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The author addresses a hypothetical securitization limited to intellectual property assets in the United States, and he discusses assigning ownership and filing liens with respect to trademarks, patents, copyrights and domain names, and other types of IP.

Desperately Seeking Security: Whole Business Securitization and Intellectual Property

By William M. Ried

I. INTRODUCTION

A whole business securitization, also known as a "WBS transaction," provides a means for a company to obtain cost-effective financing or for a company's equity holders to extract value from their holdings without selling their interest in or giving up operational control of the company. In a typical WBS transaction, an operating company ("GlobalCo") creates a special-purpose entity (the "SPE"), which is structured to be bankruptcy-remote from GlobalCo. GlobalCo sells or contributes certain assets necessary to operate its business into the SPE and the SPE engages GlobalCo to operate the business and licenses back to GlobalCo the assets necessary to operate its business as the SPE's operating agent. The SPE then issues bonds backed by the cash flow from its assets and secured by its assets. The SPE either distributes the proceeds from the issuance to GlobalCo or uses the proceeds to purchase the operating assets from GlobalCo. Upon the SPE's repayment of the bonds, the SPE may distribute its assets back to GlobalCo.

The securitization of a large company may involve all kinds of assets located around the world. Often this kind of transaction will focus on intellectual property assets. It is possible to assign and record security interests in IP assets in most countries most of the time, but this process can be time-consuming and expensive.[1] As

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[1] Some countries restrict the assignment of IP or who may own various kinds of IP, require waiting periods following assignments, or mandate a particular order to assignments. Other countries impose stamp taxes on the value of assigned IP. Many countries do not permit the recordation of security

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an introduction, therefore, this article will address a hypothetical securitization (''Project WBS'') limited to IP assets in the United States. Assignment of these IP assets will be straightforward. A combination of state Uniform Commercial Code filings and federal filings will perfect the security interest granted by the SPE to the bondholders (the ''Secured Parties'') in the SPE's patents, trademarks, trade secrets and copyrights, and any uncertainty about perfecting the Secured Parties' security interest in the SPE's domain name rights will be cleared up through an agreement locking down control of domain name registration rights.

II. ASSIGNING OWNERSHIP

A. *Trademarks.* Federal trademark and service mark (referred to herein, collectively, as ''trademark'') applications and registrations are subject to the Trademark Act of 1946 (the ''Lanham Act''),[2] which requires assignments of applications and registrations to be recorded in the U.S. Patent and Trademark Office.[3] An assignment recorded in the PTO will be effective against a subsequent purchaser for valuable consideration without notice of the assignment (a ''bona fide purchaser'') if recorded within three months of execution of the grant or prior to purchase by the bona fide purchaser.[4]

An application filed on the basis of an intention to use the mark (an ''ITU application''),[5] as opposed to use in commerce, cannot be assigned prior to filing evidence of use of the mark unless the application is transferred along with the business of the seller associated with the mark.[6] Thus, ITU applications will be carved out of the initial transfers in Project WBS and made subject to a contractual obligation of GlobalCo to hold and maintain these applications beneficially for the SPE and to transfer them to the SPE if and when this becomes possible, because an application either registers or is amended to a use basis.

B. *Patents.* The assignment of patents and patent applications is subject to the Patent Act of 1952.[7] Like a trademark assignment, a patent assignment will be effective against a bona fide purchaser if recorded with the PTO within three months of execution of the grant or prior to purchase by a bona fide purchaser.[8] However, unlike trademarks, patents are in the first instance owned by their individual inventors rather than the inventors' employers,[9] so it will be necessary to obtain and file an assignment from at least one inventor to GlobalCo prior to recording the assignment of each patent to the SPE.[10]

C. *Copyrights.* Copyrights are subject to the Copyright Act of 1976.[11] The assignment of a copyright application or registration is effective against a bona fide purchaser if recorded with the Copyright Office within one month of execution in the United States or within two months of execution if executed outside the United States.[12]

However, rights *arising out of* a copyright, such as the right to receive royalties from the performance of a copyrighted work, are assigned by contract and need not be recorded in the Copyright Office to be effective.[13] The Ninth Circuit has explained that an agreement concerning royalties is not a ''transfer of copyright ownership'' under the Copyright Act,[14] nor is it an assignment or ''other document pertaining to a copyright,'' which the Copyright Act defines as a potentially recordable document.[15] The priority of competing transfers of any interest in a copyright that do not transfer a copyright or any of the exclusive rights comprised in a copyright thus will be governed by state contract law.[16]

D. *Domain Names.* Domain name rights arise by contract between the registrant and the registrar, pursuant to rules set forth by the Internet Corporation for Assigned Names and Numbers, or ICANN.[17] As such, the assignment of a domain name is governed by the parties' contract and the rules of the particular registrar.

A generic top-level domain (''gTLD'') is a domain name ending in a suffix, such as ''<.com>,'' ''<.net>,''

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interests in general intangibles, or specifically in domain names or trademark applications. Some countries do not permit the local recordation of security interests at all while others restrict what types of liens can be recorded. Stamp taxes and fees for filing security agreements are sometimes based upon the value of the local IP assets collateralized.

[2] Trademark Act of 1946, 15 U.S.C §§ 1051-1141 (2006).

[3] 15 U.S.C. § 1060(a)(3).

[4] 15 U.S.C. § 1060(a)(4).

[5] An ITU application is filed under 15 U.S.C. § 1051(b).

[6] 15 U.S.C. § 1060(a)(1). *See Clorox v. Chemical Bank*, 40 USPQ 2d 1098, 1100, 1106 (TTAB 1996) (citing 15 U.S.C. § 1060) (even a conditional assignment of an ITU application was an assignment in violation of federal trademark law, leading to cancellation of the registration into which the application matured). Evidence of use can be submitted with an amendment of the application to a use basis, 15 U.S.C. § 1051(c), or with a statement of use filed after issuance of a notice of allowance, 15 U.S.C. § 1051(d).

[7] 35 U.S.C. §§ 1-376 (2006).

[8] 35 U.S.C. § 261.

[9] 35 U.S.C. § 111(a)(1).

[10] 35 U.S.C. § 116, *but see* 35 U.S.C. § 118 (providing for assignee to file a patent application at the discretion of the PTO director when the inventor refuses to execute an application or cannot be found).

[11] 17 U.S.C. §§ 101-1331 (2006).

[12] 17 U.S.C. § 205(d). Mask works are addressed under 17 U.S.C. §§ 901-914. Recordation of assignment of a mask work in the Copyright Office gives all persons constructive notice, 17 U.S.C. § 903(c)(1), but is *not* a condition to an effective transfer. *See* Melville B. Nimmer & David Nimmer, *Nimmer on Copyright* § 8A.08[C] (Matthew Bender & Co. 2008). Moreover, a subsequent transfer of a mask work to a bona fide purchaser will take priority over a prior recorded transfer unless the prior transfer is recorded within three months of execution and at least one day prior to execution of the subsequent transfer. 17 U.S.C. § 903(c)(2). The transferee of a mask work thus has no certainty of prevailing over a subsequent transferee unless it records its transfer the same day it is executed and maintains surveillance for the day to confirm that the transferor does not execute a subsequent transfer. *See* Nimmer § 8A.08[D].

[13] *See Broadcast Music Inc. v. Hirsch*, 104 F.3d 1163, 1167-8 (9th Cir. 1997).

[14] *Id.* at 1166 (citing *Papa's-June Music Inc. v. McLean*, 921 F. Supp. 1154, 1160 (SDNY 1996)).

[15] *Broadcast Music,* 104 F.3d at 1166 (citing 17 U.S.C. § 205(a)).

[16] *See id.* at 1167.

[17] ICANN was created as a nonprofit corporation in 1998 to oversee Internet-related tasks, including the assignment of domain names and IP addresses. *See* <http:/www.icann.org/about/> (last viewed May 13, 2008).

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''<.org>,'' ''<.biz>'' or ''<.info>,'' which can be assigned by any accredited registrar worldwide. A country code top-level domain (''ccTLD'') is a domain name ending in a country-specific suffix, such as ''<.us>'' in the United States or ''<.de>'' in Germany, which can be assigned only by a registrar in that country. Web sites linked to both gTLDs and ccTLDs are accessible by Internet users worldwide.

The administrative contact listed for GlobalCo's domain name registrations can instruct the assignment of each gTLD or <.us> ccTLD by completing the registrar's online form and paying a small fee. The parties can confirm transfers of ownership by viewing and printing the ''WHOIS'' information available through many sources online.[18]

E. *State Trademarks.* While federal trademark registrations have nationwide effect, most states also provide for registration of marks enforceable in varying degrees only within such states.[19] An assignment of a state trademark thus will be recorded in the appropriate state trademark office.[20]

F. *Other Common Law IP.* Other IP arising under state common law, such as trade secrets or common law trademarks used only intrastate, are governed by state law but are subject to no recording regime. Assignment of such rights takes place pursuant to contract, with no public notice.

III. FILING LIENS

Article 9 of the UCC provides that a lien can be created and perfected in almost any kind of personal property that is reasonably identified other than certain property delineated as exceptions therein.[21] Personal property includes ''general intangibles,'' which is a basket for all personal property that is not excluded by Article 9 and does not fall within another Article 9 collateral category (*i.e.*, all Article 9 collateral other than accounts, chattel paper, commercial tort claims, deposit accounts, documents, goods, instruments, investment property, letter-of-credit rights, letters of credit, money, and oil, gas, and other minerals before extraction).[22] While trademarks, patents and copyrights are not specifically mentioned in Article 9, the Offical Comment to UCC § 9-102 uses the term ''intellectual property'' as an example of a general intangible,[23] and ''intellectual property'' is widely understood to encompass trademarks, patents and copyrights. Thus, a lien under the UCC will ''attach,'' or become enforceable against, trademarks, copyrights, patents and other IP rights through the execution of a security agreement in which the secured party gives value for a security interest in the debtor's collateral.[24] A security interest is then ''perfected'' by filing centrally in the correct jurisdiction a financing statement in the debtor's exact name.[25] Perfection of a security interest in a general intangible under the UCC provides the perfected party priority over a bona fide purchaser,[26] unless the UCC is preempted by a federal law, statute, regulation or treaty or unless another statute of a state, foreign government or governmental unit of a state expressly governs a security interest created by such governmental unit.[27]

A. *Trademarks.* The Lanham Act provides for filing an assignment of a trademark application or registration, but the definition of ''assignment'' does not include pledges, mortgages or hypothecations.[28] A security interest in a federal trademark thus cannot be perfected by filing under the Lanham Act, but instead can be perfected only under the UCC.[29]

Nonetheless, the PTO will accept for filing security agreements or short-form notices of security interests and the SPE's lenders insist that this be done in Project WBS. Recordation in the PTO gives constructive notice to prospective purchasers or lenders that may not review the proper UCC filing. Recordation also could give actual notice to a prospective purchaser or mortgagee that actually searches the PTO records.[30] In any event, recording the lien in the PTO serves as a hedge against any possible change in the law.[31]

B. *Patents.* Similarly, courts have held that the Patent Act *does not* preempt the UCC in regard to perfecting security interests in patents and patent applications.[32] However, courts have viewed recording in the PTO as necessary to defeat a claim of a bona fide purchaser.[33] That is, a bona fide purchaser,[34] without notice of the prior security interest, will take title to the patent free of any prior security interest that was not recorded in the PTO within three months of execution.[35]

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[18] WHOIS information is available, for example, at <http://www.domainwhitepages.com>; or <http://www.dnsstuff.com>.

[19] For example, New York state trademarks are registrable pursuant to New York General Business Law §§ 360-360-r.

[20] For example, New York State trademarks are registered with the New York secretary of state. *See* N.Y. Gen. Bus. Law § 360-f.

[21] U.C.C. § 9-109 (2001).

[22] U.C.C. § 9-102(a)(42).

[23] *See* Official Comment, U.C.C. § 9-102 5(d).

[24] U.C.C. § 9-203.

[25] U.C.C. § 9-301.

[26] U.C.C. § 9-317.

[27] U.C.C. § 9-109(c).

[28] *See Joseph v. 1200 Valencia Inc. (In re 199Z Inc.)*, 137 B.R. 778, 782 (Bankr. C.D. Cal. 1992).

[29] *See, e.g.*, *In re Together Development Corp.*, 227 B.R. 439, 441 (Bankr. D. Mass. Dec. 4, 1998).

[30] *See Moldo v. Matsco Inc. (In re Cybernetic Services Inc.)*, 239 B.R. 917, 921 n.10 (B.A.P. 9th Cir. 1999), aff'd, 252 F.3d 1039 (9th Cir. 2001).

[31] *See, e.g.*, Daniel A. Scola & Robert F. Chisholm, ''IP As Collateral Presents Securitization Problems,'' *National Law Journal*, Jan. 27, 1997, at C15, C17 (''While there is no legal effect to [filing a security interest in trademarks with the PTO], recording security interests at the PTO is recommended in anticipation of future statutory or judicial recognition of such recordings.'')

[32] *See, e.g.*, *In re Transportation Design & Technology Inc.*, 48 B.R. 635, 638-40 (Bankr. S.D. Cal 1985); *City Bank & Trust Co. v. Otto Fabrics Inc.*, 83 B.R. 780, 782-83 (D. Kan. 1988).

[33] *See, e.g.*, *In re Cybernetic Services Inc.*, 239 B.R. 917; *In re Transportation Design & Tech. Inc.*, at 639.

[34] As used in the Patent Act, ''mortgage'' refers to a chattel mortgage, under which title to the patent is assigned to the creditor until the underlying debt is repaid, at which point title is reassigned to the debtor. As a security interest leaves title with the debtor, a secured party is neither a ''purchaser'' nor a ''mortgagee'' and thus a creditor need not record its security interest in the PTO to preserve its priority over a subsequent security interest. *See, e.g., In re Transportation Design & Tech Inc.*, at 639.

[35] 35 U.S.C. § 261 (2006).

A security interest in a federal patent, however, cannot be perfected by filing under the Patent Act, but instead can be perfected only by filing a UCC financing statement centrally in the proper jurisdiction.

C. *Copyrights.* The Copyright Act expressly provides for recordation in the Copyright Office of any ''transfer'' of copyright ownership,[36] which includes any ''mortgage'' or ''hypothecation'' of a copyright,[37] including a pledge of the copyright as security or collateral for a debt.[38] In addition, the Copyright Act provides that recordation in the Copyright Office of any transfer of copyright ownership gives constructive notice of the facts in the recordation of a specifically identified and registered work.[39] Thus, the Copyright Act *does* preempt the UCC as to perfecting security interests in registered copyrights.[40]

However, the UCC is not preempted by the Copyright Act as to recording security interests in unregistered copyrights, including copyright applications.[41] Copyrightable works in progress, such as motion pictures during production, thus must be secured under the UCC. Similarly, an assignment to creditors of an interest in copyright royalties is not a transfer of ownership and must be secured under the UCC rather than in the Copyright Office.[42] Because the value of GlobalCo's business depends more upon trademarks than copyrights, the lenders in Project WBS did not insist that GlobalCo apply for copyright registration of all copyrightable works so that they could be covered by a Copyright Office lien.

D. *State Law Rights.* Security interests in IP governed by state statutes or common law are perfected by filing a UCC financing statement centrally in the proper jurisdiction as indicated by Article 9 of the UCC.[43] Such IP includes trade secrets, common law trademarks used only in intrastate commerce and state trademark registrations.

E. *Domain names.* Because domain name rights arise by contract between the registrant and the registrar under the rules of ICANN, rather than under a statute or the common law, some courts view a domain name as a contract right rather than personal property.[44] In addition, a domain name is typically assignable pursuant to the registrar's online procedures, but any other assignment may be restricted by the terms of the registration agreement.[45]

A domain name registration appears to fall within the UCC definition of ''general intangibles,''[46] which would permit the creation of a security interest in a domain name.[47] However, the secured party still faces two problems: (i) how to prevent the borrower from transferring an encumbered domain name; and (ii) how to enforce a security interest in a domain name against a registrar that has no duty to the secured party.[48]

The solution in Project WBS will be to execute a domain name control agreement among the SPE, the secured party and the registrar. This agreement will require the secured party's consent to any transfer or cancellation of the domain names, and permit the secured party to transfer the domain names upon a default under the transaction agreements. Of course, the registrar must be willing to participate in the negotiation of and performance under this agreement, and can be expected to charge additional fees for these services, but such domain name control agreements have been successfully negotiated. Given the large number of domain names originally owned by GlobalCo, the control agreement in Project WBS will focus its restrictions on ''core'' domain names of central importance to the SPE business, which are those few that point to active Web sites. This focus will minimize extra fees payable to the registrar, and give GlobalCo as the SPE's agent some discretion in managing domain names held for defensive purposes or in regard to shifting marketing efforts.

F. *Additional Considerations.* The lenders' goal of securing IP in the United States may be affected by additional issues involving IP validity, existing licenses and statutory look-back periods.

First, the validity and enforceability of IP is not always apparent from registration status. Registration is only *prima facie* evidence of validity, which may to varying degrees be rebutted.[49] Without a court judgment enforcing a patent, trademark or copyright, it may be difficult to assess whether it would withstand a challenge to its validity. In the case of trademarks, moreover, being validly registered does not assure that the mark will be deemed strong when asserted in an en-

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[36] 17 U.S.C. § 205(a) (2006).

[37] 17 U.S.C. § 101. *Joseph v. 1200 Valencia Inc. (In re 199Z Inc.)*, at 782 (*citing In re Peregrine Entertainment*, 116 B.R. 194, 198-99 (C.D. Cal. 1990) (Kozinski, J.)).

[38] 17 U.S.C. § 205(c).

[39] *See, e.g., In re Peregrine Entertainment Ltd.*, 116 B.R. at 203.

[40] *See, e.g., Aerocon Eng'g Inc. v. Silicon Valley Bank*, 303 F.3d 1120, 1130 (9th Cir. 2002); *Official Unsecured Creditors' Comm. v. Zenith Prod. Ltd.*, 127 B.R. 34, 40-41 (Bankr. C.D. Cal. 1991), *aff'd*, 161 B.R. 50, 58 (B.A.P. 9th Cir. 1993); *In re Avalon Software Inc.*, 209 B.R. 517, 522-23 (Bankr. D. Ariz. 1997). Lenders can take some comfort in the fact that a copyright will typically register in approximately 5-8 months after the application is filed, as compared to 14-18 months for trademarks with no impediments and several years for patents.

[41] *See, e.g., In re World Auxiliary Power Co.*, 244 B.R. 149, 155-56 (Bankr. N.D. Cal. 1999).

[42] *See, e.g., Broadcast Music Inc. v. Hirsch*, 104 F.3d at 1166-67.

[43] U.C.C. § 9-301 (2001).

[44] *See, e.g., Dorer v. Arel*, 60 F. Supp. 2d 558, 561 (E.D. Va. 1999); *Network Solutions Inc. v. Umbro Int'l Inc.*, 529 S.E.2d 80, 86 (Va. 2000); *But see Kreman v. Cohen*, 337 F.3d 1024 (9th Cir. 2003); *Office Depot v. Zuccarini*, 2007 WL 2688460 (N.D. Cal. 2007).

[45] Both the standard Network Solutions and Register.com domain name registration agreements provide that rights under the agreements are not assignable or transferable except as provided, and any attempt by creditors to obtain an interest in rights under an agreement, whether by attachment, levy, garnishment or otherwise, renders the agreement voidable at the registrar's option. *See* <http://www.networksolutions.com/legal/static-service-agreement.jsP>; and <http://www.register.com/policy/servicesagreement.rcmx>; (last viewed May 30, 2008).

[46] U.C.C. § 9-102(a)(42).

[47] U.C.C. § 9-109.

[48] *See generally*, Margie Milam & Jeffrey S. Rothstein, ''Security Interests in Domain Names,'' *The Secured Lender*, vol. 59 Issue 6, Nov./Dec. 2003, at 26.

[49] *See, e.g.*, 35 U.S.C. § 282 (2006) (patents); 17 U.S.C. § 410(c) (2006) (copyrights); and 15 U.S.C. § 1064 (2006) (trademarks, but a mark that is ''incontestable'' under 15 U.S.C. § 1065 cannot be attacked except upon limited grounds).

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forcement action.[50] Similarly, the registration of a domain name demonstrates only that the registrant was the first to file and may be vulnerable to claims by the owners of trademarks included in the domain name.[51]

Second, IP may be valid, enforceable and subject to no prior lien and yet have diminished value because it is encumbered by existing licenses to third parties. Exclusive or nonexclusive licenses of patents, trademarks or copyrights may or may not be recorded[52] but in either event may limit the value of the secured property.

Finally, statutory look-back periods create the possibility that a prior lien may be recorded after a lender's security interest but still take priority over this interest.[53] For example, a security interest in a trademark filed within three months of execution will take priority over a subsequent security interest that is filed first. Thus, a lender filing a security interest in a trademark executed and recorded July 15 will not know until October 15 whether a prior security interest that takes priority over the lender's security interest has been filed. The register of copyrights has testified that the grace period permitted for recording transfers of copyrights ''means that a prospective purchaser cannot be completely certain that the silence of the record assures his protection . . . and the later recordation of the prior purchase will defeat him if it takes place within one month after its execution.''[54] Contractual warranties can address this vulnerability, but the only way for a lender to be certain it has a first priority security interest is to delay funding until after the conclusion of the applicable look-back period.

Additional considerations impact particular types of IP.[55] For example, a copyright is an intangible right to reproduce, distribute, publicly display or perform, and create derivative rights from a work,[56] which is separate from any rights in media embodying the work.[57] Thus, the lenders' security interest in the SPE's copyrights will not reach any inventory of books, films or software programs embodying such copyrights. In contrast, a trademark is a source identifier protected against use by a third party of a confusingly similar mark, and cannot be assigned without the associated goodwill,[58] so in order to foreclose on its security interest in the SPE's trademarks, the lenders must also secure other assets of the SPE sufficient to produce the goods and provide the GlobalCo services under these marks.[59]

IV. CONCLUSION

Because Project WBS requires assigning and securing GlobalCo's IP assets only in the United States, the parties can accomplish these steps with minimal complications. This will permit GlobalCo's owners to extract value from their holdings while continuing to run day-to-day operations and, upon repayment of bonds, to regain complete control of GlobalCo.

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[50] A mark can be enforced against a junior mark that creates a likelihood of confusion, which enforcement is assessed in terms of a number of factors, including the strength of the senior mark. *See, e.g., Polaroid Corp v. Polorad Electronics Corp.*, 287 F.2d 492, 495 (2d Cir. 1961), *cert. denied*, 368 U.S. 820 (1961) (Second Circuit factors applied).

[51] *See ICANN, Uniform Domain Name Dispute Resolution Policy*, Paragraph 4(a)(i) (Oct. 24, 1999) <http://www.icann.org/udrp/udrp-policy-24oct99.htm>.

[52] *See* 35 U.S.C. § 261 (exclusive rights in patents); 15 U.S.C. § 1060(a)(5) (trademarks); and 17 U.S.C. § 205 (copyrights).

[53] *See* 15 U.S.C. § 1060(a)(4) (three-month look-back period to file security interest against trademarks); 35 U.S.C. § 261 (three months - patents); and 17 U.S.C. § 205(d) (one to two months - copyrights).

[54] Statement of Marybeth Peters, the Register of Copyrights, before the Subcommittee on Courts and Intellectual Property, Committee on the Judiciary, U.S. House of Representatives, 106th Congress, 1st Session, at 5 (June 24, 1999).

[55] *See generally* Melvyn Simensky & Lanning G. Breyerand, *The New Role of Intellectual Property in Commercial Transactions* § 14.5(a) (John Wiley and Sons, Inc. 1994).

[56] 17 U.S.C. § 106.

[57] 17 U.S.C. § 202.

[58] 15 U.S.C. § 1060(a)(1).

[59] *See, e.g., Haymaker Sports Inc. v. Turian*, 581 F.2d 257, 260-62 (CCPA 1978); *Matter of Roman Cleanser Co.*, 802 F.2d 207, 208-09 (6th Cir. 1986).