A Malpractice Suit Waiting to Happen: The Conflict Between Perfecting Security Interests in Patents and Copyrights (A Note of Peregrine, Cybernetic and Their Progeny)

R. Scott Griffin
A MALPRACTICE SUIT WAITING TO HAPPEN: 
THE CONFLICT BETWEEN PERFECTING 
SECURITY INTERESTS IN PATENTS AND 
cOPYRIGHTS (A NOTE ON PEREGRINE, 
CYBERNETIC, AND THEIR PROGENY)

INTRODUCTION

As the song goes, "the times, they are a changin'."\(^1\) Modern businesses are using real property, such as buildings and other physical property, less frequently to secure financing.\(^2\) The collateral of choice for the 21st century is intellectual property, which causes problems as debtors find themselves in bankruptcy.\(^3\) How does a creditor take back something that, by definition, cannot be physically possessed, and how does that creditor know he is protected? In today's world, the answers do not come easily.\(^4\)

Intellectual property ("IP") is "[a] category of intangible rights protecting commercially valuable products of the human intellect ... comprise[d] primarily [by] trademark, copyright, and patent rights."\(^5\) It is an intangible type of personal property, a product of the mind, for which the owner possesses rights to prevent others from taking advantage of the IP's benefit without his permission.\(^6\)

A security interest is "[a] property interest created by agreement or by operation of law to secure performance of an obligation."\(^7\) It is personal property used to secure financing, similar to a mortgage of real property.\(^8\) Article 9 of the Uniform Commercial Code ("UCC"),

---

3. See id. at 1649.
4. See id.
which most states have adopted as their local commercial law, created security interests. 9

Although IP primarily relates to the protection of ideas, and the security interest is a recent development of commercial law, the two were interwoven in an economy that raced forward on new technology. 10 In today’s commercial landscape, IP comprises an increasing share of corporate assets compared to physical, tangible assets. 11 Given the level of IP assets, companies are increasingly using those assets to secure financing from creditors in the form of Article 9 security interests. 12

Article 9 specifies that a creditor should register a security interest with the state (by filing a financing statement) when the interest is executed. 13 Registration ensures notice to subsequent creditors that a particular asset is encumbered. 14 It also “perfects” the interest and secures the creditor’s priority in the event the debtor declares bankruptcy. 15 However, federal statutes, including the Patent Act and the Copyright Act, provide for transfers of an IP interest. 16 When a creditor executes a security interest, he has to file to perfect it, and until recent court decisions from the Ninth Circuit, where to register and perfect an interest in a patent or a copyright was a mystery. 17

Moldo v. Matsco, Inc. (In re Cybernetic Services, Inc.) 18 and National Peregrine, Inc. v. Capitol Federal Savings and Loan Association of Denver (In re Peregrine Entertainment, Ltd.) 19 are two Ninth Circuit decisions (one by the circuit court, one by a circuit judge sitting by designation at the district court level) that established the circuit’s views on perfecting security interests in patents and in

10. See Haemmerli, supra note 2, at 1647-48.
11. See id. at 1647.
12. See id.
13. Id. at 1658-59.
14. Id.
15. Id. at 1657.
17. See Haemmerli, supra note 2, at 1659-60.
18. 252 F.3d 1039 (9th Cir. 2001), cert. denied, 534 U.S. 1130 (2002).
Both cases involved a bankruptcy where the major assets of the bankrupt company were IP, one involving a patent and the other involving a set of copyrights.

Cybernetic involved Matsco, Inc.'s ("Matsco") security interest in Cybernetic Services, Inc.'s patent, which was the company's major asset. Matsco registered its security interest with the Secretary of State of California as required by the California Commercial Code (California's adoption of the UCC) but did not register the interest with the Patent and Trademark Office ("PTO"). The bankruptcy court found that Matsco's filing with the Secretary of State perfected the security interest, thus giving Matsco priority over other creditors. The Bankruptcy Appeals Panel affirmed the decision. The Ninth Circuit affirmed the Bankruptcy Appeals Panel's decision and found that (1) the Patent Act's registration provision did not preempt state law and (2) national registration was not required to perfect a security interest.

In a nearly identical set of facts, Peregrine involved the Capitol Federal Savings and Loan Association of Denver's ("CapFed") security interest in a library of copyrights that National Peregrine, Inc. ("Peregrine") owned. Peregrine acquired the library of copyrights when it acquired another company, at which time the library was already encumbered by CapFed's security interest. Peregrine filed for bankruptcy and claimed that CapFed's security interest was unperfected. The bankruptcy court held that CapFed perfected its security interest with state registration. However, the district court reversed the decision on the grounds that the Copyright

20. See Cybernetic, 252 F.3d at 1058; Peregrine, 116 B.R. at 204.
21. Cybernetic, 252 F.3d at 1044; Peregrine, 116 B.R. at 197.
22. Cybernetic, 252 F.3d at 1044.
23. Id.
25. Id.
26. See id. at 1059.
28. Id. at 197.
29. Id. at 198.
30. Id.
Act’s recording provision, which was updated more recently than the Patent Act’s recording provision, required registration of a security interest with the U.S. Copyright Office ("Copyright Office") to perfect a security interest.  

This Note provides a background of perfecting security interests in patents and copyrights and the reasoning behind the courts’ decisions in that area. It discusses the courts’ analyses in holding that the Patent Act and the Copyright Act specify different methods for perfecting security interests.

Part I provides a basic overview of patent and copyright law and of Article 9. First, it discusses the basic concepts of those types of IP and the significance of ownership in them. Second, it discusses the law of Article 9 and the significance of perfecting a security interest.

Part II analyzes the Peregrine and Cybernetic decisions and their progeny to show the most recent developments in the law. It examines (1) the statutory registration schemes for copyrights and patents, (2) how courts interpret them, and (3) whether they preempt the UCC. This Part determines whether the courts were correct in their analyses and conclusions or if different results would have been more appropriate.

Part III discusses the morass created in the conflict between the federal statutes and Article 9. It questions whether the courts are correct in their holdings and suggests opportunities to clarify the law. Furthermore, it discusses the reasons for the differences in the interpretations of the Patent Act and the Copyright Act recording provisions. This Note will conclude that instead of simplifying the issues, courts have made them more confusing, and the U.S. Supreme
Court missed an opportunity to provide a structure when it denied certiorari in *Cybernetic*.\(^{38}\)

I. THE BASICS: DEFINING PATENTS, COPYRIGHTS, AND SECURITY INTERESTS

A. Intellectual Property

Federal protection of IP is grounded in the Constitution.\(^{39}\) Article I, section 8, clause 8 empowers Congress “[t]o promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries.”\(^{40}\) The Patent Act and the Copyright Act both spring from this authority.\(^{41}\) The Constitution’s reference to “Inventors” authorizes the Patent Act, and the term “Author” authorizes the Copyright Act.\(^{42}\) The Framers believed that protecting these ideas was important to provide an incentive to enrich society, and since then Congress has strived to balance these two purposes.\(^{43}\)

1. Patents

The constitutional purpose of a patent is to advance science by securing an inventor’s monopoly over the rights for a limited period of time.\(^{44}\) Through a contract with the inventor, a patent strikes a balance between enriching societal knowledge and creating an incentive to invent.\(^{45}\) This contract restricts others from making, using, or selling the invention for 20 years from filing the application in exchange for the inventor disclosing the details of the invention.\(^{46}\)
The Patent Act established the United States Patent and Trademark Office ("USPTO"). It defined the USPTO's duties as (1) issuing patents and trademarks, (2) disseminating information to the public, and (3) establishing the governing regulations. To obtain a patent, an inventor must submit an application to the USPTO.

The Patent Act specifies that "[w]hoever invents or discovers any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof, may obtain a patent." To obtain a patent, the inventor must show the USPTO that the improvement meets certain subject matter requirements. An inventor may obtain several types of patents: utility (a "new and useful process, machine, article of manufacture, composition of matter, or . . . improvement[] to such inventions"), plant (for asexually reproducing a plant), and design ("a new, original, and ornamental design for an article of manufacture"). Therefore, when a patentee meets the requirements for obtaining a patent, he possesses the "right to exclude" others from making, using, or selling the claimed invention" for 20 years.

A patent owner possesses the fundamental right to control who uses his invention, and the law permits him to "assign, grant, or convey" the patent in one of three ways. He may transfer "(1) the whole patent . . . , (2) an undivided part or share of that exclusive right, or (3) the exclusive right . . . within a [particular geographic area] of the United States." The assignee receives through any of these types of transfers both title to the patent and the right to sue for infringement. An owner may also create licenses to any or all of the exclusive rights to make, use, and sell the invention. The license

48. Id. § 2.
49. Hildreth, supra note 45, § 1:6.2.
51. See Stin, supra note 6, at 425.
52. Id. at 425, 428-29.
54. Id. § 1:8.3.
55. Id.
56. Id.
57. Id. § 1:8.4.
may provide for any combination of the three rights. A license does not represent a transfer of ownership; the patentee maintains the title.

2. Copyrights

A copyright, similar to a patent, is actually an exclusionary right to control who may exercise the "bundle of rights" that comes with creating a work. The Copyright Act protects "original works of authorship" and grants the author the exclusive rights of reproduction, production of derivative works, distribution of the work, performance, display, and public performance of sound recordings.

The only requirements for a copyright are that it (1) fit within the specified types of authorship ("copyrightable expression") defined in the statute, (2) possess originality, and (3) be fixed in a tangible medium. Copyright protection for works created after January 1, 1978 lasts for the life of the author plus 70 years, which is significantly longer than the 20-year patent life.

Ownership of a copyright attaches to the author at the time the work is fixed in a tangible medium, and the author is always the initial owner unless he was hired to create the work. The owner possesses title to all of the rights granted to him under the Copyright Act. An owner registering the copyright creates a prima facie presumption of ownership, and the ownership of the physical material is not equivalent to ownership of the copyright. Registration is significant in a suit for infringement. To file a suit for an

58. See id.
59. HILDERETH, supra note 45, § 1:8.4.
60. STIM, supra note 6, at 47.
62. id. § 106.
63. STIM, supra note 6, at 27.
65. STIM, supra note 6, at 80, 96. This applies to works created after January 1, 1978, under the Copyright Act of 1976. Id. Prior acts required publication and notice for the right to attach. Id. at 126.
66. Id. at 81.
67. Id.
68. See id. at 129.
infringement, the owner must register the copyright with the Copyright Office; registration is a requirement for the statutory damages provided in the Copyright Act.\textsuperscript{69}

Like other types of personal property, an owner may transfer his interest in a copyright by assignment or sale and may also license any of the individual rights that comprise a copyright (for example, to copy, to reproduce, to distribute, or to make derivative works).\textsuperscript{70} The Copyright Act also provides an extensive list of the types of transfers that may be registered with the Office, and this registration has generated confusion.\textsuperscript{71}

\textbf{B. Security Interests}

Article 9 of the UCC, as adopted by the individual states, governs secured transactions.\textsuperscript{72} The basic concept of Article 9 was to create one uniform security interest to take the place of the former, numerous types of security devices.\textsuperscript{73} The UCC defines a security interest as “an interest in personal property or fixtures which secures payment or performance of an obligation.”\textsuperscript{74} Generally, a security interest is a partial interest taken in a debtor’s asset—the collateral—to secure a loan.\textsuperscript{75} Two parties create a security interest when they sign a “security agreement”\textsuperscript{76} that states the interest in the collateral that the “secured party”\textsuperscript{77}—the creditor—will receive for the “value”\textsuperscript{78} he has given.\textsuperscript{79} Once created, “the security interest . . . ‘attaches’ to [the] existing collateral.”\textsuperscript{80}

\begin{itemize}
\item[\textsuperscript{69}] Id. Although the distinction between registered and unregistered copyrights does not affect the legal rights of authors or owners unless there is a suit for infringement, it is now an important element for perfecting a security interest. See discussion infra Part II.B.
\item[\textsuperscript{70}] STIM, supra note 6, at 81, 99.
\item[\textsuperscript{71}] See discussion infra Part III.A.
\item[\textsuperscript{72}] U.C.C. § 9-101 (2002). The majority of cases discussed in this article are from California, which has adopted the UCC as its state law governing transactions. CAL. U. COM. CODE § 9101 (Deering 2003). For simplicity, all references to the UCC and Article 9 discussed in this Note should be assumed to be the law of California.
\item[\textsuperscript{73}] See Ward, supra note 8, at 396.
\item[\textsuperscript{74}] U.C.C. § 1-201(37) (2002).
\item[\textsuperscript{75}] Hämmerli, supra note 2, at 1657.
\item[\textsuperscript{76}] U.C.C. § 9-102(73) (2002).
\item[\textsuperscript{77}] Id. § 9-102(72).
\item[\textsuperscript{78}] Id. § 1-201(44).
\end{itemize}
A MALPRACTICE SUIT WAITING TO HAPPEN

Article 9 requires filing security interests with the state to serve a dual purpose: (1) notify subsequent creditors that the collateral is encumbered and (2) establish priority for the secured party if the debtor files for bankruptcy. Although the policy seems straightforward, the notice function becomes complicated because federal schemes also exist to serve a constructive notice function that an IP right is encumbered; however, the federal statute may not clearly address the parties' rights.

A key feature to security interests is that they transfer a non-title interest in the property. Although it has been the commercial law for half a century, this aspect of security interests has a profound effect on the comparison and analysis of Article 9 and the federal IP statutes' registration provisions.

Article 9 "governs the method for perfecting a security interest in personal property." When a lender perfects its security interest by filing, it achieves priority, which is "the ability to assert that its interest ranks before those of other parties with claims to that property." Perfection, once achieved, defines the rights of a creditor versus other creditors.

However, when a federal statute expresses a filing requirement, the statute preempts state-law provisions for perfecting security interests. The Supremacy Clause of the Constitution establishes this doctrine. Furthermore, Article 9 subordinates itself if "a statute, regulation, or treaty of the United States preempts [the Article]." Thus, if a provision of a federal statute requires federal registration of a security interest, not only will federal law preempt Article 9, but the

---

79. Ward, supra note 8, at 396.
80. Id.
81. See id. at 396-97.
82. See discussion infra Parts II.A-B.
83. Haemmerli, supra note 2, at 1657.
84. See id. at 1657-60; discussion infra Part II.A.
86. Haemmerli, supra note 2, at 1657.
87. Id.
88. Id. at 1702.
89. U.S. CONST. art. VI, § 1, cl. 2.
UCC requires its own acquiescence.\textsuperscript{91} Although the Copyright Act more specifically states that security interests should be registered, whether either statute (the Copyright Act or the Patent Act) actually accomplishes what the UCC requires—specific, express preemption—is questionable.\textsuperscript{92} The UCC will not automatically defer to federal law unless specifically required to do so by a sufficient federal scheme.\textsuperscript{93} Therefore, the basic question that must be answered in both Cybernetic and Peregrine is whether the Patent Act or the Copyright Act, respectively, require federal registration of security interests for perfection and, as a consequence, preempt state law.\textsuperscript{94}

II. RECORDING PROVISIONS—THE STATUTES AND INTERPRETATION IN CASE LAW

A. Patents—History and the Influence of Cybernetic

Section 261 of the Patent Act specifies that “[a]n assignment, grant or conveyance shall be void as against any subsequent purchaser or mortgagee for a valuable consideration, without notice, unless it is recorded in the USPTO within three months from its date or prior to the date of such subsequent purchase or mortgage.”\textsuperscript{95} The Patent Act’s filing requirement contains two distinct prongs: (1) the type of conveyance and (2) the status of a subsequent third party purchasing interest in the patent.\textsuperscript{96} The Ninth Circuit determined in Cybernetic that this filing requirement did not apply to a security interest because no assignment or transfer of ownership or title occurred.\textsuperscript{97} However,

\textsuperscript{91} Haemmerli, \textit{supra} note 2, at 1661.

\textsuperscript{92} U.C.C. § 9-109 cmt. 8 (2002) (“Subsection (c)(1) recognizes explicitly that this Article defers to federal law only when and to the extent that it must—i.e., when federal law preempts it.”).

\textsuperscript{93} See Ward, \textit{supra} note 8, at 412.


\textsuperscript{96} See Jason E. Pauls, \textit{Priority and Perfection of a Security Interest in a Patent: Does the Patent Act Preempt the UCC?}, 103 COM. L.J. 450, 457 (1998). Although both requirements are important, this Note only focuses on the first requirement: whether a security interest is included in the type of interests that require filing with the USPTO.

\textsuperscript{97} See Cybernetic, 252 F.3d at 1052.
some scholars state that because the Patent Act gives patents "the attributes of personal property" and the recording provision uses the term "mortgagee," the Act recognizes a "security transfer." Ample debate exists over whether the Patent Act requires a party to register a security interest in a patent with the USPTO.

The first case to encounter the issue of a patent used as collateral to secure a debt was *Waterman v. Mackenzie*. The primary issue was whether the plaintiff/inventor had standing to sue for infringement. The status of a patent used as collateral for a debt was dispositive of the case. The plaintiff invented and obtained a patent for an improvement on fountain pens. He assigned all of the interest in the patent and invention to his wife and recorded the assignment with the USPTO shortly after he received the patent. The wife licensed the plaintiff to manufacture and sell the improvement, and she subsequently assigned the patent to a business—the creditor—for $6500. The agreement stipulated that the assignment would become null and void after either the wife or the plaintiff repaid the debt. The business assigned the entire patent to another party—the owner—and several years later the wife assigned and recorded her interest in the patent back to the plaintiff. The owner licensed the defendant to manufacture and sell the pens, and the plaintiff sued for infringement.

The case hinged on the status of the assignments from the wife to the business and from the business to the owner. The Court held that (1) the assignment from the wife to the business was simply to secure a debt and, therefore, a mortgage, and (2) the owner's interest

99. See discussion *infra* Part III.A.
100. 138 U.S. 252, 257-58 (1891).
101. *Id.* at 252, 255.
102. *Id.* at 255-56.
103. *Id.* at 252.
104. *Id.* at 253.
105. *Id.*
107. *Id.* at 253-54.
108. *Id.* at 252.
109. *Id.* at 257-58.
in the patent was subject to the mortgage regardless of whether the assignment specified it. Moreover, the title to the patent belonged to the owner, who had constructive possession because the assignment was registered with the Patent Office. Because the owner never assigned an interest back to the wife, her assignment to the plaintiff was invalid. Thus, the plaintiff lacked standing to sue for infringement because he did not possess an ownership interest in the patent.

If followed to its logical conclusion, Waterman supports the idea that security interests are included in the Patent Act’s registration provision. The Patent Act would therefore recognize the validity of securing a debt with a patent as collateral and registering that interest with the USPTO. Although Waterman is still valid and the similarity to a security interest is uncanny, the problem arises with the type of interest Waterman recognized compared with that of an Article 9 security interest. The Court in Waterman based its decision on a title theory of property, which Article 9, as its goal, eviscerated in the middle of the 20th century. Nevertheless, could the courts draw some parallels to resolve the confusion, or would that further complicate the issue?

Although Waterman appears to come close to authorizing filing a security interest with the USPTO, modern courts have held that Article 9 controls perfecting a security interest in a patent and that filing with the state is required. In Cybernetic, the Ninth Circuit

110. Id. at 258.
111. Id. at 260-61.
113. See id. at 261.
114. See Gilmore, supra note 98, § 13.4, at 417.
115. See id.
116. See Ward, supra note 8, at 398.
117. See id. A security interest is not a transfer of title to the property used as collateral. See Haemmerli, supra note 2, at 1657.
118. See discussion infra Part III.A.
119. See, e.g., Moldo v. Matsco, Inc. (In re Cybernetic Servs., Inc.), 252 F.3d 1039, 1045, 1059 (9th Cir. 2001), cert. denied, 534 U.S. 1130 (2002) (holding that § 261 of the Patent Act does not preempt Article 9 and that federal registration is not required to perfect a security interest in a patent); City Bank and Trust Co. v. Otto Fabric, Inc., 83 B.R. 780, 782 (D. Kan. 1988) (noting that the Patent Act does not state a security interest must be filed with the USPTO to perfect it and that Congress amended the statute since the “advent of modern commercial law”).
Court of Appeals held that the Patent Act does not require USPTO registration to perfect a security interest; Article 9 controls and only requires state registration. Petitioners Matsco, Inc. and Matsco Financial Corporation held a security interest in a patent that Cybernetic Services, Inc. ("CSI") owned. Matsco recorded the security interest with the state of California but not with the USPTO. CSI’s creditors filed involuntary bankruptcy proceedings, and CSI’s primary asset was the patent. Matsco attempted to assert its priority with the security interest. The bankruptcy court found that Matsco had perfected its interest by filing with the state, and the Bankruptcy Appeals Panel affirmed the decision. The bankruptcy trustee, representing those creditors who had forced CSI into bankruptcy, argued that the petitioners had to file their interest with the USPTO to perfect it, but the Ninth Circuit disagreed. The court examined the Patent Act’s language and meaning when it was written in 1870 to determine that Congress did not intend a filing scheme for a non-ownership interest.

While it seems clear that the Copyright Act requires filing with the Copyright Office to perfect a security interest, authorities disagree as to whether the Patent Act similarly requires a filing to perfect a security interest. To support the argument that the Patent Act does not cover security interests, some authorities point to language in the Act that specifies that assignments (a transfer of title) must be registered and argue that a security interest is nothing more than a

120. Cybernetic, 252 F.3d at 1058-59.
121. Id. at 1044.
122. Id.
123. Id.
124. Id.
125. Id. at 1044.
126. Cybernetic, 252 F.3d at 1044, 1052.
127. Id. at 1048-52.
128. Compare Haemmerli, supra note 2, at 1668-69 (stating that the Patent Act does not preempt state law filing requirements for perfection of a security interest because it does not provide a filing requirement), and Jason A. Kidd, Note, The Ninth Circuit Falls Short While Establishing the Proper Perfection Method for Security Interests in Patents in In Re Cybernetic Services, 36 CREIGHTON L. REV. 669, 711 (2003) (citing the Ninth Circuit’s very narrow reading of the Patent Act’s filing provision), with Gilmore, supra note 98, § 13.4, at 417 (stating that because a patent has "attributes of personal property" and because an unrecorded assignment is void due to a filing provision, then the filing provision recognizes security interests in patents).
mortgage (transfer of a non-title interest). This is precisely the argument that the court embraced in Cybernetic. To support the argument that the Act covers security interests, other authorities point to language stating that an unrecorded assignment is not valid against a "subsequent . . . mortgagee" as meaning that Congress intended mortgages, or liens, to be registered. Given that "[t]he literature on patent 'mortgages' is almost as scanty as the literature on copyright 'mortgages' and . . . [is] less helpful," which is the proper argument?

It is generally accepted that a patent assignment is either a transfer of (1) ownership and title in the patent as a whole, (2) a percentage of the interest, or (3) full ownership and title in a specified geographic area of the United States. The definition of assignment underpins the court's argument in Cybernetic. To determine the meaning Congress intended for the provision, the court looked to the definition of the statutory language in 1870, the year "the current version of § 261 was enacted." The court examined first the history of the provision itself and second the history of security interests. It found that "'assignment[s],' 'grant[s],' and 'conveyance[s]'" all concerned the transfer of ownership interests and, therefore, title to the patent. If Matsco was to foreclose its interest and have priority over CSI's other creditors, the security interest could not fall within the meaning of transfers specified in § 261, or the filing with the state would not have perfected its interest. Because the court required a transfer of ownership interest for the recording provision of the

129. Haezmerli, supra note 2, at 1668-69.
130. Cybernetic, 252 F.3d at 1052.
131. GILMORE, supra note 98, § 13.4, at 417. But see Kidd, supra note 128, at 711 (noting that the Patent Act's filing provision is not as permissive as the Copyright Act's provision).
132. GILMORE, supra note 98, § 13.4, at 417.
133. STIM, supra note 6, at 458.
134. Cybernetic, 252 F.3d at 1049.
135. Id. at 1048.
136. Id. at 1048-55 & n.5 (stating that the original language of the statute specified an 'undivided part' instead of an assignment and that many types of contracts were written to secure property with all types of chattel and personal property).
137. Id. at 1050.
138. See id. at 1046.
Patent Act to preempt state law, Matsco’s priority was preserved.\footnote{Id. at 1059 (holding that § 261 only concerns ownership interests in patents so it does not preempt Article 9).} Was the court correct?

The proper argument may be that the courts should use the logic from \textit{Waterman} and read into the Patent Act a registration and a filing requirement for security interests.\footnote{\textit{See supra} notes 102-07 and accompanying text.} The Court in \textit{Waterman} decided the case under the theory of personal property prevalent at the time: the title theory.\footnote{Waterman v. Mackenzie, 138 U.S. 252, 258 (1891).} It is possible, though, to read the case as supporting registration and filing when a creditor uses a patent as collateral, which qualifies as a security interest under modern law.\footnote{\textit{See Gilmore, supra note 98, § 13.4, at 417-18. The Ninth Circuit stated, as it interpreted the meaning of the language when it was enacted in 1870, that an assignment meant the transfer of an ownership interest and a security interest, as a mortgage or lien, did not qualify. \textit{Cybernetic}, 252 F.3d at 1051-52. The court even analyzed the \textit{Waterman} case to arrive at this definition. \textit{Id.} But Gilmore gives it a completely different reading—that a “mortgage” is valid as a transfer of ownership. Gilmore, \textit{supra} note 98, § 13.4, at 417-18. The Court in \textit{Waterman} stated that because a patent is “incorporeal” property, recording the mortgage with the Patent Office is the equivalent of giving title to the mortgagee, even if the mortgagor maintains “possession.” \textit{Waterman}, 138 U.S. at 260. It logically follows that the Supreme Court recognized a mortgage or lien as a transfer of title, even if temporary, and that such a security is a transfer of ownership within the definition of the Patent Act’s recording provision. \textit{See id.}} Given that 1890 is substantially closer in time to 1870 than 2001 is to 1870, the time differences indicate that the Ninth Circuit did not follow \textit{Waterman} to its proper conclusion because, although the Court in \textit{Waterman} stated that an assignment is one of ownership interest, it also stated that a patent, if used to secure a debt, is an ownership interest and is properly perfected when registered with the USPTO.\footnote{\textit{Waterman}, 138 U.S. at 255-56.} It follows, then, that the court in \textit{Cybernetic} should have held that the Patent Act requires registration to perfect a security interest because the plaintiff’s lack of standing in \textit{Waterman} was based strictly on the fact that \textit{ownership}, and thereby the right to sue, was vested in the creditor/mortgagee who held \textit{title} because he registered the interest with the USPTO.\footnote{Id. at 260-61.}
security interest seems the most sensible policy.\textsuperscript{145} As far as patent rights are concerned, federal law preempts state law because of the Supremacy Clause of the Constitution.\textsuperscript{146} Article 9 requires an owner to register a security interest in property with the state to perfect the interest and to notify other creditors that the debtor's property is encumbered.\textsuperscript{147} Therefore, the filing (to perfect an interest) is significant in that it both (1) provides notice to subsequent creditors and (2) determines the secured creditor's rights in the event of the debtor's bankruptcy.\textsuperscript{148} Determining which provision controls, state or federal, is vital.\textsuperscript{149}

B. Copyrights—Peregrine and World Auxiliary

The Copyright Act specifies that "[a]ny transfer of copyright ownership or other document pertaining to a copyright may be recorded in the Copyright Office."\textsuperscript{150} The Copyright Act permits transfers "in whole or in part,"\textsuperscript{151} including the separation of any individual rights, of a "mortgage, . . . conveyance, alienation, or hypothecation of a copyright or of any of the exclusive rights comprised in a copyright."\textsuperscript{152} A hypothecation is "[t]he pledging of something as security without delivery of title or possession."\textsuperscript{153} Therefore, when Congress revised the Copyright Act in 1976, it specifically included security interests in the Act's registration provision and adapted the Act to the then-recent Article 9.\textsuperscript{154} One could argue that the 1976 Act's filing provision satisfies the UCC's requirement for a filing and provides both constructive notice and protection of interest holder rights.\textsuperscript{155} Others could question whether

\textsuperscript{145} See discussion infra Part II.B.
\textsuperscript{146} Haemmerli, supra note 2, at 1653.
\textsuperscript{147} Id. at 1659.
\textsuperscript{148} See id. at 1658-59.
\textsuperscript{149} See id. at 1659-60.
\textsuperscript{150} 17 U.S.C. § 205(a) (2000).
\textsuperscript{151} Id. § 201(d).
\textsuperscript{152} Id. § 101.
\textsuperscript{153} BLACK'S LAW DICTIONARY 747 (7th ed. 1999).
\textsuperscript{154} See Haemmerli, supra note 2, at 1665-66.
\textsuperscript{155} Id. at 1666-67 ("It clearly provides the type of locus for filing of security interests contemplated by section 9-302.")
the 1976 Copyright Act, even with its level of specificity, goes far enough to trigger the UCC’s internal step-back provision.\textsuperscript{156} However, the cases analyzing the Copyright Act’s recording provision have held that it (1) satisfies the UCC’s requirements to preempt state law and (2) requires perfection of a security interest by federal registration.\textsuperscript{157}

In 1990, the U.S. District Court for the Central District of California held in \textit{Peregrine} that filing with the Copyright Office is required to perfect a security interest.\textsuperscript{158} Peregrine’s principal assets were the copyrights and distribution rights to 145 films.\textsuperscript{159} CapFed extended a line of credit secured by the copyrights—the collateral—to Peregrine’s predecessor in ownership.\textsuperscript{160} CapFed filed UCC financing statements with California, Colorado, and Utah but did not file with the Copyright Office.\textsuperscript{161} Peregrine subsequently filed for bankruptcy and sought a declaratory judgment stating that (1) the security interest was unperfected because it was not filed with the Copyright Office, and (2) Peregrine was a judicial lien-holder, giving it priority to the assets.\textsuperscript{162} The bankruptcy court found for CapFed, and Peregrine appealed.\textsuperscript{163} The district court (the appellate court here) analyzed the Copyright Act’s language and the policy behind a recording provision in determining that a security interest in a copyright must be filed with the Copyright Office to be perfected and have priority.\textsuperscript{164} The court bolstered its argument by citing to Article

\textsuperscript{156} Ward, supra note 8, at 412-13. UCC § 9-311(a)(1) specifies a requirements test for perfecting a security interest. \textit{Id.} at 412. The section requires perfection against a lien holder, and if the federal statute does not have a requirement for registration against a lien holder, then the Copyright Act does not meet the UCC’s more restrictive step back provision. \textit{Id.}


\textsuperscript{158} \textit{Peregrine}, 116 B.R. at 203.

\textsuperscript{159} \textit{Id.} at 197.

\textsuperscript{160} \textit{Id.}

\textsuperscript{161} \textit{Id.} at 198.

\textsuperscript{162} \textit{Id.}


\textsuperscript{164} \textit{Id.} at 198-204.
9's self preemption clause with regards to a federal filing scheme.\textsuperscript{165} While the holding in \textit{Peregrine} left the question of unregistered copyrights (copyrights that the author did not register with the Copyright Office) open, the Ninth Circuit recently clarified the issue in \textit{Aerocon Engineering, Inc. v. Silicon Valley Bank (In re World Auxiliary)}.\textsuperscript{166}

\textit{World Auxiliary} occurred in a bankruptcy setting in which creditors asserted their interests and priority in copyrights.\textsuperscript{167} World Auxiliary and its affiliated companies ("Debtors"), owned copyrights in "drawings, technical manuals, blue-prints, and computer software" for products used to modify airplanes.\textsuperscript{168} These copyrights were not registered with the Copyright Office.\textsuperscript{169} The appellee, Silicon Valley Bank ("Bank"), financed a loan to the Debtors and secured it with the companies' assets, including the copyrights, and filed a security interest with the state.\textsuperscript{170} The Bank never filed its interest with the Copyright Office.\textsuperscript{171} The Debtors filed for bankruptcy and Aerocon Engineering ("Aerocon"), the appellant in this case and another creditor, wanted the copyrights.\textsuperscript{172} Aerocon was working on a joint venture to sell aircraft modifications with the Debtors' designs, but the Bank's security interest in the copyrights blocked it.\textsuperscript{173} Aerocon and its partners decided to purchase all of the Debtors' assets, including the power to avoid the Bank's security interest, exercise that power, and own the copyrights outright.\textsuperscript{174} After purchasing the assets, the venture fell through, and Aerocon became a part owner of the copyrights as a tenant-in-common with another party.\textsuperscript{175} The

\textsuperscript{165} \textit{Id.} at 204.
\textsuperscript{166} 303 F.3d 1120 (9th Cir. 2002).
\textsuperscript{167} \textit{Id.} at 1122-23.
\textsuperscript{168} \textit{Id.} at 1123.
\textsuperscript{169} \textit{Id.} The rights that make up a copyright attach as soon as the work is fixed in a tangible medium and does not require official registration (as in a patent). \textit{Stm, supra} note 6, at 96, 129.
\textsuperscript{170} \textit{World Auxiliary}, 303 F.3d at 1123.
\textsuperscript{171} \textit{Id.}
\textsuperscript{172} \textit{Id.}
\textsuperscript{173} \textit{Id.}
\textsuperscript{174} \textit{Id.} at 1124.
\textsuperscript{175} \textit{Id.}
Bank foreclosed on the copyrights and sold them to Aerocon’s former partners.  

Aerocon brought suit to avoid the Bank’s security interest and to recover its copyrights. The bankruptcy court found that the Bank had perfected its interest under California’s Article 9, and the district court affirmed the decision. Aerocon appealed to the Ninth Circuit.

The question before the court concerned Aerocon’s creditor status, which hinged on whether state law or federal law determined how to perfect a security interest in an unregistered copyright. Aerocon attempted to persuade the court by arguing that (1) Peregrine controls, (2) the UCC defers to the Copyright Office’s registration scheme, and (3) Congress expressly preempted the UCC with the specific filing requirements in the Copyright Act. The court rejected these arguments and held that state registration perfects a security interest in an unregistered copyright. The court found that because the copyrights were not registered with the Copyright Office (the Office did not know that they existed), recording a security interest in that Office would be ineffectual. The Ninth Circuit thereby affirmed scholars’ theory that state filing under Article 9 was the appropriate process to perfect a security interest in an unregistered copyright. Although the law for registering security interests in copyrights seems stable at this point in the Ninth Circuit, the arguments from Peregrine for a national, uniform filing are persuasive against World Auxiliary and powerful against Cybernetic.

176. World Auxiliary, 303 F.3d at 1124.
177. Id.
178. Id.
179. Id.
180. Id. at 1125.
181. See id. at 1127, 1129.
182. World Auxiliary, 303 F.3d at 1128.
183. Id.
184. Id. at 1128; Haemmerli, supra note 2, at 1667.
185. See Nat’l Peregrine, Inc. v. Capitol Fed. Sav. & Loan Ass’n (In re Peregrine Entm’t, Ltd.), 116 B.R. 194, 200-02 (C.D. Cal. 1990) (stating that a national filing scheme alleviates the confusion creditors encounter when searching many different jurisdictions to determine whether an interest was transferred or encumbered).
The court in *Peregrine* found the policy behind a national filing scheme for IP security interests very persuasive, whereas the court in *Cybernetic* simply looked at the language of the statute and expressly disregarded policy considerations.186 Whenever multiple filing schemes exist, confusion as to where an interest must be filed for what purpose also exists.187 A national filing and recordation scheme would not only definitively state where creditors search to determine whether an asset was encumbered, it would also resolve the confusion over exactly where the interest is perfected.188 This is precisely why attorneys must use the "belt and suspenders’ approach" (file with both federal and state authorities).189

III. THE CONFLICT

A. The IP Statutes and Article 9

Despite the *Waterman* holding, it is generally accepted that the Patent Act does not include security interests in its filing requirements. Conversely, the Copyright Act does include these interests.190 However, Article 9, section 9-311 of the UCC states that "filing . . . a financing statement is not necessary or effective to perfect a security interest in property subject 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 . . . preempt [s]ection 9-301(a).”191 Professor Ward believes that this provision (1) goes further than what courts have held because it retains authority at the state level unless a federal statute expressly and specifically preempts it and (2) requires the federal statute to

---


187. *See id.* at 1047.

188. *See id.*


protect the rights of a lien creditor.\textsuperscript{192} Section 9-311 requires more than section 9-109, which defers to any federal scheme that preempts it.\textsuperscript{193} The federal statute must not only provide a place for filing but must also expressly protect creditors.\textsuperscript{194} This reading is more restrictive than what courts have held as to when the UCC will subordinate itself, and it questions whether the Copyright Act is specific enough to meet the requirements.\textsuperscript{195} Given these alternate arguments, what will happen when other courts take up the issue?

As an interesting side note, the Ninth Circuit decided all three of the leading cases on the subject, \textit{Peregrine}, \textit{Cybernetic}, and \textit{World Auxiliary}.\textsuperscript{196} Of these, only \textit{Cybernetic} and \textit{World Auxiliary} are circuit court decisions.\textsuperscript{197} The United States District Court for the Central District of California with a Ninth Circuit judge sitting in designation decided \textit{Peregrine}.\textsuperscript{198} Although these appear to be generally accepted holdings, they are not binding outside of the Ninth Circuit. Therefore, the Supreme Court should have granted \textit{certiorari} in \textit{Cybernetic} to define a law that would bind all courts.\textsuperscript{199} Such a ruling would have significantly improved the quagmire that attorneys continue to trudge through.\textsuperscript{200}

\textbf{B. Copyrights v. Patents}

The current 1976 Copyright Act is very extensive in defining the meaning of a “transfer” of interest, and courts have held that it provides a sufficient filing scheme to preempt the UCC and perfect a security interest.\textsuperscript{201} Conversely, courts have held that the Patent Act

\begin{footnotes}
\textsuperscript{192} See Ward, \textit{supra} note 8, at 412-13.
\textsuperscript{194} See Ward, \textit{supra} note 8, at 412-13.
\textsuperscript{195} See \textit{supra} notes 149-56 and accompanying text; see also Ward, \textit{supra} note 8, at 413.
\textsuperscript{196} Aerocon Eng’g, Inc. v. Silicon Valley Bank (\textit{In re World Auxiliary Power Co.}, 303 F.3d 1120 (9th Cir. 2002); Moldo v. Matsco, Inc. (\textit{In re Cybernetic Servs., Inc.}, 252 F.3d 1039 (9th Cir. 2001), \textit{cert. denied}, 534 U.S. 1130 (2002); Nat’l Peregrine, Inc. v. Capitol Fed. Sav. & Loan Ass’n (\textit{In re Peregrine Entm’t, Ltd.}), 116 B.R. 194 (C.D. Cal. 1990).
\textsuperscript{197} \textit{World Auxiliary}, 303 F.3d 1120 (9th Cir. 2002); \textit{Cybernetic}, 252 F.3d at 1039.
\textsuperscript{198} \textit{Peregrine}, 116 B.R. at 194.
\textsuperscript{200} See, e.g., Booth, \textit{supra} note 189.
\textsuperscript{201} Haemmerli, \textit{supra} note 2, at 1665-66; Booth, \textit{supra} note 189.
\end{footnotes}
lacks such specific language and that the proper way to perfect a security interest in a patent is through an Article 9 filing with the appropriate state. 202 Does this discrepancy make sense, given that both copyrights and patents come from the same constitutional authority? 203

Although Congress extensively revised and updated the Copyright Act in the 1970s, it has also amended the Patent Act since the time states began adopting the UCC. 204 Therefore, Congress would have changed the filing provision (§ 261) if it intended to create a federal filing scheme for security interests in patents. 205 If security interests existed in 1870, Congress arguably would have included them in their statutory definitions of assignments or grants because the Supreme Court contemporaneously recognized in Waterman that a patent could be used as collateral for a loan. 206

Furthermore, the court in Cybernetic rejected the policy argument for a national registration system that the same court found relevant in Peregrine. 207 The court in Peregrine found it very important and persuasive that there should be one national system of registration of interests so a potential creditor could search one place to determine whether the interest was encumbered instead of embarking on a confusing and expensive search of all 50 states. 208 Why did the court reject this argument in Cybernetic? The answer is two-fold: (1) general policy interests are not as important as the language and intent of the statute, and (2) the USPTO regulations state that the filing requirement is solely for documents affecting title. 209 The court

203. See discussion supra Part I.A.
204. See, e.g., Cybernetic, 252 F.3d at 1056.
205. Id. There is another side to the argument, though, because the court based its reading of § 261 on the meaning it would have in 1870, the last time Congress amended the particular section. Id. at 1048. The argument hinges on whether one can infer that Congress' intent through inaction remained a filing for a transfer of ownership interest only. See id. at 1052, 1056.
206. See discussion supra Part II.A.
207. Cybernetic, 252 F.3d at 1055.
209. Cybernetic, 252 F.3d at 1055, 1056.
recognized that, although it was not bound by the USPTO regulations, the USPTO was entrusted to execute the statute and the court chose to follow its regulations.\textsuperscript{210} The court could have easily reasoned the other way and interpreted a registration requirement in the Act, but it did not.\textsuperscript{211} However, the court did note that the statute was "archaic" and, given its deference to the legislature, may be hinting that Congress should attempt an overhaul similar to that of the Copyright Act, or at least a revision to § 261, to conform the Patent Act to modern commercial law.\textsuperscript{212}

CONCLUSION

Under existing law, where to register a security interest in IP is at best a little confusing and at worst a malpractice suit waiting to happen. To properly protect themselves, their clients, and their clients' assets, attorneys must juggle a system of filing requirements and purposes that the courts have not simplified.\textsuperscript{213}

In the middle of the 20th century, Article 9 of the UCC introduced the security interest to create a single, uniform security device.\textsuperscript{214} It is a non-title interest in personal property to secure payment of a debt—secured collateral for a loan.\textsuperscript{215} As state law, Article 9 requires the creditor to file its interest with the Secretary of State to "perfect" a security interest and receive priority over other creditors.\textsuperscript{216} This filing also serves a notice function so that subsequent creditors may determine whether the asset is encumbered before making a decision to extend credit.\textsuperscript{217}

IP (patents, copyrights, and trademarks) is quickly replacing real and physical property as the major assets of modern businesses.\textsuperscript{218} As

\begin{flushleft}
\textsuperscript{210} Id. at 1057.
\textsuperscript{211} Id.; see discussion of Waterman, supra Part II.A.
\textsuperscript{212} Cybernetic, 262 F.3d at 1057.
\textsuperscript{213} See Booth, supra note 189.
\textsuperscript{214} Ward, supra note 8, at 396.
\textsuperscript{215} Haemmerli, supra note 2, at 1657.
\textsuperscript{216} Id. at 1659.
\textsuperscript{217} Id.
\textsuperscript{218} See id. at 1647-48.
\end{flushleft}
IP assets have become more valuable and a larger part of the economic landscape, businesses will increasingly use them as collateral to secure financing. They are often the only or most valuable assets the company possesses.

This congruence of commercial and IP law creates both a confusing mix of statutory filing schemes and court holdings that provide very few bright line rules. Each of the IP statutes discussed in this Note, the Patent Act and the Copyright Act, contains a filing scheme to record a transfer of interest. That, however, is where the similarities end. Courts have held that the Patent Act's filing provision only applies to transfers that involve an ownership interest or title to the patent. Alternatively, the courts have reasoned that the Copyright Act's filing provision includes security interests in the type of transfers that must be filed with the Copyright Office.

As a further complication, Article 9 has specific provisions concerning when federal law will preempt it. The federal filing scheme must satisfy two requirements for Article 9 to step back: (1) provide notice to subsequent creditors that the property is encumbered and (2) provide expressed protection of the lien holders (the filing will ensure the creditor has priority over others to foreclose on the asset if the debtor files for bankruptcy).

Therefore, an attorney's filing decision is based on what type of IP his client possesses. Although it is clear that both the patent and copyright filing schemes will satisfy the first prong, the second prong

219. Id.
220. See id.
221. See discussion supra Part III.
223. E.g., Moldo v. Matsco, Inc. (In re Cybernetic Servs., Inc.), 252 F.3d 1039, 1059 (9th Cir. 2001), cert. denied, 534 U.S. 1130 (2002) (holding that that § 261 of the Patent Act does not preempt Article 9 and federal registration is not required to perfect a security interest in a patent); City Bank & Trust Co. v. Otto Fabric, Inc., 83 B.R. 780, 782 (D. Kan. 1988) (holding that the Patent Act does not state that a security interest must be filed with the USPTO to perfect it and that the statute was amended since the "advent of modern commercial law").
224. E.g., Aerocon Eng’g, Inc. v. Silicon Valley Bank (In re World Auxiliary Power Co.), 303 F.3d 1120, 1131 (9th Cir. 2002) (holding that Congress provided for security interest protection by filing with the Copyright Office for registered Copyrights only); Nat’l Peregrine, Inc. v. Capitol Fed. Sav. & Loan Ass’n (In re Peregrine Entm’t, Ltd.), 116 B.R. 194, 203 (C.D. Cal. 1990).
226. See Ward, supra note 8, at 396-97.
is more difficult to satisfy. Some scholars argue that the Copyright Act, even with its very specific filing provision, still does not satisfy the protection requirement of UCC section 9-311. Courts, however, have reasoned that it does.

The Supreme Court was presented with an opportunity to establish a clear rule, at least for patents, as to where filing will perfect a security interest. However, the Court denied certiorari, and the confusion remains.

Furthermore, courts have not adequately distinguished the differing holdings for patents and copyrights given that they have the same constitutional origin. The matter is also confusing because the cases have all been decided by the same circuit, and the same court disregarded a policy argument for a national filing system where federal statutes are involved that the same court found persuasive in a prior case.

The end result for attorneys is to take great care in determining where to file an IP security interest. In some cases, filing with both the state and the appropriate federal office may be appropriate to ensure the client and his IP interest are properly protected. A filing mistake could lead to a loss of considerable property value or to a loss of a client’s capital. With the high value of today’s IP assets, considerable amounts of money are at stake, and being “perfect” with his filings is in the attorney’s best interest.

R. Scott Griffin

227. See id. at 412.
228. Id.
229. See discussion supra Part II.B.
231. Id.
232. See discussion supra Part III.B.
233. See discussion supra Part III.A.
234. Booth, supra note 189.
235. Id.
236. See id.