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Supreme Court: Trademark Licenses Survive Bankruptcy

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The US Supreme Court decided what the International Trademark Association (INTA) called "the most significant unresolved legal issue in trademark licensing" when it ruled on May 20, 2019, that bankrupt companies cannot use bankruptcy law to revoke a trademark license.

In its 8-1 decision, the court resolved a circuit split by holding that a debtor's rejection of a trademark license under Section 365 of the Bankruptcy Code, which enables a debtor to "reject any executory contract" (a contract that neither party has finished performing), amounts only to a breach of the license.

The circuits had been divided as to whether rejection of a license was simply a breach, in which case the licensee could continue to use the trademark, or a termination of the license, in which event the licensee could not.

This case arose out of a license Tempnology, LLC granted to Mission Product Holdings, Inc. to use its trademarks for clothing and accessories. Tempnology filed for bankruptcy reorganization under Chapter 11 and rejected the license. The Bankruptcy Court approved the rejection and held that the rejection terminated Mission Product's right to use the marks. The Bankruptcy Appellate Panel reversed but the Court of Appeals for the First Circuit agreed with the bankruptcy court that the rejection terminated the license.

A case in the Seventh Circuit, *Sunbeam Products, Inc. v. Chicago Am. Mfg., LLC,* 686 F. 3d 372 (7th Cir. 2012), ruled the other way. That court noted that outside the bankruptcy context, a licensor's breach of a trademark license does not terminate the licensee's right to use the mark. Because Bankruptcy Code Section 365 defines a debtor's rejection as a breach of contract, the Seventh Circuit reasoned, the rejection likewise not be deemed to terminate the license.

The Supreme Court agreed with the Seventh Circuit. Writing for the court, Justice Elena Kagan wrote "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 here [the trademark license], remain in place."

As the court explained, upon rejection the debtor "can stop performing its remaining obligations under the agreement. But the debtor cannot rescind the license already conveyed. So the licensee can continue to do whatever the license authorizes."

The Supreme Court reasoned that under bankruptcy law, the bankruptcy estate "cannot possess anything more than the debtor itself did outside bankruptcy," the court said. Here, before filing bankruptcy, Tempnology's trademark rights were subject to its license to Mission Product. If rejecting the agreement were to terminate Mission Product's license, then Tempnology's bankruptcy estate would have broader rights to the marks than Tempnology itself did.

One issue complicating this case is the fact that for a trademark license to be valid, the licensor must exercise control over the quality of the licensee's goods or services. If the licensor is in bankruptcy and has rejected the license, what assurance is there that the licensor will continue to exercise quality control over the licensed goods?

Tempnology argued that this requirement meant that trademark licenses should be treated different from other contracts under Section 365. The Supreme Court was not persuaded. "However serious Tempnology's trademark-related concerns, that would allow the tail to wag the Doberman," the court noted.

In its amicus brief in support of Mission Product's position, INTA addressed that issue, noting that a licensor's quality control obligations derive from Lanham Act Section 5, 15 U.S.C. §1055, and were not overridden by the

debtor-licensor's rights under the Bankruptcy Code. Moreover, INTA noted, to maintain its investment in the mark the licensee has an incentive to maintain quality at the pre-bankruptcy standards, as specified in the license agreement.

The case is *Mission Product Holdings, Inc. v. Tempnology, LLC*, No. 17-1657 (U.S., May 20, 2019).

Cooley's John Crittenden is Chair of INTA's International Amicus Committee.

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Key Contacts

Robert Eisenbach San Francisco	reisenbach@cooley.com +1 415 693 2094
Cathy Hershcopf New York	chershcopf@cooley.com +1 212 479 6138

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