



AMERICAN  
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## 2022 Annual Spring Meeting

# The Monetization of Intellectual Property in Bankruptcy and Restructuring

Sponsored by Cooley LLP and Gordon Brothers

**Leslie S. Zmugg, Moderator**

Gordon Brothers; Boston

**Dr. Arthur A. Daemmrigh**

The Lemelson Center; Washington, D.C.

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Limpert & Associates; Toronto

**Joshua Pichinson**

Sherwood Partners, Inc./agencyIP; Santa Clara, Calif.



**American Bankruptcy Institute 2022  
Annual Spring Meeting  
Monetization of Intellectual Property in  
Bankruptcy and Restructuring  
Friday, April 29, 2022 at 11:30 a.m.  
Eastern Time**

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## Topics to Be Discussed

- Introduction of Panel Topic
- Introduction of Moderator and Panelists
- History of Intellectual Property (IP) Monetization in Bankruptcies and Restructuring
- Scope of Intellectual Property that Will Be Discussed
- When the Team Is the IP
- Post-Acquisition Integration
- Monetization: A Solution for Financial Recovery
- Use of Special Purpose Entities
- Lending Process
- The Uniqueness of Brands
- The Impact of Licenses on IP Monetization
- Cross-Border and International Matters
- Infringement Within Bankruptcy
- Other Topics
- Closing and Questions



## Panel Description

This panel will discuss why monetization of Intellectual Property (IP) has become a key strategic tool in restructuring, bankruptcy and acquisitions, and how the importance of monetization has evolved over the decades. Discussing this topic will be experts in innovation, the role IP plays in bankruptcy and restructuring, how cross-border situations impact the monetization of IP, post-acquisition integration of the IP “footprint,” and other key topics of interest.



## Moderator and Panelists

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## History of Intellectual Property Monetization in Bankruptcies and Restructuring



## Bankruptcy and Property: Historical Perspective

- 18<sup>th</sup> century: shift from debt as a moral economy (personal, including repayment extending to the physical body of the debtor) to impersonal market relations
  - Innovations include assignability of notes and bonds
  - Insolvency shifts from being seen as sin to failure; from moral to economic
- 19<sup>th</sup> century: risk-taking becomes more acceptable, and is key to America's economic growth
  - Many speculative ventures (canals, rail), and cycles of boom and bust
  - Bankruptcy laws were passed, but also repealed as creditors felt they were too lenient on debtors
- Late 19<sup>th</sup> century
  - Era of independent inventors – thousands of Americans get patents, many start businesses, many fail
  - From 1880s on, larger firms (e.g., rail, electricity) buy up the IP from independent inventors, or acquire it after they fail
  - Some independent inventors used modern approaches. Edison's "talking doll" was sold by a separate company he established (Edison Toy Phonograph Company) to find new uses for a miniaturized version of his wax reel phonograph. Heavy and scary, they sold poorly, and the company was closed. Edison went on to other successes.



## Bankruptcy and Property: Historical Perspective

- 20<sup>th</sup> century: rise of industrial R&D (corporate-owned IP)
  - WWI and WWII: Governments expropriate IP or prevent patenting in key strategic areas
  - IP after bankruptcy mostly unused or abandoned (not enforced)
  - New approach of speculative IPOs, e.g., Tucker, whose car had numerous safety and design innovations later adopted more widely (and some not, such as the directional headlamp) – all assets auctioned in 1950 after Tucker was acquitted of fraud
- Late 20<sup>th</sup>/early 21<sup>st</sup> c.: re-emergence of independent inventors, growth of startup economy
  - Innovations in bankruptcy (assignment on behalf of creditors)





## Bankruptcy and Property: Historical Perspective

Valuing IP (especially patents) has always been challenging:

- Limited enforcement period (patents expire)
- Majority of patents do not become products on their own; even experts in the art may not know how patented technologies interrelate until a product is finalized
- Lack of public information on patent transactions (licensing, sales)

Recently, some firms have aimed to bundle patents and sell tranches (turning a limited asset class into a larger, stratified investment possibility) — this is especially feasible post-bankruptcy



## License Issues



## How Licenses Can Impact IP Monetization

- IP licensors in restructuring or bankruptcy
  - Outbound licensees can use Section 365(n) to retain many license rights
  - Generally not possible to sell IP free and clear of existing licenses if licensee objects
  - Often a major part of the value of IP is in royalties, future milestone payments, and customer revenue related to licenses
- IP licensees in restructuring or bankruptcy
  - In-licensed IP may be crucial to the company's value
  - Assignment provisions may restrict ability to assign inbound licenses in a sale
  - In some circuits, licensees in bankruptcy risk losing the inbound license entirely absent consent from the licensor
  - Termination provisions such as insolvency or an ABC may be enforceable absent licensor consent or a bankruptcy filing



## Licensor in Bankruptcy: Licensee Protections Under Section 365(n)

- Under Section 365(n), upon rejection the non-debtor licensee can make an election:
  - **Option One:** treat the license as terminated, cease using the IP, and file a damages claim
  - **Option Two:** retain rights to the licensed IP (including exclusivity) for duration of contract plus any extensions – but must pay all royalties and give up setoff/administrative claim
- Trustee/debtor in possession must:
  - Provide licensee the embodiment of the IP (to the extent provided in the license)
  - Not interfere with licensee's IP rights



## Licensor in Bankruptcy: What Is “Intellectual Property” for Bankruptcy Purposes?

Pursuant to Section 101(35A) of the Bankruptcy Code, the term “Intellectual Property” means —

- A) Trade secret;
- B) Invention, process, design, or plant protected under title 35;
- C) Patent application;
- D) Plant variety;
- E) Work of authorship protected under title 17; or
- F) Mask work protected under chapter 9 of title 17.



## Licensor in Bankruptcy: What’s Missing from the Bankruptcy Code’s IP Definition?

- Trademarks
- Service marks
- Data (if not subject to copyright or other covered IP protection)
- Other IP not protected under U.S. law



## Licensor in Bankruptcy: Trademark Licenses

- For decades, trademark licensees were at risk of losing all license rights upon rejection, with courts holding that rejection terminated the licensee's rights
- Then a circuit split developed on the impact of rejection, and the issue went before the U.S. Supreme Court
- On May 20, 2019, the Supreme Court ruled in *Mission Product Holdings, Inc. v. Tempnology, LLC*, 139 S. Ct. 1652 (2019), that **rejection means breach and not rescission**, a huge win for trademark licensees
- Rejection does not terminate trademark licensee's rights to use the trademarks
- "[R]ejection 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, remain in place."
- The "debtor can stop performing its remaining obligations" but "cannot rescind the license already conveyed," and the "licensee can continue to do whatever the license authorizes."



## Licensor in Bankruptcy: Where Does This Leave Trademark Licensees?

- The *Tempnology* decision means trademark licensees retain their license rights after rejection but leaves several open questions:
  - Does the licensee have to make required royalty and other payments?
  - Are setoffs possible?
  - Are administrative claims for breach allowed?
  - Does rejection impact license term and options to extend?
  - Do exclusive or other distribution rights survive rejection?



## After *Tempnology*: Key Trademark License Drafting Considerations

- Risk of abandonment
- Quality control
- New product approvals
- Step-in rights
- Automatic stay issues
- Access to goods manufactured by licensor
- Winding down period and termination issues



## After *Tempnology*: Other License Issues

- Protection for licensees of datasets/other IP rights not covered by Section 365(n)
- Contractually incorporate Section 365(n)'s core provisions
  - Post-rejection termination right for licensor, despite *Tempnology*
  - Delegation of quality control rights to trademark licensee or others



## After *Tempnology*: Is Section 365(n) Mandatory for Covered IP or a Safe Harbor?

- Justice Sotomayor's *Tempnology* concurrence:
  - Section 365(n) is binding on intellectual property licenses covered by its terms
  - Rights of trademark licensees are "more expansive" than licensees of IP covered under Sections 101(35A) and 365(n)
- *Tempnology* majority opinion did not state whether holding applies to IP covered by Section 365(n)
  - Called Section 365(n) a "remedial scheme embellishing on or tweaking the general rejection-as-breach rule"
  - Did not refer to Justice Sotomayor's concurring opinion



## After *Tempnology*: Is Section 365(n) Mandatory for Covered IP or a Safe Harbor?

- If Section 365(n) is just a safe harbor:
  - Can licensees of patents, copyrights or trade secrets use *Tempnology*?
  - Does licensee keep other rights, such as exclusivity?
  - Are setoff or administrative claims possible?
  - How long do license rights continue?
  - What about foreign patents?



## Licensee in Bankruptcy: Section 365(c)(1)'s Restrictions

Section 365(c)(1) of the U.S. Bankruptcy Code

(c) The trustee may not assume or assign any executory contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if —

(1)(A) applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to an entity other than the debtor or the debtor in possession, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties; and

(B) such party does not consent to such assumption or assignment



## Licensee in Bankruptcy: Can IP License Be Assigned?

- Most Courts of Appeals have ruled that “applicable law” includes patent and copyright law
- Seventh Circuit in *In re XMH Corp.*, 647 F.3d 690 (7th Cir. 2011), and an unpublished Ninth Circuit decision hold that trademark licenses are also personal and non-assignable without consent
- Federal courts generally hold that *non-exclusive* patent and copyright licenses are personal to the licensee and not assignable without consent of the licensor
- Ninth Circuit’s decision in *Gardner v. Nike*, 279 F.3d 774 (9th Cir. 2002), holds that *exclusive* copyright licenses also are not assignable without copyright-holder’s consent
- Exclusive patent licenses likely are also not assignable without the patentee’s consent, but there is little case law



## Licensee in Bankruptcy: Can an IP License Even Be Assumed?

- Two interpretations of Section 365(c)(1)'s language: the “hypothetical test” and the “actual test”
  - **Hypothetical test:** if applicable non-bankruptcy law precludes a debtor from *assigning* the executory contract to a third party outside of bankruptcy, the debtor may not assume or assign the contract, even if the debtor seeks only to assume it  
*Three Circuits (3d, 4th and 9th) have adopted this approach*
  - **Actual test:** if applicable non-bankruptcy law precludes a debtor from assigning the executory contract to a third party outside of bankruptcy, the executory contract is assumable unless the debtor actually intends to assign the contract  
*Adopted by 1st Circuit, essentially by 5th Circuit, and by numerous lower courts*



## Licensee in Bankruptcy: Another Approach to Assumption

- The *Footstar* decision from the Southern District of New York questioned whether Section 365(c)(1) even applies to a debtor in possession attempting to assume an agreement to which applicable law would preclude assignment – *In re Footstar*, 323 B.R. 566, 570-72 (Bankr. S.D.N.Y. 2005)
- *Footstar* decision functions like an actual test and allows assumption by a DIP, although likely not a trustee
- In *Footstar*, court held that Section 365(c)(1) applies only to a “trustee” and not to a debtor in possession when the DIP proposes to assume and not assign the agreement



## Licensee in Bankruptcy: Another Way to Assume or Assign an IP License

- Applicable law and Section 365(c)(1) prohibit assignment, and sometimes assumption, absent “consent” of licensor
- So what constitutes consent?
  - Many courts will enforce provisions in license agreement in which licensor gave advance, conditional consent to assignment of license
  - License agreements sometimes contain provisions consenting to assignment “in connection with a sale of all or substantially all of the assets” of the licensee
  - If consent conditions are met, may permit assumption and assignment in all circuits
  - Minority view: In *In re Sunterra Corp.*, 361 F.3d 257 (4th Cir. 2004), Fourth Circuit refused to treat prepetition consent language as sufficient consent under Section 365(c)(1)



## Licensee in Bankruptcy: Another Way to Assume or Assign an IP License

- Despite Section 365(c)(1), many IP licensors are willing to allow assumption of IP licenses and in some cases even assignment
  - In exchange for their consent, licensors may ask for an assignment fee or conditions to protect the licensor’s rights
  - These conditions may include provisions that extend beyond “adequate assurance of future performance” and impose specific, higher standards
  - Inventors or others emotionally invested in the IP, and licensors with concerns about competitors gaining control of IP or trademarks, are the most likely to object



## Infringement Claims in Bankruptcy

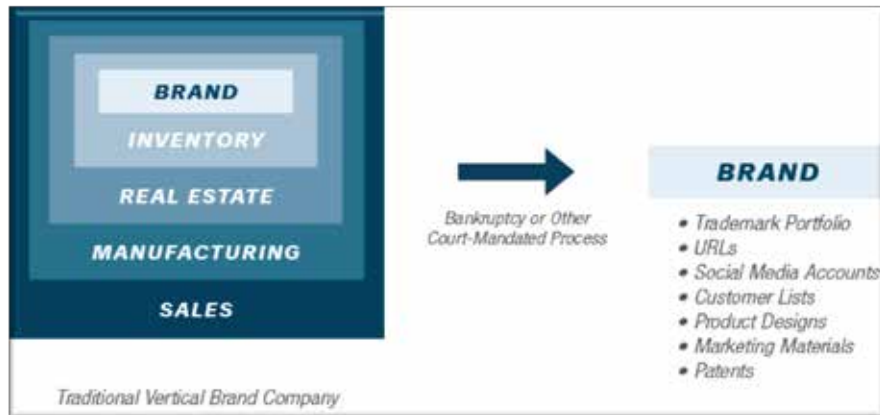
- **Continuing Infringement:**
  - If debtor continues to infringe IP rights, the IP owner may have an “administrative claim” in a chapter 11 case. See *In re Eagle-Picher Indus., Inc.*, 447 F.3d 461 (6th Cir. 2006) (claim survived plan confirmation)
  - Non-debtor IP owner may be able to pursue infringement claims, including seeking injunctive relief for continuing infringement in a non-bankruptcy court or pursuing an ITC action, although the automatic stay likely applies and relief from stay would be required
- **Past Infringement:** An IP owner can file a proof of claim for past infringement violations, but claim is unsecured and paid in bankruptcy dollars
- **Nondischargeability Issues:** Claims against an individual debtor (and possibly against a Subchapter V corporate debtor) may be nondischargeable as willful and malicious injury claims, while continuing, post-petition infringement claims are likely not even covered by the discharge



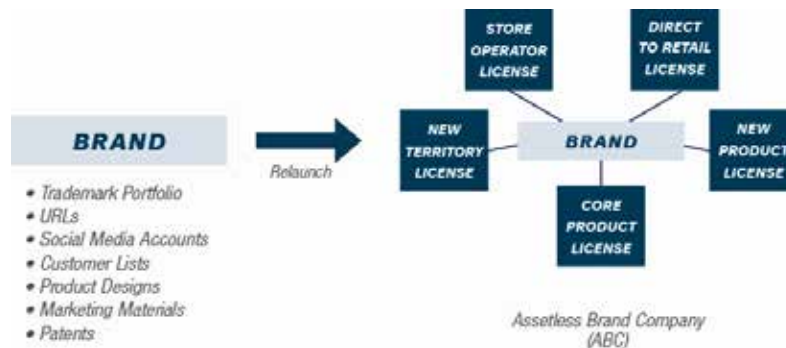
## The Uniqueness of Brands



## Saving the Brand: Conversion from OpCo to IpCo



## Leveraging the Brand: Conversion from OpCo to IpCo





## International Aspects of Monetization of IP in Bankruptcy



### IP Assets Are Different than Many Types of Assets

- The validity (scope) of registered IP rights is uncertain
- *E.g.*, In some jurisdictions, up to half of patent claims are held invalid if challenged in court proceedings
- For some types of rights (copyright/software or trade secrets/confidential information), independent creation is a full defense to allegations of infringement
- In general, you cannot determine the scope of the rights just by looking at what a patent or trademark examiner has approved



## Patents Are Subject to Freedom-to-Operate Issues

- A person (first person) holding/using patent rights may be at risk of being sued by third persons for infringing third-person patent rights
  - *i.e.*, the third person may hold blocking or enabling patents to which a license is required to use the first-person patent rights
- Having a registered patent does not guarantee that these freedom-to-operate issues have been resolved
- Uncertain scope and freedom-to-operate issues may create uncertainty about the value of IP rights



## Ownership May Be Quite Uncertain for Some Types of IP

- Ownership is often "cloudy" for copyright works (*e.g.*, software) and trade secrets/confidential information
- Unless there is a clear "chain of title," ownership can often be challenged
- It can be costly to investigate and fix these problems



## How Will IP Licenses Be Handled in Insolvency Proceedings?

Some countries (*i.e.*, Canada) have legislation that is similar to U.S. Section 365(n) permitting a license to continue despite licensor's bankruptcy

*I.e.*, trustee of insolvent licensor cannot disclaim grant of rights to licensee

Note: this does not affect "executory" aspects of license, such as licensor's obligation to provider ongoing maintenance and support of licensed software



## How Will IP Licenses Be Handled in Insolvency Proceedings? (Cont.)

- These executory aspects of an IP license can be disclaimed by trustee of insolvent licensor
  - This may significantly diminish the value of software rights, even if right to license the software continues
- Many countries do not have equivalent legislation to U.S. Section 365(n)
- In some countries, clauses terminating the license upon the insolvency proceedings of a party are valid and enforceable
- In some countries, rights of trustees to deal with insolvent licensors' licenses may be affected by whether the license is registered with the national intellectual property office



## Licensee Bankruptcy

- **Key Question:** Can the trustee/receiver of insolvent licensee assign the license to a third person?
- In some countries, a license is considered personal and cannot be assigned
- In some countries, a clause prohibiting assignment of a license by a licensee will not be valid/enforced in the insolvency proceedings of the licensee



## Cross-Border Insolvency Proceedings

UNCITRAL Model Law on Cross-Border Insolvency is applicable in U.S., Canada, U.K. and 41 other countries

Court will determine the "centre of main interests" (COMI) of the insolvent party; this determines the jurisdiction of insolvency law

However, the governing law of a license agreement determines the interpretation of the license agreement



## Many Other Legal Issues Affect Monetization of IP in Bankruptcy

- Privacy Laws:  
May affect ability of trustee to transfer personal information to third persons
- Reversionary Rights  
In some countries, insolvency proceedings initiate automatic transfer of some IP rights back to author/inventor/creator
- Moral Rights  
  
Moral rights (droits d'auteurs) exist in most countries  
  
These may affect monetization of IP, particularly if monetization involves using the IP for a significantly new purpose



## International Legal Issues Affecting Monetization of IP (Cont.)

- In some countries, inventors have a right to receive trailing royalties if the patent is successful
- March-in rights and other governmental rights to receive or grant compulsory licenses
- Standard Essential Rights (obligations to grant licenses on FRAND terms)
- In some countries, there are limited rights to take proceedings against unauthorized recipients of trade secrets and confidential information



Thank you!

# Faculty

**Dr. Arthur A. Daemmerich** is the director of the Smithsonian Institution's Lemelson Center for the Study of Invention and Innovation in Washington, D.C. Located at the National Museum of American History, the Center explores the role of invention and innovation in the U.S., particularly its historical context, and how that history relates to current events. Previously, Mr. Daemmerich was an associate professor at the University of Kansas Medical Center, a visiting professor of business administration at the China Europe International Business School, an assistant professor of business administration at the Harvard Business School's Business, Government, and the International Economy Unit, a visiting assistant professor at the University of Pennsylvania's Department of History and Sociology of Science, and a director at the Science History Institute. He is a frequent writer and lecturer and sits on the board of the American Institute of the History of Pharmacy. He also received the Dibner Award for Excellence in Museum Exhibits from the Society for the History of Technology. Mr. Daemmerich received his B.A. in history and sociology of science and German literature from the University of Pennsylvania in 1991, and his M.A. and Ph.D. in science and technology studies from Cornell University in 1996 and 2002, respectively.

**Robert L. Eisenbach, III** is Of Counsel with Cooley LLP in its Business Restructuring & Reorganization group in San Francisco. He focuses his practice on restructuring, bankruptcy, distressed M&A and related litigation. Mr. Eisenbach is regularly involved in cases throughout the country, including in California, Delaware and New York. He has been consistently listed in *The Best Lawyers in America* for Bankruptcy and Creditor-Debtor Rights Law and has been recognized as a Northern California *Super Lawyer*. For more than 30 years, Mr. Eisenbach has guided companies and their boards of directors through chapter 11 and out-of-court restructurings and recapitalizations, whether it is a billion-dollar company restructuring publicly held debt, a middle-market company or a technology startup. He is often asked to bring his distressed M&A expertise to bear in helping companies and private-equity firms navigate the unique issues involved when buying or selling assets of financially troubled or bankrupt companies. On the creditor side, Mr. Eisenbach frequently represents unsecured creditors' committees in chapter 11 cases in a range of industries, including retail, semiconductor and storage technology, biotechnology and health care. In addition, he has specific expertise in chapter 15 cross-border bankruptcy cases involving companies in Europe and Asia. Mr. Eisenbach has litigated a wide variety of bankruptcy-related disputes, director and officer liability litigation, complex commercial litigation and intellectual property cases. He received his J.D. from the University of Virginia School of Law in 1985, where he was a member of the Order of the Coif, and his B.A. *summa cum laude* in political science and economics from Louisiana State University in 1982. Upon graduation from LSU, he was awarded the University Medal for Highest Academic Achievement and received a Phi Kappa Phi National Graduate Fellowship.

**P. Bradley Limpert, CLP** is the founder of Limpert & Associates in Toronto, where his practice focuses on technology law, principally in the areas of litigation and commercialization. He previously practiced at one of Canada's largest boutiques and was a partner and chair of the National Technology Practice Group at one of Canada's largest law firms. Mr. Limpert has obtained multimillion-dollar settlements and judgments for his clients, as well as injunctive relief and civil search warrants. He has advised clients on more than 500 licensing transactions and in more than 200 financing and

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**Joshua Pichinson** is the managing director of agencyIP in Santa Clara, Calif., which represents creators and owners of intellectual property (IP) in the areas of sales, licensing and strategy. He also is managing director of Sherwood Partners Inc, agencyIP's sister company, which provides business advisory services to the venture capital, private-equity, legal and financial communities. Mr. Pichinson oversees clients' IP sales, marketing, licensing and strategy requirement, and he is responsible for the intercompany process improvement and strategy for both firms. He is experienced in the monetization of IP in going-concern businesses as well as bankruptcy and restructuring. Mr. Pichinson has been with Sherwood Partners for more than 10 years and is actively involved in due diligence associated with licensing and sales of IP, as well as the wind-down efforts of companies with significant intellectual property assets. He specializes in maximizing the value of both intangible and tangible assets. Mr. Pichinson is an active speaker on the subject of IP and for the past four years has been on the world's leading 300 IP Strategists list and recognized in *IAM Strategy 300*. He received his B.S. in business administration with an entrepreneurial emphasis from Chapman University.

**Leslie S. Zmugg** is general counsel, chief compliance officer and corporate secretary at Gordon Brothers in Boston. She is responsible for leading the firm's worldwide legal function and oversees all corporate compliance activities. Ms. Zmugg has more than 20 years of experience leading global corporate legal strategy and operations. Prior to joining Gordon Brothers, she worked in various legal roles for Caterpillar Inc., most recently as general counsel and secretary for Caterpillar Financial, its captive financing arm. In this role, she managed the company's global legal function with more than 70 legal professionals worldwide. Ms. Zmugg began her career in New York, where she focused on asset-based finance, bankruptcy and corporate restructuring. She is an active member of the planning committee for Tina's Wish and a cross-border mentor in the Black Lawyers Matter program with the Stephen James Partnership. Ms. Zmugg received her B.A. in philosophy from Binghamton University and her J.D. from Fordham University School of Law.