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SUNBEAM: A RAY OF HOPE FOR TRADEMARK LICENSEES

*Ryan Gabay**

In the 1985 decision Lubrizol Enterprises v. Richmond Metal Finishers, *the Fourth Circuit established that a licensor's rejection of an intellectual property license under § 365 of the U.S. Bankruptcy Code terminates the licensee's right to continue using the license. Concerned about the detrimental effects that* Lubrizol *would have on technological development in the United States, Congress responded swiftly by enacting the Intellectual Property Licenses in Bankruptcy Act (IPLBA), which exempted certain forms of intellectual property, such as copyrights, patents, and trade secrets, from rejection under § 365 of the Code. Trademarks, however, are notably absent from Congress's definition of "intellectual property," causing the trademark licensing community to question the reach of the IPLBA's protections.*

Recently, the Seventh Circuit held that a trademark licensee may continue using a licensed trademark following rejection, despite Congress's omission of trademarks from its listed definition of "intellectual property." This Note examines the divide between the Fourth and Seventh Circuits, and it contends that careful consideration of existing executory contract doctrine and the IPLBA's legislative history, as well as the balance of equities, suggests that trademark licensees should retain their rights to continue utilizing licensed trademarks following rejection.

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* J.D. Candidate, 2014, Fordham University School of Law; B.S., 2011, Cornell University. I would like to thank my family and friends for their patience and encouragement. I am especially grateful to my mother, Sheila, and sisters, Meredith and Alison, for their love and support.

INTRODUCTION

Suppose that Apple Inc. agrees to license its Apple logo to a hypothetical company, Company X, for use on Company X's new line of computers. Suppose further that prior to Company X selling the newly branded computers, Apple Inc. falls into financial distress and files for bankruptcy under Chapter 11 of the U.S. Bankruptcy Code. Section 365 of the Code provides that upon filing for bankruptcy, a debtor is permitted to reject an executory contract—that is, a contract in which substantial performance remains on both sides. However, intellectual property is exempted from this provision of the Code. Thus, if Apple Inc. chooses to reject its licensing agreement with Company X following Apple Inc.'s Chapter 11 filing, an interesting dilemma results: may Company X continue to utilize the Apple logo despite the licensor's rejection of the trademark license in bankruptcy?

In *Sunbeam Products, Inc. v. Chicago American Manufacturing, LLC*,[1] Chief Judge Easterbrook considered precisely this issue. Previously, in *Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc.*,[2] the Fourth Circuit held that the rejection of an intellectual property license in bankruptcy terminates the licensee's right to continue utilizing the license.[3] The Seventh Circuit, however, held that a trademark licensee is permitted to continue using the licensed trademark even after the licensor's rejection of the license.[4] Therefore, *Sunbeam* created a circuit split on the issue of whether a trademark licensee may retain its rights to continue use of a license following a debtor's rejection in bankruptcy.

Trademarks can be very valuable, and a trademark licensor has a significant interest in maintaining the right to continue utilizing a trademark after it has been rejected in bankruptcy.[5] For instance, trademarks for well-known brands such as Marlboro, Coca-Cola, and McDonald's have estimated values of approximately $44.6 billion, $43 billion, and $19 billion, respectively.[6] In addition, for companies such as Sarah Lee Corp., trademarked brand names may account for approximately 70 percent of the company's net worth.[7] Especially in the age of the internet, in which consumers are more likely to find an easily identifiable product during web searches, the value of a simple and clear brand name has escalated.[8]

1. 686 F.3d 372 (7th Cir. 2012), *cert. denied*, 133 S. Ct. 790 (2012).
2. 756 F.2d 1043 (4th Cir. 1985).
3. *See id.* at 1048.
4. *See Sunbeam*, 686 F.3d at 378.
5. Trademark protection is critical to a company seeking to build its brand. *See* Stephanie Strom, *Battle of the Brands*, N.Y. TIMES, Feb. 21, 2012, at B1 (stating that trademarks can provide tremendous value to companies in strengthening their brands and pointing to Kimberly-Clark's Kleenex facial tissues and Nike's "swoosh" logo as examples).
6. Brendan Mahaffey-Dowd, *Famous Trademarks: Ordinary Inquiry by the Courts of Marks Entitled to an Extraordinary Remedy*, 64 BROOK. L. REV. 423, 425 n.17 (1998).
7. *See id.* at 425 n.14.
8. *See* Strom, *supra* note 5, at B1. Take the Nike "swoosh" trademark, for example. The "swoosh" is Nike's core value, and the company considers its "Nike" and "swoosh"

It is commonly understood that intellectual property is comprised of copyrights, patents, trademarks, and trade secrets.[9] Accordingly, one might reasonably expect that the Intellectual Property Licenses in Bankruptcy Act (IPLBA),[10] enacted by Congress in 1988 to exempt "intellectual property" from rejection under § 365 of the Bankruptcy Code, would include all four commonly recognized forms of intellectual property within its coverage. In fact, the Bankruptcy Code does not include trademarks within its listed definition of intellectual property, despite its recognition of copyrights, patents, and trade secrets.[11] The omission of trademarks has, in many instances, had a profound impact on the rights of trademark licensees upon a debtor's rejection of the license in bankruptcy.

This Note assesses the vulnerability of trademark licenses following a licensor's rejection. Specifically, this Note seeks to address whether a licensee should be permitted to continue utilizing a licensed trademark after a licensor has rejected the trademark license under § 365(a) of the Bankruptcy Code.

Part I of this Note examines the crucial role of intellectual property licensing agreements in the business context and then addresses the IPLBA, which exempted intellectual property from rejection under § 365 of the Bankruptcy Code. Part II analyzes the conflicting positions taken by the Fourth and Seventh Circuits, as well as several bankruptcy courts, regarding the rights retained by an intellectual property licensee following rejection of the license by the debtor. Finally, in Part III, this Note argues that the circuit split should be resolved by following the Seventh Circuit's decision in *Sunbeam* in order to avoid the harsh results of *Lubrizol*, and to prevent a chilling effect on the willingness of trademark licensees to enter into licensing deals with licensors facing financial difficulties. Moreover, this Note asserts that *Lubrizol* incorrectly applied § 365(g) and contends that rejection of a trademark license constitutes a breach in which the parties' rights should not be terminated. While equitable considerations are relevant to a thorough understanding of trademark license rejection, this Note will look primarily to the Bankruptcy Code itself as a justification for

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design trademarks "to be among its most valuable assets." *See* STEPHEN PAPSON & ROBERT GOLDMAN, NIKE CULTURE: THE SIGN OF THE SWOOSH 15 (1999).

9. *See* BLACK'S LAW DICTIONARY 881 (9th ed. 2009) (defining intellectual property to "comprise[ ] primarily trademark, copyright, and patent rights, but also include[] trade-secret rights"); Jean Raymond Homere, *Intellectual Property Rights Can Help Stimulate the Economic Development of Least Developed Countries*, 27 COLUM. J.L. & ARTS 277, 279 (2004) (stating that the basic forms of intellectual property are patents, copyrights, trademarks, and trade secrets).

10. Intellectual Property Licenses in Bankruptcy Act, Pub. L. No. 100-506, 102 Stat. 2538 (1988) (codified at 11 U.S.C. § 365(n) (2006)).

11. *See* 11 U.S.C. § 101(35A) (2006). Under its definition of intellectual property, the Code lists the following: "(A) trade secret; (B) invention, process, design, or plant protected under title 35; (C) patent application; (D) plant variety; (E) work of authorship protected under title 17; or (F) mask work protected under chapter 9 of title 17; to the extent protected by applicable non-bankruptcy law." Works of authorship include pictorial, graphic, and sculptural works. *See* 17 U.S.C. § 102(a) (2006).

maintaining the rights of a trademark licensee following rejection by the debtor.

I. THE EVOLUTION OF INTELLECTUAL PROPERTY LICENSE REJECTION IN BANKRUPTCY

Part I provides an overview of important intellectual property and bankruptcy concepts, and examines the Fourth Circuit's holding in *Lubrizol* as well as Congress's enactment of the IPLBA. Part I.A describes the various types of intellectual property, specifically focusing on the value of intellectual property licenses to the financial success and efficiency of businesses. Part I.B examines the policies that underlie bankruptcy law and explains the consequences that arise following a debtor's rejection of an executory contract. Part I.C addresses the *Lubrizol* decision and Congress's subsequent response in enacting the IPLBA.

A. An Overview of Intellectual Property Doctrine

The following discussion summarizes basic intellectual property doctrine as background analysis to provide a foundation for the rest of this Note. The section begins by explaining the various categories of intellectual property. It then focuses more narrowly on trademark protection and concludes by discussing the critical role that intellectual property licenses play for both debtors and creditors in the continued success and, in many instances, survival of their businesses.

1. Protection of Original Works and Inventions: Copyrights and Patents

Intellectual property, as it is commonly understood, is comprised of copyrights, patents, trademarks, and trade secrets.[12] Both copyrights and patents are expressly referenced in the U.S. Constitution,[13] while trademarks and trade secrets are not.[14]

Copyright protection is codified as part of federal law.[15] It exists in any original work of authorship that is embodied in a tangible medium of expression and communicated either directly or with the assistance of a device.[16] The categories of works of authorship include: "(1) literary works; (2) musical works, including any accompanying words; (3) dramatic works, including any accompanying music; (4) pantomimes and choreographic works; (5) pictorial, graphic, and sculptural works; (6) motion pictures and other audiovisual works; (7) sound recordings; and

12. *See supra* note 9 and accompanying text.

13. *See* U.S. CONST. art. I, § 8, cl. 8 ("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.").

14. *See* Xuan-Thao N. Nguyen, *Bankrupting Trademarks*, 37 U.C. DAVIS L. REV. 1267, 1294, 1297 (2004).

15. *See* 17 U.S.C. § 102(a).

16. *Id.*

(8) architectural works."[17] Copyright protection may extend to the expression of an author's ideas but will not "protect the ideas themselves."[18]

Patents comprise a second category of intellectual property. Under the Patent Act, patent protection extends to any person who "invents or discovers any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof."[19] This patent eligibility inquiry, however, is only a threshold test for patent protection.[20] Additionally, even if an invention or discovery qualifies as a process, machine, manufacture, or composition of matter, it must also satisfy certain other conditions and requirements such as novelty,[21] nonobviousness,[22] and a full and particular description.[23] While section 101 of the Patent Act specifies particular subject matter that may be patented, it is meant to be a dynamic provision that is flexible enough to encompass novel and unanticipated inventions.[24] Congress chose an adaptable rule because a rigid rule denying patent protection for inventions and discoveries in areas that Congress did not anticipate would frustrate the underlying purposes of patent law.[25]

2. Identifying and Distinguishing the Source of Goods: Trademark Protection

Trademarks comprise a third type of intellectual property. The subject matter of a trademark can vary widely and might include a word, color, design, scent, symbol, sound, or a wide array of other types of indicators of the source of goods.[26] To qualify for legal protection, though, a mark must be distinctive.[27] Only those marks that adequately distinguish the trademark applicant's products from goods owned by others may be successfully registered with the U.S. Patent and Trademark Office.[28]

Thus, the statutory definition of "trademark" states that the word, name, or symbol must be used or intended to be used to identify and differentiate the trademark owner's products from goods that are manufactured or distributed by others, and to indicate the source of the products, even if the

17. *Id.*

18. *See* 9 WILLIAM L. NORTON, JR. & WILLIAM L. NORTON III, NORTON BANKRUPTCY LAW & PRACTICE § 177:8–9 (3d ed. 2013).

19. 35 U.S.C. § 101 (2006).

20. Bilski v. Kappos, 130 S. Ct. 3218, 3221 (2010).

21. *See* 35 U.S.C. § 102.

22. *See id.* § 103.

23. *See id.* § 112.

24. Bilski, 130 S. Ct. at 3227 (quoting J.E.M. Ag Supply, Inc. v. Pioneer Hi-Bred Int'l, Inc., 534 U.S. 124, 135 (2001)).

25. *See id.* (citing Diamond v. Chakrabarty, 447 U.S. 303, 315 (1980)).

26. 1–2 ANNE GILSON LALONDE, GILSON ON TRADEMARKS § 2.01 (2007) (noting that the subject matter of trademarks is potentially endless).

27. *Id.*

28. *Id.* (quoting 15 U.S.C. § 1052 (2006)).

source is not known.[29] A design or pattern that is merely considered product ornamentation does not qualify for trademark protection, because it has not adequately distinguished itself.[30]

Courts categorize marks based on a trademark distinctiveness spectrum.[31] Under this spectrum, courts will classify marks as: (1) generic, (2) merely descriptive, (3) suggestive, or (4) arbitrary or fanciful.[32] However, the determination of which category a mark will fit into is not always clear.[33] Complicating factors include the possibilities that a term might have different meanings among different sets of users,[34] and a term might refer to two separate products, each of which belongs to a separate category.[35]

In *Abercrombie & Fitch Co. v. Hunting World, Inc.*,[36] Judge Friendly formulated the test that courts use to determine where a mark falls on the trademark spectrum. According to Judge Friendly, a generic term refers broadly to the genus or group of products, under which a particular product would be classified as the species.[37] Under no circumstances may a generic mark be afforded trademark protection.[38]

A term that is descriptive but not generic is more likely to be afforded protection.[39] Section 2(e) of the Lanham Act disallows the registration of marks that are merely descriptive.[40] However, section 2(f) provides an exemption to this general rule by extending trademark protection to descriptive terms that have become distinctive of the trademark applicant's goods.[41] As prima facie evidence that a mark has become distinctive, a trademark applicant may present proof of substantially exclusive and continuous use of the mark for five continuous years prior to the application.[42]

Suggestive terms fall in between the categories of descriptive and fanciful. A term will be suggestive if it is necessary to use thought, insight,

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29. *Id.* (quoting 15 U.S.C. § 1127).

30. *See id.*

31. *See id.* § 2.01[1].

32. *Id.*

33. *See* Abercrombie & Fitch Co. v. Hunting World, Inc., 537 F.2d 4, 9 (2d Cir. 1976) ("The lines of demarcation . . . are not always bright.").

34. *See* Bayer Co. v. United Drug Co., 272 F. 505, 510 (S.D.N.Y. 1921).

35. *See Abercrombie & Fitch Co.*, 537 F.2d at 9 n.6 (providing the example that "ivory" would be classified as generic if used to describe a product derived from elephant tusks but would be classified as arbitrary with respect to soap).

36. 537 F.2d 4 (2d Cir. 1976).

37. *Id.* at 9.

38. *Id.* (stating that the Lanham Act provides for the cancellation of a registered mark if at any time it becomes the common descriptive name of an article or substance). Even if proof of a secondary meaning can be offered, a generic term cannot be transformed into a subject for trademark. *Id.*

39. *Id.* at 10 (stating that descriptive terms "stand[] on a better basis" than those that are generic).

40. *See* 15 U.S.C. § 1052 (2006). The Lanham Act is a federal act that provides statutory protection for trademarks and trade dress. *See id.* §§ 1051–1127.

41. *See Abercrombie & Fitch Co.*, 537 F.2d at 10.

42. *See id.*

and imagination to decipher the nature of the product.[43] Suggestive terms may be registered as trademarks without proof of any secondary meaning.[44]

A term is fanciful if it is derived solely for the purpose of its use as a trademark,[45] while an arbitrary term is a term that is applied in an unusual or unfamiliar way.[46] Fanciful and arbitrary terms are at the extreme end of the trademark distinctiveness spectrum and are accorded all of the rights that are given to suggestive terms as marks that require neither thought nor imagination in order to determine whether the term is simply descriptive.[47]

Important consequences attach to a mark's distinctiveness classification. In determining whether a plaintiff has demonstrated trademark infringement, courts consider several factors, including: (1) strength of the mark, (2) similarity between the marks, (3) evidence of actual confusion, and (4) evidence that the imitative mark was adopted in bad faith.[48] Notably, a term that is generic or descriptive without a secondary meaning is not a valid mark and therefore will not be entitled to protection.[49]

3. Trademark Licensing Agreements: Expanding the Scope and Reach of an Owner's Brand

Intellectual property licenses have proven to be significant in aiding the growth of industry.[50] For both debtors and creditors, an intellectual property license may be a particularly valuable asset that is important to the continuing success of a company's business.[51] Even if a license plays a secondary role in the operation of a licensee's business, the license will often remain essential to the business's profitability and efficiency.[52]

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43. *See id.* at 11 (providing a contrast between suggestive terms and descriptive terms, which convey "an immediate idea of the ingredients, qualities or characteristics of the goods" (quoting Stix Prods., Inc. v. United Merchs. & Mfrs., Inc., 295 F. Supp. 479, 488 (S.D.N.Y. 1968))).

44. *Id.*

45. *Id.* at 11 n.12.

46. *Id.*

47. *See id.* at 11. Examples of fanciful marks, which "are, in essence, made-up words expressly coined for serving as a trademark," include Clorox, Kodak, Polaroid, and Exxon. Sarah Lee Corp. v. Kayser-Roth Corp., 81 F.3d 455, 464 (4th Cir. 1996). Examples of arbitrary marks include "Camel cigarettes" and "Apple computers." *Id.*

48. *See* Kelly-Brown v. Winfrey, 717 F.3d 295, 307 (2d Cir. 2013) (quoting Polaroid Corp. v. Polorad Elecs. Corp., 287 F.2d 492 (2d Cir. 1961)); Int'l Ass'n of Machinists v. Winship Green Nursing Ctr., 103 F.3d 196, 201 (1st Cir. 1996).

49. *See supra* notes 37–42 and accompanying text; *see also* 1–2 LALONDE, *supra* note 26, § 2.01.

50. For example, patent, copyright, and trade secret licenses have been important assets in the growth of the computer industry. Robert L. Tamietti, *Technology Licenses Under the Bankruptcy Code: A Licensee's Mine Field*, 62 AM. BANKR. L.J. 295, 296 (1988) (stating that patents, copyrights, and trade secrets have been instrumental in the development of the computer industry).

51. *See* 9 NORTON & NORTON, *supra* note 18, § 177:37. "An intellectual property license often lies at the core of a debtor's business," and the essence of the business itself may be the right to use the license in connection with the licensee's goods and services. *Id.*

52. *See id.*

The Lanham Act authorizes the licensing of trademarks, acknowledging that related companies may validly enter into a trademark licensing agreement.[53] A trademark licensing agreement provides a licensee with the right to use a trademark that is associated with specific products or services in a particular field within a designated geographic area in which the licensor is not currently using the trademark.[54] A trademark licensor who grants a license to a licensee retains an interest in the mark and does not transfer all of its rights in the mark through the licensing agreement.[55] For instance, if a licensee acquires any goodwill through the use of a license, all of these benefits will be passed along to the licensor.[56]

In seeking to strengthen the impact of its brand, a trademark licensor will often include several important terms in its trademark licensing agreement. One fundamental element of a trademark licensing agreement is the identification of the scope of rights that the licensee will receive through the agreement.[57] This provision identifies whether the license is exclusively licensed to one licensee or licensed nonexclusively to multiple licensees.[58] Under an exclusive license, even the licensor itself might not be permitted to use the license.[59] In a nonexclusive license, the licensor may still use the trademark on the products or services covered by the licensing agreement and may license the trademark to others.[60] Exclusive licenses are particularly beneficial to a licensor because exclusive licenses tend to command higher royalty rates in comparison to nonexclusive licenses.[61] Furthermore, the goods and services offered under the trademark in an exclusive licensing agreement tend to consist of a higher level of quality than those licensed under a nonexclusive licensing agreement.[62]

An additional element of a trademark licensing agreement is the compensation clause.[63] Under the compensation clause, a trademark owner

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53. *See* 15 U.S.C. § 1055 (2006).

54. *See* Nguyen, *supra* note 14, at 1275; *see also* 3 J. THOMAS MCCARTHY, TRADEMARKS AND UNFAIR COMPETITION § 18:1 (4th ed. 1996) (stating that a trademark license is a "limited permit to another to use the trademark" (internal quotation marks omitted)).

55. *See* Exxon Corp. v. Oxxford Clothes, Inc., 109 F.3d 1070, 1076 (5th Cir. 1997).

56. *See* Bunn-O-Matic Corp. v. Bunn Coffee Serv., Inc., 88 F. Supp. 2d 914, 923 (C.D. Ill. 2000).

57. *See* R. Charles Henn Jr. et al., *Trademark Licensing Basics*, *in* KILPATRICK TOWNSEND & STOCKTON LLP, INTELLECTUAL PROPERTY DESK REFERENCE 69, 70–71 (6th ed. 2011), *available at* http://www.kilpatricktownsend.com/~/media/Files/Publications/IPDeskRefVolume6.ashx.

58. *Id.* at 70.

59. *Id.*

60. *Id.*

61. *Id.* at 70–71; *see also Royalty Rates*, IDEA BUYER (May 1, 2013), http://www.ideabuyer.com/news/royalty-rates/.

62. *See* Henn Jr. et al., *supra* note 57, at 70–71.

63. *Id.* at 71; *see also* Michael W. Rafter et al., *Avoiding an "Accidental" Franchise in U.S. Trademark Licensing*, INTABULLETIN (Int'l Trademark Ass'n, New York, NY), Jan. 15, 2013, at 12, 13, *available at* http://www.inta.org/INTABulletin/Documents/INTABulletinVol68No02.pdf.

may receive a flat fee or a royalty based on the use of the trademark.[64] Royalties are typically based on net sales,[65] and royalty rates are often determined based on several factors including the trademark's valuation.[66]

Two other important elements of a trademark licensing agreement are the licensing term and quality control provisions.[67] The licensing term provision states the duration of the license, allowing for either a fixed term of use or indefinite use.[68] Once the term has elapsed, use of the licensed trademark by the former licensee will constitute trademark infringement.[69]

Quality control, in which the licensor is obligated to control the quality of the products and services offered under the trademark, is also important in any trademark licensing agreement.[70] If a trademark licensor does not maintain sufficient control over the goods and services licensed under the trademark, the license may be considered a "naked" or "uncontrolled" license.[71] Trademark owners have a strong incentive to maintain the quality of licensed goods, because a "naked" or "uncontrolled" license may constitute the owner's abandonment of the trademark.[72]

A trademark owner may benefit from licensing its trademarks in several ways. By licensing its trademark to another company, the trademark owner can gain increased revenue through royalty fees without the burdens of producing and advertising the product.[73] Moreover, a trademark licensor can build the goodwill of its trademark by allowing the licensee to use the mark.[74]

The United States is a leading worldwide market for licensed merchandise.[75] In 2009, the U.S. market accounted for $83.15 billion

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64. *See* Henn Jr. et al., *supra* note 57, at 71.

65. *Id.*; *see also* Joshua Kaufman, *Royalty Rates: Not As Simple As You May Think!*, http://www.jjkaufman.com/articles/royaltyrates.htm (last visited Sept. 20, 2013) ("[G]enerally, royalty rates are based on a net figure.").

66. *See* GREGORY J. BATTERSBY & CHARLES W. GRIMES, LICENSING ROYALTY RATES § 1.02 (2008) (noting that intellectual property may be valued based on market valuation).

67. *See* Henn Jr. et al., *supra* note 57, at 72.

68. *See id.*

69. *See id.*

70. *See* Nguyen, *supra* note 14, at 1280.

71. *See* Kevin Parks, *Naked Is Not a Four-Letter Word: Debunking the Myth of the "Quality Control Requirement" in Trademark Licensing*, 82 TRADEMARK REP. 531, 534 (1992). In the absence of quality control, several detrimental effects might result, including the production of goods bearing the same mark but consisting of varying degrees of quality and consumer confusion or deception. *See id.*

72. *See id.*; *see also* Daniel K. Hampton, *Trademark Owners Beware: "Naked" Licensing Without Quality Control Can Result in Abandonment of Your Mark*, HOLLAND & KNIGHT (Sept. 24, 2002), http://www.hklaw.com/publications/Trademark-Owners-Beware-Naked-Licensing-Without-Quality-Control-Can-Result-In-Abandonment-of-Your-Mark--09-24-2002/.

73. *See* Nguyen, *supra* note 14, at 1276.

74. *See* 2 STEPHEN P. LADAS, PATENTS, TRADEMARKS, AND RELATED RIGHTS 1127 (1975).

75. *See Licensed Merchandise Sales Worldwide Down 10.8 Percent in '09: Properties from Chanel to Coca-Cola, Bakugan to Nate Berkus Span the Globe in Search of New Profit Opportunities*, EPMCOM.COM (June 1, 2010), http://www.epmcom.com/public/Licensed_Merchandise_Sales_Worldwide_Down_108_In_09_Properties_From_Chanel_To_CocaCol

worldwide, which totaled 56 percent of global sales of licensed products.[76] In addition, U.S. public companies own more than $8 trillion in intellectual capital, which includes patents, trademarks, and copyrights.[77] This provides strong support for the contention that intellectual property is "a lever for growth and innovation" in the economy.[78] In the United States, well-known brands such as the Walt Disney Company have benefitted as their brand names have grown in value and companies have become increasingly willing to spend large amounts of money to license their brands.[79]

Trademark licenses are particularly valuable sources of revenue for owners of the mark.[80] Thus, trademark owners typically devote considerable amounts of money to advertising and promoting their trademarks.[81] A trademark's value is largely derived from its distinctive, rare characteristics, as well as its selling power.[82]

Trademark licenses may also be essential to the thriving business of a licensee. Because the trademark owner has an entrenched reputation for quality and goodwill generated from its brand name, the licensee is able to profit from the use of the trademark.[83] If a licensor rejects the license in

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76. *See id.* Despite holding the top ranking for licensed merchandise worldwide, however, U.S. sales of licensed merchandise dropped by 11.6 percent between 2008 and 2009. *See id.*

77. Joff Wild, *Introduction: The Year It All Changed*, INTELL. ASSET MGMT., http://www.iam-magazine.com/issues/Article.ashx?g=f2e4b566-561e-4fca-b46b-330b79ccb2c8 (last visited Sept. 20, 2013).

78. *Id.*

79. *See Intellectual Property Licensing in the US Industry Market Research Report Now Available from IBISWorld*, PRWEB (July 18, 2012), http://www.prweb.com/releases/2012/7/prweb9709974.htm [hereinafter *Intellectual Property Licensing*]. In 2010, the Walt Disney Company was the top-ranked global licensing company, with a reported $28.6 billion in total retail sales of licensed merchandise. *See* Tom Lisanti, *Top 125 Global Licensors*, LICENSE! GLOBAL, May 2011, at T3, T3, *available at* http://www.rankingthebrands.com/PDF/Top%20125%20Global%20Licensors%202011,%20License%20Global.pdf. The second-ranked company, Iconix Brand Group, generated $12 billion in retail sales of licensed merchandise in 2010—less than half of the revenue generated by the Walt Disney Group. *See id.*

80. *See* David J. Franklyn, *The Apparent Manufacturer Doctrine, Trademark Licensors and the Third Restatement of Torts*, 49 CASE W. RES. L. REV. 671, 681 (1999) (stating that during the explosion of American industry in the early 1900s, it became evident that trademark licensing might allow companies the ability to increase the diversity of their products and maximize profits); Mahaffey-Dowd, *supra* note 6, at 425 ("[A] prominent trademark is often the most valuable asset of a company.").

81. *See* Mahaffey-Dowd, *supra* note 6, at 425 (stating that owners of famous trademarks often spend millions of dollars with the goal of promoting the mark and building an "instant association" between the mark and the product in consumers' minds). Several companies spend billions of dollars annually in an attempt to protect their marks. *See id.* at 425 n.15 (noting that in 1996, Proctor & Gamble spent $2.6 billion in advertising its products, while General Motors and Phillip Morris spent $2.37 billion and $2.28 billion, respectively).

82. *See id.* at 425 (citing Frank I. Schechter, *The Rational Basis of Trademark Protection*, 40 HARV. L. REV. 813, 831 (1927)).

83. Gregory J. Battersby & Charles W. Grimes, *Merchandising Revisited*, 76 TRADEMARK REP. 271, 272 (1986) (noting that by placing a widely recognized trademark on

bankruptcy, this decision may have disastrous consequences for the business of a licensee.[84] Thus, the risks associated with rejection of a trademark licensing agreement may threaten the health of a business that is engaged in economically efficient and profitable business practices.[85]

B. Treatment of Executory Contracts Under the Bankruptcy Code

This section addresses the intersection of intellectual property law with bankruptcy law in the context of § 365 of the Bankruptcy Code. It begins by describing the fundamental goals and policies underlying bankruptcy law. It then considers a debtor's avoiding powers under the Code. Finally, this section concludes by examining § 365 of the Code and the results that follow from the rejection of executory contracts in bankruptcy.

1. Goals and Policies of Bankruptcy Law

Bankruptcy law has several fundamental goals. These goals include securing the prompt and efficient settlement of bankruptcy estates within a reasonable period of time,[86] placing the bankrupt individual's property under the control of the court for distribution among creditors,[87] and protecting creditors from one another.[88] Bankruptcy law also seeks to enable debtors to obtain a fresh start with full opportunity to shed burdensome obligations and carry on their businesses in a financially stable manner as soon as possible.[89] Another important policy underlying the Bankruptcy Code is the consolidation of all matters relating to a bankruptcy case into one court, rather than conducting the litigation of matters in a piecemeal fashion.[90]

The Bankruptcy Code was designed to resolve a debtor's affairs rather than to hide them.[91] The Report of the Commission on the Bankruptcy

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property, a manufacturer may successfully create instant demand for his goods due to the goodwill that is already associated with the property); *see also Intellectual Property Licensing*, *supra* note 79 (stating that a licensee benefits from trademark licenses that allow the licensee to put names like "Disney" or "Nike" on its products due to increased exposure, loyalty from customers, and ability to charge a premium to customers).

84. David M. Jenkins, *Licenses, Trademarks, and Bankruptcy, Oh My!: Trademark Licensing and the Perils of Licensor Bankruptcy*, 25 J. MARSHALL L. REV. 143, 146 (1991) (stating that if a licensee's entire business depends on a trademark license, the licensor's rejection may destroy the licensee's business); Scott W. Putney, *Bankruptcy Code v. Lanham Act and Controlled Licensing*, 80 TRADEMARK REP. 140, 155 (1990) (acknowledging that a licensee's business might be destroyed due to the rejection of a trademark license).

85. *See* Jenkins, *supra* note 84, at 146.

86. Katchen v. Landy, 382 U.S. 323, 328–29 (1966).

87. *In re* First Cent. Fin. Corp., 377 F.3d 209, 217 (2d Cir. 2004) (quoting MacArthur Co. v. Johns-Manville Corp., 837 F.2d 89, 91 (2d Cir. 1988)).

88. Young v. Higbee Co., 324 U.S. 204, 210 (1945).

89. Nicholas v. United States, 384 U.S. 678, 687 (1966) (stating that the policy behind Chapter 11 is the "ultimate rehabilitation of the debtor"); *see also In re* Chalasani, 92 F.3d 1300, 1310 (2d Cir. 1996).

90. *In re* Lazar, 200 B.R. 358, 369 (Bankr. C.D. Cal. 1996).

91. *See In re* PRS Ins. Grp., Inc., 274 B.R. 381, 385 (Bankr. D. Del. 2001).

Laws of the United States identified the primary function of the bankruptcy system as maintaining uniformity and order in the open credit economy despite a debtor's difficulties repaying its debts to creditors.[92] The Report further identified free access to the bankruptcy process by both the debtor and creditor,[93] equitable treatment of claims asserted by creditors,[94] deterrence against fraudulent conduct,[95] and enhanced knowledge regarding the outcomes of bankruptcy cases[96] as goals of the bankruptcy process.

The Bankruptcy Code is codified as Title 11 of the United States Code.[97] Currently, the Bankruptcy Code includes nine Chapters: 1, 3, 5, 7, 9, 11, 12, 13, and 15.[98] Of particular relevance to this Note are Chapter 5, which concerns creditors, the debtor, and the estate,[99] and Chapter 11, which addresses the restructuring and reorganization of businesses.[100]

Under Chapter 11, the primary purpose of bankruptcy proceedings is the successful rehabilitation of the debtor.[101] Thus, maximizing the value of the estate is of paramount importance in Chapter 11 proceedings.[102] Although rehabilitation of the debtor is a crucial goal in the reorganization process, creditors may not be disadvantaged in the preservation of the debtor's business.[103]

Traditionally, bankruptcy courts have been considered courts of equity[104] that enjoy broad equitable powers.[105] As an equitable court, a bankruptcy

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92. H.R. DOC. NO. 93-137, pt. 1, at 69 (1973).

93. *Id.* at 75.

94. *Id.* at 76.

95. *Id.* at 82.

96. *Id.* at 83.

97. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, § 101, 92 Stat. 2549 (1977).

98. *See In re* Trusted Net Media Holdings, LLC, 550 F.3d 1035, 1039 (11th Cir. 2008).

99. 11 U.S.C. §§ 501–699 (2006).

100. *See id.* §§ 1101–1200.

101. *See, e.g.*, NLRB v. Bildisco & Bildisco, 465 U.S. 513, 527 (1984); *In re* Bonner Mall P'ship, 2 F.3d 899, 915 (9th Cir. 1993); *In re* Conroe Forge & Mfg. Corp., 82 B.R. 781, 784 (Bankr. W.D. Pa. 1988); *In re* Killian Co., 19 B.R. 789, 790 (Bankr. N.D. Iowa 1982).

102. *See In re* Shoen, 193 B.R. 302, 318 (Bankr. D. Ariz. 1996); *In re* Nite Lite Inns, 17 B.R. 367, 370 (Bankr. S.D. Cal. 1982) (stating that the purpose of the Code is to facilitate "the restructuring of debt and preservation of economic [value] rather than [the] dismantling of the estate").

103. *See In re* Keeley & Grabanski Land P'ship, 460 B.R. 520, 538 (Bankr. D.N.D. 2011).

104. *See, e.g.*, Granfinanciara v. Nordberg, 492 U.S. 33, 81 (1989) ("[B]ankruptcy courts are inherently proceedings in equity." (internal quotation marks omitted)); Bank of Marin v. England, 385 U.S. 99, 103 (1966) (noting the presence of an "overriding consideration that equitable principles govern the exercise of bankruptcy jurisdiction"); Pepper v. Litton, 308 U.S. 295, 308 (1939) (stating that, in exercising its equitable jurisdiction, the bankruptcy court has not only the power but the duty to see that injustice or unfairness is not done); *In re* Exquisito Servs., Inc., 823 F.2d 151, 155 (5th Cir. 1987); *In re* Chinichian, 784 F.2d 1440, 1443 (9th Cir. 1986).

105. *See, e.g.*, *In re* Ranch House of Orange-Brevard, Inc., 773 F.2d 1166, 1169 (11th Cir. 1985) (refusing to limit a bankruptcy court's power to utilize the equitable doctrines of estoppel and waiver); Gregory Germain, *Due Process in Bankruptcy: Are the New Automatic Dismissal Rules Constitutional?*, 13 U. PA. J. BUS. L. 547, 561 (2011) ("It often has been said that bankruptcy courts are courts of equity, and they often have interpreted broadly their powers to do what is right and equitable.").

court may devise novel remedies in circumstances in which those at law are inadequate.[106] The traditional equitable powers of bankruptcy courts are codified in § 105 of the Bankruptcy Code.[107]

2. Elusive Debtors: Skirting Obligations Under the Code Through the Use of an Avoiding Power

The Bankruptcy Code provides that a trustee may set aside or avoid certain obligations of the debtor, including liens on the debtor's property and transfers of property belonging to the debtor or the estate.[108] The avoidance power does not refer to the right of a debtor to payment. Instead, it provides a remedy to the trustee that invalidates otherwise legal transactions due to the bankruptcy execution process.[109] A trustee may only use an avoiding power that is expressly specified in the Bankruptcy Code.[110]

In practice, the avoidance power serves several important functions. A debtor's avoiding power significantly enhances the debtor's ability to gain a fresh start.[111] Moreover, the avoiding power prevents insolvent parties from disposing of their assets prior to the beginning of the bankruptcy period.[112] Thus, the avoiding power thwarts the depletion of the bankruptcy estate by a debtor, thereby protecting creditors from debtors who seek to give away their remaining assets for little or no value.[113]

In exercising its avoiding powers, a trustee must utilize its discretion regarding whether avoidance of a particular lien or other transfer is a prudent economic decision.[114] Moreover, the trustee must consider the interests of the debtor's creditors in utilizing its avoiding powers; the avoidance power should only be used for the benefit of creditors.[115]

While the debtor may use its avoiding power in several different contexts specified in the Bankruptcy Code,[116] the rejection of an executory contract does not constitute the use of an avoiding power.[117] Once a debtor rejects an executory contract, the licensee receives a remedy for breach of the

106. *See Chinichian*, 784 F.2d at 1443.

107. *In re* Searles, 70 B.R. 266, 272 (D.R.I. 1987). Section 105 states that a bankruptcy court "may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of [the Bankruptcy Code]. . . . This subsection shall not be interpreted to exclude bankruptcy judges . . . from its operation." 11 U.S.C. § 105(a), (c) (2006).

108. *See* 11 U.S.C. §§ 363(n), 506(d), 544–45, 547–49, 553(b), 724(a).

109. *In re* Morning Treat Coffee Co., 77 B.R. 62, 65 (Bankr. M.D. La. 1987).

110. *See In re* Ozark Rest. Equip. Co., 816 F.2d 1222, 1229–30 (8th Cir. 1987).

111. 9 NORTON & NORTON, *supra* note 18, § 56:26.

112. *In re* Hodge, 220 B.R. 386, 392 (D. Idaho 1998).

113. *Id.*

114. *See In re* Chattanooga Wholesale Antiques, Inc., 67 B.R. 899, 902 (Bankr. E.D. Tenn. 1986).

115. *See In re* MortgageAmerica Corp., 714 F.2d 1266, 1275–76 (5th Cir. 1983).

116. *See supra* note 108 and accompanying text.

117. *See In re* Drexel Burnham Lambert Grp., Inc., 138 B.R. 687, 700 n.20 (Bankr. S.D.N.Y. 1992) (stating that the rejection of an executory contract avoids the debtor's commitment to perform the contract but does not constitute an avoiding power akin to the power found in §§ 544 and 545 of the Code).

contract, often in the form of a pre-petition, general unsecured claim against the bankrupt estate.[118] However, rejection of an executory contract does not have any effect on the continued existence of the contract, and does not terminate the contract in any fashion.[119] Therefore, rejection itself does not constitute an avoiding power, although bankruptcy law's avoiding powers may operate to terminate rights in property stemming from a contract.[120]

3. Rejection of Executory Contracts in Bankruptcy

Under § 365 of the Bankruptcy Code, a debtor-in-possession may choose to either assume or reject an executory contract.[121] If a debtor assumes an executory contract, then performance under the contract continues without interruption and the rights between the contracting parties remain undisturbed.[122] A debtor's assumption of an executory contract allows the debtor, in its efforts for rehabilitation from other burdensome obligations, to enjoy the benefits of a contract that will be advantageous to its estate.[123]

Under § 365(g)(2), if an assumed executory contract is breached, then the breach is treated as occurring at the time of the breach rather than pre-petition.[124] Therefore, a damages claim arising from the breach is treated as an administrative claim, which gives priority to the nondebtor over the debtor's other creditors.[125] Administrative claims are meant to encourage meaningful participation by creditors in the reorganization process following a debtor's Chapter 11 filing.[126]

Under § 365(a), a debtor may also reject an executory contract.[127] If a debtor rejects an executory contract, § 502(g)(1)–(2) states that rejection acts as a breach of contract for which the remedy given to the nondebtor is damages.[128] The Code's treatment of executory contract rejection as a claim for damages enables the debtor to transfer the rights it previously held

118. *See* Michael T. Andrew, *Executory Contracts Revisited: A Reply to Professor Westbrook*, 62 U. COLO. L. REV. 1, 16 (1991).

119. *Id.*

120. *Id.* at 17.

121. *See* 11 U.S.C. § 365(a) (2006). A debtor's decision to assume or reject any executory contract will be "subject to the court's approval." *See id.* If an executory contract is assumed or rejected, the entire contract must be assumed or rejected; partial assumption or rejection is not permitted under the Bankruptcy Code. *See In re* CellNet Data Sys., Inc., 327 F.3d 242, 249 (3d Cir. 2003) (stating that the election to assume or reject an executory contract is an "all-or-nothing proposition").

122. *See* LAWRENCE P. KING ET AL., COLLIER ON BANKRUPTCY ¶ 365.03[2] (15th ed. 1996). Generally, an estate will assume a contract when it will receive a net benefit from performance of the contract. An estate will therefore assume a contract when the cost to the debtor of performing its obligations under the contract is less than the value of the benefits that the nondebtor is obligated to provide to the debtor. *See* Andrew, *supra* note 118, at 3.

123. *In re* Norquist, 43 B.R. 224, 225 (Bankr. E.D. Wash. 1984).

124. *See* 11 U.S.C. § 365(g)(2).

125. Andrew, *supra* note 118, at 3.

126. *See In re* AmFin Fin. Corp., 468 B.R. 827, 831 (Bankr. N.D. Ohio 2012).

127. 11 U.S.C. § 365(a).

128. *See id.* § 502(g)(1)–(2).

to the highest bidder.[129] Thus, by permitting the debtor to reject an executory contract in bankruptcy, the debtor is given the power to replace the nondebtor's contractual rights to the executory contract with a pre-petition, general unsecured claim for ensuing damages under § 502(g) of the Code.[130] Because the Bankruptcy Code places the nondebtor in the position of an unsecured creditor, the nondebtor will have a difficult time collecting the total amount of its damage claim and—depending on both the unsecured property remaining in the estate and the creditor's priority relative to other unsecured creditors—will instead likely only receive a limited amount of its total claim.[131]

The Code's recognition of the right of a debtor to reject an executory contract furthers several fundamental objectives of bankruptcy law.[132] First, rejection permits a debtor to gain relief from burdensome restrictions imposed upon it by the rejected contract.[133] Second, the rejection of an executory contract promotes two fundamental purposes of reorganization under Chapter 11 of the Bankruptcy Code: to avoid the liquidation of a debtor's assets, and to preserve the jobs and economic value generated by the debtor's business operations.[134]

In furtherance of these goals, § 365 of the Bankruptcy Code permits a debtor-in-possession or trustee of a debtor's estate to assume or reject any executory contract or unexpired lease held by the debtor.[135] However, rejection may not occur under this provision unless the contract is executory.[136] If the contract is not executory, the debtor may not reject it in bankruptcy.[137] In addition, if an executory contract is not assumed pursuant

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129. *See* Jeffrey R. Seul, Comment, *License and Franchise Agreements As Executory Contracts: A Proposed Amendment to Section 365 of the Bankruptcy Code*, 59 U. COLO. L. REV. 129, 146 (1988).

130. *See* 11 U.S.C. § 502(g); *see also In re* Holmes Envtl., Inc., 287 B.R. 363, 389 (Bankr. E.D. Va. 2002) (stating that a debtor that rejects an executory contract may be rewarded because rejection leaves the nondebtor with a general unsecured claim against the debtor).

131. *See* Seul, *supra* note 129, at 146–47; *see also In re* Chipwich, Inc., 54 B.R. 427, 429 (Bankr. S.D.N.Y. 1985) (stating that, as provided in 11 U.S.C. § 502(g), "a claim resulting from the rejection of an executory contract does not give rise to a priority expense of administration").

132. For a discussion of the fundamental objectives that underlie bankruptcy doctrine, see *supra* Part I.B.1.

133. Tamietti, *supra* note 50, at 299; *see also* Noreen M. Wiggins, *The Intellectual Property Bankruptcy Protection Act: The Legislative Response to* Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc., 16 RUTGERS COMPUTER & TECH. L.J. 603, 603–04 (1990) (stating that an executory contract imposes substantial burdens on a debtor, reducing the likelihood that the debtor will succeed in obtaining a fresh start and paying its creditors, and that rejection allows the debtor to satisfy the maximum amount of debts possible).

134. Tamietti, *supra* note 50, at 299.

135. *See* 11 U.S.C. § 365(a).

136. *See* 9 NORTON & NORTON, *supra* note 18, § 46:57 (stating that a trustee or debtor-in-possession may not reject a contract unless the contract is executory).

137. *See id.*

to § 365 of the Code, the executory contract will not become an asset of the estate.[138]

Several types of contracts have been deemed executory under the Bankruptcy Code, including gas and oil leases,[139] franchise agreements,[140] partnership agreements,[141] and collective bargaining agreements.[142] To determine whether a contract is executory, courts must look beyond the Bankruptcy Code. The Code does not explicitly define the term "executory contract,"[143] although the legislative history of § 365 does broadly address the term.[144] Specifically, Congress observed that there is no precise definition of executory contracts,[145] but noted that executory contracts are often understood to be agreements in which unperformed obligations remain due, to some extent, for the parties on both sides of the contract.[146]

To determine whether a contract is executory such that it may be assumed or rejected in bankruptcy, most courts consider whether both sides still owe one another performance to some extent,[147] and whether the failure of either party to perform its promised obligations would comprise a material breach, excusing performance of the other party.[148] Thus, a contract will be deemed executory only if both parties still have material obligations that they have yet to perform.[149] To be material, a breach must involve a failure to perform an act so important to the contract that leaving the act unperformed disregards an important purpose of the contract.[150] If either party has rendered full performance, leaving only the payment of money due from the nonperforming party, the contract is executed rather than executory.[151] Therefore, if one of the parties has performed all

138. *In re* Qintex Entm't, Inc., 950 F.2d 1492, 1495 (9th Cir. 1991) (stating that an executory contract will not become property of a debtor's estate unless it is assumed by the trustee in a timely manner).

139. *See In re* Wilson, 69 B.R. 960, 963 (Bankr. N.D. Tex. 1987).

140. *In re* Tirenational Corp., 47 B.R. 647, 651 (Bankr. N.D. Ohio 1985) (stating that it is well established that a franchise agreement is an executory contract under § 365); *see also In re* Rovine Corp., 6 B.R. 661, 666 (Bankr. W.D. Tenn. 1980).

141. *In re* Silver, 26 B.R. 526, 529 (Bankr. E.D. Pa. 1983).

142. *See* Int'l Bhd. of Teamsters v. IML Freight, Inc., 789 F.2d 1460, 1462 (10th Cir. 1986).

143. 31 SAMUEL WILLISTON & RICHARD A. LORD, A TREATISE ON THE LAW OF CONTRACTS § 78:39 (4th ed. 1990).

144. *See* H.R. REP. NO. 95-595, at 347 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6303.

145. *Id.*

146. *Id.* The Supreme Court has adopted an identical definition of the term "executory contract." *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 522 n.6 (1984).

147. *See* H.R. REP. NO. 95-595, at 347.

148. *See* 31 WILLISTON & LORD, *supra* note 143, at § 78:39; *see also* Vern Countryman, *Executory Contracts in Bankruptcy*, 57 MINN. L. REV. 439, 460 (1973). Most courts have applied this test to determine if a contract is executory. *See, e.g.*, *In re* S. Pac. Funding Corp., 268 F.3d 712, 715 (9th Cir. 2001); Gallivan v. Springfield Post Rd. Corp., 110 F.3d 848, 851 (1st Cir. 1997).

149. *See In re* Qintex Entm't, Inc., 950 F.2d 1492, 1495 (9th Cir. 1991).

150. *See In re* Holmes Envtl., Inc., 287 B.R. 363, 390 (Bankr. E.D. Va. 2002).

151. *See In re* Kmart Corp., 290 B.R. 614, 617 (Bankr. N.D. Ill. 2003). A contract is not executory if a contracting party's sole obligation remaining under the contract is the payment

material obligations under the contract, it is unlikely that the contract will be deemed executory, and the debtor will not be permitted to reject the contract.[152]

Before approving the rejection of an executory contract, courts will also require the trustee or debtor-in-possession to demonstrate that rejection will benefit the estate.[153] To decipher whether rejection will be beneficial to the estate, courts begin with the proposition that a decision by a bankrupt party must be given deference under the business judgment rule.[154] The business judgment rule states that courts should refrain from interfering with decisions reached by corporate directors regarding affairs that are within their business judgment unless the directors have acted in bad faith or with gross abuse of discretion.[155] The rule applies in the bankruptcy context to provide that a bankrupt party's decision should be shown deference unless it is made in bad faith or with gross abuse of business discretion.[156]

Not all executory contracts may be rejected under the Bankruptcy Code. While § 365(g)(1) provides for a damages remedy for the nondebtor following the rejection of an executory contract, § 365 also exempts certain types of contracts from rejection under the Code.[157] For example, certain types of intellectual property licensees receive special protection under § 365(n).[158] However, the Bankruptcy Code does not contain a specific provision that explicitly addresses the rejection of executory trademark licensing agreements.[159] Although the Code exempts certain forms of intellectual property from rejection under § 365(n), the Code's definition of intellectual property does not include trademarks.[160]

C. Lubrizol *and Congress's Response in Passing the IPLBA*

This section summarizes the Fourth Circuit's holding in *Lubrizol* and considers Congress's swift response in enacting the IPLBA. The section begins by discussing the reasoning behind the Fourth Circuit's decision in *Lubrizol*. It then examines the content of the IPLBA as well as the justifications supporting its enactment. Finally, this section explores the legislative history accompanying the IPLBA and the reasons Congress chose to exclude trademarks from coverage under the Act.

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of money. *See Holmes*, 287 B.R. at 390; *In re* Zenith Labs., Inc., 104 B.R. 667, 672 (Bankr. D.N.J. 1989).

152. *See* 9 NORTON & NORTON, *supra* note 18, § 46:57.

153. *See In re* Prestige Motorcar Gallery, Inc., 456 B.R. 541, 544 (Bankr. N.D. Fla. 2011).

154. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 523 (1984) (stating that the business judgment rule is the traditional test).

155. *See* Lubrizol Enters., Inc. v. Richmond Metal Finishers, Inc., 756 F.2d 1043, 1047 (4th Cir. 1985).

156. *See id.*

157. *See* 11 U.S.C. § 365 (2006).

158. *See id.* § 365(n). For a full discussion of the special treatment that licensees of intellectual property receive under the Bankruptcy Code, see *infra* Part I.C.2.

159. Richard Lieb, *The Interrelationship of Trademark Law and Bankruptcy Law*, 64 AM. BANKR. L.J. 1, 36 (1990).

160. *See supra* note 11 and accompanying text.

1. *Lubrizol*: A Harsh Result for Licensees

The Bankruptcy Code treats the rejection of an executory contract as a breach of contract for which the nondebtor receives a pre-petition unsecured claim for damages.[161] In *Lubrizol*, the Fourth Circuit described the consequences of the rejection of an intellectual property license in bankruptcy for the licensee of a licensed technology.[162] Richmond Metal Finishers (RMF) entered into a contract with Lubrizol that provided Lubrizol with a nonexclusive license to use RMF's metal-coating process.[163] Under the contract, RMF owed Lubrizol several ongoing duties, which included notifying Lubrizol of any patent infringement suits against it, and any other use or licensing of the metal-coating process.[164] RMF also was required, under a most favored nations clause, to reduce royalty rates under the agreement if the rates agreed upon with another licensee were lower than those RMF required Lubrizol to pay.[165] In exchange, Lubrizol was obligated to keep track of and pay royalties for the use of the metal-coating process.[166]

Before Lubrizol had used the RMF technology, RMF filed for bankruptcy pursuant to Chapter 11 of the Bankruptcy Code.[167] Under § 365(a), RMF sought to reject the licensing agreement with Lubrizol.[168] The bankruptcy court determined that the contract between the parties was an executory contract and that the rejection of the contract would be advantageous to RMF.[169] The district court reversed, stating that the contract was not executory and rejection of the contract would not be advantageous to the bankrupt party.[170]

On appeal, the Fourth Circuit held that the technology licensing agreement was an executory contract because both sides had unperformed obligations that remained due to some extent.[171] The court, applying Professor Countryman's test for determining whether a contract is executory,[172] concluded that the licensing agreement was executory because RMF owed Lubrizol the ongoing duties of informing Lubrizol of any further licensing of the metal-coating process, and decreasing Lubrizol's royalty rate in the event that RMF granted more favorable rates to any subsequent licensees.[173] RMF also owed Lubrizol the contingent

161. *See* 11 U.S.C. § 365(g)(1).
162. *See* 756 F.2d 1043 (4th Cir. 1985).
163. *Id.* at 1045.
164. *Id.*
165. *Id.*
166. *Id.*
167. *Id.*
168. *Id.*
169. *Id.*
170. *Id.*
171. *Id.*
172. *See* Countryman, *supra* note 148; *see also supra* note 148 and accompanying text.
173. *Lubrizol*, 756 F.2d at 1045.

duties of providing notice of and defending patent infringement suits.[174] A contingent obligation may still render a contract executory under § 365.[175]

The *Lubrizol* court also concluded that Lubrizol had not performed a material obligation owed to RMF, because Lubrizol owed RMF the ongoing obligation of accounting for and paying royalties for the entirety of the agreement.[176] This promise required Lubrizol to deliver written quarterly sales reports and keep books of account.[177] Because Lubrizol entered into a promise that was more substantial than simply owing debt to another, it rendered the contract executory at the critical time.[178]

The court next decided whether rejection of the executory contract under § 365 would be advantageous to the bankrupt party.[179] In deciding whether rejection would benefit the estate, the court applied the business judgment rule.[180] The court determined that the debtor exercised sound business judgment in its decision to reject the executory contract.[181]

In analyzing RMF's rejection of the intellectual property licensing agreement with Lubrizol, the court concluded that RMF was entitled to "deprive Lubrizol of all rights to the process."[182] Essentially, the court treated rejection as a breach of contract. As a remedy for the breach, the court held that § 365(g) entitles a nonbreaching party to monetary damages rather than specific performance, regardless of whether or not such a remedy would typically be given following the breach of an intellectual property licensing agreement.[183] In reaching this decision, the *Lubrizol* court stressed that the legislative history of § 365(g) clearly established that the purpose of § 365(g) is to allow the licensee to recover only a damages remedy.[184] The *Lubrizol* decision thus prompted deep concerns for

174. *Id.* at 1046.

175. *See In re* O.P.M. Servs., Inc., 23 B.R. 104, 117 (Bankr. S.D.N.Y. 1982) (holding that the duty to defend an infringement suit renders a contract executory as to the promisor).

176. *Lubrizol*, 756 F.2d at 1046.

177. *Id.*

178. *Id.* Notably, a contract is not executory if the contract simply requires a party to pay money to the other party. *See In re* Smith Jones, Inc. 26 B.R. 289, 292 (Bankr. D. Minn. 1982).

179. *Lubrizol*, 756 F.2d at 1046.

180. *See id.* at 1047; *supra* notes 154–56.

181. *Lubrizol*, 756 F.2d at 1047–48.

182. *Id.* at 1048.

183. *See id.* Under this remedy, the nonbreaching party's claim is treated as a pre-petition, general unsecured claim against the breaching party's estate for which the licensee will likely receive only a miniscule proportion of the total damage claim from the distribution to the estate's unsecured creditors. *See supra* notes 128–31 and accompanying text.

184. *Lubrizol*, 756 F.2d at 1048; *see also* H.R. REP. NO. 95-595, at 351 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6303. The *Lubrizol* court further stated that specific performance was not an appropriate remedy because allowing such a remedy would frustrate the primary purpose of rejection under § 365(a). *Lubrizol*, 756 F.2d at 1048. The court therefore refused to embrace a reading of congressional intent that provided for specific performance as a remedy. *Id.* at 1048.

intellectual property licensees, who feared that their licenses might be unilaterally terminated following a debtor's bankruptcy filing.[185]

2. The Intellectual Property Licenses in Bankruptcy Act: Exempting Certain Forms of Intellectual Property from § 365

In response to *Lubrizol*, Congress passed the IPLBA in 1988, which is now codified in § 365(n) of the Bankruptcy Code.[186] The IPLBA provides special treatment for executory contracts involving licensing rights to intellectual property.[187] While § 365(n) expressly includes copyrights and patents under its definition of intellectual property, the Code notably does not recognize trademarks.[188]

The IPLBA prevents a licensor from unilaterally terminating the right of a licensee to continue using an intellectual property license once the licensor rejects the license under § 365(a) of the Code.[189] Instead, when the licensor rejects an intellectual property license, the licensor is no longer required to perform any future obligations, and the licensee may either treat the contract as terminated or elect to continue utilizing the licensed intellectual property.[190]

If the licensee treats the contract as terminated, it may assert a breach of contract claim against the debtor's estate for damages arising from the rejection.[191] Under this option, the licensee would waive all rights to continue utilizing the license, and the breach of contract claim would be treated as a general unsecured claim against the estate.[192]

If upon the licensor's rejection, the licensee elects instead to continue utilizing the licensed intellectual property, § 365(n) permits the licensee to retain all rights under both the contract and any supplementary agreements reached under the contract as they existed prior to the debtor's bankruptcy filing.[193] The legislative history accompanying § 365(n) clarifies that when a licensor rejects an intellectual property license, the licensor is not required

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185. *See* Jeffrey W. Levitan, *'Sunbeam' Protects Trademark Licensees, but Questions Remain*, N.Y.L.J., Sept. 24, 2012, at S8 (stating that *Lubrizol* sent "shock waves throughout the business community" as uncertainty ensued over the effects of bankruptcy on the continued use of intellectual property licenses); Christopher Linden, *Seventh Circuit's Take on Section 365(n) of the Bankruptcy Code: What's the Point?*, WEIL BANKR. BLOG (July 24, 2012), http://business-finance-restructuring.weil.com/executory-contracts/seventh-circuits-take-on-section-365n-of-the-bankruptcy-code-whats-the-point/#axzz26fhKgUw0 (noting that *Lubrizol* "kept the licensee community up at night" because the decision permitted a debtor to strip a licensee of its rights to use an intellectual property license following rejection).

186. *See* Intellectual Property Licenses in Bankruptcy Act, Pub. L. No. 100-506, 102 Stat. 2538 (1988) (codified at 11 U.S.C. § 365(n) (2006)).

187. *See id.*

188. *See id.* § 101(35A); *supra* note 11.

189. *See id.* § 365(n).

190. *Id.* § 365(n)(1)(A), (B).

191. *See id.* §§ 365(g), 502(g).

192. *See id.*

193. *Id.* § 365(n)(1)(B).

to exert any affirmative performance.[194] However, the licensor remains obligated to provide the licensee with access to existing intellectual property without interfering with the licensee's rights to the property.[195]

3. Concerns Behind the Passage of the IPLBA: Legislative History and Business Justifications

In enacting the IPLBA, Congress acted in response to its concern that *Lubrizol* would have a detrimental effect on technological development.[196] The Senate stressed that intellectual property licensing was crucial to the development of technology and innovation.[197] The Senate further noted that technological development and innovation include research, development, manufacturing, and marketing.[198] These activities require financing and additional refinement that often may only be procured through contributions from people who are not the original innovators.[199] Thus, licensing is often a key mechanism for an original innovator who seeks to reap financial rewards.[200]

The Senate expressed particular concern that licensing agreement instability resulting from § 365 was beginning to introduce undesirable consequences.[201] Licensees, who previously were content to accept licenses granting the licensee the right to use the license, were pressured to demand assignments from licensors, which constituted the transfer of a full ownership interest in the intellectual property.[202] The Senate felt that this shift from licensing to assigning was wasteful, inefficient, and particularly burdensome to small businesses in the technology industry.[203] To combat these concerns, Congress enacted the IPLBA, seeking to clarify that intellectual property licensees retain their rights to use licensed intellectual

194. *See* S. REP. NO. 100-505, at 10 (1988), *reprinted in* 1988 U.S.C.C.A.N. 3200.
195. *See id.*
196. *See id.* at 1–2 (noting that several recent court decisions, including *Lubrizol*, have interpreted § 365 in a way that Congress did not intend, therefore leading to negative consequences for technological development in the United States). Due to the interpretation of § 365 endorsed by *Lubrizol* and subsequent courts, the technological licensing industry began to decline. *See* Jay Lawrence Westbrook, *The Commission's Recommendations Concerning the Treatment of Bankruptcy Contracts*, 5 AM. BANKR. INST. L. REV. 463, 470 (1997) [hereinafter Westbrook, *Commission's Recommendations*] (stating that *Lubrizol*'s impact on the licensing community was "immediate and awful"); *see also* Jay Lawrence Westbrook, *A Functional Analysis of Executory Contracts*, 74 MINN. L. REV. 227, 306–07 (1989) (stating that Congress enacted 11 U.S.C. § 365(n) in response to industry concerns that *Lubrizol* permitted any intellectual property licensor to file for Chapter 11 and reject a perfectly valid license).
197. *See* S. REP. NO. 100-505, at 3.
198. *See id.*
199. *See id.*
200. *See id.*
201. *See id.*
202. *See id.*
203. *See id.* The Senate further declared that the change from licensing to assigning intellectual property licenses constituted a sincere threat to the creative process associated with technological innovation in the United States. *See id.*

property and that these rights cannot be unilaterally terminated following a debtor's rejection of a license in bankruptcy under § 365.[204]

Congress had several goals in mind in passing the IPLBA. Through the Act, Congress aimed to benefit licensees by encouraging the continued practice of technology licensing, and by ensuring that an intellectual property licensee is not stripped of its rights under the contract following a licensor's rejection.[205] Congress also sought to benefit licensors by permitting debtors to reject executory contracts while also allowing them to encourage other parties to continue to engage in business with them following bankruptcy—something these parties would otherwise likely refuse to do.[206] Furthermore, Congress enacted the IPLBA in response to *Lubrizol*'s effects on the willingness of licensees to contract with companies in financial distress.[207]

While Congress responded quickly to *Lubrizol* "in support of the intellectual property license as a vehicle for furthering America's technology industry,"[208] the omission of trademarks from the IPLBA's listed definition of intellectual property[209] called into question whether trademark licensees should be afforded the same protections that copyright and patent licensees are provided under the Act.

In enacting § 365(n), Congress considered including trademarks within the scope of the section's protections, noting that the rejection of trademark licenses was worrisome because of *Lubrizol* and other courts' interpretation of § 365.[210] Rather than include trademark licenses under the definition of intellectual property, however, Congress decided not to address the concern, stating that it could not reach a decision on this matter "without more extensive study."[211] Instead, Congress chose to postpone action and allow bankruptcy courts, through the exercise of their equitable powers, to craft a resolution to this issue.[212]

Several other reasons supported Congress's decision to exclude trademarks from protection under the IPLBA. For one, Congress was concerned that the IPLBA would constrain technological development that

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204. *See id.* at 1.

205. *See* Michael J. Shpizner, *Congress Passes New Legislation Protecting Licensees of Intellectual Property*, 71 J. PAT. & TRADEMARK OFF. SOC'Y 177, 179 (1989).

206. *See In re* Chateaugay Corp., 10 F.3d 944, 954–55 (2d Cir. 1993).

207. *See* Wiggins, *supra* note 133, at 606–07 (stating that *Lubrizol* caused companies to become increasingly careful and thorough in checking the financial status of potential licensors, particularly if the intellectual property license comprised a large percentage of the licensee's earnings).

208. *See* Shpizner, *supra* note 205, at 178.

209. *See supra* note 11 and accompanying text; *see also* S. REP. NO. 100-505, at 5 ("[The IPLBA] does not address the rejection of executory trademark, trade name or service mark licenses by debtor-licensors.").

210. *See* S. REP. NO. 100-505, at 5.

211. *See id.*

212. *See id.*; *see also In re* Matusalem, 158 B.R. 514, 516 (Bankr. S.D. Fla. 1993) (interpreting the legislative history accompanying § 365(n) as signifying that "the ball is back in the Court's court").

is more closely associated with patents and other intellectual property.[213] In addition, the Senate Report further indicates that Congress felt that agreements to license trademarks are unique, because they rely heavily on the licensor's quality control of products and services sold under the trademark.[214]

II. THE FOURTH AND SEVENTH CIRCUITS SPLIT: POST-REJECTION RIGHTS RETAINED BY TRADEMARK LICENSEES

Part II examines the circuit split between the Fourth and Seventh Circuits concerning whether a trademark licensee may continue to retain the right to use the license following rejection. This Part begins by addressing the position articulated by *Lubrizol* and subsequent courts, in which rejection of an intellectual property license extinguishes the licensee's right to continue utilizing the license. It concludes by considering viewpoints that contrast with *Lubrizol*, primarily focusing on the reasoning articulated by the Seventh Circuit in the *Sunbeam* decision.

A. The Fourth Circuit: Rejection Extinguishes a Licensee's Right To Continue Utilizing Licensed Technology

This section first discusses the rationale underlying *Lubrizol* and other decisions reached prior to Congress's enactment of the IPLBA. It then considers the judicial interpretation of the rights retained by trademark licensees following rejection in light of *Lubrizol* and the enactment of the IPLBA.

1. *Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc.* and Other Pre-IPLBA Cases

In *Lubrizol*, the Fourth Circuit held that a licensor's rejection of a patent license constituted a breach of contract for which the licensee was entitled to a pre-petition claim for damages rather than specific performance.[215] The *Lubrizol* court determined that a licensor of an intellectual property license may reject the license in bankruptcy, thereby eliminating the right of the licensee to continue utilizing the licensed technology.[216] The court also noted that rejection of licensing contracts as executory imposes severe

213. *See* S. REP. NO. 100-505, at 2–5. *But see* Jenkins, *supra* note 84, at 160–61 (asserting that this justification is inadequate because trademarks serve an equally important function in the economy, and a licensee's loss of trademark licensing rights also has a detrimental effect on the development of both technology and industry).

214. *See* S. REP. NO. 100-505, at 2–5. *But see* Jenkins, *supra* note 84, at 161 (stating that a licensor's obligation of quality control is not relevant to the IPLBA's exemption of trademarks, because Congress chose to protect patent licensees under the Act even though patent licensing agreements also often require duties on the part of the licensor). For further discussion of a licensor's quality control duties under trademark licensing agreements, see *supra* notes 70–72.

215. *See* Lubrizol Enters., Inc. v. Richmond Metal Finishers, Inc., 756 F.2d 1043, 1048 (4th Cir. 1985). For an in-depth discussion of the *Lubrizol* decision, see *supra* Part I.C.1.

216. *See Lubrizol*, 756 F.2d at 1048.

burdens on contracting parties.[217] The court further acknowledged that allowing rejection in these types of cases might result in a general chilling effect on technology licensing because potential licensees might have serious reservations about entering into deals with companies facing financial difficulties.[218]

However, the court stated that equitable considerations—such as the chilling effect of rejection—are not relevant to the analysis of executory intellectual property agreements.[219] Rather, the court held that technology licensees do not receive any special treatment under the Code,[220] concluding that such licensees "share the general hazards created by § 365 for all business entities dealing with potential bankrupts."[221]

Lubrizol profoundly impacted subsequent decisions relating to the rejection of intellectual property agreements,[222] such as *In re Logical Software, Inc.*[223] In this case, Logical Software, Inc. (Logical) entered into a software licensing agreement with Infosystems Technology Inc. (ITI), granting ITI the exclusive rights of distribution for its LOGIX technology on certain computers.[224] The relationship between the companies became problematic, which precipitated Logical's Chapter 11 filing to relieve itself of the burdens stemming from the contract between the parties.[225]

Relying heavily on *Lubrizol*, the bankruptcy court held that Logical was permitted to reject the agreement because Logical exercised its sound business judgment.[226] The court applied the business judgment rule despite the fact that ITI's development and marketing of the licensing agreement accounted for all of its earnings.[227] Despite the high likelihood that rejection would destroy the licensee's business,[228] the court cited *Lubrizol* in support of its decision permitting the rejection of the license, noting that *Lubrizol* obviates any analysis of equitable considerations.[229]

Subsequent decisions have applied *Lubrizol* in the trademark licensing context in support of the conclusion that § 365 is meant to exclude trademarks from its protection. In one such decision, *In re Chipwich, Inc.*,[230] the Bankruptcy Court for the Southern District of New York interpreted § 365 prior to Congress's enactment of § 365(n).[231] On

217. *See id.*
218. *See id.*
219. *See id.*
220. *See id.*
221. *Id.*
222. *See* Wiggins, *supra* note 133, at 613 (noting that *Lubrizol* has been significantly relied upon regardless of Congress's amendment to the Bankruptcy Code in § 365(n)).
223. 66 B.R. 683 (Bankr. D. Mass. 1986).
224. *Id.* at 684.
225. *Id.* at 685.
226. *Id.* at 687.
227. *See id.* at 685. ITI also completely overhauled the structure of its business due to its reliance on the LOGIX license. *See id.*
228. *See* Wiggins, *supra* note 133, at 613.
229. *See Logical Software*, 66 B.R. at 687.
230. 54 B.R. 427 (Bankr. S.D.N.Y. 1985).
231. *See id.*

September 20, 1983, Chipwich, Inc. (Chipwich) entered into a licensing agreement with Farmland Dairies, Inc. (Farmland), in which Farmland was given an exclusive license in the United States to produce, sell, and distribute eggnog and flavored milk under the "Chipwich" trademark.[232] Eight days later, the companies entered into a similar agreement in which Farmland was given worldwide rights to sell and distribute a dairy shake product under the "Chipwich" trademark.[233] After Chipwich filed for bankruptcy, it sought to reject the two licenses because Farmland was not operating at a satisfactory level under the licenses, and Chipwich felt that it would be more lucrative to allow additional companies to utilize the rights to the license.[234]

The court first sought to determine whether the contract between the parties was executory under § 365(a).[235] The court concluded that the contract was executory as to both parties because both parties had material obligations that they had not yet performed.[236]

Next, the court considered whether Chipwich was entitled to reject the executory contract.[237] Citing *Lubrizol*, the court held that Farmland was permitted to treat the rejection of the contract as a breach for damages under § 365(g) and § 502(g).[238] The court stressed that there was no showing that the damages incurred by Farmland would be disproportionate to the benefits accrued by the debtor and the estate's general creditors by shedding this burdensome obligation.[239] Therefore, the debtor was permitted to terminate the licensee's rights to utilize the trademark on its goods.[240]

2. Post-IPLBA: Reasoning by Negative Implication To Exclude Trademarks from Protection

Following the *Lubrizol* and *Chipwich* decisions, Congress enacted the IPLBA in 1988.[241] In applying § 365(n), courts have routinely relied on the plain language of the provision, reasoning by negative inference that trademarks should not be included under the protections of § 365, rather

232. *Id.* at 428.
233. *Id.*
234. *Id.* at 429.
235. *See id.*
236. *Id.* at 430. Chipwich had the continuing obligations to notify Farmland of any infringements of the licensed trademarks, to ensure that any such infringements did not continue, and to indemnify Farmland for any damages resulting from such suits. *See id.* In addition, Farmland had the continuing duty to pay royalties to Chipwich for the entirety of the agreement. *See id.*
237. *See id.* at 430–31.
238. *Id.* at 431.
239. *See id.*
240. *Id.*
241. Intellectual Property Licenses in Bankruptcy Act, Pub. L. No. 100-506, 102 Stat. 2538 (1988) (codified at 11 U.S.C. § 365(n) (2006)). For a detailed discussion of the IPLBA, see *supra* Part I.C.2.

than delving further into equitable considerations relating to rejection of trademark licenses.[242]

In *In re Centura Software Corp.*,[243] the Bankruptcy Court for the Northern District of California reasoned by negative inference to conclude that the IPLBA was not meant to extend protection to trademark licensees following the rejection of the license in bankruptcy.[244] In *Centura*, Raima Corporation (Raima U.S.) licensed the trademarks associated with its software products to Raima UK Limited (Raima U.K.) for use in the United Kingdom market.[245] A merger soon followed, in which Centura Software Corporation (Centura U.S.) acquired all of the rights to Raima U.S.'s software and trademarks.[246] Approximately two years later, Centura U.S. filed a Chapter 11 petition, terminating the trademark agreement with Raima U.K. because Raima U.K. had not paid the minimum licensing fees.[247]

In seeking to determine whether the licensee may continue to utilize the license after the rejection of a trademark licensing agreement, the court noted the absence of any reported cases purporting to directly interpret § 365(n) in the context of the rejection of trademark licensing agreements.[248] However, the court asserted that the plain language of § 365(n) indicates that the provision is not meant to include trademark licenses.[249]

To support its conclusion that the plain language of the IPLBA excludes trademark licenses from its protection, the court resorted to an interpretation of §§ 365(n) and 101(35A).[250] The court explained that § 365(n) allows the licensee to retain its rights if the rejected license is intellectual property.[251] However, § 101(35A) states that intellectual property "means" several different types of intellectual property, but does not include trademarks in this listed definition.[252] Therefore, the court stated that Congress's decision to use the "more limiting term 'means' instead of 'includes'" demonstrated that Congress acted deliberately in only extending protection to the forms of intellectual property explicitly enumerated under § 101(35A).[253]

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242. *See In re* Exide Techs., 607 F.3d 957, 966 (3d Cir. 2010) (Ambro, J., concurring) (stating that "courts have reasoned by negative inference" that Congress's omission of trademark licenses from § 365(n) signified Congress's intent for *Lubrizol* to control following a debtor's rejection of a trademark license).

243. 281 B.R. 660 (Bankr. N.D. Cal. 2002).

244. *Id.* at 669.

245. *Id.* at 663.

246. *Id.*

247. *Id.*

248. *Id.* at 669.

249. *Id.*; *see also In re* Old Carco LLC, 406 B.R. 180 (Bankr. S.D.N.Y. 2009) (asserting that the Bankruptcy Code does not recognize trademarks as intellectual property).

250. *See Centura*, 281 B.R. at 669–70.

251. *See id.* at 669; *see also* Intellectual Property Licenses in Bankruptcy Act, Pub. L. No. 100-506, 102 Stat. 2538 (1988) (codified at 11 U.S.C. § 365(n) (2006)).

252. *Centura*, 281 B.R. at 669. For the complete definition of "intellectual property" contained in § 101(35A), see *supra* note 11.

253. *Centura*, 281 B.R. at 669–70.

Although the court acknowledged that the legislative history accompanying § 365(n) might indicate that Congress embraced the consideration of equitable factors with respect to trademark rejection, it concluded that an inquiry into the legislative history was unnecessary because the language of § 365(n) is unambiguous.[254] Thus, while noting that its decision may result in harsh consequences for the licensee, the court held that a licensee may not continue to utilize a trademark once the license has been rejected.[255]

Similarly, in *In re HQ Global Holdings*,[256] the Bankruptcy Court for the District of Delaware considered the effects resulting from a licensor's decision to reject executory trademark licensing agreements. HQ Global Holdings, Inc. (HQ Global) sought to reject licensing agreements that it had entered into with franchisees that granted the franchisees exclusive use of trademarks, trade names, and logos.[257] In interpreting § 365 in conjunction with § 101(35A), the court concluded that trade names and trademarks were deliberately excluded from the Code's definition of intellectual property.[258] Therefore, the franchisees were not protected under § 365(n) and were left with only a claim for damages resulting from rejection under § 365(g)(1).[259] As a consequence, the franchisees' rights to use the marks were extinguished.[260]

B. Casting Aside Lubrizol*: The Seventh Circuit Expands the Rights of Trademark Licensees Following Rejection*

This section examines viewpoints that oppose *Lubrizol*'s contention that rejection of an intellectual property license extinguishes the licensee's rights under the contract. It begins by explaining the role that equitable considerations might play in determining the rights that licensees will retain under a contract following rejection of a licensing agreement. It then considers the argument that Congress did not use reasoning by negative implication to withdraw the rights of a trademark licensee to continue utilizing the license following rejection. The section concludes by considering the Seventh Circuit's response to *Lubrizol* in *Sunbeam Products, Inc. v. Chicago American Manufacturing, LLC*.

254. *See id.* at 670.
255. *See id.* at 672–73.
256. 290 B.R. 507 (Bankr. D. Del. 2003).
257. *Id.* at 508.
258. *Id.* at 513.
259. *Id.* The court further stated that because the Bankruptcy Code excludes trademarks from the forms of intellectual property recognized under its protections, *Lubrizol*'s holding controls and the franchisees were no longer permitted to use the trademarks following rejection. *Id.*
260. *Id.*

1. The Role of Equitable Principles in License Rejection

Scholars have widely criticized *Lubrizol*, asserting that it mistakenly confuses rejection with the use of an avoiding power.[261] Because courts have found themselves bound by the plain language of § 365(n) without consideration of policy or equitable factors, the judicial consensus has become that the statute has been applied in an inequitable manner, resulting in harsh consequences for intellectual property licensees.[262] In fact, the IPLBA was enacted in direct response to the inequitable interpretation of § 365 in cases such as *Lubrizol* and *Chipwich*.[263]

In his concurring opinion in *In re Exide Technologies*,[264] Judge Ambro of the Third Circuit considered the importance of equitable considerations in determining whether the rejection of a trademark license terminates the right of the licensee to continue utilizing the license following the rejection.[265] In that case, Exide filed a petition for bankruptcy under Chapter 11 of the Bankruptcy Code, seeking to reject several agreements it had with EnerSys.[266] One of these agreements included a trademark and trade name licensing agreement in which Exide licensed its "Exide" trademark to EnerSys for use in its industrial battery business.[267] Because Exide desired to continue to use the trademark outside of the industrial battery business, Exide agreed to provide EnerSys with an exclusive, royalty-free, indefinite license to use the Exide trademark in the industrial battery business.[268] After ten years of abiding by this agreement, Exide sought to reenter the industrial battery market.[269] EnerSys, however, refused to relinquish control of the Exide trademark.[270] Consequently, in an attempt to regain control of the Exide trademark, Exide filed for bankruptcy under Chapter 11, rejecting the trademark agreement.[271]

The Third Circuit proceeded to analyze whether the contract between the two parties was an executory contract.[272] As noted above, if an agreement is not an executory contract, the debtor is not permitted to reject the contract

261. *See* Sunbeam Prods., Inc. v. Chi. Am. Mfg., LLC, 686 F.3d 372, 377 (7th Cir. 2012), *cert. denied*, 133 S. Ct. 790 (2012) (noting that scholars have "uniformly criticize[d]" *Lubrizol*). For a discussion of the debtor's avoiding powers under the Bankruptcy Code, see *supra* Part I.B.2.

262. *See* Darren W. Saunders, *Should the U.S. Bankruptcy Code Be Amended To Protect Trademark Licenses?*, 94 TRADEMARK REP. 934, 939 (2004); *see also Centura*, 281 B.R. at 673 ("*Lubrizol*'s harsh holding controls.").

263. *See* S. REP. NO. 100-505, at 5 (1988), *reprinted in* 1988 U.S.C.C.A.N. 3200 (stating that rejection of trademark licenses is "of concern because of the interpretation of § 365 by the *Lubrizol* court and others . . . [such as] *In re Chipwich*"). For a discussion of the *Lubrizol* and *Chipwich* analyses of § 365, see *supra* Part II.A.1.

264. 607 F.3d 957 (3d Cir. 2010).

265. *See id.* at 967 (Ambro, J., concurring).

266. *Id.* at 960 (majority opinion).

267. *Id.* at 960–61.

268. *Id.* at 961.

269. *Id.*

270. *Id.*

271. *Id.*

272. *See id.* at 962–64.

under § 365(a) of the Bankruptcy Code.[273] The court concluded that the agreement between Exide and EnerSys did not constitute an executory contract because EnerSys did not have any material obligations that it had yet to perform.[274] Therefore, because the agreement was not executory, Exide was not permitted to reject the contract.[275]

Judge Ambro concurred in the result, but took issue with the bankruptcy court's determination below that rejection of the agreement terminated EnerSys's right to utilize the trademark.[276] Rather, Judge Ambro advocated for the position that rejection of a trademark agreement by a trademark licensor under § 365 does not necessarily rescind or terminate the rights of the licensee to use the trademark.[277]

In the course of his analysis, Judge Ambro considered *Lubrizol*'s interpretation of intellectual property license rejection under § 365.[278] Judge Ambro noted that the *Lubrizol* court acknowledged that its interpretation of rejection under § 365 might cause a chilling effect upon the willingness of parties to enter into contracts with financially unstable businesses.[279] Moreover, Judge Ambro noted that the *Lubrizol* court refused to analyze equitable considerations in examining a contract in which a debtor has rejected an intellectual property license.[280]

Judge Ambro disagreed with this analysis, stating that the court should have used its powers as an equitable court to provide Exide with a fresh start without depriving EnerSys of its rights to utilize the Exide trademark.[281] Thus, according to Judge Ambro, while courts may apply § 365 to provide relief from burdensome duties that may hinder a bankrupt trademark licensor's attempts at reorganization,[282] the court may not use § 365 to permit the licensor to retrieve trademark rights it bargained away. Providing such rights to trademark licensors, Judge Ambro felt, would render "bankruptcy more a sword than a shield, putting debtor-licensors in a catbird seat they often do not deserve."[283]

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273. *See supra* notes 135–38 and accompanying text.

274. *Exide*, 607 F.3d at 964. For a discussion of the material obligations test utilized by the court to determine whether this was an executory contract, see *supra* notes 143–52.

275. *See Exide*, 607 F.3d at 964.

276. *See id.* at 965 (Ambro, J., concurring) (citing *In re* Exide Techs., 340 B.R. 222, 250 (Bankr. Del. 2006)). The bankruptcy court further noted that Congress certainly might have chosen to recognize trademarks under § 365(n) but instead decided not to include them within the Act's protections. Therefore, the court stated that rejection terminates the rights of a trademark licensee to continue utilizing the license, and the licensee is left with an unsecured claim for damages. *Exide*, 340 B.R. at 250 n.40.

277. *See Exide*, 607 F.3d at 965 (Ambro, J., concurring).

278. *See id.* at 965–66. For an expanded discussion of *Lubrizol*, see *supra* Part I.C.1.

279. *Exide*, 607 F.3d at 965 (Ambro, J., concurring) (citing Lubrizol Enters., Inc. v. Richmond Metal Finishers, Inc., 756 F.2d 1043, 1048 (4th Cir. 1985)).

280. *Id.*

281. *Id.*

282. *Id.*

283. *See id.* at 967–68.

Likewise, in *In re Petur U.S.A. Instrument Co.*,[284] the Bankruptcy Court for the Western District of Washington carefully considered the balance of equities in determining whether to permit the rejection of a licensing agreement following the debtor's bankruptcy filing. The debtor, Petur U.S.A. Instruments Co., (Petur U.S.A.), entered into a licensing agreement with Petur Instruments, Ltd. (Petur of Canada), which provided Petur of Canada with the exclusive right to utilize, manufacture, assemble, and sell Petur U.S.A.'s inventions in Canada.[285] Petur of Canada's entire business and income stemmed from the licensing agreement with Petur U.S.A.[286] However, Petur U.S.A. was in financial distress and felt that the agreement between it and Petur of Canada was the primary reason for its financial difficulties.[287] Petur U.S.A. therefore sought to reject the license under § 365.[288]

In response to Petur U.S.A.'s Chapter 11 filing, the court determined that the debtor properly exercised its business judgment in rejecting the licensing agreement because the company decided that rejection would be in the best interest of the company, as well as its creditors.[289] However, the court observed that if it granted Petur U.S.A.'s motion, Petur of Canada would be forced out of business because its entire business depended on the licensing agreement.[290] Thus, relying upon legal as well as equitable considerations, the court refused to authorize the rejection of the licensing agreement between the parties.[291]

In *In re Matusalem*,[292] the Bankruptcy Court for the Southern District of Florida confronted facts similar to those in *Petur*. In *Matusalem*, Matusa, a Cuban manufacturer of high-quality rum, granted a franchise to Licorera, providing it worldwide rights to sell Matusalem rum under Matusa trademarks.[293] Due to purported breaches of the franchise agreement, Matusa sought to terminate the subfranchise agreement, thereby rejecting the trademark licensing agreements.[294]

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284. 35 B.R. 561 (Bankr. W.D. Wash. 1983).
285. *Id.* at 562.
286. *Id.*
287. *Id.*
288. *Id.*
289. *Id.* at 563.
290. *Id.*
291. *Id.* To justify its decision, the court reiterated that it is commonly understood that bankruptcy courts are courts of equity. *Id.* The court stated that permitting rejection of the licensing agreement would not only result in the disappointment of legitimate expectations, but also would ruin an otherwise profitable business. *Id.* The court concluded that destruction of such a business would not be permitted under equitable considerations. *Id. But see In re* Logical Software, Inc., 66 B.R. 683, 687 (Bankr. D. Mass. 1986) (applying the business judgment rule to permit the rejection of a licensing agreement, despite the fact that the licensee derived 100 percent of its earnings from the license and noting that *Lubrizol* does not authorize a balancing of the equities).
292. 158 B.R. 514 (Bankr. S.D. Fla. 1993).
293. *Id.* at 517.
294. *Id.* at 518–19.

Applying equitable principles, the *Matusalem* court determined that in seeking to reject the licensing agreements, Matusa did not exercise sound business judgment.[295] The court reasoned that rejection of the licenses would serve no economic benefit to the debtor's estate or to the unsecured creditors.[296] In addition, the court held that rejection was not permissible because the case was likely filed in bad faith, and rejection would destroy the licensor's business.[297]

2. Reasoning by Negative Implication: An Insufficient Basis for Excluding Trademarks from the IPLBA's Protections

In his concurring opinion in *Exide*, Judge Ambro also disagreed with the practice of utilizing reasoning by negative inference to conclude that, because Congress did not explicitly include trademarks under its § 365(n) protection, *Lubrizol*'s holding controls when a licensor rejects a trademark license.[298] The legislative history of § 365(n) explicitly states that trademarks were not addressed.[299] Instead, Congress postponed action by deferring to the bankruptcy courts to use their equitable powers to craft a resolution.[300]

Moreover, the legislative history notes that in enacting § 365(n), Congress did not intend for any inference to be drawn pertaining to the treatment of executory contracts that do not relate to intellectual property.[301] Judge Ambro noted that this statement may have been included in the legislative history as a result of the recommendation by the National Bankruptcy Conference that the legislative history should contain a caveat that clearly indicates that "no negative inferences are to be drawn

295. *Id.* at 522 (stating that Matusa did not exercise good or even mediocre business judgment).

296. *Id.*

297. *Id.* The court further stated that the debtor had no existing business to reorganize, and that the case represented an effort by the debtor "to obtain vengeance . . . and create a new business on the ashes of the franchisee." *Id.*

298. *See In re* Exide Techs., 607 F.3d 957, 966 (3d Cir. 2010) (Ambro, J., concurring). For a discussion of the district courts' practice of utilizing reasoning by negative inference in support of the *Lubrizol* holding, see *supra* Part II.A.2. Several courts have embraced this reasoning technique in reaching a conclusion regarding the rights retained by a trademark licensee following rejection. *See, e.g.*, *In re* Old Carco, LLC, 406 B.R. 180, 211 (Bankr. S.D.N.Y. 2009) (stating that the Bankruptcy Code does not recognize trademarks as intellectual property, so a debtor's rejection of a trademark license terminates the right of the licensee to use the mark); *In re* HQ Global Holdings, Inc., 290 B.R. 507, 513 (Bankr. D. Del. 2003) (reasoning that because the Bankruptcy Code excludes trademarks from its definition of intellectual property, *Lubrizol* controls and franchisees may not continue utilizing a trademark following rejection); *In re* Centura Software Corp., 281 B.R. 660, 674–75 (Bankr. N.D. Cal. 2002) (observing that because § 365(n) "plainly excludes trademarks," a licensee does not retain any rights in the licensed trademark following rejection).

299. *See Exide*, 607 F.3d at 967 (Ambro, J., concurring) (quoting S. REP. NO. 100-505, at 5 (1988), *reprinted in* 1988 U.S.C.C.A.N. 3200, 3204). For a complete discussion of the legislative history accompanying § 365(n), see *supra* Part I.C.3.

300. *See Exide*, 607 F.3d at 967 (Ambro, J., concurring) (quoting S. REP. NO. 100-505, at 5 (1988), *reprinted in* 1988 U.S.C.C.A.N. 3200, 3204); *supra* Part I.C.3.

301. *See* S. REP. NO. 100-505, at 5.

or should be drawn by courts that, because Congress has legislated in a particular way a licensing agreement, those other agreements that are not within the parameters of the legislation are to be dealt with in any particular way."[302] Judge Ambro therefore concluded that such direct statements of Congress's intent signify that it is unreasonable to construe rejection of a trademark license as yielding the same result as termination of the right to continue using the license.[303]

The Eleventh Circuit's opinion in *Thompkins v. Lil' Joe Records, Inc.*[304] further supports the conclusion that reasoning by negative inference will not justify treating the rejection of a trademark license as extinguishing the rights of the licensee. In *Thompkins*, the court rejected the debtor's argument that the purpose of § 365 is to permit the debtor to effectively rescind the contract, placing the parties back in their precontract positions.[305] Instead, the court asserted that rejection simply frees the estate from its obligation to perform its duties under the contract.[306]

Under this view, rejection does not terminate the rights of both parties under the contract.[307] Equating rejection with the use of an avoiding power would therefore be mistaken.[308] Instead, rejection signifies the estate's decision to refrain from continuing to be bound by the contract because the contract is no longer beneficial to it.[309] The effect of rejection is to provide a remedy to the nondebtor for breach of contract, typically in the form of a general unsecured claim in the bankruptcy case.[310] Rejection does not have

302. *See Intellectual Property Contracts in Bankruptcy: Hearing on H.R. 4657 Before the Subcomm. on Monopolies and Commercial Law of the H. Comm. on the Judiciary,* 100th Cong. 101 (1988) (statement of George Hahn, Esq., National Bankruptcy Conference).

303. *See Exide*, 607 F.3d at 967 (Ambro, J., concurring).

304. 476 F.3d 1294, 1306 (11th Cir. 2007).

305. *Id.*

306. *Id.*; *see also In re* Drexel Burnham Lambert Grp., Inc., 138 B.R. 687, 703 (Bankr. S.D.N.Y. 1992) (stating that rejection does not lead to the disappearance of the contract).

307. Andrew, *supra* note 118, at 22; *see also* Michael T. Andrew, *Executory Contracts in Bankruptcy: Understanding "Rejection*,*"* 59 U. COLO. L. REV. 845, 918 (1988) (stating that the licensee in *Lubrizol* had what appeared to be a valid license and that there was no reason to conclude that the license was terminable or avoidable in any way); Lieb, *supra* note 159, at 36–37 (suggesting that rejection should not allow for trademark licensing rights to be rescinded, but should instead allow the licensee to continue utilizing the trademark).

308. Analyzing rejection under § 365 as the use of an avoiding power is problematic for several reasons. First, the legislative record demonstrates that each time Congress has considered the effects of the avoiding-power-rejection doctrine, it has disapproved the doctrine by enacting specific provisions. Andrew, *supra* note 118, at 11. Second, the legislative record contains no evidence that Congress ever considered, let alone approved, the avoiding-power-rejection doctrine. *See id.* Third, other provisions under § 365 are not interpreted through reasoning by negative implication, as § 365 would have to be interpreted, in order to conclude that trademarks do not fall within the protections afforded by the IPLBA. *See id.* For further discussion of a debtor's avoiding powers under the Code, see *supra* Part I.B.2.

309. *See* Andrew, *supra* note 118, at 22. Rejection is the "estate's way of saying no thank you." *Id.* (internal quotation marks omitted).

310. *See id.* at 16; *see also* Westbrook, *Commission's Recommendations*, *supra* note 196, at 471 (noting that the Code provides that rejection is the equivalent of breach of contract, providing the nondebtor with a pre-petition claim for damages). For a discussion of the

an effect on the contract's continuing existence, and it does not cancel, rescind, or terminate the contract in any fashion.[311]

3. Trademarks Are Intellectual Property: *Sunbeam Products, Inc. v. Chicago American Manufacturing, LLC*

In *Sunbeam Products, Inc. v. Chicago American Manufacturing, LLC*,[312] the Seventh Circuit rejected *Lubrizol*, expressing an alternative view on the rights of an intellectual property licensee following a licensor's rejection of the license in bankruptcy. In *Sunbeam*, Lakewood Engineering & Manufacturing Co. (Lakewood) contracted for the manufacture of its consumer products, including box fans, with Chicago American Manufacturing (CAM).[313] The contract permitted CAM to place Lakewood's trademarks on the completed fans and use Lakewood's patents.[314]

Three months into the contract, Lakewood fell into financial distress and several of its creditors filed an involuntary bankruptcy petition against the company.[315] The Lakewood assets, including the patents and trademarks, were then sold to Sunbeam Products (Sunbeam).[316] Sunbeam did not want the Lakewood-branded fans manufactured by CAM to enter the market, and Lakewood's trustee then rejected the executory part of the CAM contract under § 365(a).[317] Because CAM continued to manufacture and sell the Lakewood-branded fans, Sunbeam filed an action against the company.[318]

The *Sunbeam* court held that a trademark licensee is permitted to continue utilizing a licensed trademark even after the licensor's rejection of the license in bankruptcy.[319] Judge Easterbrook noted that several bankruptcy judges have inferred that Congress codified *Lubrizol* in § 101(35A) with respect to trademarks, because the provision fails to

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remedy provided to nonbreaching parties following rejection, see *supra* notes 128–31 and accompanying text.

311. *See* Andrew, *supra* note 118, at 16; *see also* 9 NORTON & NORTON, *supra* note 18, § 46:24 ("The Bankruptcy Code instructs us that rejection is a breach of the executory contract. It is not avoidance, rescission, or termination." (footnotes omitted)); Westbrook, *Commission's Recommendations*, *supra* note 196, at 471 (noting that the breaching party who rejects the contract may not rescind the contract or retrieve consideration that it has already provided to the nonbreaching party). Several district court cases have also asserted that rejection of an executory contract is not the equivalent of rescission. *See, e.g.*, *In re* Metro Transp. Co., 87 B.R. 338, 344 (Bankr. E.D. Pa. 1988) (holding that rejection of an executory contract does not rescind the contract); *In re* Exec. Tech. Data Sys., 79 B.R. 276, 282 (Bankr. E.D. Mich. 1987) (stating that rejection is not the equivalent of rescission); *In re* Midwest Polychem, Ltd., 61 B.R. 559, 563 (Bankr. N.D. Ill. 1986) (stating that rejection constitutes a breach and not termination of the contract).

312. 686 F.3d 372 (7th Cir. 2012), *cert. denied*, 133 S. Ct. 790 (2012).

313. *Id.* at 374.

314. *Id.*

315. *Id.*

316. *Id.*

317. *Id.*

318. *Id.*

319. *See id.* at 378.

mention trademarks.[320] However, Judge Easterbrook stated that Congress had a contrary intent in excluding trademarks from its definition of intellectual property and that "an omission is just an omission."[321] Rather than intending to exclude trademarks, Congress's limited definition of intellectual property in § 101(35A) signified that § 365(n) has no effect on trademarks.[322]

The *Sunbeam* court refused to rely on equitable grounds in holding that a licensee retains its rights to utilize the license following rejection.[323] Judge Easterbrook declared that a judge may not override the provisions of the Bankruptcy Code by stating that enforcement would lead to inequitable results.[324] Instead, the court stated that rights should depend on the Code's provisions rather than on equitable principles, concluding that *Lubrizol* did not correctly interpret § 365(g).[325]

The *Sunbeam* court began its analysis of the Bankruptcy Code's provisions by noting that outside of bankruptcy, a licensee's right to use the intellectual property does not terminate upon a licensor's breach.[326] The court asserted that by classifying rejection as breach, § 365(g) "establish[es] that in bankruptcy, as outside of it, the other party's rights remain in place."[327] While the debtor is not required to perform an order of specific performance following the rejection, the debtor is obligated to pay damages.[328] Importantly, though, the court stressed that there is no reason to conclude that rejection eliminates any of the rights possessed by the licensee prior to rejection.[329] The court further stated that rejection is not

320. *Id.* at 375.

321. *Id.*

322. *See id.*; *see also* S. REP. NO. 100-505, at 5 (1988), *reprinted in* 1988 U.S.C.C.A.N. 3200 (remarking that the omission of trademarks was designed to permit more time for study regarding whether or not to include trademarks under the Act's protections).

323. *See Sunbeam*, 686 F.3d at 375–76.

324. *Id.* at 375. Judge Easterbrook observed that notions of equity may be unreliable because the meaning of equity may vary depending on the bankruptcy judge, with some judges determining that equity favors the licensee's reliance interests and others believing that equity should favor the interests of creditors. *Id.* at 375–76.

325. *Id.* at 376. Judge Easterbrook was not alone in determining that *Lubrizol* incorrectly understood the application of § 365(g) in relation to rejection under § 365(a). *See id.* No other circuit court had agreed or disagreed with *Lubrizol*'s holding regarding the consequences of rejection on the rights of an intellectual property license holder. *See id.* However, Judge Ambro, in a concurring opinion in *Exide*, also advocated the view that when a contract is rejected under § 365(a), the licensee may still retain the right to utilize the trademark. *See id.* For a discussion of Judge Ambro's concurrence in *Exide*, see *supra* notes 264–83 and accompanying text.

326. *Sunbeam*, 686 F.3d at 376.

327. *Id.* at 377.

328. *Id.*

329. *Id.* In support of this assertion, the court drew an analogy between the rejection of an intellectual property license and the rejection of leases. A bankrupt lessee may reject the lease and pay damages as a result for abandoning the premises. However, rejection does not terminate the lease and does not give the lessor the right to end the tenant's right to possession of the premises. *See id.*

the equivalent of rescission, which returns the parties to the position they were in prior to entering into the contract.[330]

The *Sunbeam* court concluded by noting that scholars widely criticize the *Lubrizol* decision.[331] For instance, one scholar noted that *Lubrizol* might be the best example of the problems that are associated with rejection under the avoiding power doctrine.[332] Moreover, another scholar stated that the most serious consequence of executory contract doctrine has been the use of rejection as an avoiding power, noting that the Fourth Circuit's *Lubrizol* decision is the classic example of such consequences.[333]

III. ROOM FOR ONE MORE? INTERPRETING THE IPLBA AS INCLUSIVE OF TRADEMARK LICENSES

Part III evaluates the Fourth Circuit's reasoning in *Lubrizol* and concludes that this analysis is unpersuasive in light of existing executory contract doctrine. Part III.A contends that an interpretation of the Bankruptcy Code that excludes trademarks from the protections afforded to intellectual property licensees under § 365(n) does not comport with the legislative history or purposes behind the IPLBA's enactment. Part III.B advocates the *Sunbeam* view that rejection should not be equated with the use of an avoiding power. Rather, a trademark licensee should receive the benefits of its bargain following a debtor's rejection of the license under § 365.

A. Protection of Trademark Licensees Comports with a Reading of the IPLBA's Plain Language

The Fourth Circuit analyzed § 365 incorrectly in concluding that rejection of an intellectual property license extinguishes the licensee's right to continued use of the license. Congress therefore acted quickly in codifying § 365(n) to combat the negative impact that *Lubrizol* had begun to create on the intellectual property licensing community.[334] Despite Congress's notable omission with respect to trademarks in its listed definition of intellectual property,[335] there is no evidence in strong support of the contention that Congress intended to exclude trademarks from the protections afforded to intellectual property licensees under the Act.

In analyzing the bankruptcy court cases that postdate *Lubrizol* and the IPLBA, it is clear that several courts have been persuaded by the "reasoning by negative implication" justification in excluding trademarks from

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330. *Id.* (quoting Thompkins v. Lil' Joe Records, Inc., 476 F.3d 1294, 1306 (11th Cir. 2007)).

331. *Id.* The *Sunbeam* Court also stated that *Lubrizol* paid little attention to whether rejection cancels a contract, and spent far too much time addressing the correct way to identify executory contracts to which the rejection power may be applied. *See id.*

332. *See* Andrew, *supra* note 307, at 916.

333. *See* Westbrook, *Commission's Recommendations*, *supra* note 196, at 470.

334. *See supra* notes 196, 201–04, 207–08 and accompanying text.

335. *See supra* note 11 and accompanying text.

protection under the IPLBA.[336] Thus, these courts have taken the position that by excluding trademarks from the listed definition of intellectual property, Congress intended to extend protection under the Act to only those forms of intellectual property explicitly recognized under § 101(35A).[337] Under this view, licensees of forms of intellectual property that are not explicitly listed under the definition of intellectual property are not subject to the IPLBA's protections and, under *Lubrizol*, are stripped of their rights to continue utilizing the licenses following rejection.[338]

This analysis misses the mark for several reasons. First, the legislative history accompanying § 365(n) flatly contradicts this line of argument. The legislative history directly addresses Congress's omission of trademarks from the Act's protections,[339] explaining that additional study was necessary before Congress could decide whether or not to include trademarks within the definition of "intellectual property" under the Code.[340] The legislative history suggests that Congress decided to postpone taking action on the issue, concluding that it should be permitted to develop based on the equitable treatment of the bankruptcy courts.[341] At a minimum, the legislative history supports the conclusion that a decision regarding the protection offered to trademark licensees under the Act was deferred; the legislative history certainly does not support the contention that protection for trademark licensees was denied.

Second, the legislative history in fact provides better support for the contrary view: trademarks should be included under the IPLBA's protections. Because the legislative history states that whether or not protection under the IPLBA should be extended to trademarks is a question best left to the equitable treatment of bankruptcy courts, it appears that Congress intended for equity to play an important role in resolving this issue.

Bankruptcy courts have a long and well-developed history as courts of equity.[342] From a fairness perspective, it would make little sense to conclude that a court of equity would prefer to extinguish the rights of a trademark licensee to continue utilizing a license upon rejection rather than providing the licensee with the option to continue using the license. Trademark licenses are often quite valuable to the business of a licensee,[343] and a rule of law that would deny protection to trademark licensees, thus potentially destroying or severely damaging their businesses,[344] seems far from equitable. In fact, *Lubrizol* itself noted that the consequences of its decision were "harsh," which clearly does not support the view that

336. *See supra* Part II.A.2.
337. *See supra* Part II.A.2.
338. *See supra* Part II.A.2.
339. *See supra* notes 210–14 and accompanying text.
340. *See* S. REP. NO. 100-505, at 5 (1988), *reprinted in* 1988 U.S.C.C.A.N. 3200.
341. *See id.*
342. *See supra* Part I.B.1.
343. *See supra* notes 51–52, 83–85 and accompanying text.
344. *See supra* notes 84–85 and accompanying text.

extinguishing a licensee's right to continue using a license following rejection is equitable.[345] Moreover, several bankruptcy courts have relied upon equitable considerations in holding that a debtor may not reject a licensing agreement, especially when the rejection will severely damage the licensee's business.[346]

Third, the factors prompting Congress's enactment of § 365(n) strongly support a reading of the statute that grants trademark licensees the same protections afforded to licensees of patents and copyrights. Congress enacted the IPLBA in response to the detrimental effects of *Lubrizol* on licensing arrangements, as well as the negative impact of *Lubrizol* on the willingness of companies to enter into agreements with companies in financial distress.[347] These concerns apply with just as much force in the trademark licensing context as they do in copyright and patent licensing.[348] Moreover, trademark licensing is an enormous business and licensing agreements are critical to the financial stability of businesses owned by both licensors and licensees.[349] Given the size of the trademark licensing business, if courts were to interpret § 365(n) as depriving trademark licensees of their bargained-for rights following rejection, detrimental consequences may result for technological development and licensing relations.

B. Courts Should Not Equate Rejection with the Use of an Avoiding Power

The following section reevaluates the Fourth Circuit's contention in *Lubrizol* that the rejection of an executory contract results in termination of the contract. Part III.B.1 contends that courts such as *Lubrizol* have misinterpreted executory contract doctrine in concluding that rejection is the equivalent of an avoiding power. Part III.B.2 suggests an amendment to the Bankruptcy Code in order to clearly establish that trademark licensees retain their rights to use licensed trademarks following a debtor's rejection.

1. Rejection Does Not Terminate Preexisting Rights Under an Executory Contract

In holding that a trademark licensee retains the right to utilize the trademark following rejection,[350] the *Sunbeam* Court noted the widespread criticism associated with the *Lubrizol* opinion.[351] In particular, *Sunbeam* stated that scholars have "uniformly criticized" *Lubrizol* for equating rejection with the use of an avoiding power.[352]

345. *See supra* note 262 and accompanying text.
346. *See supra* notes 284–97 and accompanying text.
347. *See supra* Part I.C.3.
348. *See supra* notes 213–14 and accompanying text.
349. *See supra* Part I.A.3.
350. *See supra* Part II.B.3.
351. *See supra* notes 331–33 and accompanying text.
352. *See supra* note 331 and accompanying text.

When a debtor rejects an intellectual property licensing agreement in bankruptcy, the rights of the licensee do not evaporate.[353] This principle is the crucial idea underpinning the *Sunbeam* analysis and provides a strong justification for the contention that a trademark licensee should retain its right to use a trademark following rejection.[354] Rejection simply frees the estate from the duty to continue performing burdensome obligations under the contract.[355] In addition, a careful look at the legislative record reveals that Congress either has not considered the avoiding-power-rejection doctrine or has disapproved of it by enacting specific provisions.[356] Thus, there is ample support for the assertion that a trademark licensee should retain its rights to utilize a licensed trademark following a debtor's rejection.

2. A Proposed Amendment to the Bankruptcy Code

To avoid the negative effects stemming from *Lubrizol* in the trademark context, Congress should amend the Bankruptcy Code in one of two ways. First, and most intuitively, Congress can amend § 101(35A) to explicitly include trademarks under the IPLBA's protections. A second option that Congress might consider is amending the Act to state that rejection is not an avoiding power. Both solutions would put to rest any doubts regarding the treatment that should be given to trademark licenses under § 365(n) following rejection.

CONCLUSION

Trademark licensing is critical to technological development in the United States.[357] Shortly after *Lubrizol*, Congress passed the IPLBA to remedy the negative effects that the Fourth Circuit decision had on technological and economic growth.[358] Congress exempted patents, copyrights, and trade secrets from rejection under § 365(a), but failed to explicitly include trademarks.[359] Instead, Congress postponed consideration of trademarks, leaving the treatment of this form of intellectual property to the equitable discretion of bankruptcy courts.[360]

While many courts have excluded trademarks from coverage under the IPLBA due to reasoning by negative implication,[361] the Act's legislative history and the balance of equities both tip in favor of permitting trademark licensees to retain their rights to use the trademarks following rejection.[362] In addition, executory contract doctrine does not equate rejection of an

353. *See supra* Part I.B.2; *supra* notes 304–11 and accompanying text.
354. *See supra* notes 326, 329 and accompanying text.
355. *See supra* Part I.B.2.
356. *See supra* note 308 and accompanying text.
357. *See supra* Part I.A.3.
358. *See supra* Part I.C.3.
359. *See supra* Part I.C.2.
360. *See supra* notes 210–12 and accompanying text.
361. *See supra* Part II.A.2.
362. *See supra* notes 339–46 and accompanying text.

executory contract with the use of an avoiding power.[363] Given the importance of trademarks in the U.S. intellectual property licensing scheme,[364] the Bankruptcy Code should be amended to either include trademarks under the definition of intellectual property or explicitly provide that rejection does not give rise to an avoiding power.

363. *See supra* notes 116–20, 307–11, 353–56 and accompanying text.
364. *See supra* Part I.A.3.