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The Perfection and Priority Rules for Security Interests in Copyrights, Patents, and Trademarks: The Current Structural Dissonance and Proposed Legislative Cures

Thomas M. Ward
University of Maine School of Law

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I. INTRODUCTION

A. *The Early Title Rubric Used To Describe Security Interests in Intangible Personal Property*

The structural legal dissonance that undermines the effective financing of federal intellectual property rights (patents, trademarks registrations, copyrights, and maskworks) is rooted in the prominence of title in both the early conceptual history of personal property financing and in the language of the federal tract recording acts. While genuine ownership transfers have always represented the prototype under the federal intellectual property recording statutes,[1] transfers intended for security were also originally included because of the early judicial thinking about the importance of title to the validity (against third parties) of a "mortgage" right in intangible personal property.[2] Mortgages of intangible personal property were not protected under the recording provisions of early state chattel mortgage acts.[3] However, in the absence of record notice, the transfer or assignment of "title" (and its incidents) often served as a substitute for a transfer of "possession," which was thought necessary to protect third parties from secret liens where tangible personal property was pledged as collateral.[4] While title remained a neces-

* Professor, University of Maine School of Law.

1. Assignments, in the case of patents and trademarks, and assignments and exclusive licenses in the case of copyrights. *See, e.g.*, 35 U.S.C. § 261 (1994) (patents); 15 U.S.C. § 1060 (1994) (trademarks); 17 U.S.C. §§ 101, 201, 205 (1994) (copyrights).

2. Waterman v. Mackenzie, 138 U.S. 252 (1890). In *Waterman*, the inventor/licensee of a fountain pen holder (Waterman) brought suit to enjoin an alleged infringement. *Id.* at 252. The Supreme Court affirmed the lower court's decision that the equitable action failed because title to the patent resided not in the plaintiff Waterman but in a conditional assignee who took it in a transfer intended for security. *Id.* at 261.

3. 1 GRANT GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY § 2.8 (1965).

4. *See* Casey v. Cavaroc, 96 U.S. 467, 476-77 (1877). In *Casey*, the Supreme Court set up title as the necessary equivalent to possession when the degree of mortgagee control and thus the protection of third parties was at issue. *Id.* at 477. The relationship between title and possession in the case of a mortgaged bill of lading is described as follows:

> When, as in that case, the title has been transferred to the creditor, and the collections are made for his benefit, the pledgor merely acting as his servant or agent in making them, the character of the security is not affected at the common law by the debtor having actual possession of the collaterals, there being no fraud in the transaction. In such case, they are held by the creditor by way of mortgage as well as pledge; and a mortgage is valid notwithstanding the mortgagor has the possession. The difference ordinarily recognized between a mortgage and a pledge is, that title is transferred by the former, and possession by the latter. . . .The assignment of a bill of lading is of that

sary component for both a genuine ownership transfer of intangible property and a mortgage transfer, distinctions between the rights of titleholders who were mortgagees and those who were real assignees never really developed.[5] Professor Grant Gilmore observed that "[t]here has never been enough litigation . . . to nourish the growth of such refinements."[6]

As products of their time, the recording provisions of both the Patent Act and the Lanham Trademark Act have as their premise the protection of *bona fide* purchasers (BFP) against unrecorded transfers of "legal title" (including early conditional title transfers used in mortgage transactions). Under the Patent Act, a title transfer that has not been recorded within three months of its execution and is still unrecorded on the date of a subsequent purchase or mortgage is "void" against the purchaser or mortgagee with BFP status.[7] The more modern recording language of the Copyright Act applies broadly to a "transfer of copyright ownership or other document pertaining to a copyright."[8] However, the Copyright Act priority rule based on this recording requirement applies only to "conflicting transfers."[9] Because a transfer of copyright *ownership* includes both a mortgage and any exclusive right that is "comprised in a copyright,"[10] some portion of the copyright "title" seems to pass with all copyright transfers (including exclusive licenses) that are protected by a recording.[11] Nonexclusive licenses are expressly excluded from both the definition of a "transfer of copyright ownership" and from the operation of the discrete priority rule applicable to "conflicting transfers."[12]

If we indulge the early judicial assumption that an effective mortgage of an intangible asset turns on some title that is deemed the equivalent of constructive

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> kind. Such an assignment is necessary, where a pledge is proposed, in order to give the constructive possession required to constitute a pledge; and yet it formally transfers the title also. In such a case, there is a union of two distinct forms of security,—that of mortgage and that of pledge; mortgage by virtue of the title, and pledge by virtue of the possession.

Id.

5. *See* Tuttle v. Blow, 75 S.W. 617 (Mo. 1903) (unrecorded assignment to the mortgagee of all of the mortgagor's right, title, and interest in a certain trademark for eye salve effective against mortgagor's receiver); *see also* 1 GILMORE, *supra* note 3, at 58.

6. 1 GILMORE, *supra* note 3, at 60.

7. 35 U.S.C. § 261 (2000); 15 U.S.C. § 1060 (2000). In many ways, these federal recording provisions have more in common with real estate counterparts than with other statutes dealing with rights in personal property. As Judge Nott observed more than 100 years ago:

> Though the most intangible form of property, it still, in many characteristics, is closer in analogy to real than to personal estate. Unlike personal property, it cannot be lost or found; it is not liable to casualty or destruction; it cannot pass by manual delivery. Like real property, it may be disposed of, territorially, by metes or bounds; it has its system of conveyancing by deed and registration; estates may be created in it, such as for years and in remainder; and the statutory action for infringement bears a much closer relation to an action of trespass than to an action in trover and replevin. It has, too, what the law of real property has, a system of user by license.

A.S. Solomons v. United States, 21 Ct. Cl. 479, 483 (1886), *aff'd*, 137 U.S. 342 (1890).

8. 17 U.S.C. § 205(a) (1994).

9. *Id.* § 205(d) (1994).

10. *Id.* § 101 (1994).

11. *See In re* Simplified Info. Systems, Inc., 89 B.R. 538, 541-42 (W.D. Pa. 1988); *see also* J. Brinson, *The Copyright Act and Bankruptcy: Perfection, Priorities and Transfers*, 1 J. BANKR. L. & PRAC. 337, 353 (1992).

12. 17 U.S.C. §§ 101, 205(d)-(e) (1994).

possession and control, all of these federal recording statutes seem receptive to the transfer intended for security in its early conceptualization. However, these federal recording acts are trapped in a time warp. The underlying state law of personal property security has not been linked to title or the pledge-based incidents of constructive possession for more than half a century.

B. The State Law Concept of the "Security Interest" and Its Supporting Documents

In the middle of the last century, Article Nine of the Uniform Commercial Code reoriented the state law concept of personal property collateral around the unitary concept of a "security interest." While Article Nine went through a major revision in 1998, the basic unitary concept of a security interest and the structure that supports it remained unaltered.[13]

The "security interest," as envisioned by both the "old" and the "revised" version of U.C.C. Article Nine, is a kind of functional lien right that can be created and protected in any kind of personal property by using two prototype documents with minimum associated formalities. The first document, the Article Nine "security agreement," allows the "secured party" and the "debtor" to create a unitary "security interest" in the debtor's collateral as described in the agreement. The security agreement can provide for a security interest in both existing and after-acquired property.[14] If the secured party has given the debtor "value," the security interest created "attaches" to existing collateral of the debtor when the agreement is signed or authenticated and to after-acquired property at the moment the debtor acquires the necessary rights in the kind of collateral described.[15] The second document, the "financing statement," serves as the documentary notice of the transaction captured in the security agreement.[16] The minimum requirements for a collateral description in this shorter notice document are even more generic than the requirements for the security agreement.[17] Once properly filed under the debtor's name in the correct jurisdiction, the financing statement acts to put searching creditors and buyers on notice concerning the security interest created by the "security agreement." Under this two-document structure, creditor knowledge concerning the scope and detail of the actual "security interest" awaits some further inquiry—usually a request to inspect the underlying security agreement.

13. This Article will refer to the new 1998 text as "Revised Article Nine." As of December 1, 2000, twenty-eight states have enacted this Revised Version with minor variations and thirteen additional states have the legislation pending. Article Nine has a delayed effective date of July 1, 2001. Including states with pending legislation, twenty-three jurisdictions still have the 1995 Official Text of Article Nine as the source of their personal property security law. This pre-revision version, currently in force in many states, will be referred to as "Article Nine" or "old Article Nine." The principal characteristics of the Article Nine scheme (under both the old and Revised versions), as applied to intellectual property, are summarized in Part II.

14. U.C.C. § 9-204(1) (1995); *accord* U.C.C. [Revised] § 9-204(a).

15. U.C.C. § 9-203(1) (1995); *accord* U.C.C. [Revised] § 9-203(b).

16. Under this notice-filing approach, the security agreement used to create the security interest in the debtor's collateral need never be recorded. However, the security agreement can be filed instead of the financing statement if the secured party so elects. U.C.C. § 9-402(1) (1995).

17. Under old Article Nine the financing statement can either describe the items of collateral or indicate the types of collateral. U.C.C. § 9-402(1) (1995) & cmt. 2. Revised Article Nine permits language that is even more generic. U.C.C. [Revised] § 9-504(2).

The Article Nine concept of "perfection" or a perfected security interest builds on this two-document structure. "Perfection" is defined functionally as attachment plus one of the required forms of notice or notice-related conduct. In the overwhelming majority of cases, "perfection" is achieved by "attachment" and the proper filing of the separate and simple one-page notice document (the "financing statement") under the debtor's name.[18] Perfection is a status that carries with it a considerable, but not absolute, degree of priority protection against creditors and purchasers.[19] When used as the instrument of perfection, the properly filed financing statement serves to "perfect" with respect to property covered by the agreement that is acquired by the debtor after the date of the security agreement. That perfection occurs at the point when the debtor acquires "rights" in the new property. While no perfection in any of the debtor's property can occur until there is a valid agreement, the "financing statement" that makes subsequent perfection in the debtor's after-acquired property possible can actually be filed before the security agreement.[20] It can cover later agreements with the same debtor, as well as later advances under the original agreement made to the same debtor.[21]

C. An Outline of the Structural Problem

The principal forms of federal intellectual property (patents, trademarks registrations, copyrights, and maskworks) are "general intangibles" within the broad spectrum of personal property that is brought within the Article Nine scheme for creating, perfecting, and ordering "security interests." Some intellectual property interests under the "general intangibles" umbrella are created and defined solely under state tort or property law.[22] Some state law notions of intangible property can be created around the use of data necessary to obtain a federal entitlement, even if that data is *not* protected under the federal law defining the entitlement. The state law right recognized in *Kalitta*[23] was not preempted by the federal Copy-

18. U.C.C. §§ 9-304(1), 9-402(1) (1995); U.C.C. [Revised] §§ 9-310(a), 9-502(a)(1). For a detailed discussion of Article Nine "attachment" and "perfection" with respect to intellectual property collateral, see THOMAS M. WARD, INTELLECTUAL PROPERTY IN COMMERCE §§ 2:14-2:44 (rev. ed. 2001).

19. *See* WARD, *supra* note 18, §§ 2:31-2:44.

20. U.C.C. § 9-402(1) (1995); *accord* U.C.C. [Revised] § 9-502(d).

21. U.C.C. § 9-204 (1995).

22. Trade secrets are a prime example of state statutory or common law intellectual property. The most commonly accepted definition of a trade secret is found in the Comment to section 757 of the Restatement of Torts: "A trade secret may consist of any formula, pattern, devise or compilation of information which is used in one's business, and which gives him an advantage over competitors who do not know or use it." RESTATEMENT OF TORTS § 757 cmt. (1939).

The relative spheres of trade secret law and federal patent law were delineated by the Supreme Court in *Kewanee Oil v. Bicron*, 416 U.S. 470 (1974). In *Kewanee Oil*, the Court held that state trade secret protection was not preempted by federal patent law. Trade secrets are included within the federal definition of "intellectual property" for purposes of the rules in subsection 365(n) of the Bankruptcy Code. *See* 11 U.S.C. § 101(35A) (1994). Customer lists, business, and marketing secrets as well as technological confidences comprise a vast stock of intangible assets that are useful as collateral. Robert S. Bramson, *Intellectual Property as Collateral—Patents, Trade Secrets, Trademarks and Copyrights*, 36 BUS. LAW. 1567, 1588-90 (1981).

A "right of publicity" has been recognized under state law outside the boundaries of the federal statutes. Zacchini v. Scripps Howard, 433 U.S. 562 (1977); *see also* RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 46 (1995).

23. G.S. Rasmussen & Assoc. v. Kalitta Flying Serv., 958 F.2d 896 (9th Cir. 1992).

right Act because it protected against improper *use* of compiled data and information, not just against improper copying.[24]

These state law rights notwithstanding the debtor's *federal* intellectual property assets will normally have overriding significance as collateral. As noted above, however, if we fall into the time warp for our orientation and indulge the early title theory in order to conceptualize a mortgage of these federal assets (with the possible exception of trademark registrations), they can easily come to rest under the applicable federal tract recording act—not under the more modern state personal property security law in Article Nine. Therefore, these federal recording statutes seem to be standing above, and to varying degrees displacing, the modern state notice-based filing system that Article Nine provides for "general intangibles." In their 1992 Preliminary Report on *Security Interests in Intellectual Property*, the Joint ABA Task Force on Security Interests in Intellectual Property observed that:

> The current state of the law governing security interests in intellectual property is unsatisfactory. There is uncertainty as to where and how to file, what constitutes notice of a security interest, who has priority, and what property is covered by a security interest. This area of the law is further complicated by the fact that both federal and state law impact on these issues.[25]

II. Defining the Conflict Between Article Nine and the Tract Recording Provisions for Federal Intellectual Property

A. *The Federal Statutes*

1. *The Copyright Act*

The Copyright Act has the most comprehensive tract recording scheme of all the federal intellectual property statutes, and it presents the broadest potential overlap with the state law rules in U.C.C. Article Nine. To begin with, the Copyright Act's breadth is reflected in its definition of a "transfer of copyright ownership."[26] The definition, in section 101 of the Act, includes "assignment, mortgage, exclusive license, or any other conveyance, alienation, or hypothecation of a copyright."[27] Security interests are brought within this broad language but, standing alone, the phrase does not seem to cover involuntary lien creditors that are often in conflict with the secured party.[28] These real and hypothetical (e.g., the bankruptcy trustee)

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24. *See* Daboud v. Gibbons, 42 F.3d 285, 289 (5th Cir. 1994).

25. Task Force on Security Interests in Intellectual Property, Business Law Section, American Bar Association, PRELIMINARY REPORT 1 (June 1, 1992) [hereinafter referred to as PRELIMINARY ABA TASK FORCE REPORT]. As of March 1, 1999, the Task Force had drafted a piece of consolidated federal legislation entitled the "Federal Intellectual Property Security Act."

26. The Act provides that:

> A "transfer of copyright ownership" is 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, whether or not it is limited in time or place of effect, but not including a nonexclusive license.

17 U.S.C. § 101 (1994).

27. *Id.*

28. "Lien creditor" is defined under Article Nine as "a creditor who has acquired a lien on the property involved by attachment, levy or the like." U.C.C. § 9-301(3) (1995); *accord* U.C.C. [Revised] § 9-102(a)(52).

involuntary interests that typically engage the secured party in a contest over priority are arguably brought within the section 101 phrase "transfer of copyright ownership" by section 201 of the Copyright Act.[29] Section 201(d)(1) provides that "[t]he ownership of a copyright may be transferred . . . by any means of conveyance or by *operation of law,* and may be bequeathed by will or pass as personal property by the applicable laws of intestate succession."[30] Aside from this broad definition of transfer and ownership transfer, the language in section 205(a) that instructs as to those documents that are recordable extends to any "document pertaining to a copyright."[31]

While the *recording provisions* of the Copyright Act can be stretched to cover the full panoply of voluntary and involuntary transfers, the *priority rule* based on this tract recording structure seems to be framed with much narrower language. Section 205(d) provides the following:

> 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.[32]

The marking of the transfer's *execution*, and the *valuable consideration* required in order to award priority to the later transfer suggest that, although all transfers are recordable under subsection (a), only *voluntary* transfers seem to be regulated by the priority rule in subsection (d).[33]

2. *The Patent Act*

The Patent Act's recording provision focuses exclusively on transfers which carry full title and ownership rights to the transferee.[34] The language of section 261 of the Patent Act provides that:

> An assignment, grant or conveyance (of a patent, patent application, or interest therein) shall be void as against any subsequent purchaser or mortgagee for a valuable consideration, without notice, unless it is recorded in the Patent and Trademark Office [PTO] within three months from its date or prior to the date of such subsequent purchase or mortgage.[35]

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29. 17 U.S.C. § 201(d)(1) (1994).

30. *Id.* (emphasis added).

31. 17 U.S.C. § 205(a) (1994).

32. 17 U.S.C. § 205(d) (1994) (emphasis added).

33. In *National Peregrine, Inc. v. Capital Federal Savings & Loan Ass'n*, Judge Kozinski rejected this somewhat obvious limitation on the kinds of subsequent transfers protected under section 205(d) when he concluded that an involuntary lien creditor could be a later transfer for valuable consideration when garnished with the further characteristics of an ideal lien creditor by section 544(a)(1) of the Bankruptcy Code. *See* National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 207 (C.D. Cal. 1990) (Judge Kozinski, a member of the Ninth Circuit Court of Appeals, was sitting by designation pursuant to 28 U.S.C. § 291(b) (1994)).

34. *See infra* notes 35, 37.

35. 35 U.S.C. § 261 (1994). The language of section 261 instructs that an "assignment, grant or conveyance" be recorded within three months from its "date." In the case of an assignment of an existing patent or application, "its date" is the execution date of the assignment document. However, when "an assignment of rights in an invention is made prior to the existence of the

Compared to the scope of recording under the Copyright Act, the comparable provisions of the Patent Act are limited. The regulations limit the definition of "assignments" to include complete or partial transfer of *right, title, and interest.*[36] The title that must be transferred is the entire title, including the legal title.[37]

The early patent mortgage had a title transfer at its heart.[38] Despite the modern nontitle orientation of state chattel security law under Article Nine, a patent mortgage or collateral assignment can still be conceptualized under the Patent Act as a conditional assignment vesting title in the assignee/mortgagee.[39]

The recently modernized regulations that govern PTO recordings hold onto the concept of a conditional title transfer. Conditional assignments are covered in section 3.56 of 37 C.F.R. The section provides that:

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invention, this may be viewed as an assignment of an expectant interest. An assignment of an expectant interest can be a valid assignment." FilmTec Corp. v. Allied-Signal, Inc., 939 F.2d 1568, 1572 (Fed. Cir. 1991). The effective "date" of such an assignment is not the date of its execution, however, because legal title does not pass until "the invention is made and an application for patent is filed." *Id.* The three-month grace period should not begin to run until the effective date of the assignment. Indeed, the document that created the present assignment of the expectant interest is not recordable until it complies with the identification requirements in 37 C.F.R. section 3.21. The original document can be made recordable once a patent application is filed by the authorized addition of the application number. The PTO suggests that

> an assignment be written to allow entry of the identifying number after the execution of the assignment. An example of acceptable wording is: "I hereby authorize and request my attorney, (Insert name), of (Insert address), to insert here in parentheses (Application number ________________, filed ________________) the filing date and application number of said application when known."

Manual of Patent Examining Procedure [hereinafter MPEP] § 302.02 (1997).

36. 35 U.S.C. § 261 (1994).

37. "Assignment means a transfer by a party of all or a part of its right, title and interest in a patent or patent application." 37 C.F.R. § 3.1 (1994). The *Cybernetic* court explained that:

> The Manual of Patent Examining Procedure (7th ed. 1998) ('Patent Manual') is published by the Patent Office to provide a reference work on Patent Office practices and procedures. It is clear from the Patent Manual that the Patent Office does not consider a security interest or lien to be an "assignment" subject to the mandatory recording provision of 37 C.F.R. 3.11.
>
> The recording of "assignment" documents is governed by section 302 of the Patent Manual. Section 302 cites the language of 37 C.F.R. 3.11 pertaining to assignments of applications, patents and registrations as documents which "will be recorded." In contrast, section 313 denotes security interests as documents other than assignments and provides that these documents, which do not affect title, "may be recorded at the discretion of the Commissioner." Documents that convey a security interest are recorded under section 313 "in the public interest in order to give third parties notification of equitable interests or other matters relevant to the ownership of a patent or application."

In re Cybernetic Services, Inc., 2001 U.S. App. LEXIS 11750 at **18-28 (9th Cir. June 6, 2001); *see also* MPEP, *supra* note 35; E. LIPSCOMB, 5 WALKER ON PATENTS § 19:4 at 333-34 (3d ed. 1986) ("An assignment of a patent is an instrument in writing, which in the eye of the law, *purports to convey the entire title to that patent or to convey an undivided share in that entire title.*" (emphasis added)).

38. Waterman v. Mackenzie, 138 U.S. 252 (1890). *See* discussion *supra* note 2.

39. 35 U.S.C. § 261 (1994); *see also In re* Cybernetic Services, Inc., 239 B.R. 917, 920-21 (9th Cir. B.A.P. 1999), *aff'd*, 2001 U.S. App. LEXIS 11750 (9th Cir. June 6, 2001); Citibank & Trust Co. v. Otto Fabric, Inc., 83 B.R. 780, 782 (D. Kan. 1988); *In re* Transp., Design & Tech., Inc., 48 B.R. 635, 639 (Bankr. S.D. Cal. 1985). These cases are taken up *infra* at notes 246-301.

> Assignments which are made conditional on the performance of certain acts or events, such as the payment of money or other condition subsequent, if recorded in the Office, are regarded as absolute assignments for Office purposes until canceled with the written consent of all parties or by the decree of a court of competent jurisdiction. The Office does not determine whether such conditions have been fulfilled.[40]

The regulations thus make allowance for security instruments recordable as title transferring assignments, subject to a defeasance condition—a condition that is officially ignored under the regulations of the Patent and Trademark Office.[41]

There is understandable confusion about the kind of transfer document or instrument that qualifies as a "conditional assignment" that will, in turn, be recorded and treated as an absolute assignment under section 3.56 of the regulations. Some commentators have concluded that the term "conditional assignment" refers to a transfer for security where the debtor agrees to assign on the contingency of default.[42] However, agreements to assign in the future, even unconditional ones, carry only equitable, not legal, title.[43] Because they do not convey the *entire title* they are not within the assignment-sensitive constructive notice mandate of section 261.[44] A close reading of 37 C.F.R. section 3.56 suggests that it refers to present assignments with the condition subsequent of defeasance, in the manner of the old conditional sale.[45] The condition referred to is the "*payment of money or other condition subsequent*."[46] A *condition subsequent* arises after the assignment, not before it. "Payment of money" is an event of *defeasance*, not an event of *default*. A debtor who retains title while agreeing to assign on an event of default, on the other hand, provides a classic example of a *condition precedent*, not a condition subsequent, to assignment. Such agreements to assign are really *contingent assignments*, not conditional assignments within the meaning of section 3.56 of

40. 37 C.F.R. § 3.56 (1994).

41. *Id.*

42. A. Haemmerli, *Insecurity Interests: Where Intellectual Property and Commercial Law Collide*, 96 COLUM. L. REV. 1645, 1710-11 (1996). The 1992 comments accompanying 37 C.F.R. section 3.56 lend some support to the notion that agreements to assign on an event of default will be considered "conditional assignments." CHANGES IN PATENT & TRADEMARK ASSIGNMENT PRACTICE—DISCUSSION OF SPECIFIC SECTIONS TO BE CHANGED OR ADDED, 57 Fed. Reg. 29634, 29637 (July 6, 1992) [hereinafter referred to as CHANGES IN PATENT & TRADEMARK ASSIGNMENT PRACTICE] ("Since the Office will not determine whether a condition has been fulfilled, the Office will treat the submission of such an assignment for recordation as signifying *that the act or event has occurred.*") (emphasis added). This commentary suggests that the *condition precedent* of default will be *assumed* by the PTO in order to make the transfer absolute, rather than the *condition subsequent* of payment that would have to be *ignored* to make the transfer absolute when payment is an event of defeasance. *See* WARD, *supra* note 18, § 2:86 n.17. *But see In re* Cybernetic Services, Inc., 2001 U.S. App. LEXIS 11750 at **18-28 (9th Cir. June 6, 2001) (security interest is a mere license).

43. Arachnid, Inc. v. Merit Indus., Inc., 939 F.2d 1574, 1580-81 (Fed. Cir. 1991) ("[A] . . . provision that all rights to inventions developed during the consulting period 'will be assigned' by IDEA to Arachnid does not rise to the level of a present assignment of an existing invention, effective to transfer all legal and equitable rights therein." (Arachnid had an equitable right only.)).

44. *See supra* note 37.

45. 37 C.F.R. § 3.56 (1994).

46. *Id.* (emphasis added).

the regulations.[47] In a sense, all Article Nine security agreements in a patent are in the nature of contingent assignments.[48] This distinction between the security agreement worded as an agreement to assign in the future (equitable title only) and a conditional assignment (legal title subject to some condition subsequent of defeasance) seems to be recognized by the PTO.[49]

Prior to the new PTO regulations in September 1992, the recording of a "security interest" was not required. Security interests, as such, were recorded at the discretion of the Commissioner.[50] The current regulations specify that "other documents . . . *affecting title* . . . will be recorded as provided in this part or at the discretion of the Commissioner."[51] It is not clear how this new regulatory language applies to security agreements. Under Article Nine, security agreements transfer a *security interest* to the transferee, but they do not transfer "title," *unless the parties intend that result*.[52] If the parties do express an intention to pass present title to the secured party in the transfer document, then the regulations would consider the transfer document (e.g., modified title-bearing security agreement, conditional assignment, or patent mortgage) an "assignment" for recording purposes. The defeasance conditions in these documents will be ignored by the PTO.[53] However, whenever the parties intend that only a security interest pass to the transferee/secured party, with the rights of ownership remaining in the transferor, the

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47. *In re* 199Z, Inc., 137 B.R. 778, 782 (Bankr. C.D. Cal. 1992); Clorox Co. v. Chemical Bank, 1996 TTAB LEXIS 15, 40 U.S.P.Q.2d 1098, 1100 n.10 (TTAB 1996) (security agreement is in the nature of an agreement for a future contingent assignment). *But see In re* Cybernetic Services, Inc., 2001 U.S. App. LEXIS 11750 at **18-28 (9th Cir. June 6, 2001) (a security interest is a "mere license").

48. "[A security agreement] is a mere agreement to assign in the event of default by the debtor." *In re* 199Z, Inc., 137 B.R. at 782; *see also* Note, *Recording Security Interests in Patents: Accepting A Traditional Federal System To Preserve the Policies Of Patent Law*, 2 B.U.J. SCI. & TECH. L. 15 para. 33-34 (1996).

49. Section 313 of the Manual for Patent Examining Procedure (MPEP) provides that:

> Some documents which relate to patents and applications will be recorded although they do not constitute a transfer or change of title. Typical of these documents which are accepted for recording are license agreements and agreements which convey a security interest. *Such documents are recorded in the public interest in order to give third parties notification of equitable interests or other matters relevant to the ownership of a patent or application.*

MPEP, *supra* note 35, at § 313 (emphasis added).

50. PATENTS, TRADEMARKS, AND COPYRIGHTS, 37 C.F.R. § 1331(a), (b) (replaced September 1992).

51. *Id.* § 3.11 (1994).

52. U.C.C. §§ 2-401(1), 9-102, 9-101, cmt. ¶ 9 (1995).

Comment 9 to section 9-101 reads:

> This Article does not determine whether "title" to collateral is in the secured party or in the debtor and adopts neither a "title theory" nor a "lien theory" of security interests. Rights, obligations and remedies under the Article *do not depend on the location of title* (Section 9-202). The location of title may become important for other purposes—as, for example, in determining the incidence of taxation—and in such a case the parties are left free to contract as they will. In this connection the use of a form which has traditionally been regarded as determinative of title (e.g., the conditional sale) could reasonably be regarded as evidencing the parties' intention with respect to title to the collateral.

Id. (emphasis added).

53. 37 C.F.R. § 3.56 (2000).

transfer document is not considered an assignment under the regulations.[54] Such a document would not be recorded for constructive notice within the section 261 mandate for an "assignment, grant or conveyance."[55] However, even a plain "security agreement" is specifically referred to as a *recordable document* in the Comments accompanying revised section 3.31 of 37 C.F.R. (formalities of the new cover sheet).[56] It seems to follow that the recording of a nontitle-bearing security interest remains discretionary under the new regulations.[57] Under their internal regulations, the PTO has chosen to provide assignment-like notice of security by giving nontitle-bearing security interests equal dignity with assignments on the cover sheet.[58] The PTO policy is a convenience for searchers,[59] but it does not expand the statutory scope of the constructive notice.[60] However, the fact that a security interest filed as a discretionary document with the PTO is not statutory constructive notice does not mean that such a filing cannot have legal effect. A discretionary filing should provide actual or inquiry notice to all those prospective purchasers or mortgagees who actually consulted the PTO record.[61]

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54. Response to Public Comment on 37 C.F.R. § 3.56, PATENTS, TRADEMARKS, AND COPYRIGHTS, 57 Fed. Reg. 29,640 (July 6, 1992). The response explained:

> *Response*: Section 3.56 [on conditional assignments] is applicable only to assignments, as they are defined by § 3.1, that is, a transfer of right, title and interest in a patent or a trademark. A security interest or a security agreement is in the nature of a lien, not an assignment. Accordingly, § 3.56 would not apply to security interests or security agreements which are also recordable.

Id.

55. 35 U.S.C. § 261 (1994); *see also supra* note 37; Holt v. United States, 13 U.C.C. Rep. Serv. 336, 338-39 (D.D.C. 1973); Bramson, *supra* note 22, at 1584; MPEP, *supra* note 35, § 313 ("*Such documents are recorded in the public interest in order to give third parties notification of equitable interests or other matters relevant to the ownership of a patent or application.*") (emphasis added).

56. 37 C.F.R. § 3.31 cmt. (1994).

57. *Id.*

58. CHANGES IN PATENT & TRADEMARK ASSIGNMENT PRACTICE, *supra* note 42, at 29,636 ("Section 3.31 is added to set out the formal requirements of the cover sheet. Section 3.31 requires that each patent or trademark cover sheet must contain . . . (3) a brief description of the interest conveyed or transaction to be recorded (e.g., assignment, license, change of name, merger, security agreement, etc.).").

59. *See supra* note 37.

60. *In re* 199Z, Inc., 137 B.R. 778, 782 n.7 (Bankr. C.D. Cal. 1992). The case provides:

> This result is not altered by the fact that, as in this case, the Patent Office accepts the filing of documents memorializing the granting of a security interest in a trademark. The Lanham Act gives the Patent Office the discretion to accept various documents not expressly described in the Act; it does not, however, expressly provide for the filing of documents memorializing pledges of trademarks, as the Copyright Act does for hypothecations of copyrights.

Id.

61. 35 U.S.C. § 261 (1994) ("purchaser or mortgagee . . . without notice"); *see also In re* Cybernetic Services, Inc., 239 B.R. 917, 921 n.10 (9th Cir. B.A.P. 1999), aff'd, 2001 U.S. App. LEXIS 11750 (9th Cir. June 6, 2001). *Cybernetic* provides:

> Because the Patent Manual expressly "does not have the force of law or the force of the rules in Title 37 of the Code of Federal Regulations," it appears that the discretionary recording is for purposes of providing actual notice rather than the constructive notice provided through provisions of Article 9 of the UCC.

Id. (citations omitted).

Unfortunately, the leading decision on the relationship between section 261 of the Patent Act and Article Nine concludes that a security interest is properly characterized as a "mere license" for recording act purposes. The Ninth Circuit's recent decision in *In re Cybernetic Services, Inc.*[62] uses a "mere license" characterization to make the point that the security interest/license does not need to be recorded under section 261 because, under the venerable patent law rule, assignees take subject to the prior licenses irrespective of notice.[63] The Ninth Circuit's reason for classifying the security interest as a license in *Cybernetic Services* seems to be founded on the ancient distinction between a transfer of the whole patent (e.g., the whole exclusive right, an undivided share of that right, or the exclusive right within a specified part of the United States)[64] and a transfer of something less than the whole (a mere license).[65]

The Ninth Circuit's underlying holding that a security interest is not a section 261 assignment, grant, or conveyance is well founded. Its conclusion that it must therefore be a "mere license" is not. Although the modern security interest does not usually carry title, it is still a transfer of the whole right.[66] As noted above, in terms of historical antecedents, the security interest bears a close resemblance to the transfer of "equitable title" in the whole patent.[67] It has almost nothing in common with a license. The Ninth Circuit decision in *Cybernetic Services* is taken up *infra* at III.B.3.b.v.[68]

3. *The Lanham Trademark Act*

Section 1060 of the Lanham Act contains the most abbreviated statement on the recording of transfers in all three of the major federal intellectual property statutes. Section 1060 of the Act provides, "[a]n *assignment* shall be void as against any subsequent purchaser for valuable consideration without notice, unless it is recorded in the Patent and Trademark Office within three months after the date thereof or prior to such subsequent purchase."[69] Only "assignments" of registered marks and applications to register (other than intent-to-use applications) need to

62. 2001 U.S. App. LEXIS 11750 (9th Cir. June 6, 2001).

63. 2001 U.S. App. LEXIS 11750, at **26-28; *see* 6 E. LIPSCOMB, WALKER ON PATENTS § 20:22, at 79.

64. 2001 U.S. App. LEXIS 11750, at **23-24; *see* 35 U.S.C.A. § 261; *see also* 5 E. LIPSCOMB, WALKER ON PATENTS § 19:4, at 333-34.

65. 2001 U.S. App. LEXIS 11750, at **23-24; *see* 5 E. LIPSCOMB, WALKER ON PATENTS § 19:4, at 333-34.

66. *See* U.C.C. § 9-101 cmt. ("This Article does not determine whether 'title' to collateral is in the secured party or in the debtor and adopts neither a 'title theory' nor a 'lien theory' of security interests.").

67. *See* discussion *supra* at notes 42-52.

68. *See* discussion *infra* at notes 291-300.

69. 15 U.S.C. § 1060 (1994). Assignments of applications to register (other than intent-to-use applications) are included. 37 C.F.R. § 3.11 (1997) ("applications, patents, and registrations"); 37 C.F.R. § 3.85 (1997) ("Certificate of registration may be issued to the assignee of the applicant . . . provided . . . the appropriate document is recorded in the Office."); 37 C.F.R. § 3.16 (1997) ("No application to register a mark under 15 U.S.C. 1051(b) is assignable prior to the filing of the verified statement of use under 15 U.S.C. 1051(d) except to a successor to the business of the applicant, or portion thereof, to which the mark pertains, if that business is ongoing and existing.").

be recorded in order to be protected against "subsequent purchasers." For preemption purposes, the very limited scope of section 1060 should be contrasted with its counterpart provisions for recording federal copyrights and patents discussed earlier.

The narrow language of section 1060 is not surprising given the differences between registered trademarks and other federal intellectual property. Although trademarks are the responsibility of the same federal agency charged with supervising patents, they are a very different form of property. They differ from patents in three important ways. First, trademarks are fundamentally a state common law right that is only enhanced and protected by federal registration. Second, trademarks cannot stand alone as personal property. Finally, the recording provision for federally-registered marks reflects these distinctive aspects in its very singular and narrow "assignments" scope.

When compared to patents and copyrights, the federal stake in trademarks is not as high. Trademark rights arise under state law from the use of business names, images, sounds, and devices in association with the source and quality standard of a product or service of the enterprise. The existence of a mark depends upon customer identification of it with a particular source. Even the owner of the mark may not be able to control its creation. While federal law allows for the federal registration of trademarks, and such registration elevates the degree of protection afforded an owner of a mark,[70] federal law does not create separate exclusive property in the trademark in the same sense that it does for patents, copyrights, and maskworks.

Its state law origins are not the only thing that sets trademarks apart as "property." As the Federal Circuit has said: "Unlike patents or copyrights, trademarks are not separate property rights. They are integral and inseparable elements of the goodwill of the business or services to which they pertain."[71] While copyrights and patents can stand on their own title, trademarks cannot.[72] This dependent relationship between marks and other "goodwill" assets of the underlying user affects the usefulness of marks as a commercial asset. For example, while some security interests can be taken in a trademark standing alone (not a recommended practice),[73] no effective disposition of trademark collateral at foreclosure is pos-

70. The Lanham Act provides that "[t]he owner of a trademark used in commerce may apply to register his or her trademark under this chapter." 15 U.S.C. § 1051(a) (2000). The Lanham Act permits the potential user of a mark to file an intent-to-use application covering a mark not presently in use. *Id.* § 1051(b). However, no registration can issue on an intent-to-use application unless the mark is actually used in commerce and its use is verified in a filed statement to that effect. *Id.* § 1051(d) (2000).

71. Visa, U.S.A., Inc. v. Birmingham Trust Nat'l Bank, 696 F.2d 1371, 1375 (Fed. Cir. 1982).

72. United Drug Co. v. Theodore Rectanus Co., 248 U.S. 90, 97 (1918) ("There is no such thing as property in a trademark except as a right appurtenant to an established business or trade in connection with which the mark is employed."); Visa, U.S.A., Inc. v. Birmingham Trust Nat'l Bank, 696 F.2d at 1375 ("[A] mark may be transferred only in connection with the transfer of the goodwill of which it is a part. A naked transfer of the mark alone—also known as a transfer in gross—is invalid."); Glamorene Prod. Co. v. The Procter & Gamble Co., 538 F.2d 894 (C.C.P.A. 1976).

73. The first paragraph of the Official Comment to old Article Nine section 9-106 mentions trademarks as personal property within the category of general intangibles. U.C.C. § 9-106 cmt. ¶ 1 (1995); *see also* U.C.C. [Revised] § 9-102(a)(42) & cmt. 5(d).

sible without the transfer of the debtor's goodwill that is associated with the name or mark.[74]

It must be noted here that the characterization of trademarks as dependent under United States law is out of step with our current treaty obligations, and the rule may be in some jeopardy. Among the many provisions of the NAFTA Treaty affecting intellectual property is article 1708:11, calling for the elimination of all prohibitions on assignments-in-gross.[75] The 1993 implementing legislation was silent on the issue, however.[76] Without implementing legislation on NAFTA article 1708:11, the prohibition on assignments-in-gross under our domestic law remains in place.[77] If Congress does implement NAFTA article 1708:11, trademarks could claim the same stand-alone property characteristic of patents and copyrights. The historic and current dependent relationship between marks and other assets of the underlying user would suggest that *separate* mortgage rights generally taken by a lender or other financer, who is not an underlying user, were not viewed as included in the federal recording provision for registered marks and pending applications.

B. Common Problems with Federal Intellectual Property Recording Statutes As Repositories for Security Interest Filing

The recording provisions of all three federal schemes are one-dimensional in the sense that they focus only on the necessity of providing purchasers of the intellectual property with delayed constructive notice of prior consensual interests.[78] None of these schemes deals specifically with after-acquired rights, involuntary liens, or the rights of creditors other than purchasers. The Patent Act and the Trademark Act seem to deal only with the recording of *prior* title transfers for the protection of *subsequent* title transferees.[79] In general, the recording provisions of these schemes protect the first transfer executed as long as the transfer is recorded within a generous grace (look-back) period.[80] Prior unrecorded transfers can remain secret yet valid as to subsequent parties for long periods. While these provi-

74. Sugar Busters LLC v. Brennan, 177 F.3d 258, 265 (5th Cir. 1999) ("[A] trademark cannot be sold or assigned apart from the goodwill it symbolizes."); *see also supra* note 72.

75. North American Free Trade Agreement, opened for signature Dec. 8, 1992, 32 I.L.M. 605, art. 1708:11 [hereinafter NAFTA Treaty]; Agreement on Trade-Related Aspects of Intellectual Property Rights, Including Trade in Counterfeit Goods, Dec. 15, 1993, 33 I.L.M. 81, art. 21 [hereinafter TRIPs Agreement].

76. H.R. 3450, 103d Cong., 1st Sess., 139 CONG. REC. S16712-13 (1993) (enacted).

77. *See supra* note 72.

78. The Copyright Act protects a "later transfer" if recorded first, and "taken in good faith, for valuable consideration." 17 U.S.C. § 205(d) (1994). The concept of taking for valuable consideration has been expanded by one court to include the judicial lien creditor as constituted by statute in the bankruptcy trustee. *See* National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 207 (C.D. Cal. 1990).

79. 35 U.S.C. § 261 (1994) ("an assignment, grant or conveyance" of Patents); 15 U.S.C. § 1060 (1994)("an assignment" of Trademarks). The recording provision in the Semiconductor Chip Protection Act applies to "conflicting transfers of the exclusive rights in a mask work." 17 U.S.C. § 903 (1994). In contrast, section 205 of the Copyright Act applies to "[a]ny transfer of copyright ownership." 17 U.S.C. §§ 205(a), (d) (1994).

80. 35 U.S.C. § 261 (1994); 15 U.S.C. 1060 (1994); 17 U.S.C. § 205(d) (1994); *see also* 17 U.S.C. § 903 (1994). These long grace periods play havoc with secured party priority rules that fall within their scope. *See* WARD, *supra* note 18, §§ 2:77-2:78 (circular priority examples under section 205(d) of the Copyright Act).

sions may be tolerable for ordering ownership rights, their long look-back periods are hopelessly cumbersome when ordering lien priority. Lenders will not release the total committed funds unless they are sure that the time for protecting any potential prior interest by recording has expired.

These already long federal look-back periods are exacerbated by further "office delays." These office delays result from the fact that transfers are deemed "recorded" within the applicable look-back periods from the time they are *received* for recording, even though the internal steps necessary to make them accessible to searchers may take several months more.[81] Even after the implementation of a new voluntary cover sheet, the Copyright Office is still dealing with "office delays" that average six months.[82]

Both the recording and the priority provisions of these federal recording statutes lack the vocabulary and the structure to deal with the modern notion of a security interest. They are frozen in the nineteenth century concepts of title and formal document recordation. They are figuratively and literally in a time warp.

Despite the structural dissonance, it is clear that both old and Revised Article Nine recognize the potential and actual displacing effect of these federal intellectual property statutes. Old Article Nine seems to make positive deference to these recording provisions in its so called "step-back" language, while Revised Article Nine language purports to yield nothing to these statutes that could not be wrenched away under federal preemption theory. These Article Nine (state law) efforts at meshing the two structures are taken up next.

III. SORTING OUT THE CONFLICT BETWEEN ARTICLE NINE AND THE FEDERAL INTELLECTUAL PROPERTY RECORDING ACTS

A. Article Nine's Expressed Deference to Federal Recording Statutes

1. Positive Deferral or Merely an Unnecessary Recognition of the Effect of Preemption Doctrine?

The drafters of old Article Nine recognized that all or part of the statute would be displaced by federal recording or priority provisions that covered the same ground. The general preemptive force of federal law is recognized in old section 9-104(a). Old section 9-104(a) makes Article Nine inapplicable to "a security interest subject to any statute of the United States, *to the extent* that such statute governs the rights of parties to and third parties affected by transactions in particular types of property."[83] Revised Article Nine has a more straightforward recognition of federal preemption in Revised section 9-109(c)(1). The new language provides simply that the Article does not apply to the extent that it is preempted by "a statute, regulation, or treaty of the United States."[84]

In addition to this general recognition of federal preemption, the "filing" pro-

81. Bramson, *supra* note 22, at 1574 n.36.

82. Telephone interview with Maria L. Llacuna, Copyright Document Specialist, Copyright Office, Library of Congress, Washington, D.C. (February 3, 2000) (on file with the author).

83. U.C.C. § 9-104(a) (1995) (emphasis added).

84. U.C.C. [Revised] § 9-109(c)(1).

visions of both Article Nine versions recognized a more limited overlap with federal recording and registration laws. The general premise here is that even when Article Nine controls attachment, priority, and default issues the filing or recording instructions of the Article must sometimes yield to a pervasive federal recording system. With respect to the language used to describe the breadth of this second-level deference to federal recording provisions, however, the two versions of Article Nine differ. Old section 9-302(3)(a) makes Article Nine filing give way to "a statute . . . of the United States which provides for a national . . . registration . . . or which specifies a place of filing different from that specified in this Article for the filing of the security interest."[85] This so-called "partial step-back" in the old Article is framed in a more restrictive manner under the wording in Revised Article Nine. Revised section 9-311(a)(1) purports to limit eligibility for the filing deferral 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 preempt* [the Article Nine filing requirement for perfection]."[86]

This notion of a state law deferral at two separate levels will be taken up next along with the federal preemption doctrine. Recognition of federal preemption no doubt prompted the specific statutory deferral language in Article Nine, but the preemption doctrine itself has a constitutional source and it heeds no state statute.

2. *Complete "Step-Back" in Old Section 9-104(a) and Revised Section 9-109(c)(1)*

Transactions involving a "security interest" in personal property that are nevertheless *excluded* from old Article Nine are catalogued in section 9-104. The first exclusion is for a "security interest subject to any statute of the United States . . . to the extent that such statute governs the rights of parties to and third parties affected by transactions in particular types of property."[87] The drafters of old Article Nine had in mind the federal intellectual property schemes when the language of subsection (1) was crafted because both the Patent Act and the Copyright Act are mentioned in the Official Comment to section 9-104. At the time, the drafters did not view either the Copyright Act or the Patent Act as sufficiently comprehensive in its treatment of the security-related rights of "parties and third parties" to warrant *complete exclusion* from the Article Nine scheme.[88] Even at that time, however, the recording provision of the Copyright Act was more complete than the narrow, title-based system in effect under the Patent Act and the Lanham Trade-

85. U.C.C. § 9-302(3)(a) (1995); *accord* U.C.C. [Revised] §§ 9-311(a)(1), (b).

86. U.C.C. [Revised] § 9-311(a)(1).

87. U.C.C. § 9-104(a) (1995); *accord* U.C.C. [Revised] § 9-109(c) ("This article does not apply to the extent that: (1) a statute, regulation or treaty preempts this article.").

88. The Official Comment appended to both the 1962 and 1972 texts of section 9-104 refers to the Federal Copyright Act as an example of a statute that "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." U.C.C. § 9-104 cmt. 1 (emphasis added). This Comment also invites a comparison between the recordation provisions of the Copyright Act and the provisions of the Patent Act. *Id.*

mark Act.[89] The U.C.C. was enacted in the various states between 1955 and 1969.[90] While the recordation and priority language in both the Patent Act and the Trademark Act remain basically unchanged since the Code was written, the Copyright Act was substantially revised in 1976.[91] These 1976 revisions established a comprehensive federal priority scheme for copyrights that expanded further the already broader reach of the Copyright Act.[92] Although the present Copyright Act is not nearly as comprehensive as Article Nine, two federal court decisions from the Central District of California have concluded the Act does qualify for the complete "step-back" exclusion in U.C.C. section 9-104(a).[93] *National Peregrine, Inc. v. Capital Federal Savings & Loan Ass'n*[94] and *In re AEG Acquisitions Corp.*[95] conclude that the section 9-104(a) exclusion is mandated by federal preemption doctrine, resulting in the complete displacement of the *filing and priority* rules of Article Nine by section 205 of the Copyright Act whenever collateral rights in a copyright are contested.[96]

The drafters designed the Old section 9-104(a) exclusion so that whenever the scope of a "statute of the United States" triggered the exclusion, gaps in the "statute" could be filled by looking to Article Nine. As a source of supplementary rules, the drafters were probably thinking of Article Nine as enacted in the state having the most appropriate contacts with the secured transaction at issue.[97] Preserving some limited role for the Article Nine scheme was based on the assumption that a federal statute described in section 9-104 would not displace Article Nine completely but only "to the extent" that the federal statute governs the rights of the parties. The Code plays a similar, but not identical, supplementary role when federal preemption is the displacing theory.[98] When enacted state rules inform the federal common law, the result under the preemption doctrine should be the same as when section 9-104(a) applies. Under either approach, local law is

89. Section 30 of the 1909 Copyright Act envisioned the recording of mortgages by *subsequent* mortgagees. Copyright Act of 1909, ch. 320, § 30, 35 Stat. 1075, 1081-82 (1909) (repealed 1976). However, the Act referred only to "assignments" as recordable. *Id.* Furthermore, section 28 of the 1909 Act did not clearly make provision for mortgagee priority. *Id.* at § 28.

90. *See* H. Weinberg & W. Woodward, *Legislative Process and Commercial Law: Lessons from the Copyright Act of 1976 and the Uniform Commercial Code*, 48 BUS. LAW. 437, 454 (1993).

91. The Copyright Act of 1976, as amended, 17 U.S.C. § 101-1101 (Supp. 1999).

92. 17 U.S.C. § 205 (1994).

93. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 203-04 (C.D. Cal. 1990); *In re* AEG Acquisitions Corp., 127 B.R. 34, 41 at n.8 (Bankr. C.D. Cal. 1991), *aff'd*, 161 B.R. 50 (B.A.P. 9th Cir. 1993).

94. 116 B.R. 194 (C.D. Cal. 1990).

95. 127 B.R. 34 (Bankr. C.D. Cal. 1991), *aff'd*, 161 B.R. 50 (9th Cir. B.A.P. 1993).

96. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 203-06; *In re* AEG Acquisitions Corp., 127 B.R. at 41 n.8. The *Peregrine* decision is discussed in greater detail *infra* at notes 130-95.

97. "Thus if the federal statute contained no relevant provision, this Article could be looked to for an answer." U.C.C. § 9-104 cmt. 1.

98. When a judicial determination of complete preemption is made, Article Nine may still remain as a source of supplementary federal common law rules. The enacted law of a particular contact state will often be the appropriate source for federal common law rules necessary to supplement the applicable federal scheme. United States v. Kimbell Foods, Inc., 440 U.S. 715, 718 (1979); *see also* JAMES J. WHITE & ROBERT S. SUMMERS, THE UNIFORM COMMERCIAL CODE § 21-10, at 752-54 (4th ed. 1995).

displaced by the federal scheme but should be consulted where the federal scheme is silent. However, enacted state law will be ignored in formulating federal common law rules when there is a strong overriding interest in national uniformity and otherwise applicable state law varies from the commercial norm.[99] In such cases, the "Uniform Version" of Article Nine, rather than the version enacted in the "contact" state, may be the best place to find the supplementing federal common law.[100] The distinction may have limited importance, however, because there is general uniformity with respect to definitions and priority rules among the enacted versions of Article Nine.

3. Old Article Nine's "Partial Step-Back" for a Federal Filing and Revised Article Nine's More Limited Filing Deferral

Old section 9-302(3)(a) and Revised section 9-311(a)(1) provide for the displacement of the Article's filing rules in situations where the Article is not generally preempted and therefore, otherwise applicable to the secured transaction in question. The language of old section 9-302(3)(a) provides that the filing requirements of Article Nine are displaced if the collateral in question is subject to "a statute . . . of the United States which provides for a national or international registration or a national or international certificate of title."[101] Both the 1962 and 1972 Official Comments to section 9-302 refer to the Copyright Act as an example of "the type of federal statute referred to in paragraph (3)(a)."[102] This Comment reference is consistent with the language in Comment 1 to section 9-104, which concludes that, while security interests in copyrights are governed generally by Article Nine, filing under the Copyright Act is "recognized as the equivalent to filing under this article."[103]

The Patent Act is not mentioned in Comment 8 to section 9-302.[104] The two Official Comments can be reconciled, however, in a way that recognizes the more limited scope of Patent Act recording. If the "compare" reference in section 9-104

99. *Id.*.

100. Allen v. F.D.I.C., 599 F. Supp. 104 (E.D. Tenn. 1984); F.D.I.C. v. Morgan, 727 S.W. 2d 500 (Tenn. Ct. App. 1986).

101. U.C.C. § 9-302(3)(a) (1995); *see also* 1 GILMORE, *supra* note 3, § 19.9.

102. U.C.C. § 9-302 cmt. 8 (1995).

103. U.C.C. § 9-104 cmt. 1 (1995). Again, it should be noted that while the language of the Old Article Nine comments had not changed since 1972, the Copyright Act of 1976 created a much more comprehensive priority scheme for copyrights than the scheme that was in place when the Code Comments were written. The current Copyright Act's definition of "transfer" is very broad. 17 U.S.C. §§ 101, 201(d)(1) (1994).

104. U.C.C. § 9-302 cmt. 8 (1995). While the Patent Act is not mentioned in Comment 8 to old section 9-302, it is referred to in the comment following section 9-104. The section 9-104 reference can be construed to mean that, while the drafters did not find the Patent Act sufficiently comprehensive to displace Article Nine in general, they did view the recording provision of the Patent Act as displacing Article Nine filing. Such a construction would bring the comments to old section 9-104 into conflict with the distinction between copyright recording (displaces) and patent recording (does not displace) suggested by the comments following old section 9-302.

After mentioning the Copyright Act as an example of a statute which qualifies for the "partial step-back," the comment to old section 9-104 makes a footnote-like reference that invites the reader to "[c]ompare also with respect to patents, 35 U.S.C. § 47." Section 47 was the nearly identical predecessor to current section 261 of the Patent Act. After this express reference to old section 47, the Comment continues with the following language: "The filing provisions under

Official Comment 1 was intended to suggest a contrast between the Copyright Act and the stronger "title" orientation of the Patent Act, then the proper inference has a different, and more understandable, spin. If the "compare" language suggests contrast, then the reference in the comments after section 9-104 to "these acts" would not include the Patent Act and should be taken merely as a general reference to all present or future federal recording schemes that, like the then-extant Copyright Act, mimic the Federal Aviation Act in this regard. Under this latter view of the Official Comment to old section 9-104, recording under the Patent Act would not be viewed as a section 9-302(3)(a) substitute for perfection by filing under old Article Nine. The truncated recordation provision of that Act provides for the recording of "an assignment, grant or conveyance." This limited recording provision has changed very little since 1897.[105] Uniform Commercial Code Comment 8 to section 9-302 makes no mention of the recording provisions of the Lanham Trademark Act either.[106] The recordation provision covering trademarks was revised in 1988, but it remains very similar in scope to the comparable provision of the Patent Act.[107]

Whenever U.C.C. section 9-302(3)(a) requires a "partial step-back" in recognition of a national recording system, U.C.C. section 9-302(4) makes "compliance" with the recognized national system exclusive.[108] Furthermore, when Article Nine filing must yield, it must yield completely. The national system becomes the *exclusive* equivalent. The only decision to actually implement the partial step-back along the filing-only lines set out in section 9-302(3) and (4) is *In re Avalon Software*,[109] a Bankruptcy Court decision from the District of Arizona.[110] *Avalon Software* is a decision involving copyrightable software that rejects the

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these Acts, like the filing provisions of the Federal Aviation Act, are recognized as equivalent to filing under this Article. Section 9-302(3) and (4)." U.C.C. § 9-104 cmt. 1 (emphasis added). If "these Acts" refers to enactments previously named in the Comment, other than the Federal Aviation Act, then the drafters were implying that the recording provisions of the Patent Act also created a system of "national registration" for purposes of the section 9-302(3)(a) partial step-back. Recall, however, that the Patent Act is not mentioned in the Official Comments after section 9-302 itself, while the Copyright Act gets a prominent top billing as a displacing filing scheme. *Accord In re* Cybernetic Servs., Inc., 2001 U.S. App. LEXIS 11750 at *44-48 (9th Cir. June 6, 2001).

105. 35 U.S.C. § 261 (1994). The present statute covers the same transfers as old section 4898 of the pre-1897 Patent Act. American Solid Leather Button Co. v. Empire State Nail Co., 47 F. 741, 742 (C.C. S.D.N.Y. 1891).

106. U.C.C. § 9-302 cmt. 8 (1995); *see also* Roman Cleanser v. National Acceptance Co., 43 B.R. 940, 945 (Bankr. E.D. Mich. 1984), *aff'd*, 802 F.2d 207 (6th Cir. 1986); *In re* 199Z, Inc., 137 B.R. 778, 782 (Bankr. C.D. Cal. 1992).

107. 15 U.S.C. § 1060 (1994) ("An assignment shall be void as against any subsequent purchaser for a valuable consideration without notice, unless it is recorded in the Patent and Trademark Office."); *see also* 17 U.S.C. § 903(c)(2) (1994) (Semiconductor Chip Protection Act provision on recording).

108. U.C.C. § 9-302(4) & cmt. 8 (1995).

109. 209 B.R. 517 (Bankr. D. Ariz. 1997). *See* discussion *infra* at notes 196-223.

110. Even the partial preemption patent cases do not follow the section 9-302(3) & (4) partial step-back. These cases preserve the effectiveness of a state Article Nine-filed financing statement for "perfection" against the bankruptcy-formed lien creditor. On the other hand, these cases (all lower court decisions) also suggest that state perfection would not be enough against a subsequent assignee. Chesapeake Fiber Packaging Corp. v. Sebro Packaging Corp., 143 B.R. 360, 368, 19 U.C.C. Rep. Serv. 2d (CBC) 600, 610 (D. Md. 1992), *aff'd*, 1993 U.S. App. LEXIS

total step-back approach taken earlier in the *Peregrine* decision. *Avalon Software* concludes that once the displacing federal equivalent is found, "compliance" with that statute means achieving the fullest measure of recording act protection available under it.[111] In *Avalon Software*, the federal "it" is the Copyright Act.[112] Full "compliance" with the Copyright Act's recording provisions in section 205 means that a section 205(a) recording, by itself, is not enough.[113] The security interest must be recorded "in the manner required to give constructive notice" within the meaning of subsection (c) of section 205.[114] In order for a recording to give constructive notice under subsection (c), the underlying copyrighted work must be reasonably identified in the document recorded, and the underlying copyrighted work must be registered.[115]

The filing deferral language in Revised Article Nine purports to limit eligibility for the deferral 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 preempt* [the Article Nine filing requirement for perfection]."[116] Only statutes with "requirements" that, if met, will allow the secured party to defeat the lien creditor are treated, under the Revisions, as capable of displacing Article Nine filing.[117] Clearly, the Patent Act and the Trademark Act would not have sufficient "requirements" to trigger a filing deferral under the Revised language. Although the Copyright Act clearly seems to qualify for the partial step-back from Article Nine filing under old section 9-302(3)(a),[118] it might also fall short of the "requirements" language added by the Revisions.[119] If a subsequent transferee of a copyright ownership interest protected under section

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28605 (4th Cir. 1993); City Bank and Trust Co. v. Otto Fabric, Inc., 83 B.R. 780, 782 (D. Kan. 1988); *In re* Transp. Design and Tech., Inc., 48 B.R. 635, 639, 40 U.C.C. Rep. Serv. 2d (CBC) 1393, 1398 (Bankr. S.D. Cal. 1985). *But see In re* Cybernetic Servs., Inc., 2001 U.S. App. LEXIS 11750 at **18-28 (9th Cir. June 6, 2001) (a security interest is not an "assignment, grant or conveyance" for any recording purpose, instead it is a "mere license").

111. *In re* Avalon Software, 209 B.R. at 523.

112. *Id.* at 522.

113. *Id.*

114. 17 U.S.C. §§ 205(c)-(d) (1994). The idea that full compliance includes the stipulation that the recording be "in the manner required to give constructive notice" has also been upheld in a complete step-back case involving copyright collateral. *See In re* AEG Acquisitions Corp., 127 B.R. 34, 40-41 (Bankr. C.D. Cal. 1991), *aff'd*, 161 B.R. 50, 57 (9th Cir. B.A.P. 1993).

115. 17 U.S.C. § 205(a), (c), (d) (1994).

It can be argued that constructive notice under subsection (c) is not a recording requirement as such. A transfer of copyright ownership can be recorded even if it is not recorded in "the manner required to give constructive notice." However, the recorded document is not afforded priority under subsection (d) of section 205 unless it also provides "constructive notice." Therefore, the argument concludes, subsection (c) is a priority rule that does not trump Article Nine, rather than a "filing" requirement that must be complied with under the partial step-back mandated by U.C.C. sections 9-302(3)(a) and (4). *See id.*

Nevertheless, the *Avalon Software* court concludes that a security interest in a copyright is not "completely perfected" after a section 205(a) recording unless the copyright collateral is also registered so as to give constructive notice within the meaning of section 205(c) of the Copyright Act. See *In re* Avalon Software, Inc., 209 B.R. at 522. The *Avalon Software* decision is discussed *infra* at notes 196-223.

116. U.C.C. [Revised] §§ 9-311(a)(1) (emphasis added).

117. *See id.*

118. U.C.C. § 9-302 cmt. 8 (1995).

119. U.C.C. [Revised] 9-311.

205(d) of the Act does not include the lien creditor, a Copyright Act recording of a security interest would not meet the "requirements" test.[120] The current cases seem split on whether the "lien creditor" is a protected subsequent party under the Copyright Act's section 205(d) priority rule.[121]

4. Article Nine Deferral Language—Whistling in the Wind?

The notion of a state law deferral at two separate levels is to a great extent just wishful thinking by the Article Nine drafters. The complete step-back merely pays homage to law on preemption that would operate whether or not it was encrusted in Article Nine. The partial step-back language purports to draw its own line of proper integration between Article Nine and federal recording provisions, which provisions, in the case of patents and trademarks, also deal with priority. Even if the preemption of Article Nine by federal law is only partial, displacement has a constitutional predicate and need not heed the boundary line drawn within the displaced state statute—even a state statute with the prestige of Article Nine behind it. The next Section looks at the case law resolutions of these structural overlap issues. These cases discuss the various levels of regulation at which Article Nine should be displaced by the tract recording acts covering the major *federal* forms of intellectual property.

B. Finding the Line Between Article Nine and the Federal Intellectual Property Recording Acts in the Cases

1. Three Different Takes on the Level of Deferral and Preemption

The federal statutory recording schemes that control the fields of copyright, patent, and trademark have already been described. They are distinct but have common gaps. While each of these schemes makes some provision for recording, priority, and derivative interests (including to varying degrees security interests), none deals directly with the creation or priority of security interests. To further confuse the matter of preemption, none of these federal schemes refer to, or even acknowledge, the uniform state rules on security interests in Article Nine. Courts struggling with preemption are left with the task of deciding whether or not the particular federal scheme described earlier in Part II.A parallels the Article Nine rules to such an extent that Congress must have intended to preclude the application of state rules in favor of a particular federal rule. The differences between the federal schemes are great enough so that prior precedent under each must be examined separately and carefully. The following examination of the cases under each tract recording statute will focus on the unique preemption issues posed by each and the effect of the various judicial integrations of these statutes with both versions of Article Nine.

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120. *See* 17 U.S.C. §§ 205(a), (c), (d) (1994).

121. *Compare* National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 203-04 (C.D. Cal. 1990) (lien creditor is a protected transferee under section 205(d)), *with In re* Avalon Software, Inc., 209 B.R. 517, 521 (Bankr. D. Ariz. 1997) (federal recording mandated under present sections 9-302(3) and (4), but state law must be consulted to determine secured party/lien creditor priority).

2. Current Approaches to Reconciliation When Copyright Collateral Is Involved

a. Peregrine, Avalon Software, *and* World Auxiliary Power

The law on the preemptive effect on Article Nine of these Copyright Act recording and priority provisions revolves around three significant but somewhat inconsistent lower court decisions. All three decisions raise troubling issues about the viability of copyright collateral in debt financing transactions.

National Peregrine, Inc. v. Capital Federal Savings & Loan Ass'n,[122] a decision from the District Court for the Central District of California gives full preemptive effect to the broad transfer and recording language of the Copyright Act. *Peregrine* concludes that both the perfection and priority rules in Article Nine must yield to the recording and priority provisions of the federal Copyright Act.[123]

In re Avalon Software, Inc.,[124] a later Arizona Bankruptcy Court decision, construes the same Copyright Act language in a way that spares the priority rules in Article Nine from preemption and seems to find a mandate in the Copyright Act only for the partial "filing" step-back provided for in section 9-302(3)(a) of Article Nine. However, the decision extends the preemptive displacement of Article Nine filing by Copyright Act recording to all intangible collateral that is "copyrightable."[125]

The most recent opinion to address the subject is *In re World Auxiliary Power Company.*[126] In *World Auxiliary Power,* the Bankruptcy Court for the Northern District of California held for the secured party who had only filed under Article Nine. The court concluded that the secured party was "perfected" against the trustee because the copyright collateral at issue had not been "registered" under section 408 of the Copyright Act.[127] The theory in *World Auxiliary Power* is that Article Nine is not preempted (to any extent) when the copyright collateral is unregistered. The bankruptcy court in *World Auxiliary Power* begins with the modest suggestion that the *priority rule* in section 205(d) of the Copyright Act has no application to unregistered copyrights because registration is one of the conditions necessary for "constructive notice" and constructive notice is a condition of recording priority.[128] From that point the court goes on to the more controversial holding that the *recording* of "transfers of copyright ownership" provided for in section 205(a) of the Copyright Act does not preempt Article Nine *filing* when the copyrights are not registered.[129]

The *Peregrine* decision, its logic, and its progeny will be examined next. *Avalon Software* and *World Auxiliary Power* will be discussed against the backdrop of *Peregrine.*

122. 116 B.R. 194 (C.D. Cal. 1990).
123. *Id.* at 207.
124. 209 B.R. 517, 522-23 (Bankr, D. Ariz. 1997).
125. *Id.*
126. 244 B.R. 149 (Bankr. N.D. Cal. 1999).
127. *Id.* at 153-54.
128. *Id.* at 151 (citing 17 U.S.C. §§ 205(c)-(d) (1994)).
129. *Id.* at 154-56.

b. Peregrine: *The Complete Preemption Case*

i. Peregrine: *The Holdings*

The narrow issue in *Peregrine* was the "perfection" of copyright collateral and related receivables for purposes of section 544(a) of the Bankruptcy Code. In the bankruptcy court below, the secured party, Capital Federal, sought to enforce a security agreement covering film copyrights.[130] Capital had filed U.C.C. Article Nine financing statements covering the collateral described in its security agreement at the appropriate location in several states. However, Capital did not record the security agreement or a memorandum thereof as a "transfer of copyright ownership" in the Federal Copyright Office. The debtor in possession (armed with the rights of a bankruptcy trustee) wanted the Bankruptcy Court to treat Capital's security interest as "unperfected" in the absence of a Copyright Office recording. If Capital's interest was not perfected under Article Nine, it would be vulnerable to a lien creditor under section 9-301(1)(b),[131] and because the debtor in possession had the rights of a hypothetical lien creditor under section 544(a)(1) of the Bankruptcy Code, Capital's security interest could be avoided.[132] This seems to be the way the issue was framed in the Bankruptcy Court. In the Bankruptcy Court, the controversy seems to have been presented and resolved as a filing issue under the partial step-back rule in section 9-302(3).[133] Did the state filings perfect for purposes of the state law priority rule in Article Nine section 9-301(1)(b)? Or did Copyright Act recording displace the otherwise appropriate state filing under U.C.C. sections 9-302(3) and (4)?

In light of the partial step-back language in Article Nine sections 9-302(3)(a) and (4), the Bank's security interest seems to have been unperfected, as a matter of state law. As explained earlier in Part II.B.3 of this Article, Official Comment 8 to section 9-302 identifies the recording provisions of the Copyright Act as "a statute . . . of the United States which provides for a national . . . registration" within the meaning of the deferral rule in section 9-302(3)(a).[134] Subsection (4) of section 9-302 provides further that compliance with such a displacing statute of the United States becomes the exclusive method of perfection.[135] The Bankruptcy Court ignored section 9-302(4) and concluded that, while Capital could have "perfected" by recording in the Copyright Office, its U.C.C. filing was sufficient to give it priority against the hypothetical lien creditor.[136] The Bankruptcy Court decision in *Peregrine* seemed clearly vulnerable on the effect of a displacing national regis-

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130. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 198 (C.D. Cal. 1990).

131. U.C.C. § 9-301(1)(b) (1995). Under section 9-301(1)(b), an unperfected security interest "is subordinate to the rights of . . . a person who becomes a lien creditor before the security interest is perfected." *Id.*

132. 11 U.S.C. § 544(a)(1) (1994).

133. *See In re* National Peregrine, Inc., No. 89-01991-LF, 1989 Bankr. LEXIS 2469, at *9 (Bankr. C.D. Calif. 1989).

134. U.C.C. § 9-302, cmt. 8 (1995). *See* discussion *supra* at notes 83-121.

135. U.C.C. § 9-302(4) (1995).

136. *In re* National Peregrine, Inc., Bankr. LEXIS 2469, at *14 ("Therefore, filing in the Copyright Office is not necessary or effective to perfect a security interest in copyrights, licenses, or the proceeds thereof, against a lien creditor."). *Id.*

try under the partial step-back in section 9-302(3)(a) and (4), and the debtor in possession took an appeal to the District Court.[137] Standing alone, judicial recognition of a "partial step-back" of Article Nine *filing* rules in favor of the Copyright Act's national registration would have provided a sufficient basis on which to overturn the Bankruptcy Court and give the debtor in possession the right to avoid the Bank's security interest in debtor's copyrights. If full effect is given to the exemplary language in Official Comment 8 to section 9-302, Capital's state filing was not effective *under Article Nine* to perfect its security interest in the copyright.[138]

Indeed, in reversing the Bankruptcy Court, the District Court in *Peregrine* did hold that, under Article Nine, a security interest in a copyright could *only* be perfected by filing in the Copyright Office.[139] Instead of recognizing the propriety of Copyright Act recording under state law, however, the District Court decision in *Peregrine* went on to make a much bigger "federal case" out of the proper perfection of a security interest in a copyright. The court passed on the chance to pair the Copyright Office recording, mentioned in the commentary accompanying U.C.C. sections 9-302(3) and (4), with the Article Nine priority scheme.[140] According to the District Court, the partial step-back for filing was not enough preemption. Relying on the complete step-back language in section 9-104(a) and the federal preemption doctrine,[141] the court concluded that all of Article Nine was displaced by the Copyright Act, including its priority rules.[142] According to *Peregrine*, Article Nine did not control perfection or the rights of *any* of the parties, *including the bankruptcy trustee who stands in the shoes of a lien creditor.*[143]

ii. Peregrine: *The Lien Creditor Lurks in the "Later Transfer" Language of Section 205(d) of the Copyright Act*

In order to displace the comprehensive Article Nine priority rules, the court had to find a federal rule that covered the state law priority ground covered by section 9-301(1)(b) of Article Nine. Within the sparse language of section 205(d), the court found language that handled the conflict between the secured creditor and the "lien creditor" who was given hypothetical life under section 544(a) of the Bankruptcy Code.[144] The court's resulting construction of section 205(d) of the Copyright Act is the weakest part of the *Peregrine* opinion.

137. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194 (C.D. Cal. 1990).

138. U.C.C. § 9-302, cmt. 8.

139. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 203.

140. The Bankruptcy Court for the District of Arizona did not pass up the chance in 1997, however. *See In re* Avalon Software, Inc., 209 B.R. 517, 522-23 (Bankr, D. Ariz. 1997); *see also* discussion *infra* notes 196-223.

141. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 199-203. The *Peregrine* court noted that the 1976 Copyright Act created a federal recording system for copyrights and that the purpose of the system was to "promote national uniformity." *Id.* at 199 (quoting Community for Creative Non-Violence v. Reid, 490 U.S. 730, 740 (1989)). In cases involving copyrights and the *proceeds* of copyrights (copyright-based receivables), the federal system is equipped to handle both the consensual security interest and the nonconsensual levy. Any competing recording system would hamper the nationwide effectiveness of the federal scheme, according to the Court. *Id.* at 204-08, 206 n.17.

142. *Id.* at 205.

143. *Id.* at 205-07.

144. *Id.* at 205-06. The lien creditor priority rule under Revised Article Nine is found in Revised section 9-317(a)(2).

Ironically, the *Peregrine* holding that a complete step-back from Article Nine was mandated provided the secured party (Capital) with an argument that would have been unavailable under the Article Nine priority scheme. If the Copyright Act completely occupies the priority field, then the trustee cannot avoid Capital's security interest in the copyright collateral unless the Copyright Act contains a provision protecting the hypothetical lien creditor from prior unrecorded transfers.[145] Again, such a priority rule is clearly set out in Article Nine section 9-301(1)(b), but the complete preemption logic of *Peregrine* makes this straightforward rule unavailable.[146] Given the sparse priority rule contained in section 205(d) of the Copyright Act, finding language that was the functional equivalent of section 9-301(1)(b) seemed like a tall order. With a bit of hypothetical "constructing" of the language in section 205(d), the *Peregrine* court found and applied a federal priority rule that protected a later *lien creditor* against a prior unrecorded transfer of copyright ownership.[147]

The involuntary transfer that marks the lien creditor's rights might very well be a "transfer of copyright ownership" as broadly defined by section 101 and section 201(d)(1) of the Copyright Act.[148] However, the priority rule for "conflicting transfers" in section 205(d) does not seem to envision any involuntary transfers within the description of a protected "later transfer."[149] Under the last sentence of section 205(d), "later transfers" that escape the grace period and are first recorded prevail against prior unrecorded transfers only if "taken in good faith, for valuable consideration."[150] This language would seem to exclude the ordinary judgment creditor whose involuntary lien is never taken in exchange for consideration provided to the debtor and, thus, not "for valuable consideration." The *Peregrine* court avoided this apparent gap in section 205(d) priority by relying on the *hypothetical*, and, in this case, *artificial* nature of the lien creditor's special bankruptcy *persona*.[151] Under section 544(a)(1) of the Bankruptcy Code, the trustee gets the rights of a judicial lien creditor that also "extends credit to the debtor" on the date

145. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 206.

146. U.C.C. § 9-301(1)(b) (1995).

147. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 205-06.

148. 17 U.S.C. §§ 101, 201(d)(1) (1996).

149. *Id.* § 205(d).

150. *Id.* It can be argued that a judgment creditor acquires no rights in a federal copyright still owned by the author. Section 201(e) provides that:

> When an individual author's ownership of a copyright, or of any of the exclusive rights under a copyright, has not previously been transferred voluntarily by that individual author, no action by any governmental body or other official or organization purporting to seize, expropriate, transfer, or exercise rights of ownership with respect to the copyright, or any of the exclusive rights under a copyright, shall be given effect under this title, except as provided under title 11.

17 U.S.C. § 201(e) (1996).

The purpose of this section was to limit the extent of copyright control that the government of the old Soviet Union could exercise over the dissemination of works by Soviet authors which the government did not approve. The language is much broader than the purpose behind it, however. The language of this section can be read to prohibit any involuntary transfer of an author-owned copyright outside of bankruptcy that relies on governmental action. This reading of section 201(e) should be rejected. Although the parties failed to raise the issue in *Peregrine*, the court correctly limited section 201(e) to actions *initiated by and for* governmental bodies. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 205-06 n.16.

151. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 206.

152. 11 U.S.C. § 544(a)(1) (1996).

of the petition.[152] Based on this artificial timing restriction, the court concluded that the section 544(a)(1) lien creditor did in fact "take" for "a valuable consideration" within the meaning of section 205(d) of the Copyright Act.[153]

Peregrine's construction is a cute finesse around the language of section 205(d) of the Copyright Act that seems clearly designed to protect BFP-type voluntary transfers only. The court's construction also runs counter to the policy underlying the hypothetical simultaneous credit extension Congress used to limit the right described in section 544(a)(1) of the Bankruptcy Code.[154] The date of the section 544(a)(1) credit extension was drafted to coincide with the birth of the lien so that the trustee could not conjure up an earlier date on which the hypothetical lien creditor extended credit. Without this timing restriction, the trustee might move the date of credit extension forward in order to take advantage of the occasional state law that gave rights to a creditor who *extended* unsecured credit in the gap between the execution of another creditor's security agreement and the recording or perfection of that interest.[155] This timing language was never intended to permit the trustee to promote the simple lien creditor to the status of a voluntary for-value transferee.[156] Even if the language of section 544(a)(1) can be stretched as *Peregrine* suggests, the trick works only when the *hypothetically created* lien creditor competes with the secured party in bankruptcy; it does not make section 205(d) applicable to real involuntary liens that arise well after the debt is incurred under state judicial lien law. In that very important sense, the priority scheme of section 205(d) is incomplete. It is important to note, however, that, despite this gap, *Peregrine* finds the priority scheme of section 205(d) sufficient to displace the priority rules in Article Nine.[157]

The mischief that results from finding a lien creditor lurking in the later transfer language of section 205(d) goes far beyond security interests in copyright collateral. If federal law does indeed protect the lien creditor as a "later for-value transferee" then all unrecorded transfers of copyright ownership are vulnerable to the trustee after the grace period has expired.[158] In some cases, these unrecorded or late-recorded transfers may also be vulnerable as preferences under section 547 of the Bankruptcy Code.[159]

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153. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 207.

154. Capital argued that the trustee needed the status of a subsequent purchaser to find protection under the priority rule in section 205(d). *Id.* at 206.

155. In *Constance v. Harvey*, 215 F.2d 571 (2d Cir. 1954), the Second Circuit held that the trustee, as hypothetical lien creditor under section 70(c), could hypothecate a credit extension in the gap between the creation and perfection of a chattel mortgage, even though the mortgage had been filed and perfected before the petition date. *Id.* at 575. The Supreme Court overruled *Harvey* in *Lewis v. Manufacturers National Bank*, 364 U.S. 603, 607-10 (1961).

156. 5 COLLIER ON BANKRUPTCY ¶ 544.02, 544-11 to 544-13 (Lawrence P. King, ed., 2000). Old section 70(c) of the Bankruptcy Act did not posit the date of credit extension. A lien creditor could not take on the characteristics of a bona fide purchaser under the Act. New York Terminal Warehouse Co. v. Bullington, 213 F.2d 340, 343-44 (5th Cir. 1954); *see also* Paul Heald, *Resolving Priority Disputes in Intellectual Property Collateral*, 1 J. INTELL. PROP. L. 135, 143-44 (1993) (Copyright Act section 205(d) does not allow the debtor-in-possession to prevail against an unperfected security interest.).

157. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 207.

158. 11 U.S.C. §§ 544(a)(1), 546(b) (1994).

159. *Id.* § 547(b), (e); *See also* WARD, *supra* note §18, 4:52.

iii. Peregrine: *A Security Interest in Copyright Receivables Must Be Recorded in the Copyright Office*

Peregrine holds that a security interest in copyright royalties or other receivables generated by a copyright, must be recorded under section 205 of the Copyright Act in order to be "perfected."[160] With respect to *Peregrine* and the later holding in *Avalon Software*, it should be remembered that old Article Nine section 9-306(1) requires that licensing activity by the debtor result in a "disposition" of copyright property before proceeds are generated.[161] Revised Article Nine expands the concept of proceeds to include the income stream from all the debtor's licensing activity.[162] *Peregrine* assumes that receivables generated by copyright collateral are so integral to the copyright ownership rights transferred for security that they must also fall within the preemptive shadow of the Copyright Act. While royalties are clearly important to copyright owners, they do not arise naturally from the federal statutory basis for copyright ownership. They are, instead, the direct byproduct of private contractual agreements that have traditionally been the domain of state law.[163] Extending the reach of the preemption doctrine in *Peregrine* to cover generated receivables may be more questionable than the use of preemption to displace Article Nine priority rules.[164]

In any case, the underlying rationale for the *Peregrine* position on receivables seems to have been trumped by the Ninth Circuit in *Broadcast Music, Inc. v. Hirsch*.[165] In *Broadcast Music*, the court held that an assignment of the right to receive copyright royalties was not a transfer of copyright ownership under section 205(a) of the Copyright Act, and that such an assignment did not need to be recorded to defeat a subsequent tax lien.[166] The Ninth Circuit refused to expressly extend its holding to transfers for security, and therefore to *Peregrine*.[167] However, the Ninth Circuit's statement that "[a]ssignments of interests in royalties have

160. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 199 (C.D. Cal. 1990). Applying only a partial step-back to Article Nine filing, the decision in *Avalon Software* also mandates Copyright Office recording for copyright based receivables. *In re* Avalon Software, Inc., 209 B.R. 517, 523 (Bankr. D. Ariz. 1997). The underlying rationales in the two cases are not the same, however. *Peregrine* seems to treat receivables as a necessary incident to copyright ownership *under federal law*. *Avalon Software* seems to treat royalties as "proceeds" *under state law* that are unperfected if the copyright collateral is unperfected.

161. U.C.C. § 9-306(1) (1995); *see also In re* Transportation, Design & Tech., Inc., 48 B.R. 635, 641 (Bankr. S.D. Cal. 1985).

162. U.C.C. [Revised] § 9-102(a)(64) cmt. f.

163. Aronson v. Quick Point Pencil Co., 440 U.S. 257, 266 (1979); McCoy v. Mitsuboshi Cutlery, 67 F.3d 917, 922 (Fed. Cir. 1995) (licenses conform to state law); Power Lift, Inc. v. Weatherford Nipple-Up Systems, 871 F.2d 1082, 1085 (Fed. Cir. 1989) (patent license is a contract to be construed under state law); *see also* Robert H. Rotstein, *Paul Heald's "Resolving Priority Disputes in Intellectual Property Collateral": A Comment*, 1 J. INTELL. PROP. L. 167, 182-83 (1993) (Proceeds derived from copyright are not within the scope of section 106 of the Act and are not "work-based" assets for recordation purposes.).

164. *See* Puerto Rico v. Russell & Co., 288 U.S. 476, 483 (1933) ("[Federal law] may not be invoked . . . merely because . . . the property involved was obtained under federal statute."); *see also* A. Haemmerli, *supra* note 42, at 1680-94. (The article soundly refutes the *Peregrine* assumption that federal preemption doctrine mandates that section 205 recording and priority apply to security interests in copyright receivables.).

165. 104 F.3d 1163 (9th Cir. 1997).

166. *Id.* at 1166, 1168.

167. *Id.* at 1166-67.

no relationship to the existence, scope, duration or identification of a copyright, nor to 'rights under a copyright'" seems to undercut the premise behind *Peregrine's* extension of section 205 preemption to copyright-based receivables.[168] The *Peregrine* court saw the security interest in copyright-based receivables not only as a recordable transfer under the Act, but also as a recordable transfer that would be vulnerable in the absence of a recording under section 205(d) (remember *Peregrine* saw a complete preemption).[169] *Peregrine*'s conclusion that receivables that are not recorded under section 205(a) and (c) lose to the lien creditor under section 205(d) is therefore dependent on the premise that such receivables fit within the broad definition of a "transfer of copyright ownership."[170] In *Broadcast Music*, the Ninth Circuit concluded that an ordinary assignment of such receivables does not fit within that definition.[171] Assignments for security would seem to follow the same logic.

iv. Peregrine: *"Perfection" and the Limited Scope of Protection for Security Interests Under Section 205 of the Copyright Act*

In a classic example of understatement, Judge Kozinski noted that "filing with the Copyright Office can be much less convenient than filing under the U.C.C."[172] This reference is to the fact that Copyright Office filing is by registration number of an existing work. Recording a security interest in the specific copyright assets of a debtor with a fluid inventory of these assets (e.g., a film library) will involve "dozens, sometimes hundreds, of individual filings."[173] As the actual inventory changes, either because different works are bought and sold or because the production of a final work must go through many stages, with each stage being a distinct work in its own right, the secured party will be required to make a separate filing for each work added to or deleted from the library. Article Nine, by contrast provides a blanket notice filing on after-acquired property that gives the creditor a continuing, floating lien on the debtor's copyright without the need for periodic updates.[174]

The link between recording and the registration number of an "existing work" is not, however, a "Condition of Recordation" under section 205(a) of the Copyright Act. Subsection (a) provides that "[a]ny transfer of copyright ownership or other document pertaining to a copyright may be recorded."[175] The only condition imposed on recording under subsection (a) is that the document "bears the actual signature of the person who executed it, or . . . is accompanied by a sworn or official certification that it is a true copy of the original, signed document."[176] The link to registration arises out of the language in section 205(c) and (d) governing effectiveness of a recording for purposes of priority against subsequent transferees. Under subsection (d), only a recording "in the manner required to give

168. *Id.* at 1166 (*citing* 17 U.S.C. § 106).
169. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 205-07.
170. 17 U.S.C. § 205(a) (1994).
171. Broadcast Music, Inc. v. Hirsch, 104 F.3d at 1166.
172. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 202 n.10.
173. *Id.* at 203.
174. U.C.C. § 9-204 (1995).
175. 17 U.S.C. § 205(a) (1994).
176. *Id.*

constructive notice under subsection (c)" is good against a "later transfer."[177] In order for a security agreement to provide "constructive notice" under section 205(c), (1) the recorded document must "specifically" identify the copyrighted work so that it can be revealed to a reasonable searcher by title or registration number, and (2) the work must have been registered.[178] Because this definition of "constructive notice" requires some prior specific identification of the work transferred by the recorded document, in addition to registration of the work, an effective Copyright Act recording cannot effectively reach after-acquired property.[179] If, under *Peregrine*, "federal law [the Copyright Act] preempts state *methods of perfecting* security interests in copyrights and related accounts receivable,"[180] then *all* the notice filing *methods of perfection* in Article Nine must yield to the transaction-specific rules of the Copyright Act. The *Peregrine* view of preemption makes the debt financing of "works in process," a movie in production for example, an intolerable legal gamble for the secured party.[181] Unless the secured party requires the debtor to capture the unfinished collateral project in a sequence of titled "works" that can be separately named, registered, and transferred in a series of recordable documents, the recording provision of the Copyright Act provides no "constructive notice" protection.

v. Peregrine: *Uncertainty About the Connection Between Registration and Recording*

The connection between registration and recording may even turn out to be time-sensitive, after the manner of real estate recording. While a specific identification of the work *in the recorded instrument* is necessary to an effective Copyright Act recording of a security interest, it is not clear whether the essential section 205(c) *registration* of the copyright must precede the recording in order for the recording to be effective "constructive notice." The critical language of section 205(c)(2) states that recordation "gives . . . constructive notice . . . but only if . . . (2) registration *has been made* for the work."[182]

How important is the order of things under this language? Registration, at some point, is clearly necessary to "constructive notice." Furthermore, if the phrase "has been made" looks back from the date of recording, then a recorded security agreement would *never* be effective as constructive notice unless *preceded* in time by an effective registration of the work. However, if "has been made" merely

177. *Id.* § 205(d).

178. *Id.* § 205(c)(2).

179. *Id.* § 205(c), (d). Weinberg and Woodward have observed that: "Economically significant financing today tends to be ongoing and fluid, not discrete. In ongoing financing, the transactional approach involves considerably more expense than the notice filing approach because the transactional approach involves multiple trips to the filing office, while notice filing requires only one." Weinberg & Woodward, *Easing Transfer and Security Interest Transactions in Intellectual Property: An Agenda for Reform*, 79 KY. L.J. 61, 85 (1991).

180. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 199 (C.D. Cal. 1990) (emphasis added).

181. *See* Steven Weinberger, *Perfection of Security Interests in Copyrights: The* Peregrine *Effect on the Orion Pictures Plan of Reorganization*, 11 CARDOZO ARTS & ENT. L.J. 959, 975 (1993) (lending banks unable to properly perfect their security interests in the debtor's unreleased films because the films had not been registered within the meaning of section 205(c) of the Copyright Act).

182. 17 U.S.C. § 205(c), (c)(2) (1994) (emphasis added).

looks back from the date when the recording is effective as constructive notice or from the time the constructive notice issue becomes relevant, a recording prior to registration would be effective as long as the work is eventually registered. In such a case, however, the recorded document would only be effective as "constructive notice" under subsection (d) from the time the work was "registered."

The same bankruptcy court that was overruled by the district court in *Peregrine* has subsequently described the controlling federal system for recording copyrights as one "modeled on real property recording acts."[183] Dicta from that court's opinion in *In re AEG Acquisitions Corp.* suggests that the recordation of a copyright mortgage fourteen days before the registration of the underlying copyright might make the recordation invalid because it would be outside the "chain of title."[184] *In re AEG* seems to prefer a literal chronological reading of section 205(c)(2)—a reading that would invalidate any recording not preceded in time by a registration. This chronological reading of section 205(c)(2) may not be compelled by the present language, however.

Even where there is an effective *prior* registration of the work, a recording might be outside the chain of title if one or more of the prior transfers leading to the debtor's title remains unrecorded or was not recorded in the proper order. Nothing in section 205(c) requires such a chronological reading of the constructive notice requirement and, in general, copyright law requires only the recording of *the* transfer that shows the transferee's ownership rights.[185] Unlike real estate law, the Copyright Act does not seem to expose the transferee of a *registered* copyright who records outside the title chain to the risk of losing priority to a purchaser who does not locate the copyright transferee's interest.[186] Nevertheless, a security interest in a copyright may be enough of a derivative right to suggest that transfers necessary to locate ownership in the *immediate debtor* must be recorded before a security interest is effective as constructive notice or is properly perfected.

In 1993, Congress came close to eliminating the requirement of registration as a constructive notice condition under section 205(c).[187] The proposed Copyright Reform Act of 1993 would have provided constructive notice stature to documents that "identify the work . . . so that it would be revealed by a reasonable search under the title *or* registration number."[188] However, the Reform Act did not allow for the effective recording of agreements covering after-acquired property, since the recorded document still had to "identify the work." The Reform Act passed in the House of Representatives in late 1993 but failed to win approval in the Senate.[189]

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183. *In re* AEG Acquisitions Corp. v. Zenith Prod., Ltd., 127 B.R. 34, 41 at n.8 (Bankr. C.D. Cal. 1991), *aff'd*, 161 B.R. 50 (B.A.P. 9th Cir. 1993). Two of the works used as collateral in *AEG* were foreign films. Since the 1988 amendments to the Copyright Act, registration has not been a prerequisite to maintaining an infringement action on a Berne Convention work. 17 U.S.C. § 411(a) (1994). The 1988 Amendments pertain only to infringement suit prerequisites; however, the amendments did not dispense with registration as a condition for constructive notice of a recorded transfer. *In re* AEG Acquisition Corp. v. Zenith Prod., Ltd., 127 B.R. at 42; National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 161 B.R. at 57.

184. *In re* AEG Acquisition Corp. v. Zenith Prod., Ltd., 127 B.R. at 41 n.8. *But see* Swarovski Am., Ltd. v. Silver Deer, Ltd., 537 F. Supp. 1201 (D. Colo. 1982). *Swarovski* involved the state of record title necessary to support an infringement action.

185. *See* 3 NIMMER ON COPYRIGHT, § 12.02, at 12-59 to 12-60 (1993).

186. *See* Swarovski Am., Ltd. V. Silver Deer, Ltd., 537 F. Supp. at 1204.

187. The Copyright Reform Act of 1993, S. 373, 103d Cong., 1st Sess. § 105(b) (1994).

188. *Id.* (emphasis added).

189. 139 CONG. REC. H10308 (Nov. 20, 1993).

As long as identification of the debtor's intellectual property right is critical to an *effective* recording under section 205, a cautious lender should not be comfortable with filing a security interest in the Copyright Office unless the copyright is registered. It would also be prudent for the lender to see that the record contains any other transfer document necessary to establish the immediate debtor's ownership.

A further practical problem relates to the time lag between the "date of recordation" of a security interest filed at the Copyright Office and the date on which the document is available for public viewing. The *date of recordation* is the date when the document in proper form is *received* in the Copyright Office.[190] "Recorded" documents are examined, numbered, scheduled, and cataloged before they are made available for the public record. Prior to January 1994, the Copyright Office recording backlog averaged about eight months from the time the document was received. Implementation of a new voluntary cover sheet[191] has enabled the Copyright Office to reduce this "office delay" to an average of one-and-a-half months.[192] When this "office delay" is added to the 30-day look back period, extending credit on the strength of a copyright becomes a time-consuming process. The secured party will not advance funds until the file is clear of possible assignees or secured parties who could claim a prior execution and recording within the grace period. Because recording dates from *receipt* of the recordable document in the Copyright Office, the file cannot be considered clear until the grace period and the "office delay" period have both passed.

The link between registration and a recording "in a manner required to give constructive notice" has been made the basis for an argument that Article Nine is not preempted with respect to unregistered copyrights.[193] The courts since *Peregrine* are divided on this critical point. The registered-unregistered distinction was rejected by *In re Avalon Software, Inc.*, an opinion from the Bankruptcy Court for the District of Arizona.[194] The distinction was adopted, however, by *In re World Auxiliary Power Company*,[195] a recent decision from the Bankruptcy Court for the Northern District of California. These two decisions will be taken up next. While it is tempting to argue that *Peregrine* should be limited by this distinction or by whatever tool is available, it is the view of this Article that it would be a mistake to exclude unregistered copyrights from the scope of section 205 in order to save security interests that are filed only in the state U.C.C. files.

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190. 37 C.F.R. §§ 201.4(e), 201.25(e), 201.26(f) (2000); *see also* Copyright Office Circular #12, *Recordation of Transfers and Other Documents*. *But see* 3 NIMMER ON COPYRIGHT, § 10.07(A)(1), at n.5; Patch Factory, Inc. v. Broder, 586 F. Supp. 132 (N.D. Ga. 1984).

191. Document Cover Sheet Availability, 58 Fed. Reg. 3297 (Library of Congress, Copyright Office, Jan. 8, 1993).

192. Telephone Interview with Ms. Maria L. Llacuna, Copyright Document Specialist, Copyright Office, Library of Congress, Washington, D.C. (Feb. 3, 2000).

193. *See* Haemmerli, *supra* note 42, at 1667-68 (making the argument that unregistered copyrights should be distinguished from registered copyrights for purposes of defining the preempting scope of section 205 of the Copyright Act). This argument is criticized in this Article and in WARD, *supra* note 18, § 2:81A.

194. *In re* Avalon Software, Inc., 209 B.R. 517. 521 (Bankr. D. Ariz. 1997). This decision is discussed in detail *infra* at notes 196-223.

195. 244 B.R. 149 (Bankr. N.D. Cal. 1999). This decision is discussed in detail *infra* at notes 224-39 and accompanying text.

c. Avalon Software: *Filing-Only Deferral but a Broad Subject Matter Reach*

i. Avalon Software: *The More Limited Preemption Holding*

In a case decided seven years after *Peregrine*, the Arizona Bankruptcy Court, in *In re Avalon Software, Inc.*,[196] concluded that a reconciliation of the Copyright Act and Article Nine did not require complete preemption of Article Nine's priority rules. The *Avalon Software* court found that the partial step-back under U.C.C. sections 9-302(3)(a) and (4) is more compatible with the scope of federal preemption.[197] For the lending bank that failed to make any recording in the Copyright Office, however, the distinction between full and partial step-back was academic. The court held that the bank's security interest in all the debtor's copyrighted and copyrightable software was unperfected on the date of the petition because it had not been recorded in the Copyright Office under section 205(a) of the Copyright Act.[198] Unlike *Peregrine*, however, after finding that the bank's filing of a U.C.C. financing statement left copyright collateral unperfected, the opinion relied on Article Nine section 9-301(1)(b) (not section 205(d) of the Copyright Act) for the proposition that an unperfected security interest is subordinate to the trustee asserting the rights of a hypothetical lien creditor.[199] In addition to recognizing the vitality of U.C.C. priority rules in a case involving copyright collateral, the court also concluded that the Article Nine concept of attachment was not preempted by the Copyright Act.[200]

This more limited approach to preemption has its own problems, however. *Avalon Software* still concludes that section 205(c)'s proviso on constructive notice (specific identification of the work in the recorded document and registration of the work) is part of the displacing *recording* requirements of the Copyright Act.[201] Recall that the elements of constructive notice under section 205(c) are not actually required in order to make a subsection (a) recording.[202] These requirements arise only within the context of the Copyright Act's priority rule in section 205(d).[203] If, contrary to *Peregrine*, the priority rule in subsection (d) does not displace Article Nine priority provisions, it can be argued that constructive notice under subsection (c) should not be required if the security interest is otherwise properly recorded in the Copyright Office under section 205(a). Nevertheless, *Avalon Software* concludes that "[u]ltimate *perfection*" depends upon registration of the software product.[204] The *Avalon Software* opinion sees registration as part of the secured party's U.C.C. section 9-302(4) compliance with the national recordation system that displaces Article Nine filing under section 9-302(3)(a).[205]

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196. 209 B.R. 517 (Bankr. D. Ariz. 1997).

197. *Id.* at 521, 523.

198. *Id.* at 523-24.

199. *Id.* at 521.

200. *Id.* at 522-23.

201. *Id.*

202. 17 U.S.C. § 205(a) (1994); *see also* discussion *supra* at notes 26-33, 144-59.

203. *Id.* It can even be argued that subsection (c)'s constructive notice requirement is not critical to a recording for purposes of the nonexclusive licensee rule in section 205(e).

204. *In re* Avalon Software, Inc., 209 B.R. at 522. Recorded documents that could not be tied to an existing registration would be harder to find in a typical copyright search.

205. *Id.* at 521. U.C.C. § 9-302(3)(a), (4) & cmt. 8 (1995).

This aspect of the partial step-back can be problematic. The relationship between Copyright Act recording with its attendant registration requirement and the controlling Article Nine rules on "attachment" makes it unclear when after-acquired copyright collateral is involved. According to *Avalon Software*, federal copyright law does not alter the secured party's right to acquire an interest in the debtor's after-acquired copyright collateral under an agreement executed before the debtor acquires rights in the collateral.[206] Even if an after-acquired property clause is effective to create an interest in the debtor's later-acquired copyrights, however, perfection requires compliance with sections 205(d) and (c) of the Copyright Act.[207] *Avalon Software* suggests that the secured party could have recorded a security agreement covering after-acquired copyright collateral and then, without the need of a further recorded document, been perfected in such later-acquired property by registering the new works as they came into existence.[208] However, constructive notice under subsection (c) requires more than a recorded document with advance notice of a security interest and a subsequent registration of the work.[209] Subsection (c) requires that the recorded document, or material attached to it, *specifically identify the work to which it pertains*.[210] A document in the form of a security agreement covering after-acquired property could not satisfy the "specific identification" requirement as to copyright collateral subsequently acquired by the debtor. A subsequent registration of the new collateral does not cure the problem with the prior recorded security agreement.[211] Despite this confusing dicta in *Avalon Software*, a secured party who wants perfection in after-acquired property would be well-advised to get the debtor to sign a new agreement that specifically identifies the new work, register the new work, and record the new agreement. While *Avalon Software*'s partial step-back approach may cause less preemption mischief than *Peregrine*, clearly one of the rough spots is the meshing of the facile Article Nine law on subsequent attachment with single transaction document recording.

ii. Avalon Software: *Rejecting the Distinction Between Registered and Unregistered Copyrights*

The secured party in *Avalon Software* argued that while federal law preempted Article Nine filing in the case of registered copyright collateral, a security interest in unregistered copyrights was properly perfected under the state law in Article Nine. The *Avalon Software* court rejected what it called a "novel proposition."[212] As the court observed, acceptance of the argument would allow for state recording and priority rules on all manner of copyright transfers, not just security interests, thus upsetting the congressional scheme for a central registry.[213] Given the broad

206. *In re* Avalon Software, Inc., 209 B.R. at 522-23.

207. *Id.* at 523.

208. *Id.* ("If Imperial Bank had merely done what the law requires—that is, to record evidence of its security interest in the U.S. Office of Copyright—and had it made sure that the after-acquired property had been registered, it would have been found to be perfected.").

209. 17 U.S.C. § 205(c) (1994).

210. *Id.*

211. *See* 17 U.S.C. § 205(c) (1994).

212. *In re* Avalon Software, Inc., 209 B.R. at 523.

213. *Id.* at 523.

preemptive recording language in section 205(a),[214] the constructive notice standard in subsection (c) seems less like a line between state and federal law and more like a part of the *recording requirements* for all copyrights.[215] The latest bankruptcy decision to speak on the subject, *In re World Auxiliary Power Co.*,[216] finds the distinction between registered and unregistered copyrights convincing. That case is taken up below.[217]

iii. Avalon Software: *Adopting a Broad Definition of Collateral That Is Subject to Copyright Act Recording*

The most troublesome aspect of the decision in *Avalon Software* is the limitless subject matter scope that the court finds applicable to a section 205 recordation of a security interest. While the court seems to be on solid ground when it rejects the argument that unregistered copyrights are not within the scope of section 205,[218] the opinion goes too far in its holding that all *copyrightable* collateral must be recorded under the Copyright Act.[219] The subject matter reach of the filing preemption, according to *Avalon Software*, includes all aspects of a work that are copyrightable, even if these aspects are protected under another intellectual property regime.[220] An improvement in a software program or a new program may qualify for trade secret protection quite apart from its expressed form. A security interest in such a state-law based trade secret should be covered by Article Nine. This long subject matter reach seems to go further than the Copyright Act itself goes.[221] State trade secret law has a legitimate field of operation outside the Copyright and Patent Acts.[222] Under the current state of the law, software that has its principal intrinsic value as a patent, trademark, or trade secret should be perfected against the lien creditor (and bankruptcy trustee) by a U.C.C. filing,[223] even if the software is also copyright protected.

d. World Auxiliary Power*: Copyright Act Does Not Preempt When the Copyright Is Unregistered*

In December of 1999, the Bankruptcy Court for the Northern District of California, faced another perfection of copyright collateral issue under section 544(a) of the Bankruptcy Code. In *In re World Auxiliary Power Co.*,[224] the debtor's

214. 17 U.S.C. § 205(a) (1994) ("Any transfer of copyright ownership or other document pertaining to a copyright may be recorded in the Copyright Office.").

215. *See id.* § 205(c).

216. 244 B.R. 149 (Bankr. N.D. Cal. 1999). This decision is discussed in detail *infra* at notes 224-39.

217. *See infra* text accompanying notes 224-39.

218. *See infra* text accompanying notes 224-39.

219. *In re* Avalon Software, Inc., 209 B.R. at 523.

220. *Id.* at 523-24.

221. *See* 17 U.S.C. § 301(b)(3) (1994) (Copyright Act does not preempt state law with respect to: "[A]ctivities violating legal or equitable rights that are not equivalent to any of the exclusive rights within the general scope of copyright as specified by section 106.").

222. Kewanee Oil Co. v. Bicron Corp., 416 U.S. 470, 480 (1974).

223. Trade secret software fits the definition of a "general intangible" under section 9-106. U.C.C. § 9-106; *see also* WARD, *supra* note 18, § 1:11 (examining the extent to which a trade secret constitutes "property" apart from contract rights either express or implied that protect against nondisclosure).

224. 244 B.R. 149 (Bankr. N.D. Cal. 1999).

collateral was its copyrights in drawings, blueprints, and related software; and it was clear from the record that none of the copyright collateral was registered on the day that the bankruptcy petition was filed.[225] As was the case in *Peregrine* and *Avalon Software*, the secured party made only an Article Nine filing—nothing was recorded under section 205 of the Copyright Act.[226] Unlike *Peregrine* and *Avalon Software*, however, the *World Auxiliary Power* court held for the secured party on the theory that Article Nine is not preempted (to any extent) when the copyright collateral is unregistered.[227] The court in *World Auxiliary Power* found that the *priority rule* in 205(d) has no application to unregistered copyrights because registration is one of the conditions necessary for "constructive notice" and constructive notice is a condition of recording priority.[228] For good measure, the court also concluded that Copyright Act *recording* does not preempt Article Nine *filing* when the copyrights are not registered.[229]

The theory of *World Auxiliary Power* is that registration defines the reach of Copyright Act recording and priority. While *Peregrine* goes too far, and cutting unregistered copyrights out of its preemption holding seems like an appealing way to limit the decision, the distinction suggested by *World Auxiliary Power* does not pass careful logical scrutiny. If indeed section 205(d) provides recording and priority only for registered copyrights, individual states could provide their own priority rules or even their own alternative recording acts aimed at ordering disputes in all copyright transfers (whether or not for security) as long as the copyrights remained unregistered. This seems clearly contrary to the inclusive language in section 205(a) of the Copyright Act setting out the range of transactions that are recordable. A fair reading of section 205 as a whole suggests that registration is merely a condition for giving constructive notice of any transfer of copyright ownership, whether or not it is registered at the outset. Congress must have intended section 205 to serve as the recording rule for all copyrights—both registered and unregistered.[230]

World Auxiliary Power supports the distinction on the premise that the *Peregrine* holding could not, as a technical matter, be extended to unregistered copyrights. The court opined that, unless the copyrights in *Peregrine* had been registered, the hypothetical lien creditor (trustee under section 544(a)(1)) could not have claimed priority as a "later transfer" that must give "constructive notice" through section 205(d) of the Copyright Act.[231]

However, this argument does not credit either the range of ownership transferees who can register a copyright or the make-believe nature of the lien creditor as

225. *Id.* at 150.

226. *Id.*

227. *Id.* at 153.

228. *Id.* at 152-53.

229. *Id.* at 154-56.

230. Note that section 205(a) provides that "[a]ny transfer of copyright ownership or other document pertaining to a copyright may be recorded in the Copyright Office." 17 U.S.C. § 205(a) (1994). The scope language *does not* limit the scope of Copyright Act recording to registered copyrights.

231. *In re* World Auxiliary Power Co., 244 B.R. at 152. Unlike the Patent Act and the Lanham Trademark Act, a subsequent party does not prevail as a BFP under the Copyright Act unless it wins the race to the section 205 record and records in that record "in such manner [required to give constructive notice]." 17 U.S.C. § 205(d) (1994).

envisioned by *Peregrine*. In deciding that the lien creditor was a protected later transfer under section 205(d), the *Peregrine* court assumed the fact that a recording by the trustee had occurred.[232] Of course the bankruptcy trustee did not actually record anything. The recording was "hypothetical"—merely part of the assumed (some might say conjured) nature of the lien creditor constructed by section 544(a)(1) of the Bankruptcy Code. If registration is indeed a condition for effective recording of all copyrights, and not a limit on the reach of Copyright Act recording itself, the act of registering the copyright might also be assumed as part of the trustee's fictitious section 544(a)(1) personality. As noted above, *Peregrine* seems to go too far when it includes the involuntary lien creditor in the class of protected "later transfers."[233] If, however, *Peregrine* is right on this score and the lien creditor finds shelter in section 205(d), then an involuntary lien creditor would also seem to be vested with sufficient ownership or exclusive rights to allow it to register the work acquired under section 408(a) of the Copyright Act.[234] If a real lien creditor/transferee could register an unregistered copyright in order to give constructive notice of its recordable interest under sections 205(a) and (c), then the hypothetical lien creditor under section 544(a)(1) of the Bankruptcy Code would clearly be able to assume as much as of the petition date.[235]

Finally, even if *World Auxiliary Power*'s questionable holding that Copyright Act *priority* under *Peregrine* is only extended to registered copyrights is accepted, the separate conclusion that Article Nine filing is not displaced by a Copyright Act recording when the copyright is unregistered requires some very heavy lifting. On this second point, the court merely refuses to be guided by the reference to the Copyright Act as a displacing registry under old U.C.C. sections 9-302(3)(a) and (4).[236] It may be that intelligent speculation suggests that the drafters of old section 9-302 were not as familiar with the scope and mechanics of Copyright Act recording as they might have been. Nevertheless, the drafters clearly identified the 1909 Copyright Act as an example of a displacing registry and the 1976 amendments to the Copyright Act expanded the scope of this federal recording even further.[237] It is hard to argue with a partial preemption of Article Nine filing where the authors of the conflicting state law conclude that a state filing on copyright collateral would be ineffective because the proper recording locale is in Washington.

The language of Revised Article Nine would provide more support for *World Auxiliary Power*'s conclusion that state law does not voluntarily yield its filing rules to the copyright registry. Under the Revision language, eligibility for a filing deferral requires that the displacing federal statute have "requirements for a security interest's obtaining priority over the rights of a lien creditor."[238] However, if we accept the Copyright Act teaching of *Peregrine* (as *World Auxiliary Power* purported to do), even this new U.C.C. language invites a deferral on filing. Re-

232. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 207 (C.D. Cal. 1990).

233. *See supra* text accompanying notes 144-59.

234. 17 U.S.C. § 408(a) (1994) ("[T]he owner of copyright or of any exclusive right in the work may obtain registration.").

235. 11 U.S.C. § 544(a)(1) (1998).

236. *See In re* World Auxiliary Power Co., 244 B.R. at 154-56.

237. 17 U.S.C. § 205 (1994).

238. U.C.C. [Revised] § 9-311(a)(1).

member that *Peregrine* concluded that section 205(d) of the Copyright Act does contain a priority rule that embraces the lien creditor.[239]

Peregrine justly deserves most of the criticism it gets. However, the limit on preemption suggested by *World Auxiliary Power* is a conceptual reach, and, even if it can be justified as a matter of federal preemption, it protects state law filing only until someone registers the copyright (the debtor or any transferee or exclusive licensee). The distinction is not a very reliable safe harbor for the secured party contemplating a credit extension secured by copyright collateral.

3. *Current Approaches to Reconciliation When Patent Collateral Is Involved*

a. *Partial Preemption of Article Nine Priority Rules*

The patent case suggests a partial theory of preemption that is neither complete nor limited to complete filing displacement. Instead, the provisions of the Patent Act on recording have suggested to the courts a logical compromise on preemption. In dicta, these courts have described a partial preemption of both the filing and priority provisions of Article Nine when the security interest in a patent is in competition with a subsequent patent assignee.[240]

As noted in Part II.A.2, the title orientation of section 261 and the operating regulations suggest that an Article Nine security interest in a patent is not an "assignment, grant or conveyance" and therefore need not be recorded in the patent tract file in order to escape avoidance by a later "purchaser" or "mortgagee."[241] In keeping with that conclusion the case law has made "perfection" of a security interest in a patent a matter of state law filing under Article Nine and has related that perfection to the Article Nine priority rules. However, this conclusion is subject to two important qualifications. First, to date, the cases upholding the Article Nine perfection scheme have all involved the priority conflict between the secured party and the lien creditor.[242] What happens when the secured party comes up against a subsequent assignee from the secured party's debtor? If the secured party is not an "assignment, grant or conveyance" under section 261 of the Patent Act, then the Article Nine priority scheme should hold and old section 9-301(1)(d) (revised section 9-317(d)) would clearly award priority to the prior perfected secured party.[243] However, most of the commentators and all but one of the decided

239. *See* National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 205-07 (C.D. Cal. 1990).

240. *See supra* note 39.

241. *See supra* text accompanying notes 34 to 68; *see also* WARD, *supra* note 18, § 2:90.

242. *See In re* Cybernetic Services, Inc., 239 B.R. 917, 920 n.8 (9th Cir. B.A.P. 1999), *aff'd*, 2001 U.S. App. LEXIS 11750 (9th Cir. June 6, 2001); City Bank & Trust Co. v. Otto Fabric, Inc., 83 B.R. 780, 782 (D. Kan. 1988) (relying on *In re* Transportation Design & Tech., Inc., 48 B.R. 635, 639 (Bankr. S.D. Cal. 1985)); *cf.* National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 216 n.17 (C.D. Cal. 1990) (concluding in *dicta* that the Patent Act provides a system of "national registration" that is a complete substitute for Article Nine filing under U.C.C. § 9-302(3)(a) and (4)).

243. Priority would be based on U.C.C. sections 9-201 and 9-301(1)(d). *See* Holt v. U.S., 13 U.C.C. Rep. Serv. 336, 338-39 (D.C. Cir. 1973). *Holt* holds that Section 261 of the Patent Act would not trump the U.C.C. determined priority because the Article Nine security interest would not be considered "an assignment, grant or conveyance" under the federal priority rule set out in that section. *Id.*; *see also In re* Cybernetic Services, Inc., 239 B.R. 917, 920-21 (B.A.P. 9th Cir. 1999), *aff'd*, 2001 U.S. App. LEXIS 11750 (9th Cir. June 6, 2001) (section 261 of the Patent Act

cases involving patent collateral suggest that the Article Nine priority rule for transferees (buyers and licensees under the Revisions) gives way to the recording and priority rule in section 261 of the Patent Act.[244] This questionable conclusion is contained in dicta drawn from the patent cases on "perfection" that have been decided under section 544(a) of the Bankruptcy Code. The conclusion seems to be grounded more in the history of patent mortgages and the court's sense of continuity within the Patent Office than in the logic or the language of section 261. As mentioned at the outset of this Article, the title history of patent mortgages resonates from the Supreme Court's 1890 decision in *Waterman v. Mackenzie*.[245]

b. The Case Law Under Section 261

i. Waterman v. Mackenzie

In *Waterman v. Mackenzie*, the inventor/licensee of a fountain pen holder (Waterman) brought suit to enjoin an alleged infringement.[246] The Supreme Court affirmed the lower court's decision that the equitable action failed because title to the patent resided not in the plaintiff Waterman, but in a conditional assignee.[247] The diverting conditional assignment was intended as security for a note signed by Waterman and his wife. Prior to the conditional assignment, Waterman (then the owner of the patent) transferred the patent title to his wife reserving back an exclusive license.[248] The conditional assignment, executed by Mrs. Waterman to secure the note, was then made subject to patentee's license.[249] The Court affirmed the dismissal of Waterman's bill because a licensee without title cannot sue for infringement.[250] The Court rejected Waterman's argument that the conditional collateral assignment did not pass title to the conditional assignee.[251]

Did the Supreme Court's conclusion in *Waterman v. Mackenzie* that the conditional assignee had "title," confirmed by a proper recording, also support a holding

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does not bring the "security interest" within its title-oriented recording provisions). While *Cybernetic Services* and other recent cases hold that the security interest is outside the scope of Patent Act recording, some of these decisions have also come to the somewhat inconsistent conclusion that security interests must be recorded in the PTO in order to be protected against subsequent assignees.

244. *See* City Bank and Trust Co. v. Otto Fabric, Inc, 83 B.R. 780, 782 (D. Kan. 1988) (relying on *In re* Transportation Design and Tech., Inc., 48 B.R. 635, 639 (Bankr. S.D. Cal. 1985)); *cf.* National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 203-04, 206 n.17 (C.D. Cal. 1990) (concluding in dicta that the Patent Act provides a system of "national registration" that is a complete substitute for Article Nine filing under U.C.C. § 9-302(3)(a), (4)). For a sample of the scholarly comment see A. Haemmerli, *supra* note 42, at 1700-04; Weinberg & Woodman, *supra* note 179, at n.92; Bramson, *supra* note 22, at 1585-88.

245. 138 U.S. 252 (1890); *see also supra* note 2.

246. Waterman v. MacKenzie, 138 U.S. 252, 252 (1890).

247. *Id.* at 261. After the decision in the Supreme Court the licensee/inventor joined the title holding conditional assignee as a defendant and successfully asserted his right to sue for infringement. The second time was a charm because an infringement suit can be brought by a nontitle-holding licensee if the title holder is an infringer who cannot sue himself. Waterman v. Shipman, 55 F.2d 982 (2d Cir. 1893).

248. Waterman v. Mackenzie, 138 U.S. at 252.

249. *Id.* at 253.

250. *Id.* at 261.

251. *Id.* at 257.

that all unrecorded transfers for security are "void" as to subsequent parties under section 261 because they must be conceived as "title" transfers as a matter of federal law?[252] *Waterman v. Mackenzie* can be read as holding much less. Instead of positing a federal title theory for security transfers, the case seems to conclude that the particular conditional assignment at issue fell within the provisions of the Patent Act because *it was, in fact, cast* into a title mold under the then-extant state law and state equity practice.[253] In a particularly telling sentence from the opinion, the Supreme Court concludes that the conditional assignee "must be held entitled" to the incidents of title, "*unless otherwise provided in the mortgage*."[254] The clear suggestion is that *this* transfer for security (the one before the Court in *Waterman*) presumes title under the then-existing state law, but another such transfer might effectively reserve most, if not all, of the rights of ownership in the transferor. Title passed to the conditional assignee in *Waterman v. Mackenzie* because of the then-extant state law conceptualizations about the need to transfer title in a chattel mortgage, not because of any necessary logic derived from the federal Patent Act. When *Waterman v. Mackenzie* was decided, the only security devise recognized for this type of personalty was a form of the chattel mortgage. Legal title was the state law "concept" (some might say "fiction") used to define the right of the mortgagee to prevent waste of the asset. Unless this concept of legal title, as then recognized under state law, was somehow converted by the Supreme Court into an exclusive federal common law devise for protecting the mortgagee, the holder of an Article Nine security interest that carries no title should not be compelled to record under section 261 of the Patent Act. If a security interest is not "[a]n assignment, grant or conveyance" within the meaning of section 261, the secured party properly attached and perfected by filing under state law would prevail over a subsequent assignee of the patent even if the security interest was never recorded in the Patent Office.[255] While this more limited reading of *Waterman v. Mackenzie* has obvious analytical appeal, its application to modern Patent Act practice might be seen as a threat to the integrity of the PTO assignment records. Probably for that reason, this restricted view of *Waterman v. Mackenzie* has not been clearly

252. The cases to date have not read *Waterman* to mean that the concept of a title-based chattel mortgage preempts the Article Nine conception of a security interest as a matter of federal law. *See In re* Cybernetic Services, Inc., 239 B.R. 917, 920-21 (B.A.P. 9th Cir. 1999), *aff'd*, 2001 U.S. App. LEXIS 11750 (9th Cir. June 6, 2001); Citibank & Trust Co. v. Otto Fabric, Inc., 83 B.R. 780, 782 (D. Kan. 1988); *In re* Transportation, Design & Tech., Inc., 48 B.R. 635, 639 (Bankr. S.D. Cal. 1985). These cases are taken up *ad seriatim* in the next four Subsections.

253. *See* Waterman v. Mackenzie, 138 U.S. at 258-59; *see also In re* Cybernetic Services, Inc., 2001 U.S. App. LEXIS 11750, at **22-26 (9th Cir. June 6, 2001).

254. Waterman v. Mackenzie, 138 U.S. at 260; *see also* Curtiss v. U.S., 13 U.S.P.Q. 400, 411 (Ct. Cl. 1932).

255. *See* Holt v. United States, 13 U.C.C. Rep. Serv. 336, 338-39 (D.C. Cir. 1973). Priority would be based on U.C.C. sections 9-201 and 9-301(1)(d). Section 261 of the Patent Act would not trump the U.C.C. priority because the security interest would not be considered "an assignment, grant or conveyance" under the federal priority rule. *See also In re* Cybernetic Services, Inc., 239 B.R. at 920-21. The Bankruptcy Appellate Panel in *Cybernetic Services* concluded that section 261 deals only with transfer of title transactions and that a security interest is not title dependent. *Id.* However, the Panel also opined that an assignee of a patent would take free of a security interest that was not filed in the Patent Office. *Id.* at 920 n.8. This dicta from the B.A.P. did not survive the Ninth Circuit's affirmance, however. *In re* Cybernetic Services, Inc., 2001 U.S. App. LEXIS 11750 (9th Cir. June 6, 2001) (a security interest is a mere license).

affirmed in the case law. Four modern cases on the preemptive effect of the Patent Act, including the Ninth Circuit's recent decision in *Cybernetic Services*, are taken up next.

ii. Transportation Design: *Article Nine Governs "Perfection" of a Security Interest in Patent Collateral Under Section 544(a)(1) of the Bankruptcy Code—but What About the Assignee of the Patent?*

In re Transportation Design & Technology, Inc.[256] holds that an Article Nine local filing is effective to perfect a security interest in patent collateral against the bankruptcy trustee asserting lien creditor status under section 544(a)(1) of the Bankruptcy Code.[257] As part of this holding, the court observed that "the grant of a security interest is not a *conveyance* of a present ownership right in the patent and, . . . is not required to be recorded in the Patent Office."[258] However, after it seems to have buried *Waterman v. Mackenzie*, *dicta* in the opinion revives it long enough to make the case for a "partial" priority preemption. *Transportation Design* relies on *Waterman v. Mackenzie* for the following conclusion:

> [A] bona fide purchaser holding a duly recorded conveyance of the ownership rights in a patent or a mortgagee who has recorded its interest as a transfer of title with the Patent Office will defeat the interests of a secured creditor of the grantor or mortgagor who has not filed notice of its security interest in the Patent Office.[259]

Apparently, the court found in *Waterman v. Mackenzie* the basis for a narrow preemption of both the *filing and priority rules* in Article Nine whenever the rights of an assignee or titled mortgagee that has recorded are in conflict with the ordinary security interest.[260]

Under section 261, if a prior assignee (or conditional assignee) fails to record within three months, it must record before the *execution* of a subsequent purchase or mortgage in order to prevail over such subsequent interest.[261] The passage from *Transportation Design* quoted above notwithstanding, as long as the subsequent purchase or mortgage is *bona fide* it need never record in order to assert priority over the prior unrecorded assignment. If the secured party is assumed to be prior in time under the *dicta* in *Transportation Design*, then it must record its interest in the Patent Office.[262] However, unless the security interest is recorded as a title document, it will not fall within the constructive notice mandate of section 261.[263] Therefore, it is necessary to create a security interest by assignment

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256. 48 B.R. 635 (Bankr. S.D. Cal. 1985).

257. *Id.* at 641; *see also* 11 U.S.C. § 544(a)(1) (1994).

258. *In re* Transportation, Design & Tech., Inc., 48 B.R. at 638.

259. *Id.* at 639.

260. As already noted, there is a strong argument that neither 35 U.S.C. § 261 nor *Waterman v. Mackenzie*, 138 U.S. 252 (1890), support the "partial preemption" priority rule the court proposes.

261. 35 U.S.C. § 261 (1994).

262. *See In re* Transportation, Design & Tech., Inc., 48 B.R. 639-40.

263. If the secured party took and recorded a security agreement instead of a title-bearing conditional assignment, it would not get the absolute record protection afforded a recorded conditional assignment. In the parlance of the Patent Act, a "security agreement" would convey a "lesser" equitable right to the secured party that would not qualify as an "assignment, grant or conveyance" subject to section 261. *In re* Cybernetic Services, Inc., 239 B.R. at 920-21 (B.A.P. 9th Cir. 1999), *aff'd*, 2001 U.S. App. LEXIS 11750 (9th Cir. June 6, 2001); *In re* Transportation,

to assure priority vis-à-vis a subsequent assignee. *Waterman v. Mackenzie* is not dead![264] The alternative of filing an ordinary security agreement (a possible construction of the *Transportation Design* dicta) with the PTO as a discretionary document may provide "inquiry notice" to those who access the file, but it will not be statutory constructive notice to all. Despite the confusing *dicta* in *Transportation Design*, the Patent Act seems to require a title document for constructive notice purposes and, while the *bona fides* of the subsequent party is relevant under section 261, recording by the subsequent party is not.[265]

Transportation Design fashions an approach to partial preemption that departs from the partial and full step-back concepts that are part of the storyline in Article Nine.[266] Under the two-stage deferral approach suggested by Article Nine, the first question would be whether recording in the Patent Office was a complete and exclusive substitute for Article Nine filing under sections 9-302(3)(a) and (4). If the Patent Act "provides for a national registration" within the meaning of section 9-302(3)(a), then Article Nine filing is neither "necessary *[n]or effective*."[267] "Compliance" with the federal statute then becomes the exclusive method of "perfection" under section 9-302(4).[268] Section 9-302 makes no provision for the *partial displacement* of the Article Nine filing provisions. If the filing rules are displaced as a mode of perfection because of the operation of section 9-302, they are displaced in *all* cases where perfection is important to priority.[269] However, because *Transportation Design* ignored the section 9-302(3)(a) approach, the preliminary issue of "national registration" for security interests under the Patent Act is never *directly* addressed. Instead, the court decides half of the section 9-302(3)(a) issue *indirectly* by concluding that state "perfection" works—at least against the lien creditor under U.C.C. section 9-301(1)(b).

While preemption, even partial preemption, is federal law and operates apart

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Design & Tech., Inc., 48 B.R. at 639. However, the "without notice" condition for bona fide purchaser status in section 261 of the U.S. Code protects even equitable interests when the subsequent purchaser is chargeable with "inquiry notice" of the equitable right. Hendrie v. Sayles, 98 U.S. 546, 549 (1879); FilmTec Corp. v. Allied-Signal, Inc., 939 F.2d 1568, 1573 (Fed. Cir. 1991). Those who searched the patent record after the discretionary recording of a security agreement should take subject to the security interest created thereby. Because some actual knowledge may be necessary to trigger inquiry notice, those foolish subsequent purchasers who buy without resort to the record, as well as subsequent involuntary takers such as lien creditors who never rely on the record, may not be subject to the prior "security agreement" recorded only with the PTO.

264.

> [W]here a federal statute, such as the Patent Act, governs one area or interest which the secured creditor wishes to protect (e.g., ownership), then the federal statute preempts any other method of protecting that interest and is conclusive on the manner of protecting that interest. In other words, if the secured creditor wishes to protect itself against the debtor transferring title to the patent to a bona fide purchaser or mortgagee who properly records, then the secured creditor must bring its security interest (which is not ordinarily a transfer of title) within the provisions of the Patent Act governing transfer of title to patents.

In re Transportation, Design & Tech., Inc., 48 B.R. at 639-40.

265. *Id.*

266. U.C.C. §§ 9-104(a), 9-302(3)(a) (1995); *accord* U.C.C. [Revised] §§ 9-109(c)(1), 9-311(a)(1) & (b).

267. U.C.C. § 9-302(3) (1995) (first sentence) (emphasis added).

268. U.C.C. § 9-302(4) (1995).

269. *Id.*

from Article Nine notions, the jerry-built "partial filing and priority preemption" theory in the *Transportation Design* dicta is troublesome. It may not be a reliable guide to the scope and function of the priority rule in section 261 of the Patent Act.

iii. Chesapeake Fiber: *Infers that Section 261 Does Regulate Priority in a Patent Between a Prior Secured Party and a Subsequent "Purchaser"*

Even though the dicta in *Transportation Design* is flawed, it has had some influence. Relying on *Transportation Design*, the court in *Chesapeake Fiber Packaging Corp. v. Sebro Packaging Corp.*[270] applied section 261 to resolve a challenge by the original assignor of a patent application to the security interest held by the bankrupt assignee's secured party. The assignor argued that the secured party was unperfected without a PTO recording and thus subordinate to the assignor whose subsequent "reacquisition" made it a purchaser, protected under section 261.[271] The court in *Chesapeake Fiber* found for the secured party only because the original patent assignor could not qualify as a subsequent section 261 "purchaser," not because section 261 did not apply.[272]

iv. Otto Fabric: *Article Nine "Perfection" Dates a Transfer of Patent Collateral for Purposes of Bankruptcy Preference Law*

Three years after the decision in *Transportation Design*, the United States District Court for the District of Kansas held that a security interest in a patent was "perfected" against an imaginary lien creditor from the time it was properly filed under Article Nine, rather than from the time it was recorded with the Patent Office. The holding in *City Bank and Trust Co. v. Otto Fabric, Inc.*[273] is also accompanied by dicta that sends a mixed message about the scope of federal preemption.

Unlike the way the issue came up in *Transportation Design*, the moment of "perfection" was important in *Otto Fabric* because under section 547(e)(2) of the Bankruptcy Code "perfection" marked the "deemed" date of the security transfer for purposes of the 90-day period for avoiding preferences.[274] Except for the issue of *when* it was "deemed" to have occurred, the transfer for security in *Otto Fabric* satisfied all the other requirements for a preference that was avoidable by the bankruptcy trustee under section 547(b) of the Bankruptcy Code.[275] If the

270. 143 B.R. 360 (D. Md. 1992), *aff'd*, 8 F.3d 817 (4th Cir. 1993).

271. *Id.* at 368. Arguably the original patentee/assignor might have retained a security interest in the assigned patent that would have been good against the assignees' existing secured lender. However, it is not clear that such an interest would have qualified for purchase money priority under old Article Nine. U.C.C. §§ 9-107, 9-312(4) (1995). A purchase money interest in a pending patent application is not possible under the more restrictive language in Revised Article Nine. U.C.C. [Revised] §§ 9-103(a)(1), (b)(3); *see also* WARD, *supra* note 18, §§ 2:49, 2:49A.

272. Chesapeake Fiber Packaging Corp. v. Sebro Packaging Corp., 143 B.R. at 369. Arguably, the assignor could have protected its rights in the assigned patent with a security interest that might have qualified for purchase-money priority. See the prior discussion of this aspect of the *Sebro* case *supra* at note 269. *See, e.g.*, Haraway v. Burnett, 1997 Tenn. App. LEXIS 611 at *2-3, 33 U.C.C.2d 1256 (1997) (Assignor of patents retains security interest in them to secure assignee's obligation to make sales contract and royalty payments).

273. 83 B.R. 780 (D. Kan. 1988).

274. 11 U.S.C. § 547(e)(2)(B) & (e)(1)(B) (1994).

275. City Bank and Trust Co. v. Otto Fabric, Inc., 83 B.R. at 782.

transfer date was marked by the local U.C.C. filing, it would *not* be avoidable because it would fall *outside* the 90-day pre-petition "preference period" in section 547(b)(4)(A).[276] If perfection was marked by the later federal PTO recording, however, the security transfer would be avoidable because it would fall *within* the 90-day preference period.

The *Otto Fabrics* court held that state law and the secured party's Article Nine filing apply conclusively, *but not exclusively*, to resolve the question of "perfection" in favor of the secured party. Alternatively, the court held that if the Patent Act did preempt "the field of filing," section 261 offers no protection for lien creditors or trustees invested with lien creditor status.[277]

As was the case in *Transportation Design*, the *Otto Fabrics* court ignored the Article Nine structure that conceives of a partial deferral as a "filing" deferral under U.C.C. sections 9-302(3)(a) and (4). While federal preemption need not follow the guidelines suggested in the preempted state statute, the *Otto Fabrics* approach seems tied to three inconsistent conclusions.

The first flawed conclusion in *Otto Fabric* is that a PTO recording would work as well as an Article Nine filing to defeat the hypothetical lien creditor under state law.[278] The second flawed conclusion is that if section 261 of the Patent Act "completely preempted the field of filing," its substantive provisions would leave the lien creditor, who could have priority under Article Nine, with no federal law basis for priority against the secured party.[279] Finally, testing the complete opposite thesis, the court observes that a security interest is not really a conveyance of title or ownership rights under the recording mandate of section 261 anyway.[280]

As to the court's first observation on the applicable state law, the filing deferral rules in U.C.C. sections 9-302(3)(a) and (4) *do not* comprehend double recording. If the Patent Act recording displaces under section 9-302(3)(a), it displaces completely under section 9-302(4). On the other hand, if the Patent Act did not create a national registry that supplants Article Nine for "perfection" purposes, filing with the PTO would not protect against the lien creditor, at least under state law.[281] On the federal side, no reasonable take on the language of section 261 would allow the secured party to "perfect" its interest against the involuntary lien creditor by recording in the Patent Office.[282] Involuntary transfers are not even mentioned in the text of section 261.[283] If a section 261 recording did provide priority against the involuntary lien creditor under federal law, state law covering the same ground would surely be preempted and a U.C.C. filing would not even be an alternative way to gain priority over the lien creditor.

This observation about the narrow field of play in section 261 leads to the

276. 11 U.S.C. § 547(b)(4)(A) (1994).

277. City Bank and Trust Co. v. Otto Fabric, Inc., 83 B.R. at 782.

278. After upholding U.C.C. based perfection against the lien creditor, the court volunteered the statement that "*recording an assignment* [in the PTO would also] protect the assignee against the claims of a subsequent lien creditor." *Id.* (emphasis added).

279. *Id.*

280. *Id.* at 782-83.

281. "Perfection" here means the time when the transfer beats the lien creditor under section 547(e) of the Bankruptcy Code. 11 U.S.C. § 547(e)(1)(B) (1994); *see also* U.C.C. § 9-301(1)(b) (1995); U.C.C. [Revised] § 9-317(a)(2).

282. *See* 35 U.S.C. § 261 (1994).

283. *Id.*

court's second flawed conclusion. If federal law did in fact control, the court notes, it would leave the lien creditor without any statutory priority.[284] Any hypothesis based on complete preemption by section 261 seems an unlikely alternative holding, however. Assuming the court's reference to complete preemption of the "field of filing" really envisions complete preemption of Article Nine, then it may be true that section 261, as it stands, does not require recording to beat the lien creditor. But, as the court in *Peregrine* felt compelled to conclude,[285] complete federal preemption of Article Nine can hardly be mandated unless the displacing federal recording scheme comprehends lien creditors.[286]

At the other extreme, the title-related dicta in *Otto Fabric* deals even the partial preemption theory a final serious blow.[287] Emphasizing the theory's "partial" nature, the court noted that a security interest is not like a collateral assignment at all.[288] Relying on *Holt v. U.S.*,[289] the court uses the following language to conceptualize the creditor's security interest: "[T]o require a federal filing and thus a collateral assignment to perfect a security interest in a patent seems inconsistent with the modern notion that a grant of a security interest need not include the conveyance of title or ownership rights."[290] Of course, the problem with this statement is that it goes too far in describing the "partial" nature of the preemption. Once the security interest is placed outside the "assignment grant or conveyance" language in section 261, the secured party's priority even as against subsequent purchasers and mortgagees would be controlled by Article Nine and not by the federal Patent Act.

As was the case with *Transportation Design*, *Otto Fabric* seems to base its holding on a patchwork notion of "partial preemption." Once again, the court's attempt at guidance in the dicta is very confusing.

v. Cybernetic Services: *The New "Leading Case" on Patent Collateral*

In 1999 the Ninth Circuit Bankruptcy Appellate Panel followed the lead of both *Transportation Design* and *Otto Fabric* in concluding that Article Nine "perfection" of patent collateral is sufficient against the lien creditor. The Panel's decision in *In re Cybernetic Services, Inc.*,[291] also followed the dicta from these prior decisions, however, when it noted that an assignee will defeat a secured creditor "who has not filed notice of its security interest in the Patent Office."[292] On June 6, 2001, the Ninth Circuit affirmed the decision of the Bankruptcy Appellate Panel in an opinion that rejects this dicta and removes the Article Nine security interest from *every* ambit of Patent Act recording. In fact, the Ninth Circuit decision seems to go too far in both its characterization of the security interest as a "mere license" and in its clear inference that Patent Act recording language does not protect the

284. City Bank and Trust Co. v. Otto Fabric, Inc., 83 B.R. 780, 782 (D. Kan. 1988).

285. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 205.

286. Revised Article Nine purports to limit any federal statute that would displace the U.C.C. filing provisions to a statute "whose requirements for a security interest's obtaining priority over the rights of a lien creditor with respect to the property preempt." U.C.C. [Revised] § 9-311(a)(1).

287. City Bank and Trust Co. v. Otto Fabric, Inc., 83 B.R. at 782.

288. *Id.*

289. Holt v. United States, 13 U.C.C. Rep. Serv. 336, 338-39 (D. D.C. 1973).

290. City Bank & Trust Co. v. Otto Fabrics, Inc., 83 B.R. at 782.

291. 239 B.R. 917 (B.A.P. 9th Cir. 1999), *aff'd*, 2001 U.S. App. LEXIS 11750 (9th Cir. June 6, 2001).

292. *Id.* at 920-21 & n.8.

subsequent BFP secured party that does not take title to the patent collateral.[293]

In holding that a security interest is outside the scope of section 261's recording requirement, the Ninth Circuit opined that because the security interest is not an "assignment, grant or conveyance," it must be a "mere license" under federal patent law.[294] The Ninth Circuit's unfortunate use of this "mere license" characterization is troublesome because a "mere license" has priority over subsequent BPF assignees under the venerable patent law rule that assignees take subject to prior licenses—irrespective of notice.[295] If the "mere license" rule in "intertwined" with recording act policy under section 261 of the Patent Act, it can easily be viewed as applicable federal patent law under the Ninth Circuit's holding in *In re CFLC, Inc.*[296] If security interests in a patent are indeed "mere licenses" under applicable federal patent law, they would not need to be perfected by a proper Article Nine filing in order to have priority over subsequent BFP assignees of the patent. That is clearly not the result intended by the Ninth Circuit.[297]

Furthermore, the *Cybernetic Services* conclusion that only title-bearing transfers are protected against unrecorded patent assignments goes too far as well.[298] The Ninth Circuit was intent on disqualifying the lien creditor and its bankruptcy persona from the protection of "purchaser or mortgagee" status under section 261. But, as an involuntary transfer, the subsequent lien creditor seems easily disqualified from the protection of the patent recording provision. The Ninth Circuit did not need to exclude all non-title transfers from section 261 protection. Security interests are typically not title-bearing transfers. Under the logic of the Ninth Circuit's opinion in *Cybernetic Services*, a typical secured party would not take priority over a prior assignee who does not record within the section 261 mandate. Section 261 of the Patent Act should protect the secured party in this case, notwithstanding the contrary Article Nine rule in U.C.C. section 9-301(1)(d) and U.C.C. [Revised] section 9-317(d).[299] This is the strongest case for preemption of Article Nine by the Patent Act. It would be a mistake to deprive the subsequent secured party of the right to rely on federal record title under section 261 of the Patent Act.[300]

vi. The Common "Partial Preemption" Thread in the Recent Patent Cases

If we focus on the narrow holdings of the four patent collateral cases discussed above, and ignore sometimes confusing logic, *Cybernetic Services*, *Otto Fabric*, and *Transportation Design* all stand for the proposition that the Patent Act

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293. *In re* Cybernetic Services, Inc., U.S. App. LEXIS 11750 at **26-36.

294. *Id.* at **26-28.

295. *Id.*; *see also* 6 E. LIPSCOMB, WALKER ON PATENTS § 20:22, at 79.

296. *In re* CFLC, Inc., 89 F.3d 673, 679 (9th Cir. 1996).

297. *See* WARD, *supra* note 18, § 2:91A.

298. 2001 U.S. App. LEXIS 11750, at **28-36.

299. Under the unvarnished state law in Article Nine, a secured party who takes and perfects a security interest in a general intangible after its debtor has already assigned it away loses to the prior assignee under either U.C.C. section 9-301(1)(d) or U.C.C. [Revised] section 9-317(d). *See* U.C.C. § 9-301(1)(d); U.C.C. § 9-317(d); *see also* WARD, *supra* note 18, § 2:40. The state law rule in Article Nine imposes no obligation on the prior assignee to record in order to hold priority against a secured party. Nevertheless, most secured parties assume that in the case of *federal* intellectual property they can rely on a title search in the federal records—state law notwithstanding.

300. *See infra* text accompanying notes *303-13; see also* WARD, *supra* note 18, §§ 2:89, 2:91A.

does not render an Article Nine filing for "perfection" ineffective against the lien creditor. For purposes of Bankruptcy Code avoidance and preference law, this is the critical priority. In that contest, local Article Nine filing controls on both the perfection and the priority issue. Although *Otto Fabric* is not as clear as *Transportation Design*, both cases lean toward the idea that the secured party must record a security transfer, in title form, under section 261 of the Patent Act in order to defeat a subsequent purchaser or mortgagee.[301] In *Cybernetic Services*, the Ninth Circuit rejected even this limited view of Patent Act preemption. *Cybernetic Services* may carry the day against the long shadow cast by *Waterman v. Mackenzie*.[302] However, courts should be concerned about the integrity of the Patent Office files. The PTO file is relied on by potential buyers or assignees who need to know the state of a patent title. If a security interest must, in the context of subsequent title takers, be formed into some title-bearing assignment, then potential buyers and assignees are relieved from the burden of searching undetermined state U.C.C. files before safely acquiring an ownership interest in a patent. Notwithstanding the recent decision in *Cybernetic Services*, a cautious lender might be moved to do it both ways, at least until needed structural changes can be made to the federal recording acts. Prudence suggests that when patents are a significant part of the debtor's collateral the secured party file a "financing statement" under state law and also require that the debtor execute a "title" document that can be recorded in the Patent Office as either a patent mortgage or a conditional assignment.

c. Even If the Article Nine Secured Party Is Not Properly Viewed As the Recipient of an Assignment, Grant, or Conveyance That Must Be Recorded Under Section 261, It Should Be Afforded Priority Under That Section As Against Prior Unrecorded Assignments Because It Is a "Subsequent Purchaser or Mortgagee?"

Whether or not the Article Nine security interest is an assignment, grant, or conveyance that needs to be recorded under section 261, if a protected subsequent party includes the holder of a security interest, Article Nine's priority rule will yield to the Patent Act anytime a transfer intended for security follows an unrecorded assignment.

This hypothetical involving a priority dispute between a prior unconditional assignee and a subsequent secured party makes the strongest case for the partial preemption of Article Nine. Section 261 provides that if a patent assignee does not make a proper PTO recording within three months of the executed assignment or prior to the date of any subsequent purchase or mortgage, the assignment is "void" against the subsequent bona fide "purchaser or mortgagee." [303] Although the use of the word "void" is awkward, the negative inference under patent law is that the assignee has better rights in the patent than the subsequent purchaser or mortgagee if the assignment is filed first or within three months of its execution.[304] In the case of the prior assignee matched against a subsequent secured party, the prior assignee is squarely within the prior section 261 "assignment, grant or conveyance."[305] If the secured party is a protected section 261 "subsequent purchaser or mortgagee" as well, then inconsistent Article Nine provisions will yield to section

301. *In re* Cybernetic Services, Inc., 239 B.R. at 920 n.8; City Bank and Trust Co. v. Otto Fabric, Inc., 83 B.R. at 782; *In re* Transportation, Design & Tech., Inc., 48 B.R. at 639.

302. *See* discussion *supra* at notes 246-55.

303. 35 U.S.C. § 261 (1994).

304. Why Corp. v. Super Ironer Corp., 128 F.2d 539, 53 U.S.P.Q. 609 (6th Cir. 1942).

305. 35 U.S.C. § 261 (1994).

261 of the Patent Act every time the conflict is so formed. Unfortunately, the Ninth Circuit's recent holding in *Cybernetic Services* suggests that a secured party would not be protected as a "subsequent purchaser or mortgagee" under section 261 unless the secured transaction took the form of a title transfer or conditional assignment.

Other recent cases on the nature of the Patent Act "purchaser" suggest that the Ninth Circuit's view may be too limited. The Federal Circuit has recently concluded that the "purchaser" protected under section 261 is the same "purchaser" protected under the common law bona fide purchaser rule historically applied to patents.[306] In *Heidelberg Harris, Inc. v. Loebach*,[307] the Federal Circuit used this common law bona fide "purchaser" rule to protect an exclusive licensee who took from the legal title holder in a transaction under which the court found that the licensor had "retained ownership."[308]

While a third party who takes an interest in less than the exclusive right to make, use, and sell may not be protected,[309] a consensual lien on the whole patent would seem to be enough to qualify the secured party as a section 261 "purchaser or mortgagee"—outside the Ninth Circuit.[310] If the section 261 reference to a subsequent "purchaser or mortgagee" mimics the common law BFP, this reference may not be as title-sensitive as the "assignment, grant or conveyance" language that measures the recording mandate.[311] In other words, a secured party seems to qualify as a protected "purchaser" under section 261 of the Patent Act, whether or not the security interest is itself an "assignment, grant or conveyance," that must record or risk avoidance.[312]

After *Cybernetic Services*, however, even this best case scenario for preemption is not free from doubt. If, as the Ninth Circuit stated, the language "subsequent purchaser or mortgagee" in section 261 refers only to the title-bearing mortgagee ancestors of the Article Nine security interest, the recording provisions of section 261 do not preempt Article Nine, even in this case.[313] A secured party who

306. Heidelberg Harris, Inc. v. Loebach, 145 F.3d 1454, 1458 (Fed. Cir. 1998) ("one who acquires an interest in a patent for valuable consideration from the legal title holder"); FilmTec Corp. v. Allied-Signal, Inc., 939 F.2d 1568, 1573 (Fed. Cir. 1991) ("*Both the common law rule and the statute* [§ 261] contemplate that the subsequent purchaser be exactly that—a transferee who pays valuable consideration, and is without notice of the prior transfer.") (emphasis added).

307. Heidelberg Harris, Inc. v. Loebach, 145 F.3d at 1456.

308. 145 F.3d 1454, 46 U.S.P.Q.2d 1948 (Fed. Cir. 1998).

309. Weinar v. Rollform, Inc., 774 F.2d 797, 807 (Fed. Cir. 1984); Bailey v. Chattem, Inc., 684 F.2d 386, 392 (6th Cir. 1982).

310. 145 F.3d at 1458 (Harris was a bona fide purchaser for value of an exclusive conditional license to make use and sell.).

As for current *state* law, a secured party clearly falls within the U.C.C. definition of a "purchaser" in sections 1-201(32), and (33). U.C.C. § 1-201(32), and (33). Revised Article Nine is even more specific. U.C.C. [Revised] § 1-201(32), and (33) ("security interest" specifically included).

311. FilmTec Corp. v. Allied-Signal, Inc., 939 F.2d 1568, 1573 (Fed. Cir. 1991) ("*Both the common law rule and the statute* [§ 261] contemplate that the subsequent purchaser be exactly that—a transferee who pays valuable consideration, and is without notice of the prior transfer." (emphasis added)).

312. 35 U.S.C. § 261 (1994).

313. If the secured party must qualify as a subsequent "mortgagee," and that word retains its pre-U.C.C. "title" armor, then the protected interests described in section 261 do not include the Article Nine security interest. *In re* Cybernetic Services, Inc., 2001 U.S. App. LEXIS 11750, at **28-36 (9th Cir. June 6, 2001). *See* A. Haemmerli, *supra* note 42, at 1699-1700. *But see* WARD, *supra* note 18, § 2:89 (rev. ed. 2001).

wants "subsequent purchaser" protection in the Ninth Circuit will have to frame its security interest as an "assignment."

d. Is Article Nine Preempted by Some Non-Statutory Federal Bona Fide Purchaser Rule in the Case of Patent Collateral?

An Article Nine "security interest" can be viewed as a contingent agreement to assign in the future, thus transferring at least equitable title in the secured party.[314] If a security agreement creates equitable title in the secured party, then, under common law principles that have been applied in patent cases prior to the existence of recording provisions, a bona fide purchaser who takes from the legal title holder without notice cuts off such equitable title.[315] If this bona fide purchaser rule survives as some form of "federal common law," then an argument for preemption exists, even if security interests do not fall within the "assignment, grant or conveyance" language of section 261 of the Patent Act.[316] However, recent cases from the Federal Circuit seem to trace this common law bona fide purchaser principle back to state law applied to the transfer of federally created property.[317] It seems clear that the old state common law governing bona fide purchasers in conflict with the equity of secured parties has yielded to Article Nine.[318] Under Article Nine, the BFP without actual or inquiry notice would still be unable to cut off the secured party's right if the secured party were properly filed under Article Nine.[319]

4. Trademark Collateral: The Weakest Case for Preemption

a. Article Nine Perfection Holds Under the Cases

i. The Narrow Scope of the Language in Section 1060 Seems To Exclude Transfers for Security

As noted earlier in Part II.A.3, section 1060 of the Lanham Act contains the most abbreviated statement on the recording of transfers of all three of the major

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314. Note, *Recording Security Interests in Patents: Accepting a Traditional Federal System To Preserve the Policies of Patent Law*, 2 B.U.J. Sci. & Tech. L. 15, ¶¶ 34, 35 (1996). A *present agreement to assign* future inventions (as distinguished from a *present assignment* of future inventions) vests equitable, not legal, title in the assignee. Arachnid, Inc. v. Merit Indus., Inc., 939 F.2d 1574, 1580-81 (Fed. Cir. 1991). A prior assignor with the right to have the assignment rescinded for fraud has equitable, not legal, title prior to the actual court ordered rescission. Heidelberg Harris, Inc. v. Loebach, 145 F.3d 1454, 1458, 46 U.S.P.Q.2d 1948 (Fed. Cir. 1998).

315. 145 F.3d at 1458; FilmTec Corp. v. Allied-Signal, Inc., 939 F.2d 1568, 1573 (Fed. Cir. 1991).

316. 35 U.S.C. § 261 (1994).

317. *FilmTec* cites *Hendrie v. Sayles* [98 U.S. 546, 549 (1879)] for the proposition that a prior equitable encumbrance is cut off by a bona fide purchaser. *Heidelberg Harris, Inc.* in turn relies on *FilmTec*. 145 F.3d at 1458. The Supreme Court's pre-*Erie* decision in *Hendrie v. Sayles* relies on state law principles of derivative title and bona fide purchaser status rather than any uniquely federal policy. 98 U.S. at 551-52. *See In re* CFLC, Inc., 89 F.3d 673, 678-79 (applies federal common law where it was important to preserve federal patent policy).

318. U.C.C. § 9-203, cmt. 5.

319. U.C.C. § 9-301(1)(d) (1995). *Accord* U.C.C. [Revised] § 9-317(d).

federal intellectual property statutes. Section 1060 of the Act provides that an *assignment* shall be void as against any subsequent purchaser for a valuable consideration without notice, unless it is recorded in the Patent and Trademark Office within three months after the date thereof or prior to such subsequent purchase.[320]

Only "assignments" of registered marks and applications to register (other than intent-to-use applications) need to be recorded in order to be protected against "subsequent purchasers." For preemption purposes, the very limited scope of section 1060 should be contrasted with its counterpart provisions for recording federal copyrights and patents discussed earlier.

The Copyright Act makes recording priority applicable between conflicting "transfers of copyright ownership" under section 205.[321] A transfer of copyright ownership includes a mortgage or hypothecation.[322] Even the provisions of state law in Old Article Nine conceded filing to the Copyright Act.[323]

The *Avalon Software* decision concludes that in order to give effect to Article Nine's deferral to Copyright Act recording requirements as "perfection," all *copyrightable* intangibles must comply with both Copyright Act section 205(a) (recording) and section 205(c) (registration).[324] Note that the logical extension of *Avalon Software* is a rule that would require all trademarks that are also copyrightable to be recorded under section 205 of the Copyright Act. Indeed, the Copyright Office is currently being asked to record security agreements in trademark collateral under section 205.[325] The scope of the Copyright Act recording is clearly overstated in *Avalon Software.*

Section 261 of the Patent Act requires the recording of any prior "assignment, grant or conveyance" as against any "subsequent purchaser or mortgagee."[326] The logic and history of this language suggest that a security interest is not an "assignment grant or conveyance" that must be recorded under section 261 because the transaction does not bear "title" as now defined under Article Nine. This is the holding of the Ninth Circuit in *Cybernetic Services.* However, the patent cases outside the Ninth Circuit teach that the transfer for security should be formed and recorded in its older title characterization when priority in the ownership chain is

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320. 15 U.S.C. § 1060 (1994) (emphasis added). Assignments of applications to register (other than intent-to-use applications) are included. 37 C.F.R. § 3.11 (1997) ("applications, patents, and registrations"); 37 C.F.R. § 3.85 (1997) ("Certificate of registration may be issued to the assignee of the applicant . . . provided . . . the appropriate document is recorded in the Office."); 37 C.F.R. § 3.16 (1997) (providing that no application to register a mark under 15 U.S.C. § 1051(b) is assignable prior to the filing of the verified statement of use under 15 U.S.C. § 1051(d) except to a successor to the business of the applicant, or portion thereof, to which the mark pertains, if that business is ongoing and existing).

321. 17 U.S.C. § 205(a), (d) (1994).

322. 17 U.S.C. § 101 (1994).

323. U.C.C. § 9-302(3)(a), (4) & cmt. 8 (1995). *But see* U.C.C. [Revised] § 9-311(a)(1) ("[A] statute . . . of the United States whose requirements for a security interest's obtaining priority over the rights of a lien creditor . . . preempt[s] Section 9-310(a) [state filing of a financing statement].").

324. *In re* Avalon Software, Inc., 209 B.R. 517, 521-22 (Bankr. D. Ariz. 1997). The earlier *Peregrine* decision went even further, holding that section 205 of the Copyright Act completely displaces the perfection and priority rules in Article Nine. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 204-05 (C.D. Cal. 1990).

325. Conversation between the Author and Register of Copyrights, Marybeth Peters (Dec. 19, 1999).

326. 35 U.S.C. § 261 (1994).

at issue. These cases strongly suggest that Article Nine recording and priority rules would thus be partially preempted by the Patent Act. If, in this context, a security interest can be seen as an "assignment, grant or conveyance," subject to possible avoidance under section 261, then the Patent Act preempts Article Nine when the contest is between the secured party and assignees—and other title-taking secured parties. While the Ninth Circuit's decision in *Cybernetic Services* stands firmly against this notion of partial preemption, it may not be the last word. At least on the issue of whether a subsequent secured party can be a protected "purchaser or mortgagee" under section 261, *Cybernetics Services* seems to have ignored the legitimate role of Patent Act priority in its intersection with Article Nine.[327]

In contrast to these other federal intellectual property recording provisions, section 1060 of the Lanham Act provides only for the recording of "assignment[s]," and only as against subsequent "purchaser[s]." Section 1060 does not even mention "mortgagees" as protected subsequent parties.[328] This stark skeletal structure is no accident. Given the dependent and ancillary character of trademarks, it is not surprising that section 1060 provides recording only for those transferees who are potential users of the mark. When this characteristic is considered along with the related fact that trademarks do not share with patents the same historical link to title-based chattel mortgage theory, it can be concluded that section 1060 was intended as a recording act for true assignments only. Such a judgment would make section 1060 inapplicable to security transfers that might otherwise be artificially conceptualized as assignments.[329]

The meager case law has followed this logic and concluded that a security interest in a trademark registration is a non-title bearing transaction outside the scope of section 1060.[330] None of the cases decided to date have held or concluded that the Lanham Act preempts any part of the filing, perfection, or priority

327. *In re* Cybernetic Services, Inc., 2001 U.S. App. LEXIS 11750, at **18-36 (9th Cir. June 6, 2001). *See* critique of *Cybernetic Services supra* in text accompanying notes 291-300.

328. 15 U.S.C. § 1060 (1994). The 1988 Trademark Revision Act made extensive revisions to the federal trademark registration system. Pub. L. No. 100-667, § 102 Stat. 3938 (1988) (codified at 15 U.S.C. § 1053 (1994)). An earlier version of the legislation contained a detailed set of rules governing the recording and priority of security interests in federal trademarks which would have preempted most of the Article Nine system. S. 1883, 100th Cong., 1st Sess. § 10(b)-(f) (1987), 133 Cong. Rec. S. 16548-49 (Nov. 19, 1987). A recorded security interest was given priority over "interests subsequently granted." *Id.* at § 10(b). This ambitious provision was dropped from the final enacted version of the 1988 Act. In its current form, the Lanham Act makes no provision for security interests. Again, the dependent nature of the typical trademark transfer, and the absence of a title-related tradition around the taking of trademarks as collateral, make it hard to find a "security interest" within the section 1060 concept of an "assignment."

329. Roman Cleanser v. National Acceptance Co., 43 B.R. 940, 945 (Bankr. E.D. Mich. 1984), *aff'd*, 802 F.2d 207 (6th Cir. 1986); *In re* 199Z, Inc., 137 B.R. 778, 781-82 (Bankr. C.D. Cal. 1992); *see also In re* C.C. & Co., 86 B.R. 485, 487 (Bankr. E.D. Va. 1988) ("A grant of a security interest is merely a device to secure indebtedness.").

330. *In re* Together Development Corp., 227 B.R. 439, 441 (Bankr. D. Mass. 1998), *aff'd*, 255 B.R. 606 (D. Mass. 2000); Roman Cleanser v. National Acceptance Co., 43 B.R. at 946; *In re* 199Z, Inc., 137 B.R. at 781; *In re* C.C. & Co., 86 B.R. at 486-87; *In re* Chattanooga Choo-Choo Co., 98 B.R. 792, 796 (Bankr. E.D. Tenn. 1989); *In re* TR-3 Indus., 41 B.R. 128, 131 (Bankr. C.D. Calif. 1984); Li'l Red Barn, Inc. v. Red Barn Sys., Inc., 322 F. Supp. 98, 107 (N.D. Ind. 1970).

scheme in Article Nine.[331] The reasoning of these cases suggests that a security interest that is properly perfected under Article Nine in the appropriate state should give the secured party priority, even as against a subsequent purchaser of the trademark registration.[332]

ii. The Argument for Partial Preemption When the Security Interest Conflicts with a Subsequent Assignee of a Trademark

Secured parties want to rely on the message that security interests in a trademark will not be taken out of Article Nine. However, the fact that trademarks and patents are recorded in the same office and under the same set of regulations causes some unease. One knowledgeable commentator has suggested that the parallel administrative structure for patents and trademarks will lead courts to follow the patent preemption cases when trademark registrations or eligible applications to register are used as collateral.[333] Along these same lines, it must be noted that no trademark case to date has actually tested the partial preemption concept that first arose with respect to patents from the dicta in *In re Transportation Design and Technology, Inc.*[334] Recall that in *Transportation Design* the court held that a security interest in a patent was perfected against the bankruptcy trustee relying on his status as an Article Nine lien creditor.[335] The court went beyond that holding to observe that, despite this valid state law perfection, the security interest would not prevail against a duly recorded conveyance of patent ownership rights.[336]

Given the administrative marriage between patents and trademarks, there is always the possibility that Article Nine perfection may not be enough when the secured interest conflicts with the subsequent assignee of a trademark. That possibility has prompted some commentators to recommend dual transactional structures and dual filing (a financing statement filed under Article Nine and an outright

331. Even *Peregrine,* the vanguard case on complete preemption, concluded in dicta that the Lanham Act "contains no provision for the registration, recordation or filing of instruments establishing security interests in trademarks." National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 204 n.14 (C.D. Cal. 1990).

332. U.C.C. § 9-301(1)(d) (1995); U.C.C. [Revised] § 9-317(d).

333. Marci L. Klumb, Note, *Perfection of Security Interests in Intellectual Property: Federal Statutes Preempt Article 9,* 57 GEO. WASH. L. REV. 135, 163 (1988).

334. 48 B.R. 635, 639-40. *Contra In re* Cybernetic Services, Inc., 2001 U.S. App. LEXIS 11750, at **18-28 (9th Cir. June 6, 2001) (security interest is a "mere license").

335. *Id.*

336. *In re Transportation Design,* provided that:

> On the surface it may appear anomalous that a secured creditor could properly perfect under the U.C.C. and obtain protection against other competing lien creditors and yet not be protected against a bona fide purchaser or mortgagee who records with the Patent Office. But, a security interest has two purposes: First, it protects the interest of a secured creditor in collateral against subsequent or competing lien claimants of its debtor. Secondly, a security interest protects the secured creditor against the debtor transferring title to the collateral free of its interest. Ordinarily, perfecting a security interest in personalty in accordance with the U.C.C. would protect both interests of the secured creditor. However, where a federal statute, such as the Patent Act, governs one area or interest which the secured creditor wishes to protect (e.g., ownership), then the federal statute preempts any other method of protecting that interest and is conclusive on the manner of protecting that interest.

48 B.R. at 639-40. *But see In re* Cybernetic Services, Inc., 2001 U.S. App. LEXIS 11750, at **18-28 (9th Cir. June 6, 2001).

collateral or conditional assignment within the mandatory recording requirement of section 1060).[337] One commentator, flying in the face of the cases to date, has suggested that the secured party *file the financing statement* covering trademark registrations with the PTO, "or else the security interest may be unperfected."[338]

At least one bankruptcy court has concluded that the filing of a financing statement with the PTO will not "perfect" a security interest in a federally-registered trademark.[339] Note that a *financing statement*, by itself, may not be recordable even as a discretionary recording under the regulations. It is a pure notice document that can be executed before any actual transfer has occurred.[340] It does not really "effect title" within the meaning of 37 C.F.R. section 3.11. The Article Nine *security agreement* is recordable as a discretionary document. However, a security interest filed with the PTO would not perfect for Article Nine purposes according to *Roman Cleanser* and the other trademark registration cases to date. If the partial preemption dicta from the patent cases gets applied to trademark registrations, a recorded security agreement (so formed) will still not be constructive notice within the assignment instruction of section 1060. Nevertheless, a secured lender trying to avoid the downside risks of forming a secured transaction as an assignment may want to file the security agreement at the PTO as an additional precaution after filing the primary financing statement in the proper state office. While such a recording will not be constructive notice if *Transportation Design* spreads into trademark registrations, the discretionary filing may provide fatal actual or inquiry "notice" to section 1060 "subsequent purchasers" who rely on the PTO record.

In the unlikely event that PTO recording is made necessary because the patent cases are extended, it would be well to note that the assignment categories for recording trademarks under the regulations are the same as those applicable to patents. In particular, the PTO recordation rule on "conditional assignments" applies to trademarks as well as patents. Under the language in 37 C.F.R. section 3.56, a "conditional assignment" will be handled in the recording office as if it were an absolute assignment.[341] Any "conditional assignment" under 37 C.F.R. section 3.56 (as distinguished from a contingent assignment or agreement to assign) is therefore a present assignment of the mark subject to defeasance. Although this kind of transfer works for patents as long as the assignee/secured party can deal with some of the risks of ownership, it is an extremely problematic device

337. 2 J. THOMAS MCCARTHY, MCCARTHY ON TRADEMARKS AND UNFAIR COMPETITION § 18:1 (4th ed. 1997) ("Until either the U.C.C. or the Lanham Act is clarified the courts should treat either federal or state recordation of a conditional security assignment as sufficient to perfect such a security."); B. CLARK, THE LAW OF SECURED TRANSACTIONS ¶ 1.8(1)(e), at n.159 (1980); Bramson, *supra* note 22, at 1578-79; *see also* Baila H. Celedonia, *Advanced Seminar on Trademark Law 1996: Trademarks as Collateral*, 438 PLI/PAT. 479, 482 (Apr. 1996) ("[T]he recording with the USPTO of the lien against trademark registrations and pending applications *is constructive* notice to subsequent purchasers for value.").

338. Martin E. Hsia, *Pitfalls of Intellectual Property: What You Don't Know Could Lead You To Malpractice*, 1995-APR. HAW. B.J. 26, 27.

339. *In re* Together Dev. Corp., 227 B.R. 439, 441 (Bankr. D. Mass. 1998), *aff'd*, 255 B.R. 606 (D. Mass. 2000).

340. U.C.C. § 9-402(1) (1994); U.C.C. [Revised] § 9-502(d).

341. 40 U.S.P.Q.2d at 1101.

when used in connection with the taking of a security interest in a trademark.[342] Remember that, unlike a contingent assignment, a conditional assignment is a present assignment that must be accompanied by enough of the goodwill or other assets of the debtor's business to avoid being unenforceable as an assignment in gross.[343] Furthermore, any license back of the trademark to the real owner would make the lender responsible for monitoring the licensee's use of the mark.[344] If the licensee and licensor provide similar goods or services, the licensor might be allowed to rely on the licensee to police and maintain the quality of the mark.[345] In other cases, a long-term relationship between the parties might justify turning quality control over to the licensee.[346] A security interest between an institutional lender and a borrower who owns the mark would seem to be outside both of these exceptions. Without such monitoring, the license may be viewed as a "naked license," which results in an abandonment of rights in the mark.[347] The mark itself, not just the validity of the transfer, may be put at risk when a present assignment (even one subject to the condition subsequent of defeasance) is used as a security devise.

iii. The Downside Risks of Using a Title Document in Transferring a Trademark for Purposes of Implementing a Secured Transaction: The Clorox *Case*

The use of a present assignment of a trademark to create a security interest can have disastrous consequences if the collateral assigned includes the debtor's rights in an intent-to-use application. In *Clorox Co. v. Chemical Bank*,[348] the Trademark Trial and Appeal Board *invalidated* the debtor's registered trademark because the intent-to-use application from which it issued was made the subject of an outright assignment to the bank under the terms of a collateralized loan agreement.[349] It appeared from the facts that the assignment mechanism was used merely to carry out the intent of both parties that the assigned rights serve as security for the debtor's credit obligation. The bank clearly had no "intent to use" the mark. Nevertheless, the *Clorox* court found that the unconditional assignment device itself violated the congressional policy against trafficking in or profiting from the sale of intent-to-

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342. *In re* Roman Cleanser Co., 802 F.2d 207 (6th Cir. 1986). The internal largess of the PTO cannot expand the narrow constructive notice limits on the section 1060 mandate to record "assignments." *In re* 199Z, Inc., 137 B.R. 778, 782 n.7 (Bankr. C.D. Cal. 1992); *see also* Simensky, *Enforcing Creditors' Rights Against Trademarks*, 79 TRADEMARK REP. 569, 570-78 (1989).

343. United Drug Co. v. Theodore Rectanus Co., 248 U.S. 90, 97 (1918) ("There is no such thing as property in a trademark except as a right appurtenant to an established business or trade in connection with which the mark is employed."). *But see* NAFTA Treaty, *supra* in text accompanying notes 75-77, at art. 1708:11.

344. Dawn Donut Co. v. Hart's Food Stores, Inc., 267 F.2d 358, 367 (2d Cir. 1959).

345. *See* Visa U.S.A., Inc. v. Birmingham Trust Nat'l Bank, 696 F.2d 1371, 1376 (Fed. Cir. 1982), *cert. denied sub nom.*, South Trust Bank of Alabama, Birmingham v. Visa U.S.A., Inc., 464 U.S. 826 (1983).

346. *See* Transgo, Inc. v. Ajac Transmission Parts Corp., 768 F.2d 1001, 1017-18 (9th Cir. 1985), *cert. denied*, 474 U.S. 1059 (1986).

347. First Interstate Bancorp v. Stenquist, 16 U.S.P.Q.2d 1704, 1706 (N.D. Cal. 1990) (stating "it is well established that where a trademark owner engages in naked licensing, without any control over the quality of goods produced by the licensee, such a practice is inherently deceptive and constitutes abandonment of any rights to the trademark by the licensor").

348. 1996 TTAB LEXIS 15, 40 U.S.P.Q.2d 1098 (TTAB 1996).

349. *Id.* at 1102-03.

use applications.[350] On the remedy issue, the legislative history behind the 1988 amendments to section 1060 suggested to the court that cancellation of the mark, rather than simple invalidation of the assignment, was the appropriate order.[351]

iv. Secured Parties Should Record Their Security Interests Under the Regulations As Discretionary Contingent Transfers

Although the risks of using an absolute or "conditional assignment"[352] of a trademark outweigh any possible advantage, it would be a good idea for secured parties to record their Article Nine security agreements *with the PTO*, in addition to filing their Article Nine financing statements in the appropriate state offices. Great care should be taken, however, to form the transfer as a ordinary security agreement—not a present assignment. So formed, such a recording could cover trademark registrations and pending "non-intent-to-use" applications. Under the recording regulations applicable to both patents and trademarks, "other documents . . . affecting title to . . . registrations, will be recorded as provided in this part or at the discretion of the Commissioner."[353] A security interest in a trademark can be formed as a *recordable document* under the joint regulations covering the recording of both patents and trademarks.[354] While such a discretionary recording is not constructive notice,[355] it may provide fatal actual or inquiry notice to section 1060 "subsequent purchasers" who rely on the PTO record.

As things presently stand, a typical security agreement in a mark can and should provide for a *future contingent assignment* of the mark or application on the debtor's default.[356] Because no present title passes, there is no absolute need to transfer

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350. *Id.* at 1105-07. It would not have helped Chemical Bank if they had called the document a "security agreement" or "security interest" on the cover sheet. The court indicated that it would examine the substance of the agreement. *Id.* at 1101; *see also* CHANGES IN PATENT & TRADEMARK ASSIGNMENT PRACTICE, *supra* note 42, at 29639 ("The document will always speak for itself.").

351. Clorox Co. v. Chemical Bank, 40 U.S.P.Q.2d at 1126-27.

352. 37 C.F.R. § 3.56 (1992).

353. *Id.* § 3.11(a).

354. *Id.* §§ 3.1, 3.11, 3.56 (1994); CHANGES IN PATENT & TRADEMARK ASSIGNMENT PRACTICE, *supra* note 42, at 29636, 29640.

355 The internal largess of the PTO cannot expand the narrow constructive notice limits on the section 1060 mandate to record "assignments." *In re* 199Z, Inc., 137 B.R. 778, 782 n.7 (Bankr. C.D. Cal. 1992).

356. A security agreement on an intangible is, in effect, an agreement to assign on the event of a default. They are contingent assignments. On the other hand, the "conditional assignment" referred to in section 3.56 is a present assignment subject to reverter on condition of payment. However, there is understandable confusion. The phrase "conditional assignment" has been used to refer to agreements to assign in the future as well. Borrowing from respondent's brief, the Trademark Trial and Appeal Board in *Clorox Co. v. Chemical Bank*, 1996 TTAB LEXIS 15, 40 U.S.P.Q.2d 1098, 1101 n.10 (TTAB 1996), referred to a *contingent* assignment as an effective non-title bearing security device. This contingent assignment was described simply as an agreement to assign a trademark in the future (on an event of default). In the excerpt taken from *Clorox*, this same agreement to assign in the future was also referred to as a "conditional assignment." *Id.* So defined, this kind of "conditional assignment" is not the same as the present assignment subject to defeasance in 37 C.F.R. § 3.56. Because an agreement to assign at the occurrence of a future event (under whatever label) is not a present assignment, it risks neither trafficking nor the perils of an assignment in gross. Because it is not an assignment, it should not fall within the PTO mandate that conditional assignments be treated as absolute. As a form of security interest, however, it should be recordable at the Commissioner's discretion. 37 C.F.R. § 3.11(a) (1997).

goodwill, and no assignment in gross results. However, if an event of default occurs and the security party must realize on its trademark collateral, any present operative assignment at default, including one provided for with a power of attorney attached to the security agreement, would have to comply with section 1060.[357] Secured creditors may try to hedge their bets by having a present assignment with appurtenant goodwill executed at the same time as the security agreement and instruct an escrow agent to record it only if the debtor defaults. It should be noted, however, that a court following the *Clorox* rationale will not view this scenario any differently than it would view an executed and recorded assignment. In the case of an intent-to-use application, both raise the same "trafficking" objection that led the *Clorox* court to cancel the registration.

v. *Is the Secured Party Protected As a "Subsequent Purchaser" Under Section 1060?*

Although a security interest seems outside the definition of an assignment and beyond the policy on recordable trademark assignments, it is possible that a secured party could be a section 1060 "subsequent purchaser" protected against some real unrecorded assignments.[358] The state law rule in U.C.C. section 9-301(1)(d) would give priority to the prior transferee/assignee of the mark as long as the transferee/assignee "gave value" before perfection.[359] Because value is broadly defined under section 1-201(44),[360] it seems unlikely that a prior assignee of a trademark would ever lose to a subsequent secured party under the state law rule protecting "transferees" in section 9-301(1)(d), whether or not the assignee/transferee ever recorded. The secured party might want to argue for preemption, therefore, whenever the prior assignee fails to record within three months or prior to the attachment of the subsequent security interest. Although the Ninth Circuit concluded otherwise in *Cybernetic Services*, a "purchaser" under the Patent Act can be defined to include a party who takes a security interest in the whole right.[361] Under the U.C.C. a purchaser includes one who takes by "mortgage, pledge or lien."[362] Courts have looked to the Commercial Code as a source for federal common law definitions on other occasions.[363] When enacted state rules inform the federal common law, the result under the preemption doctrine should be the same as when section 9-104(1) applies. Under either approach, local law is displaced by

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357. *See* 1 J. THOMAS MCCARTHY, MCCARTHY ON TRADEMARKS AND UNFAIR COMPETITION § 18:1(G), at 796 (2d ed. 1984).

358. *See* the discussion on the meaning of "subsequent purchaser" under the Patent Act *supra* text accompanying notes 303-19; *see also* WARD, *supra* note 18, § 2:89.

359. U.C.C. § 9-301(1)(d) (1995); *accord* U.C.C. [Revised] § 9-317(d).

360. *See* U.C.C. § 1-201(44) (1995).

361. *In re* Cybernetic Services, Inc., 2001 U.S. App. LEXIS 11750, at **28-36 (9th Cir. June 6, 2001); see also the discussion of *Cybernetic Services* on this point *supra* at notes 298-300 and the discussion of the meaning of "subsequent purchaser" under the Patent Act *supra* at notes 303-319.

362. U.C.C. § 1-201(32), (33) (1995); *accord* U.C.C. [Revised] § 1-201(32), (33).

363. When a judicial determination of complete preemption is made, Article Nine may still remain as a source of supplementary federal common law rules. The enacted law of a particular "contact" state will often be the appropriate source for "federal common law" rules necessary to supplement the applicable federal scheme. United States v. Kimbell Foods, Inc., 440 U.S. 715 (1979); *see also* JAMES J. WHITE & ROBERT S. SUMMERS, THE UNIFORM COMMERCIAL CODE § 21-10, at 752-54 (4th ed. 1995).

the federal scheme, but should be consulted where the federal scheme is silent. However, enacted state law will be ignored in formulating federal common law rules when there is a strong overriding interest in national uniformity and otherwise applicable state law varies from the commercial norm.[364] In such cases, the "Uniform Version" of Article Nine, rather than the version enacted in the "contact" state, may be the best place to find the supplementing federal common law.[365] The distinction may have limited importance, however, because there is general uniformity with respect to definitions and priority rules among the enacted versions of Article Nine.

Finally, even if section 1060 of the Trademark Act is held to partially preempt Article Nine as to federally-registered trademarks, the lender should *still* file under Article Nine. Section 1060 does not deal with lien creditor rights at all, so lien creditor priority will surely depend on state law perfection.[366] Furthermore, unregistered trademarks are solely creatures of state law. Under Article Nine a trademark is a "general intangible," which normally means that the Secretary of State's Office is the appropriate place to file.[367]

Because the priority rule under section 1060 of the Lanham Act seems confined to "assignments" and "subsequent purchasers," the case for partial preemption is much weaker under section 1060 than under section 261 of the Patent Act.[368] But because the secured party might qualify as a section 1060 "subsequent purchaser" that would be protected against delayed or unrecorded assignments of the mark, the state law rule in U.C.C. section 9-301(1)(d) would have to give way on this point.[369] Under section 1060, the assignee needs to record within the three-month grace period, or at least before the security interest attaches.[370] If not, the secured party wins if it gives the debtor new value and has no notice of the prior assignment. Remember that even if it is viewed as a protected "purchaser," for Lanham Act purposes, the secured party is unprotected against a prior unrecorded assignment of the mark during the three-month grace period in section 1060 as well as throughout the period of any "office delay."

IV. REFORM PROPOSALS

A. *The CFA Sponsored "Quick Fix" for Copyright Collateral Only: H.R. 4351*

The Commercial Finance Association has sponsored a short piece of copyright reform legislation designed to overrule the most troublesome parts of the *Peregrine* decision. The proposed "Security Interests in Copyrights Financing Preservation Act"[371] restores Article Nine perfection and priority rules to the se-

364. United States v. Kimbell Foods, Inc., 440 U.S. at 715.

365. Allen v. F.D.I.C., 599 F. Supp. 104 (E.D. Tenn. 1984); F.D.I.C. v. Morgan, 727 S.W.2d 500 (Tenn. Ct. App. 1986).

366. *See* U.C.C. § 9-301(1)(b) (1995).

367. U.C.C. § 9-106 cmt. (1995); U.C.C. § 9-401(1)(b) (1995).

368. Roman Cleanser v. National Acceptance Co., 43 B.R. 940, 945 (Bankr. E.D. Mich. 1984), *aff'd*, 802 F.2d 207 (6th Cir. 1986).

369. U.C.C. § 9-301(1)(d) (1995).

370. 15 U.S.C. § 1060 (1994).

371. Security Interests in Copyrights Financing Preservation Act, H.R. 4351, 106th Cong., § 1, 2d Sess. (2000).

cured party/lien creditor showdown so critical under section 544(a)(1) of the Bankruptcy Code.[372]

H.R. 4351 has several key provisions. First, subsection (2)(a) of H.R. 4351 amends section 101 of the Copyright Act by adding a definition of the "lien creditor"—borrowed from the language in Old U.C.C. section 9-301(3).[373] Next, subsection (2)(b) of H.R. 4351 amends section 205 of the Copyright Act by adding a new subsection (f).[374] New subsection 205(f) provides that the Copyright Act "is not intended to preempt the Uniform Commercial Code with respect to the perfection of a security interest in a copyright or the proceeds of a copyright." "Perfection" may be achieved under either Article Nine or section 205 of the Copyright Act. Finally, all priority conflicts between the secured party and the lien creditor defer to "applicable law other than this title."[375]

Note that H.R. 4351 does not remove federal law from the priority mix entirely, however. The language of the bill's proposed section 205(f) goes on to confer *federal* priority in favor of the "transferee of an interest in a copyright or the proceeds of a copyright unless" the secured party is "perfected" under section 205 of the Copyright Act.[376] Recall that this *federal* mode of "perfection" is optional for other priority purposes. H.R. 4351 is not clear on this point, but the recording and perfection under proposed section 205(f) would seem to require that any such permissive recording of the security agreement must comply with the constructive notice requirement in section 205(c) of the Copyright Act.

The absence of a definition of "transferee" in H.R. 4351 makes it unclear whether new subsection (f) still allows a secured party to claim the status of a transferee à la *Peregrine*. While it appears that "transferees" and "transferees of a security interest" are set up as separate non-overlapping categories in the proposed language of section 205(f), *Peregrine* held that the creation of a security interest should be treated as a "transfer of copyright ownership."[377] If a "transferee of a security interest" is still capable of being defined as a plain old "transferee," after new subsection 205(f), then a priority dispute between two competing secured parties might be decided under section 205(d) of the Copyright Act, not under state law (Article Nine "first-to-file" rule).[378] The proposed anti-preemption language in subsection 205(f)(1) would not force a different result because it only refers to Article Nine issues relating to the "perfection [not priority] of a security interest in a copyright."[379] If a more limited secured party/ownership assignee priority rule is intended, the language of H.R. 4351 should define "transferees" and, in light of *Peregrine*, exclude secured transactions from that definition.

The confusion over who can be a "transferee" raises a further problem under the amendments proposed in H.R. 4351. Remember that *Peregrine*'s section 205(d) lien creditor is a "later transferee" with priority against any prior unrecorded "transfer of copyright ownership," including an unrecorded assignment (a real owner-

372. *Id.* § 2(f).
373. *Id.* § 2(a).
374. *Id.* § 2(b).
375. *Id.*
376. *Id.*
377. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194, 198 (C.D. Cal. 1990).
378. *Compare* 17 U.S.C. § 205(d) (1994) *with* U.C.C. § 9-312(5) (1995).
379. 17 U.S.C. § 205(f)(1) (1994).

ship transfer not a security interest).[380] The proposed 205(f) language in H.R. 4351 only solves this problem when a "security interest holder" comes up against the trustee in bankruptcy. The proposed language does not otherwise remove the lien creditor (and thus the bankruptcy trustee) as a lurking presence from section 205(d) altogether.

Providing that a "security interest . . . may be perfected under either the Uniform Commercial Code or this title" may not go far enough in states that still have old Article Nine. Arguably, the *state law* in these states makes an independent deferral to the Copyright Office because it "provides for a national . . . registration" under current U.C.C. section 9-302(3)(a).[381] Under that logic, the proper "state law" place to file, for all perfection purposes, is the Copyright Office. The anti-preemption language proposed in section 205(f)(1) does not restore Article Nine filing if the Copyright Office is still considered to be the proper location for filing and perfection *as a matter of the state law contained current sections 9-302(3)(a) and (4).* Revised Article Nine solves this problem of possible state law reference back to the Copyright Act in Revised section 9-311(a)(1).[382]

B. The Federal Intellectual Property Security Act: The Work of a Joint ABA Task Force

1. FIPSA: The 1992 Report and the Early Drafts

Of the proposed federal legislative reforms offered to date, the most comprehensive is the Federal Intellectual Property Security Act (FIPSA) sponsored by a Joint Task Force organized under the auspices of the American Bar Association. The Joint Task Force is composed of members from the ABA Section on Business Law and the ABA Section on Intellectual Property Law.

In 1992, the Joint ABA Task Force on Security Interests in Intellectual Property published its Preliminary Report.[383] In contrast to the Report of the Article Nine Study Committee, the Joint Task Force report called for a "mixed" filing system designed to minimize reliance on the existing federal tract recording systems. As the Preliminary Report observed:

> Under this approach, financing statements on form U.C.C.-1 would be filed under the applicable state's U.C.C. Article 9, which filing would create priority as to all manner of intellectual property against lien creditors, secured creditors, and all third parties other than subsequent purchasers/assignees for value. [This would require action by Congress.] As to the latter class, priority would be achieved by a notice filing or filings (on a debtor's name basis) of a copy of the U.C.C.-1 filed in the state office with an appropriate federal cover sheet in one or more federal offices. [There could be one combined registry for all federal intellectual property, or two or three (i.e., one each for copyrights, patents and trademarks) separate registries.] *It is contemplated by the Task Force that a secured party in any transaction in which intellectual property is, or may become, of significance would routinely file at both the state and federal level*; this would solve any problem relating to the transformation of intellectual property from the state to the federal realm.[384]

380. *See supra* text accompanying notes 144-59.
381. U.C.C. § 9-302(3)(a), (4) (1995).
382. U.C.C. § 9-311(a)(1) (1995).
383. PRELIMINARY ABA TASK FORCE REPORT, *supra* note 25.
384. PRELIMINARY ABA TASK FORCE REPORT, *supra* note 25, at 20-21 (emphasis added).

In an effort to carry out the integrated "mixed approach" recommended in the 1992 report, the Drafting Committee of the Joint Task Force initially set out to draft separate proposed amendments to the Copyright Act,[385] the Patent Act,[386] the Lanham Act,[387] and the Semiconductor Chip Act.[388] Although the four drafts were formed around the existing language and concepts in the four separate pieces of legislation, they had many common elements.

Within each discrete federal intellectual property statute, the Task Force drafts either drastically curtailed or eliminated the generous recording grace periods. Each preliminary draft created a "federal financing statement" and a notice-based federal filing system under the authority of the affected agencies. Each draft also used common language to describe a federal "race" priority rule that made security interests in the subject intellectual property "ineffective" against a "buyer" who recorded its interest in the existing tract record file before the security interest was filed in a newly-created federal notice-based filing system.[389] Common language in each draft provided further that all other issues of priority not "provided" for under the "race" rule would be determined under "non-federal law governing security interests in personal property."[390]

As of March 1, 1999, the Task Force had consolidated the common elements of its four earlier drafts into one draft statute entitled the "Federal Intellectual Property Security Act" (FIPSA).[391] FIPSA relies heavily on the common elements developed for the treatment of security interests in the prior four-Act proposal. In that sense, the new consolidated proposal represents a shorter and more streamlined piece of legislation. The next Section examines the principal provisions of the FIPSA proposal.

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385. Task Force on Security Interests in Intellectual Property, Business Law Section, American Bar Association, DRAFT AMENDMENTS TO U.S. COPYRIGHT ACT RELATING TO SECURITY INTERESTS IN COPYRIGHT (July 14, 1998) [hereinafter referred to as TASK FORCE DRAFT—COPYRIGHT Act].

386. Task Force on Security Interests in Intellectual Property, Business Law Section, American Bar Association, DRAFT AMENDMENTS TO U.S. PATENT ACT RELATING TO SECURITY INTERESTS IN PATENTS (July 14, 1998) [hereinafter referred to as TASK FORCE DRAFT—PATENT Act].

387. Task Force on Security Interests in Intellectual Property, Business Law Section, American Bar Association, DRAFT AMENDMENTS TO LANHAM ACT RELATING TO SECURITY INTERESTS IN TRADEMARKS, SERVICE MARKS AND CERTIFICATION MARKS (July 14, 1998) [hereinafter referred to as TASK FORCE DRAFT—LANHAM Act].

388. Task Force on Security Interests in Intellectual Property, Business Law Section, American Bar Association, DRAFT AMENDMENTS TO SEMICONDUCTOR CHIP ACT RELATING TO SECURITY INTERESTS IN MASK WORKS (July 14, 1998) [hereinafter referred to as TASK FORCE DRAFT—MASK WORKS].

389. TASK FORCE DRAFT—COPYRIGHT ACT, *supra* note 385, § 206(b)(2); TASK FORCE DRAFT—PATENT ACT, *supra* note 386, § 263(b)(2); TASK FORCE DRAFT—MASK WORKS, *supra* note 388, § 903A(b); TASK FORCE DRAFT—LANHAM ACT, *supra* note 387, § 1060A(b)(2).

390. TASK FORCE DRAFT—COPYRIGHT ACT, *supra* note 385, § 206(b)(1); TASK FORCE DRAFT—PATENT ACT, *supra* note 386, § 263(b)(1); TASK FORCE DRAFT—MASK WORKS, *supra* note 388, § 903A(b); TASK FORCE DRAFT—LANHAM ACT, *supra* note 387, § 1060A(b)(1).

391. Task Force on Security Interests in Intellectual Property, Business Law Section, American Bar Association, DRAFT, FEDERAL INTELLECTUAL PROPERTY SECURITY ACT (March 1, 1999)[hereinafter referred to as TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT]. The text of this proposal is set out in the conference materials and in WARD, *supra* note 18, at Appendix 1..

2. *FIPSA: Principal Elements of the Proposal*

a. FIPSA: The Elimination (in the Case of Section 205 of the Copyright Act and Section 1060 of the Lanham Act) or Drastic Reduction (in the Case of Section 261 of the Patent Act) of the Tract Recording Grace Periods

FIPSA proposes elimination of the one or two-month grace period in section 205(d) of the Copyright Act. In its place FIPSA creates a race-notice rule that gives priority to the first "executed" transfer of copyright ownership if recorded in a manner to give constructive notice "before recordation in such manner of the later transfer."[392] "Otherwise the later transfer prevails if recorded first in such manner, and if taken in good faith, for value, and without notice of the earlier transfer."[393] In a similar fashion, FIPSA amends the Semiconductor Chip Act by eliminating the three-month grace period for the first executed transfer along with the priority rule that included it.[394]

FIPSA contains a proposed amendment to section 1060 of the Lanham Act that would replace the current three-month grace period for trademark recordings with a straight notice-recording priority rule. The proposed language protects BFP "subsequent purchasers" against assignments that are unrecorded when the purchase occurs, whether or not the purchase itself is ever recorded.[395]

FIPSA's proposed amendment to section 261 of the Patent Act retains a grace period for recording a prior "assignment, grant or conveyance."[396] However, the proposed language reduces the time period from three months to ten days.[397]

These reduced grace periods do not deal with the long office delays that currently exist between the time a document is received for recording in the federal tract file and the time it actually shows up in the searchable record.

b. FIPSA: Security Interests Are Excluded Altogether from Copyright Act and Patent Act Tract Recording and Priority Rules and Are Excluded from Any Obligation to Record in the Trademark Tract Records

After dispensing with the federal recording grace periods,[398] the FIPSA removes security interests altogether from the operation of the Copyright Act and Patent Act tract recording provisions.[399]

The language designed to remove security interests from section 205 of the Copyright Act is found in a proposed subsection that revises section 205(d) and adds a new section 205(f).[400] A subtle change in the proposed section 205(d) language is the substitution of the phrase "transfers of copyright ownership" for "transfers" in describing the conflicts that fall within the tract priority rule in sec-

392. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 4(a)(2).
393. *Id.* § 4(a)(2).
394. *Id.* § 4(a)(4).
395. *Id.* § 4(b).
396. *Id.* § 4(c).
397. *Id.*
398. *See* discussion *supra* in text accompanying notes 392-97.
399. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 4.
400. *Id.* § 4(a)(2), (3).

tion 205(d) of the Copyright Act.[401] The change in language is significant because FIPSA also redefines a "transfer of copyright ownership" in section 101 so as to exclude the Article Nine security interest and its prior common law precursors.[402] By inserting this new definition in the scope sentence that introduces the 205(d) priority rule, the FIPSA language has undercut one of the holdings in the *Peregrine* case[403] to the effect that a security interest could be a "transfer of copyright ownership" within the federal priority rule in section 205(d).[404] FIPSA also excludes a "lien creditor" from the definition of a "transferee" *for purposes of the Act*.[405] However, the Act's proposed definition of a "transferee" would not seem to alter the meaning of "transfer" in current section 201(d) of the Copyright Act.[406] "Transfer" under section 201 includes involuntary transfers.[407] In *Peregrine*, Judge Kozinski relied on section 201(d) to support his conclusion that the bankruptcy trustee, as hypothetical lien creditor, could find priority in section 205(d).[408] FIPSA should propose a further amendment to the last sentence of section 205(d) to make clear that the lien creditor (even in hypothetical Bankruptcy Code form) is excluded from wearing the section 205(d) mantle of a "later transfer."

FIPSA also adds a new subsection 205(f)[409] that excludes all issues concerning the "creation, attachment, perfection, priority or enforcement of a security interest" in copyright collateral from the operation of the section 205 recording and priority rules, including the subsection (e) priority rule on nonexclusive licens-

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401. *Id.* § 4(a)(2).

402. *Id.* § 4(a)(1).

403. *See* National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. 194 (C.D. Cal. 1990).

404. *Id.* at 198-99. This amended language may not reach the most insidious holding in the *Peregrine* case, however. According to the teaching of *Peregrine*, section 205(d) of the Copyright Act displaces the Article Nine priority rules, generally, and the rule in U.C.C. section 9-301(1)(b) regulating priority between the secured party and the lien creditor, in particular. *Id.* at 205. Forced to find a *federal* priority rule that recognized the rights of the bankruptcy trustee's "lien creditor" status, Judge Kozinski concluded that this hypothetical construct (11 U.S.C. § 544(a)(1) (1994)) could be made to fit within the description of a protected later transfer "[taken] in good faith, for valuable consideration . . . without notice" under the last sentence of section 205(d) of the Copyright Act. *Id.* at 205-07; *see also* discussion *supra* in text accompanying notes 144-59. This holding provided the bankruptcy trustee with a federal right (17 U.S.C. § 205(d) (1994)) to set aside the unrecorded security interest as a "transfer of copyright ownership." 17 U.S.C. § 205(d) (1994). *Peregrine* thus builds the bankruptcy trustee up into a BFP-type "later transfer" under the Copyright Act.

The new definition of a "transfer of copyright ownership" proposed in section 4(a)(1) of the Task Force Act undercuts one of the premises of Judge Kozinski's holding. It removes security interests from the category of ownership transfers that are vulnerable to a "later transfer" when they fail to record in the section 205 copyright tract file. However, Judge Kozinski's holding that the bankruptcy trustee gets the status of a protected "later transfer" remains undisturbed. The logic of that holding can still be applied to aid a trustee who wants to upset an unrecorded copyright *assignment* that is well within the current definition of a "transfer of copyright ownership" and well within the Task Force Act's amended definition. *See* discussion *supra* in text accompanying notes 144-59.

405. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 3(a).

406. 17 U.S.C. § 201(d) (1994).

407. *See* Forster Music Publishers, Inc. v. Jerry Vogel Music Co., 62 U.S.P.Q. 142 (S.D.N.Y. 1944), *aff'd*, 147 F.2d 614 (2d Cir. 1945), *cert. denied*, 325 U.S. 880 (1945).

408. National Peregrine, Inc. v. Capital Fed. Sav. & Loan Ass'n, 116 B.R. at 205.

409. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 4(a)(3).

ees.[410] This new subsection (f) also makes clear that recording a security interest in the section 205 tract file *will not* give constructive notice "of any fact relating to the existence or priority of any security interest."[411] In similar fashion, FIPSA also excludes security interests from sections 903(a)-(d) of the Copyright Act dealing with documents that provide constructive notice with respect to mask works.[412]

FIPSA amends section 261 of the Patent Act by providing that "the rights and obligations of all persons with respect to a security interest in a patent, patent application, or the proceeds of either, including matters of creation, attachment, perfection, priority, and enforcement, shall be governed by non-federal law relating to security interests in personal property."[413] The notice-recording characteristic of current section 261 is retained, but the word "mortgagee" is deleted from the section's description of protected parties. Only the "subsequent purchaser for value, without notice" gets protected against unrecorded interests.[414] Even though the subsequent purchaser for value need not record in order to prevail over a prior unrecorded patent assignee, a subsequent purchaser of a patent or a patent application does need to record as against a prior secured party. Under FIPSA this is a new race, run on two separate tracks. The subsequent purchaser of a patent or application is vulnerable to the prior secured party unless it records in the section 261 tract file before the secured party files its financing statement in FIPSA's new federal financing statement file.[415]

The conforming amendments to the Lanham Act create a different priority dynamic, however. Unlike the FIPSA language that amends section 261 of the Patent Act, the new language proposed for section 1060 of the Lanham Act *does not* completely exclude security interests from the tract recording priority rule.[416] Instead, section 1060 provides that assignees of a mark are "subject to the rights of any secured party who has filed a federal financing statement prior to the date of filing of such assignment."[417] Under the FIPSA proposal for section 1060, a secured party's priority against a competing assignment expressly depends, not on *purchasing* prior to the recording of the assignment or on state law priority, but on the secured party *winning the race to the federal file*.[418] This specific inclusion of security interests within the recording priority provision of section 1060 means that FIPSA actually contains a different federal "race" priority rule for federal marks than it does for copyrights and patents. This aspect of FIPSA is taken up in connection with the discussion of the integrated federal "race" priority rule.[419]

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410. *Id.*
411. *Id.* § 4(a)-(c).
412. *Id.* § 4(a)(4).
413. *Id.* § 4(c).
414. *Id.*
415. *See* discussion *infra* notes 440-66 and accompanying text.
416. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 4(b).
417. *Id.*
418. *Id.*; *see also* discussion *infra* notes 440-66 and accompanying text.
419. *See* discussion *infra* notes 440-66 and accompanying text.

c. FIPSA: All Perfection and Priority Questions Are Referred to Article Nine Except for a New Federal Recording and Priority Rule that Reconfigures the Limited Federal Priority Suggested in the Transportation Design *Dicta*

Removal of security interests from the tract files (copyrights and patents) or from any obligation to record therein (trademarks) sets up FIPSA's unified federal scheme to deal with the security interests so removed. The core of this new scheme is found in FIPSA section 3(b).[420] Most of the proposed language in section 3(b) sets out the mechanical requirements for a federal financing statement and the structure for a federal notice filing system to handle financing statements covering "Federal Intellectual Property Rights."[421] The proposed notice filing system is patterned after the structure of Revised Article Nine.[422] FIPSA section 3(d) contains an instruction to each of the affected federal agencies to "coordinate their respective procedures for filings of federal financing statements as to security interests in Federal Intellectual Property Rights."[423] Despite this impressive new structure created by FIPSA, however, federal notice filing for security interests functions only in a very narrow perfection and priority corridor under sections 3(b)(1) and (2).

The priority and preemption heart of FIPSA is in sections 3(b)(2)(A) and (B).[424] Subsection (A) contains a broad congressional deferral to state law on all matters concerning the creation, perfection, and priority of a security interests in a "Federal Intellectual Property Right."[425] Subsection (B) contains a very narrow exception from this general reference to Article Nine for priority disputes between secured parties and "transferees" of a "Federal Intellectual Property Right."[426] This singular federal "race" rule renders a security interest in a Federal Intellectual Property Right "ineffective" against a "transferee" of such a "right" whenever the transferee records in the appropriate federal tract file before the secured party files one of the newly-conceived federal financing statements in the newly-conceived federal notice file under the name of the debtor.[427] The mechanics of this new federal "race" priority rule are discussed in the next Section.[428]

The most critical piece of the FIPSA solution is, however, the broadly worded and far-reaching limit on federal preemption in section 2(b)(2)(A).[429] Subsection (2)(A) refers all priority issues with respect to security interests (except for the specific federal race rule in subsection 2(B)), including those involving conflict-

420. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 3(b).

421. *Id.* § 3(b)(3), (4).

422. *Id.* § 2(a)(3); *see also* U.C.C. [Revised] § 9-501 to 9-529.

423. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 3(d).

424. *Id.* § 3(b)(2)(A), (B).

425. *Id.*

426. *Id.* § 3(b)(2)(B).

427. *Id.*

428. *See* discussion *infra* notes 440-66 and accompanying text.

429. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 3(b)(2)(A).

ing licenses, to "applicable non-federal law governing security interests in personal property (Article Nine)."[430]

Taken together, the two subsections of section 3(b)(2) set out a very limited role for federal law whenever security interests in federal intellectual property rights are involved. *Peregrine*'s federal priority rule applied to copyright collateral is gone.[431] The only trace that remains is the limited federal race priority in subsection 3(b)(2)(B) and its related "federal notice filing" requirements.[432] All other priority questions are handled under Article Nine, including the secured party/lien creditor contest so critical in bankruptcy.[433]

FIPSA dispenses with the dicta in the patent cases (e.g., *Transportation Design*)[434] to the effect that security interests must be viewed as assignments for recording purposes when they compete for priority with real assignments.[435] As noted above, the FIPSA amendments to section 261 remove security interests from the section 261 tract recording rules that govern "assignments, grants and conveyances."[436] Much of the policy underlying the dicta in the patent cases is, however, preserved and reconfigured in proposed subsection (b)(2)(B)'s race priority rule.[437] For the secured party, however, the narrow federal FIPSA race is not a race to a federal tract file. Instead, the secured party is racing to the new federal notice file with its new federal financing statement.

All priority and other issues outside the narrow race rule are governed by state law. The language on the scope of the deferral to state law in subsection (b)(2)(A) refers to "[t]he *creation, attachment, perfection, priority and enforcement* of a security interest in a Federal Intellectual Property Right."[438] The express language of deferral on issues of *perfection* seems aimed at any federal preemption doctrine that might be applied to displace state *filing* of a security interest, such as the one suggested for copyrightable collateral in *Avalon Software*.[439]

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430. *Id.* Subsection (b)(2)(A) reads:

> The creation, attachment, perfection, priority and enforcement of a security interest in a Federal Intellectual Property Right or in the proceeds thereof relative to all competing rights, claims, and interests therein and licenses thereof shall be determined by applicable non-federal law governing security interests in personal property, except as provided in subsection (b)(2)(b).

Id.

431. *Id.* § 4(a); *see also* discussion *supra* notes 399-407 and accompanying text.

432. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, §§ 2(a)(4), 3(b)(2)(A).

433. *Id.* § 3(b)(2)(A).

434. *See* discussion *supra* notes 257-73 and accompanying text.

435. *See* discussion *supra* notes 257-73 and accompanying text.

436. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 4(c)(4) ("An assignment, grant or conveyance of a patent application or a patent (but not of a security interest in a patent application or a patent) shall be void.").

437. *Id.* § 3(b)(2)(B).

438. *Id.* § 3(b)(2)(A).

439. According to the bankruptcy court decision in *Avalon Software*, the section 9-302(3)(a) filing deferral or "step-back" in favor of the Copyright Act applies to all of the debtor's "copyrightable" assets, including software the debtor may view as a trade secret. *In re* Avalon Software, Inc., 209 B.R. 517, 520-22 (Bankr. D. Ariz. 1997).

d. FIPSA: A Discrete "Race" Priority Rule Governs Conflicts Between Security Interests in "Federal Intellectual Property Rights" and Transferees of These Rights; However Current FIPSA Language Orders Patent Priority Disputes in a Manner Different from Trademark Disputes

The new federal financing statement created by FIPSA is at the core of the only federal priority rule in the proposal. The section 3(b)(2)(B) race-priority rule is designed to handle conflict between secured parties and "transferees."[440] "Transferees" are defined as those who acquire "any right or interest (other than a security interest) in, or ownership of, a Federal Intellectual Property Right."[441] Furthermore, both a "secured party" and a "lien creditor" are expressly excluded from the "transferee" definition.[442] Under the subsection (b)(2)(B) rule, a security interest is made "ineffective" against a transferee who records *"the document transferring ownership"* before the secured party files an effective federal financing statement (as long as the transferee records in the manner required for priority in the tract file).[443] Note that the "ineffectiveness" of a security interest in a federal intellectual property right that results from losing this federal race is not made applicable to the "proceeds" of the security interest in such right.[444] The language of FIPSA section 3(b)(2)(A) refers all disputes involving priority in "proceeds" to "applicable non-federal law."[445]

By itself the new federal race rule in section 3(b)(2)(B) works in an absolute sense only for the "transferee" who wins the race and can render the security interest "ineffective." The other side of "ineffectiveness" for the secured party who wins the federal race, however, is *not* a lock on priority against the transferee. The narrow FIPSA "race" rule is constructed as a limited exception to the generally applicable "default" priority rules for security interests provided for in subsection (b)(2)(A).[446] Under subsection (b)(2)(A), the default priority rules that apply in all other cases are found in "applicable non-federal law governing security interests in personal property."[447] Furthermore, this "applicable non-federal law" is made broadly applicable to all other priority disputes pitting security interests in federal intellectual property rights against "competing rights, *claims, and interests* therein and licenses thereof."[448] Because FIPSA's federal "race" rule for secured parties and "transferees" in (b)(2)(B) acts only to subordinate secured parties who lose the race, any negative inference would be unwarranted and unwise. At least in the case of patents, copyrights, and mask works, FIPSA does not, and probably should not, set out a conclusive federal first-to-file rule. FIPSA does, however, contain a more complete "race" rule for federal marks.[449]

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440. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 3(b)(2)(B).

441. *Id.* § 3(a).

442. *Id.*

443. *Id.* § 3(b)(2)(B).

444. *Id.* The Act does define "proceeds" to include "whatever is received or to be received by the owner or any other party from the transfer, disposition, license (whether or not exclusive), use or other exploitation of Federal Intellectual Property Rights, and includes (but is not limited to) the meaning given to 'proceeds' under applicable non-federal law." *Id.* § 3(a).

445. *Id.* § 3(b)(2)(A).

446. *Id.*

447. *Id.*

448. *Id.* (emphasis added).

449. *Id.* § 4(b).

With respect to patent collateral, a secured party who records first merely avoids "ineffectiveness" vis-à-vis a transferee by winning the race to the federal file—it *does not follow* that the secured party has priority. Such a secured party who escapes ineffectiveness under subsection (b)(2)(B) must look to the default priority rules in Article Nine for priority.[450] Priority may, in fact, be found in Article Nine section 9-301(1)(d) or in Revised Article Nine section 9-317(d).[451] Under the priority rule in either Article Nine version, the secured party wins as against the subsequent transferee/buyer if the secured party is perfected *under state law* before the transferee/buyer "gives value without knowledge of the security interest."[452] Therefore, a creditor with a security interest in a copyright, patent, or mask work who wins the race to the federal file with its federal financing statement can still lose if the competing "buyer" of the intellectual property *gave value for its ownership interest, free of knowledge, and before the secured party was perfected* under state law.[453] Note that the Article Nine rule protects even an unperfected secured party in some cases. If the secured party was unperfected under state law when the buyer of a "Federal Intellectual Property Right" gave value, the buyer's *knowledge* of the security interest would still give priority to the unperfected secured party under both section 9-301(1)(d) and Revised section 9-317(d).[454] Furthermore, once the buyer loses its BFP status, it may also lose any chance to render the security interest "ineffective" by subsequently winning the federal race.[455] Under one reading of the FIPSA language in section 3(b)(2)(B), a transferee cannot win the federal race unless it wins as a BFP. Section 3(b)(2)(B) requires that the transferee's recording be "in the manner required under applicable federal law . . . to give priority to such transferee's interest."[456]

However, the FIPSA race rule in section 3(b)(2) plays out differently when the collateral is a federal mark. Language added by FIPSA section 4(b) to section 1060 of the Lanham Act seems to trump the generally applicable deferral to "nonfederal law" in subsection (b)(2)(A) whenever the secured party with federal trademark collateral wins the race to the federal file.[457] As amended by FIPSA, section 1060 provides that assignees of a federal mark "shall be subject to the rights of any secured party who has filed a federal financing statement prior to the date of filing of such assignment."[458] An unrecorded trademark assignment is thus expressly made subject to a prior filed secured party. When coupled with the rule in FIPSA section 3(b)(2)(B) making security interests that lose the federal race "ineffective," the amendments to section 1060 produce a complete two-way race rule for marks. As between the transferee of an ownership interest and a secured party, the first to file or record seems to win outright.

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450. The default rule in FIPSA subsection (b)(2)(B) clearly refers to the applicable Article Nine priority rule. *Id.* § 2(a)(3).

451. U.C.C. § 9-301(1)(d) (1995); U.C.C. [Revised] § 9-317(d) (2000).

452. *Id.*

453. *Id.*

454. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY Act, *supra* note 391, § 3(b)(2)(B).

455. *Id.*

456. *Id.* This "manner required" language could refer only to the mechanics of recording not the status of the recorder for federal BFP purposes. The FIPSA language should be clearer on this point.

457. *Id.* § 4(b).

458. *Id.*

This disjointed but nevertheless exclusive race rule for marks contains none of the priority rule refinements found in Article Nine. For example, no express allowance is made for authorized assignments from the debtor. Under Article Nine, an assignee who takes after the secured party that has perfected by filing will still prevail if the secured party has authorized the assignment free of its interest—whether such authorization is derived from the security agreement or otherwise.[459] Perhaps the courts would graft an estoppel-based exception onto FIPSA's federal race rule for marks that would provide priority for authorized assignees. Nevertheless, such a significant qualification on first-in-time priority should be express. Authorized transfers are expressly accounted for under FIPSA's proposed one-way race rule for copyrights, patents, and mask works because Article Nine (with all its priority serving nuances) remains in play even after the secured party has avoided section 3(b)(2)(B) "ineffectiveness" by winning the federal race.[460] When copyright or patent collateral is involved, priority ultimately depends on the FIPSA deferral to Article Nine perfection and all the rights and limitations that flow from Article Nine perfection.

Even if the added federal race dimension in the case of federal marks is a good idea, however, it is not properly accounted for in the deferral language as it presently stands in FIPSA section 3(b)(2)(A). The subsection (b)(2)(A) language that defers to Article Nine excepts from its operation only the federal race rule in subsection (b)(2)(B).[461] Again, proposed subsection (b)(2)(B) is a one-dimensional rule that merely renders security interests "ineffective" against earlier recording transferees.[462] Having this singular (b)(2)(B) exception from deferral in (b)(2)(A) works fine for copyrights, patents, and mask works because section 3(b)(2)(B) is the only federal priority rule in FIPSA that applies to these forms of federal intellectual property.[463] However, section 3(b)(2)(B) is only half of the FIPSA race priority rule applicable to Federal marks. The additional language in section 4(b) amending section 1060, and designed to make the federal race winner the outright winner, is the other half.[464] If the additional federal race language for section 1060 is retained, the final clause in section 3(b)(2)(A) needs to be expanded to include some mention of it as an exception from deferral.

From the transferee's perspective, a practical difficulty with the section 3(b)(2)(B) race rule (in all cases) is that the transferee remains at some risk until the document transferring ownership can be recorded. The secured party is not similarly at risk because it can file its federal financing statement in advance.[465] Perhaps the transferee who takes a transfer of ownership prior to the secured party's filing of a federal financing statement should be given a short grace period (e.g.,

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459. U.C.C. § 9-306(2) & cmt. 3 (1995); *see also* U.C.C. [Revised] § 9-315(a)(1) & cmt. 2 (2000).

460. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 3(b)(2)(B).

461. *Id.* § 3(b)(2)(A).

462. *Id.* § 3(b)(2)(B).

463. Remember, the secured party that wins the federal race does not always have priority under FIPSA because proposed section 3(b)(2)(A) defers to the Article Nine default rule when the transaction is not controlled by the narrow "ineffectiveness" language of section 3(b)(2)(B). *See* discussion *supra* notes 420-39 and accompanying text.

464. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 4(b).

465. *Id.* § 3(b)(3)(C).

ten days) after the transfer to record in the tract file. Filing within the grace period would then relate back to the date of the ownership transfer. The secured party can adjust to this short grace period by recording its financing statement beforehand and by not releasing funds until the short grace period runs its course.[466]

C. What Is Needed: Federal Coordination and State Cooperation in the Creation of a Single Database or Index of Databases

FIPSA contains very important language in section 3(d) that provides for the coordination of federal filing systems and procedures.[467] This coordination could include "the creation of a single database or index of databases, a uniform form of federal financing statement, and/or a single place of filing of federal financing statements covering copyrights, patents, federal marks, or mask works."[468] The Author of this summary believes that a single (either federal or integrated multi-state) national database for security interests in intellectual property is very compelling. The ability to describe intellectual property by *type* (i.e., "general intangibles") within a notice filing system argues for such a consolidated file.[469] Any single security agreement may cover many types of intellectual property including, in all likelihood, more than one type of *federal* intellectual property. The financing statement filed for that same transaction may cast an even wider net over the debtor's collateral. A typical financing statement is designed to cover, and thus perfect, both existing and after-acquired property.[470] Some inventive concepts may eventually take a protected federal form but have not matured to that point at the time of the security agreement. There are some clear advantages to a central integrated national database covering security interests in federal intellectual property that did not displace Article Nine.

One model for such an integrated national file would be a separate federally-managed database (such as the one created under FIPSA).[471] This single federal file would be accessible to the states so as to allow financing statements to be filed in or referred to in the database. Although this model requires the creation of a duplicate federal filing apparatus, it would preserve the basic integrity of the carefully crafted state-law-based Article Nine perfection and priority scheme. At the same time, such a database would make one convenient national search possible

466. As already noted, the "buyer" who "buys" as a BFP before the secured party files in the federal file but who then loses the race to the federal file, is still protected if the secured party failed to file in the appropriate Article Nine file prior to the "buying." U.C.C. section 9-301(1)(d) would apply and protect the BFP buyer. U.C.C. § 9-301(1)(d) (1995); U.C.C. [Revised] § 9-317(d) (2000). However, the buyer who resorts only to the federal file would be unlikely to run a check for state filings. This is another example of the limitations of a dual filing system. Perhaps FIPSA's federal filing should also work as a step-back *state filing* for all forms of intellectual property.

467. TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 3(d).

468. *Id.*

469. *Id.* § 3(b)(3)(B) ("In describing the collateral, a general reference to 'intellectual property' or 'general intangibles' shall be sufficient to describe all of the debtor's interests in all Federal Intellectual Property Rights."); *see also* U.C.C. § 9-402(1) (1995); U.C.C. [Revised] §§ 9-502, 9-504, 9-108(b)(3) (2000).

470. *See* TASK FORCE DRAFT—FEDERAL INTELLECTUAL PROPERTY SECURITY ACT, *supra* note 391, § 3(b)(3)(C).

471. *See id.* § 3(b)(3)-(7).

for intellectual property collateral of all types (state and federal). Such a database could be configured to protect against expensive filing and searching mistakes inherent in a multiple jurisdiction filing scheme that covers intellectual property collateral that may change "form" (e.g., trade secret to patent application) in the hands of debtors who may change "location" without physical movement (e.g., change in organizational structure).

The integrated national file need not be "federal," however. If the current state financing statement indexes could be electronically combined in one national meta-site, then all financing statements covering "general intangibles" could be accessed by key strokes or clicks from within the federal title records for copyrights, patents, and trademarks. This integrated multi-state solution is presently being investigated in a study commissioned by the United States Patent and Trademark Office.[472]

Integration of the federal intellectual property title records and the state Article Nine files for security interests under one of these national models is likely within the next two years. When integration is achieved an important structural barrier to the efficient financing of these important business assets will finally be removed.

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472. *See* Agreement By and Between Franklin Pierce Law Center and University of Maine School of Law, app. I (Nov. 11, 1999) (Memorandum of Understanding Between the U.S. Department of Commerces [sic] Patent and Trademark Office and Franklin Pierce Law Center) (on file with the Author).