filing system should be observed given the absence of a federal statute governing recordation of security interests in domain names.

V. PERFECTING SECURITY INTERESTS IN WEB CONTENTS

A. *Perfecting Security Interests in Registered Copyright Web Contents*

The Copyright Act provides that any transfer of copyright ownership or other document pertaining to a copyright is recorded with the Copyright Office.⁶⁸ The definition of “transfer of copyright ownership” states that such transfer means “an assignment, mortgage, exclusive license, or any other conveyance, alienation, or hypothecation of a copyright or of any of the exclusive rights comprised in a copyright,

64. *Id.* at 944, 225 USPQ at 142.

65. *Id.* at 946, 225 USPQ at 142–44.

66. *Id.* at 946, 225 USPQ at 144.

67. See U.C.C. § 9-307 (2001) (providing rules to determine location of debtor).

68. 17 U.S.C. § 205(a) (2000) (“Any transfer of copyright ownership or other document pertaining to a copyright may be recorded in the Copyright Office.”); see also Official Unsecured Creditors’ Comm. v. Zenith Prods., Ltd. (*In re* AEG Acquisition Corp.), 127 B.R. 34, 41 (Bankr. C.D. Cal. 1991), *aff’d*, 161 B.R. 50 (B.A.P. 9th Cir. 1993).

whether or not it is limited in time or place of effect, but not including a nonexclusive license.”⁶⁹ The inclusion of “hypothecation” within the scope of the Copyright Act clearly indicates an intent to include security interest because the term “hypothecate” means: “to pledge property as security or collateral for a debt. Generally, there is no physical transfer of the pledged property to the lender, nor is the lender given title to the property; though he has the right to sell the pledged property upon default.”⁷⁰

The Copyright Act also provides a method of executing a transfer of copyright ownership, a recording system that gives all persons constructive notice of the transfer.⁷¹ Indeed, the “transfer of copyright ownership” is evidenced by an instrument of conveyance, a note, or memorandum of the transfer in writing and signed by the owner of the rights or its agents.⁷²

The federal filing scheme under the Copyright Act provides constructive notice not only to the status of ownership in copyrights, but security interests in copyrights.⁷³ Courts have ruled that the federal

69. 17 U.S.C. § 101 (providing definition of “transfer of copyright ownership”); *see also* *Moldo v. Matsco, Inc.* (*In re Cybernetic Servs., Inc.*), 239 B.R. 917, 921–23 (B.A.P. 9th Cir. 1999) (analyzing the relevant copyright statutes relating to perfection of security interests in copyrights), *aff’d*, 252 F.3d 1039 (9th Cir. 2001), *cert. denied*, 122 S. Ct. 1069 (2002); *In re Avalon Software Inc.*, 209 B.R. 517, 521 (Bankr. D. Ariz. 1997) (“Under federal copyright law, the grant of a security interest is defined as a ‘transfer of copyright ownership,’ because within copyright law that term includes mortgages or other forms of hypothecation.”) (citing 17 U.S.C. § 205); *Nat’l Peregrine, Inc. v. Capitol Fed. Sav. & Loan Ass’n of Denver* (*In re Peregrine Entm’t, Ltd.*), 116 B.R. 194, 198–99, 16 USPQ2d 1017, 1019 (Bankr. C.D. Cal. 1990) (citations omitted).

70. *Moldo*, 239 B.R. at 921 (quoting BLACK’S LAW DICTIONARY 742 (6th ed. 1990) defining “hypothecate”). *See also In re Together Dev. Corp.*, 227 B.R. 439, 441 (Bankr. D. Mass. 1998) (noting Congress expressly included security interests in the copyright recording system), *aff’d*, 255 B.R. 606 (Bankr. D. Mass. 2000); *Avalon Software*, 209 B.R. at 521 (stating the federal copyright law includes recordation of hypothecation, that is, security interests).

71. *Avalon Software*, 209 B.R. at 521 (“[T]he recordation of the security interest in copyrights serves to impart constructive notice to the world of the existence of the security interest.” (quoting 17 U.S.C. § 205(c)). *See also Moldo*, 239 B.R. at 922 (“Section 205 clearly sets forth a priority scheme for conflicting transfers and provides that recordation of a document in the Copyright Office ‘gives all persons constructive notice of the facts stated in the recorded document.’” (quoting 17 U.S.C. § 205)).

72. 17 U.S.C. § 204(a) provides: “A transfer of copyright ownership, other than by operation of law, is not valid unless an instrument of conveyance, or a note or memorandum of the transfer, is in writing and signed by the owner of the rights conveyed or such owner’s duly authorized agent.”

73. *Id.* § 205(c) provides:

RECORDATION OF CONSTRUCTIVE NOTICE. – Recordation as 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

filing scheme under the Copyright Act preempts the UCC filing requirements for security interests in copyrights.⁷⁴ Consequently, recordation under the UCC filing provisions has been held as ineffective to perfect a security interest in a copyright.⁷⁵ The only means to perfect a security interest in a copyright is to record the security interest in a copyright with the United States Copyright Office.⁷⁶

For example, the court in *In re Peregrine Entertainment* – the first court that addressed the issue of perfection of security interests in copyrights – broadly ruled that “federal law preempts state methods of perfecting security interests in copyrights.”⁷⁷ The *Peregrine* court rationalized its ruling with a view that the copyright statutes provide a comprehensive recordation system for copyrights and thus preempt the field of all liens and interests associated with copyrights.⁷⁸

In *Peregrine*, American National Enterprise (“ANE”) received a six million dollar line of credit from Capitol Federal Savings and Loan Association of Denver (the “Bank”).⁷⁹ The Bank received a security interest in ANE’s film library and filed both the security agreement and the UCC-1 financing statement describing the collateral as “[a]ll inventory consisting of films and all accounts, contract rights, chattel paper, general intangibles, instruments, equipment, and documents re-

(2) registration has been made for the work.

Id.

74. See *Avalon Software*, 209 B.R. 517 (concluding that the Copyright statutes preempt UCC filing for perfection of security interests in copyrights); *Official Unsecured Creditors’ Comm. v. Zenith Prods., Ltd. (In re AEG Acquisition Corp.)*, 127 B.R. 34, 40–41 (Bankr. C.D. Cal. 1991) (concluding that a security interest in copyrights could only be perfected by recordation with the Copyright Office, not with the applicable state filing office pursuant to the UCC), *aff’d*, 161 B.R. 50 (B.A.R. 9th Cir. 1993); *Peregrine*, 116 B.R. 194, 16 USPQ2d 1017 (holding the Copyright statutes preempt UCC filing provisions and thus security interests in copyrights could only be perfected by recording such interests with the Copyright Office).

75. See, e.g., *Avalon Software*, 209 B.R. 517; *Zenith Prods., Ltd.*, 127 B.R. 34; *Peregrine*, 116 B.R. 149, 16 USPQ2d 1017.

76. *Aerocon Eng’g, Inc. v. Silicon Valley Bank (In re World Auxiliary Power Co.)*, 244 B.R. 149, 152, 54 USPQ2d 1329, 1331 (Bankr. N.D. Cal. 1999) (noting the *In re Avalon Software*, *AEG Acquisition* and *Peregrine* courts all held that “a security interest could only be perfected by recordation with the Copyright Office”).

77. *Peregrine*, 116 B.R. at 199, 16 USPQ2d at 1019 (stating that “the comprehensive scope of the federal Copyright Act’s recording provisions, along with the unique federal interests they implicate, support the view that federal law preempts state methods of perfecting security interests in copyrights”).

78. *Id.* at 199, 16 USPQ2d at 1019. 17 U.S.C. § 205(e) provides:

PRIORITY BETWEEN CONFLICTING TRANSFER OF OWNERSHIP AND NONEXCLUSIVE LICENSE. – A nonexclusive license, whether recorded or not, prevails over a conflicting transfer of copyright ownership if the license is evidenced by a written instrument signed by the owner of the rights licensed or such owner’s duly authorized agent, and if –

- (1) the license was taken before execution of the transfer; or
- (2) the license was taken in good faith before recordation of the transfer and without notice of it.

Id.

79. *Peregrine*, 116 B.R. at 197, 16 USPQ2d at 1018.

lated to such inventory, now owned or hereafter acquired by the Debtor.”⁸⁰ The Bank filed its financing statements in California, Colorado, and Utah. It did not record its security interests in the United States Copyright Office.⁸¹ ANE was later merged with NPI. Subsequently, NPI filed a voluntary petition for bankruptcy and later a complaint against the Bank, contending that the Bank’s security interests in the copyrights of the films in its predecessor’s (now NPI’s) film library were unperfected for failure to record its security interests with the Copyright Office.⁸² NPI claimed that as a debtor in possession, it had a judicial lien on the copyrights and therefore sought to avoid the Bank’s security interests in the film for the benefit of the estate.⁸³

The court analyzed the Copyright Act and held that a security interest in a copyright could not be perfected by filing a financing statement in the Secretary of State’s office.⁸⁴ Perfection in such security interest could only be achieved by recording the security interest in the Copyright Office.⁸⁵ Accordingly, the debtor in possession or hypothetical judicial lien holder under Chapter 11 of the Bankruptcy Code could obtain a lien on a copyright superior to the unperfected security interest in the copyright.⁸⁶ The debtor in possession or the bankruptcy trustee could avoid the unperfected security interest in the copyright.⁸⁷

Moreover, the *Peregrine* court also ruled that the federal priority scheme for conflicting transfers of copyrights, including security interests in copyrights preempts state priority scheme.⁸⁸

Other courts later followed the federal filing scheme as advocated by *Peregrine* for perfection of security interests in copyrights.⁸⁹ Currently, no appellate court has addressed security interests in copyrights. *Peregrine*, however, failed to clarify whether the federal filing scheme is required for registered copyrights or both registered copyrights and unregistered copyrights. At least one court has opined that *Peregrine* applies strictly to registered copyrights.⁹⁰

Accordingly, if web contents are copyrightable, the content owner should obtain copyright registrations for various components of the

80. *Id.* at 197–98, 16 USPQ2d at 1018.

81. *Id.* at 198, 16 USPQ2d at 1018.

82. *Id.* at 197–98, 16 USPQ2d at 1018.

83. *Id.* at 198, 16 USPQ2d at 1018.

84. *Id.* at 198–204, 16 USPQ2d at 1019–23.

85. *Id.* at 204, 16 USPQ2d at 1023.

86. *Id.* at 206–07, 16 USPQ2d at 1026.

87. *Id.* at 207, 16 USPQ2d at 1026.

88. *Id.* at 205, 16 USPQ2d at 1024 (analyzing 17 U.S.C. § 205(d)).

89. See *In re Avalon Software, Inc.*, 209 B.R. 517 (Bankr. D. Ariz. 1997) (adopting *Peregrine*); Official Unsecured Creditors’ Comm. v. Zenith Prods., Ltd. (*In re AEG Acquisition Corp.*), 127 B.R. 34 (Bankr. C.D. Cal. 1991) (following *Peregrine*), *aff’d*, 161 B.R. 50 (B.A.P. 9th Cir. 1993).

90. *Aerocon Eng’g, Inc. v. Silicon Valley Bank (In re World Auxiliary Power Co.)*, 244 B.R. 149, 152, 54 USPQ2d 1329, 1331 (Bankr. N.D. Cal. 1999).

web contents. Under *Peregrine*, a lender must record its security interest in the registered copyright web contents with the Copyright Office. Filing the financing statement covering the registered copyright web contents with a state's office of Secretary of State is insufficient. Furthermore, the lender will lose its priority in the web contents to a subsequent purchaser of the contents or a bankruptcy trustee.⁹¹

B. *Perfecting Security Interests in Unregistered Copyright Web Contents*

Courts addressing perfection of security interests in unregistered copyrights have held that unregistered copyrights must be registered with the Copyright Office as a condition to perfecting a security interest in them.⁹² Notably, these courts held that the Copyright Act preempts the perfection scheme under Article 9 of the UCC for security interest in *all* copyrights.⁹³ Accordingly, perfection in copyrights requires two steps: registration of the copyright with the United States Copyright Office, and recordation of the registered copyright with the same office.⁹⁴ Further, the court in *In re Avalon Software, Inc.*⁹⁵ rejected the argument that perfection of unregistered copyrights are governed by state law, branding the argument as being “novel” and lacking supporting authority. The court based its rejection on the rationale that such argument “would throw Congress’[s] requirement for central filing of security interests in copyright material into chaos.”⁹⁶

Recently, a bankruptcy court in *In re World Auxiliary Power Co.*, examined *Peregrine* and its progeny to determine whether the federal filing scheme is required for security interests in unregistered copyrights.⁹⁷ The *World Auxiliary Power* court noted that *Peregrine* failed to address unregistered copyrights and its progeny failed to consider whether it was appropriate to apply the *Peregrine* analysis to unregistered copyrights.⁹⁸ “[W]hen a copyright is unregistered, a secured

91. Copyright law provides a priority scheme for conflicting transfers of security interests. See 17 U.S.C. § 205 (2000). Priority is given to the first transfer executed, provided that the transfer is recorded (a) within 30 days of the date of execution in a manner sufficient to give third parties constructive notice, if the transfer is in the United States or within two months if the transfer is outside the United States, (b) or at any time before recordation of the later transfer. Priority is given to the later transfer but recorded first if the transferee: (a) received the transfer in good faith, (b) for valuable consideration, and (c) without notice of the prior transfer. *Id.* § 205(d).

92. See *Zenith Prods., Ltd.*, 127 B.R. 34.

93. See *id.* at 40.

94. *Id.* at 41.

95. 209 B.R. 517, 523 (Bankr. D. Ariz. 1997).

96. *Id.* (citing Nat'l *Peregrine, Inc. v. Capitol Fed. Sav. & Loan Ass'n of Denver (In re Peregrine Entm't, Ltd.)*, 116 B.R. 194, 200 (Bankr. C.D. Cal. 1990)).

97. *Aerocon Eng'g, Inc. v. Silicon Valley Bank (In re World Auxiliary Power Co.)*, 244 B.R. 149, 54 USPQ2d 1329 (Bankr. N.D. Cal. 1999).

98. *Id.* at 151–54, 54 USPQ2d at 1331–33.

creditor may perfect its security interest by filing a UCC-1 financing statement with the UCC Office.”⁹⁹ The *World Auxiliary Power* court then analyzed the federal copyright law and ruled that “the Copyright Act’s recording provisions are not comprehensive as applied to an unregistered copyright. They contain no means by which a security interest in an unregistered copyright may be perfected.”¹⁰⁰ Consequently, state law must supply the means.¹⁰¹ Article 9 of the UCC provides the supplemental recordation for the Copyright Act and perfecting a security interest in unregistered copyrights thus can be achieved by compliance with Article 9 requirements.¹⁰²

Conflicting rulings regarding perfection of security interests in copyrights suggest that the safest way to protect a lender’s security interest in copyrights, in the present case copyright web contents, is to employ a dual filing system. The dual filing system includes one filing with the Copyright Office for perfection of security interests in registered copyrights (in this case, registered copyright web contents). The second filing is with the applicable state filing office necessary for perfection of security interest in unregistered copyrights (unregistered copyright web contents) and pending copyright applications (for the copyrightable web contents).¹⁰³

The dual filing system essentially imposes the federal priority of security interests scheme to registered copyrights while state law priority scheme governs unregistered copyrights and applications.¹⁰⁴ This may cause conflicting results because the federal priority scheme as provided in 17 U.S.C. § 205(d) is not as comprehensive as Article 9 priority provisions.¹⁰⁵ The federal priority scheme is, at best, too simplistic and ill-equipped to address the complexity of the priority morass

99. *Id.* at 156, 54 USPQ2d at 1335.

100. *Id.* at 154, 54 USPQ2d at 1333.

101. *Id.* at 154, 54 USPQ2d at 1333.

102. *Id.* at 154, 54 USPQ2d at 1333. The court concluded that “[i]f a copyright is registered, recordation in the Copyright Office is the only effective method by which to perfect the security interest. Only if a copyright is unregistered does filing a UCC-1 financing statement with the UCC Office perfect the security interest.” *Id.* at 154, 54 USPQ2d at 1333.

103. *Id.* at 154, 54 USPQ2d at 1333.

104. *See id.* at 154, 54 USPQ2d at 1333 (stating that state law on priority of security interests will govern unregistered copyrights); *Nat’l Peregrine, Inc. v. Capitol Fed. Sav. & Loan Ass’n of Denver (In re Peregrine Entm’t, Ltd.)*, 116 B.R. 194, 206–08, 16 USPQ2d 1017, 1024–26 (Bankr. C.D. Cal. 1990) (applying the federal law on priority of security interests in registered copyrights).

105. 17 U.S.C. § 205(d) (2000) states:

As between two conflicting transfers, the one executed first prevails if it is recorded, in the manner required to give constructive notice under subsection (c), within one month after its execution in the United States or within two months after its execution outside the United States, or at any time before recordation in such manner of the later transfer. Otherwise the later transfer prevails if recorded first in such manner, and if taken in good faith, for valuable consideration or on the basis of a binding promise to pay royalties, and without notice of the earlier transfer.

under state commercial law.¹⁰⁶ Further, federal decisional authority on priority security interest in copyrights is undeveloped as compared to voluminous state decisional authority on priority of security interests.¹⁰⁷

C. *Perfecting Security Interests in Non-Copyrightable Web Contents*

Non-copyrightable web contents are probably within the definition of "general intangible."¹⁰⁸ If the contents are valuable and could be used as collateral property to secure the online company's debt, payment, or performance of an obligation, the lender or financier must perfect its security interest in the contents by employing state filing scheme under Article 9. The lender must file a financing statement covering the web contents in the office of Secretary of State where the debtor is incorporated or has its chief executive office.¹⁰⁹

VI. CONCLUSION

Perfection of security interests in domain names and web contents is an important process in intellectual property financing in electronic commerce. Without perfection of security interest, lenders, financiers, or institutional investors will lose their security right in the online company's intangible assets to bankruptcy trustees or other creditors.

Id. Article 9, on the other hand, has a comprehensive priority of security interests system. The priority system includes provisions from U.C.C. § 9-317 to U.C.C. § 9-339 and extensive Official Comments. See U.C.C. § 9-317 to § 9-339 (2001).

106. The federal priority scheme provides no guidance as to, among others, priority of purchase money security interests in copyrights and proceeds of copyrights. See 17 U.S.C. § 205.

107. There are very few decisions on security interests in copyrights. See *Aerocon Eng'g*, 244 B.R. at 152, 54 USPQ2d at 1332; *In re Avalon Software*, 209 B.R. 517 (Bankr. D. Ariz. 1997); Official Unsecured Creditors' Comm. v. Zenith Prods., Ltd. (*In re AEG Acquisition Corp.*), 127 B.R. 34 (Bankr. C.D. Cal. 1991), *aff'd*, 161 B.R. 50 (B.A.P. 9th Cir. 1993); *Peregrine*, 116 B.R. at 206-08, 16 USPQ2d at 1024-26. Among the decisions, two failed to discuss priority of security interests in copyrights. See *Aerocon Eng'g*, 244 B.R. at 153 n.10, 54 USPQ2d at 1332 n.10 (noting "the AEG Acquisition court misstated the priority scheme established by 17 U.S.C. § 205(d) as giving priority to a transferee who records first," and "[t]he Avalon court failed to discuss the priority issue at all"); see also *MCEG Sterling, Inc. v. Phillips Nizer Benjamin Krim & Ballon*, 646 N.Y.S.2d 778 (N.Y. Sup. Ct. 1996) (noting that there were only two cases on perfection of security interests in copyrights).

108. See U.C.C. § 9-102(42) & cmt. 5.

109. See *id.* § 9-501 (filing office); § 9-307 (location of debtor).