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INTRODUCTION

Filing a petition for bankruptcy, whether voluntary or involuntary, is a strenuous experience for any business. While the number of business bankruptcy filings has consistently fallen over the last four years, over 31,000 business bankruptcy cases were filed during the twelve-month period ending March 31, 2014.[1] Although bankruptcy helps businesses get a fresh start financially by protecting and rebuilding a troubled company, it can have alarming effects on the entities that do business with them.

In the past decade, the value of patents, copyrights, trademarks and trade secrets has increased considerably, and a major portion of mergers, acquisitions, and partnerships involve the license or sale of intellectual property assets.[2] Intellectual property licensing is a vital component of business strategy, which creates a partnership between an intellectual property rights owner (licensor) and another who is authorized to use such rights (licensee) in exchange for an agreed-upon fee.[3] During these deals, companies are usually unwilling to transfer complete ownership of such valuable intangible assets. As a result, businesses of all sizes negotiate to procure licenses to use intellectual property, adding significant value and revenue to their own operations.

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* J.D. candidate, University of Pittsburgh School of Law, May 2015. The author would like to thank her family for their unwavering love and support, and all of the editors from the *Journal of Technology Law & Policy* for their contributions to this Note.

[1] *U.S. Bankruptcy Courts—Business and Nonbusiness Cases Commenced, by Chapter of the Bankruptcy Code, During the 12-Month Period Ending March 31, 2014*, United States Courts (June 3, 2014, 9:30 AM), http://www.uscourts.gov/uscourts/Statistics/BankruptcyStatistics/BankruptcyFilings/2014/0314_f2.pdf.

[2] LANNING G. BRYER & MELVIN SIMENSKY, INTELLECTUAL PROPERTY ASSETS IN MERGERS AND ACQUISITIONS (2010).

[3] *Licensing of Intellectual Property Rights; a Vital Component of the Business Strategy of Your SME.*, WORLD INTELLECTUAL PROPERTY ORGANIZATION (June 3, 2014, 9:00 AM), http://www.wipo.int/sme/en/ip_business/licensing/licensing.htm.

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When the worlds of bankruptcy and intellectual property licenses converge, licensees are placed in potentially dangerous positions. Consider the following example: Entity A acquires an intellectual property license (licensee) from Entity B (licensor). Years later, Entity B becomes financially unstable and files a petition for bankruptcy. Under the U.S. Bankruptcy Code, when a company files for bankruptcy, a trustee is appointed to handle the company's debts and finances.[4] As such, the trustee for Entity B may assume or reject any executory contract of the debtor to free Entity B from burdensome financial obligations.[5] If the licensing agreement between Entity A and Entity B is considered executory and the trustee rejects it, Entity A is left in a dangerous position where its right to continue using the licensed intellectual property could be limited or fully denied.

Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc., is the seminal case on the issue of bankruptcy and intellectual property licenses.[6] The case stands for the proposition that when a debtor licensor rejects an intellectual property license as "executory," the licensee no longer has the right "to rely on provisions within the agreement with the debtor for continued use of the technology." The licensee is then left with only the claims for damages that are still available to it under other provisions of the Bankruptcy Code.[7] The *Lubrizol* ruling was a significant blow to intellectual property licensees until Congress amended the Bankruptcy Code to protect certain technology licensees by allowing them to elect to retain limited rights to the intellectual property if the debtors or trustees rejected the licenses.[8] However, Congress' amendment of the Code purposely omitted trademarks from such protections. Thus, trademark licensees have no right to the protections granted to other forms of intellectual property under the Bankruptcy Code.

This Note addresses the protection of trademark licensees when licensors enter bankruptcy proceedings. First, this Note will outline the history of intellectual property, including some of its most common forms. Second, it will discuss the Bankruptcy Code and the meaning of an executory contract. Third, it will discuss the Intellectual Property Bankruptcy Protection Act and trademark protection specifically. Fourth, this Note will detail the circuit split created by *Sunbeam Products, Inc. v. Chicago American Manufacturing*. Finally, this Note will focus

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[4] 11 U.S.C. § 1104 (2012).

[5] 11 U.S.C. § 365(a) (2012).

[6] Lubrizol Enter. v. Richmond Metal Finishers, Inc., 756 F.2d 1043 (4th Cir. 1985).

[7] *Id.* at 1048.

[8] 11 U.S.C. § 365(n) (2012).

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on the implications of the circuit split and conclude by providing some suggestions for how courts can resolve this issue in the future.

I. A History of Intellectual Property: Patents, Copyrights, and Trademarks

Intellectual property is defined as "something (such as an idea, invention, or process) that comes from a person's mind, and includes inventions, literary and artistic works, symbols, names, and images."[9] Intellectual property protection fosters human creativity, innovation and technological advancement by incentivizing individuals and companies to invest in the creation and development of their works.[10] The most common types of intellectual property are patents, copyrights, and trademarks.

A patent is "an exclusive right granted for an invention, which is a product or a process that provides a new way of doing something, or offers a new technical solution to a problem."[11] Patents provide owners of inventions with protection from commercial use, distribution or sale of the patented invention without the owner's consent.[12] Copyright grants authors protection for their creations if such creations constitute literary works such as novels, films, artistic works, or music.[13] Copyright protection allows creators to authorize or prohibit the reproduction, public performance, broadcast, translation, and adaptation of their works.[14]

A trademark is a "work, phrase, symbol, or design . . . that identifies and distinguishes the source of the goods of one party from those of others."[15] Trademarks may come in the form of "drawings, three-dimensional signs, or a combination of words, letters, and numbers."[16] Trademarks help consumers

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[9] *Intellectual Property*, Merriam-Webster, *available at* http://www.merriam-webster.com/dictionary/intellectual%20property (last visited Jan. 9, 2014) (defining intellectual property as copyrights, patents, and trademarks).

[10] *Id.*

[11] *What is a Patent?*, World Intellectual Property Organization, http://www.wipo.int/export/sites/www/freepublications/en/patents/450/wipo_pub_l450pa.pdf.

[12] *Id.*

[13] *Id.*

[14] *Id.*

[15] *Trademark, Copyright or Patent?*, United States Patent and Trademark Office (June 3, 2014, 10:00 AM), http://www.uspto.gov/trademarks/basics/trade_defin.jsp.

[16] *What is Intellectual Property?*, World Intellectual Property Organization (June 3, 2014, 10:00 AM), http://www.wipo.int/export/sites/www/freepublications/en/intproperty/450/wipo_pub_450.pdf.

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identify products based on their specific characteristics and quality.[17] More importantly, protecting trademarks ensures that owners have the "exclusive right to authorize others to use [their marks] in return for payment."[18]

The international history of intellectual property protection dates as far back as the 19th century. The importance of intellectual property was first officially recognized in the Paris Convention for the Protection of Industrial Property ("Paris Convention") in 1883 and the Berne Convention for the Protection of Literary and Artistic Works ("Berne Convention") in 1886.[19] As one of the first intellectual property treaties, the Paris Convention established a partnership among countries for the protection of intellectual property and remains in force today.[20] Eleven countries signed the Paris Convention in 1883, and today it has 176 contracting member countries.[21] It applies to intellectual property, including patents, trademarks, industrial designs, and trade names.[22] Its substantive provisions cover national treatment of intellectual property, rights of priority, and common rules that apply to all contracting countries.[23] The Berne Convention, which focuses primarily on copyright protection, requires countries to recognize the copyright of authors from other member-countries in the same way that they recognize copyrights from their own citizens.[24] The Berne Convention is still in force today with 168 contracting member countries.[25]

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[17] *Id.*

[18] *Id.*

[19] *International Treaties and Conventions on Intellectual Property*, WORLD INTELLECTUAL PROPERTY ORGANIZATION (last visited Dec. 1, 2014, 2:37 PM), http://www.wipo.int/export/sites/www/about-ip/en/iprm/pdf/ch5.pdf.

[20] *Summary of the Paris Convention for the Protection of Industrial Property (1883)*, WORLD INTELLECTUAL PROPERTY ORGANIZATION (last visited 12 AM), http://www.wipo.int/treaties/en/ip/paris/summary_paris.html.

[21] *WIPO-Administered Treaties*, WORLD INTELLECTUAL PROPERTY ORGANIZATION (last visited Dec. 1, 2014, 2:46 PM), http://www.wipo.int/treaties/en/ShowResults.jsp?treaty_id=2.

[22] WORLD INTELLECTUAL PROPERTY ORGANIZATION, *supra* note 16.

[23] *Id.*

[24] *Summary of the Berne Convention for the Protection of Literary and Artistic Works (1886)*, WORLD INTELLECTUAL PROPERTY ORGANIZATION (last visited Sept. 30, 2014), http://www.wipo.int/treaties/en/ip/berne/summary_berne.html.

[25] *Berne Convention for the Protection of Literary Works, Status on October 15, 2014*, WORLD INTELLECTUAL PROPERTY ORGANIZATION (last visited Dec. 1, 2014, 2:51 PM), http://www.wipo.int/export/sites/www/treaties/en/documents/pdf/berne.pdf.

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Domestically, the "Patents and Copyright Clause" of the U.S. Constitution is the basis for federal copyright and patent laws.[26] The Clause provides: "Congress shall have the power. . . . To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries."[27] The Clause is "intended to motivate the creative activity of authors and inventors by the provision of a special reward, and to allow the public access to the products of their genius after the limited period of exclusive control has expired."[28]

The United States Patent and Trademark Office ("USPTO"), an agency of the Department of Commerce, governs intellectual property policy in the United States.[29] At the cutting edge of technological progress and achievement, the USPTO's mission is to "promote the progress of science and the useful arts by securing for limited times to investors the exclusive right to their respective discoveries."[30] The Federal Trademark Act of 1946, more commonly known as the Lanham Act, is the primary federal trademark statute in the United States.[31] The Lanham Act "provides a national system of trademark registration and protects the owner of a federally registered mark against the use of similar marks if such use is likely to result in consumer confusion, or if the dilution of a famous mark is likely to occur."[32] It also imposes civil liability on any person who uses, in commerce, a registered trademark without the consent of the holder.[33]

The case of *Steele v. Bulova Watch Co.* addressed the extraterritorial application of the Lanham Act.[34] In the case, the American watch company brought suit against a Texas resident, Sydney Steele, for using the company's U.S.-registered trademark in Mexico.[35] At issue was whether the United States District

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[26] U.S. CONST. art. I, § 8, cl. 8.

[27] *Id.*

[28] Sony Corp. of America v. Universal City Studios, Inc., 464 U.S. 417, 429 (1984).

[29] *Intellectual Property Law and Policy*, UNITED STATES PATENT AND TRADEMARK OFFICE (last visited Sept. 30, 2014, 12:00 AM), http://www.uspto.gov/ip/index.jsp.

[30] *The USPTO: Who We Are*, UNITED STATES PATENT AND TRADEMARK OFFICE (last visited Sept. 30, 2014, 12:00 AM), http://www.uspto.gov/about/index.jsp.

[31] 15 U.S.C. § 1051 *et seq.* (2012).

[32] *Id.*

[33] Erika M. Brown, *Extraterritorial Application of Trademark Law Under the Lanham Act: Recent Decisions from the Second Circuit*, 11 N.Y. INT'L L. REV. 55, 58 (1998).

[34] Steele v. Bulova Watch Co., 344 U.S. 280 (1952).

[35] *Id.*

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Court had jurisdiction to award Bulova Watch Co. relief against trademark infringement in another country.[36] Steele had moved his watch business to Mexico City and discovered that the 'Bulova' trademark had not been registered in the country.[37] Subsequently, he registered the 'Bulova' name in Mexico, and began selling watches under the 'Bulova' name.[38] The District Court for the Western District of Texas held that it did not have subject-matter jurisdiction to hear the case.[39]

The U.S. Supreme Court affirmed the Fifth Circuit's reversal of the District Court decisions, stating, "The Lanham Act . . . confers broad jurisdictional powers upon the courts of the United States."[40] Specifically, "[t]he statute's expressed intent is to regulate commerce within the control of Congress by making actionable the deceptive and misleading use of marks in such commerce."[41] The Court based its holding on the internationally renowned reputation of Bulova Watch Co. and concluded that Steele's counterfeit watches could adversely affect the company's trade reputation in both domestic and international markets.[42] As the only case the Supreme Court has heard regarding the extraterritorial application of the Lanham Act, *Bulova* shows the broad scope of the law and the desire of both Congress and courts to protect consumers from deceptive practices.[43]

Establishing rights in intellectual property allows the creator of such patents, copyrights, or trademarks to benefit from their own work or investment in a creation.[44] Protecting intellectual property rights has social, cultural, legal, and economic objectives. The World Intellectual Property Organization (WIPO) describes these objectives in three ways:

> First, the progress and well being of humanity rest on its capacity to create and invent new works in the areas of

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[36] *Id.* at 281.

[37] *Id.* at 285.

[38] *Id.*

[39] Bulova Watch Co. v. Steele, 194 F.2d 567, 568 (5th Cir. 1952).

[40] *Bulova*, 344 U.S. at 283.

[41] *Id.*

[42] *Id.* at 286.

[43] Erika M. Brown, *The Extraterritorial Reach of United States Trademark Law: A Review of Recent Decisions Under the Lanham Act*, 9 FORDHAM INTELL. PROP. MEDIA & ENT. L.J. 863, 864 (2006).

[44] UNITED STATES PATENT AND TRADEMARK OFFICE, *supra* note 15.

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> technology and culture. Second, the legal protection of new creations encourages the commitment of additional resources for further innovation. Third, the promotion and protection of intellectual property spurs economic growth, creates new jobs and industries, and enhances the quality and enjoyment of life.[45]

The emphasis the WIPO places on protecting intellectual property rights combined with the extraterritorial reach of the Lanham Act shows the importance of intellectual property protection.[46] It encourages innovation, and helps to drive economic growth and competitiveness.[47]

II. The Bankruptcy Code and Executory Contracts

In 1965, Congress enacted 11 U.S.C. § 365 of the Bankruptcy Code, which allows a trustee, subject to court approval, "to assume or reject any executory contract . . . of the debtor."[48] While the Bankruptcy Code does not define "executory contract," it is widely accepted that to be an executory contract, performance must be due on both sides.[49] More specifically, courts rely on the definition proffered by noted bankruptcy scholar Professor Vern Countryman, which states that a contract is "executory" if the "obligations of both the bankrupt and the other party to the contract are so far underperformed that the failure of either to complete the performance would constitute a material breach excusing the performance of the other."[50] While rejecting an executory contract gives a financially distressed debtor an opportunity to be released from costly contractual obligations, it places the non-debtor party in a vulnerable position.

Generally, "licensing agreements are considered to be executory contracts because both parties have continuing obligations to fulfill."[51] In applying § 365(a),

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[45] *Id.*

[46] *Why is IP Important?*, Global Intellectual Property Center (last visited Dec. 1, 2014, 6:24 PM), http://www.theglobalipcenter.com/resources/why-is-ip-important/.

[47] *Id.*

[48] 11 U.S.C. § 365(a).

[49] NLRB v. Bildisco & Bildisco, 465 U.S. 513, 522 (1984).

[50] Vern Countryman, *Executory Contracts in Bankruptcy: Part I*, 57 Minn. L. Rev. 439, 460 (1973).

[51] Jeffrey M. Levinsohn, *Intellectual Property Collaboration Stresses in Bankruptcy: Protecting the Rights of the Nonbankrupt Parties*, 54 Hastings L.J. 471, 474 (2003); *see* Fenix Cattle Co. v.

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the Fourth Circuit has established a harsh precedent with respect to executory contracts and intellectual property licenses. In *Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc.*, Richmond Metal Finishers ("RMF") entered into a contract granting Lubrizol a "nonexclusive license to utilize a metal coating process technology owned by RMF."[52] One year later, RMF filed for Chapter 11 bankruptcy and sought to reject its contract with Lubrizol under § 365(a) of the Bankruptcy Code.[53] The Fourth Circuit held that because there were continuing duties of performance due on both sides, the agreement between RMF and Lubrizol was an executory contract subject to the rejection provision under § 365(a).[54] The Court found that RMF owed Lubrizol the continuing duties of notifying Lubrizol of further licensing and reducing their royalty rate.[55] Conversely, Lubrizol owned RMF the continuing duty of "accounting for and paying royalties for the life of the agreement."[56] The ruling allowed RMF to "unilaterally reject its license agreement," effectively discharging Lubrizol's right to use the intellectual property in its business activities.[57]

On the surface, the *Lubrizol* ruling appears clear cut. However, the court's ruling exposed a major problem with § 365. Under *Lubrizol*, in the event of bankruptcy, a non-debtor licensee has no recourse if a debtor-licensor rejects its contract under § 365(a). "Because many businesses rely on licenses as a vital resource for survival, many businesses were faced with financial ruin due to the precedent which the *Lubrizol* case established."[58] Lubrizol urged the court to consider policy implications, including the serious burdens imposed on licensees, and the potential "chilling effect upon the willingness of such parties to contract at all with business in possible financial difficulty."[59] The court noted that it

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Silver, 625 F.2d 290, 292 (9th Cir. 1980) (holding that an obligation of a debtor to refrain from selling software packages under an exclusive licensing agreement made a contract executory).

[52] *Lubrizol Enter., Inc.*, 756 F.2d at 1045.

[53] *Id.*

[54] *Id.* at 1046.

[55] *Id.* at 1045.

[56] *Id.* at 1046.

[57] David M. Jenkins, *Licenses, Trademarks, and Bankruptcy, Oh My!: Trademark Licensing and the Perils of Licensor Bankruptcy*, 25 J. MARSHALL L. REV. 143, 151 (1991).

[58] *Id.* at 151–52.

[59] *Lubrizol Enter., Inc.*, 756 F.2d at 1048.

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"understood" Lubrizol's concerns, but concluded that they were not controlling in the case.[60] Circuit Judge Phillips wrote,

> [U]nder bankruptcy law, such equitable considerations may not be indulged by courts in respect of the type of contract here at issue. Congress has plainly provided for the rejection of executory contracts, notwithstanding the obvious adverse consequences for contracting parties thereby made inevitable. Awareness by Congress of those consequences is indeed specifically reflected in the special treatment accorded to union members under collective bargaining contracts, and to lessees of real property. But no comparable special treatment is provided for technology licensees such as Lubrizol. They share the general hazards created by § 365 for all business entities dealing with potential bankrupts in the respects at issue here.[61]

Under the business judgment rule,[62] the decision by a bankruptcy trustee to assume or reject an executory contract is entitled to deference from the court, and will only be denied for bad faith.[63] In the world of business and technology, intellectual property is often the most valuable asset that an entity holds. Its use and profitability make intellectual property an attractive asset to license to potential buyers. Post-*Lubrizol*, Congress noted, "The instability of Section 365 created for intellectual property licensing relations would force parties . . . to demand assignments. This demand for outright transfers of ownership of the intellectual property is wasteful and chilling to business innovators who would otherwise benefit from keeping their ownership rights."[64]

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[60] *Id.*

[61] *Id.*

[62] Under the business judgment rule, U.S. law provides that a court will defer to the judgment of the corporation if "in making a business decision, the directors of a corporation acted on an informed basis, in good faith, and in the honest belief that the action was in the best interest of the company." Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).

[63] Levinsohn, *supra* note 51, at 474.

[64] Jenkins, *supra* note 57, at 153.

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III. The Intellectual Property Bankruptcy Protection Act and Trademark Protection

To countermand the negative effects of the *Lubrizol* decision, Congress amended the Bankruptcy Code by enacting the Intellectual Property Bankruptcy Protection Act ("IPBPA"), adding § 365(n) in 1988. The IPBPA affords an IP licensee some protection during bankruptcy proceedings.[65] Section 365(n) provides that if a debtor-licensor rejects a license agreement as an executory contract, the licensee may either (1) treat the license as terminated; or (2) retain the rights granted (except the right to compel specific performance) immediately before the bankruptcy case commenced.[66] Ultimately, § 365(n) was enacted to "temper the traditional protections given to the estate and show partial deference to the rights of licensees or licensors under the intellectual property laws."[67] Section 365(n) provided a lifeboat to licensees by allowing them to continue using licensed intellectual property. However, the definition of "intellectual property" in the Bankruptcy Code does not include trademarks, thus, they are excluded from the protection of the IPBPA amendment.

Traditionally, trademarks have been included in the definition of intellectual property.[68] *Black's Law Dictionary* defines intellectual property as "a category of intangible rights protecting commercially valuable products of human intellect. The category comprises primarily trademark, copyright, and patent rights."[69] However, § 101(35A) of the Bankruptcy Code defines intellectual property as "U.S. patents and copyrights, and trade secrets generally."[70] Some courts take the strict view that the plain language of § 365(n) excludes trademarks since they are not included in the definition of intellectual property. Thus, if a debtor-licensor rejects a trademark license, *Lubrizol* controls and the licensee is stripped of its right to use the mark. Other courts, looking to the legislative history of § 365(n), take the view that Congress intended courts to use their equitable powers to allow a licensee to continue using the trademark license while freeing the licensor of its obligations

[65] *See* 11 U.S.C. § 365(n) (2012).

[66] *Id.*

[67] Levinsohn, *supra* note 51, at 477.

[68] *Intellectual Property*, MERRIAM-WEBSTER, *available at* http://www.merriam-webster.com/concise/intellectual%20property (last visited Jan. 9, 2014) (defining intellectual property as copyrights, patents, and trademarks).

[69] BLACK'S LAW DICTIONARY 881 (9th ed. 2009).

[70] Levinsohn, *supra* note 51, at 473 (citing 11 U.S.C. § 101(35A) (2012)).

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under the contract.[71] Thus, the critical question is whether the trademark license agreement is executory.

A. In re Exide Technologies*: Trademark Licenses Are Non-Executory*

In *Exide Technologies*, the central issue was whether a trademark license was an executory contract subject to rejection under § 365(a).[72] During its bankruptcy, Exide sought to reject a number of agreements with EnerSys Delaware, Inc., including a Trademark and Trade Name License Agreement ("Agreement").[73] Under the Agreement, Exide granted EnerSys a "perpetual, exclusive, royalty-free license" to use the Exide trademark.[74] The Bankruptcy Court found the Agreement to be an executory contract, terminating both Exide's obligations under the Agreement and EnerSys' right to use the license.[75] However, the Third Circuit reversed, holding that the contract was not executory because EnerSys did not have a continuing material obligation under the agreement with Exide.[76] The Court held that EnerSys's ongoing, unperformed obligations did not outweigh the substantial performance rendered and the benefits received by EnerSys.[77]

B. In re Interstate Bakeries Corp.*: Trademark License is Executory*

In *Interstate Bakeries*, Lewis Brothers Bakeries ("LBB"), Inc. brought suit against Interstate Bakeries Corporation ("Interstate") arguing that the trademark licensing agreement between them was not an executory contract.[78] In 1996, Interstate entered into an agreement with LBB, granting it a "perpetual, royalty-free, assignable, transferable, exclusive" license to use Interstate's brands and trademarks, which included the Wonder Bread and Hostess brands.[79] In 2004, Interstate filed a Chapter 11 voluntary bankruptcy.[80]

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[71] *In re* Centura Software Corp., 281 B.R. 660, 669–71 (Bankr. N.D. Cal. 2002) (discussing alternative approaches to treatment of a trademark licensee).

[72] *In re* Exide Techs., 607 F.3d 957 (3d Cir. 2010).

[73] *Id.* at 961.

[74] *Id.*

[75] *Id.*

[76] *Id.* at 965.

[77] *Id.* at 963.

[78] *In re* Interstate Bakeries Corp., 690 F.3d 1069, 1072 (8th Cir. 2012).

[79] *Id.* at 1071–72.

[80] *Id.* at 1072.

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The Bankruptcy Court held, and the District Court affirmed, that the agreement between Interstate and LBB was executory because material obligations remained for both parties.[81] The court found that both Interstate and LBB maintained a number of obligations, specifically to maintain the quality and character of the goods.[82] LBB relied on the Third Circuit's finding in *Exide* that quality control was not a material obligation under the agreement, rendering its contract with Interstate non-executory.[83] However, the Eighth Circuit distinguished the case by pointing out that in *Exide*, "the parties had not even contemplated or discussed any quality standards, so the court refused to import such an obligation into the agreement and thereafter conclude the obligation was material."[84] Conversely, Interstate and LBB expressly stated in the license agreement that a breach of the quality control provision would constitute a material breach.[85] As a result, the Eight Circuit found the agreement to be an executory contract subject to rejection under § 365(a).[86]

Exide and *Interstate Bakeries* exposed a critical problem in the treatment of trademark licenses in bankruptcy proceedings. As seen in *Interstate*, trademark license agreements can be considered executory contracts.[87] As long as there are continuing material obligations remaining on both sides, a debtor-licensor may reject the agreement under § 365(a). But, since trademarks are not included in the definition of "intellectual property" in the Code, trademark licensees lack recourse under Section 365(n) to retain any right to use or terminate the contract in the event the licensor rejects the contract. As such, courts continue to struggle with the holding of *Lubrizol*, and the rights of trademark licensees.

IV. CIRCUIT SPLIT: *SUNBEAM PRODUCTS, INC.* REJECTS *LUBRIZOL*'S HOLDING

The Seventh Circuit came to a different conclusion regarding a trademark licensee's right to continue using a licensed mark after rejection by a debtor-licensor. In *Sunbeam Products*, Lakewood Engineering & Manufacturing Co.

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[81] *Id.* at 1071.

[82] *Id.*

[83] *In re* Interstate Bakeries Corp., 690 F.3d 1069, 1075 (8th Cir. 2012).

[84] *Id.*

[85] *Id.*

[86] The *Interstate Bakeries* opinion was vacated June 18, 2013, and a rehearing *en banc* was granted.

[87] 11 U.S.C. § 365(a) (2012).

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("Lakewood") produced a number of consumer products, including box fans.[88] In financial distress, Lakewood entered into an agreement with Chicago American Manufacturing ("CAM") to manufacture the fans, and authorized CAM to place Lakewood trademarks on its box fans.[89] As part of the agreement, Lakewood took orders from larger retail customers and CAM shipped the fans directly to the buyers.[90] To guarantee payment in light of Lakewood's financial distress, CAM negotiated for authorization to sell the fans for its own account in the event that Lakewood did not purchase them during the 2009 season.[91] Three months later, Lakewood was forced to file for bankruptcy, and the court-appointed trustee opted to sell the business.[92] Sunbeam Products bought Lakewood, including all of its patents and trademarks.[93] To prevent CAM from selling fans branded with the Lakewood trademark in competition with Sunbeam, the company rejected the CAM licensing agreement under § 365(a).[94] CAM continued to produce and sell the fans, and Sunbeam subsequently brought suit against the company.[95]

The central issue in the case was the effect of Sunbeam's rejection of the executory contract upon CAM's right to sell the trademarked fans. The Seventh Circuit held on equitable grounds that CAM, "which invested substantial resources in making Lakewood-branded box fans," was allowed to continue using the Lakewood trademark.[96] Similar to Judge Ambro's concurrence in *Exide*, the court looked to legislative history and reasoned that "the limited definition in § 101(35A) means that § 365(n) does not affect trademarks one way or the other. According to the Senate committee report on the bill that included § 365(n), the omission was designed to allow more time for study, not to approve *Lubrizol*."[97] The court took the view that it would be unfair to strip CAM of its rights under its licensing agreement simply because the definition of intellectual property is limited under the Bankruptcy Code. The court declined to follow *Lubrizol* on the grounds that it "confuses rejection with the use of an avoiding power . . . and devoted scant

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[88] Sunbeam Products, Inc. v. Chicago Am. Manufacturing, 686 F.3d 372, 374 (7th Cir. 2012).

[89] *Id.*

[90] *Id.*

[91] *Id.*

[92] *Id.*

[93] *Id.*

[94] Sunbeam Products, Inc. v. Chicago Am. Manufacturing, 686 F.3d 372, 374 (7th Cir. 2012).

[95] *Id.*

[96] *Id.* at 375.

[97] *Id.*

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attention to the question of whether rejection cancels a contract, worrying instead about the right way to identify executory contracts to which the rejection power applies."[98]

V. Analysis

A. Implications of Circuit Split

The legislative history of § 365(n) specifically states:

> [T]he bill does not address the rejection of executory trademark, trade name or service mark licenses by debtor-licensors. While such rejection is of concern because of the interpretation of section 365 by the *Lubrizol* court and others, such contracts raise issues beyond the scope of this legislation. In particular, trademark, trade name and service mark licensing relationships depend to a large extent on control of the quality of the products or services sold by the licensee. Since these matters could not be addressed without more extensive study, it was determined to postpone congressional action in this area and to allow the development of equitable treatment of this situation by bankruptcy courts.[99]

The concurring opinion in *Exide* underscores the struggle of courts in the face of *Lubrizol* and the legislative history of § 365(n). Circuit Judge Ambro argued that the lower courts inappropriately decided that because trademarks are not "intellectual property" under the Bankruptcy Code, *Lubrizol* controls and licensees (such as *EnerSys*) lose their right to use the trademark for their products once the licensor rejects the agreement.[100] While Judge Ambro conceded that Congress did not protect trademark licenses under § 365(n), she argued that courts should "use their 'equitable powers' to give debtor-licensor's a fresh start without stripping licensees of their fairly procured trademark rights."[101] Moreover, Judge Ambro

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[98] *Id.* at 377.

[99] S. Rep. No. 100-505 (1988).

[100] *In re* Exide Techs., 607 F.3d 966 (3d Cir. 2010).

[101] *Id.* at 968 (suggesting that the rejection of a trademark license would not deprive a licensee of its rights in the licensed mark).

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noted that had the majority found the contract to be executory, she would have allowed EnerSys to keep its rights under the agreement.

The current state of the law leaves courts with three options: (1) allow courts to use equitable discretion; (2) force licensees to assess their remedial rights under § 365(g); or (3) follow the plain language of § 365(n). Each of these options poses significant risks.

The option of subjecting the licensee to the equitable discretion of the bankruptcy court lacks the predictability and stability that a bright line rule could provide. The precedent could be on both sides, with only the courts' "equitable judgment" to distinguish between cases. As Judge Easterbrook in *Sunbeam* noted,

> There are hundreds of bankruptcy judges, who have many different ideas about what is equitable in any given situation. Some may think that equity favors licensees' reliance interests; others may believe that equity favors creditors, who can realize more of their claims if the debtor can terminate IP licenses.[102]

Section 365(g) provides for the rights and remedies of licensee's pre-petition for bankruptcy.[103] Section 365(g) expressly states, "The rejection of an executory contract or unexpired lease of the debtor constitutes a breach of such contract or lease."[104] This breach is ordinarily deemed to have occurred immediately before the date of the filing for bankruptcy.[105] Some courts argue that if a licensor rejects a trademark agreement, the licensee should be directed to 365(g) for a remedy.[106]

In *In re Chipwich, Inc.*, the court grappled with the application of § 365(g) in the context of a trademark license controversy. Chipwich entered into an agreement with Farmland, granting the company an exclusive license in the U.S. "to produce, sell, distribute, sub-license, sub-contract, advertise and promote eggnog and flavored milk under the Chipwich trademark."[107] Approximately one year later, an

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[102] Sunbeam Products, Inc. v. Chicago Am. Manufacturing, 686 F.3d 372, 375–76 (7th Cir. 2012).

[103] 11 U.S.C. § 365(g)(1) (2012).

[104] *Id.*

[105] *Id.*

[106] *In re* Chipwich Inc., 54 B.R. 427, 429 (Bankr. S.D.N.Y 1985).

[107] *Id.* at 428.

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involuntary petition for bankruptcy was filed against Chipwich, and the company sought to reject its license agreement with Farmland.[108]

The court held that Chipwich was authorized to reject the agreement, thereby releasing it from the contract with Farmland.[109] The court recognized "the obvious adverse consequences for contracting parties thereby made inevitable" by § 365(a), but concluded that Farmland could treat the rejection as a breach of contract under § 365(g).[110] Here, the court reasoned "there was no showing that Farmland will be damaged disproportionately to any benefit derived by the debtor."[111]

Conversely, in *In re Petur U.S.A. Instrument Co.*, Petur USA entered into a 20-year license with Petur of Canada granting the Canadian company the exclusive right to use, manufacture, assemble, and sell the inventions of Petur USA.[112] Because Petur Canada was created for the sole purpose of marketing Petur USA's products in Canada, all of their business and income was based upon the license agreement.[113] After Petur USA filed for bankruptcy, the company attempted to reject its executory contract with Petur Canada arguing that it was within the company's business judgment and would aid in reorganization.[114] The court concluded that the agreement was executory, but refused to allow Petur USA to reject the contract because it would do too much damage to Petur Canada.[115] The court reasoned that "the destruction of the licensee's business and the size of the resulting damage claim under § 365(g) would be 'grossly disproportionate to any benefit derived.'"[116] More specifically, "the court was concerned primarily with the severity of the harm to the non-debtor that would result if rejection were permitted."[117]

Both *Chipwich* and *Petur* show the dangers of utilizing § 365(g) as a remedy for licensees because its use hinges on how much of the licensee's business is

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[108] *Id.* at 428–29.

[109] *Id.* at 431.

[110] *Id.*

[111] *Id.*

[112] *In re* Petur U.S.A. Instrument Co., 35 B.R. 561, 562 (Bankr. W.D. Wash. 1983).

[113] *Id.* at 562.

[114] *Id.* at 563.

[115] *Id.*

[116] Jeffrey R. Seul, *License and Franchise Agreements as Executory Contracts: A Proposed Amendment to Section 365 of the Bankruptcy Code*, 59 U. COLO. L. REV. 129, 142 (1988).

[117] *Id.*

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based upon the executory contract in question. If the licensee's business is not based largely on the executory contract, then damages may provide *some* monetary relief. However, if the licensee's business is in fact based exclusively on the executory contract, damages will provide little in the way of relief since the licensee will be forced out of business. Because specific performance of the contract is not an available remedy, the licensee's business is at the mercy of the court.

B. Suggestion for the Future

In his article *Licenses, Trademarks, and Bankruptcy, Oh My! Trademark Licensing and the Perils of Licensor Bankruptcy*, David Jenkins calls for a six-point revision to the Bankruptcy Code to "effectively resolve the problem of debtor-licensor rejection of executory trademark license agreements."[118] His proposal specifically calls for an amendment that would: (1) allow trademark licensees to retain their rights, (2) require courts to preliminarily assess trademark abandonment and quality control issues, (3) provide for continued delivery of materials under the license agreement, (4) guarantee the licensee's "quiet enjoyment of the right to use the trademark," (5) continue royalty payments to either the licensor or the bankruptcy estate, and (6) allow the licensee to continue its use of the trademark for the duration originally promised.[119]

Jenkins' proposed amendment is extensive, and focuses mostly on the courts preliminary assessment of abandonment and quality control issues, which were largely why Congress opted not to protect trademarks under § 365(n).[120] In order for a trademark licensee to retain its rights under a license agreement, a debtor-licensor must show that it will not abandon the trademark.[121] Trademark abandonment occurs when the licensor intends not to use the mark in commerce after it has discontinued its use.[122] It is important to make a requisite finding that the licensor will not abandon the trademark because if a licensee continues using an abandoned trademark, it risks deceiving the public as to the marks original source or guarantee of quality.[123]

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[118] Jenkins, *supra* note 57, at 165.

[119] *Id.* at 165–66.

[120] *Id.* at 160.

[121] *Id.* at 167.

[122] 15 U.S.C. § 1127 (1988).

[123] Jenkins, *supra* note 57, at 168.

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At the same time, a licensee must maintain the quality control procedures agreed to in the original licensing agreement.[124] Quality control is "the most important and complex aspect" of Jenkins' proposed amendment.[125] The measures for quality control are important because they ensure that the quality of the trademark will not be diminished and that its continued use will not deceive the public. Jenkins suggests that bankruptcy courts should find that licensee quality control measures are adequate if they are *reasonably effective* to ensure proper maintenance of the quality of the trademark.[126] He suggests that informal control requirements such as unannounced inspections of the licensee's facilities or submitting samples and inspection reports to the licensor are reasonably effective measures that the court could impose upon licensees.[127]

However, part of the hesitancy of Congress to include trademarks under § 365(n) was the issue of quality control and fear that imposing such standards on licensees would undercut the Lanham Act's quality control requirement.[128] Section 5 of the Lanham Act provides:

> When a registered mark or a mark sought to be registered is or may be used legitimately by related companies, such use shall inure to the benefit of the registrant or applicant for registration, and such use shall not affect the validity of such mark or of its registration, provided such mark is not used in such a manner as to deceive the public.[129]

Under the Lanham Act, trademark owners already have a duty to exercise quality control over its mark. The amendment suggested by Jenkins would require courts to impose stricter quality control standards than are required under the Act.

From a fairness perspective, amending § 365(n) would place trademarks on equal footing with other forms of intellectual property covered under the statute. It would give trademark licensees the option to retain their rights under a license

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[124] *Id.* at 166.

[125] *Id.*

[126] *Id.*

[127] *Id.* at 170.

[128] William M. Borchard & Richard M. Osman, *Trademark Sublicensing and Quality Control*, 70 TRADEMARK REP. 99, 102 (1980).

[129] 15 U.S.C. § 1055 (2012).

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agreement. However, the original draft of the IPBPA contained a proposal for protecting trademarks.[130] The proposal provided, in pertinent part, that the trustee would not be allowed to interfere with the licensee's rights.[131] Specifically, in the case of trademarks, the proposal permitted existing licensees to continue the use and enjoyment of the mark so long as they maintained the quality control standards.

Congress dropped this proposal from the amendment for three primary reasons: (1) a primary concern for technological development, (2) issues regarding quality control, and (3) the possibility for court-created equitable remedies.[132] First, Congress was more troubled by the technological advancements of other forms of intellectual property.[133] As noted earlier, it was also concerned with the uniqueness of trademarks and the necessary quality control requirements.[134] Lastly, Congress only sought to "postpone" action on trademark protection in order to allow bankruptcy courts to generate equitable remedies.[135] However, the rationale behind each of these reasons is weak and no longer valid.

First, intellectual property historically encompasses trademarks, which promote technological advancement and economic growth just as much as other forms of intellectual property. By their very nature, trademarks generate familiarity, trust, and certainty of a brand, which in turn facilitates technological investment and advancement.[136] Trademarks have been shown to be useful complements to other forms of IP protection, and positively linked with innovative activity and growth in companies that use them.[137] Specifically, trademarks contribute substantially to a company's intangible assets and market value.[138] A 2010 survey by Interbrand found that the value of the IP in the brand recognition alone for each of the top ten brands worldwide exceeded $25 billion.[139] Such staggering numbers show the value in strong trademark protection.

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[130] S1626, 100 Cong., 1st Sess., 133 CONG. REC. S11, 653 (1987).

[131] *Id.*

[132] Jenkins, *supra* note 57, at 160.

[133] *Id.*

[134] *Id.*

[135] *Id.*

[136] *Id.*

[137] *Intellectual Property: Powerhouse for Innovation and Economic Growth*, INTERNATIONAL CHAMBER OF COMMERCE (last visited Dec. 3, 2014, 8:15 PM), http://www.iccwbo.org/advocacy-codes-and-rules/bascap/value-of-ip/ip-and-economic-growth/.

[138] *Id.*

[139] *Id.*

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Second, the Lanham Act already imposes quality control standards upon trademark licensees.[140] The Lanham Act requires licensors to provide quality control, and courts have become increasingly lenient in the standards for sufficient quality control.[141] Further, licensees engage in their own form of quality control because they invest substantial resources into building and maintaining the quality of the mark.[142] From a practical perspective, the burden on licensors to maintain quality control standards is not so burdensome. Thus, using quality control concerns as a rationale for not protecting non-debtor licensees is senseless.

CONCLUSION

Each of the cases discussed herein highlights the continuing risks of relying on a trademark license rather than outright ownership of a trademark. Congress' rationale for excluding trademarks from § 365(n) has proven to be unworkable, outdated, and unjustifiable. The circuit split shows that courts and businesses alike need direction and finality on this issue. Moreover, the Supreme Court denied review of *Sunbeam* leaving the split in place for now. Congress must address the problems caused by the unequal treatment of trademarks in bankruptcy proceedings by amending the IPBPA to include trademarks. From both a policy and fairness perspective, the disparate treatment of trademarks as a traditional class of intellectual property can no longer be sustained.

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[140] 15 U.S.C. § 1055 (2012).

[141] Xuan-Thao N. Nguyen, *Bankrupting Trademarks*, 37 U.C. DAVIS L. REV. 1267, 1281 (2004).

[142] Laura Jelinek, *Equity for Brand Equity: The Case for Protecting Trademark Licensees in Licensor Bankruptcies*, 40 AIPLA Q.J. 365, 386 (2012).

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