No. 17-1657

IN THE

Supreme Court of the United States

MISSION PRODUCT HOLDINGS, INC.,
Petitioner,

v.

TEMPNOLOGY, LLC, N/K/A OLD COLD LLC,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

REPLY BRIEF FOR PETITIONER

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INTRODUCTION

Tempnology admits that there is a square circuit split on the question whether, under §365(g) of the Bankruptcy Code, a debtor's rejection of a trademark license agreement strips the licensee of the right to use the trademark. It does not dispute the importance of the question, to which the amicus briefs in support of certiorari attest. Nor does it dispute that, given the First Circuit's decision to adopt the discredited reasoning of the Fourth Circuit in *Lubrizol* and to reject the Seventh Circuit's contrary approach, the courts of appeals will not resolve this split on their own.

Instead, Tempnology advances the startling contention that the split should not be resolved by the courts at all. Based on the legislative history of §365(n), Tempnology argues that the Congress of 1988 intended bankruptcy courts to address this question of statutory interpretation on a case-by-case, "equitable" basis, to inform potential future legislation. It claims this Court should not "forestall … legislative action" by "reach[ing] a uniform judicial resolution" of the issue. Opp. 3, 8-9. But it has been thirty years since Congress repudiated *Lubrizol*'s understanding of rejection by adopting §365(n). The courts are nonetheless at an impasse on the question whether *Lubrizol*'s reasoning applies to trademarks and other rights not enumerated in §365(n). And there is no congressional fix on the horizon. Only the Court's intervention will restore uniformity on this important issue of bankruptcy law.

Tempnology also argues that this case is not the appropriate vehicle for deciding the issue. Those arguments fail. Tempnology claims that the question presented cannot be decided without an extensive factual record regarding the burdens purportedly placed on the debtor by policing the licensee's use of the trademark. But the question presented is a pure question of law: Is rejection of a license agreement simply a "breach," as §365(g) provides, that enables a debtor to repudiate its own affirmative performance obligations under the agreement? Or does rejection give the debtor a special power to eliminate the licensee's rights under the agreement even if, outside bankruptcy, the debtor's breach could not affect those rights? The answer to that question does not turn on how "burdensome" it might be for a debtor to monitor the trademark. Accordingly, no factual record on that issue is necessary or even relevant.

Reviving an argument the First Circuit rejected, Tempnology also wrongly suggests that this case is moot. It says that the license agreement here has expired, and that Mission never sought to use the trademark in the two years before expiration. The first point is irrelevant, and the second is false. The agreement was rejected nine months *before* it expired. And Mission did seek to use the trademarks during the wind-down period; it has sought damages stemming from Tempnology's refusal to allow Mission to exercise its rights under the license agreement during that period. The amount of damages Mission recovers will depend on the answer to the questions presented here. There is thus no doubt that this is a live dispute.

Finally, Tempnology makes no effort to defend the First Circuit's related holding that an exclusive right to sell a patented product in a given territory is not a "right to intellectual property" under §365(n). The right to sell a patented invention is perhaps the most important right attaching to a patent. Pet. 30-35. Holding that such a right is not "intellectual property" defies the statute's plain text and common sense.

Together, the First Circuit's two holdings give debtors enormous and unwarranted power to strip licensees of their rights, thwarting Congress's design and undermining the intellectual-property licensing regime that Congress deemed key to technological and economic development. This Court should grant review.

I. THE COURT SHOULD GRANT REVIEW OF THE QUESTION WHETHER REJECTION TERMINATES A LICENSEE'S RIGHTS

A. Tempnology Admits The Clear Circuit Split

Tempnology admits that there is a square circuit split regarding the effect of rejection on licensees' rights. The best it can do is to quibble with the depth of the split and argue that review is "premature." Opp. 2-3, 5-9. But Tempnology offers no good reason to wait.

1. Tempnology argues that the disagreement is a 1-1 split between the First and Seventh Circuits, rather than a 2-1 split between the First and Fourth Circuits on the one hand and the Seventh Circuit on the other. Opp. 4-6. That is incorrect. Contrary to Tempnology's claim, the Fourth Circuit's reasoning in *Lubrizol* applied not just to patent licenses, but to all intellectual property licenses and indeed to all executory contracts. *Lubrizol* was a case about the consequences of rejection under §365(g), and it held that "by rejecting [an] agreement, [a] debtor could … deprive [the licensee] of all rights" conveyed under the agreement. *Lubrizol Enters, Inc.* v. *Richmond Metal Finishers, Inc.*, 756 F.2d 1043, 1048 (4th Cir. 1985).

The Seventh Circuit accordingly framed the question in *Sunbeam* as "whether *Lubrizol* correctly understood §365(g)." *Sunbeam Prods., Inc.* v. *Chicago Am. Mfg., LLC*, 686 F.3d 372, 376 (7th Cir. 2012). Finding

"*Lubrizol* mistaken," the Seventh Circuit held that "[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." *Id.* at 376-377. It expressly stated that its decision "create[d] a conflict among the circuits." *Id.* at 378. The First Circuit likewise acknowledged that "other circuits are split" on the question and expressly rejected *Sunbeam*'s interpretation of §365(g) in favor of *Lubrizol*'s "contrary approach." App. 2a, 22a-27a.[1]

More fundamentally, it makes no meaningful difference whether the split is 1-1 or 2-1. Tempnology does not dispute that the split exists and that the First Circuit's adoption of *Lubrizol*'s widely criticized approach, despite the Seventh Circuit's rejection of *Lubrizol*, makes clear that the split will not heal itself.

2. Nor should this Court wait for "bankruptcy courts to develop law … to inform … further Congressional action" (Opp. 8). Congress enacted §365(n)—repudiating *Lubrizol*—in 1988. Courts have thus had three decades to "develop law" on this question, and the result is an entrenched split among both the courts of appeals and the bankruptcy courts. And while Congress could potentially address the issue "through legislative action" (Opp. 9), that is true of any statutory interpretation case, and certainly not a reason to deny certiorari. It is both appropriate and necessary for this Court to step in to resolve the admitted split of

[1] Bankruptcy courts are likewise divided. Pet. 18. Contrary to Tempnology's claim (at 6), those decisions do not turn on factual distinctions but on the legal question whether *Lubrizol* correctly interpreted §365(g). Pet. 18 (citing cases adopting and rejecting *Lubrizol*).

authority over the interpretation of a central provision of the Bankruptcy Code.

B. The First Circuit's Decision Is Wrong

Tempnology's efforts to defend the merits of the First Circuit's decision fail.

1. Tempnology spends considerable space arguing that trademarks are not covered by §365(n). Opp. 7-9. Mission agrees. Pet. 2-3, 10, 17-18, 27. Tempnology's lengthy argument on this undisputed point merely confuses the issue.[2]

2. When Tempnology does address the actual question presented, it never grapples with the text of §365(g), which states that rejection is a "breach," or with *Sunbeam*'s interpretation of that text. Instead, it simply asserts that the First Circuit's decision furthers the purpose of rejection: to "'release the debtor's estate from burdensome obligations that can impede a successful reorganization.'" Opp. 10 (quoting *NLRB* v. *Bildisco & Bildisco*, 465 U.S. 513, 528 (1984)). What Tempnology and the First Circuit miss is that rejection permits the debtor to repudiate burdensome obligations *to perform under contracts*, at the price of paying damages to the counterparty. It does not permit the debtor to repudiate any and all obligations that might impede its reorganization. "No legislation pursues its purposes at all costs," *American Express Co.* v. *Italian Colors Rest.*, 570 U.S. 228, 234 (2013), and the Bankruptcy Code is no exception; it does not give debtors

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[2] Tempnology's rewrite of the first question presented to ask whether trademarks are "protect[ed] … under section 365(n)" (Opp. i) is similarly misleading. The first question presented does not concern §365(n), but whether, under §365(g), rejection terminates a licensee's rights. Pet. i.

the power to do anything that makes reorganizing easier.

Rather, under §365(g), rejection "constitutes a breach" of the rejected contract. Like a breach outside bankruptcy, rejection enables the debtor to repudiate its obligation to perform under a contract it deems unprofitable. The debtor benefits because the counterparty's damages are treated as a pre-petition claim, paid only whatever percentage other general unsecured creditors receive. But, also like a breach outside bankruptcy, rejection does not take away rights already conveyed to the counterparty. "§365(g) … establish[es] that in bankruptcy, as outside of it, the other party's rights [to use licensed intellectual property] remain in place" after rejection. *Sunbeam*, 686 F.3d at 377; *see* Pet. 22-25; Law Professors' Br. 2-17; International Trademark Ass'n (INTA) Br. 14-20.

The First Circuit concluded, and Tempnology argues, that this rule cannot apply to trademarks. Permitting a licensee to use a trademark after rejection, they claim, unduly burdens debtor-licensors, who may need to monitor the use of their trademarks if they want to retain ownership of them. App. 22a-24a; Opp. 10-14. But this is not the kind of "burden" rejection enables a debtor to shed. Any need Tempnology might have had to monitor its trademarks arose not from its agreement with Mission, but from trademark law applicable to all trademark owners. Pet. 28; INTA Br. 18-19. And, as noted, rejection relieves debtors only of obligations to perform under a contract; it cannot, by definition, absolve a debtor from generally applicable, noncontractual obligations. Nor does rejection empower a debtor to strip a licensee of a previously granted license to spare the debtor the "burden" of such noncontractual obligations.

Tempnology's argument is flawed for an additional reason. Recognizing that a licensee's rights survive rejection does not compel the licensor to monitor its trademark. Licensors monitor trademarks for their own benefit, and whether to do so is a choice. If the licensor chooses not to monitor, it could potentially forfeit its ownership of the mark. INTA Br. 18-19; *see, e.g.*, *Eva's Bridal Ltd.* v. *Halanick Enters., Inc.*, 639 F.3d 788, 789-791 (7th Cir. 2011).[3] But that does not make trademark monitoring an obligation that can be rejected in bankruptcy. The choice whether to monitor a trademark is no different than other choices debtors make every day regarding property of the bankruptcy estate: either to incur the necessary costs to preserve the property's value or, if those costs outweigh the benefits, to abandon the property. Rejection cannot relieve the debtor of such choices.[4]

3. Finally, the parade of horribles Tempnology claims will ensue if this Court reverses the First Circuit (Opp. 13) is imaginary. Recognizing that §365 does not empower debtors to undo deals made before bankruptcy would not enable counterparties to demand specific performance of a debtor's unperformed contractual obligations. It would not require any performance from debtors at all. It would simply ensure that licensees

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[3] As INTA notes (at 19-20), however, the standards for monitoring licensed trademarks have become increasingly lenient, and agreements typically require licensees to maintain quality-control standards—something a licensee would still have to do after rejection.

[4] Tempnology claims (at 10-12) that trademarks are distinct from other forms of intellectual property, but fails to explain how those distinctions could make a difference to the meaning of rejection under §365(g).

retain the right to use intellectual property after rejection of a license agreement, as they would after breach of such an agreement outside bankruptcy. Nor would recognizing §365's limitations mean that licensees could use the licensed property without paying royalties. Outside bankruptcy, if a licensee wants to continue using licensed intellectual property after a licensor's breach, the licensee must still comply with the terms of the license, including any requirement to pay royalties. *See, e.g.*, *S&R Corp.* v. *Jiffy Lube Int'l, Inc.*, 968 F.2d 371, 376-378 (3d Cir. 1992); *Boscorale Operating, LLC* v. *Nautica Apparel, Inc.*, 749 N.Y.S.2d 233, 234-235 (App. Div. 2002); INTA Br. 9. The same principle applies in bankruptcy.

C. This Case Is An Excellent Vehicle For Resolving The Question

As a last resort, Tempnology attempts to manufacture vehicle problems. Those supposed problems are illusory.

1. Tempnology contends that the Court should deny review because of the "thin evidentiary record" on points like the burden on the debtor of continued policing of trademarks. Opp. 14. But that "burden" is irrelevant to the pure question of law here: whether, under §365(g), rejection of a license agreement terminates the licensee's rights that would survive breach outside bankruptcy. This question of statutory construction does not—and cannot, as a matter of logic—turn on the nature or extent of the "burden" a debtor might have to bear if the licensee's rights do survive rejection.

2. Tempnology also suggests that this case is "an academic exercise that cannot concretely affect these parties." Opp. 1, 15-16. That is untrue—as the First

Circuit concluded after the parties briefed mootness. C.A. Order (Aug. 30, 2017).

Tempnology states that the license agreement is now terminated, but that does not moot this case. The agreement terminated nine months *after* Tempnology rejected it. App. 4a-5a, 83a-84a. The parties consequently have a live disagreement over the scope of Mission's rights, and Mission's damages for the violation of those rights, during that post-rejection, pre-termination period. If this Court grants certiorari, its decision will determine how Mission's claim for over $4 million in damages will be treated. Indeed, Tempnology agreed to stay proceedings on Mission's damages claim pending this Court's resolution of the petition, acknowledging that the outcome here affects Mission's claim. C.A. Mission Resp. (Sept. 8, 2017), Ex. B (claim); Stipulated Order, Bankr. Dkt. 519.

Tempnology also contends (at 1, 16) that Mission never sought to exploit the licensed trademarks during the two years before the agreement terminated. That is incorrect. As the arbitrator found, Mission placed orders and sought to use the trademarks during that period, but Tempnology thwarted Mission by wrongfully repudiating the agreement and demanding that Mission cease using its trademarks. Partial Final Award 11-13, Bankr. Dkt. 99-2. In short, there is no obstacle to this Court's granting review.

II. THE COURT SHOULD GRANT REVIEW OF THE QUESTION WHETHER AN EXCLUSIVE RIGHT TO SELL PATENTED PRODUCTS IS A "RIGHT TO INTELLECTUAL PROPERTY" UNDER §365(n)

Tempnology does not defend the First Circuit's holding that an exclusive right to sell patented products within a particular field of use and territory is not a "right to intellectual property" under §365(n). Instead, it inexplicably addresses an entirely different question, arguing that §365(n)'s protection for exclusivity provisions extends only to provisions granting exclusive rights to intellectual property. Opp. 18. But the petition never argued otherwise. Rather, it demonstrated that the exclusive right to distribute a patented product *is* a right to intellectual property—specifically, a right to sell a patented invention—under the statute's plain language, and that the First Circuit seriously erred in holding otherwise. Pet. 31-35. Tempnology has nothing to say in response.

The First Circuit is the first court of appeals, to Mission's knowledge, to address this issue. That is undoubtedly because, before this case, no one had ever questioned whether an exclusive right to sell products practicing a patent—even if limited to a particular field of use and territory—is a right to intellectual property. Plainly, it is: It is a stick in the bundle of rights that make up patent ownership, and such sticks are often licensed individually. Pet. 31-35. Lower courts have found it obvious that such an exclusive right to sell a patented product is "precisely the kind of exclusive intellectual property right[] that [is] protected" by §365(n). *In re SIMA Int'l, Inc.*, 2018 WL 2293705, at *10 (Bankr. D. Conn. May 17, 2018); *see* Pet. 33 (citing cases).

On its own, the First Circuit's misapprehension of what constitutes a "right to intellectual property" would be a candidate for summary reversal. *See, e.g.*, *Nitro-Lift Techs., LLC* v. *Howard*, 568 U.S. 17, 18 (2012) (per curiam) (summarily vacating decision for "ignor[ing] a basic tenet of the [Federal Arbitration] Act[]"); *Marmet Health Care Ctr., Inc.* v. *Brown*, 565

U.S. 530, 532 (2012) (per curiam) (summarily vacating decision for "incorrect" interpretation of Federal Arbitration Act). But since it accompanied the First Circuit's equally misguided understanding of "rejection," as to which there is a square circuit split, this Court should grant both questions and set the case for full briefing and argument. Considering the two questions together will enable the Court to clarify the scope of intellectual property licensees' rights both under §365(g)'s definition of "rejection" and under the safe harbor of §365(n).

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The First Circuit's decision has far-reaching ramifications. Its adoption of *Lubrizol*'s discredited reasoning threatens not only trademark licensees—which would be enough—but any party to a contract whose rights would survive the other party's breach outside bankruptcy. Reading §365 to grant debtors a broad power to undo deals made before bankruptcy, without satisfying the specific criteria for avoiding transfers of property set out elsewhere in the Code, contravenes the statute's text and the consensus of courts and scholars. It also threatens licensees' ability to rely on their license agreements and thus jeopardizes the stability of the intellectual property licensing scheme as a whole. INTA Br. 21-27. And the First Circuit's failure to recognize that a right to sell a patented product is an intellectual property right exacerbates that threat by depriving a large group of licensees of §365(n)'s intended protections. The Court should grant certiorari and restore uniformity and certainty on both of the exceptionally important questions presented.

CONCLUSION

The petition should be granted.

Respectfully submitted.

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