

**ENFORCING SECURITY INTERESTS IN MEMBERSHIP INTERESTS  
AND PARTNERSHIP INTERESTS UNDER REVISED ARTICLE 9 OF  
THE UNIFORM COMMERCIAL CODE**

**By**

**DENNIS B. ARNOLD  
Gibson, Dunn & Crutcher LLP**

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COMMERCIAL CODE

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**ENFORCING SECURITY INTERESTS IN MEMBERSHIP INTERESTS AND PARTNERSHIP INTERESTS UNDER REVISED ARTICLE 9 OF THE UNIFORM COMMERCIAL CODE**

**I. REMEDIES UPON DEFAULT**

A. *Statutory Remedies.* The Uniform Commercial Code provides a secured party with a fairly broad array of remedies upon the occurrence of an "Event of Default" upon an obligation secured, whether in whole or in part, by personal property. See, UCC Section 9-601(a)<sup>1</sup>. These remedies include, without limitation, each of the following:

1. Foreclosure by Public Sale
2. Foreclosure by Private Sale
3. Retention of Collateral in Satisfaction of the Debt
4. Judicial Enforcement
  1. Judicial foreclosure
  2. Execution as a judgment creditor upon the collateral
5. Collection Rights Under UCC Section 9-607

B. *Practical Utility of Statutory Remedies.* As noted below, some of these remedies will differ in terms of practical utility in connection with an exercise of remedies in respect of collateral consisting of membership interests in a limited liability company or limited partnership interests in a limited partnership. Certain of the available range of statutory remedies, for example, retention of collateral in satisfaction of the secured debt under UCC Section 9-620, are likely to be of particular utility in the context of proceeding against collateral of this nature.

C. *Commercial Reasonableness.*

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<sup>1</sup> Both for the New York UCC and the uniform version for Article 9 use hyphens; in California, *Division Nine* (as Article 9 is known) does not use hyphens. Form of citations to each statute are utilized randomly.

Revised Article 9 imposes a duty of commercial reasonableness on all aspects of a "disposition" of collateral. *UCC Section 9-610(b)*. Unlike the former version of Article 9, the statute now clearly applies the "commercial reasonableness" standard to every aspect of a "disposition" of collateral:

*"Every aspect of a disposition of collateral, including the method, manner, time, place, and other terms, must be commercially reasonable." UCC Section 9-610(b) (Emphasis added.)*

## **II. FORECLOSURE BY PUBLIC SALE**

### **A. Notice of Sale.**

A public sale under UCC Section 9-610(b) contemplates a public auction of collateral following:

1. transmittal of notice to:
  - (a) all "debtors";
  - (b) all "secondary obligors;"
  - (c) any other party which, 10 days before the "notification date", held a security interest in the collateral perfected by the filing of a financing statement;
  - (d) "any other person from which the secured party has received, before the notification date, an authenticated notification of a claim of an interest in the collateral"; and
  - (e) "any other secured party that, 10 days before the notification date, held a security interest in the collateral perfected by compliance with a statute, regulation, or treaty described in subdivision (a) of Section 9-311."

*Note:* Notice of a disposition need not be sent to an "Obligor"; Section 9-610(c) omits "Obligors" from the category of parties entitled to receive such notice.

*Official Comment to Section 9-611, Para. 3* ("Under subsection (b), the principal obligor (borrower) is not always entitled to notification of disposition: Example: Behnfeltdt borrows on an unsecured basis, and Bruno grants a security interest in her car to secure the debt. Behnfeltdt is a primary obligor, not a secondary obligor. As such, she is not entitled to notification of disposition under this section.")

2. Public Advertising; and
3. the opportunity for members of the public to participate in the auction.

*See, Official Comment To Revised Article 9, §9610 , ¶ 7.*

4. The *form* of notice for both a "private" and "public disposition" of collateral *not* consisting of "consumer goods" is set forth in Section 9-613(5) as follows:

" (5) The following form of notification \*\*\*, when completed, \*\*\* provides sufficient information:

NOTIFICATION OF DISPOSITION OF COLLATERAL

To:

\_\_\_\_\_

(Name of debtor, obligor, or other person to which the notification is sent)

From:

\_\_\_\_\_

(Name, address, and telephone number of secured party)

Name of Debtor(s):

\_\_\_\_\_

(Include only if debtor(s) are not an addressee)

*(For a public disposition:)*

We will sell (or lease or license, as applicable) the

\_\_\_\_\_ (to the highest qualified bidder in public

(describe collateral) as follows:)

Day and Date: \_\_\_\_\_

Time: \_\_\_\_\_

Place: \_\_\_\_\_

*(For a private disposition:)*

We will sell (or license, as applicable) the \_\_\_\_\_  
describe collateral privately sometime after  
\_\_\_\_\_.

(day and date)

You are entitled to an accounting of the unpaid indebtedness secured by  
the property that we intend to sell (or lease or license, as  
applicable) (for a charge of \$\_\_\_\_\_). You may request an  
accounting by calling us at  
\_\_\_\_\_

(telephone number)"

*(Emphasis added.)*

## **B. Delivery of Notice**

### 1. Statutory Definitions: *Debtor; Obligor; Secondary Obligor.*

The revised definitions of "Debtor," "Obligor," "and "Secondary Obligor", can render the determination of the precise persons and entities to whom notice must be sent is somewhat tricky.

(a) The term "*Debtor*" is defined in Revised Article 9 Section 9-102(a)(28) as follows:

*"Debtor"* means any of the following:

(A) *A person having an interest*, other than a security interest or other lien, *in the collateral*, whether or not the person is an obligor.

(B) A seller of accounts, chattel paper, payment intangibles, or promissory notes.

(C) A consignee." (Emphasis added.)

(b) The term "*Obligor*" is defined in *Revised Article 9 Section 9-102(59)* as follows:

*"Obligor"* means *a person that*, with respect to an obligation secured by a security interest in or an agricultural lien on the collateral, (i) *owes payment or other performance of the obligation*, (ii) *has provided property other than the collateral to secure payment or other performance of the obligation*, or (iii) *is otherwise accountable in whole or in part for payment or other performance of the obligation*. The term does not include issuers or nominated persons under a letter of credit." (Emphasis added.)

(c) The term "*Secondary Obligor*" is defined in *Revised Article 9, Section 9-102(59)*

as follows:

"*Secondary obligor*" means an obligor to the extent that either of the following conditions are satisfied:

(A) The obligor's obligation is secondary.

(B) The obligor has a right of recourse with respect to an obligation secured by collateral against the debtor, another obligor, or property of either.

(d) The new definitions of "Debtor" and "Obligor" replaced the prior Article 9 definition of "Debtor" and may be somewhat confusing as regards the dividing line between a "Debtor" and an "Obligor".

For example, the definition of "Obligor" includes one who has granted a lien on collateral not consisting of personal property to secure a debt which is also secured by a security interest on personal property. Thus, an "accommodation pledgor" of property *other than personal property*, is an "*Obligor*" and must receive notice of any public sale. By contrast, one who only pledges an interest in personal property to secure a debt and is not otherwise liable for payment is a "Debtor" under Revised Article 9. This distinction between an "Obligor" and a "Debtor" is even more confusing since, under suretyship law, both of these types of "accommodation pledgors" would be classified as a "surety" since their property secures the debt of a third-party. *California Civil Code Section 2787; Restatement of the Law (Third): Suretyship and Guaranty (ALI 1996)*.

*Note:* the inclusion of "accommodation pledgors" within the statutory definition of "obligor" is counter-intuitive since an "accommodation pledgor" whose only relationship to the transaction is pledging non-personal property is not thereby obligated to pay or perform the underlying debt. By contrast, most other parties encompassed within the statutory definition of "Obligor" are obligated for payment of a debt secured by personal property.

(e) Guarantors must *always* receive notice of a public foreclosure sale. Guarantors are "secondary obligors" within the parlance of Revised Article 9.

(f) *Note:* Determination of which "obligors" are "secondary obligors" must be made with reference to law other than Revised Article 9. It is the law of suretyship that generally

determines when one's obligation is secondary and when a "surety" possess rights of recourse against others obligated upon or in respect of the same obligation. *See generally, Restatement of the Law (Third): Suretyship and Guaranty (ALI 1996).*

### **C. Advertising**

1. The defining characteristic of a "public sale" is the requirement for advertising a sale of collateral. *UCC Section 9-610(b)*. Determining whether an ad in a newspaper is sufficient to fulfill a secured party's duty of commercial reasonableness can be problematic.

2. It is prudent to view advertising of a public sale as the absolute minimum required in order to fulfill a secured party's duty of "commercial reasonableness." *See e.g., Ford & Vlahos v. ITT Commercial Finance Corp.*, 8 Cal 4th 1220 (1994).

(a) In *ITT*, the California Supreme Court unanimously held that compliance with the advertising requirements of *former* UCC Section 9-504(3) did *not* fulfill a secured party's duty to act in a "commercially reasonable" manner in disposing of collateral. "This case presents a narrow question of law: whether the California version of *Uniform Commercial Code Section 9-504*, subdivision (3), definitively limits a secured party's duty to advertise the sale of collateral merely to placing a legal notice in a newspaper. We conclude it does not\*\*\*\*\*". *Ibid.*, 8 Cal 4th at 1223.

(b) In *ITT*, the creditor advertised a public sale of a C-130 plane in the local Phoenix newspapers. The lender was the only bidder at the sale, acquired the jet for a "partial credit bid" of \$1,000,000.00 and then promptly resold the plane to a private party for approximately \$1.525 million. In rejecting the view that publication of an ad in a (then-statutorily mandated) "newspaper of general circulation" was sufficient to fulfill a secured party's burden to act in a "commercially reasonable" manner, the Supreme Court observed:

"In contrast to notice, one purpose of which is to alert the debtor and other secured creditors to take steps to protect their interests, possibly including locating bidders for their collateral, *the purpose of requiring adequate advertising of a foreclosure sale is to force the*



*secured party to ensure the auction is well attended by legitimate bidders, so that the highest commercially reasonable price for the collateral will be obtained." Ibid., 8 Cal 4th at 1232-33.*

(c) By noting the distinction between notice and publicity, the Court substantially expanded the responsibility of a foreclosing creditor to publicize a sale in a manner designed to maximize the number of bidders. "Thus, the minimum advertising required to make the publicity aspect of a sale of foreclosed collateral commercially reasonable is the notice given by publication. *But if placing the required legal notice is not a commercially reasonable method of informing potential buyers of the sale's time and place*, the sale will fail to meet the requirements of \*\*\*[commercial reasonableness]". *Ibid., 8 Cal 4th at 1233.*

(d) The Supreme Court focused upon the fact that the collateral was of a type that normally would be sold through dealers and thus held that public advertising in a newspaper, while technically required under the Code, was not enough to fulfill the burden of "commercial reasonableness" imposed upon a secured party. "A dealer in the type of property repossessed here--a valuable airplane--surely would advertise its auction in the relevant market by, for example, informing brokers, placing reasonably prominent announcements in recognized trade journals, or contacting individuals or entities known to be seeking an airplane of the type for sale." *Ibid., at 1229.*

(e) In testing the scope of advertising and publicity efforts undertaken by the creditor against what the Court believed a dealer in planes would do, the Court observed:

"We cannot conclude that the Legislature meant to provide that a sale's advertising is commercially reasonable as long as the bare requirements of formal notice are met, even if, to sell the type of collateral involved, a responsible dealer would employ more extensive advertising than placing a legal notice in a type in an obscure newspaper. *Publicity is much too important to a proper sale of foreclosed collateral for such a hypothesis to be commercially viable. For advertising is sine qua non to attendance at an auction,*

*Ibid., 8 Cal 4th at 1230. (Emphasis added).*

#### **D. Scope of Advertising.**

Revised Article 9 has eliminated the "newspaper of general circulation" designation for placement of advertising. This statutory modification cannot, however, be relied upon as a basis

for limiting the scope of advertising. The better view is to interpret the absence of a specific designated category of advertisement location as intended to eliminate any purported "safe harbor" status and thereby further underscore the *purpose* of requiring public advertising.

The placement of an ad for a public sale must, therefore, be made with reference to the stated goal of maximizing participation by the public. *ITT, supra. See, UCC Official Comment to Section 9-610, Para 7.*

1. *Intangible Collateral.* Since membership interests and partnership interests are intangible in nature, they lack a specific location. A membership interest or partnership interest representing an ownership interest in an entity which directly or indirectly owns real estate can presumably be viewed as sufficiently related to the underlying real estate as to justify advertising in local newspapers. However, to the extent that the project is significant in scope or nature, much wider advertising may be appropriate, including regional and/or national editions of the Wall Street Journal. In any event, advertising must also be made in the geographical area where the sale is to be conducted in order to comply with the statutory purpose of maximizing participation by the public.

*Form:* An example of an advertisement for a public disposition of collateral consisting of closely held "investment property" is attached as *Exhibit 1.*

2. *Location of "Market".* The "where to publish" an ad for a public sale may also be impacted by the marketplace in which the parties operated at the time the transaction was structured. To the extent that a court can discern the existence of a "market" for institutional mezzanine lenders and investors, it is conceivable that the burden of acting in a "commercially reasonable" manner may be interpreted to require additional advertising in the geographical area or areas where the parties who operate in such market are located. It is reasonable to anticipate that a debtor might try to establish that the secured party's customary scope of distribution on deals where it acts as a dealer or broker on similarly sized deals creates a "floor" for such market.

3. *Trade Journals.* If there exist trade journals or other similar publications that focus upon the *type* of property underlying the collateral, it is prudent to consider advertising

there in addition to newspapers and other broadly circulated publications. The *ITT* case clearly illustrates the likelihood that the "commercial reasonableness" of a foreclosing creditor's efforts to publicize a sale will be tested against the creditor's own custom and practice in selling assets of the same type. Advertising in publications of this nature will delay a sale in light of the longer "lead time" for magazine and journal ads. As a result, the ten-day "safe harbor" set forth in UCC Section 9-612(b) may be academic in dispositions of collateral of a type covered by trade journals.

4. In addition to public notification by advertising, the interpretation of "commercial reasonableness" under the *ITT* case indicates that additional efforts to directly notify prospective bidders of the foreclosure sale appear to be warranted. *See*, Part II C., above. These additional efforts may include notification of parties who deal in this type of collateral.

Note: Revised Article 9 provides a cause of action against a secured party to recover damages for breach of the duty to conduct a commercially reasonable disposition. *UCC Section 9-625(b)*. Similarly, UCC Section 9-615(f) imposes an additional level of scrutiny by substituting an objective standard for calculation of a deficiency for certain types of foreclosure sales at which the secured party is the purchaser and a significantly below market price is generated. Each of these should provide additional incentive to a secured party pursuing a "public sale" to seek to comply with its statutory duties.

#### **E. Public Sale**

##### 1. *What is a "public disposition"?*

Revised Article 9 does not define the term "public disposition". Nor does Revised Article 9 set forth the procedures to initiate and conduct a "public disposition. Unlike statutes governing real property foreclosures, Revised Article 9 does not specify particular procedures for the conduct of a "public sale" but instead relies upon the requirement that all dispositions be "commercially reasonable".

##### 2. *Public Access to the Sale.*

(a) The Official Comment to Revised Article 9 acknowledges the absence of a definition of "public disposition" and observes that:

"Although the term is not defined, as used in this Article, a "*public disposition*" is one at which the price is determined after the public has had a meaningful opportunity for competitive bidding. "*Meaningful opportunity*" is meant to imply that some form of advertisement or public notice must precede the sale (or other disposition) and that *the public must have access to the sale* (disposition).

*Official Comment to Sec 9-610, Paragraph 7.* (emphasis added.)

(b) Two components of a "public disposition" can readily be discerned from the foregoing excerpt from the Official Comment:

(i) "meaningful opportunity for competitive bidding"

(ii) public access to the sale.

#### **F. Restrictions on Bidding:**

##### 1. *Closely Held Securities: The Impact of State and Federal Securities Laws.*

(a) The federal and state securities laws generally prohibit the offering and public sale of unregistered securities. Virtually all membership interests in a limited liability company and all limited partnership interests are likely to be viewed as "securities". The "public sale" requirement imposed by the UCC would appear to clash directly with the state and federal prohibitions upon the public sale or offering of unregistered securities.

(b) As a result, a secured party seeking to foreclose upon closely held or other types of unregistered securities needs to tread a very narrow path between conducting a foreclosure sale that is sufficiently public to satisfy the "commercial reasonableness" standard imposed under the UCC and yet, at the same time, does not constitute a public offering of unregistered securities.

(c) The concept of circumscribing the scope of advertising and participation in bidding to only those parties who satisfy an "accredited investor" standard in order to conduct a "public disposition" in a manner which constitutes a "private placement" under applicable state and federal securities laws is recognized favorably in the Official Comments to Revised Article 9. *See, Official Comment to UCC Section 9-610, Paragraph 8.*

"Dispositions of investment property may be regulated by the federal securities laws. Although a "public" disposition of securities under this Article may implicate the registration requirements of the Securities Act of 1933, it need not do so. *A disposition that qualifies for a "private placement" exemption under the Securities Act of 1933 nevertheless may constitute a "public" disposition within the meaning of this section.* Moreover, the "commercially reasonable" requirements of subdivision (b) need not prevent a secured party from conducting a foreclosure sale without the issuer's compliance with federal registration requirements."

*Ibid., Para. 8. (emphasis added).*

## 2. *Contractual Limitations on Sale or Transfer of Collateral*

(a) In many mezzanine loans, particularly those where an underlying mortgage loan is transferred into a CMBS pool, there exist significant restrictions upon transfers of membership interests (or limited partnership interests) in a borrower or the "parent" entities which directly or indirectly control a borrower. These restrictions typically arise in three contexts:

(i) "change in control" provisions in an underlying mortgage or deed of trust which provide that transfers of the encumbered property or membership/partnership interests in a borrower or its constituent members or partners without the lender's consent constitutes an "event of default".

(ii) Intercreditor agreements between a mezzanine lender and a CMBS-mortgage holder will typically impose significant restrictions upon transfers of mezzanine collateral to anyone except a "Qualified Transferee".

(iii) Virtually all operating agreements and limited partnership agreements contain restrictions upon assignments and transfers of partnership interests or membership interests. These restrictions often include language seeking to restrict or flatly prohibit the grant of a security interest in a partnership interest, a membership interest or in cash distributions from a partnership or a limited liability company.

*Note:* The impact of restrictions contained in LLC operating agreements and partnership agreements upon the ability of a purchaser at a foreclosure sale to succeed to seek membership and enjoy all the rights and privileges of the former owner thereof are addressed in detail below in Part VII, below.

2. *Qualified Transferees.* Restrictions upon transfers of mezzanine collateral in an Intercreditor Agreement typically limit such transfers to a "Qualified Transferee". A typical example of the definition of a "Qualified Transferee"<sup>2</sup> sharply limits the scope of potential purchasers at a public foreclosure sale in the following manner:

“**Qualified Transferee**” means (i) Mezzanine Lender, or (ii) one or more of the following:

(A) a real estate investment trust, bank, saving and loan association, investment bank, insurance company, trust company, commercial credit corporation, pension plan, pension fund or pension advisory firm, mutual fund, government entity or plan, provided that any such Person referred to in this clause (A) satisfies the Eligibility Requirements;

(B) an investment company, money management firm or “qualified institutional buyer” within the meaning of Rule 144A under the Securities Act of 1933, as amended, or an institutional “accredited investor” within the meaning of Regulation D under the Securities Act of 1933, as amended, provided that any such Person referred to in this clause (B) satisfies the Eligibility Requirements;

(C) an institution substantially similar to any of the foregoing entities described in clauses (ii)(A) or (ii)(B) that satisfies the Eligibility Requirements;

(D) any entity Controlled by any of the entities described in clause (i) or clauses (ii)(A) or (ii)(C) above;

(E) a Qualified Trustee in connection with a securitization of, the creation of collateralized debt obligations (“CDO”) secured by or financing through an “owner trust” of, the Mezzanine Loan (collectively, “Securitization Vehicles”), so long as (A) the special servicer or manager of such Securitization Vehicle has the Required Special Servicer Rating and (B) the entire “controlling class” of such Securitization Vehicle, other than with respect to a CDO Securitization Vehicle, is held by one or more entities that are otherwise Qualified Transferees under clauses (ii)(A), (B), (C) or (D) of this definition; provided that the operative documents of the related Securitization Vehicle require that (1) in the case of a CDO Securitization Vehicle, the “equity interest” in such Securitization Vehicle is owned by one or more entities that are Qualified Transferees under clauses (ii)(A), (B), (C) or (D) of this definition and (2) if any of the relevant trustee, special servicer, manager fails to meet the requirements of this clause (E), such Person must be replaced by a Person meeting the requirements of this clause (E) within thirty (30) days; or

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<sup>2</sup> The definitions of "Qualified Transferee" and "Eligibility Requirements" are from a model form of Intercreditor Agreement on the Dechert website. The definitions are reprinted here with permission.

(F) an investment fund, limited liability company, limited partnership or general partnership where a Permitted Fund Manager or an entity that is otherwise a Qualified Transferee under clauses (ii)(A), (B), (C) or (D) of this definition acts as the general partner, managing member or fund manager and at least 50% of the equity interests in such investment vehicle are owned, directly or indirectly, by one or more entities that are otherwise Qualified Transferees under clauses (ii)(A), (B), (C) or (D) of this definition."

**"Eligibility Requirements"** means, with respect to any Person, that such Person (i) has total assets (in name or under management) in excess of [\$600,000,000] **[Note: for very large loans, a higher amount may be required]** and (except with respect to a pension advisory firm or similar fiduciary) capital/statutory surplus or shareholder's equity of [\$250,000,000] **[Note: for very large loans, a higher amount may be required]** and (ii) is regularly engaged in the business of making or owning commercial real estate loans or operating commercial mortgage properties."

3. *Commercial Reasonableness Issues.* Although the Official Comment to revised Article 9, Section 9-610, paragraph 8 strongly confirms that restricting the scope of bidders at a public sale to those constituting "accredited investors" in order to comply with state and federal securities laws restricting the public sale and advertising of unregistered securities will not prevent a sale which qualifies as a "private placement" for securities law purposes from qualifying as a "commercially unreasonable" public sale, there may conceivably be an issue as to whether a court might view contractually imposed restrictions upon bidding by parties who do not qualify as "Qualified Transferees" differently than the need to comply with state and federal securities laws.

(a) As noted above, the *Official Comment* to revised Article 9 views a "*public disposition*" as one where "the public has had a meaningful opportunity for competitive bidding." The Official Comment, in turn, interprets "*Meaningful opportunity*" as implying, in addition to advertising, "... *the public must have access to the sale*". See, *Official Comment to Sec 9-610, Paragraph 7.* (emphasis added.)

(b) To the extent that "public access" is truly a goal of all public sales of personal property under the UCC, there may be a potentially significant issue as to whether a sale in which only a "Qualified Transferee" can purchase the collateral to be sold is a commercially

reasonable public sale on the ground that "the public" does not truly have access to such sale. Certainly, "the public" includes many parties who cannot qualify as a "Qualified Transferee".

(c) One counter-argument in favor of a public sale in this context is the sophistication of the parties in transactions of this nature. In addition, there may well be merit in the concept that the term "public" should not be interpreted in the broadest sense of that term but rather with reference to the segment of the public that has both the capacity and interest to acquire collateral of the nature being sold. If so construed, public advertising in publications which reach that segment of the public (e.g., Wall Street Journal, etc.) may suffice for purposes of "public access". The flexible standard of "commercial reasonableness" in Revised Article 9 suggests that construing the statute to require access to members of the general public who lack the economic capacity to acquire the collateral to be sold at a public sale would not serve any useful purpose or further or statutory goal.

*Note:* The concern with the ability to conduct a "public sale" in this context may suggest that a "private sale" is a better type of disposition for collateral of this nature in those settings where the universe of acceptable purchasers is sharply circumscribed. This may effectively eliminate challenges as to whether a public disposition involving collateral which may only be transferred to a "Qualified Transferee is a "public" sale. Nonetheless, as developed in Part III, below, the foreclosing secured party may not purchase at a "private disposition" so that alternative will likely be of limited utility.

### **G. Timing**

UCC Section 9-612(b) sets forth a 10-day "safe harbor" for public dispositions of collateral as follows:

"In a transaction other than a consumer transaction, a notification of disposition sent after default and 10 days or more before the earliest time of disposition set forth in the notification is sent within a reasonable time before the disposition."  
*UCC Section 9-612(b).*

The Official Comment to Section 9-612 makes it clear that the 10-day "safe harbor" is not a minimum time for a disposition. *See, Official Comment to Section 9-612, Para. 3.* As to



some types of collateral, e.g., perishable items, a ten-day wait would clearly not be "commercially reasonable".

Section 9-611(e) also impacts upon timing by establishing a "safe harbor" which imposes a minimum 20-day wait before the "notification date".<sup>3</sup>

### **III. Foreclosure by Private Sale**

#### **A. Notice of Private Disposition.**

A private disposition of collateral is expressly authorized by UCC Section 9-610(b) under Revised Article 9. Notice of the proposed disposition must be sent to the following:

1. all "debtors";
2. all "secondary obligors;"
3. any other party which, 10 days before the "notification date", held a security interest in the collateral perfected by the filing of a financing statement;
4. "any other person from which the secured party has received, before the notification date, an authenticated notification of a claim of an interest in the collateral."

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<sup>3</sup> Section 9611(e) provides as follows:

(e) A secured party complies with the requirement for notification prescribed in subparagraph (B) of paragraph (3) of subsection (c) if it satisfies both of the following conditions:

(1) Not later than 20 days or earlier than 30 days before the notification date, the secured party request, in a commercially reasonable manner, information concerning financing statements indexed under the debtor's name in the office indicated in subparagraph (B) of paragraph (3) of subdivision (c).

(2) Before the notification date, the secured party either:

(A) Did not receive a response to the request for information.

(B) Received a response to the request for information and sent an authenticated notification of disposition to each secured party or other lienholder named in that response whose financing statement covered the collateral.

5. "any other secured party that, 10 days before the notification date, held a security interest in the collateral perfected by compliance with a statute, regulation, or treaty described in subdivision (a) of Section 9-311."

*Note:* Precisely like a notice of disposition for a public sale, notice of a *private* disposition need not be sent to an "Obligor"; Section 9-610(c) omits "Obligors" from the category of parties entitled to receive such notice. *Official Comment to Section 9-611, Para. 3*

#### **B. Form of Notice of Private Disposition.**

The *form* of notice for both a "private" and "public disposition" of collateral *not* consisting of "consumer goods" is set forth in the statute in Section 9-613(5). The statutory form of notice is set forth above in Part II. A., above.

#### **C. Private Dispositions Are Encouraged under Revised Article 9.**

1. Revised Article 9 clearly displays a bias in favor of private dispositions on the theory that a sale of collateral through typical distribution channels for such type of property is likely to generate greater proceeds than a public auction. Paragraph 2 of the Official Comment to UCC Section 9-610 underscores this policy choice by noting that "This section encourages private dispositions on the assumption that they frequently will result in higher realization on collateral for the benefit of all concerned". *Official Comment to UCC Section 9-610, Para. 2.*

2. The statutory encouragement of private dispositions is also visible in the fact that the Code does not seek to establish a time period after default during which collateral must be sold or otherwise disposed. "This Division does not specify a period within which a secured party must dispose of collateral . This is consistent with this Division's policy to encourage private dispositions through regular commercial channels." *Official Comment to UCC Section 9-610, Para. 3.*

#### **D. Distinctions Between Private and Public Dispositions**

There are *two fundamental distinctions* between public and private dispositions of collateral.

1. First, a secured party may *not* purchase collateral at a private sale unless " \*\*\* the collateral is of a kind that is customarily sold on a recognized market or the subject of widely distributed standard price quotations". *UCC Section 9-610(c)(2)*.

(a) Neither of these exceptions will be applicable to a disposition of membership interests in a limited liability company or partnership interests in a limited partnership unless such collateral is traded on a national stock exchange. "A market in which prices are individually negotiated or the items are not fungible is not a recognized market, even if the items are the subject of widely disseminated price guides or are disposed of through dealer auctions." *Official Comment to UCC Section 9-610, Para. 9*.

(b) The exception for "widely distributed standard price quotations" has typically been very narrowly construed by the judiciary.

2. Second, the scope of notification differs in that UCC Section 9-613(1)(E) mandates transmittal of notification of "the time and place of a public disposition" while a private sale simply requires notification of the "time after which" a private disposition or other intended disposition is to be made. *See, Official Comment to UCC Section 9-610, Para. 7*.

#### **E. Strategic Advantages & Disadvantages of Private Dispositions of Collateral.**

1. A private disposition is likely to be significantly cheaper as a function of the absence of advertising. In many settings, this cost savings may be significant, particularly in light of the issues addressed above as to the scope of advertising that may be required to fulfill a secured party's burden to conduct a "commercially reasonable" disposition.

2. Similarly, in transactions where contractual restrictions on the scope of potential foreclosure sale purchasers are a factor (*see, Part II. F. 2, above*), a private sale may, in theory, be an ideal vehicle to arrange a sale to a "Qualified Transferee". The actual utility of this remedy will, however, vary widely. In settings where the secured party's motivation is acquisition of mezzanine collateral in order to salvage an underlying real property investment and the interests to be sold are of little value, there is likely to be little interest from anyone other than the secured party itself so a private disposition will not be available under UCC Section 9-610(c)(2).

3. The fundamental disadvantage of a private disposition is the prohibition upon a secured party purchasing collateral at a private sale unless " \*\*\* the collateral is of a kind that is customarily sold on a recognized market or the subject of widely distributed standard price quotations". Thus, in a situation where a secured party is seeking to acquire the collateral in order to gain control of a partnership or LLC which directly or indirectly owns underlying real estate, a private sale cannot be pursued. Except where there is significant collateral value or publicly traded investment property, a private disposition will generally not be useful as a remedy to realize upon membership or partnership interests in collateral.

#### **IV. Strict Foreclosure: Acceptance of Collateral in Satisfaction of the Debt**

##### **A. Strict Foreclosure Statutorily Expanded**

###### *1. Intangible Collateral Covered Under UCC Section 9-620.*

(a) Unlike former Article 9 which only permitted strict foreclosure with respect to tangible personal property in the possession of a secured party, Revised Article 9 now expressly permits "acceptance in satisfaction" with respect to any type of collateral, whether tangible or intangible and whether or not in the secured party's possession. *See, UCC Section 9-620.* "This section eliminates the requirement in former Section 9-505 that the secured party be 'in possession' of collateral. It clarifies that intangible collateral, which cannot be possessed, may be subject to a strict foreclosure under this section". *Official Comment to UCC Section 9-620, Para. 7.*

(b) For a variety of reasons noted in greater detail below in Part IV.E, *below*, the remedy of "strict foreclosure" is likely to be of significant utility in the enforcement of security interests in membership interests in limited liability companies and partnership interests in limited partnerships and may well be the "remedy of choice" for mezzanine loans secured by such collateral on a non-recourse basis.

###### *2. Partial Satisfaction Now Available.*

(a) Former UCC Section 9-505 only contemplated acceptance in *full* satisfaction of the obligation secured by personal property collateral. UCC Section 9-620(a)

makes it clear that a secured party can propose acceptance of collateral in "*full or partial satisfaction*" of the obligation. *UCC Section 9-620(a)*.

(b) The only significant distinction between a "partial" and "full" satisfaction for purposes of the "strict foreclosure" process contemplated by Section 9-620 is the requirement under UCC Section 9-620(c)(1) for a "partial satisfaction", the debtor must affirmatively consent to the proposed "acceptance" of collateral. "Passive acceptance", i.e., the absence of an objection by the debtor within a statutorily prescribed time period can suffice for purposes of a retention in full satisfaction after transmittal of an *unconditional* proposal to accept collateral in satisfaction. However, in order to validly retain a claim for any part of the unpaid debt, a secured party "must obtain the debtor's agreement to the "strict foreclosure in a record authenticated after default."

*Official Comment to UCC Section 9-620, Para. 3.*

3. *Strict Foreclosure Encouraged.*

The Official Comment to UCC Section 9-620 strongly supports the utility of "strict foreclosure" and observes "that \*\*\* *strict foreclosures should be encouraged and often will produce better results than a disposition for all concerned.*" (*emphasis added*). *Official Comment to UCC Section 9-620, Para. 2.*

**B. To Whom Must Notice Be Delivered**

Section 9-621 mandates the parties to whom a proposal to accept collateral in satisfaction under UCC Section 9-620 must be sent to each of the following:

1. all "debtors";
2. all "secondary obligors;"
3. any other party which, 10 days before the "debtor consented to the acceptance", held a security interest in the collateral perfected by the filing of a financing statement;
4. "any person from which the secured party has received, before the debtor consented to the acceptance, an authenticated notification of a claim of an interest in the collateral"; and

5. "any other secured party that, 10 days before the debtor consented to the acceptance, held a security interest in the collateral perfected by compliance with a statute, regulation, or treaty described in subdivision (a) of Section 9-311." *UCC Section 9-621*.

6. An example of a *conditional* proposal to retain membership interests in a series of limited liability companies under UCC Section 9-620 in full satisfaction is attached as *Exhibit 2*. The form includes a document intended to evidence the debtor's consent to the proposal.

### **C. What Constitutes "Acceptance"**

1. For an acceptance in *partial satisfaction*, and for an acceptance in *full satisfaction* which is *subject to conditions* other than those relating to the condition of the collateral, the secured party must satisfy the following conditions:

(a) agreement by the debtor "to the terms of the acceptance in a record authenticated after default"; and

(b) The secured party shall not receive, within the time set forth in 9620(d), a notification of objection to the proposal authenticated by

(i) a "person to which the secured party was required to send a proposal under Section 9-621"; or

(ii) "any other person, other than the debtor, holding an interest in the collateral *subordinate* to the security interest that is the subject of the proposal." (*emphasis added*). See, *UCC Section 9-620(a)*.

2. For an acceptance of an *unconditional* proposal in *full satisfaction* the secured party must satisfy the following conditions:

(a) The secured party does not receive, within the time set forth in 9620(d), an objection to the proposal authenticated by

(i) a "person to which the secured party was required to send a proposal under Section 9-621"; or

(ii) "any other person, other than the debtor, holding an interest in the collateral *subordinate* to the security interest that is the subject of the proposal." (*emphasis added*).

(b) The secured party shall either

(i) not receive an objection from the debtor within 20 days after transmittal of a "proposal that is unconditional or subject only to a condition that collateral not in the possession of the secured party be preserved or maintained", or

(ii) obtain the debtor's agreement "to the terms of the acceptance in a record authenticated after default".

*Note:* UCC Section 9-620(a) appears to condition, in part, the effectiveness of an "acceptance in satisfaction" upon the absence of an objection from the holder of a *subordinate* interest in the collateral. However, since Section 9-621(a)(2) mandates transmittal of a proposal under UCC Section 9-620 to *all* persons holding a security interest in the collateral perfected by filing – whether senior or subordinate – and Section 9-620(a) conditions acceptance upon the absence of an objection from a "person to which the secured party was required to send a proposal under Section 9-621", the scope and purpose of the reference to the holder of a "subordinate interest" in the collateral in UCC Section 9-620 is less than clear.

### 3. *No "Passive" or Implied Acceptance by Secured Party.*

Revised Article 9 appears to effectively insulate a creditor against an assertion that passive conduct constitutes an implied retention of collateral in satisfaction. UCC Section 9-620(b) expressly requires that a secured party affirmatively consent to the acceptance in an authenticated record or send a proposal to the debtor. In the past, creditors who obtained possession of collateral or received cash distributions upon collateral without conducting a disposition over a long time frame would sometimes face a "constructive" strict foreclosure argument as a defense to a subsequent deficiency action. *See, Official Comment to UCC Section 9-620, Para. 5.*

4. *Binding Nature of Secured Party's "Proposal"*. The Code views a proposal made by a secured party under Section 9-620 as binding. The Official Comment to Section 9-620 observes that:

"The secured party's agreement to accept collateral is *self-executing* and *cannot be breached*. The secured party is bound by its agreement to accept collateral and by any proposal to which the debtor consents."

*Official Comment to Section 9-620, Para.6. (Emphasis added).*

As a practical matter, a secured party can impose conditions to the effectiveness of a proposal transmitted to a debtor. A conditional proposal would be subject to both satisfaction of the secured party's conditions and the debtor's written acceptance (i.e., "a record authenticated after default").

#### **D. Effect of Acceptance of Collateral in Satisfaction**

Acceptance of collateral upon satisfaction of the conditions imposed by UCC Section 9-620(a) & (b) effects each of the following under UCC Section 9-622(a):

1. Discharges the obligation to the extent consented to by the debtor.
2. Transfers *all* of a debtor's rights in the collateral to the secured party.
3. Discharges the security interest that is the subject of the proposal and any subordinate security interest or other subordinate lien.
4. Terminates any other subordinate interest.

*Note:* The failure by a secured party to properly notify all of the parties required under Section 9-621 will *not* prevent an acceptance of collateral under Section 9-620 from becoming effective and discharging subordinate interests in the collateral. The aggrieved junior interest holder retains a claim for damages against the secured party under UCC Section 9-625(b). *See, UCC Section 9-625(c) & Official Comment to UCC Section 9-625, Para. 3.*

#### **E. Strategic Factors**

1. *Scope of Right To Object.*

The debtor, as well as all "secondary obligors" and other persons entitled under UCC Section 9-621 to receive notice of a proposal to accept collateral in satisfaction, is authorized by



statute to "object" within a statutorily proscribed period of time-- generally 20 days-- after transmittal of notice. Nothing in Revised Article 9 imposes a requirement to set forth the basis for a timely objection under UCC Section 9-620.

2. *Impact of Objection to Proposed Acceptance.*

Receipt of a timely objection from the debtor, any person entitled to notice under Section 9-621, the holder of subordinate interests in the collateral and any "secondary obligor" will effectively terminate the secured party's proposal to accept collateral in satisfaction. The debtor's consent is insufficient if any of the persons entitled to notice under Section 9-621 object.

3. *Strategic Advantages of "Strict Foreclosure".*

As a practical matter, "strict foreclosure" is an ideal remedy for proceeding against closely-held mezzanine collateral. By obviating the requirement in a "public disposition" for advertising, a creditor can significantly reduce its costs of realization upon the collateral. In transactions where only a "Qualified Transferee" or other similar institutional purchaser may, by contract, succeed to ownership of the collateral without triggering a default in the underlying mortgage debt, retention in satisfaction under Section 9-620 eliminates any potential challenges to the "public" nature of a disposition in which participation by broad segments of the public is not truly feasible. In addition, in settings where the secured party is the only likely purchaser, whether as a function of economics or the effect of transfer restrictions, "strict foreclosure" provides a useful non-public analogue to a private disposition at which the secured party would generally be barred from acquiring the collateral.

The pace of "strict foreclosure" is noteworthy as well. The 20-day period for objections under 9-620(b) is not particularly long. Although longer than the 10-day "safe harbor" for public and private dispositions under Section 9-612(b), the 10-day "safe harbor" will, in all likelihood, not be a practical factor if the collateral is of a nature that advertising in trade journals may be required.

The non-recourse nature of most mezzanine collateral also fits the "strict foreclosure" model. Since no deficiency is legally recoverable, there is little to be gained in terms of pursuing

the steps and expense needed to satisfy Article 9 requirements for a "commercially reasonable" disposition. Retention of the collateral in full satisfaction should, in the absence of objections, produce the same transfer of ownership of the collateral with no possible deficiency rights at much less cost.

4. *Debtor's Strategic Assertion of Objection to Acceptance.*

Because of the significant cost savings and strategic advantages to a lender from utilizing "strict foreclosure" it is clear that some Debtors may perceive strategic benefit in seeking to assert an objection to a secured party's proposal to accept collateral in satisfaction. Since a creditor would be forced to pursue one of its other-and, presumably, more costly-- remedies under Revised Article 9 once a debtor makes a timely objection to a "retention in satisfaction" proposal under Section 9-620, there may be a temptation for a debtor or its counsel to use the withholding of an objection or the delivery of a consent to a strict foreclosure proposal as a device to share some of the "avoided costs".

Note: Counsel may wish to consider whether the assertion of an objection by a "debtor" or a "secondary obligor" to a strict foreclosure proposal in a setting where there exists no economic justification for the objection (e.g., collateral worth materially less than the debt secured thereby) should be a basis under a contractual non-recourse "carveout" for transforming a non-recourse loan into a "full recourse" debt. *Query:* Could conditioning the loss of insulation against recourse upon the exercise of a fundamental right reserved to debtors and "secondary obligors" under Revised Article 9 be treated as an impermissible pre-default waiver under UCC Section 9-602(10).

**E. Use of Transfer Statement**

1. The acceptance of collateral in satisfaction will not ordinarily produce a bill of sale or other instrument to evidence the transfer of title to the collateral from a debtor to the secured party. For collateral subject to registration or title certificate systems, UCC Section 9-619 contemplates use of a "transfer statement" to evidence the underlying facts, (e.g., default,

exercise of remedies, acquisition of debtor's rights to collateral) and memorialize the steps by which a creditor proceeded against collateral under the UCC.

2. Although intended solely to enable a transferee of collateral to obtain the "transfer of record of all rights of the debtor in the collateral \*\*\* in any official filing, recording, registration, or certificate of title system covering the collateral", see, *UCC Section 9-619(b)*, the form and content of a "transfer statement" will also be useful in the context of a "strict foreclosure" or other collateral disposition to "tell the tale" of how the transferee became the owner of the collateral. A "transfer statement" is defined in *UCC Section 9-619(a)* to require a broad range of information and serves as a functional checklist of the steps by which a secured party acquires collateral. While lacking in statutory purpose, the use of a "transfer statement" with regard to mezzanine collateral acquired by "strict foreclosure" will provide a convenient device to evidence the transfer of title to the secured party or other transferee. In addition, the transfer statement can also be used in fulfilling reporting obligations that may exist under an Intercreditor Agreement.

3. An example of a Transfer Statement prepared after completion of an *unconditional* acceptance of a very broad range of tangible and intangible collateral under *UCC Section 9-620* in full satisfaction is attached as *Exhibit 3*.

## **V. Judicial Enforcement**

Judicial enforcement will generally be a relatively unattractive remedy to most holders of a security interest in a membership interest/partnership interest. Judicial foreclosure of a security interest in this type of collateral is likely to be more expensive and time consuming than other remedies.

Nonetheless, there may be strategic situations where "strict foreclosure" is unavailable and other remedies, such as public disposition, are problematic. In these settings, the "safe harbor" under *UCC Section 9-627(c)* for purposes of "commercial reasonableness of any collection, enforcement, disposition, or acceptance" "approved in \*\*\* a judicial proceeding" may provide sufficient justification to utilize judicial remedies. *UCC Section 9-627(c)*. This can

also be a useful adjunct in the context of enforcing a claim against a "secondary obligor" as a tool to insulate the creditor's conduct in the disposition from subsequent attack.

## **VI. Collection Rights Under UCC Section 9-607**

### **A. Statutory Remedies**

Revised Article 9 provides a secured party with a broad array of remedies in the context of a default by the debtor/pledgor. These are set forth in *Section 9-607(a)*. In addition, Revised Article 9 continues the freedom of contract approach of existing law by specifically authorizing the exercise of certain remedies after default and, subject to agreement of the parties, *prior* to default. *Sections 9-601(a) & 9-607(a)*.

The remedies authorized by statute *include* notification of an "account debtor" or other person obligated on collateral to pay to the secured party (9-607(a)(1)), collection of proceeds under Section 9-315 (9-607(a)(2)), enforce the obligations of an account debtor or other person obligated on collateral and exercise the rights of the debtor (9-607(a)(3)) in respect of the underlying obligation. Each of these remedies relates to collateral consisting of a "payment intangible" or an "instrument". In addition, Revised Article 9 also authorizes a secured party to foreclose or reduce its claim to judgment. *Section 9-601(a)*.

### **B. Notification to the Account Debtor and Collection.**

1. *Revised Article 9 Section 9-607(a)* provides, in relevant part, that:

"If so agreed, and in any event after default, a secured party may do all of the following:

(1) Notify an account debtor or other person obligated on collateral to make payment or otherwise render performance to or for the benefit of the secured party.

\*\*\*

(3) Enforce the obligations of an account debtor or other person obligated on collateral and exercise the rights of the debtor with respect to the obligation of the account debtor or other person obligated on collateral to make payment or otherwise render performance to the debtor, and with respect to any property that secures the obligations of the account debtor or other person obligated on the collateral."

2. The term “account debtor” does *not* include the person obligated upon a promissory note or other instrument. As a result, the statute refers in the alternative to an “other person obligated on collateral”. The definition of “account debtor” in *Section 9-102(a)(3)* only encompasses “a person obligated on an account, chattel paper, or general intangible.” The definition expressly states that the term “account debtor” “... does not include persons obligated to pay a negotiable instrument....”.

3. Collection from the underlying account debtor/person obligated upon collateral is an important remedy for a secured party who holds a security interest in a promissory note. Whether such security interest is perfected by possession or filing is irrelevant under *Section 9-607* for purposes of the secured party’s right, as against the debtor, to notify the person obligated upon the collateral to pay to the secured party.

**Note:** The rights conferred upon a secured party by *Section 9-607* do not determine the rights of the secured party against the underlying account debtor/person obligated upon collateral with respect to enforcement of the collateral itself. *Section 9-607(e)* (“This section does *not* determine whether an account debtor, bank, or other person obligated on collateral owes a duty to a secured party.”)

Those rights derive from the underlying instrument in the case of a pledged promissory note. For example, a secured party who has perfected a security interest in an instrument by filing and lacks possession of the instrument itself will encounter difficulty in enforcing payment by the underlying maker of such instrument if it insists upon presentment of the instrument. In addition, the existence of a default upon the debt owed by the debtor/pledgor to the secured party does not confer any rights to foreclose a deed of trust that secures the pledged instrument in the absence of a default upon the instrument itself.

4. Significant issues can also arise in terms of the respective enforcement and collection rights of *multiple secured parties*. For example, a secured party who perfects by filing can exercise its collection rights under *Section 9-607(a)* and obtain payments upon the collateral from the person obligated thereon notwithstanding the fact that another secured party who

perfected by possession has priority. The rights of the junior secured party will be determined with reference to the rights of the respective secured parties in the medium of payment. Thus, if the junior secured party receives a payment by check from the person obligated upon the collateral, the priority of the lien arising under Revised Article 9 is *not* determinative of the respective rights of the competing secured parties in the check which is, itself an “instrument” under both Articles 3 and 9. If the junior secured party qualifies as a “holder in due course” of the check/instrument under Section 3-305 and/or Section 9-331(a), it will prevail as against the senior secured party who possesses the pledged promissory note. Similarly, the junior secured party may prevail as to the check as a “purchaser” of an instrument and therefore obtain priority in respect of the check under Revised Article 9 Section 9-330(d). *See, Official Comment to Section 9-607, Paragraph 5; Official Comment to Section 9-330, Paragraph 7.* The junior secured party may also prevail as against the senior secured party as a *transferee of money* under Revised Section 9-332(a).

## **VII. Restrictions On Admission To Membership In or As A Partner In A Limited Partnership**

### **A. Transfer Restrictions.**

1. Virtually all limited partnership agreements and limited liability company operating agreements contain restrictions upon the transfer of membership/partnership interests. These restrictions typically include both prohibitions upon any sale or transfer of a membership/partnership interest to a third party without the consent of all or a majority of the other members/partners as well as restrictions upon the grant of a security interest in or assignment of the proceeds (i.e., an "economic interest") of a membership interest or limited partnership interest.

2. Both limited liability company operating agreements and limited partnership agreements also typically include provisions which require the consent of a specified percentage of the members/partners as a condition to the admission of a transferee of a member/partner. In the absence of a contractual provision restricting admission of a transferee as a member/partner,

the operative versions of the Revised Uniform Limited Partnership Act and the Limited Liability Company Act currently in effect in most jurisdictions impose a requirement that a majority of the members/partners consent to the admission of a transferee.

For example, the relevant statutory provisions in California respectively restrict admission of an assignee as a member of a limited liability company by requiring an affirmative vote of a majority of the members:

"Except as otherwise provided in the articles of organization or the operating agreement, an assignee of an interest in a limited liability company may become a member only if a majority in interest of the other members vote in favor of the assignee's admission to the limited liability company as a member.

*California Corporations Code Section 17303(a).*

Similarly, the relevant statutory provisions in California respectively restrict admission of an assignee as a limited partner by requiring consent of a majority in interest of the limited partners. *California Corporations Code Section 15674(a).*

#### **B. Distinction Between Grant & Enforcement of A Security Interest**

The relevant Limited Liability Company Act and the Revised Uniform Limited Partnership Act in effect in most jurisdictions distinguish between the *grant* of a security interest and the *enforcement* of a security interest in a membership interest or partnership interest. Thus, the statutes insulate both the debtor and a secured party against an argument that the simple act of granting a security interest in a membership/partnership interest effectuates a "transfer" or otherwise confers any rights upon a secured party with respect to internal matters within the LLC or partnership. *See, e.g., California Corporations Code Section 17301(c).*

"The pledge of, or granting of, a security interest, lien, or other encumbrance in or against any or all of the membership interest of a member shall not cause the member to cease to be a member or to grant to anyone else the power to exercise any rights or powers of a member." *Ibid.*

#### **C. Impact of a Disposition of Collateral**

Completion of a foreclosure sale or other disposition under the UCC will not result in the purchaser at a foreclosure sale being admitted as a member/partner in the partnership/limited liability company in the absence of the requisite percentage of consents contractually or

statutorily required from limited partners/members. *E.g., California Corporations Code Sections 15674(a) & 17303(a); 6 Del Code Section 18-702(a).*

The only property rights to which a foreclosure sale purchaser would succeed in the absence of obtaining the requisite consents to be admitted as a member/partner would be an entitlement to receive "proceeds and distributions" from the limited partnership/LLC. which would otherwise have been due to be paid to the original holder of the membership/partnership interest. In Delaware, for example, the statute governing limited liability companies provides that assignment of a membership interest both terminates the member ship status of the assignor/member and only entitles the assignee to receive distributions that would otherwise have been made to the assignor.

"Unless otherwise provided in a limited liability company agreement:

\*\*\* (2) An assignment of a limited liability company interest entitles the assignee to share in such profits and losses, to receive such distribution or distributions, and to receive such allocation of income, gain, loss, deduction, or credit or similar item to which the assignor was entitled, to the extent assigned; and

(3) A member ceases to be a member and to have the power to exercise any rights or powers of a member upon assignment of all of the member's limited liability company interest." *6Del. Code Section 18-702(b)*

As a result, it is of critical importance in structuring and documenting indebtedness secured by a security interest in a membership interest/partnership interest to obtain the requisite consents from the other members/partners of a limited liability company/partnership to insure that the party acquiring the collateral after disposition will succeed to all rights, benefits and privileges accorded to the member/partner which pledged its property as collateral.

As a practical matter, a secured party which only succeeds to a "proceeds" interest or a right to receive distributions from an LLC. or a limited partnership, but does not become admitted as a member/partner is in a very challenging strategic position because the absence of rights as a member/partner will hamper efforts to enforce payment of distributions. Since " \*\*\* an assignment of a limited liability company interest does not entitle the assignee to become or to exercise any rights of powers of a member", *6 Del Code Section 18-702(b)(1)*, the assignee lacks



the statutory rights to compel an accounting or otherwise enforce the rights conferred upon the assignor in the underlying limited liability company operating agreement.

**D. UCC Sections 9406 and 9408.**

Revised Article 9 also includes two provisions, *UCC Sections 9406(d) and 9408*, which benefit creditors who obtain a security interest in a limited partnership/membership interest by invalidating certain contractual restrictions upon the creation and enforcement of security interests in particular types of personal property collateral. As a general proposition in all states *other than Delaware*, a contractual restriction in a limited liability operating agreement upon the attachment, creation, perfection and enforcement of a security interest in a "payment intangible" and other similar types of collateral is unenforceable as a matter of law under UCC Section 9-406(d).

\*\*\* a term in an agreement between an account debtor and an assignor or in a promissory note is ineffective to the extent that it does either of the following:

(1) Prohibits, restricts, or requires the consent of the account debtor or person obligated on the promissory note to the assignment or transfer of, or the creation, attachment, perfection, or enforcement of a security interest in, the account, chattel paper, *payment intangible*, or promissory note.

(2) Provides that the assignment or transfer or the creation, attachment, perfection, or enforcement of the security interest may give rise to a default, breach, right of recoupment, claim, defense, termination, right of termination, or remedy under the account, chattel paper, *payment intangible*, or promissory note.

In addition, UCC Section 9-604(f) invalidates comparable restrictions upon the grant and enforcement of a security interest in any "rule of law, statute, or regulation". *UCC Section 9-406(f). (Emphasis added.)*

UCC Section 9-408(a) & (c) also renders contractual and statutory restrictions upon "assignment or transfer of, or the creation, attachment, or perfection of a security interest in," a promissory note, health care insurance receivable or general intangible. *UCC Section 9-408(a) & (c)*. The scope of the statutory invalidation of restrictions upon the creation and enforcement of a security interest in payment intangibles under UCC Section 9-406 is significantly broader than the more limited statutory invalidation of such restrictions set forth with regard to "general intangibles" in UCC Section 9-408. This is a function of the fact that the statutory language in

Section 9-406 expressly refers to "the creation, attachment, perfection, or *enforcement* of a security interest", *UCC Section 9-406(d)(1)*, while UCC Section 9-408 only refers to "the creation, attachment or perfection of a security interest". By eliminating the concept of "enforcement" of a security interest from UCC Section 9-408, the Code substantially limits the effect of these statutory invalidations of restrictions upon assignment.

The concept of invalidating restrictions on an obligation to pay money is not a new concept in the law. Former UCC Section 9-318(4) previously invalidated contractual restrictions upon assignments of what would not be considered as "payment intangibles" under Revised Article 9.

Except with respect to a limited liability company or a limited partnership organized under the laws of the State of Delaware, UCC Section 9-406 is sufficient to ensure that a creditor who obtains a security interest in a membership interest or partnership interest will, at a minimum, be able to enforce a right to receive payments and distributions (i.e., a "payment intangible") notwithstanding provisions in a partnership agreement or LLC. operating agreement which prohibit the grant of a security interest or otherwise provide that any assignment or grant of a security interest without the requisite consent of other partners/members is void. Since UCC Section 9-408 does not invalidate restrictions upon *enforcement* of a security interest, however, this statute is not sufficient to override the statutory restrictions upon admission of a transferee as a member/partner.

**E. Delaware 's Rejection of UCC Sections 9406 and 9408.**

1. For reasons which are not entirely clear, the State of Delaware opted early in 2002 to amend the Delaware versions of the Revised Uniform Limited Partnership Act and the Limited Liability Company Act to override and thereby eliminate the invalidation of contractual and statutory restrictions under Sections 9406 and 9408 of the Uniform Commercial Code as in effect in Delaware. Thus, on February 1, 2002, Delaware added the following as paragraph (e) to Section 18-1101:

*"(e) Sections 9-406 and 9-408 of this title do not apply to any interest in a limited liability company, including all rights, powers and interests arising under a limited*

liability company agreement or this chapter. This provision prevails over §§ 9-406 and 9-408 of this title." (*Emphasis added.*)

and the following as paragraph (e) to Section 17-1101 with regard to limited partnerships:

"(e) *Sections 9-406 and 9-408 of this title do not apply to any interest in a limited partnership, including all rights, powers and interests arising under a partnership agreement or this chapter. This provision prevails over §§ 9-406 and 9-408 of this title.*" (*Emphasis added.*)

2. The effect of these two amendments is the validation of contractual restrictions in a limited partnership agreement or a limited liability company operating agreement governing limited partnerships or LLCs organized under Delaware law upon the grant of a security interest in or assignment of a membership/partnership interest. Thus, in Delaware, if the underlying operating agreement or limited partnership agreement imposes restrictions upon the grant of a security interest, those restrictions will be enforceable and preclude " the creation, attachment, perfection, or enforcement of " such security interest upon the cash distributions otherwise due to the assignor of a member. By depriving a secured party of the benefit of UCC Sections 9406, the only way a creditor can obtain a valid lien upon these payment intangibles for a partnership or LLC organized under Delaware law is to strictly comply with any restrictions or conditions imposed upon the grant of a security interest in the underlying operating agreement or partnership agreement. By contrast, in all other jurisdictions, as secured party who takes a security interest in a membership/partnership interest should obtain a valid and enforceable lien upon the right to receive cash distributions (i.e., a "payment intangible) even if it failed to obtain any contractually required consents by virtue of UCC Section 9-406(d).

3. The amendment of Delaware's RULPA and LLC statute to override two provisions of the UCC in effect in Delaware is a trap for the unwary and the wary. One searching the Delaware UCC would find no clue that the statutory invalidation of transfer restrictions in Sections 9406 and 9408 are unavailable with respect to limited partnership and membership interests. In addition, the override of the statutory invalidation renders the Delaware UCC materially non-uniform and may impact a wide range of transactions in light of

the frequency with which sophisticated parties choose to organize limited liability companies under Delaware law.

### **VIII. ALTA 16/CLTA 128 Mezzanine Loan Endorsement**

#### **A. ALTA 16/CLTA Endorsement**

The new forms of Lender's and Owner's title insurance policies promulgated in 2006 by the American Land Title Association include a form of endorsement denominated as the ALTA 16/CLTA 128 Endorsement which is intended to provide a mezzanine lender with certain benefits arising from an Owner's Policy issued under the 2006 forms. (A copy of the form of endorsement is appended as an Appendix to this outline.)

The coverage provided by the ALTA 16 Endorsement includes the following:

1. Assignment of the "net proceeds" of any insurance claim paid under the Owner's Policy after deduction of amounts paid to a "senior lender" under the Lender's Policy issued to the "mortgage lender".
2. An agreement by the title insurer not to impute knowledge of the original "insured". This also would encompass any "action or inaction" of the original "insured" as of the time of issuance of the policy.
3. The insurer's agreement that it will not deny liability to a mezzanine lender on the ground that any or all of the ownership interests, whether direct or indirect, in the insured have been transferred to or acquired by the Mezzanine Lender.

#### **B. Potential Issues.**

There are potentially significant issues which arise in the context of the ALTA 16/CLTA 128 Endorsement. These include the following:

1. *Suretyship Status.* The underlying Owner is typically not obligated to a Mezzanine Lender. Rather, the direct or indirect members or partners of the Owner are the parties obligated upon mezzanine debt in most structures. As a result, the assignment of property of the Owner sought to be effected by this endorsement may transform the underlying Owner

into a “surety” since the property of the Owner is being assigned to secure the debt of a third-party. *See, California Civil Code Section 2787.*

2. *Legal Capacity.* There may be an issue as to whether the collateral assignment of the Owner’s property under this endorsement is within the capacity or legal power of an Owner in any setting where the underlying mortgage loan is to be securitized. This issue arises as a function of the fact that many of the standard “SPE” operating agreements and partnership agreements may preclude the SPE from incurring indebtedness in favor of any party other than the “Senior Lender” in order to achieve the element of separateness required for rated debt and provide a sound basis of issuance of a "non-consolidation" opinion to the underlying mortgage lender. Similarly, there may also be limitations upon the ability of an Owner formed as a SPE to be a “surety” in respect of the obligations of a third-party.

It does not appear that the provisions of Sections 9406 and 9408 of the UCC (which are addressed above in Part VII) will override any potential lack of power or legal capacity to assign property or otherwise incur debt to anyone other than a “Senior Lender”. A lack of capacity does not appear to constitute " a term ... in an agreement ... prohibits, restricts, or requires the consent ... of the account debtor to, the assignment or transfer of, or creation, attachment or perfection of a security interest in" a general intangible within the meaning of UCC Section 9-408.

3. *Potential Impact on "Non-Con" Opinions.* The creation of a surety-principal relationship between the Owner and the entity obligated to a Mezzanine Lender may impact any non-consolidation opinions being provided by counsel to the Owner. While the nature and extent of such relationship should not preclude the issuance of such opinions, the existence of this type of endorsement and the corresponding creation of reimbursement and subrogation rights by the Owner against the entity obligated to a Mezzanine Lender may well constitute items which should be disclosed and addressed in a non-consolidation opinion.

4. *Article 9 Security Interest.* This endorsement also appears to create a security interest in an insurance policy which would be subject to the attachment, creation and perfection requirements of Division 9 of the Uniform Commercial Code. The standard form of the ALTA

16 Endorsement appears to require a signature by the Owner. This should presumably satisfy the requirement under UCC Section 9-203(b)(3) that the "debtor has authenticated a security agreement". So long as the other components of "attachment" under Section 9-203 have been satisfied, the security interest should be perfected upon issuance of the endorsement under UCC Section 9-312(b)(4). Section 9-312(b)(4) provides that:

"(4) A security interest in, or claim in or under, any policy of insurance, including unearned premiums, may be perfected only by giving written notice of the security interest or claim to the insurer. This paragraph does not apply to a health care insurance receivable. A security interest in a health care insurance receivable may be perfected only as otherwise provided in this division."

**EXHIBIT 1**

NOTICE OF PUBLIC SALE OF COLLATERAL  
\_\_\_\_\_ COMMERCIAL CODE SECTION 9610

NOTICE IS HEREBY GIVEN that the collateral described below will be sold to the highest bidder at a PUBLIC SALE to be held on \_\_\_\_\_, \_\_\_\_\_, \_\_\_\_\_, at 11:00 a.m. local time at \_\_\_\_\_, located at \_\_\_\_\_, Suite \_\_\_\_\_, California \_\_\_\_\_, by \_\_\_\_\_, a Delaware corporation (“Secured Party”), the secured party under (i) that certain Pledge Agreement, dated as of \_\_\_\_\_, executed by \_\_\_\_\_, an \_\_\_\_\_ corporation (“\_\_\_\_\_”), in favor of Secured Party, (ii) that certain Pledge Agreement, dated as of \_\_\_\_\_, executed by \_\_\_\_\_, an \_\_\_\_\_ corporation (“\_\_\_\_\_”), in favor of Secured Party, and (iii) that certain Pledge Agreement, dated as of \_\_\_\_\_, executed by \_\_\_\_\_, an \_\_\_\_\_ corporation (“\_\_\_\_\_”), in favor of Secured Party. The collateral to be sold is security for certain indebtedness owed to Secured Party, which indebtedness includes, among other things, the debt evidenced by that certain Promissory Note in the original principal amount of \$\_\_\_\_\_, dated July 1, 1999 (the “Note”), executed by \_\_\_\_\_ (“\_\_\_\_\_”) in favor of Secured Party. Debtor is in default under the Note. The total amount due under the Note as of \_\_\_\_\_, 200\_ (including principal, interest, and other fees and charges) is \$\_\_\_\_\_.

The Collateral to be sold at such public sale consists of:

(a)(i) 100,000 shares of the common stock of \_\_\_\_\_, an \_\_\_\_\_ corporation (“\_\_\_\_\_”), held by \_\_\_\_\_, representing one hundred percent (100%) of the issued and outstanding common stock of \_\_\_\_\_; (ii) all stock certificates, options or rights of any nature whatsoever issued or granted by \_\_\_\_\_ to \_\_\_\_\_; (iii) all of \_\_\_\_\_ share, right, title and interest in and to all distributions, monies, fees, payments, compensation and proceeds due and payable to \_\_\_\_\_; (iv) all contract rights, general intangibles, claims, powers, privileges, benefits and remedies relating to any of the items listed in the foregoing subparagraph (iii); and (v) all cash or non-cash proceeds of any of the items listed in the foregoing subparagraphs (iii) and (iv);

(b)(i) 9 shares of the preferred stock of \_\_\_\_\_, an \_\_\_\_\_ corporation (“\_\_\_\_\_”), held by \_\_\_\_\_, representing fifty percent (50%) of the issued and outstanding preferred stock of \_\_\_\_\_; (ii) all stock certificates, options or rights of any nature whatsoever issued or granted by \_\_\_\_\_; (iii) all of \_\_\_\_\_ share, right, title and interest in and to all distributions, monies, fees, payments, compensation and proceeds due and payable to \_\_\_\_\_; (iv) all contract rights, general intangibles, claims, powers, privileges, benefits and remedies relating to any of the items listed in the foregoing subparagraph (iii); and (v) all cash or non-cash proceeds of any of the items listed in the foregoing subparagraphs (iii) and (iv); and

**EXHIBIT 1**

(c)(i) 9 shares of the preferred stock of \_\_\_\_\_ held by \_\_\_\_\_, representing the remaining fifty percent (50%) of the issued and outstanding preferred stock of \_\_\_\_\_; (ii) all stock certificates, options or rights of any nature whatsoever issued or granted by \_\_\_\_\_; (iii) all of \_\_\_\_\_'s share, right, title and interest in and to all distributions, monies, fees, payments, compensation and proceeds due and payable to \_\_\_\_\_ by \_\_\_\_\_; (iv) all contract rights, general intangibles, claims, powers, privileges, benefits and remedies relating to any of the items listed in the foregoing subparagraph (iii); and (v) all cash or non-cash proceeds of any of the items listed in the foregoing subparagraphs (iii) and (iv).

\_\_\_\_\_ is the fee owner of the \_\_\_\_\_ located at \_\_\_\_\_, \_\_\_\_\_, California \_\_\_\_\_. One hundred percent of the common stock of \_\_\_\_\_ is owned by \_\_\_\_\_. One hundred percent (100%) of the common stock of \_\_\_\_\_ is owned by \_\_\_\_\_.

The collateral described above will be sold to the person who is the highest bidder at such public sale. *Any prospective purchaser will be required to provide evidence that such prospective purchaser is purchasing the collateral for such prospective purchaser's own investment and its own account and not with a view towards subsequent resale or distribution.* Any prospective purchaser who is the highest bidder, other than Secured Party, will be required to pay the purchase price of the collateral (i) at the time of such public sale, and (ii) in cash, by cashier's check, or in other immediately available funds. If Secured Party is the highest bidder at such public sale, Secured Party may pay the purchase price of the collateral, in whole or in part, by crediting the amount of such purchase price against the balance of the unpaid indebtedness evidenced by the Note.

The sale may be adjourned from time to time, and notice of any adjourned sale date will be given only at the time of the scheduled sale and to those who attend the sale.

FOR MORE INFORMATION RELATING TO THE PUBLIC SALE ANNOUNCED  
HEREIN OR THE COLLATERAL DESCRIBED ABOVE, PLEASE CONTACT:

\_\_\_\_\_, \_\_\_\_\_, \_\_\_\_\_, Suite \_\_\_\_\_,  
\_\_\_\_\_, California \_\_\_\_\_, (\_\_\_\_\_) \_\_\_\_\_ - \_\_\_\_\_.

DATED: \_\_\_\_\_, \_\_\_\_\_



**EXHIBIT 2**

\_\_\_\_\_, 200\_

\_\_\_\_\_  
\_\_\_\_\_  
Beverly Hills, California \_\_\_\_\_-\_\_\_\_\_

**Re: Retention of Collateral in satisfaction pursuant to Section 9-620 of the Delaware Uniform Commercial Code**

Dear Sirs:

As you are aware, we represent \_\_\_\_\_ Bank of \_\_\_\_\_, in its capacity as Trustee (the "Indenture Trustee"), under that certain Indenture of Trust (the "Original Indenture"), dated \_\_\_\_\_ between \_\_\_\_\_, LLC ("\_\_\_\_\_") and the Indenture Trustee, as heretofore amended by that certain Supplemental Indenture to the Indenture, dated as of \_\_\_\_\_, (the Original Indenture, as so amended, the "Indenture"). Pursuant to the Indenture, on \_\_\_\_\_, \_\_\_\_\_ issued \$ \_\_\_\_\_ in original aggregate principal amount of \_\_\_\_\_ Lien Bonds, and \$ \_\_\_\_\_ in original aggregate principal amount of \_\_\_\_\_ Lien Bonds, (collectively, the "Bonds"). All terms used herein and not otherwise defined herein shall have the meaning ascribed to such term in the Indenture.

On \_\_\_\_\_, \_\_\_\_\_ defaulted on the payment of interest due on each of the Bonds issued by \_\_\_\_\_ pursuant to the Indenture and \_\_\_\_\_ has made no further payments of interest or principal thereon. Notice of such payment default was duly given on or about \_\_\_\_\_. As a result of such payment defaults, an "Event of Default" (as defined in the Indenture) exists under Section 7.01(a) of the Indenture. By execution of the attached Acknowledgment and Consent attached hereto, \_\_\_\_\_ hereby unconditionally and irrevocably acknowledges and agrees that an Event of Default exists under Section 7.01(a) of the Indenture, which Event of Default entitles the Indenture Trustee, *inter alia*, to exercise any and all rights and remedies available under the Indenture, that certain Pledge Agreement, dated \_\_\_\_\_ (the "Pledge Agreement"), between \_\_\_\_\_ and the Indenture Trustee, and/or under applicable law in respect of such Event of Default. The Indenture Trustee has not waived, presently does not intend to waive, and does not hereby waive, any such Event of Default and nothing contained herein nor the transactions contemplated hereby shall constitute or be deemed to constitute any such waiver.

The Indenture Trustee proposes to retain all collateral in which a security interest was granted by \_\_\_\_\_ to and in favor of the Indenture Trustee under the Indenture and/or the Pledge Agreement (the "Collateral"), including without limitation, each and all of the "Pledged Collateral" (as defined in the Pledge Agreement) pursuant to and in accordance with

## EXHIBIT 2

Section 9-620 of the Uniform Commercial Code as in effect in the State of Delaware (the "UCC") in satisfaction of the obligations owed by \_\_\_\_\_ to the Trust (as described in the Indenture) created by the Indenture. The Collateral includes, without limitation, each and all of the following:

(1) \_\_\_\_\_'s Membership Interest<sup>4</sup> (as defined in the Pledge Agreement), including without limitation, \_\_\_\_\_'s Membership Interest in each of those certain limited liability companies identified on Exhibit "A" hereto (collectively the "Target Companies"), including without limitation:

(a) The Economic Interest (as defined in the Pledge Agreement) appurtenant thereto, including without limitation, \_\_\_\_\_'s allocable share of all rights to all distributions from or in respect of any or all of the Target Companies;

(b) All other rights and interests of \_\_\_\_\_ in and to the Target Companies, whether now owned or hereafter acquired, including without limitation, all rights to vote or participate in the management of a Target Company, all rights to information concerning the business and affairs of a Target Company, and all rights of \_\_\_\_\_ under the respective Operating Agreement governing each Target Company;

(c) All interests and rights to which \_\_\_\_\_ is entitled as an "Investor Member" under the Operating Agreement for each Target Company and all interests and rights to which \_\_\_\_\_ is entitled as a Secured Party under Section 10.4 of the respective Operating Agreement of each Target Company;

(d) All rights of \_\_\_\_\_ to appoint a Representative and an Alternate to each of the Management Committee and the Operating Committee of each Target Company (as each of the foregoing terms is defined in each Operating Agreement); and

(e) Any and all other right, interest, claim or estate to which \_\_\_\_\_ at any time is or shall be entitled with respect to \_\_\_\_\_'s Membership Interest in each Target Company.

(2) All Net Revenues, Liquidation Proceeds, Refinancing Proceeds (each as defined in the Indenture), accounts and general intangibles, now owned or hereafter acquired by \_\_\_\_\_, regardless of how generated, and all proceeds therefrom,;

\_\_\_\_\_

<sup>4</sup> The term "Membership Interest," when used with respect to a Target Company, means the Member's entire interest in the Target Company, including without limitation, such Member's Economic Interest in such Target Company, together with all rights to vote and participate in the management of such Target Company and all rights to information concerning the business and affairs of such Target Company, all in accordance with the Operating Agreement (as defined below) of such Target Company.

**EXHIBIT 2**

(3) All funds, accounts, subaccounts or property, including all moneys and securities, from time to time held by the Indenture Trustee under the terms of the Indenture (other than the \_\_\_\_\_ Fund established thereunder);

(4) Any and all other rights and interests of \_\_\_\_\_ subject to the security interest granted and existing under the Pledge Agreement; and

(5) Any and all other right, title, interest, claim and estate, of every kind, conveyed, pledged, assigned or transferred to the Trustee as and for security.

You are hereby notified that the Indenture Trustee hereby proposes to retain the entirety of the Collateral in satisfaction of the Obligations (as defined in the Pledge Agreement). Notwithstanding the foregoing, the retention of the Collateral by the Indenture Trustee in satisfaction of the Obligations is conditioned upon the occurrence of each and all of the following:

(i) the Indenture Trustee shall not have received any objections on or before \_\_\_\_ \_\_, 200\_, authenticated by \_\_\_\_\_, any other person to whom this letter is required to be sent by Section 9621 of the UCC, or any other person holding an interest in the Collateral which is subordinate to the security interest in the Collateral granted by \_\_\_\_\_ to and in favor of the Indenture Trustee;

(ii) the execution and delivery to the Indenture Trustee of written consents substantially in the form attached hereto as Exhibit "B" by each of the respective members of each Target Company and the joinder therein by the respective members of the Management Committee of each Target Company;

(iii) the admission of the Indenture Trustee as a member of each of the Target Companies vested with all right, title, interest, claim, privileges and benefits theretofore held by \_\_\_\_\_ in strict accordance with applicable law and the respective Operating Agreements of each of the Target Companies; and

(iv) \_\_\_\_\_ shall have executed and delivered the Consent attached hereto to and in favor of the Indenture Trustee no later than \_\_\_\_ \_\_, 200\_.

As of the date hereof, the aggregate unpaid balance of the Obligations, including principal, interest and all other charges is \_\_\_\_\_.

Any objections should be sent to the address set forth above.

Sincerely yours,

\_\_\_\_\_ BANK OF \_\_\_\_\_

By: \_\_\_\_\_

Its: \_\_\_\_\_

**EXHIBIT 2**

**ACKNOWLEDGEMENT AND CONSENT**

The undersigned unconditionally and irrevocably acknowledges and agrees that (i) on \_\_\_\_\_, \_\_\_\_\_ defaulted on the payment of interest due on each of the Bonds issued by \_\_\_\_\_ pursuant to the Indenture and \_\_\_\_\_ has made no further payments of interest or principal thereon; (ii) notice of such payment default was duly given on or about \_\_\_\_\_ to \_\_\_\_\_ and (iii) as a result of such payment defaults, an "Event of Default" (as defined in the Indenture) exists under Section 7.01(a) of the Indenture.

By execution and delivery of this Acknowledgment and Consent to and in favor of the Indenture Trustee, the undersigned hereby unconditionally and irrevocably consents to the retention by the Indenture Trustee of the entirety of the Collateral in satisfaction of the Obligations, upon the terms and conditions set forth above. All defined terms used herein and not otherwise defined herein shall have the meanings ascribed to such terms in that certain letter dated \_\_\_\_\_, 200\_, from the Indenture Trustee to the undersigned.

Sincerely,

\_\_\_\_\_, **LLC**

By: \_\_\_\_\_, **Inc., a Member**

By: \_\_\_\_\_

Title: \_\_\_\_\_

By: \_\_\_\_\_, **a Member**

By: \_\_\_\_\_

Title: \_\_\_\_\_

### EXHIBIT 3

#### **TRANSFER STATEMENT PURSUANT TO SECTION 9619 OF THE CALIFORNIA UNIFORM COMMERCIAL CODE**

This Transfer Statement is dated as of \_\_\_\_\_, 200\_ and is executed by \_\_\_\_\_ ("\_\_\_\_\_") pursuant to and in accordance with Section 9619 of the California Uniform Commercial Code, with reference to the following:

1. Secured Party. \_\_\_\_\_, the Secured Party, is the holder of (i) two secured promissory notes (the "Notes"), executed by \_\_\_\_\_ ("\_\_\_\_\_") as of March 31, 2002 in the respective original principal amounts of \$ \_\_\_\_\_ and \$ \_\_\_\_\_, and (ii) other obligations of \_\_\_\_\_ arising under that certain Security Agreement and Cash Collateral Agreement (the "Security Agreement") executed by \_\_\_\_\_ and \_\_\_\_\_ as of March 31, 2002 (collectively, the "Obligations"). \_\_\_\_\_ properly and timely recorded the Security Agreement in accordance with the Uniform Commercial Code in effect in the State of California.
2. Collateral. As security for payment and performance of the Notes and the Obligations, \_\_\_\_\_ granted to \_\_\_\_\_ a security interest in all of \_\_\_\_\_'s right, title, interest, claim and estate in and to certain personal property now owned or hereafter acquired by \_\_\_\_\_ pursuant to the Security Agreement and more specifically identified on Exhibit "A" attached hereto (the "Collateral"). All terms used herein and not otherwise defined herein shall have the meaning ascribed to such term in the Security Agreement.
3. Debtor's Default. As of March 1, 2003, \_\_\_\_\_ was in default on the payment of interest due on each of the Notes. \_\_\_\_\_ made no further payments of interest or principal on the Notes subsequent to March 1, 2003. Notice of such payment default, and other defaults, was given to \_\_\_\_\_ on or about March 5, 2003. As a result of such defaults, one or more "Events of Default" existed under the Security Agreement. The existence of such Events of Default entitled \_\_\_\_\_, *inter alia*, to exercise any and all rights and remedies available under the Security Agreement, the Notes and/or under applicable law in respect of such Event of Default.
4. Exercise By Secured Party Of Post-Default Remedies. \_\_\_\_\_ exercised its remedies in respect of the Collateral as follows. By letter dated May 9, 2003, \_\_\_\_\_ duly notified \_\_\_\_\_, together with each and every other person holding an interest in the Collateral subordinate to the security interest held by \_\_\_\_\_ in the Collateral, pursuant to and in strict accordance with Section 9620 of the California Uniform Commercial Code, of (a) the election by \_\_\_\_\_ under Section 9620 of the California Uniform Commercial Code to retain the Collateral in full satisfaction of the Notes and the Obligations, and (b) \_\_\_\_\_'s right to object to such retention of the Collateral in satisfaction within 20 days thereafter. A copy of this letter is attached hereto as Exhibit "B". No objection of any type or nature was ever received by \_\_\_\_\_, whether from \_\_\_\_\_ or any of the other persons to whom notice of such election under Section 9620 of the UCC was given.
5. \_\_\_\_\_ Has Acquired The Rights Of \_\_\_\_\_ In The Collateral. \_\_\_\_\_ has acquired all right, title, interest, claim and estate heretofore held by \_\_\_\_\_ in the Collateral. As

**EXHIBIT 3**

a result, \_\_\_\_\_ is entitled to, among other things, the benefit and enjoyment of all rights conferred upon \_\_\_\_\_ by Section 9619(b) of the California Uniform Commercial Code.

6. Name And Mailing Address Of \_\_\_\_\_ And \_\_\_\_\_.

(a) The name and mailing address of \_\_\_\_\_ is as follows:

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_, CA \_\_\_\_\_

(b) The name and mailing addresses of \_\_\_\_\_ (who is the transferee hereunder) is as follows:

\_\_\_\_\_, \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_, CA \_\_\_\_\_

*with a copy to*

Dennis B. Arnold  
Gibson, Dunn & Crutcher LLP  
333 South Grand Avenue  
Los Angeles, CA 90071

IN WITNESS WHEREOF, \_\_\_\_\_ has executed this Transfer Settlement as of the date first written above.

Sincerely yours,

\_\_\_\_\_, \_\_\_\_\_

By: \_\_\_\_\_

\_\_\_\_\_  
President

cc: Dennis B. Arnold, Esq.

## EXHIBIT A

### COLLATERAL

As used herein, the term "Collateral" shall mean and refer to all right, title, estate, claim and interest of \_\_\_\_\_ ("\_\_\_\_\_") in and to all presently held and after-acquired personal property of \_\_\_\_\_, whether tangible or intangible, wherever located and of whatever nature, including, without limitation, each and all of the following:

(a) the "Lockbox" (as defined in the Security Agreement) established by \_\_\_\_\_ with Wells Fargo Bank, National Association, and the deposit accounts linked thereto and maintained in connection with the operation of said Lockbox, all agreements of any type or nature executed by \_\_\_\_\_ in respect of said Lockbox and all rights of any type or nature in respect of said Lockbox and all present and future accounts, accounts receivable, royalties, license fees, book debts, any and all rights to payment for goods sold or leased or for services rendered, and any such rights evidenced by chattel paper and/or electronic chattel paper, but excluding any such rights evidenced by an instrument, whether due or to become due and whether or not earned by performance, and whether now or hereafter acquired or arising in the future, and any and all supporting obligations, rights, claims, liens, security interests, guaranties, securities, choses in action and any other personal property of \_\_\_\_\_ in respect thereof which secure, evidence or guaranty payment of or relate to any such accounts, book debts or accounts receivable;

(b) all chattel paper, electronic chattel paper, documents, instruments, notes, drafts, general intangibles, payment intangibles, supporting obligations, (including, without limitation, any and all payment intangibles and any and all other rights to payment of money other than accounts, and all rights in any returned, reclaimed and repossessed goods and all supporting obligations, rights, claims, titles, securities, security interests, liens and guaranties evidencing, securing, guarantying payment of, relating to or otherwise with respect to any such rights to payment) licenses, licensing agreements, contracts, agreements, rights to payment, royalties, license fees, leases of personal property, undertakings, surety bonds, insurance policies and insurance proceeds covering loss or damage to all or any part of the Collateral and all payments and proceeds thereof, together with the proceeds, products, renewals and replacements thereof, including prepaid and unearned premiums, all forms of obligations owing to \_\_\_\_\_ or in which \_\_\_\_\_ may have an interest, however arising or created, all present and future choses and things in action, goodwill, deposits, trade secrets, catalogs, computer programs, purchase orders, software (including, without limitation, all source codes and object codes, all media of any type or nature on which such source codes or object codes are reproduced, copied, stored or maintained at any time and from time to time, and all licenses or other rights entitling \_\_\_\_\_ to use, copy and reproduce such object codes and source codes and all licenses and other rights granted by \_\_\_\_\_ to any other person or entity to copy, use, sell, market or reproduce computer software and such source codes and object codes (all such codes, property and rights being hereinafter collectively referred to as "data-related property"), technology processes, drawings, blueprints, proprietary information, patents, patent applications, trademarks, trade names, customer lists, mailing lists, copyrights, tax refunds of every kind and nature to which \_\_\_\_\_ may now or hereafter become entitled and however arising, and all other refunds of any kind and nature;(c) all present and hereafter acquired inventory and merchandise wherever located, including, but not limited to, all present and future goods held for sale or lease or to be furnished

under a contract of service, all raw materials, work in process, finished goods, software and data-related property, returned goods, repossessed goods, all parts, supplies or materials that are or might be used or consumed in a business or in connection with the manufacture, production, marketing, packing, shipping, advertising, selling, leasing or finishing of such goods, inventory, merchandise or other personal property of any kind or type, all packing materials, supplies and containers relating to or used in connection with any of the foregoing, and all bills of lading, warehouse receipts or documents of title relating to, covering or evidencing any right, title, interest or claim therein or thereto, including, without limitation, any and all computers, printers, office supplies and equipment, audio/video and other electronic equipment, all podiums, microphones, movie and slide projectors and screens and other property related to conference and convention facilities including but not limited to such inventory and merchandise set forth in Schedule C attached hereto;

(d) all present and hereafter acquired goods and equipment in all of its forms and wherever located, (including, but not limited to, any and all machinery, machine tools, pumps, motors, controls, attachments, parts, tools, furniture, furnishings, trade fixtures, molds, dies, motor vehicles, computers, typewriters, duplicating machines, word processing equipment, adding machines, calculators, dictating equipment, printing presses and related equipment, trailers, rolling stock, ships, boats, airplanes, motors, pumps, controls, tools, parts, works of art, consumer goods, and all other equipment of any type, kind or nature used by \_\_\_\_\_ in connection with or in the conduct of its business or operations, and all attachments, accessories, accessions, replacements, substitutions, additions and improvements to any of the foregoing, and all drawings, blueprints, reports, catalogs and computer programs related to any of the above including but not limited to those goods and equipment set forth in Schedule D attached hereto;

(e) any and all fixtures, including, without limitation, any and all machinery, vehicles, equipment, appliances and fixtures for generating or distributing air, water, heat, electricity, light, fuel or refrigeration, for ventilating or sanitary purposes, for the exclusion of vermin or insects or for the removal of dust, refuse or garbage or for other purposes, furniture, built-in furniture and installations, furnishings, shelving, lockers, partitions, vaults, elevators, awnings, mirrors, window shades, screens, Venetian blinds, draperies, drapery rods and brackets, screens, floor coverings, carpets, light fixtures, fire hoses and brackets and boxes for the same, fire sprinklers, alarm systems, plumbing, sinks, basins, pipes, faucets, water closets, heating units, water heaters, incinerators, telephone, sound, television and communication systems;

(f) all present and future deposit accounts of \_\_\_\_\_, including, without limitation, any demand, time savings, passbook or like account, all money, cash and checks, drafts, notes, bills, bills of exchange and bonds deposited therein or credited thereto, and all interest accruing thereon or any other property of \_\_\_\_\_ received or receivable by \_\_\_\_\_ in respect thereof, whether or not deposited in any such deposit account;

(g) all present and future books and records, including, without limitation, books of account and ledgers of every kind and nature, computer programs, computer tapes, computer software, and all electronically recorded data relating to \_\_\_\_\_ or the business of \_\_\_\_\_ or to any or all of the Collateral, all equipment, receptacles, containers and cabinets for such books and records, and all files and correspondence relating thereto;

(h) (i) all source codes, trade secrets, inventions (whether or not patented or patentable); technical information, processes, designs, knowledge and know-how; data bases;



models; drawings; websites, domain names, and URL's, and all applications therefor and reissues, extensions, or renewals thereof, together with all choses of action and rights to sue for past, present, or future infringement thereof, (ii) all trademarks, service marks, tradenames, corporate names, business names, trade styles, service marks, logos, other source or business identifiers, prints and labels on which any of the foregoing have appeared or appear and all designs and property of like nature, (iii) all letters patent of, or rights corresponding thereto, and all copyrights, whether registered or unregistered, held pursuant to the laws of the United States, any State thereof, or of any other country; including but not limited to those set forth in Schedule \_ attached hereto, together with (A) all registrations, applications and recordings in the United States Patent and Trademark Office, the United States Copyright Office or any similar office or agency of the United States, any State thereof or any other country; (B) all continuations, reissues, renewals or extensions thereof; (C) any patents and/or registration thereof issued under any pending and/or future applications, and (D) all petty patents, divisionals, and patents of addition, and (iv) any and all agreements and/or licenses granting any rights to use any of the foregoing or any right or interest therein, (iv) all goodwill associated with or derived from any of the foregoing, and (v) all proceeds of any type or nature derived from the use, sale, transfer, exchange, license or other disposition or exploitation of all or any part of the foregoing.

(i) any and all documents and documents of title, whether or not negotiable, including, without limitation, bills of lading, warehouse receipts, trust receipts and the like;

(j) all present and future stocks, bonds, debentures, securities, subscription rights, options, warrants, puts, calls, certificates, partnership interests, joint venture interests, investments and/or brokerage accounts and all rights, preferences, privileges, dividends, distributions, redemption payments, or liquidation payments with respect thereto;

(k) all present and future accessions, appurtenances, components, repairs, repair parts, spare parts, replacements, substitutions, additions, issue and/or improvements to or of or with respect to any of the foregoing;

(l) all rights, remedies, powers and/or privileges of \_\_\_\_\_ with respect to any of the foregoing; and

(m) any and all proceeds and products of any of the foregoing, whether now owned and existing or hereafter acquired or arising, including, without limitation, (i) all rents, issues, royalties and profits of or from any of the foregoing, (ii) whatever is now or hereafter received by \_\_\_\_\_ upon the collection or sale, exchange, lease, transfer or other disposition (whether voluntary or involuntary) of, or otherwise with respect to, any item of Collateral, whether constituting accounts, general intangibles, equipment, inventory, money, deposit accounts, goods, chattel paper, documents, instruments and insurance proceeds, securities, and any other tangible or intangible personal property, (iii) any such items that are now or hereafter acquired by \_\_\_\_\_ with any proceeds or products of Collateral, (iv) any amounts now or hereafter payable under any insurance policy by reason of any loss or damage to any Collateral or any proceeds or products thereof, and (v) the right to further transfer, including to pledge, mortgage, license, assign or sell, any of the property or rights mentioned herein.

**This Transfer Statement shall not be deemed an assumption by \_\_\_\_\_ of any obligations of \_\_\_\_\_.**

**SCHEDULE**  
**to**  
**TRANSFER STATEMENT**

---

<b>PATENTS</b>		
<b>Patent</b>	<b>Registration No.</b>	<b>Registration Date</b>

<b>PATENT APPLICATIONS</b>
<b>Patent Application No.</b>

**EXHIBIT 4**

ALTA 16/CLTA 128 [Mezzanine]  
ENDORSEMENT

Attached to Policy No.

Issued by

\_\_\_\_\_ TITLE INSURANCE COMPANY

1. The Mezzanine Lender is: \_\_\_\_\_

and each successor in ownership of its loan (“Mezzanine Loan”) reserving, however, all rights and defenses as to any successor that the Company would have had against the Mezzanine Lender, unless the successor acquired the indebtedness as a purchaser for value without knowledge of the asserted defect, lien, encumbrance, adverse claim or other matter insured against by this policy as affecting title to the estate or interest in the land.

2. The insured: \_\_\_\_\_

(a) assigns to the Mezzanine Lender the right to receive amounts otherwise payable to the insured under this policy, not to exceed the outstanding indebtedness under the Mezzanine Loan; and

(b) agrees that no amendment of or endorsement to this policy can be made without the written consent of the Mezzanine Lender except as provided in Section 12(a) of the Conditions and Stipulations.

3. The Company does not waive any defenses that it may have against the insured, except as expressly stated in this endorsement.

4. In the event of a loss under the policy, the Company agrees that it will not assert the provisions of Exclusions from Coverage 3(a), (b) or (e) to refuse payment to the Mezzanine Lender solely by reason of the action or inaction or knowledge, as of Date of Policy, of the insured, provided:

(a) the Mezzanine Lender had no knowledge of the defect, lien, encumbrance or other matter creating or causing loss on Date of Policy.

(b) this limitation on the application of Exclusions from Coverage 3(a), (b) and (e) shall:

(1) apply whether or not the Mezzanine Lender has acquired an interest (direct or indirect) in the insured either on or after Date of Policy, and

(2) benefit the Mezzanine Lender only without benefiting any other individual or entity that holds an interest (direct or indirect) in the insured or the land.

#### **EXHIBIT 4**

5. In the event of a loss under the Policy, the Company also agrees that it will not deny liability to the Mezzanine Lender on the ground that any or all of the ownership interests (direct or indirect) in the insured have been transferred to or acquired by the Mezzanine Lender, either on or after the Date of Policy.
6. The Mezzanine Lender acknowledges:
  - (a) that the amount of insurance under this policy shall be reduced by any amount the Company may pay under any policy insuring a mortgage to which exception is taken in Schedule B or to which the insured has agreed, assumed, or taken subject, or which is hereafter executed by an insured and which is a charge or lien on the estate or interest described or referred to in Schedule A, and the amount so paid shall be deemed a payment under this policy; and
  - (b) that the Company shall have the right to insure mortgages or other conveyances of an interest in the land, without the consent of the Mezzanine Lender.
7. If the insured, the Mezzanine Lender or others have conflicting claims to all or part of the loss payable under the Policy, the Company may interplead the amount of the loss into Court. The insured and the Mezzanine Lender shall be jointly and severally liable for the Company's reasonable cost for the interpleader and subsequent proceedings, including attorneys' fees. The Company shall be entitled to payment of the sums for which the insured and Mezzanine Lender are liable under the preceding sentence from the funds deposited into Court, and it may apply to the Court for their payment.
8. Whenever the Company has settled a claim and paid the Mezzanine Lender pursuant to this endorsement, the Company shall be subrogated and entitled to all rights and remedies that the Mezzanine Lender may have against any person or property arising from the Mezzanine Loan. However, the Company agrees with the Mezzanine Lender that it shall only exercise these rights, or any right of the Company to indemnification, against the insured, the Mezzanine Loan borrower, or any guarantors of the Mezzanine Loan after the Mezzanine Lender has recovered its principal, interest, and costs of collection. If a payment on account of a claim does not fully cover the loss of the insured claimant, the Company shall be subrogated to all rights and remedies of the insured claimant after the insured claimant shall have recovered its principal, interest, and costs of collection.

This endorsement is issued as part of the policy. Except as it expressly states, it does not (i) modify any of the terms and provisions of the policy, (ii) modify any prior endorsements, (iii) extend the Date of Policy, or (iv) increase the Amount of Insurance. To the extent a provision of the policy or a previous endorsement is inconsistent with an express provision of this endorsement, this endorsement controls. Otherwise, this endorsement is subject to all of the terms and provisions of the policy and of any prior endorsements.

**EXHIBIT 4**

If a payment on account of a claim does not fully cover the loss of the insured claimant, the Company shall be subrogated to all rights and remedies of the insured claimant after the insured claimant shall have recovered its principal, interest, and costs of collection.

AGREED AND CONSENTED TO:

(Insert name of Insured)

(Insert name of Mezzanine Lender)

By: \_\_\_\_\_

By: \_\_\_\_\_

Print Name: \_\_\_\_\_

Print Name: \_\_\_\_\_

Dated: \_\_\_\_\_

Dated: \_\_\_\_\_

\_\_\_\_\_ TITLE INSURANCE COMPANY

BY: \_\_\_\_\_  
Authorized Signatory

**OPTIMIZING RESULTS IN LOAN WORKOUTS AND  
LIQUIDATIONS INVOLVING INTELLECTUAL PROPERTY--  
WHERE THE RUBBER MEETS THE ROAD**

by

**Janet R. Walworth  
General Counsel & Secretary  
BFI Business Finance  
jwalworth@bfifinance.com**

**American Bar Association  
San Francisco, California  
November 12, 2008**

# **OPTIMIZING RESULTS IN LOAN WORKOUTS AND LIQUIDATIONS INVOLVING INTELLECTUAL PROPERTY-- WHERE THE RUBBER MEETS THE ROAD**

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**“Begin with the end in mind”-Stephen Covey**

**I. Introduction**

**A. It’s self-evident that at the outset, a lender doesn’t know whether a given loan become a distressed loan.**

**B. Lender also doesn’t know what avenue a borrower in distress will travel. Some of the possibilities include filing a Chapter 11 case, an Assignment for Benefit of Creditors, a voluntary sale by borrower and foreclosure.**

**C. Foreclosure can be public, private or strict foreclosure.**

**D. How well a lender will fare in a workout/foreclosure will depend on the quality of due diligence, documentation, monitoring, loan workout efforts, foreclosure and sale.**

**E. At the outset of a loan, it is important to bear in mind the possible ramifications of the various possible scenarios, taking into consideration the type of collateral.**

**F. My employer is an asset based lender, providing accounts receivable lines of credit and to a lesser extent, an inventory “subfeature” as part of its a/r loans. Located in Northern and Southern California, the Pacific NW and to a lesser extent, other western states, a high percentage of our borrowers use IP, whether owned or licensed, as a central part of their businesses. While we lend to companies that are either too new, growing too fast or have hit a bump in the road, we have a very low loss ratio due to the approach we take.**

**G. The company’s strategy from the beginning of a loan to the end is to have a security interest in all collateral, and to enter into license agreements up front so we will have access to inventory that is subject to a license. We also enter into agreements with key third parties such as landlords and warehouses, so in a default scenario, as lender we will have access to borrower’s premises and warehouses. We also control all cash. Then it’s a matter of monitoring developments and staying on top of a borrower’s financial performance.**

**H. Thus, we have the ability to offer a buyer almost a “turnkey” arrangement. By foreclosing, we can liquidate all collateral, even if licensed products, offer title to collateral, and by exercising our rights through third party documents such as landlord waivers and bailment agreements, be able to offer the**



buyer locations at which to operate/store goods if needed. Under the right circumstances, we'll also finance the purchase price.

I. Generally, in this borrowing environment, the IP/licenses are not necessarily of a high value on their own but instead have value in conjunction with all of the other collateral and infrastructure, all of which contribute to the possibility of maximizing value by offering what can without a lot of difficulty be resuscitated as close as possible to a “going business”.

J. This program will focus on loans in which a portion of the collateral consists of intellectual property/licenses, and how to take actions to optimize outcome and minimize risk, with a particular emphasis on the practicalities throughout the life of the loan, in order to allow workout and foreclosure to have a better opportunity to bear fruit.

K. Emphasis of this program will be practical, based on my experience “in the trenches”.

L. To the extent that my distinguished co-panelist Dennis Arnold, Esq. of Gibson, Dunn & Crutcher LLP will be addressing the framework of the Commercial Code as it relates to the process of foreclosure, I will address that less intensively in order not to duplicate his remarks, although I will discuss this subject in this outline.

## II. Recap of Law as to Perfection in IP

A. “IP” is a bundle of various rights: patents, trademarks, copyrights, trade secrets, domain names, licensing rights.

B. Idea is to be able to withstand the challenge of a hypothetical lien creditor in a bankruptcy, assignment for benefit of creditors or other proceeding. 11 USC Section 544 (a).

### C. Patents & Patent Applications

1. To perfect a security interest in a patent, a creditor must file a UCC financing statement in the state where the borrower is located, which is the state in which borrower is organized. *In re Cybernetic Services, Inc.* 252 F3d 1039 (9<sup>th</sup> Cir. 2001); *In re Transportation Design and Technology, Inc.*, 48 Bankr. 635 (Bankr. S.D. Cal. 1985); *In re Pasteurized Eggs Corp.*, 296 BR 283, 51 UCC Rep. 2d 227 (Bankr. D. N.H. 2003).

2. It is recommended that a secured creditor also file in the PTO due to the court's ruling that a buyer which had bought a patent was a holder in due course when the security interest of a secured creditor was not reflected in a filing

recorded with the Patent and Trademark Office. *Hendrie v. Saylkes*, 98 U.S. 546, 549 (1879); *FilmTec Corp Corp v. Allied-Signal, Inc.* 939 F. 2d 1568, 1573 Fed. Circ 1991)

#### **D. Trademarks & Trademark Applications & Associated Goodwill**

1. A trademark and associated good will may be registered under federal or state law.

2. To perfect a security interest in a trademark and associated good will, a creditor must file a UCC financing statement in the state where the borrower is located, which is the state in which the borrower is organized. *In re Together Dev. Corp.*, 227 BR 439, 37 UCC Rep 227 (Bankr D. Mass. 1998); *In re 199Z, Inc.* 139 B.R. 778 (Bankr. C.D. 1992); *In re Roman Cleanser* 43 B.R. 940 (Bankr. E.D. Mich 1994), *aff'd* 802 F.2d 207 (6<sup>th</sup> Cir. 1986).

3. It is also recommended that a secured creditor file in the PTO to avoid the buyer in due course issue discussed in C2.

#### **E. Registered Copyrights & Copyright Applications**

1. A copyright is a creature of statute-the federal Copyright Act (17 U.S.C. Section 205).

2. To be perfected in a registered copyright, a creditor must file with the United States Copyright Office due to preemption by the federal Copyright Act. *In re Peregrine Entertainment* 116BR 194, 11 UCC Rep 2d 1025 (C.D. California 1990); *In re Avalon Software, Inc.* 209 BR 517, 33 UCC Rep. 2d 650 (Bankr.D. Ariz 1977), which held that to perfect in updates, modifications, derivatives and proceeds of copyrights, including rights to payment of royalties under copyright licenses, a secured creditor need to have filed in Copyright Office.

3. Borrowers/owners/VC's sometimes balk at granting a security interest in the borrower's intellectual property, which they regard as the borrower's "crown jewels". But since a secured creditor needs to be perfected in registered copyrights in order to be perfected in the accounts receivable and license royalties generated from the copyright license, one way around this problem is to insist on a pledge of the copyrights but to agree that recourse will be limited to the proceeds of the copyrights. (See the sample provision set forth in Exhibit 4).

#### **F. Unregistered Copyrights**

A creditor must file a UCC financing statement in the borrower's location, since only registered copyrights are subject to the federal copyright law (and as a practical issue, the fact that an unregistered copyrights has no registration number and hence could not be easily indexed). *In re World Auxiliary Power Co.* 303 F3d 1120, 48 UCC Rep 2d. 447 (9<sup>th</sup> Cir. 2002).

**G. Hybrids- Trademarked Goods and Copyrighted Labels. Be aware of this issue. See *Quality King Distribs., Inc. v. L'Anza Research Int'l Inc.* 523 U.S. 135, 118 S. Ct. 1125 (1998).**

#### **H. Domain Names**

**1. The law is not entirely clear as to how to perfect a security interest in domain names. In an article entitled "The Net Result", published in the September 2000 RMA Journal, Warren Agin recommends that a lender specifically be granted a security interest in a borrower's domain names, all related trademarks and good will related to the trademarks. He points out that while all three fall under the rubric of general intangibles, he recommends that a lender both file an IP Security Agreement with the PTO as to any trademarks connected with the domain name and associated good will, and a UCC financing statement as to any domain name.**

**2. To the extent that there are third party agreements with website hosting services in connection with any domain name, it has been recommended by Warren Agin that the website hosting server sign a waiver and consent.**

**3. Matthew Kavanaugh at Buchalter Nemer has prepared a form of letter agreement with website hosting service (see Exhibit 5), which he has graciously consented to share.**

**4. Again also recommends that a Lender have a power of attorney to be able to take action necessary to maintain the domain name(s) provide3 instructions to the domain name registrar and executed any documents necessary to transfer the domain name(s).**

#### **5. Trade Secrets**

**Trade secrets are general intangibles.**

#### **Licenses**

**1. For a secured creditor to have a perfected security interest in the licenses of its borrowers, which are general intangibles, the general rule is that a secured creditor must file as a general intangible in a UCC financing statement in the state in which a borrower is located.**

**2. Only apparent exception: to obtain a perfected security interest in the proceeds of a license of a registered copyright license, a secured creditor must file in the Copyright Office.**

#### **G. Recap of Pertinent Law Related to Licenses as Collateral**

- a. **While outside the scope of this program, it is worth noting some of the key issues that may come into effect involving the insolvency of a licensee or licensor.**
- b. **11 USC Section 101 defines “Intellectual Property” as trade secret, inventions processes, designs or plants protected by patents and patent applications, works (including mask works) protected by copyright. It does not include trademarks.**
- c. **11 USC 101 definition of IP does not include trademarks or trademark licenses.**
- d. **The trustee/debtor in possession (“DIP”) has the right to assume or reject executory contracts under 11 USC Section 365. If it assumes the contract, it can also assign under certain circumstance. But see *In re Catapult Entertainment, Inc.*, 165 F.3d at 750-751 that stands for the proposition that a debtor may not assume a nonexclusive patent unless it obtains the consent of the nondebtor licensor. See also *N.C.P. Marketing Group, Inc.* 337 B.R. 230 (D. Nev. 2005), holding that trademark licenses are personal and nonassignable in bankruptcy unless the trademark license stated otherwise.**
- e. **If the trustee/DIP assumes the executory contract, must cure all defaults and provide adequate assurance of performance.**
- f. **If the trustee/debtor/licensor rejects the executor contract, Section 265 (n) comes into play. Under Section 365 (n), when an executory contract is rejected, a nondebtor licensee may elect to retain its rights under the license agreement and to continue to undertake its obligations under the license to maintain its right to use the license.**

### **III. Recap of Law of Foreclosure**

**Since Dennis Arnold has provided extensive and comprehensive materials on the laws regarding foreclosure for the discussion today, and my materials are already verging on being burdensome in length, I will direct you to his materials for purposes of this presentation.**

### **IV. Stages in the Life of a Distressed Loan**

## **A. Due Diligence**

**1. Obviously, it's best to undertake due diligence on IP at the outset of the loan. If due diligence not done properly at the beginning, take the opportunity to do so when reviewing the file when the loan becomes troubled-but not ideal and may be too late/subject to preference issues.**

**2. A lender should have its prospective borrower complete an IP Questionnaire including questions about borrower's inbound and outbound licenses. (Some information to obtain is attached as Exhibit 1.)**

**3. A lender should have an "owners" search run of a prospective borrower's copyrights, trademarks, patents.**

**4. It would be wise for a lender to review any asset purchase agreements if relatively recent to make sure title has passed and that the change in title has been recorded in either the U.S. Patent and Trademark Office ("PTO") or the U.S. Copyright Office ("Copyright Office").**

**5. It may also be wise for a lender to run a Google search on the borrower and see how it describes its products and IP. See whether borrower is taking steps to protect its IP by using the various symbols: ©, ®, and ™.**

**6. A lender should review any material licenses to which a borrower is a party. To that end, a few suggestions to follow:**

- a. a lender should inquire as to whether licenses are important to Borrower in terms of revenue, key products. Understand who the licensor is and who the licensee and how the other party is to work with;**
- b. a lender should review licenses with a few key issues in mind: term, licensed products, royalties, right to assign, termination provisions, default provisions, distribution rights after termination;**
- c. As to inbound licenses, discuss early with borrower if licensor will be willing to discuss entering into an agreement to the secured creditor granting the right to use the relevant IP license for the limited purpose of liquidating collateral. . (See discussion under Documentation); and**
- d. As to outbound licenses, a lender should read and determine key provisions. Again, term, royalty payments, default and termination provisions are important.**

7. A lender should inquire about any litigation, including IP litigation.

8. If borrower is a public company, a lender should review any public filings for any reference to IP or other litigation.

9. Obviously, a lender will run a UCC search and searches about suits, liens, judgments, bankruptcies, etc.

10. A lender should also run a UCC search and litigation search on the names of any entities from whom a borrower purchased stock or assets.

## **B. Documentation**

1. A lender should have key points in loan and security agreement for IP, including domain names, discussed in greater detail below.

2. It is recommended that Lender obtain an IP Security Agreement spelling out the terms of the security interest in the IP and the rights and obligations of the parties with respect to the IP and then file it (or a Memorandum of Interest) in the PTO or Copyright Office (See Exhibit 2 for an example of a IP Security Agreement)

3. A lender should perfect its security interests in IP correctly by filing in accordance with current law as outlined above.

4. However, even when perfection can be obtained only by filing a UCC financing statement, a lender should also file in the PTO to protect against IP assets being bought, i.e. the buyer in due course issue mentioned above.

5. Lenders might want to consider using a separate specific “IP” UCC financing statement (see Exhibit 3). As a pragmatic matter, this helps in working with borrowers which may be selling various items of IP from time to time, especially to help cash flow. It also helps avoid making a mistake and releasing a blanket UCC financing statement inadvertently. Buyers seem to get comfort from seeing such a document.

6. Pamela Martinson at Bingham McCutchen provided verbiage to describe domain names:

“all rights in and to domain names in whatever form, including without limitation, [www.xyz.com](http://www.xyz.com) and all derivative URLs leading to [www.xyz.com](http://www.xyz.com).”

**7. It is also recommended that lenders have negotiated agreements in place with licensors to be able to liquidate any inventory that is subject to licenses. (See Exhibits 7, 8 and 9 for possible agreements to use with licensors).**

**8. Licensors can be very protective of their IP. Accordingly, lenders/attorneys need to be creative and nonthreatening. One method that seems to work/be less threatening to licensors is to give a different title to what is in essence a temporary license agreement. Thus, the borrower signs a pledge of the Borrower/Licensee's rights under the license agreement, and then the licensor signs a written consent to the pledge. The consent provides that the lender can liquidate the licensed products even if the license agreement forbids assignment/sublicense by Borrower to third parties or even any sales after default/termination by borrower.**

**9. A lender should consider having landlord waivers in place with borrower's landlords giving the lender the right upon a default by borrower under a lease to take possession of tangible inventory at the premises and preferably conduct a private or public sale at such location. It can be difficult to obtain a landlord waiver depending on the landlord.**

**10. A lender should consider having bailment agreements in place with any parties storing inventory acknowledging lender's security interest and agreeing to give notice of borrower's default under the provisions of the warehouse agreement.**

### **C. Monitoring Stage**

**1. If IP is an important part of a borrower's collateral, it is important to get updated IP info from time to time and take additional steps to perfect if necessary. This also tells a lender whether dates and deadlines are being met.**

**2. It's a good idea to get periodic updates on status of licenses, including any amendments, terminations, defaults and other developments.**

**3. A lender may want to perform onsite audits to try to uncover financial and operational issues and disputes under license agreements and real property leases.**

**4. If a borrower has corporate or IP counsel, it's good to check in to see if there are any developments on the IP/license front or any other disputes whether with landlords, key customers, etc.**

**5. It may be beneficial to sign up with Google to get any postings about a borrower.**

**D. Pre-Foreclosure Workout Stage**

**IP is critical.**

1. A lender should run updated searches, including IP searches if IP is critical.
2. A lender should undertake a file review.
3. Lender should ask for an updated list of account debtors.
4. Lender should ask for an updated list of inventory.
5. Lender should run an updated UCC search.
6. Lender should send default letters to reflect the current situation.
7. Lender should review third party agreements such as landlord waivers, guaranties, bailment agreements, intercreditor agreements and send notices accordingly.
8. If employees of the borrower will be laid off, Lender should consider whether the Worker Adjustment and Retraining Notification Act of 1988 (as amended, the “Warn Act”) or similar state statute applies.

9. This is the time to work with a borrower to maximize results to the greatest extent possible. If a lender is making concessions in terms of forbearance to allow a borrower time to cure a default, ask for information and necessary actions in return. Get a release of claims and waiver of notice. (See sample forbearance letter agreement attached as Exhibit 10).

10. This is also the time for a lender to get ready for a potential sale by maximizing value. See “Patent Portfolios in Bankruptcy Cases-Protecting and Maximizing Their Value”, July/August Business Law Today. This article was written by Geoff Groshong and Samantha Pak at Miller Nash in Seattle, Washington.

11. Grossly simplified, the steps recommended in the Business Law article include:

- a. Identify and protect assets by running appropriate searches, list all patents, be aware of deadlines, ensure maintenance fees are paid; and
- b. Determine value by running through the analysis outline there and prepare to meet with buyers or investors.



**12. If you may be selling customer lists of an e-commerce or dot.com company, think about privacy issues**

**13. Consider whether sales tax will be charged on any sale. Maybe not if the lender is an “occasional seller”.**

**14. Remember that the IRS is entitled to 25 days’ notice of sale, so calculate that into your timing.**

**15. Think about going on direct notice to the account debtors, but if you have a good relationship with your borrower, discuss ahead of time. But if fraud, conversion going on, then don’t delay to get notice out. Also send notice if you think a bankruptcy might be imminent.**

**16. Be aware of collection activities that other creditors may be taking against the borrower. Under certain circumstances, the lender’s future advances may become junior.**

**17. If a borrower gets served with writs of possession or execution, follow the applicable Third Party Claim procedure under state law to protect the lender’s rights.**

#### **E. Foreclosure & Sale Stage**

**1. Be prepared for this to be a tumultuous and rocky time, with many ups and downs. Stay courteous and polite at the same time that you are watching out for your borrower’s interests.**

**2. This is the time to update the UCC search in case you will be needing to send a notice of disposition, whether public or private.**

**3. Consider whether your borrower will want to surrender property in full or partial satisfaction of debt.**

**4. Oftentimes, when a company starts getting in trouble, it’s tried unsuccessfully to sell itself as a going concern. Try to get that information from the borrower for purposes of both marketing and showing commercial reasonableness.**

**5. See if a prior owner who sold the company to the borrower might want to buy back the company.**

**6. Investigate whether any other creditor might be interested in an assignment of the lender’s position.**

**7. In some instances, an auctioneer will just buy your assets or agree to a guaranteed sale.**

**8. In the real world, we find that the parties in a given industry know about the borrower's problems and will express an interest in buying by getting in contact.**

**9. Keep records of who you talk to, including contact information, so those parties can all get notice of any disposition.**

**10. If your borrower is friendly, ask who might be interested buyers. If you don't know already, find out who the borrower's competition is.**

**11. It often helps to have a daily conference call with the borrower and its counsel/workout advisor to stay on track and gauge emotions.**

**12. This is where having a guaranty from the borrower's principals keeps the borrower's principals engaged-but if the principal is too stressed or upset, sometimes it's better to have other senior management from borrower also involved or be selective in handling communications, as long as can never say the guarantors been kept in the dark.**

**13. Although notice of disposition can be waived after default, it seems wiser to send notices to debtor and guarantors, and of course secured creditors, whose liens would otherwise not be foreclosed out. The notice of disposition of private collateral states the date after which a sale can take place-so just an approximation. This gives a lender time to maneuver, negotiate, etc. without having to go forward on a given date.**

**14. In the world of our borrowers, we rarely have public sales. Usually not worth the expense and we don't have the latitude in terms of timing. Also, if a buyer can be found which wants to take over the business, it usually wants to keep equipment at the location for a period of time even if it plans to ultimately move the assets, or may just want to buy and occupy the premises.**

**15. Oftentimes a borrower has a key customer which might also have an interest in buying, providing support to the borrower or have suggested contacts for interested parties.**

**16. If licenses are key, be in touch with the licensors/licensees as the case may be and see what their commercial interests are. They generally want to have new business/be involved with more solvent concern.**

**17. Once you have the group of serious contenders, let them know how bids will be accepted, if there is a minimum bid, and if there will be a chance to increase bids. Sometimes, a private sale of collateral will turn into a "mini" public sale by telephone where the "auction frenzy" can help bid up the price.**

**18. Share the Bill of Sale documents with prospective buyers as soon as they appear serious, in order to be able to proceed to a quick sale once a buyer is chosen.**

**19. A Bill of Sale will transfer title to IP, but the transfer needs to be reflected in an assignment in the PTO or Copyright office.**

**20. Be alert to fraudulent transfer concerns if any people or entities previously involved with the borrower seek to buy the company's assets. A lender wants to be made whole, but also wants to avoid potential future litigation.**

## **Exhibit 1**

### **Intellectual Property Questionnaire** **(Information Needed to Assist in IP Search)**

- 1. Legal Name of Entity**
- 2. Date of Incorporation**
- 3. State of Incorporation**
- 4. Changes in Name**
- 5. Trade Names Used**
- 6. Chief Executive Address**
- 7. Additional Addresses**
- 8. Description of each patent and registration/application no.**
- 9. Description of each trademarks and registrations no.**
- 10. Description of each copyright and registration no.**
- 11. Names of any proprietary software**
- 12. Future plans for patents, trademarks, copyrights**
- 13. List of all licenses where borrower is the licensee**
- 14. List of all licenses where borrower is the licensor**
- 15. List any past or present disputes or litigations about IP/licenses**
- 16. Contact information about person completing questionnaire**

Exhibit 2

**INTELLECTUAL PROPERTY SECURITY AGREEMENT**

This Intellectual Property Security Agreement (this "Agreement") is made as of this \_\_\_\_\_ day of \_\_\_\_\_, 20\_\_\_\_ by and between \_\_\_\_\_, a California corporation ("Pledgor") and \_\_\_\_\_ ("Secured Party"), a California corporation.

**RECITALS**

A. Secured Party has agreed to lend to \_\_\_\_\_ (the "Borrower") a California corporation, certain funds (the "Loan"), and Borrower desires to borrow such funds from Secured Party and will be secured in part pursuant to the terms of a Security Agreement, Loan and Security Agreement, and/or Secured Promissory Note executed or to be executed in connection herewith (either, as amended, the "Loan Agreement").

B. In order to induce Secured Party to make the Loan, Pledgor has signed or will sign a General Continuing Guaranty (the "Guaranty") guaranteeing the obligations owed by Borrower to Secured Party.

C. In addition, in order to induce Secured Party to make the Loan, Pledgor has agreed to grant a security interest in certain intangible property to Secured Party for purposes of securing the obligations of Pledgor to Secured Party under the Guaranty.

**AGREEMENT**

NOW, THEREFORE, the parties hereto agree as follows:

1. Patent Mortgage and Grant of Security Interest. As collateral security for the prompt and complete payment and performance of all of Pledgor's present or future indebtedness, obligation and liabilities to Secured Party under the Guaranty, Pledgor hereby transfers, conveys and grants a mortgage to Secured Party, as security, Pledgor's entire right, title and interest in, to and under the following (all of which shall collectively be called the "Collateral"):

a. Any and all copyright rights, copyright application, copyright registrations and like protections in each work or authorship and derivative work thereof, whether published or unpublished and whether or not the same also constitutes a trade secret, now or hereafter existing, created, acquired or held, including without limitation those set forth on Exhibit A attached hereto (collectively, the "Copyrights");

b. Any and all trade secrets, and any and all intellectual property rights in computer software and computer software products now or hereafter existing, created, or acquired or held;

c. Any and all design rights which may be available to Pledgor now or hereafter existing, created, acquired or held;

d. All patents, patent applications and like protections including, without limitation, improvements, divisions, continuations, renewals, reissues, extensions and continuations-in-part of the same, including without limitation the patents and patent applications set forth on Exhibit B attached hereto (collectively, the "Patents");

e. Any trademark and service mark rights, whether registered or not, applications to register and registrations of the same and like protections, and the entire goodwill of

the business of Pledgor connected with and symbolized by such trademarks, including without limitation those set forth on Exhibit C attached hereto (collectively, the "Trademarks").

f. Any and all claims for damages by way of past, present and future infringement of any of the rights included above, with the right, but not the obligation, to sue for and collect such damages for said use or infringement of the intellectual property rights identified above;

g. All licenses or other rights to use any of the Copyrights, Patents or Trademarks, and all license fees and royalties arising from such use; and

h. All proceeds and products of the foregoing, including without limitation all payments under insurance or any indemnity or warranty payable in respect of any of the foregoing.

2. Authorization and Request. Pledgor authorizes and requests that the Register of Copyrights and the Commissioner of Patents and Trademarks record this Agreement.

3. Covenants and Warranties. Pledgor represents, warrants, covenants and agrees as follows:

a. Pledgor is now the sole owner of the Collateral, except for non-exclusive licenses granted by Pledgor to its customers in the ordinary course of business and except for liens, encumbrances or security interests described in Exhibit D attached hereto;

b. Performance of this Agreement does not conflict with or result in a breach of any agreement to which Pledgor is party or by which Pledgor is bound;

c. During the term of this Agreement, Pledgor will not transfer or otherwise encumber any interest in the Collateral, except for non-exclusive licenses granted by Pledgor, copies of which Pledgor will provide from time to time to Secured Party at the request of Secured Party;

d. Each of the Patents is valid and enforceable, and no part of the Collateral has been judged invalid or unenforceable, in whole or in part, and no claim has been made that any part of the Collateral violates the rights of any third party;

e. Pledgor shall promptly advise Secured Party of any material change in the composition of the Collateral, including but not limited to any subsequent ownership right of the Pledgor in or to any Trademark, Patent, or Copyright not specified in this Agreement;

f. Pledgor shall (i.) protect, defend and maintain the validity and enforceability of the Trademarks, Patents and Copyrights, (ii.) use its best efforts to detect infringements of the Trademarks, Patents and Copyrights and promptly advise Secured Party in writing of material infringements detected and (iii.) not allow any Trademarks, Patents or Copyrights to be abandoned, forfeited or dedicated to the public without the written consent of Secured Party, which shall not be unreasonably withheld;

g. Pledgor shall not register any maskworks, software, computer programs or other works of authorship subject to United States copyright protection with the United States Copyright Office without first complying with the following: (i) providing Secured Party with at least fifteen (15) days' prior written notice thereof; (ii) providing Secured Party with a copy of the application for any such registration; and (iii) executing and filing such other instruments, and taking such further actions as Secured Party may reasonably request from time to time to perfect or continue the perfection of Secured Party's interest in the Collateral, including without limitation the filing with the United States Copyright Office, simultaneously with the filing by Pledgor of the application for any such registration, of a copy of this Agreement or a Supplement hereto in form acceptable to Secured Party identifying the maskworks, software, computer programs or other

works of authorship being registered and confirming the grant of a security interest therein in favor of Secured Party;

h. This Agreement creates, and in the case of after acquired Collateral, this Agreement will create at the time Pledgor first has rights in such after acquired Collateral, in favor of Secured Party a valid and perfected first priority security interest in the Collateral in the United States securing the payment and performance of the obligations evidenced by the Guaranty upon making the filings referred to in clause (3.i) below;

i. Except for, and upon, the filing with the United States Patent and Trademark office with respect to the Patents and Trademarks necessary to perfect the security interests created hereunder, and, except as has been already made or obtained, no authorization, approval or other action by, and no notice to or filing with, any governmental authority or regulatory body is required either (i.) for the grant by Pledgor of the security interest granted hereby or for the execution, delivery or performance of this Agreement or by Pledgor; or (ii.) for the perfection in the United States or the exercise by Secured Party of its rights and remedies hereunder;

j. All information heretofore, herein or hereafter supplied to Secured Party by or on behalf of Pledgor with respect to the Collateral is accurate and complete in all material respects;

k. Pledgor shall not enter into any agreement that would materially impair or conflict with Pledgor's obligations hereunder without Secured Party's prior written consent. Pledgor shall not permit the inclusion in any contract to which it becomes a party of any provisions that could or might in any way impair or prevent the creation of a security interest in Pledgor's rights and interests in any property included within the definition of the Collateral acquired under such contracts; and

l. Upon any officer of Pledgor obtaining knowledge thereof, Pledgor will promptly notify Secured Party in writing of any event that materially adversely affects the value of any of the Collateral, the ability of Pledgor or Secured Party to dispose of any of the Collateral or the rights and remedies of Secured Party in relation thereto, including the levy of any legal process against any of the Collateral.

4. Secured Party's Rights. Secured Party shall have the right, but not the obligation, to take, at Pledgor's sole expense, any actions that Pledgor is required under this Agreement to take but which Pledgor fails to take, after five (5) days' telephonic or written notice to Pledgor. Pledgor shall reimburse and indemnify Secured Party for all costs and expenses incurred in the reasonable exercise of its rights under this section 4.

5. Inspection Rights. Pledgor hereby grants to Secured Party and its employees, representatives and agents the right to visit, during reasonable hours upon prior reasonable notice to Pledgor, and any of Pledgor's and its subcontractors' plants and facilities that manufacture, install or store products (or that have done so during the prior six-month period) that are sold under any of the Collateral, and to inspect the products and quality control records relating thereto upon reasonable notice to Pledgor and as often as may be reasonably requested; provided, however, nothing herein shall entitle Secured Party to access to Pledgor's trade secrets and other proprietary information.

6. Further Assurances; Attorney in Fact.

a. On a continuing basis, Pledgor will, subject to any prior licenses, encumbrances and restrictions and prospective licenses, make, execute, acknowledge and deliver, and file and record in the proper filing and recording places in the United States, all such

instruments, including, appropriate financing and continuation statements and collateral agreements and filings with the United States Patent and Trademark Office, and take all such action as may reasonably be deemed necessary or advisable, or as requested by Secured Party to carry out the intent and purposes of this Agreement, or for assuring and confirming to Secured Party the grant or perfection of a security interest in all Patents.

b. Pledgor hereby irrevocably appoints Secured Party as Pledgor's attorney-in-fact, with full authority in the place and stead of Pledgor and in the name of Pledgor, Secured Party or otherwise, from time to time in Secured Party's discretion, to take any action and to execute any instrument which Secured Party may deem necessary or advisable to accomplish the purposes of this Agreement, including:

i. To modify in its sole discretion this Agreement without first obtaining Pledgor's approval of or signature to such modification by amending Exhibit A, Exhibit B and Exhibit C thereof, to include reference to any right title or interest in any copyright, patents, or trademarks acquired by Pledgor after the execution hereof or to delete any reference to any right, title, interest in any copyrights, patents, or trademarks in which Pledgor no longer has or claims any right, title or interest; and,

ii. To file, in its sole discretion, one or more UCC financing or continuation statements and amendments thereto, relative to any of the Collateral without the signature of Pledgor where permitted by law.

7. Events of Default. The occurrence of any of the following shall constitute an Event of Default under this Agreement:

a. An Event of Default occurs under the Guaranty or any other agreement between Pledgor and Secured Party; or

b. Pledgor breaches any warranty or agreement made by Pledgor in this Agreement.

8. Remedies. Upon the occurrence of an Event of Default, Secured Party shall have the right to exercise all the remedies of a secured party under the California Uniform Commercial Code, including without limitation the right to require Pledgor to assemble the Collateral and to make it available to Secured Party at a place designated by Secured Party. Pledgor will pay any expenses (including attorneys' fees) incurred by Secured Party in connection with the exercise of any of Secured Party's rights hereunder, including without limitation any expense incurred in disposing of the Collateral. All of Secured Party's rights and remedies with respect to the Collateral shall be cumulative.

9. Indemnity. Pledgor agrees to defend, indemnify and hold harmless Secured Party and its officers, employees, and agents against: (a.) all obligations, demands, claims, and liabilities claimed or asserted by any other party in connection with the transactions contemplated by this Agreement, and (b.) all losses or expenses in any way suffered, incurred, or paid by Secured Party as a result of or in any way arising out of, following or consequential to transactions between Secured Party and Pledgor, whether under this Agreement or otherwise (including, without limitation, attorneys' fees and expenses), except for losses arising from or out of Secured Party's gross negligence or willful misconduct.

10. Release. At such time as Pledgor shall completely satisfy all of the obligations secured hereunder, Secured Party shall execute and deliver to Pledgor all deeds, releases and other instruments as may be necessary or proper to revest in Pledgor full title to the property granted hereunder, subject to any disposition thereof which may have been made by Secured Party pursuant hereto.



11. **Course of Dealing.** No course of dealing, nor any failure to exercise, nor any delay in exercising any right, power or privilege hereunder shall operate as a waiver thereof.

12. **Attorneys' Fees.** If any action relating to this Agreement is brought by either party hereto against the other party, the prevailing party shall be entitled to recover reasonable attorneys' fees, costs, and disbursements.

13. **Amendments.** This Agreement may be amended only by a written instrument signed by both parties hereto.

14. **Counterparts.** This Agreement may be executed in two or more counterparts, each of which shall be deemed an original but all of which together shall constitute the same instrument.

15. **California Law and Jurisdiction.** This Agreement shall be governed by the laws of the State of California, without regard for choice of law provisions. Pledgor and Secured Party consent to the non-exclusive jurisdiction of any state or federal court located in Santa Clara County, California.

IN WITNESS WHEREOF, the parties hereto have executed this Intellectual Property Security Agreement on the day and year first above written.

Address of Pledgor:

\_\_\_\_\_  
\_\_\_\_\_

PLEDGOR:

\_\_\_\_\_

\_\_\_\_\_  
By: \_\_\_\_\_  
Its: \_\_\_\_\_

Address of Secured Party:

SECURED PARTY:

\_\_\_\_\_  
By: \_\_\_\_\_  
Its: \_\_\_\_\_

**EXHIBIT “A”**

**COPYRIGHTS**

**All present and future registered and unregistered copyrights, including but not limited to the following:**

<b>Description of Copyright</b>	<b>Country of Registration</b>	<b>Registration or Application No.</b>

**EXHIBIT “B”**

**PATENTS**

**All present and future registered and unregistered patents, including but not limited to the following:**

<b>Patent</b>	<b>Registration Number or Serial Number</b>	<b>Date</b>

**EXHIBIT “C”**

**TRADEMARKS**

All present and future registered and unregistered trademarks, including but not limited to the following:

<b>Trademark</b>	<b>Registration Number or Serial Number</b>	<b>Date</b>

**EXHIBIT “D”**

**PERMITTED LIENS**

None

\*\*\*\*\*OR\*\*\*\*\*

<b>Jurisdiction</b>	<b>Filing Number</b>	<b>Filing Date</b>	<b>Secured Party</b>

Intellectual Property UCC



UCC FINANCING STATEMENT

FOLLOW INSTRUCTIONS (front and back) CAREFULLY

Form section for Debtor information including Name & Phone of Contact at Filer, Send Acknowledgment To (Name and Address), and Filed In: California (S.O.S.)



THE ABOVE SPACE IS FOR FILING OFFICE USE ONLY

Main form sections 1, 2, and 3 for Debtor's Exact Full Legal Name, Mailing Address, and Secured Party's Name, including fields for Organization Name, Individual's Last Name, First Name, Middle Name, Suffix, City, State, Postal Code, and Country.

Section 4: This FINANCING STATEMENT covers the following collateral: All general intangibles including but not limited to those reflected on the UCC1 AD attached hereto and made a part hereof, whether now owned or hereafter acquired, whether registered or unregistered, including but not limited to copyrights, patents, and trademarks including all accessions, additions, replacements, substitutions, products and proceeds of the foregoing.

Section 5: ALTERNATIVE DESIGNATION (if applicable) and Section 6: This FINANCING STATEMENT is to be filed (or recorded) in the REAL ESTATE RECORDS. Includes checkboxes for LESSEE/LESSOR, CONSIGNEE/CONSIGNOR, BAILEE/BAILOR, SELLER/BUYER, A.G. LIEN, NON-UCC FILING, and SEARCH REPORT (S) on Debtor(s).

FILING OFFICE COPY — UCC FINANCING STATEMENT (FORM UCC1) (REV. 05/22/02)

**UCC FINANCING STATEMENT ADDENDUM**

**FOLLOW INSTRUCTIONS (front and back) CAREFULLY**

**9. NAME OF FIRST DEBTOR (1a or 1b) ON RELATED FINANCING STATEMENT**

9a. ORGANIZATION'S NAME		
OR	9b. INDIVIDUAL'S LAST NAME	
	FIRST NAME	MIDDLE NAME, SUFFIX

**10. MISCELLANEOUS:**



**THE ABOVE SPACE IS FOR FILING OFFICE USE ONLY**

**11. ADDITIONAL DEBTOR'S EXACT FULL LEGAL NAME - insert only one name (11a or 11b) - do not abbreviate or combine names**

11a. ORGANIZATION'S NAME						
OR	11b. INDIVIDUAL'S LAST NAME		FIRST NAME	MIDDLE NAME	SUFFIX	
11c. MAILING ADDRESS			CITY	STATE	POSTAL CODE	COUNTRY
11d. SEE INSTRUCTIONS	ADD'L INFO RE ORGANIZATION DEBTOR	11e. TYPE OF ORGANIZATION	11f. JURISDICTION OF ORGANIZATION	11g. ORGANIZATIONAL ID #, if any		
<input type="checkbox"/> NONE						

**12. ADDITIONAL SECURED PARTY'S or ASSIGNOR S/P'S NAME - insert only one name (12a or 12b)**

12a. ORGANIZATION'S NAME						
OR	12b. INDIVIDUAL'S LAST NAME		FIRST NAME	MIDDLE NAME	SUFFIX	
12c. MAILING ADDRESS			CITY	STATE	POSTAL CODE	COUNTRY

13. This FINANCING STATEMENT covers  timber to be cut or  as-extracted collateral, or is filed as a  future filing.

14. Description of real estate:

15. Name and address of a RECORD OWNER of above-described real estate (if Debtor does not have a record interest):

**16. Additional collateral description:**

registrations of the same and like protections, and the entire goodwill of the business of Debtor connected with and symbolized by such trademarks, including, without limitation, those set forth in the following SECTION 3 (collectively, the "Trademarks").

(f) Any and all claims for damages by way of past, present and future infringement of any of the rights included above, with the right, but not the obligation, to sue for and collect such damages for said use or infringement of the intellectual property rights identified above;

(g) Any and all present and future licenses or other rights to use any of the Trademarks, Patents or Copyrights, and all license fees and royalties arising from such use to the extent permitted by such license or rights;

(h) Any and all present and future rights in and to domain names in whatever form, and all derivative URLs;

(i) All amendments, extensions, renewals and extensions of any of the Copyrights, Trademarks or Patents; and

(j) Any and all proceeds and products of any of the foregoing, including, without limitation, all payments under insurance or any indemnity or warranty payable in respect of any of the foregoing.

**SECTION 1: COPYRIGHTS**

Any and all present and future registered and unregistered copyrights, including but

17. Check only if applicable and check only one box.

Debtor is a  Trust or  Trustee acting with respect to property held in trust or  Decedent's Estate

18. Check only if applicable and check only one box.

- Debtor is a TRANSMITTING UTILITY
- Filed in connection with a Manufactured-Home Transaction — effective 30 years
- Filed in connection with a Public-Finance Transaction — effective 30 years

**FILING OFFICE COPY — UCC FINANCING STATEMENT ADDENDUM (FORM UCC1Ad) (REV. 05/22/02)**

UCC FINANCING STATEMENT ADDENDUM

FOLLOW INSTRUCTIONS (front and back) CAREFULLY

9. NAME OF FIRST DEBTOR (1a or 1b) ON RELATED FINANCING STATEMENT

9a. ORGANIZATION'S NAME

OR

9b. INDIVIDUAL'S LAST NAME      FIRST NAME      MIDDLE NAME, SUFFIX

10. MISCELLANEOUS:



THE ABOVE SPACE IS FOR FILING OFFICE USE ONLY

11. ADDITIONAL DEBTOR'S EXACT FULL LEGAL NAME - insert only one name (11a or 11b) - do not abbreviate or combine names

11a. ORGANIZATION'S NAME

OR

11b. INDIVIDUAL'S LAST NAME      FIRST NAME      MIDDLE NAME      SUFFIX

11c. MAILING ADDRESS      CITY      STATE      POSTAL CODE      COUNTRY

11d. SEE INSTRUCTIONS      ADD'L INFO RE ORGANIZATION DEBTOR      11e. TYPE OF ORGANIZATION      11f. JURISDICTION OF ORGANIZATION      11g. ORGANIZATIONAL ID #, if any  NONE

12.  ADDITIONAL SECURED PARTY'S or  ASSIGNOR S/P'S NAME - insert only one name (12a or 12b)

12a. ORGANIZATION'S NAME

OR

12b. INDIVIDUAL'S LAST NAME      FIRST NAME      MIDDLE NAME      SUFFIX

12c. MAILING ADDRESS      CITY      STATE      POSTAL CODE      COUNTRY

13. This FINANCING STATEMENT covers  timber to be cut or  as-extracted collateral, or is filed as a  fixture filing.

14. Description of real estate:

16. Additional collateral description: not limited to the following:

[enter table of copyrights here]

SECTION 2: PATENTS  
Any and all present and future registered and unregistered patents, including but not limited to the following:

[enter table of patents here]

SECTION 3: TRADEMARKS  
Any and all present and future registered and unregistered trademarks, including but not limited to the following:

[enter table of trademarks here]

15. Name and address of a RECORD OWNER of above-described real estate (if Debtor does not have a record interest):

17. Check only if applicable and check only one box.  
Debtor is a  Trust or  Trustee acting with respect to property held in trust or  Decedent's Estate

18. Check only if applicable and check only one box.  
 Debtor is a TRANSMITTING UTILITY  
 Filed in connection with a Manufactured-Home Transaction — effective 30 years  
 Filed in connection with a Public-Finance Transaction — effective 30 years

FILING OFFICE COPY — UCC FINANCING STATEMENT ADDENDUM (FORM UCC1Ad) (REV. 05/22/02)

Exhibit 4

Provision limiting recourse against IP to accounts receivable and other proceeds

**Notwithstanding any contrary provision of the definition of the term “Collateral” in Section 2, “Collateral” shall only include any copyrights, patents, trademarks, service marks and applications for any of the foregoing, now owned or hereafter acquired, or any claims for damages by way of any past present and future infringement of any of the foregoing (collectively, the “Intellectual Property”) to the extent necessary to grant Lender a perfected security interest in all Accounts and General Intangibles that consist of rights to payment and proceeds from the sale, licensing or disposition of all or any part, or rights in, the foregoing (collectively, the “Rights to Payment”). Lender agrees that it shall only have recourse against the Intellectual Property to the extent of the Rights to Payment.**

**Lender specifically acknowledges and agrees that, except to the extent necessary to permit Lender to realize on the Rights to Payment, Lender has no right to sell, dispose of or otherwise transfer the Intellectual Property or any interests therein.**



**Exhibit 4**

**Letter to Domain Name Website Host**

**Courtesy of Matt Kavanaugh**

## Exhibit 5

Some terms regarding borrower's licenses to include in a loan and security agreement:

**A. Definitions Section:**

1. "Eligible Inventory" shall not include Inventory that is subject to any license agreement unless Lender shall (a) have been provided with a Temporary License Agreement/Consent in form and substance satisfactory to Lender; or (b) Lender shall have consented in writing.

2. "License Agreement" means that certain License Agreement dated – by and between Borrower and Licensor/Licensee in connection with the license (the "License") of products (the "Licensed Products") more fully described in the License Agreement.

**B. Conditions Precedent Section:**

1. Lender shall have been provided with fully executed copy of the License Agreement.

2. Lender shall have received a fully executed Temporary License Agreement from Licensor in form and substance satisfactory to Lender granting Lender the right to liquidate and sell the Licensed Products upon the occurrence of an Event of Default by Borrower.

**C. Representations and Warranties Section:**

1. Borrower represents and warrants that: (a) all of the conditions precedent to the effectiveness of the License Agreement have occurred; (b) Borrower is in compliance with all of the terms of the License Agreement; Borrower has not received any notice of default under its License Agreement; and (c) is and at all times shall be in compliance with the terms and conditions of the License Agreement

2. Borrower has not entered into and is not subject to any agreement regarding the right to license any products other than the License Agreement.

**D. Affirmative Covenants Section:**

1. Borrower shall comply with all of the terms of the License Agreement.

2. Borrower shall advise Lender thirty (30) days prior to entering into any additional license agreement, and shall provide Lender with a fully executed temporary license agreement in form and substance satisfactory to Lender prior to entering into such license agreement.

**3. Borrower shall advise Lender promptly on receipt should it receive any notice of default or termination under the License Agreement.**

**E. Default Section:**

**1. It shall be an Event of Default under this Agreement and the Loan Documents if Borrower defaults under the License Agreement unless such default shall be cured within any cure period given by Licensor/Licensee to Borrower.**

Exhibit 7

CONSENT OF LICENSOR

Note:

1. Royalty was required to be paid.
2. No other document related to the trademark license agreement was signed due to extreme reluctance on borrower and licensor's part.

This Consent of Licensor (this "Agreement") is dated this \_\_\_\_ day of by and between \_\_\_\_\_, a \_\_\_\_\_ ("Licensor") on the one hand, and \_\_\_\_\_, a \_\_\_\_\_ ("Lender"), on the other hand, at San Jose, California.

RECITALS

A. Licensor and \_\_\_\_\_ ("Borrower") have entered into that certain License Agreement dated \_\_\_\_\_ (the "Trademark License Agreement"), a copy of which is attached hereto as Exhibit A and incorporated herein by this reference. The Trademark License Agreement grants Borrower a license to use those trademarks reflected in the Trademark License Agreement (collectively, the "Trademarks") as set forth more completely in the Trademark License Agreement.

B. Lender has been asked to make a line of credit available to Borrower pursuant to certain loan documents, including but not limited to a Loan and Security Agreement (as such documents may be amended from time to time collectively, the "Loan Documents").

C. If, after the occurrence of an event of default by Borrower under the Loan Documents, Lender is required in the future in its role as Lender to sell the inventory of Borrower, Lender would need the agreement of Licensor to use the Trademarks as necessary to sell such inventory, in which case Lender would pay to Licensor any royalty associated with such sale.

D. In order to permit Borrower to obtain the line of credit from Lender, Licensor is willing to agree to Lender's request.

AGREEMENT

In consideration of the foregoing, the parties agree as follows:

1. Licensor agrees that Lender in the future acting as lender, may use the Trademarks only to the extent necessary for Lender to sell the inventory of Borrower after the occurrence of an Event of Default by Borrower under the Agreement and collect the sales proceeds, and Licensor consents to the use of the Trademarks for this use only, and Lender agrees to pay any applicable royalty to Licensor as provided in the Trademark License Agreement.

2. Any notice required or permitted to be given under this Agreement shall be by written communications by way of telex or air letter, registered and postage prepaid, or by confirmed facsimile message or personal delivery, and shall be directed by one party to

**the other at its respective address as follows unless otherwise provided for in this Agreement:**

**If to Licensor:**

**Name**  
**Address**  
**Attention:**  
**Phone:**  
**Fax:**

**If to Lender:**

**Name**  
**Address**  
**Attention:**  
**Phone:**  
**Fax:**

**Either party may change its address to which notices or requests shall be directed by written notice to the other party, but until such change of address has been received, any notice or request sent to the above addresses shall be effective upon mailing and shall be considered as having been received.**

3. This Agreement may not be modified in any manner except by an instrument in writing signed by the parties. The construction and performance of this Agreement will be governed by the internal, substantive laws of the State of California without regard to its choice of law rules. This Agreement may be executed in any number of counterparts, all of which, taken together, shall constitute a single original.

IN WITNESS WHEREOF, each of the parties has caused this Consent of Licenser to be executed by its duly authorized representatives on the respective dates entered below.

Lender:

Licenser:

By: \_\_\_\_\_

By: \_\_\_\_\_

Name: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_

Title: \_\_\_\_\_

**EXHIBIT 8**

**Pledge of License Agreement**

**PLEDGE OF LICENSE AGREEMENT FOR COLLATERAL PURPOSES ONLY**

**Note:**

**Use with Consent that is Exhibit 9**

**This Pledge of License Agreement for Collateral Purposes Only (this “Pledge”) is made on \_\_\_\_\_ between \_\_\_\_\_, a \_\_\_\_\_, with an address of \_\_\_\_\_ (“Licensee”), and \_\_\_\_\_, a \_\_\_\_\_, with an address of \_\_\_\_\_ (“Secured Party”) at \_\_\_\_\_.”**

**RECITALS**

**A. \_\_\_\_\_, a \_\_\_\_\_ (“Licensor”) and Licensee are parties to a License Agreement dated effective as of \_\_\_\_\_ (the “License Agreement”), a copy of which is attached hereto as Exhibit “A” and is incorporated herein by this reference.**

**B. Licensee has requested financing from Secured Party pursuant to a Loan and Security Agreement (Accounts & Inventory) dated \_\_\_\_\_ (as modified, the “Loan Agreement”) and related loan documents (as modified, and together with the Loan Agreement, collectively, the “Loan Documents”). Included in the Loan Documents is an Intellectual Property Security Agreement dated \_\_\_\_\_ (as modified, the “IP Security Agreement”).**

**C. Secured Party is willing to provide such financing to Licensee, provided that Licensee has granted Secured Party a security interest in all of Licensee’s personal property, including certain rights under the License Agreement, which Lender agrees it will only enforce to the extent necessary, in the event of a default by Licensee under the Loan Documents to take the following actions: (i) dispose, pursuant to the Commercial Code, Licensee’s (a) inventory that is subject to the License Agreement; and (b) accounts receivable and other proceeds of sale of such inventory.**

**D. Section \_\_\_\_\_ of the License Agreement prohibits any assignment of the License Agreement without the consent of the parties. To the extent that such prohibition on assignment may be deemed to prohibit the execution of this Pledge by Licensee, Secured Party will require, as a condition to funding the loan under the Loan Documents, that Licensor sign a Consent Agreement to (i) acknowledge that this Pledge does not cause Licensee to be in violation of the License Agreement; and (ii) consent to the execution of this Pledge Agreement by Licensee.**

## AGREEMENT

For good and valuable consideration, receipt of which is hereby acknowledged, Licensee and Secured Party agree as follows:

1. The foregoing Recitals and the documents referred to therein are incorporated herein by this reference.
2. Licensee hereby pledges for collateral purposes only and grants a security interest in and to the License Agreement by Licensee to Secured Party, which Secured Party agrees it will enforce only to the extent set forth in Recital C.
3. Until such time as Secured Party has been paid in full under the Loan Documents, Licensee will comply with all terms of the License Agreement, with failure to comply with such terms to constitute an Event of Default under the Loan Documents.
4. Licensee will notify Secured Party of any notices of default or other notices it may receive from Licensor under the License Agreement and of any amendments to the License Agreement.
5. Nothing in this Pledge shall be deemed to be an outright assignment for purposes of ownership of Licensee's rights in and obligations under the License Agreement, and Secured Party shall be entitled to exercise those rights under this Pledge as are set forth in the Consent Agreement dated \_\_\_\_\_ by and among Licensee, Licensor, and \_\_\_\_\_ (the "Consent Agreement"), and shall have no obligations under the License Agreement to perform any obligations under the License Agreement or otherwise except as set forth in the Consent Agreement.
6. This Pledge shall be governed by California law without regard to conflict of law principles.
7. This Pledge may be executed in two or more counterparts, each of which shall be deemed to be an original, and all of which shall constitute one instrument.
8. This Pledge, taken together with the terms and conditions of the IP Property Security Agreement and all of the other Loan Documents, shall constitute the final expression of the parties with respect to the subject matter hereof. Any amendment hereto shall be signed by all of the parties hereto.



**IN WITNESS WHEREOF, the parties have signed this Pledge of License Agreement for Collateral Purposes Only as of the date first written above.**

\_\_\_\_\_

**By:** \_\_\_\_\_

**Title:** \_\_\_\_\_

\_\_\_\_\_

**By:** \_\_\_\_\_

**Title:**

Exhibit 9

CONSENT AGREEMENT RE: PLEDGE OF LICENSE

Note:

1. This Consent Agreement was used with the Pledge of License that is Exhibit 8
2. No royalty was required to be paid by Secured Party here if it exercised its right to liquidate trademarked goods. But this loan involved an affiliated licensor and licensee, so the licensor was very accommodating.

This Consent Agreement (this "Consent") is made as of \_\_\_\_\_, by and among \_\_\_\_\_ ("Licensor"), a California corporation, with an address of \_\_\_\_\_, \_\_\_\_\_ ("Licensee"), a California corporation, with an address of \_\_\_\_\_ and \_\_\_\_\_ ("Secured Party"), a California corporation, with an address of \_\_\_\_\_. This Consent was entered into in the City of \_\_\_\_\_, State of \_\_\_\_\_.

RECITALS

- A. Licensor and Licensee are parties to a License Agreement dated \_\_\_\_\_ (the "License Agreement").
- B. Licensee has requested financing from Secured Party pursuant to a Loan and Security Agreement (Accounts & Inventory) dated June 19, 2008 (as modified, the "Loan Agreement") and related loan documents (as modified, and together with the Loan Agreement, collectively, the "Loan Documents").
- C. Secured Party is willing to provide such financing to Licensee, provided that Licensee has granted Secured Party a security interest in all of Licensee's personal property, including certain rights under the License Agreement, which Lender agrees it will only enforce to the extent necessary, in the event of a default by Licensee under the Loan Documents to take the following actions: (i) dispose, pursuant to the Commercial Code, Licensee's (a) inventory that is subject to the License Agreement; and (b) accounts receivable and other proceeds of sale of such inventory ("Permitted Actions").
- D. Licensee has executed or will execute that certain Pledge of License Agreement for Collateral Purposes Only in the form attached hereto as Exhibit 1, which is incorporated herein by this reference with respect to the License Agreement (as modified, the "Pledge").
- E. Section \_\_\_\_\_ of the License Agreement prohibits any assignment of the License Agreement without the consent of the parties. To the extent that such prohibition on assignment may be deemed to prohibit the execution of this Pledge by Licensee, Secured Party will require, as a condition to funding the loan under the Loan Documents, that Licensor sign a Consent Agreement to (i) acknowledge that this Pledge does not cause Licensee to be in violation of the License Agreement; and (ii) consent to the execution of this Pledge Agreement by Licensee.

## AGREEMENT

For good and valuable consideration, the receipt of which is hereby acknowledged, the parties agree as set forth below.

1. The foregoing Recitals and the documents referred to therein are incorporated herein by this reference as though set forth in full herein.
2. Licensors consents to the execution of the Pledge by Licensee to Secured Party, which Secured Party will only enforce to the extent they constitute Permitted Actions.
3. Subject to the limitations of the Secured Party as set forth in the Pledge, Licensors consents to the disposition by Secured Party under the Uniform Commercial Code of Licensee's inventory that is subject to the License Agreement and any accounts receivable or other proceeds of the sale of such inventory upon the occurrence of an Event of Default under any of the Loan Documents.
4. Nothing in this Consent or the Pledge shall be deemed to be an outright assignment for purposes of ownership of Licensee's rights in and obligations under the License Agreement and Secured Party shall be entitled to exercise its rights under the Pledge without having any obligations under the License Agreement, whether to pay any monies to Licensors, perform any obligations under the License Agreement or otherwise, except as provided in this Consent or the Pledge.
5. This Consent shall be governed by California law without regard to conflict of law principles.
6. This Pledge may be executed in two or more counterparts, each of which shall be deemed to be an original, and all of which taken together shall constitute one instrument.
7. This Consent shall constitute the final expression of the parties with respect to the subject matter hereof. Any amendment hereto shall be signed by all of the parties hereto.

**IN WITNESS WHEREOF, the parties have signed this Consent Agreement as of the first date above written.**

**Licensor**

**By:** \_\_\_\_\_

**Print Name:** \_\_\_\_\_

**Print Title:** \_\_\_\_\_

**Licensee**

**By:** \_\_\_\_\_

**Print Name:** \_\_\_\_\_

**Print Title:** \_\_\_\_\_

**Secured Party**

**By:** \_\_\_\_\_

**Print Name:** \_\_\_\_\_

**Print Title:** \_\_\_\_\_

**Exhibit 10**

**FORBEARANCE AGREEMENT**

This Forbearance Agreement (this "Agreement") is entered into by and between \_\_\_\_\_ ("Borrower"), \_\_\_\_\_ ("Guarantor") and \_\_\_\_\_ ("Lender") as of this \_\_\_\_ day of \_\_\_\_\_ 2008, at \_\_\_\_\_, California.

**RECITALS**

A. Lender and Borrower have previously entered into a Loan and Security Agreement (the "Loan Agreement") dated \_\_\_\_\_, \_\_\_\_, \_\_\_\_ and documents executed in connection therewith (the "Loan Documents"). (The amount outstanding under the Loan Agreement is hereinafter sometimes referred to as the "Line of Credit".)

B. Lender has been advised by Borrower that Borrower failed to pay certain obligations that it owes to its landlord for the premises located at \_\_\_\_\_ due to a serious deterioration in the cash flow of Borrower.

C. In light of the persistent cash flow difficulties of Borrower, Lender has permitted Borrower to maintain overadvances under the Loan Agreement (collectively, the "Overadvance"). Borrower has been unable to cure the Overadvance by generating additional acceptable accounts receivable or working capital.

D. Additionally, Borrower has not provided Lender with a current listing of Borrower's patents, trademarks, copyrights and domain names (the "IP") as required under the Loan Agreement.

E. The foregoing are all violations of the Loan Agreement and the Loan Documents (the "Existing Defaults").

F. Borrower, has requested that notwithstanding the Existing Defaults, Lender forbear from exercising its rights and remedies under the Agreement, and Lender has so agreed, subject to the terms and conditions of this Agreement, as set forth in greater detail below and the documents to be executed concurrently herewith.

**AGREEMENT**

For good and valuable consideration, the parties agree as set forth below:

1. **Incorporation by Reference.** The Recitals and Agreement and the documents executed in connection therewith and thereafter, as modified hereby, are incorporated herein by this reference.

2. **Effective Date.** The terms of this Agreement (the "Forbearance Terms") shall be in full force and effect as of \_\_\_\_\_, \_\_\_\_, \_\_\_\_ and shall continue until the last day for compliance set forth in this Agreement.

3. **Terms of Forbearance.** The terms on which Lender is willing to forbear are as follows:

3.1 Borrower shall obtain a capital infusion in a minimum amount of \_\_\_\_\_ and \_\_\_/100 Dollars (\$\_\_\_\_,\_\_\_\_,00) within thirty (30) days.

3.2. Such infusion of capital shall be paid directly to Lender to reduce the Overadvance;

3.2 \_\_\_\_\_ shall have signed a General Continuing Guaranty (the "Guaranty") in favor of BFI in form and content satisfactory to Lender, which Guaranty shall be secured by that certain Deed of Trust and Assignment of Rents encumbering that certain real property commonly known as \_\_\_\_\_;

3.3 Borrower shall have provided Lender with a complete and current listing of all of Borrower's IP.

3.4 Borrower shall have provided Lender with a fully executed Amended and Restated Intellectual Property Security Agreement with respect to its IP.

4. **Attorneys' Fees.** At the time of execution of the Agreement, Borrower agrees to pay all of the attorney's fees and costs incurred by Lender in connection with the negotiation and preparation of this Agreement and the documents executed herewith.

5. **Release.** Borrower and Guarantor individually and on behalf of its successors, assigns, and present and future stockholders, officers, directors, employees, agents and attorneys, hereby remises, releases and forever discharges Lender and Lender's present and former officers, directors, stockholders, employees, agents, attorneys, successors and assigns from any and all claims, rights, actions, causes of action, suits, liabilities, defenses, damages and costs that (a) exist or may exist as of the date hereof; and (b) arise from or are otherwise related to the Loan Agreement or the other Loan Documents, and any transaction contemplated thereby, the administration of the Loans and other financial accommodations made thereunder, the collateral security given in connection therewith, or any related discussions or negotiations, in each case whether known or unknown, suspected or unsuspected. Borrower waives any and all claims, rights and benefits it may have under any law of any jurisdiction that would render ineffective a release made by a creditor of claims that the creditor does not know or suspect to exist in its favor at the time of executing the release and that, if known by either, would have materially affected its settlement with the applicable debtor. Borrower and Guarantor acknowledges that it is aware of the following provisions of Section 1542 of the California Civil Code:

A general release does not extend to claims which the creditor does not know or suspect to exist in his favor at the time of executing the release, which if known by him must have materially affected his settlement with the debtor.

6. **Waivers.** Borrower expressly and voluntarily waives each and all claims, rights, or benefits it has or may have under Section 1542 of the California Civil Code, or any other similar law of any other jurisdiction, to the full extent that it may lawfully waive such claims, rights and benefits in connection with this release. Borrower acknowledges that (i) if Borrower so desires, it has been represented by independent legal counsel of its own choice throughout all of the negotiations that preceded the execution of this Letter Agreement and that it has executed this Letter Agreement after receiving the advice of such independent legal counsel if sought; and (ii) it and its respective counsel, if counsel was sought, have had an adequate opportunity to make whatever investigation or inquiry they deemed necessary or desirable in connection with the release contained in this Letter Agreement.

7. **Remedies.** In the event that the Existing Defaults are not cured by the dates set forth in this Agreement, Lender shall be entitled to exercise all rights and remedies under the Loan Agreement, the Loan Documents and applicable law, including but not limited to exercising its right to take possession of and sell the collateral securing the obligations of Borrower under the Loan

Agreement. Borrower and Guarantor acknowledge and agree that they will cooperate with providing peaceful possession to Lender of the assets of Borrower so that Borrower might exercise its rights and remedies with respect to such collateral.

8. Execution by Guarantor. It shall be a condition precedent to the effectiveness of this Agreement that Guarantor shall have signed as guarantor to indicate his acknowledgement of and agreement to the terms and conditions of this Agreement.

9. Counterparts. This Agreement and the documents to be executed in connection herewith may be executed in any number of counterparts, each of which shall be deemed an original but all of which taken together shall constitute a single original. Delivery of an executed counterpart of the signature page to this Agreement by telefacsimile shall be effective as delivery of a manually executed counterpart of this Agreement, and any party delivering such an executed counterpart of the signature page to this Agreement by telefacsimile to any other party shall thereafter also promptly deliver a manually executed counterpart of this Agreement to such other party, provided that the failure to deliver such manually executed counterpart shall not affect the validity, enforceability, or binding effect of this Agreement.

10. Successors and Assigns. This Agreement and the documents to be executed concurrently herewith shall be binding on and shall inure to the benefit of the successors and assigns of the parties to this Agreement.

11. Governing Law. This Agreement shall be governed by California law.

12. Legal Effect. Except as specifically set forth in this Agreement, all of the terms and conditions of the Loan Agreement and the Loan Documents remain in full force and effect.

13. Integration. This is an integrated Agreement and, together with the \_\_\_\_\_ Loan Documents as modified by this Agreement and the documents to be executed in connection herewith supersedes all prior negotiations and agreements regarding the subject matter hereof. All amendments hereto and thereto must be in writing and signed by the parties.

IN WITNESS WHEREOF, the parties have executed this Forbearance Agreement as of the date first set forth above.

Lender

Borrower

\_\_\_\_\_  
By: Name  
Its: Title

\_\_\_\_\_  
By: Name  
Its: Title

Guarantor

\_\_\_\_\_  
Name, Individually

**Exhibit 11**

**AGREEMENT FOR ACCEPTANCE OF COLLATERAL IN FULL  
SATISFACTION OF DEBT**

**Note:**

- 1. This Agreement was used where Lender had been collecting A/R and selling other tangible assets and then later decided to surrender the remainder of the collateral**

**This Agreement for Acceptance of Collateral in Full Satisfaction of Debt (this “Agreement”) is made by and between \_\_\_\_\_ (“Lender”), a California corporation and \_\_\_\_\_ (“Borrower”), as of \_\_\_\_\_.**

**RECITALS**

**A. Borrower acknowledges that as of \_\_\_\_\_, it is currently indebted to \_\_ in the sum of (a) \_\_\_\_\_ and \_\_/100 Dollars (\$ \_\_\_\_\_) under that certain Loan & Security Agreement (Accounts Receivable and Inventory Line of Credit) dated \_\_\_\_\_ heretofore executed and now existing between Lender and Borrower, together with attorneys’ fees and legal and other costs and expenses (as such amount may change from time to time, the “Loan Balance”). (The foregoing documents, together with other written agreements and UCC-1 Financing Statements, are sometimes hereinafter collectively referred to as the “Loan Documents”.)**

**B. Borrower further acknowledges that Lender has a perfected security interest in all of the property described in the Loan Documents, including, without limitation, all of Borrower’s inventory, new and used, presently owned and hereafter acquired, together with all proceeds of the sale or other disposition thereof, and all equipment, present and future, used or intended for use in conjunction therewith, and all accounts, furniture, fixtures, contract rights, accounts receivable, chattel paper, general intangibles presently existing and hereafter arising, wherever located, together with all proceeds of the sale or other disposition thereof (collectively, the “Collateral”).**

**C. Borrower further acknowledges that it is in default under the terms of the Loan Documents, that said indebtedness is now wholly due and owing, and that Borrower cannot presently satisfy said indebtedness and will not be able to satisfy the indebtedness.**

**D. Borrower finds itself in a position of being unable to continue the operation of its business.**



**E. Borrower has previously sold all of its inventory and equipment to third parties, with the proceeds thereof having been paid to the secured creditors of Borrower as their respective interests appeared.**

**F. Borrower has previously requested that Lender exercise its rights as a creditor in Borrower's accounts receivable for collection purposes.**

**G. The items of Collateral that Borrower retains ownership of are described in Exhibit A hereto (collectively, the "Remaining Collateral").**

**H. Borrower has concluded that the realizable value of the items of the Remaining Collateral is less than the amount of liens and secured claims encumbering them, which liens are held by Lender and XYZ Corporation ("XYZ"), and that as a result, the continued cost of retaining and recovering such value is not warranted and surrender of the possession of and transfer and assignment of all right, title and interest to LENDER of that Borrower has in and to the Remaining Collateral is appropriate.**

**I. Lender has given notice to all secured creditors of record pursuant to Commercial Code Section 9620.**

**J. Lender wishes to take possession of and accept the transfer and assignment of all of Borrower' right, title and interest in and to the items of Remaining Collateral and to accept the Remaining Collateral in full satisfaction of the obligations owed to Lender, pursuant to the provisions of California Commercial Code Section 9620.**

### **AGREEMENT**

**For good and valuable consideration, receipt of which is hereby acknowledged, the parties agree as set forth below.**

**1. Voluntary Surrender, Transfer and Assignment. Concurrently with the execution of this Agreement, Borrower shall voluntarily and unconditionally surrenders possession of and requests that Lender take possession of the Remaining Collateral to the extent that possession thereof was not already surrendered to Lender. Borrower further requests that Lender exercise its remedies in the Remaining Collateral as provided in the Loan Documents and in accordance with the California Commercial Code as it deems appropriate. Borrower further transfers and assigns all right, title and interest in and to the Remaining Collateral to Lender and acknowledges and agrees that Borrower shall have no right to, claim upon or interest in the Remaining Collateral or any right to demand, assert control over, make a claim upon or otherwise attempt to assert an interest in the Remaining Collateral.**

**2. Disclaimer. Lender acknowledges and agrees that it is acquiring the Remaining Collateral in its present condition, "as is, where is and with all faults"; that Borrower has made no representations or warranty, express or implied or**

arising by operation of law, regarding the Remaining Collateral; and that Lender shall have no recourse whatsoever against Borrower in connection with the assignment of the Remaining Collateral and all risks of loss with respect thereto shall be borne by Lender.

3. **Election to Retain Surrendered Assets in Satisfaction of Debt.** Lender and Borrower agree that pursuant to California Commercial Code Section 9620, the acceptance of the Remaining Collateral pursuant to the terms of this Agreement constitute an election by Lender to retain the Remaining Collateral in full satisfaction of all obligations owed to Borrower by Lender.

4. **Waiver of Right by Borrower.** Borrower hereby waives any right to notice under Commercial Code Section 9620 or opportunity to object to acceptance of the Collateral by Lender in satisfaction of the obligations to Lender. Borrower further waives any right under Section 9601 et seq. of the California Commercial Code to require a public sale or private sale of the Remaining Collateral, or any portion thereof or any right to notice of such sale. Borrower hereby agrees that Lender and/or its designees, assignees and/or successors-in-interest may sell, use or make other any other disposition of the Collateral, or any portion thereof, that they desire. Notwithstanding the foregoing, Borrower acknowledges and agrees that this Agreement shall constitute notice of private sale under Section 9611 of the Commercial Code to the extent any such notice might be required and that Lender may conduct such private sale at anytime hereafter if it so chooses.

5. **Entire Agreement.** This Agreement constitutes the entire agreement between the parties pertaining to the subject matter contained in it and supersedes all prior and contemporaneous agreements, representations, and understandings of the parties regarding foreclosure upon or disposition of the Remaining Collateral. This Agreement does not, however, supersede or modify the Loan Agreement or any of the Other Loan Documents.

6. **Counterparts.** This Agreement may be executed in one or more counterparts or by facsimile transmission, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

7. **Binding Effect.** This Agreement shall be binding on and inure to the benefit of, the parties, their respective affiliates, representatives, agents, officers, directors, shareholders, and successors and assigns.

8. **Applicable Law.** This Agreement and the rights and obligations of the parties shall be construed, interpreted and enforced pursuant to the laws of the State of California, but without regard to those provisions in the law which construe ambiguities against the drafter and conflicts of laws, rules and principles.

9. **Further Assurances.** Borrower agrees to perform any further acts and execute and deliver any documents that may be reasonably necessary to carry out the terms of this Agreement surrender of the Remaining Collateral.

**IN WITNESS WHEREOF, the parties have executed this Agreement for Acceptance of Collateral in Full Satisfaction of Debt as of the date first above written.**

**Debtor**

**By: \_\_\_\_\_**

**Its: \_\_\_\_\_**

**By: \_\_\_\_\_**

**Its: \_\_\_\_\_**

**The foregoing is hereby agreed:**

**Lender**

**By: \_\_\_\_\_**

**Title: \_\_\_\_\_**

**Exhibit A**

**REMAINING COLLATERAL**

- 1. All remaining accounts receivable**
- 2. All remaining sales documentation supporting all remaining accounts receivable, all files, all other documents and all software necessary to collect the remaining accounts receivable and all related hardware;**
- 3. All remaining refunds, including without limitation, all insurance refunds;**
- 4. All remaining deposits, including without limitation, all utility deposits;**
- 5. All general intangibles; and**
- 6. All proceeds and products of all of the foregoing.**

**CONSENT OF XYZ Corporation**

**XYZ Corporation (“XYZ”) hereby represents that as of \_\_\_\_\_, it is owed approximately \_\_\_\_\_ and \_\_\_/100 Dollars (\$\_\_\_\_\_) in principal, plus interest and charges by Borrower, and that it has a duly perfected security interest in all of the personal property of Borrower. XYZ hereby consents to the terms of the foregoing Agreement for Acceptance of Collateral in Full Satisfaction of Debt (the Agreement”). XYZ further waives its right to receive written notice pursuant to and its right to object under Commercial Code Section 9620. XYZ further waives its right to receive written notice of disposition of collateral pursuant to Commercial Code section 9611. XYZ’s consent to the foregoing is conditioned upon the terms of the Agreement, including without limitation, Lender’s agreement to pay the Excess Proceeds, as defined in the Agreement, to XYZ.**

**XYZ Corporation**

**By: \_\_\_\_\_**

**Title: \_\_\_\_\_**

Exhibit 12

**ACKNOWLEDGMENT OF DEFAULT AND  
SURRENDER OF POSSESSION**

**Note:**

- 1. This version does not have a waiver of notice by Borrower and Guarantors because was not negotiated.**
- 2. This document states that turnover is effective upon demand by Lender.**

**TO:** Secured Lender's Name ("Lender")

**OF:** Secured Lender's Address

**FROM:** Debtor's Name

**OF:** Debtor's Address ("Debtor")

**DATE:** (Date Executed)

**1. Debtor acknowledges that as of the date set forth above it is indebted to Lender in the sum of \_\_\_\_\_ and \_\_\_/100 Dollars (\$\_\_\_\_\_) plus interest accruing thereon and attorneys' fees and costs, which indebtedness arose under and pursuant to those certain agreements and other written instruments heretofore executed and now existing between Lender and Debtor, including but not limited to certain Loan and Security Agreement dated and UCC-1 Financing Statements dated \_\_\_\_\_ (together with any other loan agreements, collectively, the "Agreements").**

**2. Debtor further acknowledges that it is in default under the terms of the Agreements, that said indebtedness is now wholly due and owing, and that Debtor cannot presently satisfy said indebtedness.**

**3. Debtor further acknowledges that Lender has a perfected security interest in all of the property described in the Agreements, including, without limitation, all of Debtor's present and future interest in any of the following: (a) accounts receivable ; (b) inventory, (c) equipment, including without limitation, all motor vehicles, furnishings, furniture, fixtures of the Debtor; (d) all general intangibles; and (e) all proceeds and products of the disposition thereof and insurance for all of the foregoing (collectively, the "Collateral").**

**4. Debtor finds itself in a position of being unable to continue the operation of its business at the address described above or at all.**

**5. Effective as of demand by Lender, Debtor will unconditionally surrender possession of all the Collateral and request that Lender take possession of**

all of the Collateral. Debtor will further request that Lender exercise its remedies as provided in the Agreements and in accordance with the California Uniform Commercial Code.

6. Debtor agrees to cooperate with Debtor in the possession and liquidation of the Collateral and to take such other steps as are necessary to effectuate the purpose of this Agreement.

7. By this Acknowledgment of Default and Surrender of Possession, Lender does not waive any of its rights as against any party, including without limitation, those rights and remedies set forth in the Agreements.

Debtor

By: \_\_\_\_\_  
Its: \_\_\_\_\_

By: \_\_\_\_\_  
Its: \_\_\_\_\_

**Acknowledgment and Agreement by Guarantor**

The foregoing is hereby acknowledged and agreed, and Guarantor hereby acknowledges and agrees that the Guaranty dated \_\_\_\_\_ and all collateral pledged to secure such Guaranty remains in full force and effect:

\_\_\_\_\_  
\_\_\_\_\_, Guarantor

Accepted Effective Upon Demand:

Lender

By: \_\_\_\_\_

Its: \_\_\_\_\_

t

**Exhibit 13-A**

**Date**

**NOTICE OF DISPOSITION OF COLLATERAL  
PRIVATE SALE**

**To:** See attached list of Addressees  
Sent via Overnight Delivery and US Mail

**From:**

**Name of Debtor:** (“Debtor”)

**Names of Guarantors:**

**We will sell (or license, as applicable) the property described below privately sometime on or after \_\_\_\_\_. Upon such sale, you will no longer have any right to the property sold and the proceeds from such sale will be used to reduce the obligations owed to Lender until such obligations have been satisfied in full.**

**You may request information an accounting by calling \_\_\_\_\_ at (\_\_\_\_).**

**Description of Property:**

**All accounts receivable, general intangibles, equipment, and inventory still in existence and located or formerly located at any of the addresses of Debtor listed below (the “Premises”).**

**Names & Addressees of Parties Receiving Notice Via Overnight Mail and US Mail:**

**Debtor:**

1. \_\_\_\_\_ (“Debtor”)  
Address  
City, State, Zip

**Guarantors:**

1. \_\_\_\_\_  
Address  
City, State, Zip



**Secured Creditors/Lienholders/:**

- 1. \_\_\_\_\_  
Address  
City, State, Zip

**Possible Interested Buyers**

- 1. \_\_\_\_\_  
Address  
City, State, Zip

**Exhibit 13-B  
Notice of Disposition of Collateral (Public Sale)**

**October \_\_, 2008**

**NOTICE OF DISPOSITION OF COLLATERAL  
PUBLIC SALE**

**To:** See attached list of Addressees  
Sent via Overnight Delivery and US Mail

**From:**

**Name of Debtor:** (“Debtor”)

**Names of Guarantors:**

**We will sell (or license, as applicable), to the highest qualified bidder in public, the property described below publicly on;**

\_\_\_\_\_ (Date); at

\_\_\_\_\_ (Time); the following location(s):

\_\_\_\_\_

**Upon such sale, you will no longer have any right to the property sold and the proceeds from such sale will be used to reduce the obligations owed to \_\_\_\_\_ until such obligations have been satisfied in full.**

**You may request information an accounting by calling \_\_\_\_\_ at (\_\_\_\_).**

**Description of Property:**

**All accounts receivable, general intangibles, equipment, and inventory still in existence and located or formerly located at any of the addresses of Debtor listed below (the “Premises”).**

**Names & Addressees of Parties Receiving Notice Via Overnight Mail and US Mail:**

**Debtor:**

1. \_\_\_\_\_ (“Debtor”) at:

**Address**  
**City, State, Zip**

**Guarantors:**

1. \_\_\_\_\_  
**Address**  
**City, State, Zip**

**Secured Creditors/Lienholders:**

2. \_\_\_\_\_  
**Address**  
**City, State, Zip**

**Potential Interested Buyers**

2. \_\_\_\_\_  
**Address**  
**City, State, Zip**

**Exhibit 14**

**BILL OF SALE  
(EQUIPMENT, INVENTORY, CUSTOMER LIST, TRADEMARKS AND OTHER  
GENERAL INTANGIBLES)**

This Bill of Sale (Equipment, Inventory, Customer List, Patents and other General Intangibles) (this "Bill of Sale") is entered into as of \_\_\_\_\_, by and between \_\_\_\_\_, a \_\_\_\_\_, with its headquarters address at \_\_\_\_\_ ("Seller") and \_\_\_\_\_ a \_\_\_\_\_, with an address at \_\_\_\_\_ ("Buyer").

**RECITALS**

A. Seller has foreclosed by private foreclosure on its security interest in certain assets of \_\_\_\_\_ ("Borrower") consisting of all equipment, inventory, customer lists, patents and other general intangibles previously owned by Borrower and still existing and all available books and records (the "Assets").

B. Buyer wishes to purchase all of Seller's right, title, and interest in and to the Assets and Seller wishes to sell the Assets pursuant to the terms of this Bill of Sale.

**AGREEMENT**

Therefore, in consideration of the foregoing and the conditions set forth herein below, Buyer and Seller agree as follows:

1. The foregoing Recitals are incorporated herein by this reference.
2. Subject to the execution of this Bill of Sale and receipt of the Purchase Price by Seller from Buyer, as defined in Paragraph 3, Seller hereby sells, assigns and transfers to Buyer all of Seller's right, title and interest in and to the Assets.
3. In consideration of the aforementioned sale by Seller to Buyer, Buyer shall pay to Seller the sum of \_\_\_\_\_ and 00/100 Dollars (\$\_\_\_\_\_) (the "Purchase Price"). The Purchase Price shall be paid by \_\_\_\_\_.
4. **THIS SALE IS MADE "AS IS," "WHERE IS," "IF IS" WITH NO WARRANTIES OR REPRESENTATIONS OF ANY KIND BY SELLER TO BUYER. SELLER MAKES, AND HAS MADE, NO WARRANTIES, EXPRESS OR IMPLIED, TO BUYER AND BUYER HEREBY EXPRESSLY WAIVES THE IMPLIED WARRANTIES OR MERCHANTABILITY AND FITNESS FOR USE, IF ANY, AND ALL OTHER WARRANTIES EXPRESS OR IMPLIED. BUYER ACKNOWLEDGES THAT BUYER IS NOT RELYING UPON ANY REPRESENTATIONS OF SELLER AND THAT BUYER HAS UNDERTAKEN**

**BUYER'S OWN DUE DILIGENCE REGARDING THE QUALITY, CONDITION AND VALUE, IF ANY, OF THE ASSETS AND THE INTEREST BEING SOLD HEREIN.**

5. Buyer acknowledges that Buyer will bear all costs associated with the purchase of the Assets.

6. Buyer acknowledges that the risk of loss on the Assets has been transferred to Buyer. Buyer assumes responsibility for any personal or other injury that may be caused to Buyer, Buyer's agent or employees or others in the removal of the Assets.

7. The parties acknowledge that this is an isolated sale under California state laws and Seller has not collected any sales tax. To the extent any sales tax may be due, Buyer will pay for same.

8. Concurrently with the execution hereof Seller has delivered to Lender for recordation in the United States Patent and Trademark Office ("PTO") an Assignment of Patent in the form attached hereto as Exhibit "A".

9. This is an integrated Bill of Sale. Taken together with the Assignment of Patent to be filed in the PTO, it supersedes all prior representations and agreements regarding the subject matter hereof, if any, between the parties to this Bill of Sale. This Bill of Sale when executed and the Assignment of Patent contain the entire and only understanding between the parties regarding the subject matter hereof, and may not be altered, amended or extinguished, except by a writing that expressly refers to this Bill of Sale and is signed by the parties subsequent to the execution of this Bill of Sale.

The parties have read the foregoing Bill of Sale (Equipment, Inventory, Customer List and Other General Intangibles) and understand and agree to the terms thereof as of the date first set forth above.

Buyer: \_\_\_\_\_

By: \_\_\_\_\_

Its: \_\_\_\_\_

Seller: \_\_\_\_\_

By: \_\_\_\_\_

Its: \_\_\_\_\_

**Exhibit A**

**PATENT ASSIGNMENT**

**THIS ASSIGNMENT** (this "Assignment") is made effective as of ---, by and between \_\_\_\_\_, a \_\_\_\_\_, with its business address at \_\_\_\_\_ ("Assignor") and \_\_\_\_\_, a \_\_\_\_\_, with its business address at -----, ----- ("Assignor").

**WHEREAS** Assignor is the sole and exclusive owner of the patents, including applications and registrations listed on Exhibit A to attached hereto and made a part hereof (collectively, the "Patents"); and

**WHEREAS** Assignee desires to acquire the entire right, title, and interest in the Patents.

**NOW, THEREFORE**, for good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, Assignor hereby assign and transfer the Patents to Assignee as follows:

Pursuant to a Bill of Sale executed concurrently herewith (the "Bill of Sale"), Assignor hereby sells, assigns, and transfers to Assignee, its successors and assigns, without recourse, all of its right, title and interest in and to the Patents.

**ASSIGNOR:**

**ASSIGNEE:**

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_  
Dated: \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_  
Dated: \_\_\_\_\_

**EXHIBIT A**

**Patent Assignment**

<b>ISSUED PATENT/ SERIAL NO.</b>	<b>DESCRIPTION</b>	<b>BACKGROUND</b>