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6 KEY TAKEAWAYS

Takeaways from *Mission Product vs. Tempnology* for Brand Licensing and Franchising

Kilpatrick Townsend's Paul Rosenblatt and David Posner, bankruptcy partners, and Marc Lieberstein, a brand licensing and franchise partner, recently published an article in the New York State Bar Association Intellectual Property Section Bright Ideas publication in January 2020 titled The Impact of Mission Product v. Tempnology on Brand License and Franchise Agreements. David also spoke at the January 28, 2020 Annual Meeting for the Intellectual Property Section on this recent Supreme Court decision that impacts the way trademark licensors/ franchisors and licensees/franchisees approach their respective agreements. We thought our clients and colleagues would appreciate the following takeaways:

1 The law is now settled, the rejection of an executory trademark license/franchise agreement by a bankrupt licensor/franchisor results in a breach of that agreement rather than an unwinding of the agreement.

2 While the Supreme Court clarified the law with respect to the effect of a rejection of a trademark license/franchise agreement, the Court did not hold the inverse, namely, that the licensee/franchisee can continue using the mark in every instance following rejection. Rather, the inquiry is whether the licensee's right to continue using the mark would survive under applicable non-bankruptcy law or the terms of the relevant agreement had the licensor breached the agreement outside of a bankruptcy case.

3 One way the parties can address their respective rights post-bankruptcy is to expressly incorporate the provisions of Section 365(n) of the Bankruptcy Code into their agreement. This will result in a licensee/franchisee being allowed to use the trademark after bankruptcy, but it will mandate that the licensee/franchisee fully comply with their obligations under the license/franchise agreement including making royalty payments without any reciprocal obligations by the debtor licensor. The licensee/franchisee will also forfeit the ability to set off against the royalties due for any failures of the debtor licensor to perform under the agreement and the licensee/franchisee will no longer have a right to seek specific performance from the debtor licensor.

Given that the licensee's post-rejection rights may be greater under the agreement or applicable non-bankruptcy law than those provided by 365(n), the parties to such agreement should carefully look at applicable law governing termination to see if those applicable non-bankruptcy laws are more favorable to their specific commercial situation than the provisions of 365(n) would be. This is particularly true in the franchising context where there are several states whose law make it much more difficult for a franchisor to terminate the franchise agreement.

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Non-debtor trademark licensee/franchisees must remain vigilant in the face of a debtor licensor/franchisor's bankruptcy. A debtor that seeks permission from the bankruptcy court to reject a trademark license could also ask the bankruptcy court to restrict the non-debtor licensee/franchisee's continued use of the license/franchise based upon applicable equitable principles. The law in this area is developing. Failing to respond to a debtor's motion seeking such relief could result in the bankruptcy court entering an order that is adverse to the non-debtor licensee/franchisee's continue use rights.

While not related to *Mission Product v. Tempnology*, here's an extra bankruptcy takeaway for those franchisors or brand owners thinking about starting up a cannabis business -- a business that is related to, sells to or derives substantial revenue from a cannabis business or licenses marks to or from a cannabis business -- if for some reason things do not go well, bankruptcy may not be an option for you or the company you are doing business with. Notwithstanding state laws legalizing cannabis, cannabis is still an "illegal drug" under the Controlled Substance Act the result of which is that the Department of Justice and most bankruptcy courts have taken the position that cannabis companies and companies that are related to a cannabis business – whether growers, marketers, retail stores, landlords, or manufacturers of products used by cannabis companies – are not eligible to file for bankruptcy as it would require a federal court to put its approval on a business that operates in violation of federal criminal law. In other words, no protection from creditors via bankruptcy, no ability to reorganize, take time to pay off debts or maximizing the value of assets via the protections of a bankruptcy sale process where often times intellectual property is the most valuable asset. While thinking about the end of a business is usually not the best way to start one, it's probably wise to consider an exit strategy before investing in a cannabis or related business.

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