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Bright Ideas

A publication of the Intellectual Property Law Section of the New York State Bar Association

Message from the Chair

Kelly M. Slavitt

Another successful Annual Meeting!

Thank you to everyone who joined us at the Annual Meeting in January in Manhattan. An outstanding program, "Judicial and Legal Activism and Their Impact on the Practice of IP Law," featured a keynote address by the Honorable Randall R. Rader, Chief Judge of the Court of Appeals for the Federal Circuit. Panels dealt with timely topics such as branding and rebranding, fashion design protection, advertising law, judicial activism in damages analyses, and legal ethics in the digital world.

The Section again hosted a table at the highly successful Diversity Reception in connection with the Annual Meeting, with Executive Committee members on hand to answer questions, promote the Section, encourage new memberships, and make new friends. And the Section again hosted a reception at the end of the day's CLE program, targeted at Young Lawyers. This reception continues to be an excellent way for us to recruit and mentor young lawyers and to get them involved in the Section.

With the Annual Meeting behind us, we've started planning our Fall Meeting. Mark your calendars for October 17-20, 2013 at The Sagamore. Marc Lieberstein of Kilpatrick Townsend & Stockton LLP, David Bassett of Wilmer Hale LLP, and Itai Maytal of Miller Korzenik Sommers LLP are putting together an internationally focused program for us this year. Watch for details, and sign up before it sells out.

Our committees have also been active. The Trademark Law Committee hosted a roundtable on IP licenses in bankruptcy, and the Litigation Committee presented a program on litigation strategy featuring speaker Fred Whitmer of Kilpatrick Townsend, author of *Litigation Is War: Strategy and Tactics for the Litigation Battlefield*. Visit www.nysba.org/IPL for details on upcoming committee roundtables and events. If you have not yet done so, I also encourage you to join an IP Law Section committee; see the "Join this Section" link on the Section's web page.

Our two new initiatives are going extremely well. The first is the renewed focus on our committees. One of the committees hosts each monthly Executive Committee meeting and updates us on a topic in that area and reports on the events they are planning for the year. We are also making an effort to do more joint programs with multiple committees and with other Sections. Statistics show an increase in Section membership that I attribute to our ability to recruit new members through these smaller outreach programs where potential members have the ability to meet existing members in a smaller setting and get to know us better.

Inside

The second is the In-House Initiative. You may have noticed that our Committee Chairs are more diverse—one in-house attorney and one law firm practitioner for each committee. You also may have noticed at the Fall Meeting and Annual Meeting, as well as at our committee CLE programs, that our panelists are increasingly diverse in their practices. Our goal of an in-house practitioner on each panel is becoming a reality, as is our goal of more diverse panels comprised of a mix of law firm practitioners, government officials, and non-profit attorneys. Cheherazade Chemcham of Louis Vuitton is chairing this initiative. She has worked with the Membership Department to identify in-house members of NYSBA and of the IP Law Section who would be most interested in this initiative and the related events. The kick-off event is in its final planning stages, so watch for an announcement. I hope you'll join us to further the Initiative's goal of promoting new relationships, membership, and diversity.

If you want to get involved, or more involved, in the Section's activities, please email me at kelly.slavitt@rb.com and let me know your area of practice and how you would like to be involved. We'll be happy to find a way to accommodate you.

Kelly M. Slavitt

Thank You

The Intellectual Property Law Section extends its gratitude to the following for their significant sponsorship over the past year:

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Transitioning to the America Invents Act

By Christopher White

I. Introduction

The America Invents Act[1] (AIA) has been in full effect since March 16, 2013. The AIA represents the most sweeping change the U.S. patent law has seen since 1952.[2] As with previous changes in the law, patent practitioners will be prosecuting old-law applications in parallel with new-law applications for years to come. Although the changes in the AIA are numerous, they are not as significant in day-to-day prosecution as might have been feared. This article discusses the effects of these changes on patent procurement and provides reference tables for use when switching between work on pre-AIA applications and work on AIA applications. It provides an overview of pre-AIA and AIA statutes, a comparison of first-inventor-to-file provisions to the former first-to-invent provisions, and analysis of the laws relating to the best-mode requirement and publication before filing.

"Although the changes in the AIA are numerous, they are not as significant in day-to-day prosecution as might have been feared."

The AIA primarily amends Title 35, U.S. Code (U.S.C.), the patent law. I use "AIA" to refer to both the AIA statutes and the rules in Title 37, Code of Federal Regulations (C.F.R.), as amended to conform to those statutes. Prior to the AIA, the CREATE Act[3] was the last substantive change to the patentability standards.[4] I therefore refer to the pre-AIA 35 U.S.C. and 37 C.F.R. as the "CREATE" law for convenience. All references herein to the Manual of Patent Examining Procedure (MPEP) are to MPEP E8R9 (8th ed. 2001, Rev. 9, Aug. 2012).

II. Comparison of CREATE and AIA Provisions

A. First-Inventor-to-File Versus First-to-Invent

The CREATE system is a "first-to-invent" system, so the date of invention and the date of filing both can be considered in determining patentability. In contrast, the AIA system is a "first-inventor-to-file" system. Generally, only the date of filing, not the date of invention, is relevant to patentability under the AIA. Unlike the pure "first-to-file" system found in many jurisdictions around the world, the AIA's "first-inventor-to-file" system provides a unique grace period for inventor disclosures and a unique set of procedures for demonstrating that a patent applicant derived a claimed invention from another.

First-inventor-to-file is not as drastic a change from first-to-invent as it may seem. It is true that the critical dates for patent applications are different under AIA than under CREATE, so the content of the prior art will be different. However, the form and content of rejections should be largely the same. Effective rebuttals of rejections also should generally be the same under AIA as under CREATE. The U.S. Patent and Trademark Office (PTO) has stated that "Office personnel may and should continue to rely upon pre-AIA 35 U.S.C. §§ 102 and 103 case law and the discussion of that case law in MPEP chapter 2100," except where the AIA specifically does not carry forward a CREATE principle of law.[5] Principles of law still valid under AIA include, for example, the *KSR*[6] standard of obviousness.[7]

In addition to its similarities to CREATE law, the AIA system is also similar in many ways to practice in other jurisdictions, such as Europe and China. For example, in Europe, European Patent Convention (EPC) Art. 60(2)[8] provides that the inventor with the earlier filing date is entitled to the patent, similar to AIA 35 U.S.C. § 102(a)(1). Art. 61(1) EPC[9] establishes remedies for an actual inventor who is "entitled to the grant of a European patent" when the applicant for patent is not; this is similar on its face to "derivation proceedings" provided by the AIA.[10] Chinese practice is similar; Art. 9 of the Chinese patent law[11] sets forth that the first applicant to file for an identical invention receives a patent. Art. 65[12] provides penalties for "[usurping] the right of an inventor or creator to apply for a patent" not made for hire.

Patent procurement under the AIA thus should not be unfamiliar territory. Practitioners accustomed to prosecuting in the United States, Europe, or China will find much that is familiar. Moreover, the standards for drafting applications continue largely unchanged; the written-description and enablement requirements carry forward unchanged from CREATE. Although the AIA best mode requirement has generated considerable controversy, I also recommend carrying best mode practice forward from CREATE.

B. The Best Mode Requirement

35 U.S.C. § 112, both AIA and CREATE, sets forth that "the specification…*shall* set forth the best mode contemplated by the inventor of carrying out his invention" (CREATE, emphasis added). The "best mode" requirement remains in the statute under AIA. However, the AIA provides that "failure to disclose the best mode shall not be a basis on which any claim of a patent may be canceled or held invalid or otherwise unenforceable."[13] Moreover, domestic priority claims to provisional or nonprovisional applications are no longer barred if the priority application does not set forth the best mode.[14]

The removal of the best mode requirement from litigation and from priority claims has caused much discussion about the "death" of the best mode requirement.[15] But the best mode requirement still exists and is enforceable during examination.[16] The AIA's provisions are not entirely internally consistent; each application is still required by the letter of the law to set forth the best mode, but no post-grant penalty attaches to failure to do so. Furthermore, recent case law expressly interprets away the plain meaning of the statute by substituting "lack of concealment" for explicit disclosure.[17] Should a judge or justice at some point pause on the variance between the "shall set forth" of the statute and the "lack of concealment" standard developing in the case law, a change in best mode might come about. Therefore, I recommend continuing to disclose the best mode as under CREATE in case the law changes.

In addition, failure to disclose the best mode may put priority claims at risk. The Paris Convention states that "a regular national filing [is] any filing that is adequate to establish the date on which the application was filed in the country concerned."[18] Such a "regular national filing" "[gives] rise to the right of priority."[19] There now are two ways to look at U.S. best mode law with regard to whether an application that does *not* disclose the best mode still gives rise to a right of priority under the Paris Convention (and thus also under PCT, the Patent Cooperation Treaty[20]). On the one hand, 35 U.S.C. § 111(a)(2), both CREATE and AIA, states that an "application shall include—(A) a specification as prescribed by section 112." Section 112, both CREATE and AIA, states that "the specification…*shall set forth* the best mode" (emphasis added).[21] Therefore, one could argue that a U.S. application that does not disclose the best mode is not complete, so it is not entitled to a filing date and thus does not give rise to a right of priority.

On the other hand, AIA 35 U.S.C. §§ 119(e) and 120 provide that a domestic priority application does not have to set forth the best mode. Therefore, a filing that does not set forth the best mode is arguably "adequate to establish the date on which the application was filed" in the United States, for purposes of claiming priority in the United States. Therefore, such a filing also would be adequate to obtain a Paris right of priority. Until this question is litigated and one of these interpretations is selected, I recommend including the best mode in patent applications.

C. Date of Invention Versus Effective Filing Date and Derivation Proceedings

Under both CREATE and AIA, each claim has a single "birthday." This is the earliest date used to determine what is prior art. The AIA applies to any patent application as soon as that application includes any claim with a birthday (specifically, an "effective filing date," as discussed below) on or after March 16, 2013. Once an application is under the AIA, it stays under the AIA even if all claims with birthdays from March 16, 2013, are canceled.[22] Moreover, all continuations, divisionals, or continuations-in-part of an AIA application are under the AIA.

Under CREATE, a claim's birthday is the date the claimed subject matter was invented. Specifically, the birthday is the earliest date at which the inventor had "possession of either the whole invention claimed or something falling within the claim (such as a species of a claimed genus), in the sense that the claim as a whole reads on it."[23] Normally, the birthday is the filing date of the application ("constructive reduction to practice")[24] or the date the claimed device was actually made or the claimed method was first practiced ("actual reduction to practice").[25]

Under AIA, a claim's birthday is the "effective filing date." This is the filing date of the earliest application in a priority chain that supports the claim.[26] If the claim is in an original (non-continuing) application, the effective filing date is simply the filing date of that application. Under CREATE, 37 C.F.R. § 1.131 affidavits could be used to "swear back" of references, i.e., to show an earlier date of invention than a reference to disqualify that reference as prior art under CREATE 35 U.S.C. § 102(a). Under the AIA, these affidavits are no longer available, since prior art critical dates are not reckoned from the date of invention. However, as under CREATE, records should still be kept of conception, diligence, and reduction to practice, to be able to prove derivation should it become necessary.

Derivation proceedings, which replace interference practice, permit a petitioner to challenge a claim as not having been invented by the named inventors but instead having been derived from the petitioner.[27] Derivation proceedings must be filed in a pending patent or reissue application within one year of publication of the application as a pre-grant publication or patent, when an earlier filed application includes an allegedly derived, patentably indistinct invention.[28]

D. Prior Art

AIA broadens the scope of prior art in some ways and narrows it in others. AIA adds to the available prior art some references between the date of invention and the date of filing. However, AIA narrows prior art by excluding from prior art commonly assigned applications and patents published after the filing date.[29] CREATE provided this exclusion for obviousness, and the AIA extends the exclusion to novelty. AIA also excludes private sales and other activity not available to the public from the prior art. AIA 35 U.S.C. § 102(a)(1) describes prior art as that, among other things, "in public use, on sale, *or otherwise available to the public*" (emphasis added). There was some ambiguity in the language and in the Congressional Record as to whether "available to the public" modified "on sale." Until the courts rule on this question, the PTO has adopted the interpretation that "public" does modify "on sale," so private sales are no longer prior art.[30]

Table 1 is a reminder of the types of prior art available for use in rejections under CREATE. For reference as you start to receive AIA office actions, look up the AIA basis for rejection in **Table 2** to find the corresponding CREATE provision.

E. Post-Grant Review

The AIA provides a variety of new post-grant options. However, most of them (e.g., reissue and Certificates of Correction) carry forward from CREATE. **Tables 3** and **4** summarize the CREATE procedures and the AIA procedures, respectively. **Table 5** is a timeline showing generally when the various AIA post-grant provisions, and derivation proceedings, are applicable.

Post-grant review[31] is a new procedure somewhat similar to opposition in the European Patent Office. Within nine months of issuance, the requester can challenge a claim under any ground that can serve as a defense in litigation.[32] This includes AIA 35 U.S.C. § 112 minus the best-mode requirement (discussed below). A new transitional program for covered business method patents is very similar to post-grant review but with restrictions on the prior art available.[33] There is no nine-month deadline, but it is only applicable to certain business method patents. Moreover, the program only runs until September 16, 2020.[34]

The AIA replaces *inter partes* reexamination with a new *inter partes* review procedure.[35] *Inter partes* review is designed to align more closely with the flow of patent litigation than *inter partes* reexamination. *Inter partes* review must be requested within one year of being notified of alleged infringement and automatically stays any subsequently filed civil suit.

Supplemental examination[36] is a new AIA procedure that permits the patent owner to request reexamination on a broader range of issues than normal *ex parte* reexamination (which itself carries forward largely unchanged from CREATE to AIA). Via supplemental examination the patent owner can request *ex parte* reexamination for any information that raises a substantial new question of patentability ("SNQ"). This is in contrast to normal *ex parte* reexamination, which permits the patentee or a third party to request reexamination based only on patents or printed publications that are prior art and that raise an SNQ.[37]

Supplemental examination was designed, at least in part, to permit patent owners to restore value to issued patents tainted by legal errors during prosecution.[38] This provision addresses a long-felt concern over litigation to invalidate a patent because of inequitable conduct, independent of the patentability of any claim.[39] To address this concern, the AIA provides that submitting the supplemental examination request generally forecloses a holding of unenforceability based on the information submitted with the request.[40]

II. Publications, Disclosures, and Statutory Bars

A. Statutory Bars

Under CREATE, the phrase "statutory bar" generally referred to 35 U.S.C. § 102(b) prior art, particularly publications or other public disclosures. These events could not be sworn back of using a CREATE 37 C.F.R. § 1.131 affidavit (as discussed above), and filing even one day late would result in a loss of patent rights.

Under the AIA, all prior art is a "statutory bar" as practitioners have been accustomed to thinking about it. There is almost no way to overcome a disclosure by another made before a claim's birthday, and the one-year grace period provided for public disclosures by the inventor now applies uniformly to all AIA prior art.[41]

The one way to overcome a prior disclosure by another who did not derive the information disclosed from the inventor is this: if the inventor has publicly disclosed the invention, prior art arising after the inventor's disclosure is not prior art against the inventor's later patent application.[42] A similar exception was implicit in CREATE § 102(a); if a public disclosure proved a date of invention before the date of filing, references arising after the date of the disclosure were therefore after the date of invention and so not prior art under CREATE § 102(a). This exception is now clearly stated in the AIA.

B. "First to Publish"

The AIA exceptions to prior art after the inventor's disclosure[43] led some commentators to regard early drafts of the AIA as establishing a "first-to-publish" system.[44] That is, the statutory exceptions of AIA §§ 102(b)(1)(B) and 102(b)(2)(B) led some to believe that publishing as early as possible, up to a full year before filing the application, would take maximum advantage of the grace period and reduce the space of prior art available against the application.

I do not recommend following this line of thinking. Under the AIA Examination Guidelines,[45] if the inventor's disclosure contains certain elements, any element in a disclosure intervening between the inventor's disclosure and the effective filing date of the application that is not one of those certain elements will be available as prior art.[46] The only exception is that an intervening "more general description of the subject matter previously publicly disclosed by the inventor or a joint inventor" will not be prior art. For example, an intervening genus disclosure is not prior art if the inventor's disclosure contained a species in that genus.[47] This also applies to the AIA § 102(b)(2)(B) exception to AIA § 102(a)(2) (similar to CREATE § 102(e)) prior art.[48]

Therefore, making a public disclosure that starts the one-year grace-period timer of AIA 35 U.S.C. § 102(b) has largely the same drawbacks as filing a provisional application and none of the benefits. Like a provisional, the public disclosure has the drawback that it does not provide any protection or priority date for subject matter developed between the disclosure and the filing. Unlike a provisional, which gives rise to a right of priority, the publication does not provide a basis to claim priority. Also unlike a provisional, the publication serves as a statutory bar in absolute-novelty jurisdictions.[49] The only advantage of publication under AIA is that it may be used to show disclosure of the invention before an intervening disclosure and so trigger the prior-art exceptions of §§ 102(b)(1)(B) and (b)(2)(B) to the extent of what is disclosed in the publication.[50] This does not appear to justify considering the AIA a "first-to-publish" system. I recommend continuing to think of an inventor's pre-filing publications as statutory-bar events. If you happen to have a case with a pre-filing publication and an intervening disclosure, certainly take advantage of AIA 35 U.S.C. §§ 102(b)(1)(B) and (b)(2)(B), but do not count on deriving any particular benefit from those sections in any given case.

C. Effect of Disclosures Before the Effective Date of AIA on Applications Filed Under AIA

The effect on AIA applications of disclosures made after March 16, 2012 is very similar to the effect had the AIA not been enacted. In general, if a patent applicant is able to claim priority of the disclosure, the effective filing date of the claim is that of the disclosure. If the applicant is not able to claim priority of the disclosure, and it was a public disclosure, AIA 35 U.S.C. §§ 102(b)(1)(B) and 102(b)(2)(B) may remove intervening disclosures from the prior art. Assuming that an earlier disclosure took place between March 16, 2012, and March 15, 2013, and a nonprovisional application is to be filed on or after March 16, 2013, the following paragraphs describe the effects of various types of earlier disclosures on the nonprovisional to be filed.

If the earlier disclosure was a public disclosure, e.g., a conference paper, there is a one-year bar date. Just as the disclosure started a CREATE 35 U.S.C. § 102(b) one-year clock running, that clock continues under AIA 35 U.S.C. § 102(b)(1)(A). File the nonprovisional within one year or the public disclosure will be prior art under AIA § 102(a)(1). However, keep in mind that the AIA 35 U.S.C. §§ 102(b)(1)(B) and 102(b)(2)(B) exceptions may apply.

If the earlier disclosure was a provisional application, the question is whether the nonprovisional can claim the priority date of the provisional.[51] As long as the provisional satisfies the written-description and enablement requirements of AIA 35 U.S.C. § 112(a), its priority can be claimed under AIA § 119(e) (best mode is not required). Therefore, the AIA "effective filing date" of the application is the date of the provisional, so the application will be examined under CREATE rules unless a new, March-16-on claim is added to it.

However, if the provisional does not satisfy the written-description and enablement requirements, and a publication claiming the priority of that provisional later publishes, that publication is prior art as of the date of the provisional. However, the AIA 35 U.S.C. §§ 102(b)(2)(A) and 102(b)(2)(C) exceptions will prevent the provisional from being used against the nonprovisional application as long as the provisional shares an inventor with the nonprovisional or was commonly owned as of the filing date of the nonprovisional.

If the earlier disclosure was a nonprovisional application, as with a provisional, if the parent application provides written description and enablement, the child application has the filing date of the parent. If the parent application does not provide those, its eighteen-month publication will be prior art against the later application under AIA 35 U.S.C. § 102(a)(2) if the AIA §§ 102(b)(2)(A) and 102(b)(2)(C) exceptions do not apply.

If the earlier disclosure is a U.S. application claiming foreign priority, remember that the Hilmer doctrine[52] was abolished by the AIA, so U.S. applications claiming foreign priority are prior art as of their foreign priority dates. There is no one-year bar on unpublished-patent-document prior art (AIA 35 U.S.C. § 102(a)(2)), so common-inventor or commonly assigned U.S. patents and applications claiming foreign priority but published after the filing date of the nonprovisional are not prior art against that nonprovisional.

As under CREATE, novelty-defeating events are still significant. When filing an application in view of a pre-AIA disclosure, consider the subject matter carefully, just as you would have under CREATE in view of an earlier disclosure.

III. Conclusion

Under AIA as under CREATE, the daily work of a patent practitioner is to draft applications that satisfy 35 U.S.C. § 112 and to argue that cited references do not anticipate claims or render them obvious (35 U.S.C. §§ 102-103). The AIA should not significantly change application-drafting practice. Although the AIA does change which documents can be used in rejections, it does not change the form or content of rejections nor the ways of arguing in response to them. There is significant continuity from CREATE to AIA, and practitioners will likely readily adapt to the new laws.

Table 1: Types of Prior Art under CREATE

Paragraph in § 102	Relevant date	Prior art before the relevant date is
(a)	Date of invention	what was known or used by others in the U.S. or patented or published anywhere
(b)	One year before date of filing	what was patented or published anywhere, or in public use in the U.S. or on sale (public or private) in the U.S.
(c)	N/A	abandonment of the *invention* (not any specific application claiming the invention)
(d)	Date of publication	a foreign patent by the applicant applied for more than one year before the U.S. filing date and issued before the U.S. filing date
(e)	Date of invention	a U.S. patent or pre-grant publication filed before the date of invention or a PCT application designating the U.S. and filed in English before the date of invention
(f)	N/A	theft of the invention: claims applied for by someone who "did not himself invent the subject matter sought to be patented" will be rejected under 102(f)
(g)	Date of invention	invention of the same claimed subject matter by another who reduced it to practice first or conceived it first and diligently worked until reduction to practice, even if reduction to practice was after the applicant's date of invention

Table 2: Comparison of CREATE and AIA Patentability Provisions

The table is sorted by CREATE provisions rather than AIA provisions, since many of the specific provisions of CREATE no longer exist under AIA. The "keyword" column is a quick reminder of what the CREATE provision covers.

CREATE §,¶	Keyword	AIA §, ¶	Description
102(a) 102(b)	pre-invention pre-filing	102(a)(1)	All non-patent-document prior art is now under AIA 35 U.S.C. § 102(a)(1) and relates to the effective filing date.
102(c) 102(d)	abandoning the invention prior foreign patent	None	Activity before the effective filing date is no longer relevant (*see* MPEP 2134).
102(e)	unpublished patent prior art	102(a)(2)	PCT applications designating the U.S. now count, even if they are not in English.[53] (This provision may turn out to be one of the more significant changes to prior art, especially as machine translation tools improve.)
102(f)	stealing the invention	No direct equivalent; see §§ 115 (b)(2), (h)(3); 135; 291	Nothing in the AIA directly covers former § 102(f).[54] However, the PTO presently plans to reject applications naming incorrect inventors under both §§ 101 and 115.[55]
102(g)	Interference	N/A; see §§ 135, 291	Since date of invention is no longer relevant, except to the extent that an application was derived from another, interference practice no longer exists.
103(a)	Obviousness	103	Various exceptions and details have been moved into AIA 35 U.S.C. § 102, so § 103 now covers only CREATE § 103(a).
103(b)	biotech composition, process claims	None	This provision imputed the non-obviousness of a composition of matter to commonly assigned methods of making or using that composition. The provision has been removed; each claim now stands or falls on its own.
103(c)	exception to (e)-(g) for commonly-assigned art	102(b)(2)(C), 102(c)	This exception has been moved into § 102. Therefore, commonly-assigned patents and published applications filed before the effective filing date but published after are now no longer prior art for obviousness *or novelty*.[56]

Table 3: Summary of CREATE Post-Grant Procedures

CREATE Procedure	Applies to	Effect
Reissue[57]	Any issued patent that is "through error without any deceptive intention, deemed wholly or partly inoperative or invalid."[58] Clerical errors do not qualify.[59]	Prosecution is reopened, and any error as described in "applies to" can be corrected, including errors in priority claims. Broader claims can be presented within two years of the original issue date.
Certificate of Correction[60]	A patent containing a mistake the record shows to be the PTO's fault,[61] or a minor error that is the Applicant's fault.[62]	The corrected patent is as if it had been issued in corrected form.
Correction of inventorship[63]	Inventors listed incorrectly, or omitted incorrectly, through error without deceptive intention.	Correcting inventorship errors means those errors are no longer grounds for invalidating the patent. If not all inventors are in agreement about the change, use reissue instead.
Terminal Disclaimer[64]	Most commonly used in pending applications; however, can also be used in issued patents.	Overcomes nonstatutory obviousness-type double-patenting rejections in pending applications.[65]
Statutory Disclaimer[66]	any issued patent.	Makes the disclaimed claims ineffective; dedicates their contents to the public.
Ex parte reexamination[67]	any issued patent with a claim for which a "substantial new question of patentability" is raised by prior art.[68]	Re-opens examination, particularly to consider the claims with respect to the cited art. Can be used by patentees to preemptively establish the presumption of validity over new art. Can also be used by opponents to challenge patent validity.
Inter partes reexamination[69]	A patent issued on an application filed on or after Nov. 29, 1999. Only a third party files, not the patentee.	As *ex parte* reexamination, but the third-party requester is able to respond to the patentee's arguments.

Table 4: AIA Post-Grant Procedures

Procedures that are substantially unchanged from CREATE are listed "As in CREATE" in the Status column and are described only briefly. *See* Table 3 for more details.

AIA Procedure	Status	Applies to	Effect
Reissue[70]	As in CREATE	"inoperative" issued patents	Corrects the error
Certificate of Correction[71]	As in CREATE	PTO or clerical errors	Corrects the error
Correction of inventorship[72]	As in CREATE	Inventors listed or omitted through error	Corrects the error
Terminal Disclaimer[73]	As in CREATE	Generally, pending applications	Overcomes nonstatutory double-patenting rejections
Statutory Disclaimer[74]	As in CREATE	Any issued patent	Makes the disclaimed claims ineffective
Ex parte reexamination[75]	Broader than in CREATE	Any issued patent with a claim for which a "substantial new question of patentability" is raised by prior art.[76] Can be filed by patentee or a third party.	Re-opens examination, particularly to consider the claims with respect to the cited art. Unlike CREATE, patent owner's statements of record in court or PTO proceedings can be considered during re-examination, although they cannot trigger re-examination.[77]
Post-grant review[78]	New	Any issued patent, within nine months of the issue date (or reissue date). Only a third party files, not the patentee.	The requester can challenge a claim under any ground that can serve as a defense in litigation.[79] This includes AIA 35 U.S.C. 112 minus the best-mode requirement.
Transitional program for covered business method patents	New	A patent with claims for data processing for financial products or services, provided the requester has been accused of infringement. Does not need to be filed within nine months after grant. Only a third party files, not the patentee.	Substantially as post-grant review but with restrictions on the prior art available.[80]
Inter partes review[81]	Replaces *inter partes* reexamination	Any issued patent, starting nine months after issue or after a post-grant review. Only a third party files, not the patentee.	The requester can challenge a claim under AIA 35 U.S.C. 102 or 103 on the basis of patents or printed publications. Must be requested within one year of an allegation of infringement.
Supplemental examination[82]	New	Any issued patent. May be filed by the patentee only.	The patent owner can request *ex parte* reexamination for any information that raises a substantial new question of patentability. Submitting the supplemental-examination request generally forecloses a holding of unenforceability based on the information submitted with the request.[83]

Table 5: Timeline of AIA Post-Grant Procedures

Date	Action by patentee			By either	Action by third party	
			Request a derivation proceeding (same claimed invention; file within one year of own application publication or of issuance).			
Patent issues	Request reissue (error that renders the patent inoperative); Request certificate of correction (PTO or clerical errors); Correct inventorship; File terminal or statutory disclaimer.	Request supple-mental examin-ation[84] (any information that raises a substantial new question of patentability).		Request *ex parte* reexamination. (to consider a substantial new question of patentability raised by patents or printed publications).	Request a transitional proceeding (post-grant review) if the patent is a covered business method patent. Request before Sept. 16, 2020.	Request post-grant review.
issue +9 months						Request *inter partes* review.
issue +12 months						
Infringement alleged						
allegation +1 year						
Patent expires						
expiration +6 years						

Endnotes

1. Leahy-Smith America Invents Act, Pub. L. No. 112-29, 125 Stat. 284 (Sept. 16, 2011).
2. The Patent Act of 1952 (66 Stat. 792) established modern American patent law.
3. Cooperative Research and Technology Enhancement (CREATE) Act of 2004, Pub. L. No. 108-453, http://www.gpo.gov/fdsys/pkg/PLAW-108publ453/html/PLAW-108publ453.htm (accessed Feb. 25, 2013).
4. CREATE codified the exception that commonly assigned patent applications were not 102(e) prior art; see tables at http://uscode.house.gov/classification/priortables.shtml (accessed Feb. 25, 2013), for recent history of Title 35. This includes, curiously, a minor change relating to biological products made by The Patient Protection and Affordable Care Act, Pub. L. 111-148.
5. 78 FR 11059, 11060, left column.
6. *KSR Int'l Co. v. Teleflex Inc.*, 550 U.S. 398 (2007).
7. 78 FR 11059, 11083, left column.
8. Art. 60 EPC, Nov. 29, 2000, http://www.epo.org/law-practice/legal-texts/html/epc/2010/e/ar60.html, retrieved Feb. 25, 2013.
9. Art. 61 EPC, Nov. 29, 2000, http://www.epo.org/law-practice/legal-texts/html/epc/2010/e/ar61.html (accessed Feb. 25, 2013).
10. AIA 35 U.S.C. § 291 (right to relief) and § 135 (requirements for obtaining relief).
11. Patent Law of the People's Republic of China, Aug. 25, 2000, http://www.sipo.gov.cn/sipo_English/laws/lawsregulations/200804/t20080416_380327.html (accessed Feb. 25, 2013).
12. *Id.*
13. AIA § 15(a), codified in AIA 35 U.S.C. §282(b)(3)(A).
14. AIA § 15(b), codified in AIA 35 U.S.C. §§ 119(e)(1) and 120.
15. *See, e.g.*, Crouch, D., *Overkill of the best mode*, Nov. 8, 2012, http://www.patentlyo.com/patent/2012/11/overkill-of-the-best-mode.html, retrieved Feb. 26, 2013.
16. MPEP 2165, II.
17. *Joy v. Cincinnati Mine*, No. 2012-1153 (CAFC 2012, nonprecedential) held that "[to] establish that [a claim] fails the best mode requirement, [the accused infringer] must prove by clear and convincing evidence that the [inventor] *concealed a best mode* of practicing his claimed invention from the public" (emphasis added). *Joy* cites *Young v. Q3*, 112 F.3d 1137, 144 (CAFC 1997) to support the proposition that the best mode need not be disclosed, as the plain language of the statute requires, as long as "the specification adequately disclosed what the inventor contemplated as the best mode so that those having ordinary skill in the art could practice it."
18. Art. 4(A)(3) Paris Convention.
19. Art. 4(A)(2) Paris Convention.
20. The PCT imports the Paris requirements by reference in Article 8(2)(a) PCT. Moreover, the PCT has a best mode requirement of its own (Rule 5(a)(v) PCT, Oct. 9, 2012, http://www.wipo.int/pct/en/texts/rules/r5.htm, retrieved Feb. 26, 2013), albeit one that does not apply to any designated state whose national law does not require best mode.
21. See also MPEP 201.06(c), I: "In order to be complete *for filing date purposes*, all applications filed under 37 C.F.R. 1.53(b) must include a specification as prescribed by 35 U.S.C. 112" (emphasis added).
22. AIA, Pub. L. 112-29, § 3(n)(1).
23. MPEP 715.02; 37 C.F.R. § 1.131.
24. Discussed in MPEP 2138 et seq.
25. *See* MPEP 2163, cited in MPEP 2103, IV.B.1.
26. AIA 35 U.S.C. §§ 100(i)–(j).
27. "If a dispute arises as to which of two applicants is a true inventor (as opposed to who invented it first), it will be resolved through a derivation proceeding conducted by the Board." 77 FR 56068, left column.
28. *Id.* at 56070, center column; AIA 37 C.F.R. § 42.402, reproduced *Id.* at 56091.
29. AIA 35 U.S.C. § 102(b)(2)(C).
30. 78 FR at 11060, right column.
31. AIA 35 U.S.C. §§ 321-329.
32. *See* AIA 35 U.S.C. § 282(b).
33. *See* AIA 35 U.S.C. § 18(a)(1)(C).
34. 77 FR 48680, 48687.
35. AIA 35 U.S.C. §§ 311-319.
36. AIA 35 U.S.C. § 257.
37. AIA 35 U.S.C. §§ 301(a), 302.
38. Lisa Dolak, *Supplemental Examinations and the Client-Practitioner Relationship*, Dec. 30, 2011, http://www.patentlyo.com/patent/2011/12/guest-post-supplemental-examinations-and-the-client-practitioner-relationship-html (accessed Mar. 7, 2013). This is discussed in the Congressional Record, e.g., by Sen. Jon Kyl (Arizona): "[Supplemental examination] will ensure that small and startup companies with important and valid patents will not be denied investment capital because of legal technicalities" such as may be introduced by "an in-house attorney who does a good enough job but who is unfamiliar with all of the sharp corners and pitfalls of the inequitable conduct doctrine." 157 Cong. Rec. S5319 (daily ed. Sept. 6, 2011), right column. This point is also made by the omission from the enacted bill of a provision that would have required that "[no] supplemental examination may be commenced by the Director on, and any pending supplemental examination shall be immediately terminated regarding, an application or patent in connection with which fraud on the Office was practiced or attempted." 157 Cong. Rec. H4420, H4444 (daily ed. June 22, 2011).
39. Barring the AIA 35 U.S.C. § 257(c)(1) effect of supplemental examination, if "inequitable conduct is discovered after a patent issues, the patent will be unenforceable even if it is otherwise valid and infringed." Chisum, Donald S., *Best Mode Concealment and Inequitable Conduct in Patent Procurement: A Nutshell, a Review of Recent Federal Circuit Cases and a Plea for Modest Reform*, 13 Santa Clara Computer & High Tech. L.J. 277, 305 (1997). Available at: http://digitalcommons.law.scu.edu/chtlj/vol13/iss2/1/, retrieved Mar. 7, 2013.
40. AIA 35 U.S.C. § 257(c)(1), but see the exceptions in (c)(2), (e), and (f).
41. Under CREATE, 35 U.S.C. § 102(b) applies to disclosures made more than one year before filing, so implicitly establishes the one-year grace period. Under AIA, 35 U.S.C. § 102(b)(1) expressly establishes a one-year grace period.
42. AIA 35 U.S.C. § 102(b)(1)(B) and (b)(2)(B).
43. 35 U.S.C. § 102(b)(1)(B) and (b)(2)(B).
44. *See, e.g.*, references in Bledsoe, M., & Neu, J. *United States: First To Invent, First To File, Or First To Disclose? Patent Reform's Real Incentive,* Dec. 9, 2011, http://www.mondaq.com/unitedstates/x/156824/, retrieved Feb. 27, 2013.
45. 78 FR 11059.
46. *Id.* at 11077.
47. *Id.*
48. *Id.* at 11079.
49. In Europe, there is a six-month grace period only for "an evident abuse" or for a disclosure made at an international exhibition. *See*

Art. 54(2) EPC, Nov. 29, 2000, http://www.epo.org/law-practice/legal-texts/html/epc/2010/e/ar54.html (accessed Feb. 27, 2013), for the bar and Art. 55(1)(b) EPC, Oct. 5, 1973, http://www.epo.org/law-practice/legal-texts/html/epc/2010/e/ar55.html (accessed Feb. 27, 2013), for the exhibition exception.

50. AIA 37 C.F.R. § 1.130(b); see 78 FR 11059, 11080-11081.
51. Keep in mind MPEP 201.07: "an application that claims benefit of a provisional application is a nonprovisional application of a provisional application, not a continuation, division, or continuation-in-part of the provisional application." However, under AIA 35 U.S.C. § 100(i)(1), "effective filing date" is defined uniformly whether the priority is domestic (35 U.S.C. § 120) or foreign (35 U.S.C. § 119).
52. *In re Hilmer*, 359 F. 2d 859 (CCPA 1966).
53. AIA 35 U.S.C. § 374.
54. Joshua D. Sarnoff, *Derivat*ion and Prior Art Problems with the New Patent Act, 2011 Patently-O Patent Law Review 12, Oct. 7, 2011; a*vailable at* http://www.patentlyo.com/files/sarnoff.2011.derivation.pdf (accessed Mar. 7, 2013).
55. See 78 FR 11059, 11082, center column, § IV. AIA 35 U.S.C. §§ 135, 291 provide only for limited enforcement against derivers of inventions, so the requirements of § 115 are the primary barriers to filing for someone else's invention. Note, however, that § 115(h)(3) does not positively state that a defective oath will render a patent invalid or unenforceable, and does not clearly set forth anything related to pending applications. It will be interesting to see if Congress clarifies this language in the future.
56. Patents issued or applications published before the effective filing date are prior art under AIA § 102(a)(1), except as provided in AIA § 102(b)(1); see 78 FR 11059, 11072, left column.
57. MPEP 1401-1470.
58. CREATE 35 U.S.C. § 251.
59. MPEP 1402.
60. MPEP 1480-1485.
61. 35 U.S.C. § 254.
62. 35 U.S.C. § 255.
63. MPEP 1412.04; 35 U.S.C. § 256.
64. MPEP 1490; 35 U.S.C. § 253.
65. 37 C.F.R. § 1.321(c).
66. MPEP 1490; 35 U.S.C. § 253.
67. MPEP ch. 2200.
68. MPEP 2209.
69. MPEP ch. 2600.
70. MPEP 1401-1470.
71. MPEP 1480-1485.
72. MPEP 1412.04, 35 U.S.C. § 256.
73. MPEP 1490; 35 U.S.C. § 253.
74. *Id*.
75. MPEP ch. 2200.
76. MPEP 2209.
77. AIA 35 U.S.C. § 301(d). See 77 FR 46615, 46616, center column: "Section 6(g) of the AIA amends 35 U.S.C. 301 to expand the information that may be submitted in the file of an issued patent to include written statements of a patent owner filed in a proceeding before a Federal court or the Office in which the patent owner took a position on the scope of any claim of the patent. This amendment limits the Office's use of such written statements to determining the meaning of a patent claim in ex parte reexamination proceedings that have already been ordered and in inter partes review and post grant review proceedings that have already been instituted."
78. AIA 35 U.S.C. §§ 321-329.
79. Grounds for post-grant review are the patent defenses listed in AIA 35 U.S.C. § 282(b).
80. See AIA § 18(a)(1)(C).
81. AIA 35 U.S.C. §§ 311-319.
82. AIA 35 U.S.C. § 257.
83. AIA 35 U.S.C. § 257(c)(1), but see the exceptions in (c)(2), (e), and (f).
84. 77 FR 48828, 48833.

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Clarifying Intellectual Property Rights in Secured Transactions

By Fitzgerald Angrand

I. Introduction

The conflict between the law of secured transactions and intellectual property law makes it an area ripe for legislative action. With the emergence of intellectual property as a driving economic force, Congress should consider establishing a centralized system from which intellectual property can be more easily and efficiently used as collateral by businesses. The law currently struggles to facilitate capital-raising by both emerging and established companies that have valuable intellectual property rights. As a result, practitioners, lenders and debtors are left with uncertainty concerning many of the nuanced issues relating to secured transactions. Creating a federal registry for secured interests in intellectual property would provide the certainty and efficiency necessary to establish, maintain, record, and transfer rights in intellectual property and thereby ensure the sustained growth of its financing.

This article addresses the role of commercial law in promoting the use of secured credit by minimizing transaction costs and enabling simplicity and efficiency in secured transactions. It details basic concepts of intellectual property and secured transactions and discusses the issues and conflicts that arise in the field of secured transactions in intellectual property. It also examines prior efforts to ameliorate some of the problems in this area, and, finally, proposes a legislative solution.

II. The Law of Secured Financing

The purpose and objective of the law of secured transactions is to promote the use of secured credit by allowing parties to obtain security rights in a simple and efficient manner. Secured financing is predicated on the terms by which creditors agree to extend credit.[1] These terms reflect various factors, the most important of which is the transaction costs of making the loan. Ultimately, these costs are passed on to the debtor and borne by society as a whole. The role of the law in secured transactions is to bring certainty to financing transactions, thereby reducing transaction costs and the costs of credit.[2] Because of the constant threat of bankruptcy and default, creditors take measures necessary to ensure that the debtor does not engage in behavior that will threaten its ability to repay. Rather than forcing the creditor to incur the costs of protecting its loan and preventing debtor misbehavior, the law of secured transactions provides rules and procedures meant to do so.[3]

In a credit transaction of any complexity, to protect its security interest the creditor will engage in some monitoring and demand additional compensation for whatever risk of misbehavior remains after all cost-justified monitoring steps have been taken.[4] This monitoring is a result of the creditor's informational disadvantage. Typically, the existence of any liens or encumbrances on intellectual property rights currently is known only to the debtor, despite being critical to the creditor's decision-making process.[5] Costs associated with the risk of debtor misbehavior—such as the cost of the creditor's monitoring activities and the cost of the increased compensation the creditor will demand for assuming the risk of misbehavior—that cannot be eliminated by cost-justified monitoring can be eliminated through legislative change.[6] Instead of forcing parties to structure their agreement to minimize these costs, the law should eliminate the creditor's informational disadvantage and allow for both parties to share in the savings that derive from the efficiency.

> *"Creating a federal registry for secured interests in intellectual property would provide the certainty and efficiency necessary to establish, maintain, record, and transfer rights in intellectual property and thereby ensure the sustained growth of its financing."*

The core principles of the law of secured transactions should supply the basis for assessing the state of secured transactions and for identifying the need for reform. The European Bank, in an attempt to assist member nations in adopting the European Bank for Reconstruction and Development's (EBRD) 1994 Model Law of secured transactions, published a list of core principles to be considered when implementing the law of secured transactions.[7] An important principle was that the law should provide confidence in reducing the risk of giving credit, which, in turn, would increase the availability of credit on improved terms.[8] When analyzing the guiding principles for registry systems, the EBRD acknowledged that the system for publicizing information should be simple, fast, and inexpensive.[9] Despite being based on the European model, the effectiveness of the EBRD's core principles hold true for secured transaction law in general.

III. Fundamentals of Secured Transactions in Intellectual Property

With the growing role of intellectual property in the economy, every effort should be made to facilitate the use of these property rights in financing agreements. This can be achieved most easily by minimizing the complications that arise in connection with transactions. Intellectual property is a crucial part of the country's economic infrastructure. For businesses, intellectual property rights serve as market differentiators that increase the overall value of a product or service. Many secured agreements now use intellectual property as collateral. Given intellectual property's growing popularity in secured transactions and its role in our economy, the law should assure that such transactions are simple and efficient. However, issues relating to the use of intellectual property as collateral persist, and legal uncertainty causes delays and significantly increases the cost of loan transactions. Legislatures should work to eliminate the issues that arise in this context.

IV. Intellectual Property Rights

U.S. law recognizes four types of intangible intellectual property: trade secrets, patents, trademarks, and copyrights. These rights are governed, respectively, by tort and contract law, the Patent Act, the Lanham Act, and the Copyright Act. In addition, to the extent allowed by federal law, states have enacted relevant rules and regulations.

A. Trade Secrets

A trade secret is any information, including formulas, patterns, devices, or compilations, that can be used in the operation of a business or other enterprise that is sufficiently valuable and secret to afford an actual or potential economic advantage over another.[10] Trade secret developed from state common-law protection of propriety information.[11] Thus, trade secrets generally are defined and governed by state common law. State regulation of trade secrets is not preempted by federal law.[12]

B. Copyrights

A copyright is a federal right granted to the creator or owner of an original work of authorship that is fixed in a tangible medium of expression.[13] A copyright owner has the right to prevent others from doing any of the following five activities in connection with the copyright work: (1) reproduction; (2) adaptation; (3) public distribution; (4) public performance; or (5) public display.[14] Registration with the Copyright Office is not required to create legal rights in a work, but registration is a prerequisite to bringing an infringement action. The Copyright Act preempts state law to the extent it implicates copyrightable subject matter and rights commensurate with any of the exclusive copyright rights.[15]

One of the principal benefits of copyright ownership is the ability to transfer some or all of those rights. These transfers can involve all of the rights in a work (an outright assignment) or can be limited to specific rights (a license).[16] Following an assignment, the original owner can no longer control how the transferee exercises its rights. In contrast, with a license the copyright owner maintains ownership of the rights involved but allows a third party to exercise some or all of them.[17] A transfer or license agreement may be recorded in the Copyright Office. Although recordation is not required for a valid copyright transfer, recordation gives all persons constructive notice of the facts stated in the recorded document, as long as the work is specifically identified and registered.[18] In addition, as between two conflicting transfers, a recorded transfer takes priority over an unrecorded one.[19]

C. Patents

A patent is a grant by the federal government to an inventor of the right to exclude others from making, using, or selling the invention for twenty years. Like copyright law, patent law lies solely within the power of the federal government.[20] The U.S. patent system is administrated by the U.S. Patent and Trademark Office (PTO). A patent owner may assign the entire patent right or any lesser interest to another party, and written assignments must be recorded with the PTO.[21]

D. Trademark

A trademark serves as an indication of the origin of those goods or services. Although federally granted trademarks are the responsibility of the PTO, trademark rights arise under state law from the use of business names, images, sounds, and devices in association with the product or service of an enterprise. A trademark that is used in interstate commerce or commerce between a state and a foreign country may be registered with the PTO under the Lanham Act.[22] Trademarks are integral and inseparable elements of the goodwill of the business or service to which they pertain; they cannot be transferred separately from that goodwill.[23]

V. Creation of Security Interest in Intellectual Property Under the UCC

Article 9 of the Uniform Commercial Code (UCC) governs the creation of security interests and the rights of the parties to the security agreement. As revised in 2001, it has been enacted and modified to varying degrees in all fifty states. Article 9 applies specifically to secured transactions in personal property. Intangible property, which includes intellectual property,[24] is a type of personal property. Thus, security interests in intellectual property are covered by Article 9. These rules facilitate financing by creating a comprehensive scheme for the regulation of security interests and by providing creditors with an efficient method of perfecting their security interests. Once the necessary events for the creation of a security interest have occurred, the interest is attached, and it is enforceable against the debtor as to the collateral.

VI. Perfecting a Security Interest

A secured party must perfect its interest in the collateral in order to put the world on notice of the interest and to gain priority rights in the collateral. Perfecting a security interest validates the interest in the collateral against other creditors. Article 9 provides various methods of perfecting security interests. In a financing deal, perfection may be the most important element of the transaction.[25] Perfection of security interests in intellectual property generally is achieved by filing a financing statement with the central filing office in the state where the debtor is deemed to be located.[26] Filing gives constructive notice to the world that a secured party has obtained priority over future creditors with regard to the collateral in question. Despite the simplicity of filing under the UCC, complications arise in connection with the various types of intellectual property rights and the varied role that federal law plays in regulating them. The question of how to perfect security interests in various types of intellectual property turns primarily on the issue of federal preemption.

VII. Issues That Arise in the Field of Secured Transactions in Intellectual Property

A. Preemption

The preemption issue exemplifies the troubling state of the relationship of secured transactions and intellectual property law. The problem arises as a result of the interplay of federal law, which governs the creation, ownership, and transfer of intellectual property, and Article 9 state law, which governs the creation, attachment, perfection, and priority of security interests in personal property. The debate focuses on whether federal or state law should govern the perfection and priority of security interests in patents, copyrights, and trademarks. As a result of conflicting language in federal intellectual property statutes, state Article 9 law, and courts' arbitrary distinctions between similarly situated property rights, contracting parties are compelled to take additional measures to protect their interests. These additional measures cost time and money, which is contrary to the simplicity and efficiency the law is meant to provide.

While all federal preemption ultimately is based on the Supremacy Clause of the U.S. Constitution and the nature of federal law, Article 9 of the UCC also calls for preemption in specific circumstances. The Supremacy Clause provides that the laws of the United States are the supreme law of the land.[27] Thus, the federal government, in exercising its Constitutional powers, prevails over any conflicting or inconsistent state exercise of power.[28] Consequently, where federal statutes govern intellectual property rights, the Supremacy Clause dictates preemption of inconsistent state law. Article 9 expressly exempts assets governed by federal law. Section 9-311(a) provides that the filing of a financing statement is neither necessary nor effective to perfect a security interest in collateral that is subject to a statute, regulation, or treaty of the United States, the requirements of which for a security interest have priority over the rights of a lien creditor and preempt Article 9-310(a).[29] That section states, however, that the state filing system, as under the UCC, must defer to the federal filing system only to the extent the federal statute requires preemption of the state filing requirement.[30] Accordingly, Article 9 still applies when the federal statute does not specifically require preemption.

Where the federal statute clearly preempts, compliance with the federal statute is deemed to be "equivalent" to filing a proper UCC financing statement, and such compliance becomes the exclusive means of perfecting a security interest. UCC § 9-109(c)(1) similarly calls for the preemption of state Article 9 rules.[31] Section 9-109 preemption, rather than applying to rules perfecting security interests, governs other interests, such as the rights of parties to, and third parties affected by, transactions in particular types of property.[32]

Because none of the intellectual property statutes provides for the creation of security interests, but all have rules pertaining to the filing of ownership interests, in order to determine whether the respective federal statute preempts Article 9, courts must engage in statutory interpretation to determine the extent to which they preempt.[33] Courts have interpreted the two Article 9 preemption sections as mandating preemption only when the federal statute fits within the preemption language of Article 9 and when the statute reflects the intent to create a registration system that would serve the notice function of the UCC filing system. This has resulted in great disparity among the different types of intellectual property. Courts in patent and trademark cases have agreed that at least to a certain extent state Article 9 law governs financing transactions involving the use of these intellectual property assets as collateral. As explained below, however, courts in copyright cases have reached a different conclusion

B. Copyrights

The Copyright Act provides that agreements granting security interests in copyrights should be filed with the Copyright Office rather than with the state recordation office as under the UCC,[34] but the courts have created distinctions that leave parties to copyright-centered transactions uncertain about their interests.[35] In contrast to the other federal intellectual property statutes, the Copyright Act defines ownership to include transfers of security interests.[36] Consequently, the ownership recordation rules described in the statute have been interpreted to include security interests. Moreover, courts have held that filing security agreement documents establishes constructive notice and triggers certain basic priority rules. Therefore, the filing system established by the Act is adequate for security interests in registered copyrights. Three leading cases—all from the Ninth Circuit—address the preemptive effect of the Copyright Act on Article 9: *In re Peregrine*,[37] *In re Avalon Software*,[38] and *In re World Auxiliary Power Co*.[39]

In *In re Peregrine*, the trustee in a bankruptcy proceeding challenged the Article 9 perfection by filing a security interest in the debtor's copyrighted film library.[40] In holding that the Article 9 perfection and priority rules must yield to the recording and priority provisions of the Copyright Act, the Ninth Circuit noted that the value of a recording system lies in giving parties a specific place to look to discover, with certainty, whether a particular interest has been transferred or encumbered. The court reasoned that since the Copyright Act and Article 9 set forth different priority schemes leading to different results, this conflict warranted preemption of Article 9.[41] But the court recognized the cumbersome aspects of a federal copyright filing system.[42] For example, it held that a commercial lender who seeks collateral in a borrower's copyright must file individual applications for each work and must continue to update filings as new works are created. Federal filing requirements also put a burden on the lender by requiring it to ensure that the borrower maintains registration of the copyright via a renewal process.[43] This result, as applied to the parties in *In re Peregrine*, would require the lender to renew its interest every time the debtor added a new work to its copyright library.

The court in *In re Avalon* followed the ruling in *In re Peregrine* that the Copyright Act governs perfection of security interests.[44] The court observed that a product entitled to be registered at the Copyright Office does not change its character, and with it the requirement to file a security interest with the Copyright Office, simply because its creator did not actually register it with the Copyright Office. The *Avalon* court held that it is "immaterial whether the debtor has registered its copyrightable material." Where an unregistered copyright is at issue, the court concluded that a creditor has the burden of perfecting a security interest by ensuring that the copyright is registered and that notice of the security interest is filed with the Copyright Office. Thus, an unregistered copyright may be perfected only by both registering the copyright and recording the security interest with the Copyright Office.

In *In re World Auxiliary Power Co*., the court distinguished unregistered copyrights from registered copyrights for perfection purposes.[45] The court adopted the holding of *Peregrine,* limited to registered copyrights, but it declined to follow *In re Avalon* as it applied to unregistered copyrights. Resolving a split among district courts, the Ninth Circuit concluded that none of the provisions of Article 9 are displaced by the Copyright Act where the copyright collateral has not been registered.[46] Although registration is not a prerequisite for the creation of copyright rights, the court held that so long as the work remains unregistered, there is no record of the copyright. Consequently, no creditor may file a security interest in an unregistered copyright. Therefore, the perfection of security interests in registered copyrights requires filing with the Copyright Office, while filing financing statements for unregistered copyrights must be done in accordance with the UCC.

This situation involving the perfection of unregistered copyrights invites legislation. In its absence, lenders will be unsure as to whether they should file with the Copyright Office or with the state recordation office. As a result of this uncertainty, creditors could file in both places to ensure proper perfection.[47] Alternatively, the creditor can require that the debtor register its copyrights prior to filing with the Copyright Office. For a special fee, the Copyright Office allows for expedited registration, which would be beneficial in such cases.[48] In either case, the financial burden of the uncertainty ultimately falls on the contracting parties.

It has been argued that because it is easy to identify registered copyrights through the Copyright Office, recordation under federal law suffices to serve basic recordation purposes.[49] Further, in the context of the entertainment industry—the area in which copyrights are used as security interests most frequently—lenders want security with respect to the specific asset, rather than with respect to the owner.[50] Since state Article 9 registries generally do not prioritize with respect to the asset, copyrights would be better registered in the federal registry, where prioritization is arranged by asset. Others have argued that because the seminal court decisions predated the 2001 Article 9 revisions, they reflect the prior, less restrictive preemption provision. It is argued that Section 311 of the revised Article 9 attempts to avoid preemption by using narrow language, recommending that only federal laws that specifically discuss the priority rules of security interests should preempt the UCC. While many commentators agree that the revised Article 9 may prompt courts to construe preemption more narrowly and expand the scope of property covered by Article 9, skeptics argue that it will not change the registration procedures[51] and that current case law will continue to control.[52]

C. Patents

Courts have held that the Patent Act does not preempt Article 9 and that a security interest in a patent may be perfected by filing a UCC financing statement,[53] whereas an assignment of a patent is governed by the Patent Act. The court in *In re Transportation Design*, and subsequently the Ninth Circuit in *In re Cybernetic Services*, held that the Patent Act does not sufficiently address the perfection of patents and that the UCC therefore is to be followed in perfecting a patent.[54] The Ninth Circuit concluded that the Patent Act preempts state filing only with respect to ownership interests in patents, not with respect to secured interests in patents. Further, it held that the Patent Act does not preempt Article 9 because the Patent Act addresses only ownership interest transfers.[55]

However, the utility and value of patents derive from their ability to be assigned, granted, or conveyed. Assignments and conveyances that go beyond mere licensing are governed by the Patent Act. Therefore, priority rules, as they relate to assignments, are governed by the Patent Act as well.[56] Section 261 of the Act provides that an assignment of a patent is void against subsequent purchasers without notice unless it is recorded in the PTO.[57] As a result of this requirement, any assignment transferred in accordance with Article 9 will be construed by the courts as a "mere license."[58] Therefore, an improperly filed conveyance can be detrimental to the interest of an assignee.[59]

In sum, patents must be perfected under Article 9, while assignments must be recorded in accordance with the Patent Act.

D. Trademarks

While the rule governing the perfection of security interests in trademarks is straightforward, the existence of different rules for priority causes confusion. Courts have held that perfecting a security interest in a federally registered trademark can be achieved only with a UCC filing statement.[60] A right in trademark is acquired through use in commerce, fundamentally a state common-law entitlement.[61] Although federal law (Lanham Act) provides for a federally recognized trademark right, its provision for registration and recordation is extremely limited and has been held not to preempt the UCC.[62] However, the Lanham Act does provide priority rules for the assignment of federally registered trademarks to govern the claims of subsequent purchasers for valuable consideration without notice. Since a security agreement generally does not involve a present assignment or transfer of title, the Lanham Act is thought to apply only upon a subsequent purchase without notice.[63]

Courts have interpreted the interplay of the UCC rule and the Lanham Act as providing that the recording of a security interest in a trademark at the PTO is ineffective for perfection and that the term "assignment" in the Act does not include security interests.[64] Uncertainty remains as to whether a UCC filing will perfect a registered mark as against a subsequent purchaser. Consequently, to protect their rights against third parties, lenders will file with the PTO as well as with the state.[65]

VIII. Other Issues Under Federal Rules

A serious argument against following the federal intellectual property statutes rather than Article 9 with respect to security interests is that the statutes do not address the nuanced issues that arise in complex secured transactions that otherwise would be addressed by the UCC. It is recognized that applying federal law to the perfection of security interests in intellectual property, or related proceeds or rights to payments, including license royalties, creates problems for lenders and ultimately for borrowers. These problems include the lack of a floating lien and filing and search delays.

A. Floating Lien

The federal filing system does not have a mechanism for recording floating liens. Often, a creditor will request as collateral not only the debtor's current assets, but also property it later comes to own. These encumbrances, referred to as floating liens, are governed by Section 9-204 of the UCC, which validates a security agreement that creates or provides for a security interest in property the debtor acquires after the security interest attaches.[66] The UCC does not require the lender to file a separate financing statement every time the debtor acquires new property. In contrast, federal filings are on an individual basis; there is nothing comparable to a floating lien for patents, trademarks, or copyrights. The federal system requires a description of the property right being recorded, which leaves lenders unable to file claims to patents, trademarks, or copyrights that do not yet exist. This results from the federal registry being organized by asset rather than by owner. Consequently, lenders cannot file floating liens on all property, present and future, owned by the debtor. This contrasts with the Article 9 recordation system, which organizes property rights by owner. This more effectively allows the lender to secure rights over the debtor's future property.

B. Filing and Search Delays

The recordation provisions of the federal statutes call for an extensive grace period following a transfer or assignment to allow for the property right to be recorded in the federal office. For example, Section 261 of the Patent Act provides for a three-month look-back period, the effect of which is to void an assignment as against any subsequent purchaser for valuable consideration without notice unless it is recorded in the PTO within three months from its date or any time prior to the subsequent purchase.[67] As a result, a subsequent purchaser who searches the federal records for a previous purchaser may not see recorded a sale that occurred in the previous three months that may have priority over its own purchase.[68] The grace period causes a three-month delay for subsequent purchasers, which can seriously disrupt loan transaction closings unless the lender is willing to take the chance that there is no prior transfer.[69] However, it is unlikely that a lender would be willing to release the agreed-upon loan without first ensuring that the time for protecting any potential prior interest by recording has expired.[70] As a result, this grace period causes a three-month delay on transaction closings. There are no such grace periods in Article 9.

IX. Prior Attempts at Reform

The debate over federal preemption versus state regulation has inspired many proposals but no successful legislative efforts. One such proposal was made by the

American Bar Association Intellectual Property Law Section, the ABA Business Law Section, and the Commercial Finance Association. The Federal Intellectual Property Security Act (FIPSA), proposed in 1999, advocated a dual system for perfection of copyrights where security interests are filed at the state level and ownership interests at the federal level.[71] The stated purpose of the bill was to "make substantive and procedural changes to the law in order to provide uniformity and certainty and to facilitate financing of Federal intellectual property, consistent with the rights of owners and assignees of interests in such property."[72]

Since courts have identified different requirements for perfecting notice with respect to copyrights as opposed to patents and/or trademarks, the bill was meant to create a federal financing statement for recording security interests in federal intellectual property.[73] Filing the federal financing statement would provide nationwide notice to all interested parties of the security interest in a particular intellectual property or properties.[74] The ABA subcommittee's main concern was the devaluing of intellectual property by lenders to reflect the risks and uncertainty associated with secured lending. In proposing the mixed system, in which perfection is governed by the UCC and priority and transfers are governed by the federal filing system, the proposal reasoned that lenders prefer the UCC filing system because: (1) the UCC permits floating liens without requiring registration of derivative works; (2) UCC notice filings can be made by describing the collateral in general terms, even in advance of the closing of the transaction; (3) a lender can conduct UCC searches in the applicable state by reference to the debtor's name instead of by registration number in the Copyright Office; and (4) the UCC does not use a look-back provision.[75]

This dual approach has the UCC govern where appropriate, thereby allowing parties to take advantage of the Code's accepted principles where applicable, while still following the federal rules where applicable.[76] In addition, it alleviates the confusion over which system to follow by requiring filing in both. The *Peregrine* court, however, identified the key argument against this type of dual filing by pointing out that recordation schemes best serve their purpose when interested parties can obtain notice of all encumbrances by referring to a single, precisely defined recordation system.[77] The problem with a dual recordation system is that the effectiveness of one system at putting parties on constructive notice as to encumbrances on the property would interfere with the effectiveness of the other. To the extent the two systems compete, the utility of each diminishes.[78]

Another issue with recognition of a state recordation system is that its acceptance would effectively have copyrights, which are meant to be recognized nationally, supported by state record offices rather than by the Copyright Office.[79] The UCC, which ordinarily deals with assets that fit easily within the regulatory reach of individual states, is not well-equipped to handle assets that can exist in multiple states.

The Copyright Modernization Act is another proposal to solve the problem of confusing and conflicting filing requirements.[80] This bill, which was first proposed by the American Film Marketing Institute, calls for a federal regime to resolve the issues concerning floating liens and after-acquired property.[81] It calls for the Copyright Office to implement a dual indexing system that catalogs copyrighted works under the owner's name and under the title of the work. Once the filings are linked, the computerized system would be able to recognize encumbrances put on a particular individual's property as well as the works that are encumbered. Either index would serve notice as well as be necessary for perfection.[82] The primary issue with this proposal was that it put an undue burden on the Copyright Office.

X. Argument for Proposal

A. Economic and Practical Issues That Call for a Unified Registry

The overall goal of the recordation system is to provide a means for sharing information and ordering priority with the aim of helping lenders minimize their credit risks while reducing transaction costs. Searchers need a specific place to look to determine whether a property interest has been encumbered or transferred. To the extent there are competing recordation schemes, it lessens the utility of each.[83] Easy access to ownership and security interests concerning a debtor's intellectual property assets would ease the burden on the lender in researching proposed collateral. In addition, one central registry for perfecting security interests would ease the burden on the lender in determining how to perfect its interest so as to obtain priority.

As long as there is uncertainty and confusion as to how to perfect its interest, the lender will have to take additional, arguably unnecessary, steps to ensure that its title or lien rights are not defective. The cost of these additional measures ultimately will be borne by the debtor through the terms of the security agreement. Since an entity granting credit will usually ensure that all costs connected with the credit are passed on to the debtor, high costs of security will be reflected in the price for credit and will diminish the efficiency of the credit market. The inefficiency described above not only cuts against the core principles of the law of secured transactions but also results in the debtor being forced to pay for the uncertainty in the law.

A uniform central system for all transactions relating to intellectual property would best meet the realities of the growing role of complex intellectual property transactions. Modern secured transaction involving intellectual property often will consist of collective packages of multiple intellectual property rights. As a result, for one transaction, a lender may be dealing with each of the different property rights and with the differing rules that come with them.

Currently, a lender perfecting its interest in such packages will have to search the different federal registries as well as the state registries and to follow the differing filing rules applicable to each property right.[84] This obviously is cumbersome. In addition, the federal statutes governing intellectual property are not well equipped to handle the minute issues that can arise in complex secured transactions. Individual states, on the other hand, are not well-equipped to handle intellectual property, which by its nature crosses borders and affects interstate commerce. The best way to address these issues is to create a federal registry that clearly governs transactions involving intellectual property ownership rights.

A registry that combines the ownership registry and the security interest registry would provide a "one-stop shop" for all parties that intend to transact with intellectual property. Since intellectual property assets can be used as collateral, secured creditors should be able to search state and federal records within a single electronic operation and have a single reliable mode for the perfection of security interests in these types of intellectual property. This would create ease for creditors looking to protect their title and ensuring that there has been no previous transfer or that there will be no future unauthorized transfers that can endanger the transaction.

B. Proposal

A central registry can serve as an informational portal that collects data pertaining to ownership rights from the various federal recordation registries. In addition, it would contain data for all secured transactions as related to particular property interests. Using this system, a secured creditor or a prospective creditor would be able to search for previous encumbrances and conveyances to ensure that their interests are protected as against other claimants. The registry would allow the creditor to secure its interest, whether in an assignment, a license, or a secured credit, by filing an agreement or financing statement with the registry. This filing would protect that creditor from future claims made on the property.

Interests would be searchable under both the owner and the property and would be cross-referenced so that a search for a particular owner would reveal a complete list of that owner's intellectual property interests, as would a search of a particular property right. Similar to real property registries, a search of a property interest would reveal all conveyances of that property right to have occurred within a certain period of time. These rules combine the search methods that currently exist in both the state and federal registries as well as in state real estate registries, which this model strongly resembles. This method would allow a creditor to secure an interest in a debtor's property that may not have existed at the time of the agreement or the filing.

In contrast to the current federal system, which requires the lender to make multiple, burdensome filings and to rely on the record or on the word of the borrower, this proposal would solve the notice issue of floating liens. This structure will not require the creditor to rely on the debtor to be forthright whenever it comes to own a new intellectual property right. Moreover, this protection of floating liens would not run afoul of the notice requirement of federal intellectual property laws, since constructive notice would be provided by the debtor's name at the time the floating lien is filed. As a practical matter, lenders should not be required to monitor thousands of intangibles to ensure that their registrations are filed and renewed. This new process will save creditors substantial time and energy and will give them assurance when providing funding to new ventures.

This proposed system would also eliminate the look-back grace periods provided by the federal statutes. Modeling itself on the UCC rather than on the federal statutes, the registry will provide that proper filing, which effectively puts the world on notice, merits priority over future claims. Until an interest is recorded, subsequent filers would take priority. This would help the lender easily ascertain whether competing interests already exist. Because the system provides a simple way to file interests in property, a responsible lender can easily ensure protection of their interest by going to the registry.

In line with the core principles of secured transactions law, the proposed unified registry would provide simplicity and efficiency to contracting parties. The unified registry would limit the work creditors must do to protect their interest. Instead of having to research the law only to determine that they need to record their interest everywhere because the rules are not clear, creditors will be able easily search one database and use this same system for recordation. This, in turn, will drive down the cost of transacting and incentivize lenders to continue providing loans to companies that may have only intellectual property to serve as collateral. The centralized system would maximize the effectiveness of recordation by allowing lenders to value their transactions based solely on asset value rather than on the excess transaction costs.

A similar proposal was made in the Copyright Modernization Act. The critics of the proposal argued that it would place too much of a burden on the federal government. But given the inefficiency of the current system, and the impediment it presents to intellectual property transactions, the economic benefits will outweigh the costs to the government. Promoting lower transactional risks will promote the growth of intellectual property in keeping with the principles of secured transactions.

States may be reluctant to relinquish jurisdiction over this type of secured transaction, but the proposal does not require complete abandonment of state Article 9 rules. The registry would serve the purpose of collecting and providing information and would be a uniform means of perfecting interests. However, the state would maintain the right to govern the priority and other ownership rules. The proposed system would allow parties to record their interests, so it would comply with the UCC "file to perfect" requirement and—being federally run—would not run afoul of the Supremacy clause or UCC preemption rules.

XI. Conclusion

Intellectual property is a driving force in the U.S. economy and will continue to grow in importance. Secured interests in intangible assets have to be clearly established, easily searchable, and uncomplicated to create. When that is the case, they will be recognized by financial markets as part of a company's overall asset value. An integrated registry for intellectual property would ease the burden and restore cost-efficiency and predictability to financing agreements, to the benefit of all parties involved.

Endnotes

1. *See* UNCITRAL, *UNCITRAL Legislative Guide on Secured Transactions: Terminology and Recommendations*, United Nations Publication, December 2009, http://www.uncitral.org/pdf/english/texts/security-lg/e/Terminology-and-Recs.18-1-10.pdf (last visited Dec. 4, 2012).
2. *See id.*
3. *See id.*
4. *See* Kronman, Anthony Townsend and Jackson, Thomas H., *Secured Financing and Priorities Among Creditors* (1979), Faculty Scholarship Series. Paper 1070, http://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=2069&context=fss_papers (last visited December 4, 2012).
5. *See* William J. Murphy, *Proposal for a Centralized and Integrated Registry for Security Interests in Intellectual Property*, 41 IDEA: The Journal of Law and Technology, 297, 306 (2002).
6. *See id.*
7. *See* European Bank for Reconstruction and Development, "Core Principles for a Secured Transactions Law," July 2, 2010, http://www.ebrd.com/pages/sector/legal/secured/core/coreprinciples.shtml (last visited Dec. 3, 2012).
8. *See id*.
9. *See id*.
10. *See id*.
11. *See id.*
12. *See id.*
13. *See* 17 U.S.C.A. § 101.
14. *See supra* note 5.
15. *See id.*
16. *See* Beck & Tysver Law–Bitlaw, *Copyright Licenses and Assignments*, http://www.bitlaw.com/copyright/license.html (last visited Feb. 20, 2013).
17. *See id*.
18. *See* 17 U.S.C.A. § 205.
19. *See id*.
20. *See id.* at 311.
21. *See id.*
22. *See* Susan Barbieri Montgomery, *Security Interests in Intellectual Property*, SM088 ALI-ABA 373, 400 (2007).
23. *See id.* at 401.
24. Official Comment 5(d) to UCC 9-102 makes clear that intellectual property rights are viewed as general intangibles in the UCC.
25. *See* Jennifer Sarnelli, *Grasping for Air: Revised Article 9 and Intellectual Property in an Electronic World*, 11 UCLA Ent. L. Rev. 103, 110 (Winter 2004).
26. *See* § 9-310. When Filing Required to Perfect Security Interest or Agricultural Lien; Security Interests and Agricultural Liens to Which Filing Provisions Do Not Apply, Unif. Commercial Code § 9-310.
27. *See* U.S. Const. art. VI, cl. 2.
28. *See id.*
29. *See* § 9-311. Perfection of Security Interests in Property Subject to Certain Statutes, Regulations, and Treaties, Unif. Commercial Code § 9-311.
30. *See id.*
31. *See* § 9-109(c)(1). Scope., Unif. Commercial Code § 9-109.
32. *See supra* note 22.
33. *See id.*
34. A security agreement providing for a security interest in the debtor's copyrights is a "transfer" of copyright under the Copyright Act, and is thus recordable in the Copyright Office. The Copyright Act priority rule in Section 205(c) applies only to "transfer," but would appear also to apply to an appropriate "notice or memorandum of the transfer" authorized by Section 204. As a result, it is only necessary to file with the Copyright Office either the actual security agreement or an appropriate "notice or memorandum" of the security interest grant.
35. *See* 17 U.S.C.A. § 101.
36. *See id.*
37. *See In re Peregrine Entm't, Ltd.*, 116 B.R. 194 (C.D. Cal. 1990).
38. *See In re Avalon Software Inc.*, 209 B.R. 517 (Bankr. D. Ariz. 1997).
39. *See In re World Auxiliary Power Co.*, 303 F.3d 1120, 1135 (9th Cir. 2002).
40. *See In re Peregrine Entm't, Ltd*.
41. *See id.*
42. *See supra* note 25.
43. *See id.*
44. *See In re Avalon Software Inc*.
45. *See In re World Auxiliary Power Co*.
46. *See id.*
47. *See supra* note 25.
48. *See id.*
49. *See* Warren E. Agin, *The Internet Bankruptcy: What Happens When the Bell Tolls for the eCommerce Industry?*, 1 J.HighTech.L. 1 (2002).
50. *See id.*
51. *See supra* note 25.
52. *See id*.
53. *See In re Cybernetic Services, Inc.*, 252 F.3d 1039 (9th Cir. 2001).

54. *See id.*
55. *See id.*
56. *See* 35 U.S.C.A 261.
57. *See id*.
58. A license differs greatly from an assignment or conveyance in that a license merely serves as an authorization by the owner of the right to another party to use those rights while an assignment effectively transfers title and ownership right to the purchasing party.
59. *See* Joseph Richard Falcon, *Managing Intellectual Property Rights: The Cost of Innovation*, 6 Duq.Bus.L.J. 241, 262 (Spring 2004).
60. *See supra* note 28.
61. *See* Thomas M. Ward, *Intellectual Property Collateral Perfection and Proceeds in Bankruptcy*, SN086 ALI-ABA 379, 405 (2008).
62. *See id.* at 393.
63. *See id.*
64. *See id.*
65. *See supra* note 22.
66. *See* § 9-204. After-Acquired Property; Future Advances., Unif. Commercial Code § 9-204.
67. *See* 35 U.S.C.A. § 261.
68. *See supra* note 5.
69. *See id.*
70. *See id.*
71. *See supra* note 22.
72. *See* Todd Dickinson: Former Acting Assistant Secretary of Commerce and Acting Commissioner of Patents and Trademarks, "Before the Subcommittee on Courts and Intellectual Property Committee on the Judiciary, U.S. House of Representatives, June, 24, 1999, http://www.ogc.doc.gov/ogc/legreg/testimon/106f/dickinson0624.htm (last visited December 4, 2012).
73. *See id.*
74. *See id.*
75. *See* Ara A. Babaian, *Striving for Perfection: The Reform Proposals for Copyright-Secured Financing*, 33 Loy. L.A. L. Rev. 1205, 1228 (2000).
76. *See id.*
77. *See id.*
78. *See id.*
79. *See id.*
80. *See id.* at 1234.
81. *See id.*
82. *See id.*
83. *See supra* note 75.
84. *See id*.

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Does the First Sale Doctrine Protect the Resale of Digital Music Files?

By Heather C. Hili

I. Introduction

Eventually, many of us reach a point where we no longer need or want some of the music we have purchased and look to resell it. In the past, the resale took place through a used record store. Now, however, when most music is purchased online in the form of digital music files, the issue arises of how to resell digital music purchased through an online music store such as iTunes. Recently, a website known as ReDigi[1] was developed to solve this problem by creating an online market for "used" digital music. ReDigi describes itself as "your favorite used record store, but for digital music files."[2] Through ReDigi a consumer can buy "used" digital music files for 79 cents[3] rather than purchasing a "new" copy of the same song on iTunes for 99 cents or more.[4] Unlike a used CD, when a "used" digital music file is sold for a lower price, it is of the same quality and value as a "new" digital music file. Therefore, there is no logical justification in terms of product quality for the price discount. While this is a good thing for consumers, it creates unwanted competition for record labels.

Although the consumer owns the copy of the sound recording, the record label owns the copyright.[5] The issue presented by ReDigi is whether any of the record label's rights are infringed when ReDigi allows consumers to sell "used" digital music files or whether the first sale doctrine[6] protects ReDigi's act of reselling.

The theory that ReDigi is a copyright infringer is being tested in the case brought against ReDigi by Capitol Records ("Capitol") in the Southern District of New York.[7] Capitol alleges that ReDigi has infringed its reproduction and distribution rights in its copyrighted sound recordings.[8] This article will explore the issues involved in the lawsuit, in particular the applicability of the first sale doctrine to digital technology.

II. The Right to Reproduce and Distribute Sound Recordings

Section 102(a)(7) of the Copyright Act,[9] which provides copyright protection for sound recordings, gives record labels certain exclusive rights.[10] Under section 106(1) the copyright owner has the exclusive right to reproduce and authorize the reproduction of the copyrighted work. Accordingly, if a sound recording is copied without permission of the record label, the record label's reproduction right has been infringed.[11]

The other exclusive copyright right relevant to ReDigi is the section 106(3) distribution right, which gives the copyright owner the right to "control the first public distribution of any material embodiment of the work, whether or not the copy or phonorecord was lawfully made."[12] An important limitation on the distribution right is the first sale doctrine, codified in section 109(a), which provides that "[n]otwithstanding the provisions of section 106(3), the owner of a particular copy or phonorecord lawfully made under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord."[13] Section 109(a) "makes clear [that]…the copyright owner's rights under section 106(3) cease with respect to a particular copy or phonorecord once he has parted with ownership of it."[14]

> *"The issue presented by ReDigi is whether any of the record label's rights are infringed when ReDigi allows consumers to sell 'used' digital music files or whether the first sale doctrine protects ReDigi's act of reselling."*

III. The First Sale Doctrine

A. Origins

The first sale doctrine originated with the Supreme Court decision in *Bobbs-Merrill Co. v. Straus*.[15] In that case, the defendants—the Macy's department store—purchased copies of a novel from wholesale dealers to sell for 89 cents per copy despite a notice printed in the book that "The price of this book at retail is $1 net. No dealer is licensed to sell it at a less price, and a sale at a less price will be treated as an infringement of the copyright."[16] The copyright owners sued to "restrain the sale of [the] copyrighted novel…at retail at less than $1 for each copy."[17] The case turned on whether "power to control further sales is given by statute to the owner of such a copyright."[18] The Court held that the copyright law, "while protecting the owner of the copyright in his right to multiply and sell his production, do[es] not create the right to impose…a limitation at which the book shall be sold at retail by future purchasers, with whom there is no privity of contract."[19] The Court explained that the copyright owner exercised its right to create copies of the novel and to sell the copies at a price it found to be satisfactory.[20] However, the Court held that the statute did not create a right to control future retail sales of the copies, stating that "[t]he purchaser of a book, once sold by authority of the owner of the copyright, may sell it again, although he could not publish a new edition of it."[21]

One year later Congress codified the first sale doctrine in section 27 of the 1909 Copyright Act, which provided that "nothing in this title shall be deemed to forbid, prevent, or restrict the transfer of any copy of a copyrighted work the possession of which has been lawfully obtained."[22] Later, when Congress enacted the Copyright Act of 1976, the first sale doctrine was carried over and codified in section 109(a).[23]

B. Rationale

A 1984 House Report concerning the rental, lease, and lending of sound recordings described the first sale doctrine as having its roots in the English common law rule against restraints on alienation of property.[24] The report explained that American courts, in applying the first sale doctrine, have distinguished between the copyright owner's exclusive rights in the copyrighted work and the rights of the owner of an object embodying the copyrighted work.[25] In a case brought under the 1909 Copyright Act, *C.M. Paula Co. v. Logan*,[26] the court explained that

> continued control over the vending of copies is not so much a supplement to the intangible copyright, but is rather primarily a device for controlling the disposition of the tangible personal property which embodies the copyrighted work. Therefore, at this point the policy favoring a copyright monopoly for authors gives way to the policy opposing restraints of trade and to restraints on alienation.[27]

Courts also have discussed an economic rationale for the first sale doctrine. In *Burke & Van Heusen, Inc. v. Arrow Drug, Inc.*,[28] the court explained that "the ultimate question under the 'first sale' doctrine is whether or not there has been such a disposition of the copyrighted article that it may fairly be said that the copyright proprietor has received his reward for its use."[29] *Arrow Drug* involved the resale of records, and the court ruled in favor of the defendant after concluding that the plaintiff already had received its reward in the form of royalties from the first sale of the records.[30]

The first sale doctrine arose in connection with the transfer of tangible goods, but many of these tangible works are now available in digital form, which raises questions about the continued applicability of the first sale doctrine to digital media.

C. Changes in Technology and the First Sale Doctrine

In 2001 the Copyright Office issued a report on the Digital Millennium Copyright Act[31] which included a discussion about the relationship between section 109 and existing and emerging technology.[32] The report also focused on three proposals, one of which was the creation of a "digital first sale doctrine,"[33] and it also discussed the idea of expanding the first sale doctrine to encompass the digital transmission of copyrighted works.[34]

In analyzing the relationship between the first sale doctrine and technology, the report explored the difficulty of applying the concept of the free alienability of tangible goods[35] to digital works:

> The tangible nature of a copy is a defining element of the first sale doctrine and critical to its rationale. The digital transmission of a work does not implicate the alienability of a physical artifact. When a work is transmitted, the sender is exercising control over the intangible work through its reproduction rather than common law dominion over an item of tangible personal property.[36]

In other words, transmitting a digital work implicates the right of reproduction, whereas transmitting a tangible work does not.[37]

In addition to digital transmission not fitting into the property law rationale behind the first sale doctrine, the Copyright Office explained why transmitting digital works also does not fit into the economic rationale:

> Physical copies degrade with time and use; digital information does not. Works in digital format can be reproduced flawlessly, and disseminated to nearly any point on the globe instantly and at negligible cost. Digital transmissions can adversely affect the market for the original to a much greater degree than transfers of physical copies.[38]

As noted above, the economic reasoning behind the first sale doctrine is that the copyright owner already has been rewarded for the sale of the work.[39] This reasoning applies to digital works only to a certain extent. Although it is true that the copyright owner will be rewarded for the first sale of the work, the report suggests that transmitting works in a digital format will adversely affect the market for the original work and therefore negatively impact the copyright owner.[40] There is, of course, an adverse effect on the market for the original work when physical works are resold, but the significant difference is that the value of physical works decreases over time, whereas the value of a digital work does not.[41] In other words, there will, arguably, always be a market for a new copy of a physical work, but the same cannot be said for a digital work because the "new" and "used" copies are identical.[42]

The Copyright Office rejected the proposal for a "digital first sale doctrine."[43] The report focused on the question of "whether the conduct of transmitting the work digitally, so that another person received a copy of the work, falls within the scope of the defense."[44] The scope of the defense under section 109(a) is limited to the copyright owner's distribution right;[45] it does not cover the reproduction right.[46] "Therefore," the report states, "when the owner of a lawful copy of a copyrighted work digitally transmits that work in a way that exercises the reproduction right without authorization, section 109 does not provide a defense to infringement."[47]

After concluding that the first sale doctrine does not provide a defense against unauthorized digital transmissions, the report turned to the idea of expanding the first sale doctrine to cover such a process.[48] Proponents of the expansion argued that there are similarities between the transfer of a physical work and the transfer of a digital work.[49] This argument focused on the assumption that transferring a physical copy is the same as transferring a digital copy because in the end the transferor no longer has a copy.[50] This assumption is based on the implication of "forward and delete" technology, in which the original owner no longer has access to his or her copy of the file after forwarding it.[51] However, the report concludes that the differences outweigh the similarities and that the first sale doctrine therefore should not be expanded.[52] It suggests that even if a "forward and delete" technology were implicated, the first sale doctrine should not apply because it would be difficult to ascertain whether the act of deleting the original copy actually took place, and this uncertainty comes with an increased risk of infringement.[53] Removing legal limitations on retransmissions would "make it too easy for unauthorized copies to be made and distributed, seriously harming the market for those works."[54]

The report ultimately concluded that no change should be made to the first sale doctrine.[55] However, the Copyright Office acknowledged legitimate concerns about the effects of technology such as "forward and delete" becoming available.[56] Today "forward and delete" does exist;[57] as a result, the Copyright Office should revisit whether this new technology warrants creating a digital first sale doctrine. Or, does the first sale doctrine currently apply when a digital file is transmitted without making a copy of that file?[58]

IV. ReDigi

ReDigi provides three services to users who download and install its "ReDigi Marketplace App": storing, streaming, and selling digital music.[59] By downloading and installing this system, users have access to free, unlimited cloud storage for the songs in their library that are "eligible" under ReDigi's "Verification Engine."[60] Currently, the only songs that are deemed "eligible" are those purchased from iTunes or ReDigi.[61] This cloud storage system[62] allows users to take the "eligible" songs off their hard drive and store them on this cloud technology,[63] giving users the benefit of freeing up space on their hard drives and having the ability to access their music anytime, anywhere.[64]

According to ReDigi's website, no copies are made during the transaction process.[65] "Upon transfer, ReDigi systematically removes any personal use copies of the file from the user's computer and synced devices so that the original, or non-infringing 'copy' is the only one that exists, safely stored in the user's Cloud space."[66] This applies to both storing and selling music; even if a user wishes to use the cloud service just for storage, ReDigi will remove the song from the user's hard drive and synced devices and allow the user to have access to that song only through the cloud system.[67]

ReDigi also maintains that copies are not made during the buying and selling process. "When someone buys it, the song and its corresponding license is transferred to the buyer, who then becomes its new owner. This is called an Atomic Transaction. No copies are made during this process."[68] The "used" songs are sold for 79 cents. For every sale a user makes; the user will receive "credit" toward future songs purchases on ReDigi.[69] In addition, a user receives "coupons" for every song the user lists for sale on ReDigi's "marketplace."[70] These coupons, valued at 20 cents each, can be applied toward a user's next purchase on ReDigi, so that a song will cost 59 cents, rather than 79 cents.[71]

V. The Claim That ReDigi Infringes

As noted, two of a record label's exclusive rights are implicated when ReDigi resells "used" digital music files:[72] the section 106(1) exclusive right to reproduce a copyrighted work and the section 106(3) exclusive right to distribute copies or phonorecords of a copyrighted work.[73] Below, I discuss the claims relating to each of these rights.

A. Reproduction Right

ReDigi contends that no copy of the digital music file is made when a song is uploaded, stored, and sold through its cloud system.[74] As noted, ReDigi explains that once a song is "uploaded" to its system, all other copies are deleted.[75] However, Capitol argues that uploading "can only be accomplished by making an unauthorized copy of the original user's track."[76] Capital also argues that the song "'stored' in and offered to consumers from ReDigi's 'cloud' is necessarily a copy of the user's original file."[77] In addition, although ReDigi states that songs are "transferred" from the seller to the buyer,[78] Capitol contends that this "can only be accomplished by the creation and transfer of yet another copy of what was once the original user's digital file."[79]

There are multiple times during the process of uploading and transferring a digital sound recording in which illegal copying may be taking place. *A&M Records, Inc. v. Napster, Inc.*[80] involved "peer to peer" file sharing, a process in which "[t]he requesting user's computer uses [] information to establish a connection with the host user and downloads a copy of the contents of the MP3 file from one computer to the other over the Internet…."[81] The Ninth Circuit found such acts infringed at least two of the copyright holders' exclusive rights, the rights of reproduction and distribution: "Napster users who upload file names…for others to copy violate plaintiffs' distribution rights. Napster users who download files containing copyrighted music violate plaintiffs' reproduction rights."[82] If it is found that a copy is in fact being made at any point, then ReDigi will have infringed Capitol's reproduction right.

B. Distribution Right

Capitol contends that ReDigi violates its distribution right. In 2001, the U.S. Supreme Court in *New York Times Co., Inc. v. Tasini*[83] found that the copyright owners' distribution rights in freelance articles were violated when copies of the copyrighted articles were sold through an online database.[84] According to Nimmer, *Tasini* "cements the…proposition that an electronic transmission of a copyrighted work implicates that owner's distribution right as to copies."[85] As discussed above, the distribution right applies to both legally and illegally made copies.[86] Thus, whether or not ReDigi is making unlawful copies, Capitol can pursue a claim against ReDigi for unauthorized distribution. However, if is it found that ReDigi is not making and distributing illegal copies and is instead transmitting the original legal copy to another person, this may be protected under the first sale doctrine.[87]

VI. Argument That the First Sale Doctrine Does Not Apply to ReDigi

As noted, ReDigi maintains that its cloud system and marketplace are structured to fall within the first sale doctrine.[88] Capitol disputes this assertion. If it were found that ReDigi were selling unlawfully made copies, Capitol argues, the first sale doctrine would not protect these sales because the first sale doctrine

> permits "owners of a particular copy or phonorecord lawfully made under this title…to sell" that copy or phonorecord. ReDigi, however, is not an "owner" of any such lawfully made copy, nor is ReDigi disposing of the actual "particular copy" purchased by a user. Rather, ReDigi and its users are making and distributing unauthorized copies of that original file.[89]

On the other hand, if it is found that ReDigi transfers the original, legal digital music file without making any illegal copies,[90] Capitol believes the first sale doctrine does not apply because the distribution right is still implicated. Capitol's argument is grounded in the proposition that the first sale doctrine "does not readily transfer to the digital environment."[91] In addition to the Copyright Office report discussed above,[92] a 1996 letter from the Register of Copyrights to the House of Representatives Subcommittee on Courts and Intellectual Property supports Capitol's position.[93] The letter, written in response to questions from the House concerning the National Information Infrastructure Copyright Protection Act,[94] answers a question that directly addresses ReDigi's situation:

> Is it possible [to] transfer an original in the digital environment without simultaneously making an infringing copy? If it is possible, do you believe that the first sale doctrine should be limited in the digital context for the same reasons that it was limited in 17 U.S.C Section 109(b)(1)(A) (Supp. 1995)?[95]

The answer, provided by then Register of Copyrights Marybeth Peters, is that "simply requiring the original to be destroyed does not result in an entirely equivalent situation" to transferring a physical copy:

> First, the destruction requires an affirmative act, which may not always take place, and will be hard to prove or disprove. Second, the potential to interfere with the copyright owner's market is much greater. In a transfer involving a tangible copy, there has been a single act of reproduction, for which the copyright owner has received recompense. The transfer requires a physical activity, entailing some inconvenience, similar to visiting the bookstore. In addition, the physical copy is no longer new, making it less valuable or appealing in certain respects. In the on-line world, in contrast, the transmission can take place instantaneously, there can be multiple transmissions from a single transferor, the quality of the copy remains equivalent, and the recipient need not leave home to obtain it.[96]

Even if an "affirmative" act were not required to remove the original copy from the transferor, the argument can be made that although ReDigi removes copies from hard drives and other synced devices,[97] it cannot ensure that the transferor no longer possesses a copy, such as on a CD made by "burning" the song from the transferor's hard drive onto the CD.

The Peters letter concluded that the first sale doctrine should not protect digital distributions of copyrighted works based on

> the facts that digital transmissions do not implicate the core policies behind the first sale doctrine, that no hardship to users has been demonstrated, and that it may not be possible to craft an equivalent exception for transmissions without significantly impairing the copyright owner's market for exploiting the work through digital networks….[98]

Capitol could add that "[t]he diminution of the copy owner's right to dispose of her property has been justified by the need to preserve the creative incentive that drives development"[99] and that "'[w]hatever loss may occur from the absence of a first-sale right in the digital environment should be more than offset by the lower[ ] costs and vastly broader selection of content made possible by Internet distribution.'"[100]

VII. ReDigi's First Sale Defense

A. The Reproduction Right

ReDigi disputes Capitol's contention that during each step of the process (uploading, storing, and transferring) a copy is made.[101] Being able to demonstrate that ReDigi never makes a copy of the digital music files that are uploaded, stored, and transferred on its system is critical for ReDigi to distinguish itself from other systems, such as Napster, that have been found to violate of a record label's reproduction right.

ReDigi distinguishes its system from file-sharing systems:

> If you own a music file, that file is copied into the computer's memory whenever you listen to it. This copying is legal. Making copies for your own use is also generally permissible. Making unauthorized copies of music files and handing them out or making them available to anyone who wants them is not legal. ReDigi does not share files and does not make it easy to share files. ReDigi will not allow its users to sell their legally allowable music files if it discovers copies of those files on their computer or on another users' computer.[102]

It remains to be seen whether or not ReDigi can prove this.[103]

B. The Distribution Right

Despite the suggestion from the Copyright Office that the first sale doctrine does not apply to digital works, ReDigi has some support for its argument that it does.[104] Nimmer lists the four elements that must be met to establish that the first sale doctrine applies: "(a) the copy was lawfully produced, (b) it was transferred under plaintiff's authority, (c) the defendant is the lawful owner of the copy, and (d) the defendant simply distributed that particular copy."[105] Nimmer argues that the first sale doctrine applies to digital distributions, using the example of the transfer of a digital copy of a movie. Nimmer asserts that the first sale doctrine applies if the file passes from one computer to the other without making a copy (just as a DVD can be handed from one person to another) and if the transferor's file is then expunged from his or her computer.[106] ReDigi similarly describes its system as transferring a file from the seller's cloud to the buyer's cloud, without making a copy, and, in the process, removing the file from the seller's possession.[107]

From ReDigi's perspective, there is no reason why the reasoning of *C.M. Paula Co. v. Logen*[108] does not apply: "[T]he policy favoring a copyright monopoly for authors gives way to the policy opposing restraints of trade and restraints on alienation."[109]

ReDigi's argument focuses on the consumer's rights and its objective to translate the right to transfer into the digital world. While the Copyright Office "presents a compelling argument for the copyright holders against unrestricted trade of digital files, it does not address the other side of the balance: the right of an owner of a legal copy to dispose of it."[110] In deciding which side has the stronger case, it is important for a court to take into account all of the rights at issue.

VIII. Additional Arguments Made in *Capitol Records v. ReDigi, Inc.*

One allegation made by Capitol in its complaint, not discussed above, is that the first sale doctrine does not apply because "neither ReDigi nor its users resell the original material object that resides on the original user's computer."[111] ReDigi points out that section 106 refers only to "copies" and "phonorecords."[112] If these terms are to be limited to their definitions in section 101, the label's exclusive right does not extend to digital works, and ReDigi therefore does not infringe. In fact, the courts have interpreted "copies" and "phonorecords" as applying to digital works.[113]

Capitol also questions the reliability of ReDigi's "Verification Engine," which is used to determine if a user's tracks were "legally downloaded."[114] The complaint alleges that even if files are lawfully obtained, they still may be restricted from resale by the original vendor.[115] "For example, Amazon.com—a common source and likely the origin of many ReDigi uploads—expressly prohibits users of its MP3 Music Service from any distribution, transfer, or sale of recordings downloaded via that service."[116] However, on ReDigi's website, and in its preliminary injunction brief, it asserts that the only files eligible for upload to its system are those legally acquired through iTunes, not Amazon or other online music stores.[117]

Finally, ReDigi acknowledges that some copying does take place. Specifically, it states that during the uploading process and the storing process copies are made, but it claims these copies are protected by the fair use doctrine and the essential-step defense.[118]

IX. Conclusion

However *Capitol Records, LLC v. ReDigi, Inc.* is resolved, it is sure to have a significant impact on both the music industry and consumers. If ReDigi prevails, there might be a negative impact on the market for "new" digital music, and this may reduce the incentives of the labels to create new works. Eventually, Congress may have to amend the Copyright Act to reflect these technological changes so that the Copyright Act continues to reflect its ultimate objective, "[t]o promote the Progress of Science and useful Arts…." [119]

Editor's Note

On March 30, 2013, as this issue was going to press, the court granted Capitol's motion for summary judgment. The court rejected ReDigi's first sale defense (as well as its fair use defense) and held ReDigi directly, contributorily, and vicariously liable for violating Capitol's reproduction and distribution rights. The court held that because ReDigi made new unauthorized copies of its users' music files in violation of Capitol's reproduction rights, its first sale defense failed because the copies were neither " lawfully made" nor the "particular" copies owned by the seller, as section 109(a) requires.

Endnotes

1. *See* ReDigi, https://www.redigi.com/ (last visited Feb. 26, 2013).
2. *What is ReDigi?*, ReDigi.com, https://www.redigi.com/help (last visited Feb. 26, 2013).
3. *ReDigi Coupons*, ReDigi.com, https://www.redigi.com/#!/learn (last visited Feb. 26, 2013).
4. *iTunes—What's on iTunes*, Apple.com, http://www.apple.com/itunes/what-is/ (last visited Feb. 26, 2013) (stating that some songs sell for 69 cents; however, it is rare to find a song at this price).
5. 17 U.S.C. § 106 (2006) (providing copyright owner with exclusive rights in a copyrighted work); 17 U.S.C. §501(b) (giving the owner of an exclusive right the ability "to institute an action for any infringement of that particular right").
6. *Id.* at § 109(a) (codifying the first sale doctrine).
7. *See* Complaint, *Capitol Records, LLC v. ReDigi Inc.*, 2012 WL 32056 (S.D.N.Y. 2012) (No. 12 Civ. 0095) (hereinafter "Complaint").
8. *Id.* Capitol is also alleging inducement, contributory copyright infringement, vicarious copyright infringement, and common law copyright infringement. It also is alleging infringement of its performance right, but that is beyond the scope of this article.
9. 17 U.S.C. § 102(a)(7).
10. *See id.* at § 106 (including, generally, the right to reproduce, prepare derivative works, distribute, perform, display, and perform by digital audio transmission).
11. *Id.* at § 501 (explaining copyright infringement).
12. Craig Joyce et al., Copyright Law 498 (Matthew Bender & Co., Inc., 8th ed. 2010).
13. 17 U.S.C. § 109(a).
14. H.R. Rep. No. 94-1476 at 62, 79–80, 169 (1976), *reprinted in* 1976 U.S.C.C.A.N. 5659, 5675–76, 5693–94, 5785.
15. 210 U.S. 339 (1908).
16. *Bobbs-Merrill Co.*, 210 U.S. at 341.
17. *Id.*
18. *Id.* at 343.
19. *Id.* at 350 (referencing the controlling statute at the time, Section 4952 of the Revised Statutes of the United States, which created a "sole right to vend").
20. *Id.* at 351.
21. *Id.* at 350.
22. 17 U.S.C. § 27 (1977).
23. 17 U.S.C. 109(a).
24. *See* H.R. Rep. No. 98-987, at 2, *reprinted in* 1984 U.S.C.C.A.N. 2898, 2899 (citing Zechariah Chafee, Jr., *Equitable Servitudes on Chattels*, 41 Harv. L. Rev. 945, 982 (1928)).
25. *See* H.R. Rep. No. 98-987, at 2, *reprinted in* 1984 U.S.C.C.A.N. 2898, 2899 (citing *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339; *Harrison v. Maynard, Merrill & Co.*, 61 F. 689, 690 (2d. Cir. 1894)).
26. 355 F. Supp. 189 (N.D. Tex. 1973).
27. *C.M. Paula Co. v. Logan*, 355 F. Supp. 189, 191 (N.D. Tex. 1973).
28. 233 F. Supp. 881 (E.D. Pa. 1964).
29. *Burke & Van Heusen, Inc. v. Arrow Drug, Inc.*, 233 F. Supp. 881, 884 (E.D. Pa. 1964) (citing *Platt & Munk Co. v. Republic Graphics, Inc.*, 315 F.2d 847, 854 (2d Cir. 1963)).
30. *Arrow Drug*, 233 F. Supp. at 884.
31. U.S. Copyright Office, DMCA Section 104 Report, at v (Aug. 2001) [hereinafter DMCA Report], *available at* http:// www.copyright.gov/reports/studies/dmca/sec-104-report-vol-1.pdf (according to the report, the Digital Millennium Copyright Act mandated such reports from the Register of Copyrights to assist Congress in evaluating the relationship between copyright law and changes in technology).
32. *Id.*
33. *Id.* (listing the other two proposals as the "creation of an exemption for the making of certain temporary incidental copies; and the expansion of the archival copying exemption for computer programs in section 117 of the Act").
34. *Id.* at 80-81.
35. *Id.* at xix ("The underlying policy of the first sale doctrine as adopted by the courts was to give effect to the common law rule against restraints on the alienation of tangible property").

36. *Id.*

37. *Id.* The argument here is based on the idea that a copy of the digital work needs to be made before transmitting it. Part VIII below will discuss ReDigi's argument that the First Sale Doctrine should apply when the digital work is being transmitted with technology that can transmit the work without first creating a copy.

38. *Id.*

39. *See supra* Part III.B.

40. DMCA Report, *supra* note 31, at xix.

41. *Id.*

42. *Id.* at 83.

43. *Id.* at 78.

44. *Id.* at 79.

45. *See* 17 U.S.C. § 109; *see also* DMCA Report, *supra* note 31, at 79.

46. DMCA Report, *supra* note 31, at 79.

47. *Id.* at 80.

48. *Id.* at 80-81.

49. *Id.* at 81.

50. *Id.*

51. *Id.* at 81-82.

52. *Id.* at 82.

53. *Id.* at 83-84.

54. *Id.* at 84.

55. *Id.* at 96.

56. *Id.* at 98.

57. *See infra* Part IV (explaining how ReDigi implicates the type of "forward and delete" technology discussed by the Copyright Office in its report).

58. Melville B. Nimmer & David Nimmer, Nimmer on Copyright § 8.12 (E) (2008) [hereinafter Nimmer on Copyright].

59. *See Learn More About ReDigi*, ReDigi.com, https://www.redigi.com/learn (last visited Feb. 26, 2013).

60. *What is Free Unlimited Cloud Storage?,* ReDigi.com, https://www.redigi.com/help (last visited Feb. 26, 2013).

61. *Id.*

62. *See* Letter from Kathryn J. Fritz, Attorney for Google Inc., to Honorable Richard J. Sullivan, Chairman, U.S. District Judge (Feb. 1, 2012) *available at* http://beckermanlegal.com/Lawyer_Copyright_Internet_Law/capitol_redigi_120201GoogleLetterReAmicusBrief.pdf (explaining that "[c]loud computing enables users to store and process data remotely, in the 'cloud' of networked computer servers connected through the internet to the user's computer, thus freeing users from the need to keep physical files and process data locally within their own hard drives and powerful computers").

63. *What is Free Unlimited Cloud Storage?*, *supra* note 60.

64. *What is ReDigi?*, *supra* note 2.

65. *Is ReDigi Legal?*, ReDigi.com, https://www.redigi.com/help (last visited Feb. 26, 2013).

66. *Is ReDigi Legal? Yes!*, ReDigi.com, https://www.redigi.com/legal (last visited Feb. 26, 2013).

67. *Id.*

68. *Is ReDigi Legal?*, *supra* note 65.

69. *ReDigi Coupons, supra* note 3.

70. *Id.*

71. *Id.* (explaining that only one coupon can be applied per song).

72. Other infringing acts may be taking place on ReDigi's website, but this article focuses on those rights infringed just by the act of reselling digital music files.

73. *See supra* Part II.

74. *Is ReDigi Legal? Yes!*, *supra* note 66; *see also supra* Part V.

75. *Id.*

76. Complaint, *supra* note 7, at 6.

77. *Id.* (emphasis in original).

78. *Is ReDigi Legal? Yes!*, *supra* note 66.

79. Complaint, *supra* note 7, at 6.

80. 239 F.3d 1004 (9th Cir. 2001).

81. *Napster*, *Inc.*, 239 F.3d at 1012.

82. *Id.*

83. 533 U.S. 483 (2001).

84. *New York Times Co., Inc. v. Tasini*, 533 U.S. 483, 498 (2001).

85. Nimmer on Copyright, *supra* note 58, at § 8.12 (E).

86. *See supra* Part II.

87. 17 U.S.C. § 109(a) (providing protection only for selling or disposing of legally made copies).

88. *See Is ReDigi Legal? Yes!*, *supra* note 66.

89. Complaint, *supra* note 7, at 9; *see also* 17 U.S.C. § 109(a).

90. *See Is ReDigi Legal? Yes!*, *supra* note 66.

91. Letter from Marybeth Peters, Register of Copyrights, to Honorable Carlos J. Moorhead, Chairman, U.S. House of Representatives, Subcommittee on Courts and Intellectual Property (Feb. 15, 1996) [hereinafter "Peters Letter"], *available at* http://www.copyright.gov/docs/niistat.html.

92. *See supra* Part III.C. (discussing why there should not be a "digital first sale doctrine" or an expansion of the current first sale doctrine).

93. Peters Letter, *supra* note 91.

94. Economic Espionage Act of 1996, Pub. L. No. 104-294, 110 Stat. 3488 (1996).

95. Peters Letter, *supra* note 91 (referring to 17 U.S.C. § 109(b)(1)(A) (Supp. 1995) which discusses the right to rent, lease, or lend a sound recording or computer program).

96. *Id.*

97. *See Is ReDigi Legal? Yes!*, *supra* note 66.

98. Peters Letter, *supra* note 91.

99. Eurie Hayes Smith IV, *Digital First Sale: Friend or Foe?*, 22 Cardozo Arts & Ent. L.J. 853, 855 (2005) (citing *Music, Motion Picture Companies File Appeal in Grokster, Morpheus Case*, 2-8 Mealey's Litig. Rep. Copyright 4 (Sept. 2003)).

100. Smith, *Digital First Sale: Friend or Foe?*, 22 Cardozo Arts & Ent. L.J. at 855 (citing Frank G. Hausman, *Protecting Intellectual Property in the Digital Age, in Copy Fights: The Future of Intellectual Property in the Information Age* 17, 205, 215 (Adam Thierer & Wayne Crews eds., 2002)).

101. *See supra* Part IV.

102. *See Is ReDigi Legal? Yes!*, *supra* note 66.

103. *See supra* Part I.

104. *See supra* Part III.C.

105. Nakimuli Davis, *Reselling Digital Music: Is There A Digital First Sale Doctrine?*, 29 Loy. L.A. Ent. L. Rev. 363, 372 (2009) (citing Melville B. Nimmer & David Nimmer, Nimmer on Copyright § 8.12 (E) (2008)).

106. Nimmer on Copyright, *supra* note 58, at § 8.12 (E).

107. *See Is ReDigi Legal? Yes!*, *supra* note 66.

108. 355 F. Supp. 189, 191 (N.D. Tex. 1973).

109. *C.M. Paula Co. v. Logan*, 355 F. Supp. at 191.

110. Smith, *Digital First Sale: Friend or Foe?*, 22 Cardozo Arts & Ent. L.J. at 855.

111. Complaint, *supra* note 7, at 9.

112. Defendant's Memorandum of Law in Opposition to Plaintiff's Motion for a Preliminary Injunction, *Capitol Records, LLC v. ReDigi Inc.*, 2012 WL 32056, at 21 (S.D.N.Y. 2012) (No. 12 Civ. 0095) [hereinafter Defendant's Memorandum], *available at* http://www.wired.com/images_blogs/threatlevel/2012/02/sabatogeletter.pdf (discussing only the distribution right, but the same would apply to the reproduction right); *see also* 17 U.S.C. § 106(1), (3).

113. *Napster, Inc.*, 239 F.3d at 1012; *Tasini*, 533 U.S. at 498.

114. Complaint, *supra* note 7, at 8.

115. *Id.*

116. *Id.*

117. *See What is Free Unlimited Cloud Storage?*, *supra* note 60; *see also* Complaint, *supra* note 7, at 8 (explaining that iTunes passes title to music files to the customer upon download, therefore a customer "owns" the file, whereas Amazon restricts the customer rights to a file, thereby providing a "license").

118. Defendant's Memorandum, *supra* note 112, at 9-14.

119. U.S. Const. art. I, § 8, cl. 8.

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Scorpio S.A. v. Willis and Termination Rights

By Ana-Karine Hallum

I. Introduction

Most people in the United States are familiar with the Village People song "Y.M.C.A.," and many even know the accompanying hand motions. Less well known is that one of its writers, Victor Willis, has been embroiled in a legal battle for the last year attempting to recapture his rights in the song.[1]

After spending twenty-six weeks on the Billboard top 100 in the 1970s,[2] "Y.M.C.A." sold over a million copies in the United States in less than two weeks and was certified platinum by the Record Industry Association of America.[3] For the first three weeks of 1979, the single was also Number One on the British charts.[4]

The Village People began to withdraw from the limelight in the 1980s. The group's music stayed popular mostly at smaller-scale events; it was hired to perform at weddings, bar mitzvahs, and corporate gatherings.[5] Although "Y.M.C.A." was no longer as popular or lucrative as it had been, the song still had emotional impact. "['Y.M.C.A'] is the single most important song to hit the Jewish religion since 'Hava Nagila," Roger Bennett, co-author of *Bar Mitzvah Disco,* told Spin magazine. "They opened our eyes to different career possibilities: a cop, a builder, a flamboyant Indian.…"[6] It wasn't until the 1990s that "Y.M.C.A." snuck back into the hearts and minds of the American public, however, due in large part to Joseph Malloy, the son-in-law of the late New York Yankees owner George Steinbrenner, who made "Y.M.C.A." a staple of the fifth-inning grounds crew routine at Yankee Stadium. Other teams took notice,[7] and the song became part of a baseball routine that continues to this day.[8]

Affection for "Y.M.C.A." and other Village People hits has translated into dollars for the copyright owners. This inspired Willis to seek to take advantage of this continued revenue stream by terminating the licenses and assignments he had granted for "Y.M.C.A." and other Village People hits in accordance with the termination provisions of the Copyright Act.

Sections 203 and 304 of the Copyright Act give authors "a second bite at the apple"[9] by affording them a second chance to fully exploit the value of their works. Both provisions were enacted to protect authors from unremunerative transfers made before the value of a work was known.[10] Section 203 addresses grants made on or after January 1, 1978, while interests transferred before January 1, 1978 are addressed in section 304.[11] Under section 203, the termination of transfers executed on or after January 1, 1978 may be effected during a five-year period beginning thirty-five years after the date of the transfer by serving notice in writing.[12] Thus, grants that occurred in 1978 become eligible for termination in 2013.

Willis was among the first to take advantage of section 203. He filed notices of termination "on the first date [he was] able to"[13] of grants relating to thirty-three songs.[14] Thereafter, Scorpio, a French publishing company, Can't Stop Productions, Inc., (CSP), and Can't Stop Music (CSM), Scorpio's exclusive sub-publisher and U.S. administrator, respectively, brought an action in the Southern District of California challenging the validity of the termination notices.[15] The court, however, sided with Willis, holding that a joint author who individually transfers his copyright interest has the right to terminate that grant unilaterally pursuant to section 203. Many expect the ruling to have a significant bearing on termination efforts that are anticipated to be filed by popular artists of the 1970s, including Bruce Springsteen, Bob Dylan, Billy Joel, Tom Petty, and many others.[16]

"Sections 203 and 304 of the Copyright Act give authors 'a second bite at the apple' by affording them a second chance to fully exploit the value of their works."

This article evaluates the ruling in *Scorpio v. Willis* with a focus on the continuing evolution of the termination provisions. It first explores the origin and development of section 203 as well as the authorship issues implicated by section 203. It then discusses *Scorpio v. Willis* and concludes by discussing some potential implications of the case.

II. The Termination Right

A. Origin of the Termination Provisions

When federal copyright protection began in the United States in the late 1700s, Congress attempted to ameliorate the harsh consequences of unremunerative transfers from authors to publishers by providing copyright protection in two separate terms: an initial term and a renewal term that commenced, if exercised, at the end of the first term. These terms were initially fourteen years each,[17] which was changed to an initial term of twenty-eight years and a renewal term of fourteen years.[18] The 1909 Copyright Act provided initial and renewal terms of twenty-eight years each.[19] For copyright protection to be extended into the renewal term, the author or the author's heirs had to file for renewal during the year prior to the end of the initial term.[20] Congress justified the renewal period by explaining that authors often transfer their copyright interests for a little money to publishers at or near the time of creation.[21] However, often a work would be successful beyond its initial term, and Congress felt that the author should be able to sell the copyright in a work without losing the renewal rights—that it "should be the exclusive right of the author to take the renewal term" of the work.[22]

Unfortunately, this frequently resulted in authors granting the rights to both a work's original term and to its renewal term.[23] The Supreme Court held in *Fred Fisher Music Co. v. Witmark & Sons*[24] that, although it ran contrary to legislative intent as expressed in reports of the House and Senate Committees, more explicit statutory language was required in order to find a restraint on the granting of renewal rights.[25] The Court reasoned that such a purpose would have been included in the language of the statute had the Act been intended to end the practice of assigning renewal interests, which had become the common practice prior to passage of the 1909 Act.[26] This ruling strengthened the ability of publishers to request or even demand grants of renewal rights from their authors. Because publishers routinely required writers to assign both original and renewal terms, it often was only upon the author's death that the assigned renewal rights reverted to the author's heirs.[27]

The 1976 Copyright Act extended the life of copyright from two shorter terms to a single longer term,[28] and it gave authors the right to terminate grants that may have proven to be unfavorable.[29] As noted, the termination provisions—sections 203 and 304—addressed grants executed by the author on or after January 1, 1978, and grants executed before January 1, 1978, respectively.[30] The purpose of these provisions is to protect authors from unremunerative transfers that occurred before the value of a work was known[31] and to give them (or their heirs) a second chance to exploit the value of their works by recapturing the copyright rights.

The House Report on the 1976 Act specified that a termination right was needed "because of the unequal bargaining position of authors, resulting in part from the impossibility of determining a work's value until it has been exploited."[32] While the purpose of the 1909 Act renewal terms was similar,[33] the 1976 Act responded to the Supreme Court's invitation to provide expressly nonwaivable termination rights.[34] The new provisions also included another change: rather than the work falling into the public domain, if an author does not exercise his right to terminate his original grant, the rights to the work now remain with the grantee.

According to Professor Paul Goldstein, the renewal provisions of the 1909 Act rested on three propositions: (1) the term of copyright should be long enough to consist of both an initial and a renewal term; (2) works that have no significant commercial value by the end of their initial term usually will fall into the public domain because their authors have no incentive to renew; and (3) "because works that continue to enjoy commercial value after the initial term are more likely to owe their success to the genius of their authors than to the capital and labor contributed by the author's assignees or licensees, the author has the stronger entitlement to revenues earned in the renewal term."[35] However, while the termination provisions of the 1976 Act share the first and third of these premises, they allow a non-terminated transfer to subsist for the full term of copyright rather than allowing the work to fall into the public domain.[36] This change inherently places a higher value on the commercial viability of the work by automatically assigning ownership to either the author or the grantee for the duration of the copyright.

When section 203 termination rights are not exercised, an author still may take advantage of them through commercial forbearance. That ownership interests remain with the assignee or licensee, rather than passing automatically to the public domain or to the author, does not mean that Congress meant to benefit the transferee at the expense of the author. An author can use section 203 as leverage to obtain better licensing terms with the grantee.

B. Who Has the Right to Terminate?

As noted, the termination of transfers for works created on or after January 1, 1978 may be exercised at any time during a five-year period between 35 and 40 years after the date of the transfer.[37] The copyright owner must give written notice to both the transferee and to the Copyright Office stating the intended termination date, and the notice must be sent any time between two and ten years prior to the termination date.[38] If the transferee transferred the copyright, notice must be sent to the current owner if the terminating party is aware of the transfer.[39]

An important question of statutory interpretation has arisen concerning section 203. Section 203(a)(1) provides that "[i]n the case of a grant executed by one author, termination of the grant may be effected by that author."[40] It further provides that "[i]n the case of a grant executed by two or more authors of a joint work, termination of the grant may be effected by a majority of the authors who executed it."[41] Whether a notice of termination must be effected by a majority of authors who executed the particular grant or by a majority of the co-authors of the work is a key question in *Willis*. Several respected commentators have interpreted the statute as requiring consent from a majority of the authors.[42]

But on its face the statute seems to imply that section 203 refers only to authors who are party to the grant at issue. The language refers to the termination of a grant "effected by a majority of the authors who executed it"; "grant," it would appear, is the antecedent of "it." Thus, if two or more joint authors participate in a single grant, a majority of them must terminate the grant.[43] This implies that an author of a joint work who has entered into a grant pertaining only to his own copyright interest can terminate that grant without the participation of other authors under the first part of section 203(a).[44] If there is more than one grant, the section 203 termination right can be exercised separately for each grant.

The term "grant" as used in section 203 is not defined. Transfers of copyright ownership are defined in section 101 to include "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 non-exclusive license."[45] Assignments and exclusive licenses are the most common types of transfers.[46] While the 1909 Copyright Act defined copyright ownership as indivisible, the 1976 Act allows ownership to be divided among the section 106 copyright rights without restriction.[47] The Copyright Act also requires that transfers of ownership must be in writing and signed by the owner of the rights conveyed (or the owner's authorized agent).[48]

C. Who Is an Author?

Putting aside works made for hire, anyone who has made a creative contribution to a work might have an authorship claim.[49] This is important in the context of termination provisions because one must be an author to terminate a grant.[50] Unless Congress defines the term, courts will continue to determine how to construe authorship. A recent article jested that even after allegedly collaborating with over seventy people on three solo albums, Beyoncé and her "army of writers…still [couldn't] come up with songs that are original."[51] Beyoncé's third solo album, *I Am...Sasha Fierce*, credits so many songwriters, engineers, producers, mixers, and arrangers that it reads like a small-town phone book. Whether any of these people are co-authors will depend on their creative contributions, the intent of the participants, and, in some cases, written agreements. However, written acknowledgment does not necessarily indicate authorship, and it is also possible that uncredited participants may legitimately claim authorship.

A "joint work" is a work "prepared by two or more authors with the intention that their contributions be merged into inseparable or interdependent parts of a unitary whole."[52] Nimmer proposes that a joint work should instead be defined as one in which the copyright "is owned in undivided shares by two or more persons."[53] It follows that while the product of joint authorship is a joint work, a joint work may not necessarily be the product of joint authorship. Nimmer explains that a joint work will result in the following circumstances:

> (1) if the work is a product of joint authorship; (2) if the author or copyright proprietor transfers such copyright to more than one person; (3) if the author or copyright proprietor transfers an undivided interest in such copyright to one or more persons, reserving to himself an undivided interest; (4) if upon the death of the author or copyright proprietor, such copyright passes by will or intestacy to more than one person; (5) if the renewal rights under the Copyright Act or the terminated rights under the termination of transfers provisions, vest in a class consisting of more than one person; (6) if the work is subject to state community property laws.[54]

Because jointly authored works are a type of joint work, each contributor owns an undivided interest in the work, including in the contributions of the other authors.[55] In works of joint authorship, a "joint laboring in furtherance of a preconcerted common design" is essential.[56] Without it, the resulting work should not be considered a joint work. There must be an intention at the work's inception that the contributions be merged.[57] This does not mean that joint authors must necessarily work in the same room at the same time or that each author's contributions must be qualitatively or quantitatively similar.[58]

Some cases have focused on whether a claimed author is "the mastermind" of the work,[59] but this test has sometimes been rejected due to its susceptibility to inequitable treatment.[60] Although the purpose of looking for the "mastermind" may be to identify a single author, there is no basis for the proposition that a creative contributor should be denied co-authorship rights because he did not play the most important role in the creation of the work. A creative contribution need not be qualitatively or quantitatively equal to another's to qualify for joint authorship.[61] Justice Holmes stated that many ideas "grow better when transplanted into another mind than the one where they sprang up."[62] It has been pointed out that while many assume that featured performers, along with their "creative hands-on record producer[s]," are the authors of sound recordings, time may reveal more complicated entanglements of people involved in the creative processes. According to former Register of Copyrights Marybeth Peters, courts "are going to look at what the contribution is, as opposed to all the creative efforts as a whole, to decide who rises to the level of an author."[63]

Copyright protection for sound recordings is relatively recent.[64] Unlike a musical composition, which may be fixed in sheet music by one or more authors, a sound recording often involves the participation of a large number of people. Musicians, vocalists, and some producers are selected for the way that they will contribute to the sound of the works.[65] However, it is possible that co-authorship in a sound recording will be easier to establish than co-authorship in a musical composition.[66] If an author engages a particular musician or producer because he is "identifiable" and sounds "unique," that in itself is a basis for arguing that the individual may be a co-author of the resulting sound recording.[67] Mixing engineers, thanks to their manipulation of sounds into a final product, also may be recognized as co-authors.[68]

Music attorney Bob Donnelly posits, however, that music engineers generally will not be viewed as co-authors of sound recordings[69] because in most cases they are simply "executing the creative vision of the artist and producer."[70] But he points out that there are some "superstar mixers and engineers" who are hired to contribute their unique creative vision.[71] As a practical rule, Donnelly believes that record producers, who routinely participate actively in the creation of sound recordings, will be considered authors.[72] While there is no standard producer-as-author test, Donnelly suggests that if a producer is receiving a portion of royalty payments, it is a likely sign that he contributed creatively in a substantial way and thus will be considered an author.[73]

In the case of studio musicians or backup vocalists, on the other hand, Donnelly assumes that they generally are not entitled to co-authorship status. In the case of songs written in the studio, authorship in sound recordings could mirror authorship in compositions. In either scenario authorship depends on whether the musician is singing or playing a part that was written, arranged, and directed by another person or if his or her contributions add an extraordinary creative sound, lyric, or notes.[74] Donnelly cites Jimmy Page's work on "You Really Got Me" and Martha Wash's "Everybody Dance Now" on C+C Music Factory's "Gonna Make You Sweat" as potential examples of co-authorship.[75] In many cases, studio musicians and vocalists sign written declarations assigning all right, title, and interest in their contribution as a work for hire.[76] However, the validity of many standard work-for-hire declarations, particularly in the context of sound recordings, is yet to be determined.

III. The Village People as Authors

With this background, we turn back to the *Willis* case. One of the arguments Scorpio made was that Willis was a mere employee, simply doing as he was told, and therefore was not an author. However, even the story of the inception of the Village People is ambiguous, with different people credited with varying levels of participation. In one version, the late French composer Jacques Morali is credited with creating the group in 1977 with his friend and business partner Henri Belolo.[77] According to this version, the two of them came up with the concept around 1975 after Morali followed a Native American with bells on his feet through New York's Greenwich Village and into a bar. At the bar, a man dressed as a cowboy watched the Native American dance.[78] The scene so strongly impressed Morali that it sparked a fantasy of different characters that, to him, represented the "American man." Together, Morali and Belolo used these characters to create The Village People.[79] A slightly different version of the story has bartender and dancer Felipe Rose, the group's original "Native American" character, as the man that Morali and Belolo followed.[80] Rose allegedly was invited to take part in sessions for the first album, singing behind Willis.[81] However, Willis was not writing for the group yet. Some original album tracks, such as "San Francisco (You've Got Me)," credit Jacques Morali, Henri Belolo, Peter Whitehead, and Phil Hurtt as writers.[82]

While one account has Morali and Belolo selling their label on the Village People concept before any of the roles were cast,[83] Willis' website states that the group was not created until after Morali and Belolo met and recorded with Willis.[84] In this version of events, Morali and Belolo were so impressed by Willis' performance in "The Wiz" on Broadway that they developed the concept of the Village People around his voice.[85] Morali approached Willis and told him "I had a dream that you sang lead on my album[,] and it went very, very big."[86] Willis agreed to perform on the album as lead singer, with background tracks provided mostly by studio musicians.[87] Because the first album was recorded before the entire group was formed, the album art showed mostly models.[88] Eventually, a group was assembled and characters chosen. Willis chose the cop persona—"to keep the law and order"[89]—and under his leadership the group thrived

Scorpio initially alleged that CSM hired Willis between 1977 and 1979 merely to translate and create new lyrics for certain songs owned and published by Scorpio in France.[90] But the copyright registrations for all thirty-three compositions at issue, all rights to which were transferred after January 1, 1978, list Willis as one of several writers (i.e., not merely as a translator).[91] These songs include "Y.M.C.A.," "In the Navy," and "Go West."[92] The Copyright Office lists Jacques Morali, Henri Belolo, and Victor Willis as the writers of those three songs as well as of many of the others Willis sought to recapture.[93] Willis transferred his copyright interests in the works through adaptation agreements to CSM. CSM then assigned its rights in the lyrics to Scorpio.[94] The agreements provided that Willis would receive a percentage of the gross receipts from exploitation of the works.[95]

IV. The Lawsuit

After Willis served notices of termination in January of 2011 with respect to his interest in thirty-three compositions, Scorpio (hereinafter including CSM and CSP) sued for a declaration that the termination notices were void.[96] Scorpio made two arguments: (1) that Willis was employed by CSM as a singer and songwriter on a work-for-hire basis, writing and translating under supervision in paid-for facilities, and, alternatively, (2) that the compositions were joint works, and, pursuant to section 203, a majority of authors must execute the termination notice.[97] At the hearing Scorpio withdrew the work-for-hire argument.[98] In the event that the termination were found to be valid, Scorpio requested that Willis's reversion of rights be limited to his percentage of compensation as agreed in his original transfers.[99] Scorpio also requested that Willis be enjoined from terminating any licenses issued or derivative works authorized by Scorpio prior to termination of the copyright assignment.[100]

Willis moved to dismiss, with the support of an amicus brief by the Songwriter's Guild of America.[101] Willis did not argue that he was the sole author of the works but, rather, claimed he was the sole grantor of the transfers at issue.[102] Willis also contended that Belolo, although listed as an author on the copyright registrations, was not actually a co-author.[103] In its opposition, Scorpio contended that Willis could not terminate the copyright assignment in joint works because a majority of the joint authors of a work or their respective successors are required to terminate under section 203.[104] Willis replied that termination must be effected by a majority of the authors who executed the grant, not a majority of the authors of the work.[105]

In its May 2012 ruling,[106] the court looked to the language and purpose of section 203 and held that a joint author who transfers his copyright interest separately from other authors of the work has the right to terminate that grant unilaterally pursuant to section 203.[107]

Scorpio had argued that Willis' notice of termination would terminate the interest of all other authors in their separate grants, relying on the following passage from Nimmer:

> Suppose that a work is written by five joint authors, only three of whom join in executing a grant either of their interest in the copyright or of a nonexclusive license of the work.… If two of three executing joint authors join in a termination (regardless of how many authors wrote the work), they thereby terminate the rights granted by the third executing joint author. It is the grant per se, and not merely the terminating authors' respective grants of rights therein, that is terminated. A termination by two of the three executing joint authors also affects the rights of the remaining joint authors who neither joined in the original execution of the grant nor in its subsequent termination. Whatever rights were properly conveyed in a joint work are terminated if the requisite number of authors who made the grant join in the termination. This status remains true even though the grant and its termination may affect (either favorably or adversely) the rights of nongranting joint authors.[108]

The court, however, noted that the "plain meaning" of section 203 refers to a single grant.[109] This means that if a grant only lists one author, that author may terminate without regard to how many grants exist pertaining to the work; however, if a grant is executed by multiple authors, a majority of those authors is required for termination. The court further determined that Congress "was aware that a joint author may grant his interest in the joint work separately from his co-authors or may join in a grant with one or more of his co-authors,"[110] emphasizing the statutory language "*[i]n the case* of a grant executed by two or more authors of a joint work."[111] "In the case of" implies that a grant in a joint work may, in a different case, be executed by just one co-author, with different conditions for termination. Similarly, the statute does not state that "where two or more joint authors enter into separate grants, a majority of those authors is needed to terminate any of those grants."[112] The court also noted that the range of dates in which a notice of termination is sent is determined by the date of the grant's execution; if the statute refers to all grants, there is no instruction in the statute as to how to determine which grant's execution date governs the notice.

As for Scorpio's request that in the event Willis were found to have a right to terminate his grants of copyright interest he be "limited to the same percentage ownership as he receives as compensation relating to the Compositions and as set forth in the Agreements,"[113] the court held that Willis is entitled to his undivided, equal interest as a joint author upon termination, not to the percentage of royalties provided for in the agreement.[114] Because Willis transferred his entire interest in the works, the termination should restore those interests to him. Absent an agreement between the joint authors that ownership interests be split in a specific way, joint authors share equal, undivided ownership interests in their joint works.[115] Thus, because there is no evidence of an agreement between Willis and his co-authors,[116] for songs such as "Y.M.C.A.," where Willis is listed as one of three authors, he will acquire a one-third undivided ownership interest in the work at the moment of termination[117] even though his agreement provided for a 20 percent royalty on proceeds from the work.[118]

V. Analysis

The critical issue before the court was whether one co-author of a joint work may terminate his separate grant of an interest in the joint work or whether a majority of the authors of the work are needed to effect a termination.[119] As one of several writers credited with writing the thirty-three songs at issue, it was undisputed that Willis was a joint author. As such, he had an ownership interest in each work as a tenant-in-common, assuming an equal, undivided, independent interest in each work. As the court put it, "each co-owner of a joint work becomes a holder of an undivided interest in the whole."[120] While it may seem strange that Willis, one of at least three authors, would make a separate grant, he may have done so at the urging of his co-authors; Scorpio and CSP were created and controlled by co-authors Morali and Belolo,[121] so it is possible that Willis wanted to separate rights transfers from Willis to the company from those of Morali and Belolo. In any event, Scorpio argued that the "grant" in section 203 refers to all grants in a joint work collectively, but there is no textual support for this claim.

In the case of a grant by a sole author, section 203 provides that termination of the grant may be effected by the author. On the other hand, section 203(a)(1) states that "in the case of a grant executed by two or more authors of a joint work, termination of the grant may be effected by a majority of the authors who executed it." "It" logically refers to the antecedent "grant" rather than to the multiple authors who "executed" the work. However, 37 C.F.R. section 201.10, which prescribes the content of the termination notices, instructs the grantors to include, "in the case of a joint work, the authors who executed the grant being terminated."[122] It does not require inclusion of any information concerning non-executing authors, consistent with the statutory language requesting information relating to authors who executed the grant.

The district court's conclusion that since Willis had transferred his rights as a joint author separately from other co-authors, he was able to validly serve a notice of termination accords with Congressional intent.[123] In addition to leaving any co-authors' interests unaffected by Willis' termination,[124] favoring Willis effectuates Congress' intent to "'safeguard[ ] authors against unremunerative transfers' and address 'the unequal bargaining position of authors, resulting in part from the impossibility of determining a work's value until it has been exploited.'"[125] While the outcome is helpful to authors who have executed grants separately from their co-authors, it gives individual grantors in joint works a significant advantage over those who were party to grants by multiple authors. Publishers and other grantees can simply adapt industry forms to take this into account, thus heightening the likelihood of avoiding termination threats altogether. If Willis had been party to the same grant as Belolo and Morali, Belolo and Morali would have had the power to prevent Willis from terminating.

Although the court's reasoning is consistent with the plain meaning of the statute, it begs the question of why any author would choose to execute a grant with his co-authors if he can do so without them, thereby avoiding the burden of garnering a majority of grantors (or their heirs) to effectuate termination down the road. If the ability of a single grantor to terminate his grant were what Congress intended, then there would appear to be no reason that Congress would not have also have wanted a joint author who executed a grant with co-authors to have the ability to terminate only his interest in that grant. Even if only a small number of authors executes a grant, if any of them should die before termination rights vest, an estate potentially consisting of multiple people acquires the termination right. Obtaining consent to terminate from numerous unfamiliar people places a considerable burden on the surviving author who wishes to terminate. In Willis' case, had he shared a grant with Belolo and Morali, he would have had to convince a majority of Morali's estate to permit termination.

> *"While Willis is a sympathetic defendant—not only as one of the first musicians to litigate a section 203 termination, but also as a character in a beloved musical group going up against a company that sought to diminish his creative contributions—the decision has the potential to influence future section 203 cases without regard to such dynamics."*

VI. Conclusion: Potential Implications of *Scorpio v. Willis*

Scorpio v. Willis stands for the proposition that "one author who gives a grant to a publishing company has the right to recapture the copyright interest he created 35 years ago regardless of what other co-authors do or don't do."[126]

The decision reinforces Congress' intent to give authors the opportunity to regain control of their works. While Willis is a sympathetic defendant—not only as one of the first musicians to litigate a section 203 termination, but also as a character in a beloved musical group going up against a company that sought to diminish his creative contributions—the decision has the potential to influence future section 203 cases without regard to such dynamics. Even though the court's holding that individual grantors of joint works may terminate work to the detriment of authors who executed grants jointly with their co-authors, it follows the language of the statute. If Congress disagrees with the court's interpretation of section 203, it is of course free to amend the statute.

The most one can hope for is a healthy balance between protecting artists from unremunerative transfers and not disproportionately punishing grantees. Creativity is vital, but one cannot discount the significance of the publisher's role in the life of a work. Unfortunately, the premise of an author having to affirmatively exercise his statutory termination right has the potential to foster hostility on the part of even the most level-headed grantee. Perhaps an automatic, unwaivable reversion after thirty-five years would better fit the intent of the 1976 Act provisions, in addition to encouraging publishers and record labels to plan ahead for reversions and removing at least some of the temptation of trying to stop them from happening.

Endnotes

1. *Scorpio S.A. v. Willis*, No. 11cv1557, 2012 WL 1598043 (S.D. Cal. May 7, 2012).
2. Randy Jones & Mark Bego, Macho Man: The Disco Era and Gay America's "Coming Out" 89 (Praeger Publishers 2008).
3. *Id.* at 89.
4. *Id*.
5. Jeff Pearlman, *"Y.M.C.A." (An Oral History)*, Spin Magazine (May 27, 2008 3:22 PM), available at http://www.spin.com/articles/ymca-oral-history.
6. Pearlman, *supra* note 5.
7. *Id.*
8. Blaine Spence, *Sport's Oddest Traditions Explained*, Bleacher Report, available at http://bleacherreport.com/articles/210912-sports-oddest-traditions-explained/page/4.
9. Margo E. Crespin, *A Second Bite of the Apple: A Guide to Terminating Transfers under Section 203 of the Copyright Act*, The Authors Guild, *available at* www.authorsguild.org/pdfs/TerminatingTransfers.pdf.
10. H.R. Rep. No. 94–1476, at 124 (1976).
11. 17 U.S.C. §§ 203, 304(c).
12. 17 U.S.C. § 203 (a)(3), (a)(4).
13. Eriq Gardner, *Village People Singer Victor Willis Breaks Silence About Copyright Lawsuit Win*, Hollywood Reporter (May 11, 2012), *available at* http://www.hollywoodreporter.com/thr-esq/village-people-victor-willis-copyright-lawsuit-323489.
14. Complaint for Declaratory Relief at Ex. A, *Scorpio S.A. v. Willis*, No. 11cv1557, 2012 WL 1598043 (S.D. Cal. May 7, 2012).
15. Compl. at 1, 12.
16. Matthew Perpetua, *Village People Singer Files to Regain Copyright Control*, Rolling Stone Magazine (August 17, 2011 2:50 PM), *available at* http://www.rollingstone.com/music/news/village-people-singer-files-to-regain-copyright-control-20110817. Artists from Tom Waits' fame to "Eye of the Tiger" co-writer Jim Peterik are also expected to serve termination notices.
17. *See* Act of May 31, 1790, ch. 15, § 1, 1 Stat. 124, 124 (repealed 1802).
18. *See* Act of Feb. 3, 1831, ch. 16, § 1, 4 Stat. 436, 436.
19. *See* Act of Mar. 4, 1909, ch. 320, § 23, 35 Stat. 1075, 1080.
20. *Id.*
21. Hearings before the Committees on Patents of the Senate and House of Representatives on Pending Bills to Amend and Consolidate the Acts respecting Copyright, 60th Cong., 1st Sess., p. 20.
22. H.R. REP. NO. 2222, 60th Cong., 2d Sess. 14 (1909).
23. David J. Moser, Moser on Music Copyright 56 (Artistpro 2006).
24. 318 U.S. 643 (1943).
25. *Id.* at 656.
26. *Id.*
27. Moser, *supra* note 23, at 58. *See also Miller Music v. Daniels*, 362 U.S. 373 (1960).
28. 17 U.S.C. §§ 203, 303.
29. 17 U.S.C. §§ 203, 304(c)(5).
30. 17 U.S.C. §§ 203, 304(c).
31. H.R.Rep. No. 94-1476, at 124 (1976).
32. *Id.*.
33. "The 1909 Act provided that an author was entitled to 28 years of protection from the date he or she secured a copyright on a work, and that the copyright could, before the first 28-year period expired, be renewed for another 28-year term." *Twin Books v. Walt Disney*, 83 F.3d 1162, 1165 (9th Cir. 1996).
34. Paul Goldstein, *Copyright*, § 5.4 at 113 (1989). The Supreme Court held that authors could transfer by contract the renewal term of a work's copyright before it vested by contract. *Fred Fisher Music Co. v. M. Witmark & Sons*, 318 U.S. 643 (1943).
35. *Goldstein Treatise*, § 5.4 at 113.
36. *Id.* at 113.
37. Moser, *supra* note 23, at 58.
38. *Id*. at 58.
39. *Id.*
40. 17 U.S.C. § 204(a)(1).
41. *Id.*
42. *See* Moser, *supra* note 23, at 58. "A majority of the persons who hold the termination interest is required to exercise the termination right. If a work has more than one author, termination can be made by a majority of the authors or their successors." In the case of joint authors, "…a majority of the authors must agree to file the Termination Notice," and "[p]ursuant to Section 203 of the Copyright Act, for post-January 1, 1978 works that were created by joint authors, a majority of the joint authors, or their respective successors, are required to terminate," Bob Donnelly, *Everything You Need to Know About Copyright Reversions*, 2 St. John's Entm't., Arts & Sports J. 17, 23.
43. *Scorpio*, 2012 WL 1598043, at *2.
44. *Id.* at *2.
45. 17 U.S.C. § 101.
46. Moser, *supra* note 23, at 53.
47. *Id.*
48. 17 U.S.C. § 204(a).
49. *See Childress v. Taylor*, 945 F.2d 500 (2d Cir. N.Y. 1991) (discussing joint authorship and outlining that authors must contribute something of creative value to the work).
50. 17 U.S.C. §§ 203, 304.
51. *Beyoncé Knowles: An Unhip White Guy's Guide to Her Lyrics*, Cracked.com, *available at* http://www.cracked.com/funny-466-beyonce-knowles/#ixzz1v1eqKH16.
52. 17 U.S.C. § 101 (1994).
53. *Id.*
54. *Id.*
55. Nimmer § 6.03.
56. *Id.*
57. *Id.*
58. *Id.*
59. *Aalmuhammed*, 202 F.3d at 1233 (*quoting Burrow-Giles v. Sarony*, 111 U.S. 53 (1884), *quoting Nottage v. Jackson*, 11 Q.B.D. 627 (1883)).
60. Nimmer (*quoting Berman v. Johnson*, 518 F. Supp. 2d 791, 797 (E.D. Va. 2007), *aff'd mem*., 315 Fed. Appx. 461 (4th Cir. 2009)).

61. *See* Nimmer § 6.07; *see also Brown v. Flowers,* 297 F. Supp. 2d 846, 851 (M.D.N.C. 2003) (Treatise cited); *Maurel v. Smith*, 271 F. 211 (2d Cir. 1921); *Sweet Music, Inc. v. Melrose Music Corp*., 189 F. Supp. 655 (S.D. Cal. 1960).

62. Ernie Schenck, The Houdini Solution: Put Creativity And Innovation to Work by Thinking Inside the Box 152 (McGraw-Hill 2006).

63. Susan Butler, *In the Vault*, Billboard Magazine 5 (Aug. 12, 2006). *See generally Gaiman v. McFarlane*, 360 F.3d 644 (7th Cir. 2004).

64. *See* Pub.L.No. 92-140, §3, 85 Stat. 391, 392 (1976) (extending the federal copyright to sound recordings in the Sound Recording Amendment of 1971). In addition, under section 101 of the Copyright Act, sound recordings are defined as: "works that result from the fixation of a series of musical, spoken, or other sounds, but not including the sounds accompanying a motion picture or other audiovisual work, regardless of the nature of the material objects, such as disks, tapes, or other phonorecords, in which they are embodied."

65. Butler, *supra* note 63, at 6.

66. *Id.*

67. *Id.* (quoting Marybeth Peters.).

68. *Id.*

69. Donnelly, *supra* note 42, at 13.

70. *Id.*

71. *Id.*

72. *Id.* at 12.

73. *Id.* at 13.

74. *Id.* at 14.

75. *Id.*

76. *Id.*

77. *Village People*, Rolling Stone, Apr. 18, 1979 (Vol. 289).

78. *Village People*, *supra* note 77.

79. *20/20: Village People* (ABC television broadcast Oct. 18, 1979), *available at* http://www.youtube.com/watch?v=e574yOofK8w.

80. *Village People*, *supra* note 77.

81. *Id*.

82. SAN FRANCISCO (YOU'VE GOT ME), Registration No. PA 32-175 (1979).

83. Pearlman, *supra* note 5.

84. *About Victor Willis*, Victor Willis World, http://www.victorwillisworld.com/about_victor.htm (last visited May 8, 2012).

85. *About Victor Willis*, *supra* note 84.

86. *Village People*, *supra* note 77.

87. *About Victor Willis*, *supra* note 84.

88. *20/20*, *supra* note 79.

89. *Disco diva! Village People star Victor Willis sues bandmates for $1.5m*, Daily Mail Online (May 1, 2011 6:06 PM), *available at* http://www.dailymail.co.uk/tvshowbiz/article-1382475/Village-People-star-Victor-Willis-sues-bandmates--1-5m.html#ixzz1v3duTk6F.

90. *Id.*

91. *Id.*

92. Jones, *supra* note 2, at 184-85.

93. Y.M.C.A., Registration No. PA0000025983 (1978); IN THE NAVY, Registration No. PA0000037990 (1979); GO WEST, Registration No. PA0000038571 (1979).

94. *Scorpio*, 2012 WL 1598043, at *1.

95. *Id.* at *1.

96. Compl. at 1.

97. *Id.* at 1.

98. *Scorpio*, 2012 WL 1598043, at *1.

99. *Id.*

100. *Id.*

101. Memorandum of Amicus Part Songwriters Guild of America in Support of Defendant's Motion to Dismiss, *Scorpio S.A. v. Willis*, No. 11cv1557, 2012 WL 1598043 (S.D. Cal. May 7, 2012).

102. *Id.*

103. *Id.* at *6.

104. Compl. at 5.

105. Reply Memorandum of Points and Authorities in Support of Defendant's Motion to Dismiss the Complaint, *Scorpio S.A. v. Willis,* No. 11cv1557, 2012 WL 1598043 (S.D. Cal. May 7, 2012).

106. *Scorpio*, 2012 WL 1598043, at *1.

107. *Id.* at *5.

108. Nimmer § 11.03.

109. *Scorpio,* 2012 WL 1598043, at *2-3 (citing *In re Roman Catholic Archbishop of Portland in Oregon*, 661 F.3d 417, 433 (9th Cir. 2011)).

110. *Scorpio,* 2012 WL 1598043, at *3.

111. 17 U.S.C. § 203(a)(1).

112. *Id.*

113. *Scorpio*, at *5 (*quoting* Compl. at 9).

114. *Id.*

115. *Id.*

116. *Id.*

117. *Id.*

118. *Id.*

119. *Id.* at *2.

120. *Id.* at *3 (*citing Pye v. Mitchell*, 574 F.2d 476, 480 (9th Cir. 1978)).

121. *See Company Profile: Scorpio Music*, Linked In, *available at* http://www.linkedin.com/company/scorpio-music.

122. 37 C.F.R. § 201.10(b)(2)(iv).

123. *Id.* at *5.

124. *Id.*

125. *Id. at* *4 (quoting H.R.Rep. No. 94–1476, at 124 (1976)).

126. Gardner, Village People Singer Victor Willis Breaks Silence About Copyright Lawsuit Win, THE HOLLYWOOD REPORTER (May 11, 2012 12:04 PM), available at http://www.hollywoodreporter.com/thr-esq/village-people-victor-willis-copyright-lawsuit-323489.

Ana-Karine Hallum is a third-year student at St. John's University School of Law. A version of this article won second prize in the Section's Annual Law Student Writing Contest.

Section Activities and Notices

On February 25 the **Trademark Law Committee** held a roundtable on "IP Licenses in Bankruptcy" at Baker & McKenzie. Panelists James W. Grudus, Chief Creditors' Rights Counsel at AT&T, and Casey Servais, an associate in the Financial Restructuring Department at Cadwalader, Wickersham & Taft, discussed current issues relating to intellectual property licenses and their treatment in the context of bankruptcy proceedings. Topics covered included special provisions of the Bankruptcy Code governing intellectual property, differences between the bankruptcy treatment of trademarks and other types of intellectual property, and the bankruptcy treatment of executory contracts and criteria for determining whether a licensing agreement is an executory contract. Moderated by Committee Co-Chairs Lisa Rosaya and Bill Samuels, the CLE panel also touched on practical strategies for dealing with a licensor's or licensee's bankruptcy filing in light of emerging and unresolved issues in bankruptcy law and the treatment of intellectual property licenses.

The **Litigation** and **Trademark Law Committees** will hold a joint program on May 15 covering preliminary injunctions in trademark cases. The discussion, to be held at Sheppard Mullin Richter & Hampton, will include a panel of in-house counsel and litigation specialists that will consider the current state of preliminary and permanent injunctions in trademark cases. Issues covered will include the likelihood of getting a preliminary injunction, the cost-benefit analysis of seeking injunctions, how these concerns affect litigation strategy, how to advise clients in such efforts, and developments to watch for going forward.

Scenes from the Intellectual Property Law Section

ANNUAL MEETING

January 22, 2013

The Hilton • New York City

Photos by Richard Ravin


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New York State Bar Association

INTELLECTUAL PROPERTY LAW SECTION

Membership in the New York State Bar Association's Intellectual Property Law Section is a valuable way to:

- enhance professional skills;
- keep up-to-date with important developments in the legal profession;
- join colleagues in exciting Section events.

OPPORTUNITIES FOR EDUCATION

The Intellectual Property Law Section offers both the experienced and novice practitioner excellent opportunities to enhance their practical and legal knowledge and expertise. Through Section activities, including conferences on intellectual property (an annual Winter event), members may examine vital legal developments in intellectual property law. The Section's Web site provides current information regarding Section events and offers "members only" access to current issues of *Bright Ideas* and current Committee bulletins providing updates on intellectual property law. The Section sponsors continuing legal education (CLE) credit-bearing programs for Section members at reduced rates. Recent programs offered by the Section related to computer software and biotechnology protection, conducting intellectual property audits, and practical considerations in trade secret law. Now, with Mandatory Continuing Legal Education (MCLE) requirements, Intellectual Property Law Section membership is more valuable than ever before! The Section also sponsors joint programs with Law Schools including an annual writing contest for law students wherein the winning articles appear in an issue of *Bright Ideas*.

OPPORTUNITIES FOR PROFESSIONAL DEVELOPMENT

Intellectual Property Law Section committees address unique issues facing attorneys, the profession and the public. The Section offers opportunities to serve on committees such as Copyright Law; Diversity Initiative; Ethics; Greentech; International IP Law; Internet & Technology Law; Legislative/Amicus; Litigation; Patent Law; Pro Bono and Public Interest; Trademark Law; Trade Secrets; Transactional Law; and Young Lawyers.

Committees allow you to network with other attorneys from across the state and give you the opportunity to research issues and influence the laws that can affect your practice. Committees are also an outstanding way to achieve professional development and recognition. Law students are automatically members of the Young Lawyers Committee. Section members may join more than one committee.

A VOICE IN THE ASSOCIATION

The Intellectual Property Law Section takes positions on major professional issues that affect practitioners and advocates those positions within the New York State Bar Association, the legislature, and the public.

See page 45 to become a member of the Intellectual Property Law Section

COMMITTEE ASSIGNMENT REQUEST

Please designate, from the list below, those committees in which you wish to participate. For a list of Committee Chairs and their e-mail addresses, please refer to page 46 of this issue.

___ Copyright Law (IPS1100)
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___ Greentech (IPS2800)
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___ International Intellectual Property Law (IPS2200)
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___ Patent Law (IPS1300)
___ Pro Bono and Public Interest (IPS2700)
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___ Trade Secrets (IPS1500)
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___ Young Lawyers (IPS1700)

Please e-mail your committee selection(s) to IntellectualProperty@nysba.org

* * *

To be eligible for membership in the Intellectual Property Law Section, you first **must** be a member of the NYSBA.

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Anyone wishing to submit an article, announcement, practice tip, etc., for publication in an upcoming issue of *Bright Ideas* is encouraged to do so. Articles should be works of original authorship on any topic relating to intellectual property. Submissions may be of any length.

Submissions should preferably be sent by e-mail to Jonathan Bloom, Editor-in-Chief, at the address indicated on this page. Submissions for the Fall 2013 issue must be received by July 1, 2013.

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