WAKE FOREST JOURNAL OF BUSINESS AND INTELLECTUAL PROPERTY LAW

VOLUME 16 SPRING 2016 NUMBER 3

ADDRESSING UNFAIRNESS TO NON-DEBTOR PATENT LICENSEES IN BANKRUPTCY FREE AND CLEAR OF SALES: ISSUES OF TIMING, NOTICE & CONSENT

Anne M. Culotta[†]

[†] Anne Culotta is an IP attorney in private practice serving clients as a one stop shop for new product and service commercialization. Anne's academic achievements include a Ph.D. in chemistry, an M.B.A., a J.D. and LL.M in IP. Her full bio is available at https://www.linkedin.com/in/culottalawfirm. Anne offers deepest thanks to Professor Greg. R. Vetter, Professor of Law, University of Houston Law Center; Co-Director, Institute for Intellectual Property and Information Law. Professor Vetter supervised this writing project, provided instructive feedback and a superb process for academic legal writing. Additionally, thanks go to Assoc. Professor Spencer Simons, Director of O'Quinn Law Library, and Assistant Clinical Professor Lauren Simpson.

I. INTRODUCTION[1]

Under United States bankruptcy law, Title 11 U.S.C. § 363(f) empowers a debtor licensor to sell property "free and clear" of any patent license under certain conditions.[2] This writing considers the sale of any one or more of the following by a licensor in a Chapter 11 or Chapter 7 bankruptcy: (1) a non-exclusively licensed patent, (2) either a non-exclusive patent license or sub-license, and (3) an exclusive patent license. The debtor licensor may sell any one or more of these assets to the same buyer or to different buyers.[3]

The central claim of this writing is that § 363(f) sales are unfair to licensees in three ways implicating issues of timing, notice and consent. The aim of this writing is to provide licensee with guidance useful in defending a valuable license against the possibility of extinguishment in a § 363(f) sale.

Part II of this writing begins with two test cases ("Test Cases") and three questions in order to fully understand the potential unfairness to patent licensees in a § 363(f) sale. The purpose of the Test Cases is to delineate which assets the debtor licensor has to sell to extinguish the licensee's patent license. The three questions structure this article as a guide for the reader.

Part III applies the plain language of § 363(f) to the Test Cases in order to gain a basic understanding of the statute. The first Test Case will be referred to as the "Patent Test Case" and the second Test Case as the "License Test Case." The Patent Test Case involves the debtor licensor's sale of either or both of a non-exclusively licensed patent and a non-exclusive patent license agreement.

The License Test Case replaces the sale of the non-exclusively licensed patent in the Patent Test Case with the sale of an exclusive patent license agreement under which the exclusive licensee has granted a non-exclusive sub-license. Like the Patent Test Case, the debtor may sell either or both of the exclusive patent license agreement and the non-exclusive patent sub-license agreement.

---

[1] This writing employs the following terminology. "Code" means United States bankruptcy law, 11 U.S.C. § 101 (2012), published in the United States Code Volumes 2012 and Supp. II 2015. Unless otherwise indicated, all citations to the Code refer to those volumes and publication years. "Rules" means the Federal Rules of Bankruptcy Procedure. "Rule xxxx" means Federal Rule of Bankruptcy Procedure xxxx. For example, Rule 6004 means FED. R. BANKR. P. 6004. "Trustee" means either debtor in possession in a Chapter 11 bankruptcy, or trustee. In the context of Chapter 11, a debtor in possession can, and frequently does, remain in control of the debtor and has essentially the same powers and duties as a trustee in Chapter 11. This writing uses the terms contract and agreement interchangeably and the terms sale and transfer interchangeably.

[2] 11 U.S.C. § 363(f) (2012).

[3] *See* 11 U.S.C. § 365(n) (2012).

Part IV takes up and answers the first question, which considers what laws govern the facts of the Test Cases when the selling licensor is not bankrupt. For example, absent bankruptcy, what happens to a non-exclusive or exclusive patent license agreement when the licensed patent is sold to a new owner? Also, what happens when a licensor sells a patent license agreement?

Part V takes up the second of the three questions and asks how the law outside bankruptcy is applied inside a bankruptcy § 363(f) sale. As will be demonstrated in Part V, what happens external to bankruptcy does not happen inside bankruptcy. Section 363(f)(1) incorporates the law external to bankruptcy, discussed in Part IV. But bankruptcy courts do not follow that law in sales involving patent licenses and licensed patents.

Part VI takes up the third of the three questions. Using the facts of the Test Cases again, what is a licensee in a § 363(f) sale to do to protect its license from extinguishment? Part VI identifies three particular aspects of unfairness to patent licensees in § 363(f) sales: (1) timing issues, (2) notice issues, and (3) consent issues. The Part further discusses how licensees might address these issues.

Part VI.A addresses timing issues from a procedural point of view in the licensor's bankruptcy. Bankruptcy law only requires the debtor licensor to give twenty-one days advance notice of a license-extinguishing sale, further reducible for cause.[4] In some circumstances, notice by general publication in a newspaper may be adequate.[5] The notice will advise of a hearing date and deadline for the filing of written objections. This leaves licensees little time to seek what protection bankruptcy law purports to offer.

For example, section 365(n) was designed to protect patent license agreements in bankruptcy but such license protections are ephemeral.[6] Such protections are triggered only upon the licensor's rejection of a patent license. However, debtor licensors do not have an obligation to reject a patent license agreement in bankruptcy. In fact, the licensor can sell a licensed patent and do nothing with the license agreement. Absent timely objection by the licensee, the sale will extinguish the license.[7]

In another example, the debtor can delay a decision to assume or reject a license agreement until after the § 363(f) sale, an aspect desirable to bankruptcy buyers.[8] The resulting question is, what should

[4] FED. R. BANKR. P. 2002(a).

[5] *See In re* Smidth & Co., 413 B.R. 161, 165 (Bankr. D. Del. 2009).

[6] *See* 11 U.S.C. § 365(n)(1) (2012).

[7] *See* 11 U.S.C. § 365(f)(1) (2012).

[8] *See* John D. Ayer, Michael Bernstein & Johnathan Friedland, *The Life Cycle of a Chapter 11 Debtor Through the Debtor's Eyes*, AM. BANKR. INST. J. (Sept. 2003),

continued . . .

the threatened licensee do to protect itself when the sale that extinguishes a patent license occurs before the possibility of protection under § 365(n)?

Part VI.A. concludes with suggestions to licensees for dealing with unfair timing problems before and after the sale. After the sale, with the possible exception of adequacy of notice, a licensee's appeal to vacate or modify a § 363(f) sale is not likely to succeed.[9] The balance of this writing provides guidance for addressing the unfairness of notice and consent issues prior to closing of a § 363(f) sale.

Part VI.B. addresses the adequacy of notice due licensees before a license may be extinguished. Challenges to the adequacy of notice in a § 363(f) sale constitute one of the most frequent reasons bankruptcy courts vacate or modify a sale order.[10] Other than such notice challenges, final sale orders can be extremely difficult to change.

Part VI.C addresses consent. In sales other than those involving licensed patents, some bankruptcy courts explicitly require the affirmative consent of interest holders.[11] Others take the opposite view by deeming that the adequately noticed interest holder's lack of objection constitutes consent.[12] In the sale of licensed patents, many bankruptcy courts have followed this deemed consent approach.[13]

Bankruptcy courts following such a deemed consent approach justify the approach on the basis that requiring affirmative consent would slow the pace of sales needed to generate cash for the debtor. Part VI.C takes the position that, in the context of the law external to bankruptcy that would not permit such a sale without the consent of the licensee, it is unfair to follow a contrary rule by deeming consent given inside of bankruptcy. Part VI.C closes with guidance for licensees in addressing the unfairness of deemed consent.

---

http://www.abi.org/abi-journal/the-life-cycle-of-a-chapter-11-debtor-through-the-debtors-eyes-part-i.

[9] *See infra* notes 123–24 and accompanying text.

[10] *See infra* note 139.

[11] *See infra* note 168.

[12] *See infra* notes 169–70 and accompanying text.

[13] *See, e.g.*, FutureSource L.L.C. v. Reuters Ltd., 312 F.3d 281, 286 (7th Cir. 2002) (construing licensee's failure to timely object to properly noticed sale of copyrights in software and data as consent); *In re* Eastman Kodak Co., No. 12-10202 (ALG), 2013 WL 588965 (Bankr. S.D.N.Y. Feb. 13, 2013) (deeming, in sale order paragraph GG, that failure to timely object to the sale, including licensed patents, constitutes consent to the sale under the noticed sale terms); *In re* Nortel Networks, Inc., No. 09–10138 KG, 2011 WL 1661524, at *7 (Bankr. D. Del. May 2, 2011) (deeming, in a bankruptcy sale order, consent given to assumption and assignment of executory license agreements in the absence of timely objection).

II. TWO TEST CASES AND THREE QUESTIONS

A. The Patent Test Case

Your client, Distributor, is a party to a non-exclusive patent license agreement with KnifeCo. Distributor is the licensee. Distributor makes and sells specialty cooking knives covered by KnifeCo's patents.

KnifeCo, licensor to Distributor, fell on hard times and filed for Chapter 11 bankruptcy, hoping to reorganize its business and return to profitability. KnifeCo needs cash to continue operating in bankruptcy. To generate cash, KnifeCo has decided to sell some of its property in a "free and clear" bankruptcy sale, possibly including the patents and license agreement with Distributor.[14] The free and clear sale can extinguish "interests in property," including Distributor's non-exclusive patent license rights.

Competitor and Distributor are archrivals, having tussled more than once in previous litigation. Competitor makes and sells knives different from, but competitive with, Distributor's knives. Competitor is negotiating behind the scenes with KnifeCo hoping to buy some of KnifeCo's property in the sale, which could include the patents, non-exclusive license, or both.[15]

You return to your office and re-read Distributor's patent license agreement with KnifeCo. The patent license is non-exclusive and each party owes the other ongoing performance.[16] There is no mention of either party's authority to assign its rights or delegate its duties under the agreement. A "no oral modifications" clause was included in the

[14] This writing examines a free and clear sale from two perspectives. First, under Test Case One, KnifeCo is a debtor and patent licensor. Second, under Test Case Two, KnifeCo is both a debtor licensee (through the exclusive patent license with the third party) and debtor licensor (through the non-exclusive sub-license agreement with Distributor).

[15] Competitor is playing the role of stalking horse bidder in a free and clear sale. The stalking horse bidder establishes the minimum price of the property to be sold in an asset purchase agreement for the § 363(f) sale. The sale bidding procedures will establish the requirements for higher, better offers. In the absence of any such offers in the sale, and on approval the sale by the bankruptcy court, the stalking horse can proceed to close the sale with the trustee. *See infra* Figure 1.

[16] *See* AM. BANKR. INST., COMMISSION TO STUDY THE REFORM OF CHAPTER 11 (2012–2014), FINAL REPORT AND RECOMMENDATIONS 112 (2015) (recommending codification of the Countryman definition because of, among several reasons, the body of case law developed around the Countryman definition); Vern Countryman, *Executory Contracts in Bankruptcy: Part I*, 57 MINN. L. REV. 439, 460 (1973) (proposing that an executory contract should be defined as a "contract under which the obligation of both the bankrupt and the other party to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing the performance of the other.").

agreement. You also know that neither KnifeCo nor your client has breached the license agreement. Distributor has always timely paid the running royalties due under the license agreement.

Neither you nor your client, Distributor, has received any communications from KnifeCo. You are not certain of what KnifeCo might actually plan to sell. For example, KnifeCo could sell (1) the patent, (2) the non-exclusive license agreement, or (3) both.[17] Each asset could potentially be sold to the same buyer or to different buyers.

B. The License Test Case

In this test case, assume that KnifeCo does not own the patent licensed to your client, Distributor. Instead, a third party owns the patent and KnifeCo has an exclusive license to the patent with the right to sub-license. The exclusive license is something less than what would be construed to be a complete assignment of title to the patent.[18] The exclusive patent license agreement explicitly prohibits assignment of the exclusive license agreement by either of the third party licensor or KnifeCo without the prior written consent of the non-assigning party.

Your client, Distributor, obtained a non-exclusive sub-license to the third party's patent by sub-licensing from KnifeCo. Like the non-exclusive patent license agreement in Patent Test Case, the non-exclusive sub-license agreement between KnifeCo and Distributor is silent as to assignment. Each party owes the other ongoing performance.[19]

Here, KnifeCo can potentially sell (1) the exclusive patent license agreement between the third party and KnifeCo (as licensee), (2) the non-exclusive sub-license agreement between itself and Distributor (KnifeCo as licensor), or (3) both. Each asset could potentially be sold to the same buyer or to different buyers.

[17] The Test Cases are oversimplified in providing that the non-exclusive patent license agreements are silent as to assignment.

[18] Elaine D. Ziff, *The Effect of Corporate Acquisitions on the Target Company's License Rights*, 57 BUS. LAW. 771–75 (2002) (noting that the question of whether an exclusive patent license is tantamount to an outright assignment of the licensed patent turns, in part, on the extent of the rights granted to the exclusive licensee and other terms of the license agreement).

[19] *See* Countryman, *supra* note 16.

C. Three Questions

The questions raised by the Test Cases include:

1. External to bankruptcy, what laws govern the transfer of (a) the Patent Test Case non-exclusively licensed patent, (b) in both Test Cases, the non-exclusive patent license agreements, and (c) the License Test Case exclusive patent license?[20]

2. Considering a bankruptcy free and clear sale under § 363(f), how is the law external to bankruptcy applied in bankruptcy?

3. What actions should Distributor take to protect itself as a non-exclusive patent licensee, and when?

Part IV takes up the first question. Part V takes up the second and Part VI the third. Figure 1 provides an example of a § 363(f) sale timeline. Figure 2 provides a generalized example timeline of bankruptcy to set the § 363(f) timeline in context of the entire case. Figure 3 summarizes all possible asset sales considered by the Test Cases and summarizes the general findings of this writing. What follows next is a brief introduction to § 363(f) using the Test Cases.

III. THE PLAIN LANGUAGE OF § 363(f)

A. Introduction to § 363(f)

This Part III introduces the plain language of 11 U.S.C. § 363(f), which governs free and clear sales in bankruptcy.[21] Part III.B introduces terminology used in the Code and Rules; interests susceptible to extinguishment in the sale, and also a few concepts for understanding free and clear sales. Part III.C applies § 363(f)(1)-(2) to the Test Cases.

Section 363(f) provides as follows:

[20] The License Test Case is intentionally oversimplified. The exclusive patent license agreement expressly prohibits assignment by either of KnifeCo or the third party.

[21] 11 U.S.C. § 363(f) (2012). Other types of bankruptcy sales exist. S*ee* 11 U.S.C. § 1123(b)(4) (2012) (providing for the sale of all or substantially all of the property of the estate as part of a confirmed plan for the debtor's reorganization). *See also* 11 U.S.C. § 363(b) (2012) (providing for sale of property of the estate outside of the ordinary course of the debtor's business subject to liens on the property); 11 U.S.C. § 363(c)(1) (2012) (providing for sale of property of the estate in the ordinary course of the debtor's business without further need to seek the bankruptcy court's approval).

> The trustee may sell property under section (b) or (c) of this section [363] free and clear of any interest in such property of an entity other than the estate, ***only if*** –
>
> (1) applicable non-bankruptcy law permits sale of such property free and clear of such interest;
>
> (2) such entity consents;
>
> (3) such interest is a lien and the price at which such property is to be sold is greater than the aggregate value of all liens on such property;
>
> (4) such interest is in bona fide dispute; or
>
> (5) such entity could be compelled, in a legal or equitable proceeding, to accept a money satisfaction of such interest.[22]

The five conditions stated in §§ 363(f)(1)-(5) are listed in the alternative. Only one of the five conditions need be applicable for a bankruptcy court to approve the sale.[23] This writing addresses the first two of the five conditions.

B. Requirements and Terminology Pertinent to § 363(f)

There exist a few other requirements not specifically mentioned in § 363(f), and a few terms in the Code, used repeatedly, yet undefined. Figure 1 provides an example timeline of a § 363(f) sale. To begin, the sale must not be of the kind conducted in the ordinary course of the debtor's business.[24] The trustee must request, by motion to the bankruptcy court, approval to conduct the sale.[25] In its motion, the

[22] 11 U.S.C. § 363(f) (2012) (emphasis added).

[23] Sections 363(f)(3)–(f)(5) are beyond the scope of this writing. Section 363(f)(3) is pertinent when there is a security interest in the property to be sold. The security interest attaches to the sale proceeds, leaving the previously secured property unencumbered by the security interest. Under § 363(f)(4) the bankruptcy court will allow the sale to proceed when the interest is in bona fide dispute but protect the interest holder so that the issue can be later resolved. Section 363(f)(5) permits the sale in the case that the interest holder could be compelled in a legal or equitable proceeding to accept money in exchange for the interest.

[24] 11 U.S.C. § 363(b)(1) (2012) ("other than in the ordinary course of the debtor's business"). *Compare* FED. R. BANKR. P. 6004(g) (requiring the trustee to seek permission for a sale outside of the ordinary course of the debtor's business), *with* § 363(c)(1) (not requiring the trustee to seek permission when the sale is in the ordinary course of the debtor's business).

[25] Section 363(f) incorporates § 363(b)(1) by stating, "The trustee may sell property under subsection [363](b)[.]" 11 U.S.C. § 363(f) (2012). Section 363(b)(1) states, "The trustee, after notice and a hearing, may . . . sell . . . property of the

continued . . .

trustee must articulate a sound business justification for the sale.[26] The trustee must provide all interested parties with at least twenty-one days notice of the sale, including the deadline for receipt of objections to the sale, and of the sale hearing date.[27]

The Code and Rules leave a number of terms undefined. "Interest" is one such term.[28] "Interest," of the type at risk of extinguishment in a § 363(f) sale, has been construed to include the right to be included in a waiting list to buy full golfing privileges at an exclusive club.[29] An

---

estate[.]" 11 U.S.C. § 363(b)(1).

[26] Section 363(f) incorporates the requirements of § 363(b) requiring a sound business justification. 11 U.S.C. § 363(f) (2012). *See, e.g.*, *In re* Lionel Corp., 722 F.2d 1063 (2d Cir. 1983). Requiring a sound business justification for the sale is one measure of due process protection that accompanies the "notice and hearing" requirements of § 363(b)(1). *Lionel Corp.*, 722 F.2d at 1066. The Second Circuit decided whether the bankruptcy court abused its discretion in authorizing the sale of the debtor's most valuable asset outside of the ordinary course of business. *Id*. at 1066. The Second Circuit required a "sound business justification" and developed a now widely adopted non-exclusive list of factors to determine if such justification exists:

"(1) the proportionate value of the asset to the estate as a whole,

(2) the amount of elapsed time since the filing of the bankruptcy petition,

(3) the likelihood that a plan of reorganization will be proposed and confirmed in the near future,

(4) the effect of the proposed disposition on future plans of reorganization,

(5) the proceeds to be obtained from the disposition vis-a-vis any appraisals of the property,

(6) alternative of use, sale or lease of the property to be sold, and

(7) whether the asset is increasing or decreasing in value." *Id*. at 1071.

[27] *See* FED. R. BANKR. P. 6004(c) stating in pertinent part:

"A motion for authority to sell property free and clear of liens or other interests shall be made. . . and shall be served on the parties who have liens or other interests in the property to be sold. The notice . . . shall include the date of the hearing on the motion and the time within which objections may be filed and served on the debtor in possession or trustee." FED. R. BANKR. P. 6004(c). The following quote from the 1983 enactment of the Federal Rules of Bankruptcy is instructive of the procedures that accompany the trustee's notice of a proposed sale: "The notice of a proposed sale affords creditors an opportunity to object to the sale and raise a dispute for the court's attention. Section 363(b) of the Code permits the trustee or debtor in possession to sell property, other than in the ordinary course of business, only after notice and hearing. If no objection is raised after notice, § 102(1) provides that there need not be an actual hearing. Thus, absent objection, there would be no court involvement with respect to a trustee's sale. Once an objection is raised, only the court may pass on it." FED. R. BANKR. P. 2002(a) advisory committee's notes to the 1983 enactment.

[28] *See* FutureSource L.L.C. v. Reuters Ltd., 312 F.3d 281, 285 (7th Cir. 2002) (recognizing that "interest" is undefined in the Code).

[29] *See, e.g.*, *In re* Magness, 972 F.2d 689, 692 (6th Cir. 1992) (finding the interest to be extinguished in this a § 363(f) sale was not club membership, but rather the "rights of other club members to apply for golf membership as set out in the

continued . . .

easement in real property has also been considered.[30]

In *Precision v. Qualitech* ("*Precision*"), a lease of real property was also found to be an interest which can be extinguished by the sale of the property.[31] 11 U.S.C. § 365(h) (2012) provides lessees the option to retain rights in a lease if rejected by the lessor.[32] The lessee in *Precision* failed to exercise its option to retain rights in the lease.[33] This failure is partly attributable to the bankruptcy court's sale order authorizing a delay of the decision to assume or reject the property lease until after the § 363(f) sale of the property.[34] This exposes a timing issue explored throughout this writing.[35] Code § 365(n) is analogous to § 365(h) and applies to intellectual property ("IP") licenses.[36]

In view of *Precision*, IP commentators predicted that if property

---

rules, procedures and practices of the club").

[30] *See* Gregory G. Hesse & Cameron W. Kinvig, *How Problem Easements Can Limit Sale Rights*, AM. BANKR. INST. JOURNAL 32–33 (May 2014) (discussing cases involving a § 363(f) sale of land burdened by an easement or other covenant running with the land).

[31] *See, e.g.*, Precision Indus. v. Qualitech Steel SBQ, L.L.C., 327 F.3d 537, 540–541 (7th Cir. 2003) (A debtor lessor intended to sell its leased real property in a § 363(f) free and clear sale. The debtor properly noticed the lessee providing sale terms, a hearing date and objection due date. The sale terms provided for the buyer to choose whether to assume or reject the lease after the close of the sale.).

[32] *See Precision*, 327 F.3d at 542. Under § 365(h)(1)(A)(ii), upon rejection of a property lease, the lessee is entitled to elect to retain possession of the lease property "for the balance of the term [of the lease] and for any enforceable extensions of the term." *Id.*

[33] *Id.* at 541.

[34] *Id.* at 541–42. The bankruptcy court's sale order reserved the debtor's right to assume and assign the lease after the sale. *Id.* at 541. Presumably, the lease was not extinguished in the sale based upon the sale order. *Id.* at 542. However, after the sale and the lapse of time provided to the buyer to decide whether to assume or reject the lease, the lease was rejected by operation of law. *Id.* at 541. Upon such rejection, the lessee still had the right to elect to retain rights under the lease under § 365(h)(1)(A)(ii). *Id.* The case never mentions an election by the licensee to retain rights in the lease following rejection by operation of law.

[35] The timing issue in *Precision*, can also arise in the context of IP licenses as taken up in Part V. *Id.* The reader may care to refer to Figure 1 providing a generalized timeline in a § 363(f) sale. To preview the timing issue, in *Precision*, the § 363(f) sale of the property purports to extinguish the lease in the property. *Id.* at 541. The buyer obtained the right to assume or reject the lease after the close of the sale. *Id.* The protections of § 365(h) are only available to the lessee after rejection. *Id.* at 542. In *Precision*, the sale of the leased property purported to extinguish the lease before rejection, in effect circumventing the lessee's option to retain rights under the lease unless otherwise protected by the bankruptcy court's sale order. *Id.*

[36] *See* S. REP. NO. 100-505, at 4 (1988), *as reprinted in* 1988 U.S.C.C.A.N. 3200, 3203 (acknowledging a licensee's lack of alternatives upon license rejection and intending for § 365(n) to provide protection of intellectual property licenses in a "manner that parallels generally the treatment of real estate leases" in § 365(h)).

leases are extinguishable by the sale of real property, an IP license is extinguishable by the sale of the underlying IP rights.[37] The IP community's predictions of license extinguishment were borne out in a case involving a license to data and software copyrights.[38] Patent licenses have also been considered an interest that can be extinguished in a § 363(f) sale.[39] Part IV provides guidance to licensees in pursuing the ephemeral protections provided under § 365(n) addressing timing problems, including that encountered in *Precision*[40] but applied to patent licenses.

It appears that interests in IP at risk of extinguishment in a § 363(f) sale may be quite broad. For example, a bankruptcy court has considered patent-related obligations to or from standards setting organizations as an interest.[41] At least one bankruptcy court excluded from a § 363(f) sale data created by a company under a federal research grant.[42] This exclusion suggests that the bankruptcy court considered the possibility that an interest of the federal government in data or intellectual property rights created through federal research funding may be extinguished in a § 363(f) sale.

Yet another bankruptcy court recently issued an interim sale order purporting to sell patents free and clear of requests for injunctive relief and copyright infringement claims.[43] The requests for injunctive relief

[37] *See, e.g.*, John C. "Kit" Weitnauer & Jay E. Sloman, *The Potential Impact of* Precision Inds. v. Qualitech Steel, SBQ, LLC *on Licensees*, 9 No. 7 Cyberspace Law 3 (2004) (predicting that if § 363(f) could trump the § 365(h) protections to threatened lessees, § 365(n) protections for licensees would suffer a similar fate).

[38] FutureSource, L.L.C. v. Reuters, Ltd., 312 F.3d 281, 283–84 (7th Cir. 2002) (The facts of this case are similar to the Patent Test Case except that the licensed subject matter included copyrights in software, and perhaps databases).

[39] *See In re* Particle Drilling, Nos. 09-33744, 09-33830, 2009 WL 2382030, at *4 (Bankr. S.D. Tex. July 29, 2009) (considering an exclusive patent licensee's objection to a trustee's proposed 363(f) sale of the licensed patents as an interest in property that could be extinguished); Compak Cos, LLC v. Johnson, 415 B.R. 334, 342 (N.D. Ill. 2009) (holding a patent license is an interest in a patent that can be extinguished in a § 363(f) sale).

[40] *Precision*, 327 F.3d at 541.

[41] *See, e.g.*, *In re* Nortel Networks Inc., No. 09-10138, 2011 WL 4831218, at *10 (Bankr. D. Del. July 11, 2011) (excluding patent holder's obligations to standards setting organizations in order authorizing a § 363(f) sale thereby preserving obligee's interest). S*ee also In re* Eastman Kodak Co., No. 12-10202 (ALG), 2012 WL 2255719, at *10 (June 15, 2012) (ensuring that any interest or obligation to a standards setting organization would not be extinguished in a free and clear sale).

[42] *See, e.g.*, Documents 81, 1, 4, *In re* Atmospheric Glow Techs, Inc., No. 08-31320 (Bankr. N.D. Tenn. 2008) (the documents from the *Atmospheric Glow* bankruptcy litigation will be identified by their assigned document number rather than their description).

[43] *In re* Aereo, Inc., No. 14-13200-shl, 2015 WL 1419104, at *5 (Bankr.

continued . . .

and copyright infringement claims arose out of the debtor's operating within the scope of its own patent claims found to infringe copyrights of television broadcast networks.[44]

Like the term "interest" discussed above, "party in interest" is also undefined in the Code and the Rules.[45] "Party in interest" is generally understood to include all persons whose pecuniary interests are directly affected by the bankruptcy proceedings.[46]

Unlike the terms "interest" and "party in interest," "creditor" is defined in the Code. A creditor is always a party in interest; however, a party in interest is not always a creditor. A creditor is defined in the Code, in pertinent part, as an "entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor."[47] Therefore, in the Test Cases, Distributor cannot be a creditor of KnifeCo (assuming no other obligations exist). Prior to filing for bankruptcy, KnifeCo had not breached any patent license agreement. Therefore, Distributor has no possible claim against KnifeCo.[48] Below, this writing will use the term "party in interest" to refer to both creditors

S.D.N.Y. Mar. 12, 2015).

[44] *See* Am. Broad. Cos. v. Aereo, Inc., 134 S. Ct. 2498, 2511 (2014) (holding Aereo publicly performed plaintiff's copyrighted works and remanding for further proceedings).

[45] *See, e.g.*, *In re* ANC Rental Corp., 278 B.R. 714, 718–19 (Bankr. D. Del. 2002) (granting standing as parties in interest to non-debtor parties to an un-breached executory agreement that were not creditors of the debtor); *In re* Manshul Const. Corp., 223 B.R. 428, 429 (Bankr. S.D.N.Y. 1998) (acknowledging that neither the Code nor Rules define "party in interest" but incorrectly limiting the term to "creditors with a claim"); *In re* Pub. Serv. Co. of N.H., 88 B.R. 546, 551 (Bankr. D.N.H. 1988) (finding no definition of "party in interest" in either the Code or Rules despite the term's appearance forty-six times therein).

[46] *See* FutureSource, L.L.C. v. Reuters, Ltd., 312 F.3d 281, 283–84 (7th Cir. 2002) (characterizing the licensee as a "party in interest in the context of a § 363(f) sale and neither party breached the license agreement pre-bankruptcy); *In re* Alpex Computer Corp., 71 F.3d 353, 356 (10th Cir. 1995) (observing that the term party in interest "is generally understood to include all persons whose pecuniary interests are, directly affected by the bankruptcy proceedings").

[47] The term "creditor" means . . . "entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor." 11 U.S.C. § 101(10)(A) (2012). Portions B and C of the definition of "creditor" are not pertinent to this writing and are omitted.

[48] The term "claim" means:

(A) right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or (B) right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured. 11 U.S.C. § 101(5) (2012).

and party in interest.

Although each of the terms "consent" and "objection" appear in the Code and the Rules, neither term is defined. As will be demonstrated in Part VI.C, each term contributes to the unfairness to patent licensees in § 363(f) sales.

Finally, an important concept to keep in mind for the discussion that follows is the distinction between a license and a license agreement.[49] A license is a permission to do something that would otherwise be prohibited.[50] A license agreement embodies the conditions and covenants under which the license is granted.[51]

C. Section 363(f)(1)-(2) Applied to the Test Cases: Distinguishing Which Sales Extinguish a License

This writing addresses only the first two of the five conditions for the sale in § 363(f). In the Test Cases, consider how § 363(f)(1) "applicable non-bankruptcy law" or § 363(f)(2) "consent" of the interest holder would apply to each possible asset sale.

In theory, in the Patent Test Case, KnifeCo can sell any, or both of: (1) the non-exclusively licensed patent and (2) the non-exclusive patent license with Distributor. In theory, in the License Test Case, KnifeCo, can sell any, or both of: (1) the exclusive patent license with the third party, and (2) the non-exclusive patent sub-license with Distributor (Figure 3). The Test Cases demonstrate the dual nature of executory agreements in bankruptcy as potentially an interest burdening property on the one hand and yet on the other hand, property that the debtor can sell.

KnifeCo cannot extinguish its own interest as a party to a license agreement by selling any license agreement as property.[52] It is

---

[49] *See* Christopher M. Newman, *A License is Not a "Contract Not to Sue": Disentangling Property and Contract in the Law of Copyright Licenses*, 98 IOWA L. REV. 1101, 1153 (2013) (distinguishing license as a property interest from the attendant conditions and covenants between the parties in an agreement conveying license privileges).

[50] *See* DAVID M. EPSTEIN, *Introduction to Licensing Issues*, 1 ECKSTROM'S LICENSING IN FOREIGN AND DOMESTIC OPERATIONS § 1.1 (database updated November 2015) (stating that the historical definition of a license is a "right or rights by some competent authority to do an act which, without such license, would be illegal").

[51] ERIC E. BENSEN, *Preface: License Versus License Agreement*, 1-1 INTELLECTUAL PROPERTY IN BANKRUPTCY: A COLLIER MONOGRAPH § 4:1 (database updated 2012) ("[A] license is a right to do something while a license agreement is a contract that conveys a license, typically, along with other rights and obligations").

[52] *See* 11 U.S.C. § 363(f) (2012). "Free and clear" only applies to interests "other than the estate."

important to think through what law, external to bankruptcy, governs the transfers contemplated above. Section 363(f)(1) incorporates the law external to bankruptcy as "applicable non-bankruptcy law."[53] Absent a finding that applicable non-bankruptcy law permits a sale, § 363(f)(2) requires consent of the interest holder. Part VI.C takes up aspects of consent. Next, in Part IV, this writing takes up "applicable non-bankruptcy law" under § 363(f)(1).

IV. SALES EXTERNAL TO BANKRUPTCY

External to bankruptcy, two general rules govern the transfer of patent licenses and licensed patents, respectively. This Part IV will demonstrate that, under these two rules, non-exclusive patent license rights persist despite transfers of licensed patents. The licensee is not required to take any affirmative action for its non-exclusive license to persist. The non-exclusive licensee may need to litigate to enforce its rights in a license in the case of a transfer of ownership in the licensed patent. However, the point remains that, external to bankruptcy, the non-exclusive licensee will show up to the litigation with its license rights still in existence. Part V will demonstrate that this is not necessarily so inside a bankruptcy § 363(f) sale. If the license does nothing, the transfer will extinguish the license with finality.

A. General Rules Characterized as Applicable Non-Bankruptcy Law Under § 363(f)(1)

Consider the Test Cases (but external to bankruptcy) with the following two rules in mind. The first rule deals with the assignment of a non-exclusive patent license agreement, and the second with the transfer of a non-exclusively licensed patent. Part IV.B will address separately the assignment of an exclusive patent license agreement.

The first rule provides that a non-exclusive patent license agreement is not assignable absent an express intention to the contrary by the non-assigning party.[54] This general rule of non-assignability is the opposite of state contract law favoring free assignability of both property and contracts.[55]

---

[53] *Id.*

[54] *See* ROBERT A. MATTHEWS, JR., 5 ANNOTATED PATENT DIGEST § 35:36 (2016) (summarizing cases that follow the general rule of non-assignment of patent and copyright licenses). *See also* Unarco Indus. v. Kelley Co., 465 F.2d 1303, 1305–06 (7th Cir. 1972) (applying federal, not state, law under an exception in Erie R. Co. v. Tompkins, 304 U.S. 64, 78 (1938) and holding a non-exclusive patent license is not assignable).

[55] Superbrace, Inc. v. Tidwell, 124 Cal. App. 4th 388, 396 (2004) (citing Farmland Irrigation Co. v. Dopplmaier, 48 Cal.2d 208, 222 (1957) for the

continued . . .

Generally, patent license agreements use one of three approaches to assignment: (1) silence, (2) express prohibition of assignment, or (3) conditional language authorizing assignment.[56] Under the last approach, a bankruptcy court may be required to interpret the conditional language and determine whether the conditions authorizing assignment materialized. This writing intentionally oversimplifies the Test Cases in order to avoid the complexities that arise with conditional assignment language.

The second rule provides that, "the transferee of the patent takes title 'subject to' the license."[57] Generally, this rule also applies to exclusively licensed patents.[58]

The reader may ask why the first rule prohibits assignment of a non-exclusive patent license agreement absent consent of the non-assigning party, but the second rule requires that the transferee of the licensed patent be bound by the non-exclusive license whether or not the transferee is aware of the license. The license, not the license agreement, diminishes the patent by the right to sue one entity, the licensee.[59] In selling such a non-exclusively licensed patent, the owner cannot transfer to the buyer what he does not own.[60] The patent owner

proposition that state statutes favor a policy of free transferability of property, including contracts but not when the duties in a contract are personal to the parties as with non-exclusive patent licenses).

[56] Bd. Of Regents of the Univ. of Neb. v. BASF Corp., No. 4:04CV3356, 2007 WL 3342406, at *12 (D. Neb. Nov. 6, 2007) ("[T]he law treats a patent license as if it contained restrictions of non-assignabiity and non-transferability in the absence of express provisions to the contrary.").

[57] *See* Keystone Type Foundry v. Fastpress Co., 272 F. 242, 245 (2nd Cir. 1921) (citations omitted) ("[I]t had long passed into the textbooks that such an assignee acquired title [to the patent] subject to prior licenses of which the assignee must inform himself as best he can, and at his own risk."); Innovus Prime, L.L.C. v. Panasonic Corp., No. C-12-00660-RMW, 2013 WL 3354390, at *5 (N.D. Cal. July 2, 2013) ("It is a longstanding principle that an assignee of a patent takes the patent subject to prior licenses"); Jones v. Berger, 58 F. 1006, 1007 (D. Md. 1863) (holding oral patent license granted prior to transfer of the patent to plaintiff constitutes valid defense to infringement).

[58] *See* Armstrong Pump, Inc. v. Hartman, 745 F. Supp. 2d 227, 233–34 (W.D.N.Y. 2010) (finding buyer of exclusively licensed patent would take the patent subject to the license). *See also* MATTHEWS, JR., *supra* note 54, § 35:4 (summarizing cases wherein the assignee of a licensed patent takes the patent subject to the license, including an exclusive patent license).

[59] *See* V-Formation, Inc. v. Benetton Group SPA, No.02-CV-02259 PSF CBS, 2006 WL 650374, at *5 (D. Colo. Mar. 10, 2006) (holding the transferee of a patent licensed pre-transfer does not own the right to sue the licensee because the transferor parted with that right and could not convey to the transferee what it did not own).

[60] *See Innovus Prime*, 2013 WL 3354390, at *7. The Court in the Northern District of California first equated a covenant not to sue with a patent license. *Id.* at *8. The court then held that the non-exclusive patent license was effective against

continued . . .

does not own the right to sue the licensee.[61]

B. Transfers of Patent Licenses

Consider each of the Test Cases, but external to bankruptcy. Each of the non-exclusive license agreements in the Test Cases is silent as to assignment. Under the general rule of non-assignment of patent license agreements, would an assignment from KnifeCo to Competitor be permissible? No. Silence under such circumstances is generally not construed as consent. Therefore, in each Test Case external to bankruptcy, the general rule of non-assignment of non-exclusive patent license agreements prevents the assignment by KnifeCo unless Distributor consents.

The License Test Case also includes the possibility that KnifeCo could sell the exclusive patent license agreement with the third party. The law governing assignment of exclusive patent license agreements is unsettled[62] relative to the rules pertaining to non-exclusive patent license agreements discussed above.[63] The unsettled nature of the law as to exclusive patent license agreements is explained, in part, by the confusion in determining when an exclusive patent license is tantamount to an assignment of the patent and when the exclusive patent license is something less than a complete assignment of a patent.[64] The License Test Case is oversimplified in the following ways. The exclusive patent license agreement is less than a complete assignment of the patent. In addition, the exclusive license agreement expressly prohibits assignment by either party without advance written consent of

---

the plaintiff patent holder in a patent infringement suit despite four intervening transfers of the patent. *Id.* at *7. The court simply noted that licensing a patent merely diminishes the patent by the right to sue one entity. *Id.* at *5.

[61] *V-Formation*, 2006 WL 650374, at *5.

[62] *See* Peter M. Gilhuly, et al., *Intellectually Bankrupt?: The Comprehensive Guide to Navigating IP Issues in Chapter 11*, 21 AM. BANKR. INST. L. REV. 1, 27–29 (2013) (acknowledging that the assignability of exclusive patent licenses is unsettled and providing an overview of pertinent cases).

[63] Ziff, *supra* note 18, at 771 ("Non-exclusive patent licenses which are silent (or deemed, by virtue of the Bankruptcy Code, to be silent) as to prohibitions on assignment have virtually unanimously been found not assignable.").

[64] *See id*. *See generally* Superbrace, Inc. v. Tidwell, 124 Cal. App. 4th 388 (2004). *Superbrace* provides a useful history of the general rule of non-assignment of patent licenses. *Id.* at 393–401. The court, construed an agreement for the sale of a patent under a payment installment plan as an exclusive patent license and not an outright assignment. *Id.* at 403. The buyer failed to make all installment payments and arranged to sell the agreement for sale to a third party over the objections of the licensor *Id.* The court construed the agreement for sale to permit assignment of the agreement to the third party, but prohibited further sales. *Id.* at 405.

the non-assigning party.

C. Transfers of Licensed Patents

Consider the Patent Test Case external to bankruptcy involving the sale of the non-exclusively licensed patent to Competitor. Such sale implicates the rule that the transferee of a licensed patent takes subject to the license. KnifeCo can transfer the non-exclusively licensed patent to Competitor.[65] Distributor's license will persist because Competitor takes the patent diminished by KnifeCo's license with Distributor.[66] Finally, in the Patent Test Case but external to bankruptcy, consider the possibility that KnifeCo could sell both the non-exclusively licensed patent and the non-exclusive patent license agreement with Distributor. The result should be no different than as discussed above.[67]

This Part IV answers the first of the three test questions posed in Part II.C, which asked, external to bankruptcy, what laws govern the transfers posed in the Test Cases? To recap, this Part IV provided a synopsis of two general rules external to bankruptcy regarding the transfer of licensed patents and patent license agreements. Part IV.C demonstrated that external to bankruptcy, a non-exclusive patent licensee does not need to take any affirmative action to ensure that its rights exist through a transfer of the licensed patent. Inside bankruptcy, § 363(f)(1) refers to "applicable non-bankruptcy law."[68] The discussion in this Part is the "applicable non-bankruptcy law" of § 363(f)(1). Below, this writing takes up the next of the three questions and turns to patent licenses inside bankruptcy in a § 363(f) sale.

V. PATENT LICENSE AGREEMENTS INSIDE BANKRUPTCY IN VIEW OF A § 363(F) FREE AND CLEAR SALE

An understanding of this Part provides context necessary for exploring the actions Distributor can take to protect its license, taken up in Part VI. This Part V returns to the second of the three questions in

[65] KnifeCo could still potentially be liable, for example, for a breach of contract or breach of warranty claim by Distributor. It is arguable that neither type of claim, without more, will prohibit or void the transfer of the patent from KnifeCo to Competitor. Distributor will be left to argue breach of contract or breach of warranty damages.

[66] Innovus Prime, L.L.C. v. Panasonic Corp., No. C-12-00660-RMW, 2013 WL 3354390, at *5 (N.D. Cal. July 2, 2013).

[67] *See, e.g.*, PPG Indus. v. Guardian Indus., 597 F.2d 1090 (1979) (holding non-exclusive patent license agreements not transferred by operation of law under state merger statute even when licensed patents also transferred).

[68] 11 U.S.C. § 363(f)(1) (2012).

Part II.C. Considering a bankruptcy free and clear sale under § 363(f), how is the law external to bankruptcy applied in bankruptcy?

Each of the Test Cases involves at least one executory patent license agreement whether exclusive or non-exclusive. The trustee for KnifeCo has four options at its disposal with respect to executory patent licenses.[69] The trustee may (1) assume,[70] (2) assume and assign,[71] (3) reject,[72] or (4) do nothing.[73] Assumption alone is not pertinent to this writing.

As will be demonstrated in this Part, the trustee can use a § 363(f) sale of a licensed patent to circumvent § 365(n) licensee protections and an ongoing burden to the patent. To sell a patent license agreement, the trustee must first obtain bankruptcy court approval to assume and assign the license agreement (option two).[74]

Consider the Patent Test Case. What if the trustee sells the patent and does nothing with the non-exclusive patent license agreement? Doing nothing (trustee's option four) is not rejection (option three). Rejection triggers § 365(n) and the possibility of protecting Distributor's license.[75] Absent objection by the licensee, the license will be extinguished.[76]

The License Test Case forces the issue of assumption and assignment. The trustee only has an exclusive patent license agreement

---

[69] Generally, courts find many patent license agreements to be executory, hence this writing does not explore what constitutes an executory agreement. *See generally,* THOMAS M. WARD, INTELLECTUAL PROPERTY IN COMMERCE § 4:76, *available at* Westlaw (database updated Nov. 2015).

[70] Assumption, the first option, is not pertinent to this writing. In the Test Cases, the trustee needs the second option which is to assume and then assign any license agreement the trustee intends to sell.

[71] *See, e.g.*, *In re* Lockwood, No. 05-31424-DM, 2008 WL 943025, at *4 (Bankr. N.D. Cal. Apr. 7, 2008) (approving the debtor licensor's assumption of a patent license agreement and assignment to the licensee).

[72] *See, e.g.*, *In re* Ice Mgmt. Sys., Inc., No. CC-14-1046-KiKuDa, 2014 WL 6892739, at *2 (B.A.P. 9th Cir. Dec. 8, 2014). A patent license agreement was rejected by operation of law when the debtor neither assumed nor rejected the license within the period required under Chapter 7 of the Code. *Id.* The following day, the rejected licensee elected to retain its rights as provided under 11 U.S.C. § 365(n). *Id.*

[73] *See In re* JZ L.L.C., 371 B.R. 412, 426 (B.A.P. 9th Cir. 2007) (holding that the parties did nothing with respect to an executory license agreement, therefore the agreement "rode through" bankruptcy).

[74] 11 U.S.C. § 365(a) (2012); FED. R. BANKR. P. 6004(c), (d).

[75] *In re Ice Mgmt.*, 2014 WL 6892739, at *2.

[76] Jeffrey S. Berkowitz & Brett S. Theisen, *Intellectual Property Licensees Should Pay Close Attention to Kodak's Planned Auction Sale*, 8 PRATT'S J. BANKR. L. 230, 234 (Apr. 2012) (warning licensees of Kodak patents of the consequences of a § 363(f) sale and advising licensees of the option to elect to retain licensed rights under § 365(n) upon licensor rejection).

to sell. Selling the exclusive license agreement purports to extinguish Distributor's non-exclusive patent sub-license. This Part introduces bankruptcy law actual and hypothetical assignment tests applied to license agreements in bankruptcy.

Trustee delay is a truncated form of doing nothing under option four. Buyers in § 363(f) sales manage risk by asking the trustee to delay the decision to assume or reject an executory license agreement until after the sale.[77] Bankruptcy courts generally approve such requests in order to attract buyers. This is the timing dilemma of *Precision* in the context of patent licenses.[78] Unless Distributor provides a timely written objection before the sale, Distributor is likely to fall into the timing trap of *Precision*.[79] Below, this Part explores the latter three of the trustee's four options. In the context of a § 363(f) sale, this Part examines how the trustee's exercise of its options impacts the licensee. Part VI addresses how Distributor, as the licensee, can counter the trustee's exercise of its options.

A. Assumption and Assignment of Non-Exclusive Patent License Agreements

In the Test Cases, the trustee for KnifeCo must have the power to assume and assign any license agreement included in the sale.[80] Generally, courts analyze whether the trustee has such power under one of two tests: (1) the actual assignment test ("actual test"), and (2) the hypothetical assignment test ("hypothetical test").[81] Others' writings provide a more in-depth discussion of these assignment tests, considered one of the most complex areas of bankruptcy law.[82]

To simplify each test, consider in order the following two prongs of inquiry: (1) whether the trustee has the power to assume an executory

---

[77] *See, e.g.*, *In re* Nortel Networks, Inc., No. 09-10138 (KG), 2011 WL 4831218, at *6 (Bankr. D. Del. July 11, 2011) (finding buyer would not have entered into § 363(f) sale agreement without the right to assume or reject executory patent license agreements after the sale).

[78] Precision Indus. v. Qualitech Steel SBQ, L.L.C., 327 F.3d 537, 541 (7th Cir. 2003).

[79] *Id*. at 548.

[80] *See* FED. R. BANKR. P. 6004 advisory committee's note (requiring the bankruptcy court's permission for the sale of the property).

[81] AM. BANKR. INST., *supra* note 16, at 123.

[82] *See generally* N.C.P. Mktng. Grp. v. BG Star Prods., 556 U.S. 1145 (2009) (denying certiorari and signaling a desire to resolve whether the actual test or the hypothetical test should govern questions of assumption if presented with an appropriate fact pattern); WARD, *supra* note 69, § 4:87, § 4:89–90, § 4:92; Alex Tucker, *Bankruptcy's (Mis)Treatment of Intellectual Property: Why 365(N) Is Not Enough – Part I*, 24 No. 11 INTELL. PROP. & TECH. L.J. 17, 18–21 (2012).

license agreement, and (2) if yes to the first question, whether the trustee has the power to assign the executory license agreement to the buyer.

Under the actual test, the trustee has the power to assume a non-exclusive patent license agreement even without the licensee's consent.[83] This is so because bankruptcy law treats the pre-bankruptcy debtor and trustee in bankruptcy as identical even though the two are technically separate entities.[84] Turning to the second prong of the inquiry under the actual test, the trustee has the power to assign only if an actual assignee exists and the assignment would be permitted by applicable non-bankruptcy law (as previously discussed in Part IV.B).[85]

Turn now to the hypothetical test. The hypothetical test treats the pre-bankruptcy debtor and the trustee as separate entities (the opposite of the actual test). Considering the first prong of the inquiry under the hypothetical test, the trustee has the power to assume an executory agreement only if the agreement would permit assignment to the trustee. Under the second prong of the inquiry under the hypothetical test, the trustee has the power to assign an executory patent license agreement only if the agreement permits the assignment to a hypothetical third party whether or not such party actually exists (as previously discussed in Part IV.B).[86]

The License Test Case forces the issue of assignability of patent license agreements. Part VI.C.2 will analyze whether the trustee for KnifeCo has the power to assume and assign the license agreements to Competitor. Doing so allows full development of Distributor's possible arguments in objecting to the sale by demonstrating lack of consent. The analysis requires integration of the rules of non-assignment of patent license agreements (Part IV.B, discussing § 363(f)(1) "applicable non-bankruptcy law"). For now, realize that in the oversimplified Test Cases, each prong of the analysis is going to cause the trustee a problem. As will be demonstrated in Part VI.C.2, which prong of the analysis causes a problem depends upon which test is used.

B. Rejection of Non-Exclusive Patent License Agreements

This Part V.B addresses the third of the trustee's four options. The third option is for the trustee to reject an executory agreement.[87] In the

[83] AM. BANKR. INST., *supra* note 16, at 123. *See also* WARD, *supra* note 69, § 4:88 (asserting assumption not generally an issue under the actual test when the pre-bankruptcy debtor and debtor are identical but open to challenge when not identical).

[84] City of Jamestown v. James Cable Partners, L.P., 27 F.3d 534, 537 (11th Cir. 1994).

[85] AM. BANKR. INST., *supra* note 16, at 123.

[86] Perlman v. Catapult Entertainment, 165 F.3d 747, 754–55 (9th Cir. 1999).

[87] AM. BANKR. INST., *supra* note 16, at 114.

Test Cases, imagine that the trustee for KnifeCo believes that KnifeCo stands to lose more than it will gain in assuming the non-exclusive patent license agreement with Distributor. In that case, the trustee can reject the non-exclusive patent license agreement.

When the trustee rejects a non-exclusive patent license agreement, two options become available to the licensee. Consider these options from Distributor's position in the Test Cases. Distributor may elect: (1) to retain rights under any of the rejected licenses in the Test Cases[88] or (2) elect to treat the trustee's rejection as a breach of the license agreement and file a claim for breach of contract damages in the bankruptcy proceeding.[89] Distributor cannot exercise its two options until the trustee rejects the non-exclusive patent license agreement.

Code § 365(n) is complex and has been covered extensively by others.[90] Generally speaking, a post-rejection election to retain rights under § 365(n) provides Distributor with fewer rights under the pre-rejection license.[91] Nevertheless, an election under § 365(n) may be better than no license rights. For example, imagine that Distributor invested millions of dollars in specialized knife making equipment, the operation of which would be infringing absent its patent license agreement with KnifeCo. Imagine how Distributor would be harmed if Distributor were to have no rights under its license.

---

[88] From the licensee's perspective, electing to retain rights under the license as provided in § 365(n)(1)(B) is less preferred relative to having the original license agreement. *See* AM. BANKR. INST., *supra* note 16, at 124. For example, the licensee cannot compel the debtor's performance of affirmative obligations. *Id.* Rather, the licensee only retains rights to the extent that the right existed as of the bankruptcy petition date, and for any applicable term of extension. *Id.* Of course, the licensee is required to continue payment of all royalties and other fees under the retained license agreement. *Id.*

[89] *See* WARD, *supra* note 69, *§ 4:97*. The licensee may treat the licensor's rejection as a pre-bankruptcy breach of the license agreement. *Id.* Accordingly, the rejected licensee may file a claim against the bankruptcy estate for breach of contract damages under § 502(g)(1). *Id.* However, the licensee is likely to receive only pennies on the dollar for such claim (assuming the licensee's claim is unsecured).

It is important to note that rejection by the debtor licensor and the licensee's breach of contract claim does not, without more, terminate the license agreement. *Id.* However, if an independent ground for termination can be found to exist (for example, material breach by the debtor licensor which would excuse continued performance under applicable state law), then the licensee may have an independent ground for terminating the license agreement if it so chooses. *Id.*

[90] *See, e.g.*, Debra A. Dandeneau, *The Interplay Between Intellectual Property Rights and Bankruptcy*, *in* IP ISSUES IN BUSINESS TRANSACTIONS 2015 INTELLECTUAL PROPERTY COURSE HANDBOOK SERIES NUMBER G-1212, 436–41 (Steven I. Weisburd, Eric A. Prager, et. al, eds., Practicing Law Institute 2013) (discussing the intricacies of § 365(n) in detail).

[91] *See id.* at 430–36.

C. Trustee Delay and Ride Through Doctrine

The trustee's fourth option as to executory agreements is to do nothing.[92] Delay is a truncated form of doing nothing. When both parties do nothing with respect to an executory agreement for the entire bankruptcy, a court may determine the agreement simply "rides through" the bankruptcy.[93]

In Chapter 11 bankruptcies, the trustee may delay deciding whether to assume and assign or reject a license agreement as late as the reorganization plan confirmation (Figure 2).[94] Plan confirmation occurs at the end of the bankruptcy proceeding; whereas a §363(f) sale typically occurs earlier in the bankruptcy process.[95] The policy reason underlying this generous time allocation is to maximize the debtor's opportunities to reorganize successfully.[96]

The trustee may delay rather than do nothing. Doing so exploits the timing issue in *Precision v. Qualitech* by delaying assumption and assignment or rejection until after the sale.[97] This option is attractive to buyers such as Competitor for the purposes of risk management. In either Test Case, Distributor's licenses are in peril under the trustee's do nothing option. Part VI addresses the actions Distributor may take in dealing with this possibility.

To summarize, this Part V introduced the trustee's four options in

---

[92] *In re* JZ, L.L.C., 357 B.R. 816, 821 (Bankr. D. Idaho), *aff'd*, 371 B.R. 412 (B.A.P. 9th Cir. 2007).

[93] *See id.* at 820–21 (Ride through may be appealing if neither party has breached the agreement and no more than the status quo is required at the conclusion of a bankruptcy. Sometimes ride through just arises out of sub-optimal license agreement management. For example, either party to a license agreement can lose track of the agreement. Additionally, a licensee may not be aware of a licensor's bankruptcy.).

[94] *See* 11 U.S.C. § 365(d)(2) (2013) (providing, in Chapter 11, for the trustee's assumption or rejection of an executory agreement any time before plan confirmation and also providing the other party to the agreement an opportunity to ask the bankruptcy court to order the trustee to specify a time when the determination will be made). *See also* 11 U.S.C. § 365(d)(1) (2013) (rejecting by operation of law, executory agreements of the debtor in Chapter 7 if such agreements are not assumed or rejected "within 60 days after the order for relief, or within such additional time as the court, for cause, within such 60-day period, fixes").

[95] *See infra* Figure 2 (providing an example of a bankruptcy timeline and demonstrating that a § 363(f) sale can occur earlier than plan confirmation and discharge).

[96] *See, e.g.*, *In re* Kmart Corp., 290 B.R. 614, 619–20 (Bankr. N.D. Ill. 2003) (justifying the debtor's delay and the court's refusal to compel an earlier decision on the goal of successful debtor reorganization).

[97] *See* Precision Indus. v. Qualitech Steel SBQ, L.L.C., 327 F.3d 537, 542 (7th Cir. 2003).

dealing with executory patent license agreements in bankruptcy. With respect to the sale of a patent license, the trustee needs to assume and assign the license agreement to a buyer (option two of four). This issue necessarily arises in the License Test Case. Distributor can challenge the trustee's power by applying the hypothetical or actual assignment tests as applicable in the jurisdiction of the debtor's bankruptcy.

However, as is the trustee's right, the trustee may do nothing (option four). The trustee can sell the patent and extinguish Distributor's patent license, circumventing § 365(n).[98] As was the case in *Precision,* buyers such as Competitor may obtain the right to choose which license agreements to assume or reject after the sale.[99] Absent action by Distributor, the sale will extinguish Distributor's license. Part VI takes up Distributor's options in view of the issues raised in this Part and returns to the last of the three questions.

VI. DEALING WITH UNFAIRNESS IN SECTION 363(f) SALES

This Part takes up the last of the three questions posed in Part II.C. What actions should Distributor take to protect itself as a non-exclusive patent licensee, and when? Continuing with the theme of trustee delay first introduced above in Part V.C, assume in the Test Cases that Competitor obtains the right to assume and assign or reject any license agreement up to thirty days after the closing in KnifeCo's § 363(f) sale.[100] This is similar to the timing issue in *Precision.*[101]

The same issue involving cross-licensed patents arose in *Kodak*.[102] In *Kodak*, the debtor in a Chapter 11 case sought the approval of the bankruptcy court in the Southern District of New York to sell licensed and cross-licensed patents as part of Kodak's digital imaging business.[103] Numerous licensees of the Kodak patents objected to the

[98] *See id.* at 548. *See also* James E. Raymond, *Software Licenses, Source Code Escrows, and Trustee Powers Under 11 U.S.C. S 365*, 1 J. BUS. ENTREPRENEURSHIP & L. 43, 62–65 (2007).

[99] *Precision*, 327 F.3d at 541–42.

[100] *In re* Nortel Networks, Inc., No. 09-10138 (KG), 2011 WL 4831218, at *7 (Bankr. D. Del. July 11, 2011). *See infra* number 7 in Figure 1.

[101] This timing problem is analogous to that in *Precision*, 327 F.3d at 541–42, first introduced in Part III.B and further discussed in Part V.C. The buyer is allowed to choose which executory agreements may be assumed and assigned or rejected after the interest-extinguishing sale effectively circumventing protections available under the Code (e.g., § 365(h) for property leases). *Precision*, 327 F.3d at 548.

[102] *In re* Eastman Kodak Co., 479 B.R. 280, 305 (Bankr. S.D.N.Y. 2012).

[103] *In re* Eastman Kodak Co., No. 12-102-02 (ALG), 2013 WL 588965, at *5 (Bankr. S.D.N.Y. Feb. 13, 2013).

proposed sale of the licensed patents to Intellectual Ventures.[104] The licensees expressed concern that Intellectual Ventures had the right to reject license agreements following the sale, which could extinguish a licensee's rights prior to an opportunity to elect to retain rights under § 365(n), which is triggered by rejection.[105]

What is Distributor supposed to do to protect its non-exclusive license if the sale of the licensed patent extinguishes its license without a rejection of the license agreement by the trustee? The balance of this writing addresses Distributor's options, arranged in order of timing, notice and consent.

Part VI.A addresses timing issues before and after the sale. Before the sale, the licensee has two non-mutually exclusive options. After the sale, other than adequacy of notice, Distributor's likelihood of success on appeal is low. Part VI.B addresses the notice due licensees in a § 363(f) sale, more frequently a basis for vacating or modifying a sale order. [106]

Part VI.C addresses consent of the licensee under § 363(f)(2). That Part will demonstrate that it is unfair for a bankruptcy court to deem a properly noticed licensee's silence as consent to the sale if applicable non-bankruptcy law would not do so. In the Test Cases, the wise course is for Distributor to timely raise all possible challenges to a proposed § 363(f) sale in writing by the due date for receiving objections (Number 3 in Figure 1). Part VI.C guides the reader through the arguments Distributor can present in objection, and in so doing will bring closure to the timing problem first identified in *Precision*.[107]

A. Timing

Figure 1 provides a sample timeline in a § 363(f) sale. The trustee for KnifeCo is only required to give Distributor twenty-one days' notice of the § 363(f) sale.[108] A bankruptcy court may reduce this short period even further for cause.[109] The notice of sale will provide a due date for

---

[104] *Id*. at *9.

[105] *Id.*

[106] Compak Cos. v. Johnson, 415 B.R. 334, 341 (N.D. Ill. 2009) ("By far the most frequent mistake or infirmity held to warrant vacating a confirmed sale is defective notice to interested parties of the judicial sale.").

[107] Precision Indus. v. Qualitech Steel SBQ, L.L.C., 327 F.3d 537, 541–42 (7th Cir. 2003).

[108] FED. R. BANKR. P. 2002(a).

[109] *Id*. at 2002(a)(2). E.*g.*, *In re* Borders Grp., Inc., 453 B.R. 477, 485 (Bankr. S.D.N.Y. 2011) (reducing sale notice period from twenty-one to five days because a streamlined sale would benefit the bankruptcy estate and still provide adequate time for objection).

receipt of objections and also a sale hearing date.[110] At the latest, a hearing date will be the day of entry of the final sale order, generally one to three days after the conduct of the sale. These items are summarized in Figure 1 providing an exemplary timeline in a § 363(f) sale. This appears unfair, constituting precious little time for Distributor to address the possible extinguishment of a license.

As discussed in Part V.C, in the Test Cases, the trustee can do nothing with respect to the executory license agreements. Distributor need not allow this. In either Test Case, doing so puts the non-exclusive patent license in peril. Below, this Part takes up two options Distributor can take before the sale. After the sale closes, other than adequacy of notice, Distributor's avenues for appeal are limited. This Part considers appeals and Part V1.B addresses adequacy of notice.

1. How Licensees Can Address Trustee Delay Before the Sale

This Part is limited to two non-mutually exclusive approaches available to the licensee in addressing timing problems: (1) compel the trustee to decide whether to assume or reject a license agreement before the sale, and (2) change the licensee's role and bargaining power in the bankruptcy. That said, Distributor should not rely exclusively on these approaches (and duly consider the other Parts herein).

In the first approach, Distributor can request that the bankruptcy court fix a time for the trustee's assumption or rejection of an executory agreement before the sale.[111] Chapter 11 of the Code does not fix the time for the trustee to assume or reject executory agreements as it does in Chapter 7 (Figure 2).[112] The requesting party must state a justifiable need. However, no clear standard for justifiable need exists.[113] Bankruptcy courts are generally reluctant to interfere with the trustee's decisions; particularly when the debtor's reorganization is complex,

[110] FED. R. BANKR. P. 6004(c). *See, e.g.,* Document 2612*, In re* Eastman Kodak Co., No. 12-10202 (Bankr. S.D.N.Y. 2012) (providing notice and hearing dates).

[111] 11 U.S.C. § 365(d)(2). This Code section provides, in pertinent part, that any party to executory contract with the debtor may ask the court to order the trustee "to determine within a specified period of time whether to assume or reject such contract . . . ."

[112] 11 U.S.C § 365(d)(1)–(2).

[113] *See, e.g.*, *In re* Kmart Corp., 290 B.R. 614, 619–20 (Bankr. N.D. Ill. 2003) (acknowledging that no clear standard exists to justify a court compelling a debtor to set a time for assumption or rejection but signaling that an agreement that "is the cornerstone of . . . [a] reorganization" might fulfill the standard) (quoting *In re* Resource Tech., Corp., 254 B.R. 215, 227 (Bankr. N.D. Ill. 2000)). *See also In re* Dynamic Tooling Sys., Inc., 349 B.R. 847, 850 (Bankr. D. Kan. 2006) (admonishing the appellant licensee because the licensee could have sought the bankruptcy court's help under 11 U.S.C. § 365(d)(2) but did not).

involving numerous assets and executory agreements.[114] For example, the bankruptcy court in *Kmart* signaled a willingness to compel the debtor to decide earlier when an executory agreement "is the cornerstone of . . . [a] reorganization."[115]

Consider the second approach. Distributor can ask the bankruptcy court to estimate the dollar value of a claim against the debtor as if the trustee rejected the license agreement.[116] This approach has the added potential benefit of changing Distributor's role in the bankruptcy from party in interest to unsecured creditor.[117] An unsecured creditor is entitled to be heard on all matters in a bankruptcy proceeding whereas a party in interest is limited to those matters that affect its interest in property.[118] Additionally, an unsecured creditor is entitled to vote on the debtor's proposed plan for reorganization (letter "D" in Figure 2).[119] These aspects may raise the licensee's bargaining power in the

---

[114] *See In re Kmart Corp.*, 290 B.R. at 620.

[115] *Id.* (quoting *Resource Tech.*, 254 B.R. at 227).

[116] *See* 11 U.S.C. § 502(c)(1)–(2) (2012). That Code section provides a mechanism for estimating and allowing a claim in a bankruptcy proceeding in the case of an executory agreement that has not been breached, assumed or rejected. In such circumstance under § 502(c)(1)–(2), the bankruptcy court "shall" for the "purpose of allowance" of a claim under § 502 estimate:

"(1) any contingent or unliquidated claim, the fixing or liquidation of which, as the case may be, would unduly delay the administration of the case; or

(2) any right to payment arising from a right to an equitable remedy for breach of performance." *Id.*

See, e.g., *Dynamic Tooling*, 349 B.R. at 857. The bankruptcy court noted that the non-exclusive licensee could, at any time, have become a creditor of the debtor in the bankruptcy proceeding by invoking § 502(c)(1)–(2). *Dynamic Tooling*, 349 B.R. at 857. The court pointed out that attaining the status of an unsecured creditor with an allowed claim in the proceeding would have entitled the licensee to vote on the reorganization plan confirmation, potentially to the licensee's advantage. *Id.* at 857.

[117] 11 U.S.C. § 502(c)(1)–(2). *See In re Dynamic Tooling*, 349 B.R. at 857.

[118] *See*, *e.g.*, Philip A. Schovanec, *Bankruptcy: The Sale of Property Under Section 363: The Validity of Sales Conducted Without Proper Notice,* 46 OKLA. L. REV. 489, 498–99 (1993) ("Because of the importance placed on each party's stake in the property to be sold, even a single creditor has a sufficient interest to have a proposed sale reviewed, and if appropriate denied."). *See also* 1 BANKRUPTCY LITIGATION § 6:33, *available at* Westlaw (database updated August 2015). In the case of a creditor, the creditor may or may not have an interest in the property up for sale, yet still has the opportunity to review the sale terms and object. *Id.* By contrast, a party in interest only has standing to object if that party's interest is affected by the sale. *Id.*

[119] LEE MORRIS, *Reorganization in Chapter 11*, *in* BANKRUPTCY ROADMAP at 262, n. 38 (State Bar of Texas 2010) (citations omitted) ("[T]he holders of at least two-thirds in amount and more than half in number of the allowed claims of such class must vote in favor [of a plan for reorganization].").

bankruptcy, depending upon the dollar value of the claim.[120]

2. Appeals After the Sale Closes

There is a third timing issue to consider. Rule 6004(h) provides for the automatic issuance of a fourteen-day stay after entry of a final sale order "unless the court orders otherwise (number 6 in Figure 1)."[121] Absent objection, the bankruptcy court may shorten or waive the stay on the request of the trustee.[122] Absent the stay, a timely filed appeal to vacate or modify a final sale order is likely to be dismissed as equitably moot.[123] This may be so even if the underlying facts and arguments are favorable to the appellant.[124]

The stay is even more important if the sale order includes a § 363(m) good faith purchaser finding.[125] In that case and without a stay, that finding generally insulates the sale order from an appeal. To obtain a new stay, the appellant must post a supersedeas bond,[126] and present successful arguments in support of the stay.[127]

---

[120] *Id.* at 270–71.

[121] FED. R. BANKR. P. 6004(h). *See also* Hower v. Molding Sys. Eng'g Corp., 445 F.3d 935, 937–38. (7th Cir. 2006) (holding no abuse of discretion in the bankruptcy court's authorization of the sale order with no stay because the debtor required cash immediately and dismissing losing bidder's appeal of the sale order as moot).

[122] FED. R. BANKR. P. 2002(a), Notes of Advisory Committee on Rules, *supra* note 27.

[123] *See, e.g.*, *In re* Dynamic Tooling Sys., Inc., Nos. KS-06-105, KS-06-111, 04-15900-11, 2007 WL 1747045, at *3 (B.A.P. 10th Cir. June 18, 2007). The Tenth Circuit employed the five-factor test applied in *In re Continental Airlines* to determine whether an appeal from a bankruptcy court's order should be dismissed on the grounds of equitable mootness. *In re Continental Airlines*, 91 F.3d 553 (3d Cir.1996). One of the factors was whether or not a stay of the order pending appeal had been obtained. *In re Dynamic Tooling Sys.*, 2007 WL 1747045, at *3.

[124] *See, e.g.*, *In re Dynamic Tooling Systems, Inc.*, 2007 WL 1747045, at *2–3 (refusing to consider an appeal of the sale order on the grounds of both equitable mootness and constitutional mootness because the appellant failed to obtain a stay of the sale, and the completed sale could not be easily unwound).

[125] Pusser's (2001) Ltd. v. HMX, L.L.C., No. 11C4659, 2012 WL 1068756, at *6 (N.D. Ill. Mar. 28, 2012) (dismissing plaintiff's challenge of a bankruptcy court's orders based, in part, on a § 363(m) good faith purchaser finding). *But see In re* Fulks, 343 B.R. 701, 711 (Bankr. M.D. Fla. 2006) (sitting in equity, vacating the sale of patents to the debtor on the basis of grossly inadequate price).

[126] FED. R. BANKR. P. 8007(a)(1)(B).

[127] *Id.* at 8007. *See, e.g.*, *In re* Virgin Offshore USA, Inc., No. 11-13028, 2012 WL 6059359, at *3 (Bankr. E.D. La. Dec. 6, 2012) (denying appellant's request for a stay pending appeal under the four-factor test used in requests for injunctive relief). The four factors favoring grant of the stay are: (1) the appellant's likelihood of success on the merits, (2) the appellant will be irreparably harmed, (3) other parties

continued . . .

Even with the existence of a stay and a timely filed appeal, bankruptcy courts are extremely reluctant to overturn prior sale orders in a § 363(f) sale.[128] After the close of a bankruptcy sale, bankruptcy courts favor a policy of finality of sales not likely to favor the licensee.[129] Further, in the event of an appeal, bankruptcy courts have jurisdiction to interpret their own sale orders.[130] Yet, the sale order is likely to incorporate language suggested by the trustee favoring the debtor and buyer and not the licensee.[131]

In further appeals after entry of a final sale order, a reviewing higher level court will not set aside the bankruptcy court's findings of fact unless clearly erroneous, again favoring the debtor and buyer over the licensee.[132] Conclusions of law in the sale order are subject to a de novo standard of review and may be more susceptible to modification relative

---

in interest would be substantially harmed absent the stay, and (4) grant of the stay is not contrary to the public interest. *In re Virgin Offshore*, 2012 WL 6059359, at *3.

[128] *In re Fulks*, 343 B.R. at 706–07 (reluctantly overturning an order for sale of infringed patents because of grossly inadequate consideration paid, and stating "[t]here must be a stability in sales and the time must come when a fair bid is accepted and the proceeding is ended."). *See also* LAWRENCE R. AHERN, III AND NANCY FRAAS MACLEAN, BANKR. PROC. MANUAL § 6004:1 (2016 Ed.), *available at* Westlaw (database updated Jan. 2016). The authors highlight the reluctance of courts to invalidate a sale because of concern for public confidence in the finality of judicial sales. *Id.* at § 6004:1. The authors also note the added protection from the possibility of a court reversing a sale under 11 U.S.C. § 363(m). AHERN & MACLEAN *supra*, at § 6004:1. Under § 363(m), a sale order finding that the buyer was acting in good faith cannot reversed on appeal. AHERN & MACLEAN *supra*, § 6004:1.

[129] *In re* Edwards, 962 F.2d 641, 643 (7th Cir. 1992) ("If purchasers at judicially approved sales of property of a bankrupt estate, and their lenders, cannot rely on the deed that they receive at the sale, it will be difficult to liquidate bankrupt estates at positive prices.").

[130] *See, e.g.*, *In re* Novon Int'l., Inc., No. 98-CV-0677E(F), 96-BK-15463B, 2000 WL 432848, at *1 (W.D.N.Y Mar. 31, 2000). A district court sits in review of a bankruptcy court's interpretation of its own prior order. *Id.* at *1. *See also In re* Ice Mgmt. Sys., Inc., No. CC-14-1046-KiKuDa, 2014 WL 6892739, at *4 (B.A.P. 9th Cir. Dec. 8, 2014) (reviewing bankruptcy "conclusions of law and questions of statutory interpretation de novo, and factual findings for clear error.") (quoting Clear Channel Outdoor, Inc. v. Knupfer (*In re* PW, L.L.C.), 391 B.R. 25, 30 (9th Cir. 2008)); Pusser's (2001) Ltd. v. HMX, L.L.C., No. 11C5659, 2012 WL 1068756, at *5 (N.D. Ill. 2012) (cause dismissed Sept. 28, 2012) ("Where a bankruptcy court interprets its own order, however, such interpretation is entitled to more deference and is reviewed for an abuse of discretion").

[131] *See* Document 34 at 6, *In re* Atmospheric Glow Techs., Inc., Case No. 08-31320 (Bankr. E.D. Tenn. June 17, 2008) (proposing certain provisions presented by the trustee be included in a sale order).

[132] *In re Ice Mgmt.*, 2014 WL 682739, at *4; *In re Novon*, 2000 WL 432848, at *1.

to fact finding.[133] Other than adequate notice, taken up in the next Part, the licensee should temper its expectations of success in appealing a sale order.

To summarize, this Part suggested two approaches Distributor can use to address trustee delay. The first approach involved attempting to compel the trustee to decide between assuming and assigning or rejecting a license agreement before the sale. The second approach involved changing Distributor's role from party in interest to unsecured creditor. This Part concluded with a warning about appeals. With the possible exception of adequate notice discussed below, appeals favor debtors like KnifeCo and buyers like Competitor. Appeals do not favor licensees like Distributor. The wiser course for Distributor is to raise all possible challenges to the sale by the objection due date, or in any event before entry of a final sale order (number 7 in Figure 1). What follows next is a discussion of adequacy of notice.

B. Adequate Notice Requirements

A § 363(f) sale that purports to extinguish a non-exclusive patent license with the sale of the licensed patent constitutes depriving a person of property.[134] The Fifth Amendment of the United States Constitution prohibits depriving a person of property, or an interest in property, without due process.[135] Therefore, in the context of a § 363(f) free and clear sale, bankruptcy law requires constitutionally mandated due process including adequate notice.[136]

If a party in interest receives adequate notice of a § 363(f) sale and fails to object, the party's interest will usually be extinguished by the sale.[137] A party in interest can appeal a sale order on the basis of

[133] W. Auto Supply Co. v. Savage Arms, Inc. (*In re* Savage Indus.) 43 F.3d 714, 719 n.8 (1st Cir. 1994) (requiring de novo standard of review under same appellate standards as district court review).

[134] *See* sources cited *infra* note 136.

[135] U.S. CONST. amend. V ("No person shall be . . . deprived of life, liberty, or property, without due process of law. . . .").

[136] *See generally* 11 U.S.C. § 324 (2012); FED. R. BANKR. P. 2002(a), 6004(c) (addressing aspects of notice pertinent to this writing further developed in case law). *See, e.g.*, Unaatuq, L.L.C. v. Green (*In re* Catholic Bishop of N. Alaska), 509 B.R. 229, 241–42 (Bankr. D. Alaska 2014) (stating "[u]ndoubtedly, parties holding known liens or asserting known interests in property to be sold are entitled to actual notice of a debtor's intent to sell such property free and clear of those interests. This is required by the Bankruptcy Code, the bankruptcy rules, and the due process clause of the Fifth Amendment." (internal footnotes omitted)).

[137] *See, e.g.*, FutureSource L.L.C. v. Reuters Ltd., 312 F.3d 281, 285–86 (7th Cir. 2002) (finding a licensee's rights in licensed software and data extinguished in a § 363(f) sale because the licensee had adequate notice and did not object).

inadequate notice,[138] which has become a common procedure.[139] The party claiming inadequate notice must make a prima facie showing that the notice was indeed inadequate.[140] In an order approving the trustee's motion to sell assets under § 363(f), a finding of adequate notice reduces the buyer's risk and, depending upon the sale terms, also the seller's.[141] What constitutes adequate notice depends upon whether a party in interest is known or unknown.[142]

1. Known Parties in Interest

The debtor in bankruptcy is required to provide the court a list of its

[138] *See, e.g.*, Compak Cos. v. Johnson, 415 B.R. 334 (N.D. Ill. 2009). Known parties in interest had general knowledge of a § 363(f) sale of licensed patents but never received actual notice including hearing and bar dates. *Id.* at 339–40. In an appeal of the sale challenging the adequacy of notice, the district court considered the circumstances of the sale and held "terminating the DuoTech License pursuant to the Sale Order would violate Holdings' [the licensee's] right to due process of law under the Fifth Amendment to the Constitution of the United States." *Id.* at 340. Emphasizing the "strong policy of finality in bankruptcy sales," the district court voided only that portion of the sale order necessary to protect the non-debtor licensee's rights. *Id.* at 341–43.

[139] *Id.* at 341 ("By far the most frequent mistake or infirmity held to warrant vacating a confirmed sale is defective notice to interested parties of the judicial sale."). *But see In re* Edwards, 962 F.2d 641, 645 (7th Cir. 1992) (denying property owner's defective notice challenge, in part, because of the appellant's delay even though notice was defective).

[140] *In re Catholic Bishop*, 509 B.R. at 249 ("The claimants have the burden 'of proving a prima facie error [of notice] in service.'").

[141] *See, e.g.*, *In re* Nortel Networks Inc., No. 09–10138 KG, 2011 WL 1661524 at *5 (Bankr. D. Del. May 2, 2011) (approving, in the sale order, notice to unknown patent licensees by national publication as reasonably calculated to put unknown patent licensees on notice).

[142] As to the difference in level of notice required,

"The level of notice required by the Due Process Clause depends on whether a creditor is 'known' or 'unknown.' A debtor must provide actual notice to all 'known creditors' in order to discharge their claims. Known creditors include both claimants actually known to the debtor and those whose identities are 'reasonably ascertainable.' A claimant is 'reasonably ascertainable' if he can be discovered through 'reasonably diligent efforts.' [I]n order for a claim to be reasonably ascertainable, the debtor must have in his possession, at the very least, some specific information that reasonably suggests both the claim for which the debtor may be liable and the entity to whom he would be liable. By contrast, the debtor need only provide 'unknown creditors' with constructive notice by publication. Publication in a national newspaper such as *The Wall Street Journal* is sufficient." Williams v. Placid Oil Co. (*In re* Placid Oil Co.), 753 F.3d 151, 154–55 (5th Cir. 2014) (internal citations omitted). *See In re* Argonaut Fin. Serv., Inc., 164 B.R. 107, 112 (N.D. Cal. 1994) ("Generally, however, in bankruptcy cases, courts have found that known creditors are deserving of actual notice while unknown creditors are owed only publication notice.").

creditors.[143] The debtor is also required to provide a list of executory agreements to the court along with the address of the other party (or parties) to the executory agreement.[144] At times, debtors fail to include all executory agreements in the schedules it is required to submit.[145] Presumably, any party on the debtor's schedules is "known" to the debtor for the purposes of notice.

A known party in interest is entitled to written notice by mail, to a specifically named person, at the address provided in a license agreement at issue whether it is the licensed patent or the patent license that is the subject of the sale.[146] The known party may request that notice be provided at a different address or by a different method.[147]

2. Unknown Parties in Interest

The notice standard for unknown parties in interest is different from the standard for known parties in interest. The standard for unknown parties in interest requires "notice reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections."[148] Mere general knowledge of a bankruptcy is insufficient for the purposes of providing adequate notice.[149]

The bankruptcy court may specify the conditions under which notice by publication satisfies the reasonably calculated standard.[150] The Nortel Networks bankruptcy provides an example of proper notice to unknown licensees.[151] Nortel Networks conducted a § 363(f) sale of

[143] FED. R. BANKR. P. 1007(a).

[144] *Id*. at 1007(b)(1)(C).

[145] For example, the debtor did not disclose an executory patent license agreement as either an asset or an executory agreement. *In re* JZ L.L.C., 357 B.R. 816, 819 (Bankr D. Idaho 2006).

[146] FED. R. BANKR. P. 2002(g)(1). *See* Compak Cos. v. Johnson, 415 B.R. 334, 338–39 (N.D. Ill. 2009) ("Unless a creditor specifies a different mailing address, notices must be mailed to the address shown on the list of creditors or schedule of liabilities, whichever is filed later.").

[147] FED. R. BANKR. P. 2002(g).

[148] *See, e.g.*, *In re* Gencor Indus., 298 B.R. 902, 914–915 (Bankr. M.D. Fla. 2002) (stating that general knowledge is insufficient and requiring that adequate notice includes dates relevant to the party receiving notice).

[149] *Id.*

[150] FED. R. BANKR. P. 2002(a)(i).

[151] *Id.*; *In re* Nortel Networks Inc., No. 09-10138 KG, 2011 WL 1661524, at *5 (Bankr. D. Del. May 2, 2011) (ordering an approved publication in nationally distributed publications, including *The Wall Street Journal* (National Edition), *The Globe and Mail* (National Edition), *The New York Times* (National Edition) and *The Financial Times* (International Edition), within five (5) business days of entry of the bankruptcy court's Bidding Procedures Order).

approximately six thousand patents covering wireless communications technologies.[152] Patents in such technology areas are usually the subjects of multiple non-exclusive license agreements ensuring freedom to operate by multiple industry participants.[153]

In the Nortel sale, the stalking horse bidder was concerned with its potential risk related to the possibility of unknown licensees of the Nortel patents.[154] In the order approving the sale and bidding procedures, the bankruptcy court found that the notice to unknown licensees was sufficient.[155]

3. How Licensees Can Address Notice

From the discussion so far and in the context of the Test Cases, the reader may ask how the threatened licensee can challenge notice in a § 363(f) sale, ensure timely receipt of notice, and also how to ensure an early warning that licensor bankruptcy is on the horizon. This Part addresses each of these questions.

As discussed previously in Part VI.A.2, bankruptcy courts are extremely reluctant to overturn previous orders relating to a § 363(f) sale.[156] The policy justification for this position is that bankruptcy courts do not want to create the appearance of uncertainty for buyers in such sales as doing so would discourage future buyer participation in bankruptcies.[157] However, notice is the cornerstone[158] of due process in bankruptcy and susceptible to challenge at the bankruptcy court level and on appeal.[159]

---

[152] *Id.* at *5.

[153] *See generally* Michael Kerman, *Delaware Bankruptcy Court Approves Sale of $4.5 Billion of Nortel Networks, Inc. Assets*, BANKRUPTCY LAW REPORTER (BNA July 14, 2011) (describing the potential for the purchased wireless communications patents to cover a variety of third party products).

[154] *See In re Nortel Networks,* 2011 WL 1661524, at *3. The bankruptcy court order included a finding that the stalking horse bidder would not have entered into the purchase agreement had the order approving the sale not authorized the buyer to assume or reject executory license agreements. *Id.*

[155] *Id.* at *5.

[156] *See, e.g., In re* Fulks, 343 B.R. 701, 706–07 (Bankr. M.D. Fla. 2006). *See also* AHERN & MACLEAN, *supra* note 128, § 6004:1.

[157] *See, e.g., In re Fulks*, 343 B.R. at 706–07; *see also* AHERN & MACLEAN, *supra* note 128, § 6004:1. *See generally In re* Edwards, 962 F.2d 641, 643 (7th Cir. 1992) (predicting that "positive prices" would be difficult to obtain absent reliance on judicially approved bankruptcy sales).

[158] *In re* Savage Indus., 43 F.3d 714, 720 (1st Cir. 1994).

[159] Challenges to adequate notice at the Bankruptcy Court level: *In re* Crumbs Bake Shop, 522 B.R. 766, 774 (Bankr. D. N.J. 2014) (holding notice of sale to known trademark licensees inadequate); *In re* Golden Books Family Entm't, Inc., 269 B.R. 300, 303–04 (Bankr. D. Del. 2001) (holding notice of motion for sale of a

continued . . .

Consider in the Test Cases what Distributor can do to ensure timely receipt of notice. Distributor can at least check to ensure that KnifeCo listed the non-exclusive license agreement with Distributor on the schedule of KnifeCo's executory agreements. Distributor would be entitled to notice of a § 363(f) sale as a party in interest. Distributor may care to elect to receive notices as a party in interest in the bankruptcy proceeding electronically to minimize regular mail time lags.[160]

In the future, and to get an earlier warning of impending or actual bankruptcy of a licensor such as KnifeCo, Distributor may consider using internet-based information systems. For example, systems such as Pacer can be used to follow a bankruptcy case.[161] However, the knowledge of the jurisdiction of the bankruptcy and party name are required.[162] Pacer does not push notices to users.[163] Other no or low fee-based information services do push information to users, but still require some advance knowledge of jurisdiction and party name.[164] Higher cost fee-based services require no prior knowledge.[165] The parties to a license agreement can also include notice provisions related to events such as bankruptcy in the agreement.[166]

---

copyright license agreement inadequate by failure to address the notice to a named individual). Challenges to adequate notice on appeal of a sale order: Compak Cos. v. Johnson, 415 B.R. 334 (N.D. Ill. 2009) (upholding bankruptcy court's finding of inadequate notice to licensees).

[160] *See* MORRIS, *supra* note 119, at 5–6 (describing general practices relating to notice in bankruptcy motions and highlighting the necessity of checking local rules of a bankruptcy court, which may even vary from judge to judge in a given court). Under 11 U.S.C. § 1109(b) (2012), a party in interest may file a request for special notice with the bankruptcy court. *See* 1 BANKRUPTCY LITIGATION § 5:27, *available at* Westlaw.

[161] *See* PACER, http://www.pacer.gov (last visited Feb. 10, 2016).

[162] *Id.*

[163] *See id.*

[164] *See, e.g.*, *How Email Noticing Works*, ELEC. BANKR. NOTICING, http://www.ebnuscourts.com/register/link_works.adp (last visited Feb. 10, 2016). This Electronic Bankruptcy Noticing website pushes information to registered users based upon the party name in the case title. There is no charge for the first instance of document retrieval, however, fees will apply upon any subsequent access to the same document. To minimize costs, download documents on the first instance of access.

[165] For example, Westlaw, Lexis Nexis and Bloomberg information services allow a user to create an alert based upon the filing of a document in a bankruptcy court in any jurisdiction in the United States based upon a search of the licensor's name in the case title. The alert user will be notified when a new filing occurs meeting the alert criteria. *See* MICHAEL L. BERNSTEIN & GEORGE W. KUNEY, BANKRUPTCY IN PRACTICE § 2.33 (5th ed. 2015), *available at* Westlaw (providing a short list of very useful websites including, for example, www.bankruptcydata.com).

[166] *See* Cross License Agreement between Intuitive Surgical, Inc. and Hansen

continued . . .

To summarize, a licensee may use any aspect of notice discussed in this Part in an objection to a § 363(f) sale, and even in challenging an order for sale. Appeals of final sale orders require a stay. Licensees should take care to prevent waiver of the automatic stay period after the close of the sale (Numbers 6 and 7 in Figure 1).

C. Consent

Courts are divided as to what constitutes consent of the non-exclusive licensee under § 363(f)(2).[167] As will be demonstrated below, deeming consent given absent the licensee's objection to a sale is unfair when applicable non-bankruptcy law already prohibits the sale. Bankruptcy courts seem not to follow applicable bankruptcy law applied to patent licenses. This leaves only one safe choice when dealing with the consent requirement in § 363(f)(2) in the context of the Test Cases. That choice is to timely object to the sale in writing by the due date. What follows below is a brief discussion of the jurisdictional split over the consent requirement under § 363(f)(2). Thereafter, Part VI.E.2 turns to how the threatened licensee, like Distributor, can address consent.

1. Consent May be Express or Implied but Construing Silence as Consent is Unfair

Outside of the patent licensing context and assuming proper notice, some courts require the trustee to approach the interest holder and obtain express consent prior to an interest-extinguishing sale.[168] In the patent

Medical, Inc. (Sept. 1, 2005), *available at* http://www.sec.gov/Archives/edgar/data/1276591/000095013406021209/f22304a3exv10w15.htm (last visited Feb. 10, 2016). Paragraph 5.4 of the agreement provides for immediate notice to the other party in the event of an insolvency event or filing of a bankruptcy petition.

[167] Michael J. Lichtenstein, *Can Consent Be Implied in a Sale of Property Free and Clear of Liens Under Section 363(f) of the Bankruptcy Code?*, J. BANKR. L. 2015.01-5 (2015). Except for FutureSource v. Reuters Ltd., 312 F.3d 281, 285–86 (7th Cir. 2002), the author discusses cases of express and implied consent of lienholders under § 363(f) (implicating § 363(f)(2)–(3)). *FutureSource* concerned the sale of copyrighted software and data that extinguished a software license implicating § 363(f)(1)–(2). Jon Minear, *Your Licensor Has a License to Kill, and It May Be Yours: Why the Ninth Circuit Should Resist Bankruptcy Law that Threatens Intellectual Property Licensing Rights*, 31 SEATTLE U. L. REV. 107, 124 (2007).

[168] *See, e.g.*, Lichtenstein, *supra* note 167, at 2. In *In re DeCelis*, the debtor co-owned a house subject to four liens. *In re* DeCelis, 349 B.R. 465, 466–67 (Bankr. E.D. Va. 2006). The co-owner never responded to any bankruptcy notices and never participated in the bankruptcy proceeding. *Id.* In a well-reasoned denial of the trustee's motion, bankruptcy court Judge Robert G. Mayer held that the co-owner's

continued . . .

licensing realm, this author is unaware of a bankruptcy court requiring a trustee to affirmatively seek a licensee's consent in a § 363(f) sale. This author is aware of one case that stands for the proposition that a failure to object to the sale of copyrights in software and data constitutes consent of a properly noticed licensee.[169] A number of bankruptcy court orders in the realm of patent licensing deem lack of objection to be consent of a properly noticed licensee.[170]

To deem lack of objection on the part of a patent licensee as consent is a departure from applicable non-bankruptcy law applied to patent licenses and licensed patents.[171] This is unfair to licensees. The licensee may fail to affirmatively object inside bankruptcy in reliance on applicable non-bankruptcy law and lose an important license. Conflicting word use between the Code and the Rules may also be to

---

silence does not constitute consent. *Id.* at 474 n.10. The trustee relied upon the cases in 3 COLLIER ON BANKRUPTCY ¶ 363.06[3] n. 27 (15th ed. 2006) and also the case of *In re* Gabel, 61 B.R. 661 (Bankr. W.D. La. 1985). *In re Decelis*, 349 B.R. at 469. Judge Mayer distinguished each case pointing out that the trustee may provide evidence of express or implied consent but that silence of the interest holder alone cannot be construed as consent. *Id.* at 469–74. *See also In re* Roberts, 249 B.R. 152, 158 (Bankr. W.D. Mich. 2000) (holding that lack of objection does not constitute consent and identifying the procedural posture of *In re* Gabel as cause for the misguided view that silence in a § 363(f) sale can constitute an interest holder's consent to the sale.).

[169] *FutureSource*, 312 F.3d at 285–86 (construing licensee's failure to timely object to properly noticed sale of copyrights in software and data as consent).

[170] *See In re* Eastman Kodak Co., No. 12-10202 (ALG), 2013 WL 588965 (Bankr. S.D.N.Y. Feb. 13, 2013) (deeming in sale order paragraph GG that failure to timely object to the sale, including licensed patents, constitutes consent to the sale under the noticed sale terms); *In re* Nortel Networks, Inc., No. 09-10138 KG, 2011 WL 1661524, at *7 (Bankr. D. Del. May 2, 2011) (deeming, in a bankruptcy sale order, consent given to assumption and assignment of executory license agreements in the absence of timely objection). *But see* Digital Domain Media Grp. Inc., No. 12-12568(BLS), 2012 WL 6571072, at *43–44 (Bankr. D. Del. Dec. 11, 2012) (objecting to the proposed § 363(b) sale of licensed patents in licensee's written motion); *In re* Digital Domain Media Grp., Inc., No. 12-12568 (BLS), 2012 WL 5427546, at *20–21 (Bankr. D. Del. Sept. 12, 2012) (deeming in paragraph 17 of a § 363(b) sale order that the assumption and assignment of executory licenses in the sale of licensed patents consented to over ongoing vigorous objection by Disney); *In re* Aviza Tech., Inc., No. 09-54511-RLE-11, 2009 WL 4720035, at *6 (Bankr. N.D. Cal. Sept. 29, 2009) (finding in a sale order that proper notice and requirements of § 363(f)(1)–(5) were satisfied, but silent on deemed consent in the absence of timely objection); *In re* DDMG Estate, 594 F. App'x 92, 92 (3d Cir. 2015) (preserving Disney's license under § 363(b) but construing the license narrowly). *See also* Pusser's (2001) Ltd. v. HMX, L.L.C., No. 11 C 4659, 2012 WL 1068756, at *8 (N.D. Ill. Mar. 28, 2012) (*cause dismissed* Sept. 28, 2012) (deeming consent given in a sale order in the absence of objection and rendering § 363(f) sale of a trademark free of a trademark cancellation claim).

[171] *See supra* Part IV.

blame, at least in part. [172]

The policy justification for construing a failure to object as consent is predicated upon the transaction costs of obtaining consent. [173] Whatever the policy justification, the safe course of action is for the threatened licensee to timely object in writing to the sale of a licensed patent or sub-licensed exclusive patent license even if applicable non-bankruptcy law already prohibits the sale.

2. Ensuring Non-Consent: Arguments Used in Objection

What follows below is a discussion of the arguments a licensee can raise in timely written objection to a § 363(f) sale. The specific content of the objection will depend upon which of the following, whether alone or in combination, is for sale: (1) the non-exclusively licensed patent (Patent Test Case), (2) the non-exclusive patent licenses (both Test Cases), and (3) the exclusive patent license (License Test Case). These arguments use other sections of § 363 and implement the legal concepts introduced in Part V.

a. Sale of The Non-Exclusively Licensed Patent of Test Case One

Consider the Patent Test Case and the sale of the non-exclusively licensed patent therein. This Part introduces a new sub-section of § 363 helpful to Distributor, namely § 363(e). Section 363(e) provides:

> The bankruptcy court on the request of an interest holder in property to be sold 'shall prohibit or condition' a sale or proposed sale of property 'as is necessary to provide adequate protection of such interest.'[174]

Under § 363(e), Distributor may ask the bankruptcy court to protect its rights in the license through the sale.[175] For example, § 363(e) was

---

[172] Section 363(f)(2) uses the word "consent" if applicable non-bankruptcy law does not permit the sale. However, Rule 6004 pertaining to § 363(f), uses the phrase "opportunity to object."

[173] *FutureSource*, 312 F.3d at 285–86 ("[T]ransaction costs would be prohibitive if everyone who might have an interest in the bankrupt's assets had to execute a formal consent before they could be sold.").

[174] 11 U.S.C. § 363(e) (2012).

[175] *See, e.g.*, Patrick A. Jackson & Ian J. Bambrick, *Debunking the Perceived Conflict Between §§ 365(h) and 363(f)*, 33 AM. BANKR. INST. J. (Oct. 2014) ("[Section] 363(e) is one of the Bankruptcy Code's 'you snooze, you lose' provisions. Thus, if the non-debtor does not request adequate protection, the court is under no obligation to provide it, but if the non-debtor is not caught snoozing and is able to prove the validity of its leasehold interest, adequate protection must be

continued . . .

available to a threatened licensee in the case of *In re Dynamic Tooling Systems, Inc*.[176] That case involved a free and clear sale of licensed patents as part of a Chapter 11 plan confirmation, similar to a § 363(f) sale.[177] The trustee neither assumed nor rejected the patent license agreement before the sale. The § 363(f) asset purchase agreement provided the buyer with the option to assume or reject the license agreement up to thirty days after the sale.[178]

The bankruptcy court overruled the non-exclusive patent licensee's objection to the reorganization plan, which included the sale of the licensed patents.[179] The bankruptcy court recognized that the licensee's option to retain under § 365(n) would only be triggered upon the buyer's rejection of the license agreement following the license extinguishing sale.[180] The bankruptcy court pointed out that § 363(e) protection of the license agreement through the sale by express order of the bankruptcy court would have been available.[181] The bankruptcy court's opinion did not expressly find that the licensee did not ask for § 363(e) protection of its license agreement. However, one is left to conclude that *In re Dynamic Tooling* stands for the proposition that the licensee who does not ask for § 363(e) protection of its license agreement does not get it.[182]

Distributor, however, need not rest solely on § 363(e) for protection. At least one commentator questioned whether § 365 and § 363(e) are mutually exclusive.[183] Fortunately, § 363(e) is not the only source of protection for licensees in the sale of a non-exclusively licensed patent. For example, in at least one case the licensee invoked § 365(n)(4)(B) for protection and not § 363(e).[184]

Section 363(n)(4)(B) provides, in pertinent part,

> Unless and until the trustee rejects such contract, on the written request of the licensee the trustee shall . . . not

provided.").

[176] *In re* Dynamic Tooling Sys., Inc., 349 B.R. 847, 850–51 (Bankr. D. Kan. July 29, 2009).

[177] *Id.*

[178] *Id.*

[179] *Id.* at 858.

[180] *Id.* at 856.

[181] *Id. See also* Compak Cos. v. Johnson, 415 B.R. 334, 343 (N.D. Ill. 2009) ("Compak was authorized to sell its intellectual property free and clear under another subsection of § 363(f), the defendants could have requested adequate protection under § 363(e).").

[182] *In re Dynamic Tooling*, 349 B.R. at 855.

[183] WARD, *supra* note 69, § 4:66.

[184] *In re* Particle Drilling Techs., Inc., No. 09-33744, 2009 WL 2382030, at *4 (Bankr. S.D. Tex. July 29, 2009) (approving a patent licensee's request for protection of its license under § 365(n)(4)(B) in a friendly bankruptcy proceeding).

> interfere with the rights of the licensee as provided in such contract, or any agreement supplementary to such contract, to such intellectual property (including such embodiment), including any right to obtain such intellectual property (or such embodiment) from another entity.[185]

In the case of *In re Particle Drilling*, a patent licensee objected to a proposed free and clear sale of the debtor's non-exclusively licensed patents.[186] The licensee asked the bankruptcy court to protect its rights to a non-exclusive license, directly invoking § 365(n)(4)(B) but not § 363(e).[187]

There is an argument that the licensee in *In re Particle Drilling* did not go far enough in its request for protection under § 365(n)(4)(B). The debtor did not contest the licensee's objection and request for protection from the bankruptcy court.[188] As will be demonstrated further below, other threatened licensees have gone further by invoking §§ 365(n)(1)(B) and 365(n)(2).[189] There is a sound reason for doing so. Section 365(n)(4) protections end at the trustee's rejection.[190] In theory, such protections would not be sufficient in the case that a buyer is allowed to assume or reject a license agreement days after the close of the bankruptcy sale. Because of this possibility, threatened licensees object to such sales by asking the bankruptcy court to preserve the right to elect under § 365(n)(2) through the § 363(f) sale.[191]

The case of *In re Ice Management*[192] is unique because the threatened licensee asked the bankruptcy court for protection of its

---

[185] 11 U.S.C § 365(n)(4)(B) (2012).

[186] *Particle Drilling*, 2009 WL 2382030, at *1.

[187] *Id.* at *3.

[188] *Id.*

[189] 11 U.S.C. § 365(n)(1)(B) provides for the licensee's option to elect to retain at least some of its licensed rights upon a debtor licensor's rejection of an executory patent license agreement. Section 365(n)(2) provides that the trustee shall allow the licensee to exercise its right to retain the license. The licensee must pay royalties owed and agree to waive the right allowable claims and set-off (if any). 11 U.S.C. § 365(n)(2) (2012).

[190] 11 U.S.C. § 365(n)(4) (2012) (The preamble states, "Unless and until the trustee rejects. . . .").

[191] *See In re* DNL Indus., No. 13-22079 (RDD), 2013 WL 3778348, at *10 (Bankr. S.D.N.Y. July 12, 2013) (preserving objecting licensee's rights under § 365(n) in the event of license rejection). *See also In re* GameTech Intl., Inc., No. 12-11964 (PJW), 2012 WL 5464489, at *16 (Bankr. D. Del. Nov. 7, 2012) (preserving objecting software licensee's rights under § 365(n)).

[192] *In re* Ice Mgmt. Sys., Inc., No. BAP CC-14-1046, 2014 WL 6892739, at *1 (B.A.P. 9th Cir. Dec. 8, 2014).

elected 365(n) rights prior to the sale.[193] *In re Ice Management* involved the sale of licensed patents.[194] The license agreement was deemed rejected prior to the § 363(f) sale.[195] The licensee elected to retain its rights in the license agreement to the extent provided in § 365(n).[196] The trustee sought the bankruptcy court's approval to sell the licensed patents free and clear.[197] The threatened licensee argued that under § 363(e), the bankruptcy court could not sufficiently protect the licensee's elected rights under § 365(n).[198] The bankruptcy court upheld the licensee's objection and asked the trustee to modify the terms of the sale.[199] The trustee modified the asset purchase agreement to provide that the sale of the licensed patents would be subject to the licenses and other liens against the licensed patents under 11 U.S.C. § 363(b).[200] The bankruptcy court approved the trustee's modified purchase agreement.[201]

Return to the facts of the Patent Test Case and note the argument not needed in the sale of the non-exclusively licensed patent. Distributor need not object to the sale of the non-exclusive patent license agreements with Distributor. The trustee cannot extinguish Distributor's non-exclusive rights by selling the non-exclusive license agreements in either Test Case. In the License Test Case, this reasoning also applies to the sale of the non-exclusive sub-license. However, this reasoning *does not apply* to the sale of the exclusive patent license agreement, which purports to extinguish the non-exclusive patent sub-license in the sale (Figure 3). Hence, the analysis below considers the arguments Distributor can use to object to the sale of the exclusive patent license.

b. Sale of the Exclusive Patent License

This Part considers the License Test Case and the arguments Distributor may raise in opposition to the sale of the exclusive patent license agreement. First, Distributor may use the arguments against assignment of the agreement introduced in Part V.A. Those arguments

---

[193] *Id.* at *2.

[194] *Id.* at *1.

[195] *Id.* at *2. *In re* Ice Management Systems involved a Chapter 7 bankruptcy proceeding. Under 11 U.S.C. § 365(d)(1), an executory agreement is deemed rejected by operation of law if neither assumed nor rejected within sixty days after the bankruptcy petition date and automatic stay.

[196] *In re Ice Mgmt.*, 2014 WL 6892739, at *2.

[197] *Id.*

[198] *Id.*

[199] *Id.*

[200] *Id.* at *2–3.

[201] *Id.* at *3–4.

implicate the hypothetical and actual assignment tests that govern the assignability of executory agreements in bankruptcy. Second, Distributor may also use the same approach considered for the Patent Test Case addressing the sale of the non-exclusively licensed patent. That approach involved asking the court to protect Distributor's rights through the sale under both § 363(e) and also § 365(n) as discussed in Part VI.C.2.a.

The sale of the exclusive patent license purports to extinguish the non-exclusive patent sub-license. Recall that license agreements deal with assignment language in three possible ways: (1) silence, (2) express prohibition of assignment, or (3) conditional language authorizing assignment.[202] The exclusive patent license agreement expressly prohibits assignment.

Under the hypothetical test, the trustee lacks the power to assume the exclusive patent license agreement. External to bankruptcy, express prohibition of assignment bars the assignment. Inside bankruptcy, the trustee cannot assume the agreement because the trustee cannot assign the agreement. Yes, this is a circular argument; but in this case the trustee cannot assume what it cannot assign.

In an actual test jurisdiction, express prohibition of assignment of the exclusive license agreement delivers the same result, but for different reasons. The trustee for KnifeCo might, or might not, be able to assume the exclusive license agreement. However, the trustee does not have the power to assign the agreement to Competitor. Like silence, which bars assignment, express prohibition yields the same result.

Consider two twists to the License Test Case. First, assume that the exclusive patent license agreement does not expressly prohibit assignment by either party. Instead, assume that the agreement is silent as to assignment as with the non-exclusive patent license agreements in either Test Case. Silence as to assignment is the same as express prohibition of assignment. Therefore, the result should be the same as discussed above under either the actual or hypothetical tests. The trustee does not have the power to assign the exclusive license agreement to Competitor.

For the second twist to the License Test Case, assume that the exclusive patent license agreement does not expressly prohibit assignment by either party. Instead, assume that the agreement provides conditions under which the exclusive patent license agreement can be assigned without the consent of Distributor. The bankruptcy court will determine (1) which of the hypothetical or actual assignment tests should apply, and (2) analyzing the assignment language, whether the

[202] Bd. of Regents of Univ. of Neb. v. BASF Corp., No. 4:04CV3356, 2007 WL 3342406, at *12 (D. Neb. Nov. 6, 2007).

trustee is permitted to assign the license agreement. The outcome will depend upon both aspects.

Here is the unfairness to licensees in a nutshell. Whether the license agreement is silent on assignment or expressly prohibits assignment, the result should be the same under either test. The trustee does not have the power to assign the agreement. In such circumstances, the sale should not go through whether or not the licensee objects.[203] But this is not what happens in § 363(f) sales when licensees remain silent. Unless the licensee timely objects to the sale in writing, it is likely to encounter a bankruptcy court sale order that deems the licensee's consent given.[204] This is so even when the trustee does not have the power to assign the license agreement.[205] Further, the licensee's avenues for appeal on grounds other than inadequate notice will be virtually non-existent after the close of the sale.

Turn now to Distributor's other considerations. Can Distributor's non-exclusive patent sub-license agreement really be extinguished if the trustee sells KnifeCo's exclusive patent license agreement in a § 363(f) sale? Most likely, yes.[206] The exclusive patent license agreement has

[203] In the case that a license agreement provides some conditions under which assignment might be permitted and those conditions, in fact, do not exist, licensees still face the same unfairness. The sale should not go through. *See* Philip S. Warden et al., *Bankruptcy Issues in Trademarks*, 19 IP LITIGATOR 14, 19 (2013).

[204] *Id.*

[205] *Id.*

[206] *See, e.g., In re* Atmospheric Glow Techs., Inc., No. 08-31320 (Bankr. E.D. Tenn. June 17, 2008). The debtor, Atmospheric Glow Technologies, Inc. ("ATG"), exclusively licensed certain patents from the University of Tennessee Research Foundation ("UTRF") within a specified field of use and with the right to grant sub-licenses. Document 38, at 2, *In re* Atmospheric Glow Tech., Inc., No. 08-31320 (Bankr. E.D.Tenn. June 17, 2008). "01,LLC" entered into a patent and know-how sub-license agreement with ATG. *Id.* at 1. Therefore, like Test Case Two, ATG was both a debtor exclusive licensee (through the exclusive patent license with UTRF) and also a debtor sub-licensor (through the sub-license agreement with 01,LLC). The trustee for ATG submitted a motion for authority to sell debtor ATG's assets. Document 34, at 1. The asset purchase agreement included provisions for both the sale of ATG's patents (not UTRF's) and also assignment of the exclusive license agreement between UTRF and ATG. Document 34-1, at 2. However, ATG never sought permission from the bankruptcy court to assign the exclusive patent license agreement with UTRF. Document 38, at 2–3. In its objection to the trustee's motion for sale, 01,LLC also highlighted that the exclusive license agreement between ATG and UTRF required UTRF's express permission to assign the agreement and that no such permission had been given by UTRF. *Id.* at 3–4. Curiously, however, 01,LLC never asked for protection from the bankruptcy court under any of § 363(e) or § 365(n) of the Code. Presumably, 01,LLC could have done so. In a second objection to the proposed sale, 01,LLC did specifically object to a possible assumption and assignment of the sub-license agreement to a § 363(f) buyer, but again, without reference to either § 363(e) or § 365(n). Document 55 at 2–3. One possible

continued . . .

the attributes of property. The non-exclusive sub-license agreement is the interest. As with the Patent Test Case, the arguments articulated in Part VI.C.2.a employing the protections of one or more of §§ 363(e), 365(n)(2), and 365(n)(4)(B) should be applicable.

What if the trustee for KnifeCo asks for the option to choose which of KnifeCo's executory agreements are to be assumed and assigned, and which are to be rejected after the close of a § 363(f) sale to Competitor? Before the § 363(f) sale, Distributor should timely object to the trustee's assignment of the exclusive license agreement.[207] Distributor should also ask the bankruptcy court to protect its rights under § 365(n) through the sale and also under § 363(e).

VII. CONCLUSION

Bankruptcy law empowers a debtor licensor to sell patent rights "free and clear" of any patent license under certain conditions. This writing considered the sale of any one or more of: (1) a non-exclusively licensed patent; (2) either a non-exclusive patent license or sub-license; and (3) an exclusive patent license. Section 363(f) sales are unfair to licensees in aspects of timing, notice and consent. A properly noticed patent licensee is highly likely to lose its license in a § 363(f) sale if the licensee fails to act. This writing is intended to be reference for a licensee's use in addressing a § 363(f) license-extinguishing sale.

This writing is limited to two of the conditions permitting a free and clear sale under § 363(f). Those two conditions permit the sale if "applicable non-bankruptcy law" would permit the sale or if the licensee consents to the sale that purports to extinguish the license. Using two over-simplified Test Cases and three questions, this writing explored the transfer of both licensed patents and patent licenses first outside of bankruptcy and then inside bankruptcy. The Test Cases raised and addressed the following issues in a § 363(f) sale:

- Whether a non-exclusive patent sub-license can be extinguished by the sale of the non-exclusively licensed patent. Yes.
- Whether a § 363(f) sale of an exclusive patent

explanation for 01,LLC's actions may be that it had already entered into a separate letter agreement with UTRF. Under that agreement, UTRF would license directly to 01,LLC in the event that the license was deemed either terminated or rejected. Document 38, at 2. The bankruptcy court excluded 01, LLC's sublicense from the sale in its Order Approving Sale of Assets. Document 81, at 1, 4.

[207] Distributor did not need those arguments for the non-exclusive patent license agreements only because those agreements cannot be extinguished by a § 363(f) sale. *See* 11 U.S.C. § 363(f) (2012).

> license can extinguish the non-exclusive sub-license therefrom. Likely yes.

In terms of timing, a licensee is entitled to no more than twenty-one days' advance notice of a § 363(f) sale. This notice period is further reducible for cause. In some cases, notice may be by general publication in a newspaper. A licensee is likely to have precious little time to act to protect its license through the sale that purports to extinguish its license.

Section 363(f) provides a debtor licensor opportunities to use timing to circumvent a licensee's options for protecting its license, purportedly available under § 365(n). Section 365(n) protections are only available at the licensee's option after the debtor licensor first rejects an executory license agreement. In a § 363(f) sale, the debtor licensor can extinguish the license in the sale without rejecting it. All the licensor has to do is sell the licensed patent and do nothing at all about the license. Absent objection by the licensee, the license will be extinguished.

The licensor can also circumvent § 365(n) licensee protections by delaying executory license agreement assumption and rejection decisions until after the sale that extinguishes the license. Bankruptcy courts usually grant requests for such delay, because the delay is attractive to buyers. In effect, buyers take control of assumption and rejection decisions regarding executory license agreements after the sale as a way to manage risk.

There are ways for licensees to deal with these timing issues in a timely written objection to the sale. For example, with a sufficiently strong argument, licensees can try to compel the debtor to assume or reject a license agreement before the § 363(f) sale. This approach is useful in the case of the trustee's lack of rejection of a license agreement, or delay until after the sale. A licensee need not wait until a sale notice to use this tactic.

Turning to notice, a § 363(f) sale purports to deprive a person of property. Any failure of adequate notice to a licensee raises due process issues under the Fifth Amendment of the United States Constitution. Such failure of notice can include the debtor providing notice by general publication when specific notice is required. The licensee can also challenge the correctness of the notice addressee, address, property description, sale and hearing dates, or any other aspect of notice that fails to adequately apprise the licensee of its rights.

With respect to patent license agreements, the consent requirement under § 363(f)(2) turns "applicable bankruptcy law" on its head. Generally, license agreements are not assignable and transfers of licensed patents are subject to the license. Outside of bankruptcy, the transfer of a licensed patent or a patent license does not extinguish the

licensee's rights even in the face of licensee inaction.

Section 363(f)(1) specifically refers to and adopts the general rules above as "applicable non-bankruptcy law." Unfairly, this is not the law that bankruptcy courts apply in a § 363(f) sale of licensed patents or patent licenses. Instead, a bankruptcy court's sale order will "deem" properly noticed licenses to have consented to the sale absent a timely written objection. The trustee will conduct the sale, hope nobody objects in time, and expedite the entry of the bankruptcy court's final sale order including the "deemed" consent of licensees. Following a policy of finality of bankruptcy sales designed to entice buyers, bankruptcy courts are reluctant to overturn final sale orders.

Turning the consent requirement on its head is understandable but not fair. Most contracts other than license agreements are freely assignable—the opposite of that required for patent license agreements. There is a fair argument that it is both judicially and administratively inefficient to require a licensee's affirmative consent in a § 363(f) sale. There is a fair argument that without the finality of sales in bankruptcy, willing buyers would not participate.

This writing does not suggest a change in the law. This writing addresses how licensees can play the hand they are dealt. To best play this hand, licensees have to timely object in writing to a sale notice. Silence is not an option if the licensee wants to keep its license.

For example, if the sale includes a license agreement, the licensee's objection can challenge the trustee's authority to assign the license agreement as provided in this writing. But what if the sale includes the licensed patent and the trustee delays or does nothing with respect to the license agreement? The licensee can still object and ask the bankruptcy court to protect its options under § 365(n) through the sale. Finally, the licensee can also ask for more generalized protections under § 363(e).

If there is one thing that surprised this author, it is the breadth of intellectual property-related interests that can be purportedly extinguished in a § 363(f) sale. These interests extend beyond a patent license or sub-license. For example, consider the recent § 363(f) sale of patents by debtor Aereo following Aereo's loss in the Supreme Court of the United States.[208] Aereo infringed a broadcaster's copyrights in television programming by operating within the scope of its own patents.[209] As of March 2015, the television broadcasters continue to object to the sale of Aereo's patents. The interests asserted by the broadcasters include not just retrospective claims for copyright

[208] *See* Am. Broad. Cos. v. Aereo, Inc., 134 S. Ct. 2498, 2511 (2014).

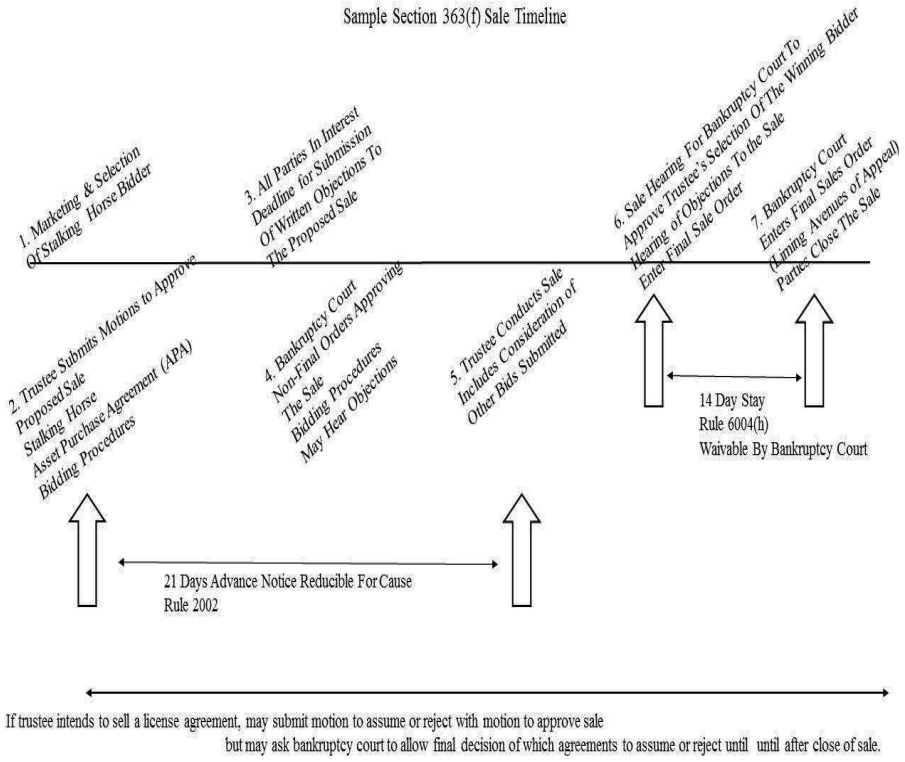
[209] *Id.* (holding Aereo publicly performed plaintiff's copyrighted works and remanding for further proceedings).

infringement and injunctive relief, but also prospective.[210]

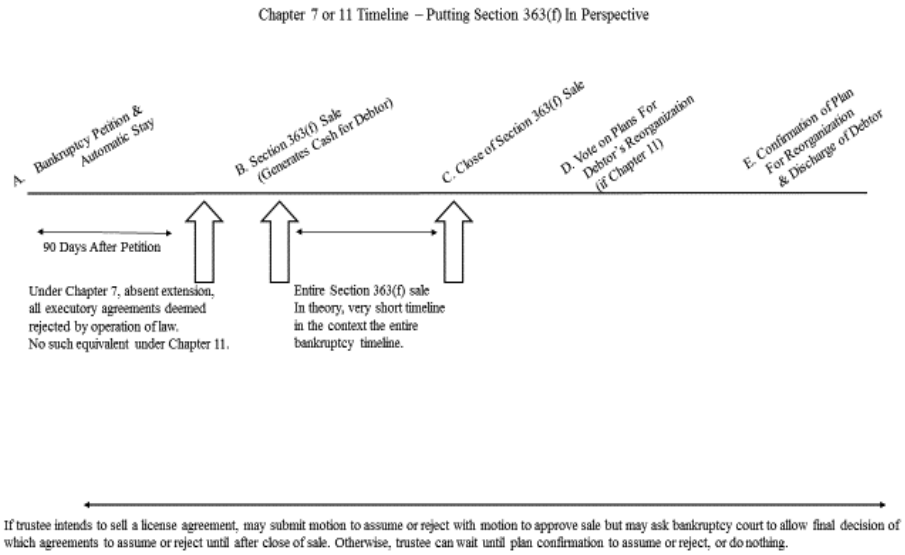
[210] *In re* Aereo, Inc., No. 14-13200-shl, 2015 WL 1419104, at *5 (Bankr. S.D.N.Y. Mar. 12, 2015).

VIII. FIGURES

A. Figure 1. Example of a § 363 Sale Timeline



B. Figure 2. Section 363(f) Sale in the Context of a Chapter 7 or 11 Bankruptcy Timeline



C. Figure 3. Summary of Rules External to Bankruptcy

EXTERNAL TO BANKRUPTCY			
Patent Test Case Asset to Be Sold	**Part Location & Rule**	**License Test Case Asset to Be Sold**	**Part Location & Rule**
Non-exclusively licensed patent	**Part IV.C.** Generally, transferee of licensed patent takes subject to the license whether or not transferee knows of license agreement.	Exclusive license agreement	**Part IV.B.** Law unsettled. If exclusive license agreement not tantamount to patent assignment,general rule of non-assignment should apply.
Non-exclusive patent license agreement	**Part IV.B.** Absent express agreement to the contrary, license agreement not assignable.	Non-exclusive patent sub-license agreement	**Part IV.B.** Absent express agreement to the contrary, license agreement not assignable.

D. Figure 4. Summary of Rules External to Bankruptcy

INSIDE A BANKRUPTCY SECTION 363(f) SALE			
Patent Test Case Asset to Be Sold	**Part Location & Rule**	**License Test Case Asset to Be Sold**	**Part Location & Rule**
Non-exclusively licensed patent	**Part VI.C.2.a.** Sale of patent can extinguish the non-exclusive patent license.	Exclusive license agreement	**Part III.C.** Sale cannot extinguish the exclusive patent license but can likely extinguish the non-exclusive patent sub-license
Non-exclusive patent license agreement	**Part III.C.** Sale cannot extinguish the non-exclusive patent license.	Non-exclusive patent sub-license agreement	**Part VI.C.2.b.** Sale cannot extinguish the non-exclusive patent license.