

They Might Survive Trademark Licenses in Bankruptcy

By: Nathan G. Kanute, Partner, Snell & Wilmer



**Nathan G.
Kanute**

Trademarks can be valuable intellectual property.¹ The ability to use another company's trademark—a license—can come at a premium if the license is exclusive or the trademark is well known. Knowing what happens to a trademark license when the trademark owner files bankruptcy, therefore, can be vital to a company's bottom line. The U.S. Supreme Court recently provided guidance for trademark licensors and licensees in the case *Mission Product Holdings, Inc. v. Tempnology, LLC*.

Tempnology, a clothing manufacturer that owned trademarks used to market and sell athletic apparel, entered into contracts with Mission Product Holdings. Mission Product obtained a non-exclusive license to use one of Tempnology's trademarks. Prior to the expiration of the license, Tempnology filed a Chapter 11 bankruptcy petition and sought to reject the license under Section 365 of the Bankruptcy Code, which permits assumption or rejection of certain contracts in bankruptcy. The rejection of the trademark license was approved and Tempnology sought a determination that Mission Product was no longer allowed to use the licensed trademark. The Bankruptcy Court agreed reasoning that the lack of a special protection for trademark licensees in the Code, which does include special protections for licensees of other intellectual property, meant there were no such protections.

The Bankruptcy Appellate Panel rejected the Bankruptcy Court's conclusion. The First Circuit Court of Appeals, however, reinstated the Bankruptcy Court's ruling. The First Circuit was persuaded by the lack of special trademark protection in the Code and concerned that the trademark owner, though not contractually bound after a rejection of the license, could risk losing the right to its marks if it did not undertake monitoring and quality control efforts. The First Circuit reasoned that these continuing obligations ran afoul of the intent behind allowing rejection of a burdensome contract. The decision of the First Circuit set up a direct conflict with the Seventh Circuit Court of Appeals, which had ruled in *Sunbeam Products, Inc. v. Chicago Am. Mfg., LLC* that

rejection does not necessarily terminate a trademark licensee's rights. The Supreme Court agreed with the Seventh Circuit and focused on the legal effect of a Section 365 rejection.

The Code explicitly provides that a rejection of any contract is a "breach." The Court noted that the resulting effects of a breach on contractual rights are determined by non-bankruptcy contract law.² Under non-bankruptcy law, the non-breaching party to a contract can choose to terminate the agreement and stop performing after a breach or it can continue performing under the contract, retain its rights under that contract and sue for damages. The breach does not act as an automatic rescission. Therefore, Mission Product, provided it continued to perform its obligations under the license, could be permitted to continue its use of Tempnology's trademarks. The ultimate outcome was a matter of contract law.

The Court rejected Tempnology's arguments regarding the lack of a special trademark provision and the concerns that the trademark owner would still have obligations if the licensee continued to use the trademark. The later concern, the Court said, was a consideration that the trademark owner would have to take into account if it sought to protect its marks, but it should not alter the Code's balance between debtors and contractual counterparties. The Court remanded the case for a determination of what Mission Product's rights would have been under non-bankruptcy contractual law.

Companies dealing with trademark licenses should consider the ruling in *Mission Product Holdings* when drafting license agreements. The implications of a breach on the licensee's ability to use the marks under state law and the terms of the contract should be discussed and potentially negotiated. 🌿

¹ Trademarks, however, are not included in the definition of "intellectual property" under the Bankruptcy Code.

² The only twist the Court notes is that a rejection in bankruptcy treats the timing of the breach as occurring immediately before the filing of the bankruptcy.