RUTGERS LAW RECORD

The Internet Journal of Rutgers School of Law | Newark

www.lawrecord.com

Volume 40 **2012-2013**

SEVENTH CIRCUIT COURT OF APPEALS IN *SUNBEAM PRODUCTS, INC. V. CHICAGO AMERICAN MFG., LLC* SETS A NEW COURSE FOR TRADEMARK LICENSE REJECTION IN BANKRUPTCY

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Abstract: On July 9, 2012, the Seventh Circuit Court of Appeals concluded that Chicago American Manufacturing, LLC possessed a continuing right to use trademarks owned by Lakewood Engineering and Manufacturing Co., a Chapter 7 debtor. The ruling created a circuit split with the Fourth Circuit, which ruled in *Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc.* that when an intellectual property licensing agreement is rejected in bankruptcy, the licensee loses the ability to use any licensed trademarks. This Comment argues that the Seventh Circuit's approach better accomplishes the goals of bankruptcy law by preventing parties from abusing the contract rejection power of §365 of the Bankruptcy Code as a de facto avoidance power. The Seventh Circuit approach thus preserves the state-law contract rights of debtors and creditors, as intended by Congress and recommended by bankruptcy scholars.

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Introduction

Section 365(a) of the U.S. Bankruptcy Code provides that "the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor."[1] Courts have often struggled to clarify the powers contained in section 365.[2] The applicability of the section with respect to intellectual property rights has been a specific concern.[3]

At first, courts were uncertain as to how rejection affected the rights of contracting parties.[4] Some courts equated rejection with avoidance.[5] In such cases, the courts allowed insolvent sellers, lessors, and licensors to retake their previously held property, with little compensation to the previous transferee.[6] The avoidance approach had the potential to discourage parties from relying on contracts as predictable and legally binding instruments of wealth creation.[7]

In 1985, the U.S. Court of Appeals for the Fourth Circuit in *Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc.* held that a trustee's choice to reject a contract allowed the debtor's estate to retake intellectual property rights licensed to another party by that contract.[8] Congress reacted by amending section 365 to include subsection (n).[9] Subsection (n) provides that intellectual property licensees

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[1] 11 U.S.C. § 365(a)(2011).
[2] *See generally* Michael T. Andrew, *Executory Contracts in Bankruptcy: Understanding "Rejection,"* 59 U. COLO. L. REV. 845 (1988) (illustrating the difficulty that courts have in determining the effect of rejection in bankruptcy).
[3] *See id.* at 916–19; Jay Lawrence Westbrook, *The Commission's Recommendations Concerning the Treatment of Bankruptcy Contracts,* 5 AM. BANKR. INST. L. REV. 463, 470–71 (1997) (responding to National Bankruptcy Review Commissions invitation for suggested bankruptcy contract law reforms).
[4] Andrew, *supra* note 2, at 847. Assumption, by contrast, is well understood. *See id.* at 846. By assuming a contract or lease, the assuming party, initially a stranger to a pending contract, takes on the obligations of a contracting party. *Id.* Assumption in bankruptcy is identical to assumption under state law. *Id.* In bankruptcy, the debtor's estate can assume the debtor's existing contractual obligations. *See id.* at 846; 11 U.S.C. § 365. One definition of rejection is simply the decision not to assume. Andrew, *supra* note 2, at 849; *see* 11 U.S.C. § 365(a). In fact, rejection is presumed in bankruptcy; section 365(d)(1) provides that a contract is deemed rejected if not assumed within 60 days of the debtor's order for relief. 11 U.S.C. § 365(d)(1).
[5] Andrew, *supra* note 2, at 916–19. Avoidance is the power of the court to void a transaction and reclaim property transferred by the debtor to another party prior to filing bankruptcy. *See, e.g.*, 11 U.S.C. §§ 544, 547–48 (listing circumstances in which a trustee may avoid transactions).
[6] *See* Lubrizol Enter., Inc. v. Richmond Metal Finishers, Inc., 756 F.2d 1043, 1048 (4th Cir. 1985)(finding that rejection terminated property rights of a non-bankrupt party).
[7] Andrew, *supra* note 2, at 916–19; 133 CONG. REC. 23204–05 (1987).
[8] *See Lubrizol*, 756 F.2d at 1048.
[9] *See* 11 U.S.C. § 365(n); 133 CONG. REC. 23204–05 (1987).

retain their rights following contract rejection.[10] In essence, it provides intellectual property licensee creditors the same protections in bankruptcy as previously existed for other parties under section 365.[11] Subsection (n), however, incorporated the Bankruptcy Code's limited definition of "intellectual property."[12] Under the Bankruptcy Code, "intellectual property" is a term of art that does not include trademarks.[13] Therefore, Congress left trademark licensing contracts vulnerable to the precedent set by *Lubrizol*.[14]

In 2012, the U.S. Court of Appeals for the Seventh Circuit rejected the *Lubrizol* precedent with regard to trademark licensing in *Sunbeam Products, Inc. v. Chicago American Mfg., LLC.*[15] In so doing, the Seventh Circuit caused a circuit split on the issue.[16]Facing similar facts to those of *Lubrizol*, the court in *Sunbeam* found that a debtor that wished to reject a license agreement lacked the power to terminate the license.[17] *Sunbeam* is an important expansion of the intellectual property protections enacted after *Lubrizol*.[18] It is consistent with both Congress's intent and the desires of scholars and practitioners post-*Lubrizol*.[19]

Part I of this Comment provides a brief overview of section 365 of the Bankruptcy Code.[20] Part II discusses *Lubrizol* and its impact.[21] It then discusses the special legal status of trademarks.[22] It then discusses the resolution of the rejection controversy with the Seventh Circuit's decision in *Sun-*

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[10] *See* 11 U.S.C. § 365(n); 133 CONG. REC. 23204–05 (1987).
[11] *See* 11 U.S.C. § 365(n); 133 CONG. REC. 23204–05 (1987).
[12] *See* 11 U.S.C. § 365(n).
[13] 11 U.S.C. § 101(35A)(defining intellectual property as including only trade secrets, patents and patent applications, plant varieties, works of authorship, and mask works).
[14] *See* Sunbeam Prods., Inc. v. Chi. Am. Mfg., LLC, 686 F.3d 372, 375 (7th Cir. 2012), *cert. denied*, 133 S. Ct. 790 (2012); *In re* Exide Techs., 607 F.3d 957, 966–67 (3rd Cir. 2010) (Ambro, J., concurring) (concluding that section 365(n) neither codifies nor disapproves of *Lubrizol* as applied to trademarks).
[15] Sunbeam, 686 F.3d at 377–78.
[16] *See id.*
[17] *See id.*
[18] *See* Andrew, *supra* note 2, at 916–22; Westbrook, *supra* note 3, at 470–71.
[19] *See* Andrew, *supra* note 2, at 916–22; Westbrook, *supra* note 3, at 470–71.
[20] *See infra* notes 25–45 and accompanying text.
[21] *See infra* notes 49–57and accompanying text.
[22] *See infra* notes 58–68 and accompanying text.

beam.[23] Finally, Part III argues that the approach taken in *Sunbeam* better serves the spirit of section 365 and the rights of both debtors and creditors in bankruptcy.[24]

I. The Rejection Power in Bankruptcy

Part A of this section describes the statutory process and policy goals supporting rejection of contracts.[25] Part B describes the judicial controversy regarding the rejection power.[26]

A. *Statutory Process and Policy*

Under Chapter 5 of the Bankruptcy Code, a separate legal entity is created that succeeds to the debtor's property.[27] This "estate" is managed by a court-appointed trustee for the benefit of the debtor's creditors.[28] The trustee has two fundamental tasks: first, to ensure the debtor's "fresh start" free from previous burdens, and second, to maximize the value of the estate and thus the payout to creditors.[29]

Contracts entered into by the debtor prior to filing bankruptcy generally become assets of the bankruptcy estate.[30] The trustee or "debtor in possession" (hereafter "DIP") can assume the contract if doing so would be beneficial to the estate.[31] In other words, the trustee or DIP exercises "business judgment" about the value of the contract.[32]

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[23] *See infra* notes 70–99 and accompanying text.
[24] *See infra* notes 100–119 and accompanying text.
[25] *See infra* notes 27–37 and accompanying text.
[26] *See infra* notes 38–45 and accompanying text.
[27] 11 U.S.C. § 541(a)(2011).
[28] 11 U.S.C. §§ 323(a), 704 (granting the trustee authority and enumerating its specific duties).
[29] *See* 11 U.S.C. § 704. Duties of the trustee include collection and dispersal of funds, investigation of possible legal claims by and against the debtor, and others. *Id.*
[30] *See* 11 U.S.C. § 541(a)(1)(stating that "[s]uch estate is comprised of . . . all legal . . . interests of the debtor").
[31] Andrew, *supra* note 2, at 895–96 (stating that the issue for the trustee is "[w]hat use or disposition of the assets of the estate is best calculated to maximize the return to creditors?") (citing In re Minges*,* 602 F.2d 38, 44 (2nd Cir. 1979)(Mansfield, J., concurring). Notably, the language of section 365 only applies to "executory contracts." 11 U.S.C. § 365(g). The issue of whether certain types of contracts are executory is subject to controversy, but not directly pertinent to *Lubrizol* and *Sunbeam. See, e.g.,* In re Kellstrom Indus., 286 B.R. 833, 834–35 (Bankr. D. Del. 2002)(debating executoriness and describing points of view of different courts); Andrew, *supra* note 2, at 892–94 (providing alternate definitions to Countryman's and concluding that the definition is unimportant); Vern Countryman, *Executory Contracts in Bankruptcy: Part I,* 57 MINN L. REV. 439, 460 (1973)(supplying a definition employed by the majority of courts since its publication).
[32] Andrew, *supra* note 2, at 895–96.

Often, a trustee or DIP will determine that a contract is burdensome to the debtor and its creditors.[33] In such cases, the trustee or DIP will reject the contract.[34] If it does so, the rejection is treated pursuant to section 365(g) as a breach of contract that is back-dated to the moment before the filing of the bankruptcy petition.[35] This backdating allows the party aggrieved by the breach to become a creditor by filing a claim in the bankruptcy proceeding.[36] It thereby allows that claim to be paid by the debtor's estate and/or eventually discharged, which aids the debtor's fresh start.[37]

B. *Misconceptions of Rejection*

Prior to *Lubrizol* and Congress's post-*Lubrizol* amendment of the Bankruptcy Code, courts often explained rejection by analogy to other actions and powers common in bankruptcy proceedings.[38] Rejection was described as "release," "repeal," and through other vague terminology.[39] The descriptions held in common the idea that rejection of a contract involves termination of some rights in or to property transferred by contract.[40] Often, courts disagreed on how these various descriptions and interpretations correlated to the policy goals of bankruptcy law.[41]

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[33] *See, e.g.,* Sunbeam Prods., Inc. v. Chi. Am. Mfg. 686 F.3d 372, 374 (7th Cir. 2012) (observing that the trustee viewed a contract as less beneficial than options that might become available following rejection), *cert. denied*, 133 S. Ct. 790 (2012).
[34] *See* 11 U.S.C. § 365(a); Andrew, *supra* note 2, at 895–96 (discussing business judgment).
[35] 11 U.S.C. § 365(g).
[36] *See id.* Usually, parties may only file a claim in a debtor's bankruptcy if they are owed or aggrieved prior to the filing. *See, e.g.,*11 U.S.C. §§101(10), 501 (defining "creditor" as an entity holding a claim arising concurrent or previous to the debtor's order of relief and stating that creditors may file claims, respectively).
[37] *See* Marrama v. Citizens Bank of Mass., 549 U.S. 365, 367 (2007) (noting that "[t]he principal purpose of the Bankruptcy Code is to grant a 'fresh start'")(citing to Grogan v. Garner, 498 U.S. 279, 286 (1991)); NLRB v. Bildisco and Bildisco, 465 U.S. 513, 528 (1984) (noting that "[t]he fundamental purpose of reorganization is to prevent a debtor from going into liquidation, with an attendant loss of jobs and possible misuse of economic resources"); Union Bank v. Wolas, 502 U.S. 151, 161 (1991)(observing "the prime bankruptcy policy of equality of distribution among creditors of the debtor").
[38] *See* Andrew, *supra* note 2, at 847; Westbrook, *supra* note 3, at 470–71.
[39] *See, e.g.*, Bildisco, 465 U.S. at 528 (describing rejection as permitting "release"); *In re* Stable Mews Assoc., Inc., 41 Bankr.594, 596 (Bankr. S.D.N.Y. 1984) (describing rejection as permitting "repeal"); *see also*Andrew,*supra* note 2, at 847 (listing other cases and verbiage).
[40] *See* Andrew, *supra* note 2, at 847; Westbrook, *supra* note 3, at 470–71.
[41] *See* Andrew, *supra* note 2, at 847–848 (noting that "the jurisprudence of 'rejection' is profoundly confused"); Westbrook, *supra* note 3, at 470–71 (observing that "state law will not give the *breaching party*—the estate rejecting the contract—the right to rescind the contract or take back the consideration it has already given. Nothing in bankruptcy law does that either, so there is no basis for using rejection as an avoiding power").

Many judges, practitioners, and scholars regarded *Lubrizol* as a realization of judicial misconceptions of rejection.[42] After *Lubrizol*, consensus began to form around a new definition.[43] Today, the power to assume or reject contracts merely allows the trustee to make business decisions transferring assets and liabilities to a bankruptcy entity, the estate.[44] It does not create or terminate rights that exist at state law.[45]

II. Executory Contracts and Intellectual Properties

Part A of this section describes the impact of *Lubrizol* on the bankruptcy landscape.[46] Part B describes the special legal status of trademarks.[47] Part C describes the factual history of *Sunbeam* and the role of the case in the rejection controversy.[48]

A. Lubrizol*'s Lasting Impact*

In 1985, the U.S. Court of Appeals for the Fourth Circuit decided*Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc.*[49] In its decision, the court allowed rejection of a licensing agreement to terminate the licensor's state-law rights in the licensed property.[50] In *Lubrizol*, the debtor, Richmond Metal Finishers, Inc. ("Richmond") had licensed technology to the plaintiff, Lubrizol Enterprises,

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[42] *See, e.g., Sunbeam*, 686 F.3d at 377–78 (finding *Lubrizol* unpersuasive from a judicial standpoint and noting that "scholars uniformly criticize" it); Andrew, *supra* note 2, at 916–22 (noting that *Lubrizol* "illustrates perhaps better than any other" case what is wrong with avoiding-power rejection); Westbrook, *supra* note 3, at 470–71 (calling *Lubrizol* a "classic example" of the problem and noting its "immediate and awful" effects).
[43] *See, e.g.,* 11 U.S.C. § 365(n)(2011)(providing a protocol for rejection of intellectual property indicative of Congress's views on rejection); Andrew, *supra* note 2, at 916–22 (complaining about the effects of *Lubrizol*); Westbrook, *supra* note 3, at 470–71 (agreeing with Congress's actions but advocating further action).
[44] *See* 11 U.S.C. § 365; Andrew, *supra* note 2, at 846–851 (advocating for such a definition based on extensive case and policy research); 3–365 *Collier* on Bankruptcy ¶ 365.10[3] (16th ed. 2012) ("the effect of rejection . . . is limited to a breach or abandonment by the trustee or debtor in possession rather than a complete termination").
[45] *See* 11 U.S.C. § 365; Andrew, *supra* note 2, at 846–851; 3–365 *Collier* on Bankruptcy ¶ 365.10[3] (16th ed. 2012).
[46] *See infra* notes 49–57and accompanying text.
[47] *See infra* notes 58–68 and accompanying text.
[48] *See infra* notes 70–99 and accompanying text.
[49] Lubrizol Enter., Inc. v. Richmond Metal Finishers, Inc., 756 F.2d 1043, 1043 (4th Cir. 1985).
[50] *Id.* at 1048

Inc. ("Lubrizol").[51] In Chapter 11 bankruptcy proceedings, the debtor sought to reject the license in order to re-sell the technology at a higher price.[52]

In its finding, the Fourth Circuit overruled the district court.[53] The district court had noted that avoidance of a prior transaction was not a component of the rejection power.[54] According to the lower court, the mere fact that the debtor had sold an asset and could profit by taking it back to re-sell at a better price did not justify undermining contract law.[55]

The effect of *Lubrizol* was immediately and economically harmful.[56] Corporate activity faltered due to fears that a bankruptcy filing could nullify the benefits of any intellectual property rights contract.[57]

B. *Congress Leaves Out Trademarks*

Congress responded to *Lubrizol* in 1988 by passing the Intellectual Property Bankruptcy Protection Act ("IPBPA").[58] The IPBPA amended the Bankruptcy Code, adding subsection 365(n).[59] It appeared at first that section 365(n) would completely overrule *Lubrizol*.[60] The omission of trademarks from the Bankruptcy Code's definition of intellectual property, however, excluded them from the reach of subsection 365(n).[61] In light of this omission, until the *Sunbeam* decision, *Lubrizol* stood as the most relevant precedent regarding rejection of trademark licensing agreements in bankruptcy.[62]

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[51] *Id.* at 1045.
[52] *See id.*
[53] *Id.* at 1048 (noting that its decision conformed with the bankruptcy court holding).
[54] *See In re* Richmond Metal Finishers, Inc., 38 B.R. 341, 344 (Bankr. E.D. Va. 1984).
[55] *See id.*
[56] Westbrook, *supra* note 3, at 470 (noting the "immediate and awful" effects of *Lubrizol*).
[57] *See id.* As Senator Dennis DeConcini noted at the time, an intellectual property licensing agreement became "nothing more than a promise that can be broken." 133 CONG. REC. 23204–05 (1987).
[58] Westbrook, *supra* note 3, at 470. The IPBPA was passed as P.L. 100-506 (S. 1626) without an official title. Pub.L. 100-506 (S. 1626) (Oct. 18, 1988).
[59] *See* 133 CONG. REC. 23204–05 (1987); *see* 11 U.S.C. § 365(n)(2011)(providing that "if the trustee rejects an executory contract under which the debtor or licensor of a right to intellectual property, the licensee under such contract may elect to treat such contract as terminated . . . or to retain its rights . . . under such contract").
[60] *See* Sunbeam Prods., Inc. v. Chi. Am. Mfg.686 F.3d 372, 375 (7th Cir. 2012), *cert. denied*, 133 S. Ct. 790 (2012); 11 U.S.C. §§ 101(35A), 365(n).
[61] *See* 11 U.S.C. §§ 101(35A), 365(n).
[62] *See Sunbeam*, 686 F.3d at 375, 378 (stating that *Lubrizol* is the most relevant precedent and that there now exists a conflict among the circuits, respectively).

Evidence suggests that Congressional intent was primarily to protect companies in technology-intensive industries dependent on patents and copyrights.[63] The utility of trademarks was seen as being limited to quality assurance.[64] Therefore, the need to expand intellectual property protections to trademark licenses was seen as less urgent.[65]

Congress recognized in 1988 that trademarks licensed by a debtor occupy a special position in bankruptcy.[66] The Lanham Act requires that trademark licensing agreements include provisions for quality assurance.[67] If the licensor enters liquidation proceedings, it may be unable to assure the quality of the trademarked products.[68] Failure to assure quality by exercising reasonable control over the products subject to the mark results in abandonment of the mark by the licensor.[69]

C. *Factual and Procedural History of* Sunbeam Products

Lakewood Engineering and Manufacturing Co. ("Lakewood") manufactured and sold a variety of consumer products.[70] In 2008, it sold Chicago American Manufacturing, LLC ("CAM") the right

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[63] *See* Xuan-Thao N. Nguyen, *Bankrupting Trademarks*, 37 U.C. DAVIS L. REV. 1267, 1289–91 (2004)(referring to the bill by another unofficial title, the Intellectual Property Licensing in Bankruptcy Act); *see, e.g.,* H.R. 100-4657, at 13 (1988)(noting in the Judiciary Committee's opening statement the concerns of high-technology companies considered vital to the national economy).

[64] *See* Nguyen, *supra* note 63, at 1290–92; 133 CONG. REC. 23205 (1987).

[65] *Id.*

[66] *See* 133 CONG. REC. 23204–05 (showing that Congress understood the special nature of the problem in 1987); 3 MCCARTHY ON TRADEMARKS AND UNFAIR COMPETITION § 18:42 (4th ed.)(indicating the ongoing performance requirements of trademark licensing, which complicate rejection in bankruptcy). In fact, the status of the law regarding quality control in trademark licensing agreements is in flux. *See* Irene Calboli, *The Sunset of "Quality Control" in Modern Trademark Licensing*, 57 AM. U. L. REV. 341, 376–80 (2007)(noting that factors such as propertizing, franchising, and internationalization have diminished the rigor and utility of quality control). It is clear that licensors may hire third parties to assure quality. *See, e.g.,* Westco Group, Inc. v. K. B.Assocs., 128 F. Supp. 2d 1082, 1091 (N.D. Ohio 2001)(finding that the licensor exerted sufficient control over the licensee by monitoring operations through industry sources and sales representatives); *see also* Calboli, *supra* at 368–71 (describing methods of quality control deemed sufficient by the courts). In cases of longstanding business relationships between contracting parties, some courts have allowed licensees to police themselves. *See, e.g.,* Transgo, Inc. v. Ajac Transmission Parts Corp., 768 F.2d 1001, 1018 (9th Cir. 1985).

[67] Lanham Act § 5, 15 U.S.C. §§ 1051, 1055, 1127 (2011).

[68] *See, e.g.,* Eva's Bridal Ltd. v. Halanick Enter., Inc., 639 F.3d 788, 790 (7th Cir. 2011) (noting that failure to exercise reasonable control over the goods and services on which the mark is used by the licensee would result in abandonment of the trademark); Gen. Motors Corp. v. Gibson Chem. & Oil Corp., 786 F.2d 105, 110 (2d Cir. 1986) (stating that "[t]he critical question . . . is whether the licensees' operations are policed adequately to guarantee the quality of the products sold under the mark").

[69] *Eva's Bridal*, 639 F.3d at 790; RESTATEMENT (THIRD) OF UNFAIR COMPETITION§33(1995).

[70] *Sunbeam*, 686 F.3dat 374.

to practice Lakewood's fan patents, put Lakewood's trademarks on the completed fans, and ship the fans directly to Lakewood's customers for the 2009 box fan vending season.[71]

Lakewood's financial distress at the time informed the terms of the contract.[72] Because the deal required CAM to pay the upfront costs of manufacturing over one million fans, CAM refused to agree to the deal without some assurance against Lakewood's potential insolvency.[73] Lakewood therefore provided that if Lakewood failed to purchase the CAM-manufactured fans for its own sales accounts, CAM could sell the 2009 run of fans on its own behalf.[74]

Three months into the contract, Lakewood's creditors filed an involuntary bankruptcy petition against it.[75] The Chapter 7 trustee sold Lakewood's business, including the intellectual properties licensed to CAM, to Sunbeam Products, Inc. ("Sunbeam").[76] Sunbeam desired neither to buy CAM's Lakewood-branded fans nor to compete with CAM in the consumer fan market.[77] The trustee rejected the contract.[78] CAM continued to make and sell the Lakewood fans.[79] Sunbeam and the trustee filed an adversary proceeding to enjoin CAM from selling the fans.[80]

The bankruptcy court found for CAM on equitable grounds.[81] The court found that the unique requirements surrounding trademark law suggest that decisions in a bankruptcy context should be made on equitable grounds.[82] The quality assurance provisions of the license agreement were satisfied by CAM's upfront investment in the materials, packaging, and factory upgrades required to sell

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[71] *Id.*
[72] *Id.*
[73] *Id.*
[74] *Id.*
[75] *Id.*
[76] *Id.*
[77] *Id.*
[78] *Id.*
[79] *Id.*
[80] *Id.*
[81] *Id.* at 375.
[82] *See In re* Lakewood Eng'r & Mfg. Co., Inc., 459 B.R. 306, 345 (Bankr. N.D. Ill. 2011); In re Exide Technologies, 607 F.3d 957, 966–67 (3rd Cir. 2010)(Ambro, J., concurring)(providing analysis cited by In re *Lakewood* and *Sunbeam*).

Lakewood's fans.[83] Lakewood by that time had substantially completed its duties of quality assurance with regard to the fans produced by CAM.[84] Therefore, rejection of the license would not even burden the debtor with abandonment of the trademark.[85] There was no reason to terminate the trademark license.[86]

Sunbeam appealed to the Seventh Circuit.[87] In finding for CAM on appeal, the Seventh Circuit noted that outside of bankruptcy, a licensor's breach does not terminate a licensee's right to use intellectual property.[88] The court found no reason to treat a breach resulting from section 365 any differently than a state-law breach of contract claim.[89] The Seventh Circuit rejected the bankruptcy court's equitable grounds of decision.[90] It found that the Bankruptcy Code provided adequate and precise guidance on the issue.[91]

The Seventh Circuit's interpretation of the Bankruptcy Code also conflicted with *Lubrizol*.[92] In accordance with subsection 365(g), the Seventh Circuit restricted the rejection power to causation of a state-law breach of contract.[93] In so doing, the court ensured that rejection would be used the same way with regard to intellectual property as real and personal property.[94] The court noted that the avoidance powers of a trustee are limited to specified sections of the Bankruptcy Code.[95] The court noted on this basis that rejection is not functionally equivalent to rescission.[96] Based on this

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[83] *See In re Lakewood*, 459 B.R. at 314–15.
[84] *See id.* (describing Lakewood's oversight as CAM rebuilt and refurnished its manufacturing facility, hired new staff, and manufactured, packaged, and shipped the first orders of several hundred thousand fans).
[85] *See id.*at 345–47.
[86] *See id.*
[87] *See Sunbeam*, 686 F.3d at 375.
[88] *Id.* at 376.If the licensor fails to exercise reasonable control over the products governed by its mark, however, the mark will be abandoned. *See supra* note 69 and accompanying text.
[89] *See id.* at 376–77; *see also* 11 U.S.C. § 365(g)(2011).
[90] *Sunbeam*, 686 F.3d at 375–78.
[91] *See id.* at 375–77.
[92] *Id.* at 378.
[93] *Id.* at 377.
[94] *Id.* at 375–77.
[95] *Id.* at 377; *see also* 11 U.S.C. § 544(1998); 11 U.S.C. §§ 547-48 (2010)
[96] *Sunbeam*, 686 F.3d at 377.

distinction between rejection and avoidance, the court declined to void the contract.[97] The court stated that rejection would merely free the estate from the continuing obligation to perform under the contract.[98] The issue of how the licensor's future non-performance would affect the licensee was merely one of non-bankruptcy trademark law.[99]

III. The Case Against Avoidance and Equity

Sunbeam's holding is consistent with the Bankruptcy Code.[100] Section 365 states that rejection causes a backdated breach of contract, not a termination of rights of contracting parties.[101] A licensor's breach of a trademark agreement does not rescind the licensee's property rights.[102] In fact, such a breach would abandon the trademark to the licensee.[103]

Parties should know that a contract to license a trademark is a meaningful promise.[104] The *Lubrizol* approach would assist only a few undeserving debtors.[105] It would harm many parties and create an incentive against socially productive conduct.[106]

Furthermore, the equitable grounds approach ignores both the requirements of the Bankruptcy Code and the reality of trademark law.[107] If bankruptcy renders a licensor unable to assure the quali-

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[97] *Id.* at 377–78 (quoting Thompkins v. Lil' Joe Records, Inc., 476 F.3d 1294, 1306 (11th Cir. 2007).
[98] *Id.*
[99] *See id.*; *supra* note 88 and accompanying text.
[100] *See Sunbeam*, 686 F.3d at 377 (noting that *Lubrizol* conflicts with a clear interpretation of the Bankruptcy Code); Andrew, *supra* note 2, at 916–19; Westbrook, *supra* note 3, at 470–71; 133 CONG. REC. 23204–05 (1987).
[101] 11 U.S.C. § 365(g)(2011).
[102] *See Eva's Bridal*, 639 F.3d at 790; RESTATEMENT (THIRD) OF UNFAIR COMPETITION§33(1995).
[103] *See Eva's Bridal*, 639 F.3d at 790; RESTATEMENT (THIRD) OF UNFAIR COMPETITION§33. The fact that rejection would cause the licensor debtor to abandon its trademark and actually lose property is a policy argument against *Sunbeam*. *See supra* notes 29–32 and accompanying text (explaining the debtor's fresh start and the role of section 365 in allowing the trustee to make business decisions aiding the debtor). The unique restrictions on trademarks force courts to choose, however, between the bankruptcy policy of relieving the debtor of its burdens and the bankruptcy/property law policy of protecting creditors' rights. *See id.* The Seventh Circuit and a number of scholars simply argue that property protections are more important. *See infra* note 105 and accompanying text.
[104] *See* Andrew, *supra* note 2, at 916–19 (noting that the plaintiff in *Lubrizol* lost its valid license because of flimsy interpretations of executoriness); Westbrook, *supra* note 3, at 470–71 (noting that the resulting distrust of contract law after *Lubrizol* was "immediate and awful").
[105] *See* Andrew, *supra* note 2, at 916–19 (noting flimsiness of defendant's claims in *Lubrizol* and the fact that property rights should not be retaken once bargained away); Westbrook, *supra* note 3, at 470–71 (observing that established bankruptcy principles already serve the interests of most debtors seeking rejection).
[106] *See* Andrew, *supra* note 2, at 916–19; Westbrook, *supra* note 3, at 470–71.

ty of the products for which it has licensed its trademark, then the trademark will be considered abandoned.[108] Therefore, ruling on equity grounds merely gives trustees or DIPs an opportunity to confuse the business judgment foundation of section 365 with the special purpose of trademarks to assure product quality.[109] Bankruptcy law should not permit trustees and DIPs to re-sell previously disposed assets to the highest bidder.[110] Doing so would ultimately detract generally from public confidence in property rights, and specifically from the utility of trademarks to consumers.[111]

Both the *Lubrizol* and the equitable approaches would place contracting parties in positions of heightened risk and unpredictability.[112] The added burden to the already-volatile trademark licensing system would render parties hesitant to engage in commerce with any party perceived as even a slight bankruptcy risk.[113] Small businesses would be unable to afford such risk.[114] Large businesses would conduct transactions in foreign countries when at all possible.[115] Financially distressed companies holding valuable assets would find themselves unable to deploy them.[116]

The *Lubrizol* holding detracted from social welfare and the expectations of parties byover-privileging the interests of certain debtors.[117] The equitable approach subjugates the Bankruptcy

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[107] *See* RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065, 2073 (2012)(noting that courts must interpret the Bankruptcy Code itself clearly and predictably); Blum v. Stenson, 465 U.S. 886, 896 (1984)(noting that the language of the Bankruptcy Code is of paramount importance); *supra* note 88 and accompanying text.
[108] *See Gen. Motors*, 786 F.2d at 110.
[109] *See Sunbeam*, 686 F.3d at 375–77 (noting that judges' views of equitability are unreliable and that "rights depend . . . on what the Code provides rather than on notions of equity").
[110] *See id.*.
[111] *See id.*; *Calboli*, *supra* note 66, at 374 (noting that uncertainty surrounding quality control requirements of trademark licensing agreements has resulted in judicial uncertainty).
[112] *See* Lubrizol Enter., Inc. v. Richmond Metal Finishers, Inc., 756 F.2d 1043, 1043–48 (4th Cir. 1985)(holding that transferee's intellectual property rights were terminated by rejection); *In re* Lakewood, 459 B.R. at 345–47 (holding that effect of rejection on intellectual property rights was subject to equitability determination); Andrew, *supra* note 2, at 916–19 (criticizing *Lubrizol*).
[113] *See, e.g.,Sunbeam*, 686 F.3d at 374 (observing that Lakewood's financial distress had already rendered CAM wary).
[114] 133 CONG. REC. 23204 (1987)(observing that in a hypothetical *Lubrizol* scenario, "[a] successful business folds because it no longer has access to the intellectual property that its foundation was built on").
[115] *Id.* (noting that "this quirk in the bankruptcy law threatens American licensors competing in the international marketplace")
[116] *See, e.g.,Sunbeam*, 686 F.3d at 374–77 (indicating that if CAM had known it would lose its license in Lakewood's bankruptcy, it would not have entered into the contract); *see* Andrew, *supra* note 2, at 916–19; Westbrook, *supra* note 3, at 470–71.
[117] *See Sunbeam*, 686 F.3d at 374–77; Andrew, *supra* note 2, at 916–19; Westbrook, *supra* note 3, at 470–71.

Code and established principles of trademark law to more arbitrary standards of equity.[118] The Seventh Circuit was thus correct in its decision to effectively extend section 365(n) to include trademark licenses within intellectual property rights protections in bankruptcy.[119]

Conclusion

In *Sunbeam Products,* the Seventh Circuit created a circuit split by disagreeing with the Fourth Circuit's 1985 holding in *Lubrizol.* In so doing, the court extended the intellectual property protections provided by Congress in the 1988 IPBPA, and ruled in a manner consistent with the spirit of section 365 and the Bankruptcy Code in general. In the future, bankruptcy courts should follow *Sunbeam Products* in protecting the rights of trademark licensees subject to rejection actions in bankruptcy.

[118] *See* RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065, 2073 (2012); Blum v. Stenson, 465 U.S. 886, 896 (1984); Sunbeam, 686 F.3d at 375–76.
[119] *See Sunbeam*, 686 F.3d at 377; Andrew, *supra* note 2, at 916–19; Westbrook, *supra* note 3, at 470–71.