

## Domain Names: Obtaining and Perfecting a Security Interest

by Warren E. Agin

**T**he July/August 2000 issue of the *Journal* presented “Websites: Obtaining and Perfecting a Security Interest.” This article, also excerpted from Agin’s book, *Bankruptcy and Secured Lending in Cyberspace*, provides due diligence steps and concerns vis-à-vis domain names, as well as covenants to allow maintenance and recovery of Website-related collateral.



**I**s a domain name registration an asset that can be subject to a security interest? How does a secured lender obtain a security interest in the domain name and then protect its rights in that name? These are interesting questions for an industry just starting to face the issues raised by borrowers’ use of domain names. Almost all businesses either have now or will have a domain name. Certainly, every large corporation has registered at least one domain name. When a bank grants a loan secured by all the borrower’s assets, it should

ensure it has a security interest in the borrower’s domain names as well. Otherwise, the bank may find itself unable to foreclose an important asset. Possibly, a financially troubled borrower will sell its domain names without surrendering the proceeds to the lender.

As domain names become more valuable, domain name holders may attempt to securitize them. For example, The Industrial Bank of Korea established a program to lend against domain names. The bank uses an eight-member appraisal group to establish a domain name’s value.

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The bank then will lend up to 30% of the appraised value. Securitizing domain names is possible by working with a domain name registration service, Internet Plaza City, which provides the appraisal services and allows the bank with greater control over the domain name collateral. U.S. banks will have to find their own methods for lending against domain names.

Whether a license or a contract right, a domain name will be considered a general intangible under the UCC. The category of “general intangibles” is a catch-all, encompassing any personal property not included in the other asset categories provided by the UCC. Thus, in *In re Hengalo Enters*, the U.S. Bankruptcy Court for the Southern District of Florida considered a franchise agreement to be a general intangible. Domain names differ somewhat from the traditional contract in that they constitute, in one sense, an indirect government grant of the right to use the domain name. Another form of license by government grant, the liquor license, has been held to be a general intangible, potentially subject to a security interest. Domain names share features in common with telephone numbers, which courts have considered subject to security interests as general intangibles. These parallels indicate that the user of a domain name can grant a lender a valid security interest in the right to use the domain name.

Contractual terms in a domain name registration agreement may affect both the domain name holder’s right to grant a security interest in the domain name and

the lender’s ability to recover the domain name upon default. For example, Network Solution’s agreement includes the following clause:

**Non-Assignment.** Your rights under this Agreement are not assignable. Any attempt by you to assign your rights shall render this Agreement voidable at our option. Any attempt by your creditors to obtain an interest in your rights under this Agreement, whether by attachment, garnishment or otherwise, shall render this Agreement voidable at our option.

How this or similar clauses affect a lender’s ability to obtain a consensual lien against a domain name will depend on the rights the borrower has to the domain name. Characterizing the domain name as an intellectual property right held by the domain name holder will give the holder rights outside of the contract, which the lender can take as collateral. However, defining domain name rights as just those rights contractually granted by the registrar means that restrictions on assignment, like those described above, will prevent a domain name holder from granting a consensual lien against a domain name.

#### Due Diligence for Secured Lenders

**Ownership of domain names.** The first step in performing a due diligence review of a domain name is determining the borrower’s ownership rights. What constitutes ownership in a domain name is still not very clear. Ownership of a domain name can be

defined by the ability to control the domain name, the existence of a contract with the registration authority, or an equitable right to use the domain name in connection with a Website. Depending on the method used to register the domain name, the ownership attributes could be divided among several parties. For example, a common practice is for a third-party Website hosting service to register a domain name on behalf of a customer. In this case, the customer may not be a legal party to the license agreement but may be the administrative contact and will have an equitable right as against the hosting service to use the domain name.

Most domain names, including those in the .com, .net, and .org top-level domains are registered through Network Solutions (although other registrars do exist). When a domain name is registered with Network Solutions, the registering party must provide the name of the entity that will use the domain name. Network Solutions treats this entity as the “owner” of the right to use the domain name. The name of the entity using the domain name should be the same as that of the borrower. Before March 30, 1998, Network Solutions did not request the name of the domain name user, just the administrative, billing, and technical contacts. It treated the administrative contact as the holder of the right to use the domain name. Sometimes this assumption was correct. Other times, the administrative contact was a Website hosting service or an employee of the correct

THE LENDER SHOULD ASCERTAIN THE STRENGTH OF THE TRADEMARK. THIS INVOLVES ANALYZING THE USES OF THE TRADEMARK, BOTH ON- AND OFF-LINE, THE AMOUNT OF TIME THE TRADEMARK HAS BEEN IN USE, THE EXTENT TO WHICH IT HAS ACQUIRED SECONDARY MEANING, AND THE RELATIONSHIP BETWEEN IT AND THE PRODUCT OR SERVICE PROVIDED.

—WARREN AGIN



domain name holder. For domain names originally registered with Network Solutions before March 30, 1998, the party listed as the domain name holder may in fact be the old administrative contact.

Trademarks related to domain names. The right to use a domain name is closely tied to trademark rights, and the lender should examine the trademark rights held by the borrower in the domain name as part of the due diligence process. The borrower may have obtained trademark rights in the domain name because of the domain name's use in identifying the source of products or services offered through the borrower's Website. The borrower may also have established trademark rights in the domain name by using the trademark in non-Internet-related trade or commerce. Because the borrower's right to continue to use the domain name may depend on the strength of the borrower's trademark, the attributes of the trademark must be examined.

The lender should ascertain the strength of the trademark. This involves analyzing the uses of the trademark, both on- and off-

line, the amount of time the trademark has been in use, the extent to which it has acquired secondary meaning, and the relationship between it and the product or service provided (for example, whether the trademark is fanciful or generic). The lender also needs to determine whether the trademark has been registered with the U.S. Patent and Trademark Office or has been registered outside of the United States. The lender should determine the status of any trademark registration, confirm that all fees have been paid, and review the records of the U.S. Patent and Trademark Office to determine whether any rights to the trademark have been assigned or otherwise encumbered. The lender also should determine whether any disputes over trademark use exist, and if so, the status of the disputes.

#### Security Agreements for Domain Names

The lender needs to prepare a security agreement that ensures that the lender will obtain a perfected security interest in the domain name and all attendant rights, the collateral will be main-

tained during the loan term, and the lender will be able to obtain control over the domain name in the event of a default. These provisions are appropriate not just to loans to Internet-based businesses, but to loans to any business with a domain name. Possibly, similar provisions should be part of any loan because the borrower that currently lacks a domain name now will probably obtain one in the future. The lender should be prepared in any case.

Collateral description. The lender should obtain a security interest in the domain name, all related trademark rights, and goodwill related to the trademark. A security interest in all "general intangibles" should suffice to cover all three elements. However, because of the uncertainty regarding the nature of domain names, the security interest should also reference a security interest in all rights in and to the domain name. Alternatively, the lender can include language such as "including without limitation all rights, of whatever form whatsoever, in and to domain names" in the collateral description. A separate security agreement may be needed for fil-

ing with the U.S. Patent and Trademark Office. The security agreement should be filed along with Form PTO-1618A, Recordation Form Cover Sheet.

**Warranties and covenants.** The security agreements should include basic warranties and covenants designed to protect the lender:

- The borrower should warrant that it is the owner of the domain name and that its rights to the domain name are not subject to any rights of third parties, such as a lease or security interest.
- The borrower should warrant the identity and location of the servers used in connection with the domain name, and should warrant the identity of the party having control over the domain name servers. The borrower should agree not to change the domain name servers without notification to the lender.
- The borrower should warrant the identity of the administrative contact with the registry and covenant that it will not cause any change in the registry's contact information without prior written approval of the lender.
- The security agreement should contain covenants requiring the borrower to maintain the trademark by defending against any infringement suits and by policing the trademark. The lender should have the option to perform these tasks at the borrower's expense if the borrower fails to perform them. The borrower should be

required to maintain continued use of the trademark in commerce.

- The borrower should covenant to renew the domain name registration during the loan term.
- The borrower should warrant the name of the registrar and should warrant not to change registrars without the lender's consent.
- The borrower should agree to make all payments to the domain name registrar necessary to maintain the domain name.

#### **Power of attorney scope.**

Transferring domain name and trademark registrations requires filing documents signed by the registrant. The lender must have the ability to execute on behalf of the borrower the necessary papers. The borrower needs to provide the lender with a power of attorney sufficient to allow the lender to take any action—and sign on behalf of the borrower any document—necessary to maintain the domain name, maintain any trademark rights, file an actual assignment of the trademark and related goodwill with the U.S. Patent and Trademark Office, provide instructions to the domain name registrar regarding the domain name, and execute on behalf of the borrower any documents necessary to transfer registration of the domain name.

#### **Third-Party Agreements with Website Hosting Services**

A Website hosting service used by the borrower will play a role in the lender's relationship with the borrower. The hosting service may act as the administra-

tive contact and billing contact for the domain name. The hosting service also will be responsible for maintaining the two domain name servers required by Network Solutions in connection with any domain name registration. Even if the borrower maintains its own Website, it will lease its connection to the Internet from an ISP.

The lender will want the Website hosting service or ISP to enter a waiver and consent agreement with the borrower and the lender, providing for the following:

- The hosting service recognizes the lender's security interest in the domain name and in any contracts between the hosting service and the borrower, regardless of perfection.
- The hosting service will act as the administrative contact with the domain name registrar.
- The hosting service will promptly notify the borrower and the lender of any notice of adverse action received from the registrar, or any other party, through its administrative contact.
- The hosting service recognizes that the borrower is the owner of the domain name, subject to the borrower's interest, and that the hosting service has no ownership right in the domain name.
- The hosting service will not make any changes in the contact information at the registrar other than as instructed by the borrower or lender, and only in accordance with the waiver and consent agreement.
- The hosting service will, upon receipt from the lender of notice of the borrower's

default, recognize an assignment of contractual rights to the lender or its designee, and will change the contact information at the registrar as directed by the lender.

- The hosting service will, as administrative contact, implement such security measures as necessary to ensure that

third parties cannot affect the domain name contact information at the registrar.

- The lender will, on exercising its rights against the domain name and/or Internet connection under the security interest, assume defined payment responsibilities to the hosting service.

In some cases, the hosting service will be either unable or unwilling to enter such an agreement. In such cases, a third party should be enlisted to act as the administrative contact as a sort of “escrow agent,” unless the lender is willing to accept the responsibility. □