APPENDIX 16 - 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 Arizona, faced another perfection of copyright collateral issue under § 544(a) of the Bankruptcy Code. In the case of *In re World Auxiliary Power Co*.,[1] the debtor's 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 with the Copyright Office on the day that the bankruptcy petition was filed. 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. Unlike *Peregrine* and *Avalon Software*, however, *World Auxiliary Power* held for the secured party on the theory that Article Nine is not preempted (to any extent) when the copyright collateral is unregistered. 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. For good measure, the court also concluded that Copyright Act *recording* does not preempt Article Nine *filing* when the copyrights are not registered.[2]

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 necessary condition for giving constructive notice of any transfer of copyright ownership, whether or not it is registered at the outset. Congress

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1 *In re World Auxiliary Power Co*., 244 B.R. 149 (Bankr. N.D. Calif. 1999).

2 244 B.R. at 154-56.

must have intended section 205 to serve as the recording rule for all copyrights - both registered and unregistered.[3]

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 opines that, unless the copyrights in *Peregrine* had been registered, the hypothetical lien creditor [trustee under 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.[4]

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 envisioned by *Peregrine*. In deciding that the lien creditor was a protected later transfer under section 205(d), the *Peregrine* court assumes the fact that a Copyright Office recording by the trustee had occurred.[5] 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 § 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 § 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."[6] If, however, *Peregrine* is right on this score and the involuntary lien creditor finds shelter in section 205(d), then that same lien creditor would also seem to be vested with sufficient "copyright ownership" to allow it to register the work so acquired under section 408(a) of the Copyright Act.[7] If a real lien creditor/transferee could register an unregistered copyright in order to give constructive notice of its recordable ownership interest under 205(a) and (c),

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[3] 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.

[4] 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).

[5] National Peregrine, Inc. v. Capital Federal Savings & Loan Ass'n, 116 B.R. 194, 207 (C.D. Cal. 1990).

[6] *See supra* text accompanying notes 122 to 130.

[7] 17 U.S.C. § 408(a) (1994)("... the owner of a copyright or of any exclusive right in the work may obtain registration").

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.[8]

Finally, the result in *World Auxiliary Power* seems flawed even if one accepts the Court's questionable first holding that Copyright Act *priority* under the teaching of *Peregrine* is only extended to registered Copyrights. The Court's second, and severable, conclusion that Article Nine *filing* is not displaced by Copyright Act recording when the copyright is unregistered also requires some very heavy lifting. On this second point the Court merely refuses to be guided by the unequivocal reference to the Copyright Act as a displacing registry under old U.C.C. § 9-302(3)(a)&(4).[9] 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. It is hard to argue with partial preemption, extending only to Article Nine filing, where the authors of Article Nine themselves 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 much more support for *World Auxiliary Power's* second conclusion that state law does not voluntarily yield its filing rules to the Copyright records. Under the Revision language (now applicable in California but not applicable under the facts of the case), 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 . . . ."[10] However, if we accept the most extreme teaching of *Peregrine* (as *World Auxiliary Power* purports to do) even this new U.C.C. language invites a deferral on state filing. Remember that *Peregrine* concludes that section 205(d) of the Copyright Act does contain a priority rule that embraces the lien creditor.[11]

Peregrine justly deserves most of the criticism it gets. However, the limit on preemption suggested by *World Auxiliary Power* is a conceptual and statutory reach. Even if it can be justified as a matter of federal preemption, it protects state law filing only until someone with ownership rights registers the copyright (the debtor or any transferee or exclusive licensee). This questionable distinction based on whether or not copyright collateral is

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8 11 U.S.C. § 544(a)(1) (1998).

9 244 B.R. at 154-56.

10 U.C.C. [Revised] § 9-311(a)(1).

11 116 B.R. at 203-04.

registered is anything but a safe harbor for the secured party contemplating a credit extension secured by copyright collateral.