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Rejection Hurts: Trademark Licenses and the Bankruptcy Code

Section 365 of the Bankruptcy Code empowers debtors to reject burdensome executory contracts. From 1988 until May 2019, the effect of such a rejection on trademark licenses was unclear. The Supreme Court's recent decision in Mission Product Holdings, Inc. v. Tempnology, LLC *settled the matter definitively: all rejections under § 365(g) operate exactly as a breach would outside the bankruptcy context. As such, if the trademark license would allow the licensee to continue using the mark after a breach, the licensee may continue to use the mark after a rejection. While this decision comports with the language of the Code and gives effect to the parties' contracted terms, it may functionally deprive debtors of the ability to reject trademark licenses. The problem lies in trademark law's quality control requirements, which obligate licensors to exert actual control over the trademark's quality. If a debtor-licensor rejects a trademark license and then fails to exert this control—an obligation it should theoretically be relieved of by the rejection—it could face claims of naked licensing and abandonment. Because a successful abandonment claim would render the trademark much less valuable, or even worthless, bankruptcy courts may refuse to approve such a rejection on the grounds that it does not satisfy the business judgment test. As a result, debtor-licensors may be faced with an unsavory decision: pursue a rejection that does not function to relieve the estate of all its obligations, or assume the license. This Note proposes that an equitable solution is only possible with congressional intervention. Specifically, § 365 should be amended to allow licensees to retain (1) an adjusted prepetition claim to damages for breach of contract and (2) the rights and obligations, as set out in the contract's breach provisions, to products already produced or possessed by the licensee and controlled for quality by the licensor at the time rejection is approved. The enactment of this brightline, middle-ground solution would adequately balance party interests, give effect to the parties' negotiated breach terms, and create a more predictable structure for trademark license rejections.*

INTRODUCTION

Imagine you own a small clothing boutique that you inherited from your parents and you want to start carrying new brands of clothing. You notice that the company Ecolothes has a line of environmentally friendly clothing that has been gaining popularity on Instagram, so you decide to reach out to them. You manage to snag a five-year contract with Ecolothes, and shortly thereafter you start carrying their trademarked merchandise. After two years, a scandal breaks on Twitter—the clothes are not quite as environmentally friendly as advertised. Consumers rapidly lose interest. Unfortunately for you, the scandal hits mere days after Ecolothes fulfilled your quarterly order, and your storeroom is full of Ecolothes-branded products you already purchased. Then, the next month, Ecolothes declares bankruptcy, and you receive notice that Ecolothes has made a motion to reject your contract under § 365 of the Bankruptcy Code. Soon thereafter, the bankruptcy judge approves the motion and your contract is rejected. Your lawyer tells you this rejection means you have a claim for damages against Ecolothes, but your main question is whether the rejection means you no longer have the right to sell Ecolothes-branded products—including those you already have. Essentially, you need to know if you have a storeroom full of products you cannot sell.

Section 365 of the Bankruptcy Code allows debtors to "assume or reject any executory contract or unexpired lease" with court approval.[1] This section allows a debtor to excuse itself from certain contracts that are no longer financially feasible or beneficial. Section 365(g) instructs that such a rejection "constitutes a breach . . . immediately before the date of the filing of the petition."[2] That is, once an executory contract is rejected, the court treats it as if the debtor breached the agreement prepetition—just before filing for bankruptcy. Consequently, the counterparty may file a claim for prepetition damages.[3] However, none of this really answers the question: Can you still sell the Ecolothes products you already have in your storeroom?

Until May 20, 2019, the answer depended on your location. A trademark licensee residing in Illinois, Indiana, or Wisconsin could continue to exercise her rights under the contract[4] and sell the products because the U.S. Court of Appeals for the Seventh Circuit held that a rejection only frees the *debtor* from the contract.[5] On the other hand, a trademark licensee residing in Maine, Massachusetts, New Hampshire, Rhode Island, or Puerto Rico could not continue to exercise her rights under the contract, as the U.S. Court of Appeals for the First Circuit held that a rejection extinguishes the licensee's rights *and* the licensor's obligations.[6] In *Mission Product Holdings, Inc. v. Tempnology, LLC*, the Supreme Court resolved this circuit split[7] and held that a rejection under § 365 of the Bankruptcy Code operates just like a breach outside of bankruptcy.[8] As such, you can still sell the Ecolothes products in your

1. 11 U.S.C. § 365(a) (2012).

2. 11 U.S.C. § 365(g)(1). This is the default rule for executory contracts. Subsections (g)(2)–(p) of 11 U.S.C. § 365 establish specialty rules for various types of executory contracts, including unexpired leases of real property and intellectual property licenses.

3. *See* 11 U.S.C. § 502(g) (2012) ("A claim arising from the rejection . . . shall be allowed under subsection (a), (b), or (c) of this section or disallowed under subsection (d) or (e) of this section, the same as if such claim had arisen before the date of filing of the petition."); *see also* 11 U.S.C. § 502(a) ("A claim or interest . . . is deemed allowed, unless a party in interest . . . objects.").

4. Excluding the right to specific performance. Sunbeam Prods. v. Chi. Am. Mfg., LLC, 686 F.3d 372, 377 (7th Cir. 2012) (citing NLRB v. Bildisco & Bildisco, 465 U.S. 513, 531 (1984)).

5. *Id.* at 376–77. The Third Circuit has never directly engaged with this question but indicated support for the Seventh Circuit's approach in *In re Exide Technologies*, 607 F.3d 957, 965 (3d Cir. 2010) (Ambro, J., concurring).

6. Mission Prod. Holdings, Inc. v. Tempnology, LLC (*In re* Tempnology), 879 F.3d 389, 402–03 (1st Cir. 2018), *rev'd*, 139 S. Ct. 1652 (2019).

7. *Compare In re* Tempnology, 879 F.3d at 402–03 (holding a rejection essentially functioned as a rescission), *rev'd*, 139 S. Ct. 1652, *with* Sunbeam Prods. v. Chi. Am. Mfg., LLC, 686 F.3d 372, 376–77 (7th Cir. 2012) (holding a rejection functioned similarly to a breach outside of the bankruptcy context), *cert. denied*, 568 U.S. 1076 (2012). This circuit split was rooted in the courts' understanding of quality-control concerns inherent in trademark protection and a negative inference based on how Congress treated different types of intellectual property when amending the Bankruptcy Code. For a discussion of these issues, see *infra* Section I.C and notes 127–130 and accompanying text.

8. Mission Prod. Holdings, Inc. v. Tempnology, LLC, 139 S. Ct. 1652, 1657–58 (2019).

storeroom as long as the terms of your original contract[9] allow you to continue selling the items after a breach.[10]

This Note proposes that § 365 should be amended to allow trademark licensees to retain (1) an adjusted prepetition claim to damages for breach of contract and (2) any rights and obligations, as set out in the contract's breach provisions, to products already produced or possessed by the licensee and controlled for quality by the licensor at the time rejection is approved. Part I of this Note provides an overview of rejection in the Bankruptcy Code and the difficulties trademark license contracts pose to the use of that power. Part II discusses the various ways lower courts have handled these difficulties and several proposed legislative solutions. Finally, Part III considers the Supreme Court's decision in *Mission Product* and argues that the Court was unable to provide a truly equitable solution because the Bankruptcy Code does not allow for one. This Note ultimately proposes that Congress must codify an equitable solution that protects licensors from claims of trademark abandonment and licensees from a total loss of investment on products already produced or possessed.

I. SETTING THE STAGE: § 365 AND QUALITY CONTROL

The "purpose of the Bankruptcy Code is to grant a 'fresh start' to the 'honest but unfortunate debtor.' "[11] This "fresh start" may be attained not only by individuals but also by business entities. Many businesses use the Bankruptcy Code as a restructuring tool to reorganize their debts and assets to avoid liquidation.[12] One of the many tools the Code provides to these debtors is the power to reject certain contracts. Businesses in Chapter 11 bankruptcy may invoke § 365 to "assume or reject any executory contract [subject to the court's approval]."[13]

This Part sets the stage for our discussion. Section I.A lays out the prerequisites for a rejection: the contract at issue must be executory in nature, and the rejection must pass a business judgment test. Section

9. The Court also noted that there may be cases where state law prohibits the sale. *Id.* at 1662.

10. *See id.* at 1666 (Sotomayor, J., concurring) ("Special terms in a licensing contract or state law could bear on [whether the licensee's rights would survive a breach under applicable nonbankruptcy law].").

11. Marrama v. Citizens Bank of Mass., 549 U.S. 365, 367 (2007) (quoting Grogan v. Garner, 498 U.S. 279, 286–87 (1991)).

12. 1 COLLIER ON BANKRUPTCY ¶ 1.01 (Richard Levin & Henry J. Sommer eds., 16th ed. 2019).

13. 11 U.S.C. § 365(a) (2012). Note that in Chapter 11 bankruptcy, a trustee, rather than the debtor, represents the estate and manages the proceedings. 11 U.S.C. § 323(a) (2012).

I.B discusses the effect such a rejection will have on the parties to an intellectual property licensing agreement. This discussion is rooted in an analysis of *Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc.*,[14] which interpreted the effect of § 365(g) on licensing agreements, and the congressional response in the Intellectual Property Licenses in Bankruptcy Act ("IPBLA"), which enacted § 365(n) to supersede *Lubrizol*.[15] Finally, Section I.C discusses why trademark licenses were excluded from the IPBLA's solution.

A. Prerequisites to Rejection: Executory Contracts and Business Judgment

To approve a rejection, a court must first determine that the contract in question is "executory."[16] Unfortunately, the Code does not define this term.[17] Courts have developed a number of tests to determine whether a contract is executory, with the majority of courts adopting what is known as the "material breach" test.[18] Under this test, a contract is executory if both parties involved have performance obligations remaining, such that a single party's failure to perform is a material breach that relieves the other party of its duty to perform.[19] Thus, the executory nature of a contract depends on the extent of the parties' remaining obligations. If both parties still have duties that

14. 756 F.2d 1043 (4th Cir. 1985), *superseded in part by statute,* 11 U.S.C. § 365(n).

15. Pub. L. No. 100-506, 102 Stat. 2538 (1988) (codified in 11 U.S.C. §§ 101, 365(n) (2012)).

16. 11 U.S.C. § 365(a) (limiting the application of the section to "executory contract[s] [and] unexpired lease[s]"). As an intellectual property license cannot qualify as an unexpired lease, this Note will not discuss the latter.

17. *See* 11 U.S.C. § 101.

18. 1 JAMES M. LAWNICZAK, 1 COLLIER LENDING INSTITUTIONS AND THE BANKRUPTCY CODE ¶ 4.03 (LexisNexis 2d ed.) ("[T]he most popular view is that a contract is 'executory' only if material obligations remain to be performed by both the debtor and the nondebtor party to the contract such that a failure to perform by either would excuse the performance of the other."). Some courts have rejected the material breach test in favor of a more simplistic performance test, a now-disfavored purpose test, or a functional test developed by Professors Westbrook and Andrews. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 522 n.6 (1984) (noting, but not holding, that the general definition of "executory" means both parties have *some* remaining performance obligations), *superseded by statute on other grounds*, 11 U.S.C. § 1113 (2012); *In re* Becknell & Crace Coal Co., 761 F.2d 319, 322 (6th Cir. 1985) (arguing that a contract is executory only if the debtor's purposes for rejection can be achieved through rejection); Simmons Capital Advisors, Ltd. v. Bachinski (*In re* Bachinski), 393 B.R. 522, 543 n.11 (Bankr. S.D. Ohio 2008) (collecting examples from 1988–2006 that show courts in the U.S. Court of Appeals for the Sixth Circuit no longer use the purpose test); Cohen v. Drexel Burnham Lambert Grp., 138 B.R. 687, 708–09 (Bankr. S.D.N.Y. 1992) (using the functional test developed by Professors Westbrook and Andrews to evaluate the executory nature of the contract).

19. Vern Countryman, *Executory Contracts in Bankruptcy: Part I*, 57 MINN. L. REV. 439, 460 (1973). This test is often referred to as the "Countryman test," for its creator. 1 LAWNICZAK, *supra* note 18, ¶ 4.03.

"go[ ] to the root or essence of the contract," then one party's failure to perform those duties would constitute a material breach.[20]

The simplest way to explain the material breach test is through example. Imagine a mortgage contract: if the bank has already advanced the funds to the debtor-mortgagor, the contract is not executory because the debtor-mortgagor's failure to repay the loan cannot relieve the bank of its obligation to advance those funds—the bank has already fulfilled that obligation.[21] On the other hand, imagine an employment contract: if the employer declares bankruptcy partway through the contract, both the employer and the employee have material obligations remaining (the employer is obligated to pay the employee, and the employee is obligated to work), and either party's failure to perform relieves the other.[22]

Despite the popularity of the material breach test, it is unclear whether the test survives *Mission Product Holdings, Inc. v. Tempnology, LLC*. There, the Supreme Court advanced a simpler understanding of executory contracts rooted in the legislative history of § 365. Under this reading, "executory contracts" include any "contract that neither party has finished performing,"[23] that is, any contract where "performance remains due to *some* extent on both sides."[24] This definition expands the scope of executory contracts to include those where parties have only immaterial obligations remaining.[25] However, because the parties in *Mission Product* did not contest the executory nature of their contract, this definition may be dicta.[26]

20. *See* 15 RICHARD A. LORD, WILLISTON ON CONTRACTS § 44:55 (4th ed. 2018) ("Substantial performance is the antithesis of material breach; if it is determined that a breach is material, or goes to the root or essence of the contract, it follows that substantial performance has not been rendered . . . .").

21. *See id.*

22. *Id.*

23. Mission Prod. Holdings, Inc. v. Tempnology, LLC, 139 S. Ct. 1652, 1657 (2019).

24. *Id.* at 1658 (emphasis added) (quoting NLRB v. Bildisco & Bildisco, 465 U.S. 513, 522 n.6 (1984)); *see also* H.R. REP. NO. 95-595, at 347 (1977), *as reprinted in* 1978 U.S.C.C.A.N. 5963, 6303 ("Though there is no precise definition of what contracts are executory, it generally includes contracts on which performance remains extent on both sides.").

25. See, for example, the contract at issue in *In re* Exide Techs., 607 F.3d 957 (3d Cir. 2010), wherein merely immaterial obligations remained for the contract.

26. Mission Prod. Holdings, Inc. v. Tempnology LLC (*In re* Tempnology LLC), 559 B.R. 809 (B.A.P. 1st Cir. 2016) (noting that creditor-licensee only objected to the application of § 365(n), not § 365 in its entirety). The simplest definition of dicta is in opposition to holding. *Black's Law Dictionary* defines obitur dictum as "[a] judicial comment made while delivering a judicial opinion, but one that is unnecessary to the decision in the case and therefore not precedential (although it may be considered persuasive)." *Obiter Dictum*, BLACK'S LAW DICTIONARY (11th ed. 2019). Because the parties in *Mission Product* did not contest that their agreement was executory, the Court's definition of the term was not "[ ]necessary to the decision."

This is not the first time the Supreme Court has advanced this definition. *Mission Product* quotes *NLRB v. Bildisco & Bildisco*, a 1984 case where the parties similarly did not contest the executory nature of the contract.[27] There, the executory contract definition appeared in footnote 6, where Justice Rehnquist explained, "[T]he legislative history to § 365(a) indicates that Congress intended the term to mean a contract 'on which performance is due to some extent on both sides.' "[28] Thus, while the Court has not squarely held what "executory" means, two majority opinions have used the same definition, and the *Mission Product* Court opted to include it in the body of the opinion rather than relegate it to a footnote.[29] This could signal the Court's support for an expansive definition of executory contracts. However, the point remains that the definition was dicta in both *Mission Product* and *Bildisco & Bildisco* because the parties did not contest the nature of the contracts at hand. Further, the material breach test can certainly coexist with this simple definition; proponents argue it simply clarifies to what extent performance is still required.[30]

Under either formulation, intellectual property contracts are typically deemed executory because they include terms that require ongoing obligations for the life of the contract and those obligations are often material.[31] For example, terms that require exclusivity,[32]

27. *Mission Prod.*, 139 S. Ct. at 1656 (quoting *Bildisco & Bildisco*, 465 U.S. at 522 n.6).

28. *Bildisco & Bildisco*, 465 U.S. at 522 n.6 (quoting H.R. REP. NO. 95-595, at 347).

29. *Compare Mission Prod.*, 139 S. Ct. at 1656 (quoting *Bildisco & Bildisco*, 465 U.S. at 522 n.6), *with Bildisco & Bildisco*, 465 U.S. at 522 n.6 (quoting H.R. REP. NO. 95-595, at 347).

30. *See* Jay Lawrence Westbrook, *A Functional Analysis of Executory Contracts*, 74 MINN. L. REV. 227, 236–37 (1989) (noting that the legislative history of § 365 references the material breach test and that courts across the country have adopted it for its clarity).

31. *See* Benjamin Howard, Note, *Reconciling Trademark Law with Bankruptcy Law in License Rejection*, 2014 COLUM. BUS. L. REV. 172, 176–78 (explaining the unique characteristics of licensing agreements that require ongoing obligations). *But see* Lewis Bros. Bakeries Corp. v. Interstate Brands Corp. (*In re* Interstate Brands Corp.), 751 F.3d 955, 964 (8th Cir. 2014) (holding the trademark license agreement had to be considered along with the purchase agreement and was therefore not executory because the debtor-licensor had substantially performed); *In re* Exide Techs., 607 F.3d 957, 962–64 (3d Cir. 2010) (holding that the trademark license at issue was not executory because the debtor's failure to perform its remaining duties would not constitute a material breach under the material breach test).

32. *See, e.g.*, Hayes Lemmerz Int'l v. Epilogics Grp., 531 F. Supp. 2d 789, 802 n.6 (E.D. Mich. 2007) (finding a patent license was executory because it required exclusivity from the licensor and a commercialization schedule from the licensee).

accounting for and payment of royalties,[33] confidentiality,[34] assistance,[35] reporting of certain events,[36] and defense against IP litigation[37] have been used to deem a contract executory. In the context of trademark licenses, terms that require ongoing quality control, which are required under trademark law, often form the basis of a determination that the contract is executory.[38] Parties should not assume, however, that the executory nature of their license is a foregone conclusion. In *In re Exide Technologies*, the Third Circuit held the parties' trademark license was not executory because the licensee "had substantially performed" its obligations.[39] The court reasoned that because the licensee's "performance rendered outweigh[ed] its performance remaining and the extent to which the parties [had already] benefitted [was] substantial," a breach would not be material and the contract therefore was not executory.[40]

Once it is determined that a contract is executory, the judge must decide whether rejection is appropriate using a business judgment test.[41] Under this test, if the rejection or assumption of a contract

33. *See, e.g.*, Lubrizol Enters. v. Richmond Metal Finishers, Inc., 756 F.2d 1043, 1045–46 (4th Cir. 1985) (finding a patent license was executory in part because it required forbearance from the licensor and "written quarterly sales reports and . . . books of account" from the licensee), *superseded in part by statute*, 11 U.S.C. § 365(n) (2012). The requirement that the licensee merely pay royalties is likely not enough to make the agreement executory. *Id.* at 1046 ("[I]f [the licensee] had owed [the licensor] nothing more than a duty to make fixed payments or cancel specified indebtedness under the agreement, the agreement would not be executory as to [the licensee].""). *But see In re* Petur U.S.A. Instrument Co., 35 B.R. 561, 563 (Bankr. E.D. Wash. 1983) (finding a license agreement was executory even though the licensee was only required to pay royalties).

34. *See, e.g.*, RCI Tech. Corp. v. Sunterra Corp. (*In re* Sunterra Corp.), 361 F.3d 257, 264 (4th Cir. 2004) (finding a patent license was executory because both the licensee and licensor were obligated "to maintain the confidentiality of the source code of the software developed by the other").

35. *See, e.g.*, *In re* Petur U.S.A. Instrument Co., 35 B.R. at 563 (finding a license agreement was executory because the licensor was required to "provid[e] product, information and know-how, and consulting services," while the licensee was required to pay royalties).

36. *See, e.g.*, Tech Pharm. Servs. v. RPD Holdings, LLC (*In re* Provider Meds, LLC), 2017 Bankr. LEXIS 166, at *43 (Bankr. N.D. Tex. Jan. 18, 2017) (finding a license agreement was executory because the licensee was required to "release all [existing] infringement claims" against the licensor and the licensor was required to "provide quarterly reports" regarding its use of the patented technology).

37. *See, e.g.*, *In re* Aerobox Composite Structures, 373 B.R. 135, 139 (Bankr. D.N.M. 2007) (holding a license agreement was executory even though all monetary obligations had been paid because the licensor was obligated "to defend the patent against validity challenges of third parties" and the licensee was required to maintain confidentiality and use the product per certain restrictions).

38. For a discussion of quality control, see Section I.C.

39. 607 F.3d 957, 962–64 (3d Cir. 2010).

40. *Id.* at 963.

41. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 523 (1984) (noting that the business judgment test is usually applied to determine if rejection of an executory contract is appropriate), *superseded by statute on other grounds*, 11 U.S.C. § 1113 (2012); Grp. of Institutional Inv'rs v. Chi.,

reflects a reasonable business judgment, it is approved. According to the *Mission Product* Court, a court "will generally approve" assumption if "the contract is a good deal for the estate going forward."[42] On the other hand, a court will generally approve a rejection if escaping the obligations of the contract is a better deal than remaining subject to it. The general rule of thumb is that the rejection or assumption should net a benefit for the estate.[43]

B. The Original Sin: Lubrizol

Once it is determined that a contract is executory and the debtor may reject it using § 365, the court must determine the effect of that rejection on the nondebtor. The power to reject an intellectual property license under § 365 was first recognized by the U.S. Court of Appeals for the Fourth Circuit in its controversial *Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc.* decision.[44] There, the court held the debtor-licensor's rejection of a patent licensing agreement deprived the licensee of *all* rights under the contract, effectively constituting a complete rescission.[45] As a result, the rejected licensee was entitled only to a claim for damages that was treated "the same as if such claim had arisen before the date of the [licensor's] filing of the petition."[46] In other words, the licensee was left with a prepetition claim for damages—a claim that is unsecured, nonpriority, and dischargeable.[47]

Essentially, the *Lubrizol* court held that rejected licensees were only entitled to a claim of damages so low in the hierarchy of claims

Milwaukee, St. Paul & Pac. R.R. Co., 318 U.S. 523, 550 (1943) ("[T]he question whether a [contract] should be rejected and if not on what terms should be assumed is one of business judgment."); *see also* Mission Prod. Holdings, Inc. v. Tempnology, LLC, 139 S. Ct. 1652, 1658 (2019) (acknowledging the use of the business judgment test).

42. 139 S. Ct. at 1658.

43. *But see* Control Data Corp. v. Zelman (*In re* Minges), 602 F.2d 38, 43 (2d Cir. 1979) (arguing that while the business judgment test asks whether rejecting the contract will benefit the estate, the test should be applied flexibly to avoid "substantial injustice" to creditors). Some courts conceive of the business judgment standard in terms of benefit to the general unsecured creditors rather than the estate, but this distinction is simply a reflection of the purpose of a bankruptcy estate, not of a different test. *See In re* Chi-Feng Huang, 23 Bankr. 798, 801 (B.A.P. 9th Cir. 1982) (defining the business judgment test in terms of benefit to the creditors).

44. 756 F.2d 1043, 1046 (4th Cir. 1985), *cert. denied*, Lubrizol Enters., Inc. v. Canfield, 475 U.S. 1057 (1986), *superseded in part by statute*, 11 U.S.C. § 365(n) (2012).

45. *See id.* at 1048.

46. 11 U.S.C. § 502(g)(1) (2012).

47. *See* 11 U.S.C. § 506(a)(1) (defining secured claims to include only those secured by a lien on the debtor's property); 11 U.S.C. § 507 (prioritizing payment of certain types of claims); 11 U.S.C. § 1141(d)(1) (2012) ("[T]he confirmation of a plan discharges the debtor from . . . any debt of a kind specified in section 502(g) . . . .").

that the licensee was likely to receive pennies on the dollar.[48] The court acknowledged the harshness of its decision, saying it "impose[d] serious burdens upon contracting parties" and "could have a general chilling effect upon the willingness of such parties to contract at all with businesses in possible financial difficulty."[49] But the court felt bound to abide by its interpretation of the Bankruptcy Code's text because "Congress ha[d] plainly provided for the rejection of executory contracts," so it was not free to consider the equities of the situation.[50]

When the Supreme Court denied certiorari in *Lubrizol*,[51] Congress stepped in to prevent the Fourth Circuit's precedent from chilling U.S. industry.[52] To this end, Congress passed the IPLBA, which defined "intellectual property" and enacted § 365(n) to govern license rejections.[53] Under the new section, an intellectual property licensee has a choice in the event of a rejection: it can "treat [the] contract as terminated," or it can "elect . . . to retain its rights" as defined by the licensing contract, except for the right to specific performance by the debtor.[54] In effect, § 365(n) gives intellectual property licensees the power to decide if they want to treat the debtor's rejection as a simple breach or as a sort of disengagement in which the licensee elects to continue alone. If a licensee elects the latter option, it retains the right to enforce "negative covenants, such as a covenant not to sue or, in the case of an exclusive license, a covenant not to license others to the technology,"[55] and "to demand that the trustee provide any intellectual property, including an embodiment of the intellectual property, held by the trustee, to the extent provided in the license agreement."[56]

Unfortunately, the post-*Lubrizol* reforms do not apply to trademark licenses: § 101(35A) defines "intellectual property" to

48. Jarrod N. Cone, Note, *A "Sunbeam" of Hope: The Seventh Circuit's Solution Overcoming Disparaging Treatment to Trademark Licensees Under the Bankruptcy Code*, 20 J. INTELL. PROP. L. 347, 358 (2013); Derek I. Hunter, Note, *Nobody Likes Rejection: Protecting IP Licenses in Cross-Border Insolvency*, 47 GEO. J. INT'L L. 1167, 1177 (2016); *see* Anthony Giaccio, *The Effect of Bankruptcy on the Licensing of Intellectual Property Rights*, 2 ALB. L.J. SCI. & TECH. 93, 102 & n.54 (1992) ("[T]he licensee becomes a general unsecured creditor and is not guaranteed to recover a dollar for dollar return for the debtor's breach.").

49. *Lubrizol Enters.*, 756 F.2d at 1048.

50. *Id.*

51. Lubrizol Enters., Inc. v. Canfield, 475 U.S. 1057 (1986) (denying certiorari).

52. *See* S. REP. NO. 100-505, at 1–2 (1988), *as reprinted in* 1988 U.S.C.C.A.N. 3200, 3203 ("Certain recent court decisions interpreting Section 365 have imposed a burden on American technological development that was never intended by Congress in enacting Section 365.").

53. *See* 11 U.S.C. § 101(35A) (2012) (defining the term "intellectual property"); 11 U.S.C. § 365(n) (2012) (governing license rejections).

54. 11 U.S.C. § 365(n)(1)(A)–(B).

55. S. REP. NO. 100-505, at 12, *as reprinted in* 1988 U.S.C.C.A.N. at 3209.

56. *Id.* at 12, *as reprinted in* 1988 U.S.C.C.A.N. at 3209–10.

exclude trademarks.[57] Instead, trademark licenses are governed by § 365(g), which simply states that "the rejection of an executory contract . . . constitutes a breach of such contract."[58] As a result, a straight reading of the statute leaves trademark licensing contracts out of the IPLBA solution and arguably in the same situation as the patent licensing contract in *Lubrizol*.[59] The Senate acknowledged this exclusion in its report, claiming that, while "of concern," trademark licenses could not be handled at the time because they "raise[d] issues beyond the scope of [the] legislation."[60] In other words, Congress was not sure how a rejection would operate in light of trademark law's quality control requirements.[61] Rather than stepping in prematurely, Congress elected to wait it out—hoping "the development of equitable treatment . . . by bankruptcy courts" would offer more guidance.[62]

C. Quality Control and Rejection

Quality control requirements are relatively unique to trademarks. Generally speaking, when one thinks of intellectual property, three main categories come to mind—copyright, patent, and trademark. While this is a useful grouping because it encompasses the majority of intellectual property we encounter in everyday life, it belies the stark difference between copyrights and patents, which are meant to protect creators, and trademarks, which are meant to protect consumers.[63]

The presence of a trademark is meant to guarantee to the consumer that the product meets the publicly known quality standards associated with the brand.[64] The Lanham Act provides that this quality standard must be met even when trademark owners license the right to

57. 11 U.S.C. § 101(35A) (including only intellectual property classified as a "(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").

58. 11 U.S.C. § 365(g).

59. For further discussion on the interplay between the amendments and *Lubrizol*, see discussion *infra* notes 122–130 and accompanying text.

60. S. REP. NO. 100-505, at 5, *as reprinted in* 1988 U.S.C.C.A.N. at 3204.

61. *See id.*

62. *Id.*

63. *See* ALEXANDER I. POLTORAK & PAUL J. LERNER, ESSENTIALS OF INTELLECTUAL PROPERTY: LAW, ECONOMICS, AND STRATEGY 32–33 (2011).

64. *See, e.g.*, 2 ANNE GILSON LALONDE, GILSON ON TRADEMARKS § 6.04 (2018):

> [I]f a restaurant franchisee, for instance, has lower standards of quality than the franchisor has set out, customers who expect the same experience at each franchise will be not only disappointed but also deceived. Thus, in order to prevent public deception, a licensor must retain sufficient control over its licensees' use of the licensed mark.

use aspects of their brand to others.[65] If an owner fails to ensure the licensee meets quality control standards, it risks facing a claim of naked licensing because it has failed to ensure the product does not mislead the public.[66] Because one of the main purposes of trademarks is to prevent consumers from being misled about the quality of a branded product, the charge of naked licensing is quite serious.[67] A successful naked licensing claim can result in a trademark being deemed abandoned.[68] When a trademark is deemed abandoned, the owner loses the ability to assert its rights against another party, including the right to protect the trademark from infringement.[69] In sum, it is of utmost importance to trademark owners that they maintain quality control standards whenever they enter into a licensing agreement.

Despite the mandate that owners maintain quality control over trademarks, the Lanham Act does not define "quality" or "control."[70] In response, courts have adopted various definitions and balancing tests

65. *See* 1 ROGER M. MILGRIM & ERIC E. BENSEN, MILGRIM ON LICENSING § 4.53 (2018) (citing 15 U.S.C. § 1055 (2012) and 15 U.S.C. § 1127 (2012)). "[A] registered mark . . . may be used legitimately by related companies . . . provided such mark is not used in such manner as to deceive the public." 15 U.S.C. § 1055.

66. *See* 2 LALONDE, *supra* note 64, § 6.04 ("If the licensor fails to maintain adequate control, . . . the license is a 'bare' or 'naked' license and the trademark owner faces possible abandonment of its trademark rights and consequently an inability to maintain an infringement action based on those rights."). A claim of naked licensing is most likely to come up in the context of a trademark infringement case. Imagine you own a popular pizzeria, Mario's Pizza, and your brother works as the manager. After five years, your brother approaches you about opening another location. He proposes you franchise the restaurant and let him open a new Mario's Pizza a few towns over. You happily agree and the new Mario's Pizza opens without a hitch. Because you trust your brother to protect the good name of Mario's Pizza and run his location to the same standard he always ran the original, you never check in on the quality of his store or his pizza. Then, directly across the street from your restaurant, your estranged cousin opens a Mario's Pizzeria. Worried about the competition and the confusion the similar name may cause, you sue for trademark infringement. Your cousin, who suspects you have failed to perform adequate quality control, defends and claims you have engaged in naked licensing. If she proves this claim, your trademark may be declared abandonded and she will get to keep Mario's Pizzeria open. For a case with similar facts, see *Taco Cabana International, Inc. v. Two Pesos, Inc.*, 932 F.2d 1113, 1121 (5th Cir. 1991), *aff'd on other grounds*, 505 U.S. 763 (1992).

67. *See* JAY DRATLER JR., LICENSING OF INTELLECTUAL PROPERTY § 11.03 (2019) ("Naked licensing risks forfeiture of legal protection."); 2 LALONDE, *supra* note 64, § 6.04 ("Abandonment of a mark through naked licensing will estop the licensor from asserting any rights to that mark.").

68. *See* TMT N. Am., Inc. v. Magic Tough GmbH, 124 F.3d 876, 887 (7th Cir. 1997) ("[Licensee's] use of the marks . . . may have been so uncontrolled that [the licensor] may have abandoned the marks."). Some scholars use the terms "invalidation" and "forfeiture" in place of "abandonment" to convey the involuntary nature of this result. *See, e.g.*, DRATLER JR., *supra* note 67, § 11.03.

69. *See* 15 U.S.C. § 1115(b)(2) (2012) (terming abandonment a defense against claims of infringement); DRATLER JR., *supra* note 67, § 11.03 (discussing the availability of abandonment as a defense against an infringement claim); 2 LALONDE, *supra* note 64, § 6.04 (same); Irene Calboli, *The Sunset of "Quality Control" in Modern Trademark Licensing*, 57 AM. U. L. REV. 341, 345 (2007) ("Without . . . control, courts [have] considered licenses 'naked' and trademark rights forfeited . . . .").

70. *See* Calboli, *supra* note 69, at 355 (citing 15 U.S.C. § 1055 and 11 U.S.C. § 1127).

over the years.[71] Today, the majority of courts ask whether the licensor exercised actual control over the trademark's quality. If she did, they will uphold the trademark.[72] A minority of courts, however, uphold trademarks in the absence of actual control where the licensor and licensee have a particularly close relationship.[73]

To meet the actual control standard used by most courts, a licensor must have "sufficiently policed and inspected its licensees' operations to guarantee the quality of the products they sold under its trademarks to the public."[74] Thus, even absent contractual provisions governing quality control, a licensor may maintain its trademark by actually exercising control over the quality of the products.[75] Absent this actual control, however, contractual provisions cannot save a licensor from claims of abandonment and naked licensing.[76]

It is unclear how much control courts expect licensors to exercise. Originally conceived in the Second Circuit's 1959 decision in *Dawn Donut Co. v. Hart's Food Stores, Inc.*, the actual control test first asked whether the licensor had "sufficient" control.[77] Since then, courts around the country have continually refined the standard, typically to the benefit of licensors and the continued validity of their trademarks.[78] In 1977, the Fifth Circuit went so far as to hold that "[r]etention of a trademark requires only minimal quality control."[79] Further, some scholars have found that modern courts typically uphold trademarks where the licensor can show "*any* sign of control."[80]

A small number of courts, however, have upheld trademarks absent any indicia of control where the licensor and licensee have an unusually close relationship and the quality of the product remained consistent. In *Land O'Lakes Creameries, Inc. v. Oconomowoc Canning Co.*, the Seventh Circuit refused to hold the licensor's trademark was naked even though the licensee was wholly responsible for quality

71. *See id.* at 364–65 (reviewing courts' handling of the terms over time).

72. *Id.* at 369 (noting that " 'actual' rather than contractual control could support valid licensing").

73. *See* discussion *infra* notes 81–88 and accompanying text.

74. Dawn Donut Co. v. Hart's Food Stores, Inc., 267 F.2d 358, 367 (2d Cir. 1959).

75. *See id.*; *see also id.* at 368 (Lumbard, J., dissenting in part) (agreeing with the majority that a licensor "may in fact . . . exercise[ ] control in spite of the absence of any express grant by licensees of the right to inspect and supervise").

76. *See id.* at 368 (agreeing with the majority that it is actual control, not contractual control, that matters).

77. *See id.* at 367 (majority opinion).

78. *See* Calboli, *supra* note 69, at 369–70 (collecting cases).

79. Ky. Fried Chicken Corp. v. Diversified Packaging Corp., 549 F.2d 368, 387 (5th Cir. 1977).

80. Calboli, *supra* note 69, at 370 (emphasis added).

control.[81] Instead the court reasoned that the licensor's control "should be deemed sufficient" to satisfy the Lanham Act because no quality complaints had been issued over the forty-year arrangement.[82] Likewise, in *Transgo, Inc. v. Ajac Transmission Parts Corp.*, the Ninth Circuit refused to hold that the licensor's trademark was naked on similar grounds.[83] There, the licensor and licensee had worked together for ten years and the licensor considered the licensee "second only to . . . himself in overall knowledge and ability in product development."[84] The court reasoned that the parties' close relationship, the licensor's well-grounded faith in the licensee's quality control standards, and the lack of any quality complaints indicated sufficient quality control.[85] Similarly, in *Taco Cabana International, Inc. v. Two Pesos, Inc.*, the Fifth Circuit argued that "the law requires consistent quality, not [sufficient] policing."[86] There, the court refused to hold naked a technically uncontrolled trademark because the parties were brothers that had previously run the licensing business together and the quality was consistent between the two.[87] The court argued that punishing a licensor "simply for want of all the inspection and control formalities" would violate the purpose of the Lanham Act.[88]

Given the increasingly flexible interpretation of quality control, particularly in instances where the parties have a close relationship, some scholars argue the standard has been reduced to a mere formality.[89] Unfortunately for debtor-licensors, however, it remains to be seen if they could satisfy even that level of control under the current rejection scheme. Under the majority approach, if a debtor uses rejection for its stated purpose—to free itself from performance obligations under the contract—it cannot possibly show minimal actual control postrejection because exercising any level of control would

81. 330 F.2d 667, 670 (7th Cir. 1964). Instead the licensor relied on the licensee's quality control standards. *Id.*

82. *Id.*

83. 768 F.2d 1001, 1017–18 (9th Cir. 1985).

84. *Id.* at 1018.

85. *Id.* at 1017–18.

86. 932 F.2d 1113, 1121 (5th Cir. 1991), *aff'd on other grounds*, 505 U.S. 763 (1992). The court took the length of the parties' relationship as evidence of their close relationship. *Id.*

87. *Id.* at 1117, 1121.

88. *Id.* at 1121.

89. *See* Calboli, *supra* note 69–70; Xuan-Thao Nguyen, *Selling it First, Stealing it Later: The Trouble with Trademarks in Corporate Transactions in Bankruptcy*, 44 GONZ. L. REV. 1, 5 (2009) (arguing that the standard has become so flexible that licensors are often "no longer directly involved in quality control" and instead permissibly "rely on the reputation and expertise of the licesees for the quality control of trademarked products"); Glenn Walberg, *Wrestling Control From The UNICAP Regulations: The Irrelevance of Quality Control in Determining Capitalizable Trademark Royalties*, 16 FLA. TAX REV. 223, 254 (2014) ("[M]odern trademark law and licensing practices suggest that the control language operates as a mere formality in many arrangements.").

require performance.[90] Further, under the minority approach, even if a debtor could establish a close relationship with the licensee, it would not be able to show functional control or consistency if it uses reorganization as an opportunity to change its quality standards (to ensure profitability postbankruptcy).[91] As a result, it is possible that allowing trademark licensees to retain their rights after a rejection would functionally deprive debtor-licensors of rejection power because the risk of trademark abandonment would harm the estate to the extent that the proposed rejection fails the business judgment test.[92] Even if the estate would benefit from the rejection of the specific contract at hand, the debtor may be prevented from doing so by the harms inherent in the threat of abandonment.[93]

II. THE EFFECT OF § 365 REJECTION: VARIOUS APPROACHES

The functional deprivation problem lies at the heart of Congress's decision to omit trademarks from the definition of intellectual property in the Bankruptcy Code.[94] Despite this omission, and consequent exclusion from § 365(n), it seems the Senate was unsatisfied with leaving trademark licenses to *Lubrizol* and § 365(g) long term. As discussed, the Senate Report reflects an intent simply to "postpone" a final decision to allow bankruptcy courts to develop and test equitable solutions.[95] However, this "solution" led bankruptcy courts down different paths, created a circuit split, and ultimately required Supreme Court intervention.

A. Lubrizol *and Its Progeny: Rights Revoked*

To fully understand the recent decision in *Mission Product*, this Note traces the circuit split the Court was confronted with back to the

90. *See* 11 U.S.C. § 365 (2012); Calboli, *supra* note 69, at 368–70.

91. *See* Calboli, *supra* note 69, at 371–73.

92. See *supra* notes 41–43 and accompanying text for a discussion of the business judgment test.

93. *See* Mission Prod. Holdings, Inc. v. Tempnology, LLC (*In re* Tempnology), 879 F.3d 389, 403 (1st Cir. 2018), *rev'd*, 139 S. Ct. 1652:

> The Seventh Circuit's approach . . . would allow [the licensee] to retain the use of Debtor's trademarks in a manner that would force Debtor to choose between performing executory obligations arising from the continuance of the license or risking the permanent loss of its trademarks, thereby diminishing their value to Debtor.

94. *See* S. REP. NO. 100-505, at 5 (1988), *as reprinted in* 1988 U.S.C.C.A.N. 3200, 3204.

95. *Id.*

source: *Lubrizol*.[96] There, the Fourth Circuit held that a debtor-licensor's rejection of an intellectual property licensing contract left the licensee with nothing but an unsecured, prepetition damages claim.[97] Essentially, the court held that the rejection power allowed a debtor-licensor to revoke a contract and deprive the licensee of its rights, even if those rights would have remained if the debtor breached the contract outside the bankruptcy context.[98] When the Supreme Court denied certiorari and the IPLBA omitted trademarks from the new scheme, many argued "that legislators [had] affirmed *Lubrizol*'s holding for trademarks."[99]

Indeed, before the *Mission Product* decision, many bankruptcy courts followed *Lubrizol* and held that the rejection of a trademark license left a licensee with only a prepetition claim for damages. For example, in 1990, the Bankruptcy Court for the District of Rhode Island held that the proper rejection of a trademark licensing agreement "transferred back to the debtor [the license and tradename]."[100] In 2002, the Bankruptcy Court for the Northern District of California held that "[w]hile the result may appear harsh . . . once a license has been rejected, the [licensee] may not continue to use the trademarks."[101] In 2003, the Bankruptcy Court for the District of Delaware held that "[a]s a result of the rejection, [the] affirmative obligation of the [licensor] to allow the [licensee] to use the marks is excused."[102] Similarly, in 2009, the Bankruptcy Court for the Southern District of New York held that a rejection deprives the licensee of its rights under the contract and that this deprivation did not violate the Takings Clause of the Fifth Amendment.[103] The Eighth Circuit seemingly adopted this stance in its 2012 decision, *Lewis Bros. Bakeries v. Interstate Brands Corp.* (*In re Interstate Bakeries Corp.*), but the holding was vacated and reversed en banc on the ground that the contract at issue was not executory.[104]

96. Lubrizol Enters., Inc. v. Richmond Metal Finishers, Inc., 756 F.2d 1043 (4th Cir. 1984), *cert. denied*, Lubrizol Enters., Inc. v. Canfield, 475 U.S. 1057 (1986), *superseded in part by statute*, 11 U.S.C. § 365(n) (2012).

97. *See id.* at 1048; *see also* 11 U.S.C. § 502(g) (2012) (treating a damages claim arising under § 365 "the same as if such claim had arisen before the date of the filing of the petition").

98. *See Lubrizol Enters.*, 756 F.2d at 1048; Westbrook, *supra* note 30, at 309–11.

99. Chandra J. Critchelow, Comment, *A Solution-Based Approach to Rejecting Trademark Licenses in Bankruptcy*, 13 J. MARSHALL REV. INTELL. PROP. L. 623, 637 (2014) (collecting cases).

100. *In re* Blackstone Potato Chip Co., 109 B.R. 557, 562 (Bankr. D.R.I. 1990).

101. Raima UK Ltd. v. Centura Software Corp. (*In re* Centura), 281 B.R. 660, 662 (Bankr. N.D. Cali. 2002).

102. *In re* HQ Global Holdings, Inc., 290 B.R. 507, 513 (Bankr. D. Del. 2003).

103. *In re* Old Carco LLC, 406 B.R. 180, 211 (Bankr. S.D.N.Y. 2009).

104. *See* 690 F.3d 1069, 1072, 1075 (8th Cir. 2012) (holding that the licensing contract was executory and the licensee had no promissory estoppel claim to prevent the licensor from revoking

Prior to *Mission Product*, which explicitly refused to follow *Lubrizol*, bankruptcy courts advanced two main arguments for following *Lubrizol*'s lead. First, courts argued that despite its harsh effect, the language of § 365 is clear, and therefore it would be inappropriate to follow the legislative history's suggestion that courts find equitable solutions.[105] For example, the Bankruptcy Court for the Northern District of California stressed that "where the language is clear, judicial inquiry is complete," and courts are not permitted to consider the legislative history.[106] Here, § 365(n) clearly leaves trademarks out of its protection, so trademark licensees are left to § 365(g).[107] Further, these courts contended that, by leaving § 365(g) unamended, Congress endorsed *Lubrizol*'s treatment of § 365(g) rejections and so they must follow its guidance.[108]

Second, courts maintained that *Lubrizol* advanced the only possible interpretation of the term "rejection" as it applies to trademarks.[109] Before *Mission Product*, there was longstanding confusion over the contours of the rejection power.[110] Some courts interpreted the ability to "reject" as equivalent to the power to breach outside of bankruptcy, while others interpreted it as the power to avoid or rescind the contract.[111] Many critics of *Lubrizol* argued that rejection should function only as a breach and that the Fourth Circuit incorrectly interpreted the power as an avoiding power.[112] Supporters have argued that the nature of a trademark license blurs this line. The Bankruptcy Court for the District of Delaware, for example, explicitly countered this argument in *In re HQ Global Holdings, Inc.*[113] In that case, Judge Walrath explained that, because the purpose of the rejection power is to relieve the debtor of its obligations under a contract, and "the essence" of a trademark license is the licensor's ongoing and "affirmative grant . . . of the right to use [its] proprietary marks," the effect of rejecting this obligation *is* the revocation of the right to use the

the trademark), *vacated*, 2013 U.S. App. LEXIS 12463 (8th Cir. June 18, 2013), *rev'd en banc,* 751 F.3d 955 (8th Cir. 2014).

105. *In re Centura*, 281 B.R. at 670.

106. *Id.* (citing Barnhart v. Sigmon Coal Co., 534 U.S. 438 (2002)).

107. *Id.* at 673.

108. *In re* Exide Techs., 340 B.R. 222, 250 n.40 (Bankr. D. Del. 2006). Courts feel comfortable using this type of negative inference when interpreting § 365 because the Supreme Court used a negative inference to interpret the section in *NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 522–23 (1984), *superseded by statute on other grounds*, 11 U.S.C. § 1113 (2012).

109. *See In re* HQ Global Holdings, Inc., 290 B.R. 507, 513 (Bankr. D. Del. 2003).

110. Critchelow, *supra* note 99, at 639–40.

111. *Id.*

112. *See, e.g.*, Westbrook, *supra* note 30, at 310–11.

113. 290 B.R. at 513.

mark.[114] As such, supporters of *Lubrizol* contend that that the decision correctly interprets the term "rejection," and that the similarities between rejecting a trademark license and avoiding it are based on the nature of the contractual right, not the application of the power.

Despite its application in the courts, support for *Lubrizol* and its progeny is sparse in the academic community. Professor Jay Lawrence Westbrook, a leading scholar on rejection in the Bankruptcy Code, argues that academics agree *Lubrizol* was incorrectly decided, and thus its progeny were too.[115] Westbrook, along with Professor Michael T. Andrew, has argued since the late 1980s that a bankruptcy rejection is simply a breach of contract.[116] The pair wrote a series of three articles from 1988 to 1991 asserting that, rather than functioning as some "special bankruptcy 'power,' " rejection simply breaches the contract.[117] Accordingly, they argue that the rejected licensee should retain the same rights it would have if the breach occurred outside bankruptcy—that is, the licensee would continue to have rights to the trademark if allowed under the breach provisions of the contract.[118]

This understanding of trademark licenses cannot be squared with that of Judge Walrath and *Lubrizol*'s other supporters. Westbrook and Andrew understand the licensee's right to use a trademark as a right that the licensor signed away for a given period of time.[119] Judge Walrath, on the other hand, sees the licensee's right to use the trademark as a right the licensor *continually* grants.[120] As such, each

114. *Id.* ("The essence of the [licensing] Agreements was the Debtors' affirmative grant to the Franchisees of the right to use their proprietary marks. As the result of the rejection, that affirmative obligation of the Debtors to allow the Franchisees to use the marks is excused.").

115. Brief of Law Professors as Amici Curiae Supporting Petitioner at 12–13, 13 n.8, Mission Prod. Holdings, Inc. v. Tempnology, LLC (*In re* Tempnology), 139 S. Ct. 1652 (2019) (No. 17-1657), 2018 WL 6618029, at *12–13, 13 n.8 (citing over twenty articles and notes).

116. Michael T. Andrew, *Executory Contracts in Bankruptcy: Understanding 'Rejection,'* 59 U. COLO. L. REV. 845, 881, 921, 923 (1988) [hereinafter Andrew, *Understanding 'Rejection'*]; Michael T. Andrew, *Executory Contracts Revisited: A Reply to Professor Westbrook*, 62 U. COLO. L. REV. 1, 8 (1991) [hereinafter Andrew, *Reply*]; Westbrook, *supra* note 30, at 281–82.

117. *See* Andrew, *Understanding 'Rejection,' supra* note 116, at 878, 921 ("Rejection of a contract by the estate . . . is not a rescission or cancellation of the contract. It is merely the estate's decision not to become obligated on it."); Andrew, *Reply*, *supra* note 116 at 8 (" '[R]ejection' is not some mystical power to cause contracts to vanish, nor a power to terminate, cancel, or repudiate them . . . . Rejection has the consequence of creating a deemed breach."); Westbrook, *supra* note 30, at 281–82.

118. Westbrook, *supra* note 30, at 309–11. Note that Professors Andrew and Westbrook do not suggest that trademark licensees should be able to retain *all* their contractual rights like licensees governed under § 365(n), but rather that they be able to retain any rights due to them in a regular breaching scenario. *Compare* 11 U.S.C § 365(n) (2012), *with* Westbrook, *supra* note 30, at 309–11.

119. *See* Andrew, *Understanding 'Rejection,' supra* note 116, at 921; Andrew, *Reply*, *supra* note 116, at 8; Westbrook, *supra* note 30, at 281–82.

120. *See In re* HQ Global Holdings, Inc., 290 B.R. 507, 513 (Bankr. D. Del. 2003) ("The essence of the Agreements was the Debtors' affirmative grant to the Franchisees of the right to use their proprietary marks.").

party believes its solution properly carries out the Code's instruction that rejected licenses be treated as breached.[121]

Westbrook also is one of three professors who wrote an amicus brief in *Mission Product*, arguing that both *Lubrizol* and the IPLBA are irrelevant to trademark license rejections.[122] The brief contends that because *Lubrizol* did not involve trademark licenses, its holding is not binding in cases involving such licenses.[123] Because *Lubrizol*'s holding was not binding on trademark licenses, Congress was not pressed to include trademarks in its counter to *Lubrizol*—the IPLBA—so no negative inferences can be drawn from the exclusion.[124] Since neither *Lubrizol* nor the IPLBA governs trademark licenses, courts should look only to § 365(g) for guidance.[125] Finally, as § 365(g) plainly states that a rejection "constitutes a breach," courts must treat the contract like any other contract that has been breached.[126]

This impressive chain of logic, however, ignores the true interplay between *Lubrizol* and the IPLBA. Had Congress truly taken issue with the "[p]seudo [a]voiding [p]ower" *Lubrizol* allegedly gave § 365(g) rejection,[127] why did it not fix that problem by amending the text of § 365(g)? Instead Congress responded to *Lubrizol* by enacting § 365(n) to protect intellectual property from the harsh consequences of § 365(g) rejection, but said nothing about those consequences being incorrect when applied to any other executory contract.[128] The truth is, we do not know whether Congress *actually* intended for the IPLBA to change the way courts interpreted § 365(g). The Senate Report states: "Certain recent court decisions interpreting Section 365 have imposed a burden on American technological development that was never intended by Congress in enacting Section 365."[129] But this statement is open to two possible interpretations: (1) that Congress never intended for § 365 to be interpreted as it had been in *Lubrizol* or (2) that Congress

121. *See* 11 U.S.C. § 365(g).

122. *See* Brief of Law Professors, *supra* note 115, at 16 ("Trademark licensees are not included in [§ 365(g)], but neither were they covered by *Lubrizol*; legislative correction was, therefore, unnecessary.").

123. *Id.*

124. *Id.*

125. *Id.*

126. *Id.* at 17; *see* 11 U.S.C. § 365(g) ("Except as provided in subsections (h)(2) and (i)(2) of this section, the rejection of an executory contract or unexpired lease of the debtor constitutes a breach of such contract or lease . . . .").

127. *See* Westbrook, *supra* note 30, at 309 ("The courts often use executory contract analysis as a type of avoiding power . . . .").

128. *See* S. REP. NO. 100-505, at 4–5 (1988), *as reprinted in* 1988 U.S.C.C.A.N. 3200, 3203 (noting that § 365(n) "does not accord special treatment for intellectual property" but rather simply "limits the consequences of the breach or rejection of the contract").

129. *Id.* at 1–2, *as reprinted in* 1988 U.S.C.C.A.N. at 3200.

never intended for § 365 to impose a heavy burden on intellectual property licensees. Since Congress amended the Code to address the latter problem and not the former, it seems that the true aim of the IPLBA was to remove intellectual property from the harsh reality of § 365(g), not to change the interpretation of § 365(g) rejection. For this reason, supporters argued *Lubrizol* stood as valid guidance for the interpretation of § 365(g) rejection until *Mission Product* held otherwise.[130]

B. Sunbeam *and Its Supporters: Rights Retained*

The first circuit court to wade into the post-*Lubrizol* and IPLBA mess avoided the issue. In 2010, the Third Circuit skirted the question regarding postrejection rights for a trademark licensee by holding that the contract was not executory and therefore could not be rejected.[131] Judge Ambro penned a concurring opinion, arguing that § 365(g) rejection "does not necessarily deprive the trademark licensee of its rights in the licensed mark."[132] Specifically, Judge Ambro was dissatisfied with the bankruptcy court's negative inference that because the IPLBA does not cover trademarks, Congress intended for *Lubrizol* to "retain vitality" for trademark licenses.[133] Judge Ambro argued this negative inference is inappropriate in light of the Senate Report's statement, "Nor does the bill address or *intend any inference* to be drawn concerning the treatment of executory contracts which are unrelated to intellectual property."[134] Instead, Judge Ambro advocated for the bankruptcy court to use its equitable powers to fashion a solution fair to both parties.[135]

In 2011, the Bankruptcy Court for the Northern District of Illinois heeded Judge Ambro's suggestion.[136] The court held that it was

130. This is the logic of the aforementioned negative inference. *See In re* Exide Techs., 340 B.R. 222, 250 n.40 (Bankr. D. Del. 2006) (embracing the idea that Congress's silence on trademarks gives rise to a negative inference that § 365(n) does not protect trademarks and trademark licensees, meaning that *Lubrizol* remains valid in this context).

131. *In re* Exide Techs., 607 F.3d 957, 962–64 (3d Cir. 2010) ("Because the Agreement is not an executory contract, [the debtor] cannot reject it.").

132. *Id.* at 965 (Ambro, J., concurring).

133. *Id.* at 966 (quoting *In re Exide Techs.*, 340 B.R., at 250 n.40).

134. *Id.* at 967 (quoting S. REP. NO. 100-505, at 5, *as reprinted in* 1988 U.S.C.C.A.N. at 3204) (emphasis added).

135. *Id.*

136. Szilagyi v. Chi. Am. Mfg., LLC (*In re* Lakewood Eng'g & Mfg. Co.), 459 B.R. 306, 345–46 (N.D. Ill. 2011) ("In the absence of controlling authority on this point from the Seventh Circuit, this court is persuaded by Judge Ambro's reasoning."), *aff'd on other grounds sub nom.* Sunbeam Prods., Inc. v. Chi. Am. Mfg., LLC, 686 F.3d 372 (7th Cir. 2012), *cert. denied*, 568 U.S. 1076 (2012).

within its equitable powers to fashion a solution to its liking.[137] The case, known as *Sunbeam*, involved three major parties: Lakewood Engineering & Manufacturing Co. ("Lakewood"), Chicago American Manufacturing ("CAM"), and Sunbeam Products.[138] Lakewood, the debtor-licensor, was a failing company that produced and sold box fans, among other products.[139] In 2008, Lakewood entered into a licensing contract with CAM, the licensee, whereby CAM would manufacture Lakewood-branded box fans for "the 2009 cooling season."[140] This contract required CAM to manufacture 1.2 million fans, and included a provision that allowed CAM to sell these fans on its own if Lakewood failed to purchase them.[141] Lakewood was forced into bankruptcy three months after the contract was signed, however, and the trustee opted to sell the business to Sunbeam Products.[142] As part of this sale, Sunbeam Products purchased all Lakewood's assets, including the patents and trademarks that CAM was licensed to use.[143] After the sale, Sunbeam Products rejected the licensing contract with CAM: it intended to sell the box fans under its own name, so it did not want to purchase Lakewood-branded fans from CAM or allow CAM to sell them in competition.[144] Despite the rejection, CAM continued to manufacture and sell the fans, prompting Sunbeam Products to file suit to prevent it from doing so.[145]

The bankruptcy court allowed Sunbeam Products to reject the contract, but held that, for equitable purposes, CAM could continue to sell the fans under the terms of the original agreement.[146] The court argued it would be inequitable to hold that the rejection somehow vaporized CAM's rights.[147] After all, the parties had specifically negotiated terms that allowed CAM to continue selling fans in the event that Lakewood breached the contract by failing to purchase them.[148]

137. *Id.* at 347.

138. *See Sunbeam Prods.*, 686 F.3d at 374. Sunbeam Products did business under the name Jarden Consumer Solutions, and the cases refer to the party as such. *E.g.*, *id.* For ease of understanding, this Note will refer to this party only as "Sunbeam Products."

139. *Id.*

140. *Id.*

141. *Id.*

142. *Id.* Lakewood was forced into bankruptcy after "several of [its] creditors filed an involuntary . . . petition against it." *Id.*

143. *Id.*

144. *Id.*

145. *Id.*

146. Szilagyi v. Chi. Am. Mfg., LLC (*In re* Lakewood Eng'g & Mfg. Co.), 459 B.R. 306, 346 (N.D. Ill. 2011), *aff'd on other grounds sub nom.* Sunbeam Prods., Inc. v. Chi. Am. Mfg., LLC, 686 F.3d 372 (7th Cir. 2012), *cert. denied*, 568 U.S. 1076 (2012).

147. *Id.* at 345–46.

148. *Id.* at 315–16, 346.

Further, CAM had made significant investments to meet Lakewood's manufacturing requirements, including "chang[ing] the entire layout of its facility," hiring new workers, and purchasing new equipment.[149] Leaning on the Senate Report's suggestion that courts should fashion equitable solutions,[150] the court held that it was only fair to allow CAM to continue selling the Lakewood-branded fans.[151] Importantly, this holding included the 108,984 fans manufactured *after* Sunbeam Products rejected the contract and therefore stopped overseeing quality.[152] Perhaps fearful of the effect this would have on its newly acquired trademark, Sunbeam Products appealed.[153]

The Seventh Circuit rejected the bankruptcy court's equity argument but affirmed on the grounds that allowing CAM to retain its right to sell was the correct outcome under § 365(g).[154] Writing for the court, Judge Easterbrook stated that bankruptcy courts cannot be allowed to develop their own solutions under the guise of equitability but instead must follow the Bankruptcy Code.[155] According to Judge Easterbrook, allowing courts to develop their own equitable solutions would encourage forum shopping and undercut the Code's predictability.[156]

Nevertheless, the Seventh Circuit still affirmed, arguing "[w]hat § 365(g) does by classifying rejection as breach is establish that in bankruptcy, as outside of it, the other party's rights remain in place."[157] Essentially, because § 365(g) classifies a rejection as a breach, it must be treated as a nonbankruptcy breach would be treated.[158] Accordingly, because these two parties had a provision in their agreement stating that CAM could continue to sell Lakewood-branded fans in the event Lakewood failed to purchase them (that is, in the event of a breach), that provision controlled and CAM retained the right to sell

149. *Id.* at 313–14, 346. CAM estimates it spent approximately one million dollars to ready its facility. *Id.* at 314.

150. S. REP. NO. 100-505, at 5 (1988), *as reprinted in* 1988 U.S.C.C.A.N. 3200, 3204.

151. *Szilagyi*, 459 B.R. at 346–47.

152. *Id.* at 346.

153. *See* Sunbeam Prods., Inc. v. Chi. Am. Mfg., LLC, 686 F.3d 372, 375 (7th Cir. 2012), *cert. denied*, 568 U.S. 1076 (2012).

154. *Id.* at 375–77.

155. *Id.* at 375–76 ("There are hundreds of bankruptcy judges, who have many different ideas about what is equitable in any given situation. . . . Rights depend, however, on what the Code provides rather than on notions of equity.").

156. *Id.* ("[I]t is our obligation to interpret the Code clearly and predictably . . . ." (quoting RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065, 2073 (2012))).

157. *Id.* at 377.

158. *Id.*; *see* 11 U.S.C. § 365(g) (2012) ("[T]he rejection of an executory contract . . . constitutes a breach of such contract . . . .").

postrejection.[159] Judge Easterbrook argued that to hold otherwise would be to conflate the *rejection* power, which frees debtors from their performance obligations, and the *avoiding* power, which allows debtors to rescind certain contracts entirely.[160] Quality control received no mention in the decision.[161]

After *Sunbeam*, scholars, commentators, and law firms across the nation published articles praising the decision as a "[r]ay of [l]ight for . . . [l]icensees."[162] Scholars argued that *Sunbeam* is the correct interpretation of § 365(g) rejection for two main reasons. First, they maintained that *Sunbeam* correctly understands the rejection power as a breaching power, not an avoiding one.[163] Professor Westbrook asserted that "a contractual breach does not vaporize a trademark license, either as a matter of trademark or contract law. Accordingly, neither does rejection under Section 365."[164] Essentially, advocates of *Sunbeam* argued that because the Code provides *separate* avoiding and rejecting powers, they must be interpreted as functioning differently.[165]

This argument, however, is weakened by the reality that *Lubrizol* and its progeny *do* treat the rejection and avoiding powers differently. For example, imagine a debtor who writes his mother a check for $10,000 the day before he declares bankruptcy because he does not want that money to go toward repaying his debts. When the trustee elects to avoid this fraudulent transfer, the mother must return the money, and the payment is then treated as if it *never happened*.[166]

159. *Sunbeam Prods.*, 686 F.3d at 377.

160. *Id.* For a discussion of the *Lubrizol* camp's counterargument, see text accompanying notes 113–114.

161. *See Sunbeam Prods.*, 686 F.3d at 374–78.

162. Sunbeam Products—*Offering a Ray of Light for Trademark Licensees When Licensors File for Bankruptcy*, DAVIS POLK 1 (July 16, 2012), https://www.davispolk.com/files/files/Publication/0fb243e0-006a-4bc0-af93-497c27d69e62/Preview/PublicationAttachment/e86b86bf-45ab-40a8-86b4-ecb55e187681/071612_Sunbeam.pdf [https://perma.cc/5XYB-L4YA]; *see, e.g.*, Cone, *supra* note 48; Alan N. Resnick, Sunbeam *Offers a Ray of Sunshine for the Licensee When a Licensor Rejects a Trademark License Agreement in Bankruptcy*, 66 SMU L. REV. 817 (2013); Alexander N. Kreisman, Note, *Calling All Supreme Court Justices! It Might Be Time to Settle this "Rejection" Business Once and For All: A Look at* Sunbeam Products v. Chicago American Manufacturing *and the Resulting Circuit Split*, 8 SEVENTH CIR. REV. 36 (2012); Alexander Weatherbie, Comment, *Shining* Sunbeam *Through a Prism*, 4 BUS. & BANKR. L.J. 267 (2017); Geri Haight, Sunbeam *Decision Gives a Ray of Hope to Trademark Licensees*, MINTZ (July 31, 2012), https://www.mintz.com/insights-center/viewpoints/2251/2012-07-sunbeam-decision-gives-ray-hope-trademark-licensees [https://perma.cc/ZYP7-7WUK].

163. Brief of Law Professors, *supra* note 115, at 21.

164. *Id.*

165. *See* Ryan Gabay, Note, Sunbeam*: A Ray of Hope for Trademark Licensees*, 82 FORDHAM L. REV 245, 282–83 (2013) (proposing that Congress should amend the Bankruptcy Code to make this distinction clearer). *Compare* 11 U.S.C. § 365 (2012) (rejection power), *with* 11 U.S.C. §§ 544–545, 547–549, 553(b), 724(a) (2012) (avoiding powers).

166. *See* 11 U.S.C. § 548; 5 COLLIER ON BANKRUPTCY, *supra* note 12, ¶ 547.01.

In this example, because the mother never had a right to the money, she must return it and she receives nothing in exchange—the avoidance does not entitle her to a claim for damages. On the other hand, when a contract is rejected, the creditor becomes entitled to a prepetition claim for damages.[167] Critics of *Lubrizol* avoid acknowledging this clear distinction by constraining their argument to the interpretation of the word "rejection" in § 365 alone, rather than the interpretation of the power throughout the whole Code. As such, these critics miss the mark: the Code, as interpreted by *Lubrizol* and read in its entirety, can be read to treat rejection and avoidance differently.

Second, advocates argued that *Sunbeam* makes the most sense from a policy perspective. They claimed that *Sunbeam* adequately responds to the common criticism that *Lubrizol* and its progeny would have a chilling effect on industry.[168] While the solution would place the impetus on licensees to carefully draft breach provisions to protect their rights, the transaction costs associated with this change would eventually decrease as industry standards emerge.[169] Further, they claimed *Sunbeam* appropriately places the power back into the hands of the contracting parties and prevents debtor-licensors from using the Code as a sword against innocent licensees.[170]

Despite its popularity, the Seventh Circuit's decision in *Sunbeam* ignores the realities of trademark law in favor of what feels equitable. Trademark licensors have an "affirmative duty" to control the quality of branded products, and they risk losing their trademark if they fail to do so.[171] It is admittedly unusual for courts to declare a trademark abandoned by naked licensing.[172] But caselaw indicates that a postrejection trademark licensor would be particularly vulnerable to a claim of abandonment. Courts have declared trademarks naked and abandoned in two main situations: (1) where the licensor exercises no control, contractual or actual, over the products and (2) where the licensor and licensee have no special relationship justifying reliance on

167. 11 U.S.C. § 502(g)(1).

168. *See, e.g.*, Cone *supra* note 48, at 376 ("Adopting *Sunbeam* also avoids the 'chilling effect' that accompanies holdings such as *Lubrizol*'s.").

169. *Id.*

170. *Id.*; *see* Kreisman, *supra* note 162, at 60 (criticizing *Lubrizol* for allowing debtor-licensors to use the Code as a sword rather than a shield); Weatherbie, *supra* note 162, at 279–80 (arguing that technology-based companies could be particularly brutalized by an unexpected rejection under *Lubrizol*).

171. Benjamin Howard, Note, *Reconciling Trademark Law with Bankruptcy Law in License Rejection*, 2014 COLUM. BUS. L. REV. 172, 197–202 (2014) (quoting Dawn Donut Co. v. Hart's Food Stores, Inc., 267 F.2d 358, 367 (2d Cir. 1959)).

172. DRATLER JR., *supra* note 67, § 11.03 ("Courts have actually decreed forfeitures, and the Patent and Trademark Office has refused to register marks on grounds of naked licensing in only a handful of cases.").

the licensee for quality control.[173] This is a close reflection of the majority and minority approaches to quality control.[174] Because rejection frees licensors from their obligations, they cannot be said to exercise control over the trademarked products sold by the licensee postrejection. Further, because licensors often sell their trademarks or change their quality standards as part of the reorganization process, licensors cannot be said to justifiably rely on licensees for quality control.

For example, in the aftermath of the *Sunbeam* decision, Sunbeam Products was open to a colorable claim that it had abandoned the Lakewood trademark because CAM was permitted to sell 108,984 Lakewood-branded fans manufactured after the rejection took place.[175] As the rejection relieved Sunbeam Products, the new licensor, of its performance obligations, it likely did not exercise quality control over these products.[176] Under the majority approach to quality control, Sunbeam Products would fail because it did not exercise *any* control after the rejection.[177] Even under the more flexible minority approach, Sunbeam Products would still fail as it would not be able to prove a close relationship with CAM. As such, the implications of *Sunbeam* seriously endangered the trademark.

The *Sunbeam* scheme functionally leaves debtor-licensors with two options: (1) sell their trademark for a lower price, or (2) assume, rather than reject, the contract. Under this scheme, a purchaser like Sunbeam Products now needs to offer a low enough price to the debtor that it has enough resources left to purchase all the licensee's products and dispose of them. This means that trademarks are worth less under the *Sunbeam* scheme, which reduces the amount available to repay creditors. If the debtor-licensor does not wish to sell its trademark, the scheme functionally deprives it of the right to reject. As previously discussed, courts must approve the decision to reject a contract using a business judgment test.[178] Typically this involves determining whether

173. *Id.* (collecting cases). For specific examples, see discussion *infra* notes 190–192 and accompanying text.

174. *See supra* Section I.C.

175. Szilagyi v. Chi. Am. Mfg., LLC (*In re* Lakewood Eng'g & Mfg. Co.), 459 B.R. 306, 346 (N.D. Ill. 2011), *aff'd on other grounds sub nom.* Sunbeam Prods., Inc. v. Chi. Am. Mfg., LLC, 686 F.3d 372 (7th Cir. 2012), *cert. denied*, 568 U.S. 1076 (2012).

176. *See* 11 U.S.C. § 365 (2012). As no trademark challenge was ever filed on these grounds, it is unknown if Sunbeam actually exercised any quality control.

177. *See* Calboli, *supra* note 69, at 370 (noting that the majority of courts require some "minimal" level of control to declare a license invalid).

178. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 523 (1984) (discussing the general use of the business judgment test), *superseded by statute on other grounds*, 11 U.S.C. § 1113 (2012); discussion *supra* notes 41–43 and accompanying text.

the contract is burdensome and the rejection would reap a net benefit to the estate.[179] Because the cost of losing a trademark is so high, debtor-licensors are less likely to pass the business judgment test, rendering them unable to reject. Despite these clear dangers, the Supreme Court refused to grant certiorari to review the decision.[180]

C. Proposed Statutory Amendments

Since Congress passed the IPLBA in 1988, scholars have been puzzled over the proper treatment of trademark licenses. In the last thirty years, several commentators have proposed amendments that would ensure trademark licensees have the opportunity to retain their rights in certain situations. Interestingly, few scholars have argued for statutory amendments. Instead, the majority of scholars have focused their energies on the correct interpretation of the current version of the Code.[181] This Part will not address that scholarship, but instead will analyze several suggested statutory amendments. The majority of these proposals fall into two categories: (1) amendments that would codify *Sunbeam* where equitable and (2) amendments that would simply expand § 365(n) to include trademark licenses.

1. A Balancing Act: Proposals to Codify *Sunbeam* Where Appropriate

Several commentators have proposed amendments that attempt to codify a balance between the interests of licensors and licensees. Darren W. Saunders, a practitioner at Kilpatrick & Lockhart LLP, argues that Congress should amend the Code to allow licensees to retain their rights depending on the facts and equitable considerations.[182] Specifically, he recommends § 365(n) be amended to allow trademark licensees to elect to retain their rights when "there is, in fact, reasonable control . . . such that there will be no likelihood of public deception."[183] Saunders also recommends that § 365(n) be amended to specify that such election should only be allowed "subject to principles of equity."[184] Similarly, Timothy J. Keough argues that

179. *See* Control Data Corp. v. Zelman (*In re* Minges), 602 F.2d 38, 43 (2d Cir. 1979) ("It is enough, if, as a matter of business judgment, rejection of the burdensome contract may benefit the estate.").

180. Sunbeam Prods., Inc. v. Chi. Am. Mfg., LLC, 568 U.S. 1076 (2012) (denying certiorari).

181. *See, e.g.*, Brief of Law Professors, *supra* note 115, at 13 n.8 (collecting articles arguing for the *Sunbeam* court's interpretation of § 365(g)).

182. Darren W. Saunders, *Should the Bankruptcy Code be Amended to Protect Trademark Licensees?*, 94 TRADEMARK REP. 934, 934 n.a1, 939–40 (2004).

183. *Id.* at 940.

184. *Id.*

Congress should amend the Code to allow licensees to retain their rights when the trademark does not require ongoing maintenance by the licensor.[185] Essentially, Keough proposes that where the licensee is responsible for maintaining quality control under the original terms of the licensing contract, the licensee should be allowed to retain its rights along with those obligations.[186] Finally, David M. Jenkins proposed a similar amendment with the caveat that the licensee should only be able to retain its rights where the court first finds that (1) the licensee is able to maintain the quality control and (2) the licensor does not intend to abandon its trademark.[187]

These solutions all suffer from the same problems: they underestimate the danger of a naked licensing claim, they create uncertainty, and they encourage forum shopping. All three solutions contend that postrejection quality control responsibilities should be shifted to the licensee entirely. While this comports with the current judicial trend treating the quality control requirement flexibly,[188] it goes too far. The majority of courts have adopted the actual control test,[189] and these three solutions propose that debtor-licensors formally surrender all control to the licensees. While it is admittedly rare for a court to deem trademarks abandoned, it has happened in cases where the licensor failed to exercise adequate control or relied exclusively on the licensee to maintain quality.[190] For example, in *Eva's Bridal, Ltd. v. Halanick Enterprises*, the Seventh Circuit held a licensor had engaged in naked licensing and abandoned its trademark because it "did not retain *any* control—not via the license agreement, not via course of

185. Timothy J. Keough, Note, *You're Asking the Wrong Question—The Effect of a Licensor's Rejection on the Trademark License*, 47 SUFFOLK U. L. REV. 165, 185–86 (2014).

186. *Id.* at 185.

187. David M. Jenkins, Note, *Licenses, Trademarks, and Bankruptcy, Oh My!: Trademark Licensing and the Perils of Licensor Bankruptcy*, 25 J. MARSHALL L. REV. 143, 165–66 (1991). Jenkins proposed a relatively elaborate six-part amendment that also mandated "the delivery of any materials which were promised in the license agreement," the "guarantee [of] a licensee's quiet enjoyment of the right," the "continue[d] payment of royalties to the licensor," and the preservation of the original contract's term. *Id.*

188. *See* Calboli, *supra* note 69, at 369–70 (noting that modern courts often simply look for "any sign of control").

189. *Id.* at 369.

190. *See, e.g.*, Barcamerica Int'l USA Tr. v. Tyfield Imps., Inc., 289 F.3d 589, 596–97 (9th Cir. 2002) (holding the trademark was naked in part because there were no quality control provisions and the licensee maintained the licensor did not attempt to exercise actual control); First Interstate Bancorp. v. Stenquist, No. C-89-4106 MHP, 1990 U.S. Dist. LEXIS 19426, at *2–3, 9 (N.D. Cal. July 13, 1990) (holding a trademark naked where the contract did not include control provisions and in fact specifically contemplated exclusive control by the licensee); Midwest Fur Producers Ass'n v. Mutation Mink Breeders Ass'n, 127 F. Supp. 217, 229 (W.D. Wis. 1954) (holding the trademark naked because the license agreement contained no quality control provisions and the licensor did not exercise actual control).

performance."[191] Similarly, in *FreecycleSunnyvale v. Freecycle Network*, the Ninth Circuit held a licensor had engaged in naked licensing and abandoned its trademark because it "granted [the licensee] the right to use the trademarks without either (1) the right to control or (2) the exercise of actual control."[192]

If a debtor-licensor were to reject a trademark license and allow the licensee to continue operating uncontrolled for the term of the contract, it would be vulnerable to this type of claim. Like the licensors in both *Eva's Bridal* and *Freecycle*, the debtor-licensor would not exercise contractual control—because the contract would have been rejected—and it would not exercise actual control—because the purpose of rejection is to alleviate it of such obligations. Only Jenkins's proposal contemplates the danger of a naked licensing claim. However, his requirement that the bankruptcy court find that the trademark licensor has no intent to abandon the trademark[193] does not actually guard against claims of naked licensing and abandonment.[194] Abandonment by naked licensing is not a voluntary act that the licensor *intends* to undertake; it is instead the automatic result of the licensor's failure to exercise quality control.[195] In fact, case law is quite clear that the licensor's intent is irrelevant when considering abandonment as a result of naked licensing.[196] Thus, all three of the proposed amendments would put debtor-licensors at risk of losing their trademarks.

Further, while these solutions may balance the needs of the licensor and the licensee, they would ultimately cause uncertainty and forum shopping. These proposals put the fate of parties squarely in the hands of judges and their varying understandings of the interests at hand. As *Sunbeam*'s Judge Easterbrook put it when he rejected the notion that bankruptcy courts could use their equitable powers to determine postrejection rights:

> There are hundreds of bankruptcy judges, who have many different ideas about what is equitable in any given situation. Some may think that equity favors licensees' reliance

191. 639 F.3d 788, 790–91 (7th Cir. 2011).

192. 626 F.3d 509, 514 (9th Cir. 2010).

193. Jenkins, *supra* note 187, at 166–67 (arguing his amendment would ensure that rejection was not construed as "an abandonment, *per se*").

194. *See also* Article Review, 83 TRADEMARK REP. 624, 624 (1993) (criticizing Jenkins' article for its "simplistic" understanding of trademark concepts).

195. DRATLER JR., *supra* note 67, § 11.03 ("[T]here is nothing voluntary about the[ ] consequences [of naked licensing] as the word 'abandonment' might imply.").

196. *See* Barcamerica Int'l USA Tr. v. Tyfield Imps., Inc., 289 F.3d 589, 595–96 (9th Cir. 2002) (noting that abandonment resulting from naked licensing is involuntary because the licensor's intent is irrelevant); Exxon Corp. v. Oxxford Clothes, Inc., 109 F.3d 1070, 1080 (5th Cir. 1997) ("Abandonment due to naked licensing is 'involuntary' because, unlike abandonment through non-use . . . an intent to abandon the mark is expressly not required to prove abandonment under [the statute].").

> interests; others may believe that equity favors the creditors, who can realize more of their claims if the debtor can terminate IP licenses.[197]

Ultimately, these solutions would undermine the legitimacy of the Code and could result in harsh—and completely unforeseen—results for both licensees and licensors.

In contrast, some proposals argue the proper balance is to include trademarks in the scope of § 365(n) but continue to impose quality control requirements on licensors. One of the earliest proposals of this type is from 1990, predating *Sunbeam* and much of the recent discussion. Scott W. Putney, a practitioner at the Department of Justice, argued that Congress should amend the Code to include trademark licensees in the protections of § 365(n) on the condition that they be required to "comply with the quality control portions of the rejected license."[198] Notably, the International Trademark Association ("INTA") and some members of Congress seem to favor this solution. In 2012, the INTA adopted a board resolution proposing trademarks be included in the scope of § 365(n).[199] Further, it proposed that § 365(n) be amended to clarify explicitly that rejection does not alleviate quality control obligations.[200] According to the background on the board resolution, the INTA believes it "is critical . . . that the [debtor-licensor] not be statutorily discharged from its obligation to perform [the quality control] function by virtue of the rejection."[201] In 2013, the House of Representatives passed the Innovation Act, which proposed much the same.[202] The bill proposed § 101(35A) be amended to include "a trademark, service mark, or trade name, as those terms are defined in section 45 of the Act of July 5, 1946."[203] The bill also included a new subsection for § 365(n)—§ 365(n)(1)(D), stating "in the case of a trademark, service mark, or trade name, the trustee shall not be relieved of a contractual obligation to monitor and control the quality of a licensed product or service."[204] The Innovation Act was received in the Senate and referred to the Senate Committee on the Judiciary in

197. Sunbeam Prods., Inc. v. Chi. Am. Mfg., 686 F.3d 372, 375–76 (7th Cir. 2012), *cert. denied*, 568 U.S. 1076 (2012).

198. Scott W. Putney, *Bankruptcy Code v. Lanham Act and Controlled Licensing*, 80 TRADEMARK REP. 140, 158 (1990).

199. *Board Resolutions: Trademark Licenses under the Federal Bankruptcy Code*, INT'L TRADEMARK ASS'N (Nov. 7, 2012), https://www.inta.org/Advocacy/Pages/TrademarkLicenses undertheUSFederalBankruptcyCodeResolution.aspx [https://perma.cc/H7RW-KC4J].

200. *Id.* ("Section 365(n) should be further amended to explicitly state that the statute does not relieve debtor licensors from any existing contractual obligations or authority to monitor and control the quality of licenses products bearing a licensed trademark.").

201. *Id.*

202. Innovation Act, H.R. 3309, 113th Cong. (2013).

203. *Id.* § 6(d)(2)(A)(iii).

204. *Id.* § 6(d)(2)(B)(iii).

December of 2013 but has seen no movement since.[205] According to the House Report's Section-by-Section Analysis, the bill was meant to "effectively codify[ ]" *Sunbeam* by clarifying that "trademark licenses are protected against being voided in bankruptcy."[206] This section provides no explanation for the proposed addition of § 365(n)(1)(D).[207]

While these proposals offer a balance between the needs of debtor-licensors and licensees, they all fundamentally misunderstand rejections. The purpose of a rejection is to relieve the debtor of its remaining obligations under the subject contract.[208] To allow a rejection but still impose quality control requirements loses sight of this purpose because it fails to relieve the debtor. The natural argument against this is to point out that Congress has allowed certain types of rejections that do not relieve the debtor of *all* obligations. Under § 365(h)(1)(A)(ii), for example, if a debtor-lessor rejects an unexpired lease of real property, the lessee may elect to "retain its rights under such lease . . . that are in or appurtenant to the real property."[209] The Code notes that the lessee can retain rights "such as those relating to the amount and timing of payment of rent and other amounts payable by the lessee and any right of use, possession, quiet enjoyment, subletting, assignment, or hypothecation."[210] However, when a lessee makes a § 365(h)(1)(A)(ii) election, only the leasehold and those rights appurtenant to it survive rejection—not any of the debtor-lessor's performance obligations. For example, the rejection relieves the debtor of covenants to provide provide heat, water, or electricity.[211] As such, while § 365(h)(1)(A)(ii) respects the purpose of rejection by allowing the debtor to relieve itself of its remaining performance obligations, the proposals to codify quality control in § 365(n) do not because they would affirmatively enforce a performance obligation.

205. *H.R. 3309 – Innovation Act*, CONGRESS.GOV, https://www.congress.gov/bill/113th-congress/house-bill/3309 (last visited Apr. 4, 2020) [https://perma.cc/3FEW-B8K5].

206. H.R. REP. NO. 113-279, at 64 (2013).

207. *See id.*

208. *See, e.g.*, Mission Prod. Holdings, Inc. v. Tempnology, LLC, 139 S. Ct. 1652, 1658 (2019) (noting that a rejection allows a debtor to "repudiat[e] any further performance of its duties"); *In re* HQ Global Holdings, Inc., 290 B.R. 507, 513 (Bankr. D. Del. 2003) (noting that a "rejection does not terminate or repudiate a contract but simply relieves the estate from its obligation to perform").

209. 11 U.S.C. § 365(h)(1)(A)(ii) (2012).

210. 11 U.S.C. § 365(h)(a)(A)(ii).

211. Megafoods Stores v. Flagstadd Realty Assocs. (*In re* Flagstaff Realty Assocs.), 60 F.3d 1031, 1034 (3d Cir. 1995) ("The primary function of rejection is to 'allow[ ] a debtor-lessor to escape the burden of providing continuing services to a tenant' " (quoting *In re* Lee Rd. Partners, Ltd., 155 B.R. 55, 60 (Bankr. E.D.N.Y. 1993) (alterations in original)); Dishi & Sons v. Bay Condos LLC, 510 B.R. 696, 705 (S.D.N.Y. 2014) ("As a practical matter, rejection of a lease frees the estate from the debtor-lessor's obligations thereunder, such as providing heat, water, and electricity.").

Aside from this fundamental issue, the proposals also suffer from their failure to consider different types of bankruptcy. It is theoretically possible for a Chapter 11 debtor to continue to control the quality of licensed products so long as it continues to operate after the bankruptcy concludes. But § 365 does not apply only to Chapter 11 debtors, it also applies to Chapter 7 and Chapter 15 debtors.[212] Imagine a debtor-licensor in a Chapter 7 liquidation case that seeks to reject a trademark licensing contract with five more years in its term. If the Innovation Act was passed, it would "impose[ ] an affirmative duty . . . to monitor and control"[213] on this debtor, meaning it would have performance obligations for the next five years. If the debtor successfully liquidates, this is an impossibility—it will cease to exist and therefore cannot meet the obligation. This debtor may have nothing to fear in terms of a naked licensing claim—it may in fact intend to abandon the license in the bankruptcy—but it would still have postrejection, post-existence obligations under this scheme. Alternatively, imagine a Chapter 11 debtor seeking to reject the same license because it intends to change the quality of its brand in order to become more profitable. If the debtor-licensor must continue to monitor and control the products governed by this license under the old standards, its trademark will cease to hold weight because it will not function to assure the public of the product's quality.[214] This would render the mark deceptive and could seriously damage the business's goodwill.[215] If the trademark forms the center of the debtor's business, this could spell disaster and prevent the debtor from reorganizing successfully and becoming profitable. As such, proposals that seek to balance the needs of licensors and licensees by including trademarks within the scope of § 365(n) but still imposing quality control requirements are simply untenable.

2. No Balancing Necessary: Proposals to Include Trademarks in § 365(n)

Alternatively, several commentators have proposed solutions that would bring the treatment of trademark licenses directly in line

212. *See* H.R. REP. NO. 113-279, at 98–99 (2013) (noting that the proposed amendment—like all of § 365, "would apply to all types of bankruptcy cases").

213. *Id.*

214. *See supra* notes 66–67 and accompanying text for a discussion of the purpose of trademarks.

215. *See, e.g.*, *In re* XMH Corp., 647 F.3d 690, 696 (7th Cir. 2011) (" '[T]he trademark is a shorthand way of telling me that the attributes are the same as that of the like-branded product I enjoyed earlier.' If without notice the seller reduces the quality of his brand, the trademark becomes deceptive because its assurance of continuity of quality is no longer truthful.").

with other types of intellectual property. Rather than attempting to balance the specific needs of trademark licensors and licensees, these solutions argue that § 365(n) alone is equitable enough. Keith Waters and Ryan Gabay both propose that Congress amend the Code to include trademarks in the definition of intellectual property.[216] Both students argue that Congress has already fashioned an equitable solution for intellectual property licenses and that the distinct treatment of trademarks is arbitrary.[217] Gabay goes one step further and proposes Congress also amend the Code to make clear that rejection and avoidance are separate powers with different functions.[218] Chandra Critchelow similarly recommends an amendment to § 365 to clarify the meaning of the rejection power.[219] She proposes that Congress should replace the term "rejection" with "election to breach" to clarify the true meaning of the § 365 power.[220] Critchelow argues that this type of amendment would not run afoul of congressional concerns regarding quality control because the requirement is not interpreted as strictly as it was in the 1980s.[221]

While these solutions would encourage consistency and discourage forum shopping, they do not account for potential trademark abandonment claims. What these proposals fail to recognize is that the distinction between trademarks and other types of intellectual property is not arbitrary, but is instead rooted in the problem of quality control. As previously discussed, debtor-licensors would not be able to show minimal actual control to satisfy the majority approach to quality control, and it would be unlikely that they could show a longstanding relationship and consistent quality to satisfy the minority approach.[222] As such, this type of amendment would either leave debtors open to claims of naked licensing and abandonment or would require a concurrent amendment to the Lanham Act. In sum, although these

216. Gabay, *supra* note 165, at 283; Keith Waters, Note, Sunbeam *and Its Impact on the Rejection of Trademark Licenses in Bankruptcy*, 65 ALA. L. REV. 833, 846 (2014).

217. Gabay, *supra* note 165, at 283; Waters, *supra* note 216, at 842–46.

218. Gabay, *supra* note 165, at 283.

219. Critchelow, *supra* note 99, at 641. Critchelow also argues that § 365(n) should be expanded to include trademarks and proposes two possible judicial solutions to the circuit split, as she believes a congressional amendment is unlikely. *Id.* at 641–43.

220. *Id.* at 641. Critchelow notes that a 1997 bankruptcy committee proposed that rejection should be replaced with "election to breach," but that Congress never adopted this proposal. *Id.* (citing NAT'L BANKR. REVIEW COMM'N, BANKRUPTCY: THE NEXT TWENTY YEARS § 2.4.1 (1997)). Critchelow argues that if Congress did not intend for rejection to mean the election to breach, it should instead replace the term with "election to terminate." *Id.*

221. *See id.* at 635–36 ("The modernization of quality control requirements with trademark law should be considered when determining whether trademarks should now be included in the definition of 'intellectual property' under the [IPLBA].").

222. *See* discussion *supra* notes 89–93 and accompanying text.

proposed statutory amendments—those that codify parts of *Sunbeam* and those that seek to amend § 365(n)—address some of the concerns that stem from postrejection rights to trademark licenses, they fail to protect the Code's legitimacy while also protecting the licensor from abandonment claim.

III. A TIME FOR CLARITY AND A TIME FOR EQUITY

A. Opportunity Strikes: In re Tempnology

Recently, the First Circuit entered the debate and offered the Supreme Court the perfect opportunity to clarify postrejection rights. In *Mission Product Holdings, Inc. v. Tempnology, LLC* (*In re Tempnology*), the First Circuit rejected the Seventh Circuit's *Sunbeam* reasoning and instead held that a rejection left the trademark licensee with no rights except for a prepetition claim for damages.[223] Effectively, the decision revived *Lubrizol* at the circuit level and established an indisputable circuit split.[224]

Writing for the majority, Judge Kayatta maintained that this was the correct course of action for several reasons. First, he explained that the language of § 365 is clear, so it would be inappropriate for the bankruptcy court to fashion an equitable solution rather than simply applying the text.[225] Next, he countered the argument that "rejection" can and should be interpreted as a simple breach like it was in *Sunbeam*.[226] Judge Kayatta argued that the Seventh Circuit's approach is untenable because it fails to take quality control into account—the decision "force[s] [the] Debtor to choose between performing executory obligations arising from the continuance of the license or risking the permanent loss of its trademarks, thereby diminishing their value to Debtor."[227] Finally, Judge Kayatta pointed out that *Sunbeam* and its supporters falsely claim that *Lubrizol* conflated rejection and avoidance: "[R]ejection as Congress viewed it does not 'vaporize' a right [but rather] . . . converts the right into a pre-petition claim for damages."[228] In sum, Judge Kayatta's opinion discussed every major

223. 879 F.3d 389, 402–04 (1st Cir. 2018), *rev'd*, 139 S. Ct. 1652 (2019).

224. Even before the *In re Tempnology* decision, some maintained there was a circuit split between the Fourth and Seventh Circuits on the grounds that the IPLBA did not overturn *Lubrizol* as it pertained to trademarks. Petition for a Writ of Certiorari at 9–12, Sunbeam Prods., Inc. v. Chi. Am. Mfg., LLC, 568 U.S. 1076 (2012) (denying certiorari) (No. 12-431), 2012 U.S. S. Ct. Briefs LEXIS 4346, at *12–16.

225. *In re Tempnology*, 879 F.3d at 401.

226. *Id.* at 402–03.

227. *Id.* at 403.

228. *Id.* at 402.

argument in favor of adopting *Lubrizol* and countered every major argument in favor of adopting *Sunbeam*. The licensee, Mission Products, appealed and presented the Supreme Court with the perfect vehicle to settle the issue.

B. Bound by Text: Mission Product Holdings

In *Mission Product Holdings, Inc. v. Tempnology, LLC*, the Supreme Court reversed *In re Tempnology* and affirmed the reasoning of *Sunbeam*.[229] Justice Elena Kagan opened the opinion with a strong statement of the holding: "A rejection breaches a contract but does not rescind it. And that means all the rights that would ordinarily survive a contract breach, including those conveyed [by a trademark license], remain in place."[230]

The Court began its analysis with the text of § 365 and "[found] that it does much of the work."[231] The Court noted that where the Bankruptcy Code does not define a term, it generally "incorporate[s] the established meaning" outside the Code.[232] As § 365(g) defines a rejection simply as a "breach," and the Code does not define breach in § 101,[233] the Court held that "[breach] means in the Code what [breach] means in contract law outside bankruptcy."[234] As breaches do not function as rescissions outside of bankruptcy—depriving licensees of their rights simply because licensors fail to uphold their end of the bargain—the Court reasoned they could not function that way within bankruptcy.[235]

This understanding of rejection comports with the general mandate that a debtor's estate should not contain more than the debtor possessed before bankruptcy.[236] That is, the Code should not be a tool debtors can use to claw back property they have no right to possess.[237]

229. Mission Prod. Holdings, Inc. v. Tempnology, LLC, 139 S. Ct. 1652, 1660 (2019). For clarity, this Note calls the Supreme Court decision *Mission Product* and the First Circuit decision *In re Tempnology*.

230. *Id.* at 1657–58.

231. *Id.* at 1661.

232. *Id.* (quoting Field v. Mans, 516 U.S. 59, 69 (1995)).

233. *See* 11 U.S.C. § 101 (2012).

234. *Mission Prod.*, 139 S. Ct. at 1661.

235. *Id.* at 1661–63.

236. *Id.* at 1663.

237. There are times when a debtor's estate *should* contain more than the debtor possessed immediately before bankruptcy because it was inappropriate for the debtor to part with the missing property. For example, imagine a debtor drains its bank accounts to pay its largest unsecured creditor $100,000 on the eve of bankruptcy. In all likelihood, this transfer would be a preferential payment that can be avoided under 11 U.S.C. § 547 (2012). In other words, the creditor could be forced to return the money to the estate. This clawback of funds is allowed only because it serves to place all the creditors on fair and equitable footing, not because it benefits the debtor. In contrast, allowing a debtor to enact a recission of a contract purely to benefit its business does

Like many in the pro-*Sunbeam* camp,[238] the Court also reasoned that this interpretation of rejection distinguishes it from avoidance and rescission, which *do* allow the debtor to claw back property.[239] Arguing that the Code imposes "stringent limits on 'avoidance' actions," the Court concluded that it would be inappropriate to allow rejection to be a "functional[ ] equivalent."[240]

The Court, unfortunately, fell into the same trap that the *Sunbeam* supporters did by failing to consider the Code as a whole.[241] Affirming the *In re Tempnology* decision would not have elided rejection and avoidance because the remedies would still be distinct—a rejection would entitle the licensee to a claim for prepetition damages resulting from the rejection,[242] while an avoidance would entitle the licensee to nothing.[243] As such, there is nothing equivalent to the rights counterparties receive between a rejection under *In re Tempnology* and an avoidance.

The Court also advanced an argument against the negative inference preferred by supporters of *Lubrizol* and its progeny.[244] The Court reasoned that adopting the negative inference would require it to accept a silent redefinition of § 365(g). In other words, the Court would have to hold that when Congress said that a "rejection . . . constitutes a breach,"[245] it actually meant that a rejection looks nothing like a breach as we understand it outside of bankruptcy.[246] To adopt this definition would defy the common meaning of the term "breach" and assume Congress rejected the common meaning by adopting piecemeal exceptions to § 365(g).[247] The Court also argued that the adoption of these exceptions implies that *Lubrizol* was incorrect—because each exception was adopted in response to a court imposing a *Lubrizol*-style scheme.[248] Section 365(n) was specifically adopted to avoid the *Lubrizol* decision, and § 365(h) was adopted to avoid a similar decision in the

not advance equity; instead, it would allow debtors to unfairly use the Code as a sword against creditors rather than a shield.

238. *See* discussion *supra* notes 163–165 and accompanying text.

239. *Mission Prod.,* 139 S. Ct. at 1663.

240. *Id.*

241. *See* discussion *supra* notes 166–167 and accompanying text.

242. 11 U.S.C. § 502(g)(1) (2012).

243. *See* 5 COLLIER ON BANKRUPTCY, *supra* note 12, ¶ 547.01; discussion *supra* notes 166–167 and accompanying text.

244. *See* discussion *supra* Section II.A (discussing the negative inference that because Congress did not include trademarks in the IPBLA, *Lubrizol* stands as valid guidance that a rejection deprives the licensee of all its rights, including those covered in breach provisions).

245. 11 U.S.C. § 365(g) (2012).

246. Mission Prod. Holdings, Inc. v. Tempnology, LLC, 139 S. Ct. 1652, 1664 (2019).

247. *Id.*

248. *Id.*

context of leases.[249] As the Court put it, "Congress whacked [*Lubrizol*-style] rejection wherever it raised its head."[250]

Finally, the Court argued that affirming the *In re Tempnology* decision "would allow the tail to wag the Doberman."[251] Section 365(g) is meant to apply to *all* executory contracts except those specifically excepted. While there may be strong arguments that the interaction between trademark law and rejection may harm debtor-licensors seeking to reject, there is no argument for interpreting the generally applicable § 365(g) specifically to meet the needs of a small subset of executory contracts.[252] This argument reflects the Court's position in *Mission Product*—even if the Court wanted to rule in favor of Tempnology and deprive licensees of postrejection rights, the text of the current statute simply does not leave room for such a decision. As Justice Sotomayor's concurrence acknowledged, if this solution is unsatisfactory, Congress should "tailor a provision for trademark licenses."[253]

Ultimately, Justice Sotomayor hits the nail on the head: the Supreme Court alone cannot solve the problem of § 365(g). While bankruptcy courts have been willing to implement equitable solutions, the circuit courts have felt bound to a stricter interpretation of the statute.[254] Judge Easterbrook, for example, noted that even "wise public policy[ ] cannot be used to supersede the Code's provisions."[255] According to Kenneth Klee, a leading bankruptcy scholar,[256] the Supreme Court has also made it clear that bankruptcy courts may not "rely on legislative history to support the use of equitable powers to

249. *Id.* at 1664 & n.2; *see* Andrew, *Understanding 'Rejection,' supra* note 116, at 903 n.200 (noting that a failure to address the practical question post-rejection between a lessee and a property owner "led to the more elaborate provision of Bankruptcy Code § 365(h)").

250. *Mission Prod.*, 139 S. Ct. at 1664–65.

251. *Id.* at 1665.

252. *Id.*

253. *Id.* at 1667 (Sotomayor, J., concurring).

254. *See* Sunbeam Prods., Inc. v. Chi. Am. Mfg., LLC, 686 F.3d 372, 376 (7th Cir. 2012) (criticizing the bankruptcy court for basing its decision on equitable concerns rather than the text of the Code), *cert. denied*, 568 U.S. 1076 (2012); *cf.* S. REP. NO. 100-505, at 5 (1988), *as reprinted in* 1988 U.S.C.C.A.N. 3200, 3204 (noting that the IPLBA did not address trademark licenses as Congress wanted to "allow the development of equitable treatment . . . by bankruptcy courts").

255. *Sunbeam Prods.*, 686 F.3d at 375–76.

256. Klee "was a principal draftsman of the Bankruptcy Code" when he served as Associate Counsel for the House Committee on the Judiciary, served as a contributing and consulting editor of COLLIER ON BANKRUPTCY, and is a Professor Emeritus at UCLA School of Law. *Attorneys: Kenneth N. Klee*, KTBS LAW LLP, https://www.ktbslaw.com/attorneys-29.html (last visited Apr. 4, 2020) [https://perma.cc/2SXW-EE25]. Klee has written a variety of books, law review articles, and treatise chapters on bankruptcy. *Id.*

override the statute."[257] As such, the Senate made a grave error in locating its call for equitable solutions in its report rather than in the Code itself.[258]

C. Congressional Intervention: The Only Option for Equity

This Note argues that Congress should amend § 365 to include a new subsection that more equitably deals with trademark licenses. This subsection should state that a rejection of a trademark license leaves the licensee with: (1) an adjusted prepetition claim for damages and (2) any rights and obligations, as set out in the contract's breach provisions, to products already produced or possessed by the licensee and controlled for quality by the licensor at the time rejection is approved. This solution best balances the needs of debtor-licensors and creditor-licensees and can be applied predictably throughout the country.

To begin, this amendment would more adequately compensate licensees for their losses. First, licensees would be permitted to sell, and therefore to recover their investment on, any products in their possession that were controlled for quality before the rejection. Second, licensees would then be allowed to file a claim for damages for the loss of the contract moving forward. As such, licensees would recover more of their investment costs even if the amount of damages paid out remains very small because they would no longer be left with storerooms full of unsellable products. In this way, the amendment would adopt those features of the *Sunbeam* and *Mission Product* solutions that best benefit licensees.[259]

Next, this amendment would allow trademark licensors to reject licenses without fear that doing so could result in naked licensing and abandonment. The licensees would retain rights only to a very specific type of product—those already in their possession and controlled for quality. Further, the amendment would require licensees to continue fulfilling any obligations that accompany their rights to those products, meaning licensees would remain obligated to maintain the quality of the products per the original agreement. As long as the debtor-licensor adequately controls the quality before the rejection, there can be no claim of naked licensing resulting from the sale of the protected

257. KENNETH KLEE, BANKRUPTCY AND THE SUPREME COURT 231 (2008) (citing various Supreme Court cases establishing this principle).

258. *Compare* S. REP. NO. 100-505, at 5, *as reprinted in* 1988 U.S.C.C.A.N. at 3204, *with* 11 U.S.C. § 365 (2012).

259. *See Sunbeam Prods.*, 686 F.3d at 376–77 (preserving the licensee's rights to sell products it has already produced as well as converting the licensor's unfulfilled obligations to damages).

products.[260] As such, this scheme guarantees three important things: (1) licensors may use the rejection power to relieve themselves of *all* obligations under the contract; (2) licensees may retain their rights and obligations to possessed products so they may recoup some of their losses; and (3) this retention will not leave licensors open to claims of naked licensing, as the products to which licensees retain rights will already have met the quality control requirement. In this way, the amendment would adopt the features of the *Lubrizol* and *In re Tempnology* solutions that best protect licensors.[261]

This amendment would enact a brightline rule: The only products the licensee would retain rights over are those that are in their possession and controlled for quality at the time rejection is approved. Because of this definitive rule, this solution does not raise the predictability and forum-shopping concerns that often accompany equitable proposals.[262] This middle ground allows the bankruptcy system to balance party interests without wading too far into the weeds and without leaving the balancing up to individual bankruptcy judges.[263] This solution appropriately places power back into the hands of the contracting parties. Licensors and licensees carefully draft their contracts and breach provisions, and this solution allows for those negotiations to remain binding on the parties where equitable. In short, it prevents a licensor from using bankruptcy as a "sword" to *unfairly* "take back trademark rights it bargained away,"[264] while also guaranteeing that licensors can reject burdensome contracts in good faith.

Opponents may argue that this solution could result in fact-specific inquiries that would burden bankruptcy courts' schedules. If adopted, the rejection process would require courts to determine (1) if a contract is executory; (2) if the rejection reflects good business

260. Any such claim that *does* exist would have existed outside the bankruptcy and so cannot be attributed to the consequences of rejection.

261. *See* Mission Prod. Holdings, Inc. v. Tempnology, LLC (*In re* Tempnology), 879 F.3d 389, 392 (1st Cir. 2018) (relieving the debtor of "any obligations"), *rev'd,* 139 S. Ct. 1652 (2019); *see also* Lubrizol Enters., Inc. v. Richmond Metal Finishers, Inc., 756 F.2d 1043, 1046–48 (4th Cir. 1985) ("Allowing specific performance would obviously undercut the core purpose of rejection under § 365(a), and that consequence cannot therefore be read into congressional intent."), *superseded in part by statute*, 11 U.S.C. § 365(n) (2012).

262. *See supra* Section II.C.1.

263. *See Sunbeam Prods.*, 686 F.3d at 375–76 (criticizing the notion that bankruptcy judges, "who have many different ideas about what is equitable in any given situation," should be allowed to determine the rights of parties in the event of a rejection).

264. *See* Szilagyi v. Chi. Am. Mfg., LLC (*In re* Lakewood Eng'g & Mfg. Co.), 459 B.R. 306, 344–46 (N.D. Ill. 2011) (quoting *In re Exide Techs.* 607 F.3d 957, 967 (Ambro, J., concurring)) (adopting an equitable solution to prevent debtor-licensor from doing just that), *aff'd on other grounds*, *Sunbeam Prods.*, 686 F.3d 372.

judgment; and (3) which products are covered in the protection of this solution. While this *does* add a third step to the process, the brightline nature of the rule makes the final inquiry short and sweet. Creditors would simply declare which products were already in their possession and controlled for quality at the time of rejection.

Opponents may also contend that this amendment would incentivize licensees to frontload manufacturing trademarked goods to ensure they fall within the protections. This could certainly have serious unintended consequences for licensees in industries that have volatile markets. Licensees manufacturing pharmaceuticals, for example, could open themselves up to a complete loss in the event the FDA withdraws approval for the medicine. However, it is most appropriate for courts to leave the balancing of such specific dangers to industry players. Further, this danger would be counterbalanced by the licensor's incentive to put licensees on a more regimented manufacturing schedule. Any way you cut it, this solution places the power back into the hands of the parties, balances their interests evenly, and provides a clear and predictable scheme.

CONCLUSION

Section 365 of the Bankruptcy Code empowers debtors to reject burdensome executory contracts.[265] From 1988 until May 2019, the effect of such a rejection on trademark licenses was unclear. The Supreme Court's recent decision in *Mission Product Holdings, Inc. v. Tempnology, LLC*, however, settled the matter and definitively held that a rejection under § 365(g) is a simple breach, operating exactly as it would outside the bankruptcy context.[266] The current language of the Code provides trademark licensors and licensees with no opportunity for a more equitable ruling.

This Note proposes that Congress amend § 365 to codify a more equitable treatment of rejected trademark license agreements. Specifically, the section should be amended to allow licensees to retain (1) an adjusted prepetition claim to damages for breach of contract and (2) any rights and obligations, as set out in the contract's breach provisions, to products already produced or possessed by the licensee and controlled for quality by the licensor at the time rejection is approved. The enactment of this brightline, middle-ground amendment would adequately balance party interests, give effect to the parties'

265. 11 U.S.C. § 365.
266. 139 S. Ct. 1652, 1658 (2019).

negotiated breach terms, and create a more predictable structure for trademark license rejections.

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