Going under: how to handle trade mark licences on an insolvency

With some 16,000 British companies going into liquidation last year, knowledge of how to keep licences of registered trade marks afloat could be crucial. Sarah Byrt of Mayer Brown looks at the types of insolvency and the impact they have

Start here: terminology

The main UK insolvency procedures are:

- administration – the most popular, used where the company might be rescued as a going concern;
- a company voluntary arrangement – where the directors make a proposal for the creditors to vote on;
- liquidation (aka winding up) – involves the company's assets being sold off before (usually) it is dissolved; now used less often than administration but raises the spectre of a licence being "disclaimed" (see below); and
- bankruptcy, a term used for individuals rather than corporates in the UK.

Licensor insolvency

Unless the licence is registered, the licensor's insolvency practitioner might sell off the trade marks to someone who has no idea that they are licensed. (Section 25(3)(a) of the 1994 Act of course provides that an unregistered licence is ineffective against someone acquiring a conflicting interest in ignorance of it.) As well as registering your licence, if you are a licensee whose licensor has gone into insolvency proceedings, you should write a formal letter to the insolvency practitioner to notify it of your licence and consider paying upcoming fees normally paid by the licensor, to keep the marks alive (but that may be throwing good money after bad, as explained below).

In a liquidation (but not in an administration), the most worrying aspect is the liquidator's power to disclaim (or reject) what is called "onerous property", which means: "*(1)* any unprofitable contract, and *(2)* any other property of the company that is unsaleable or not readily saleable or… may give rise to a liability to pay money or perform any other onerous act."

A trade mark licence might be "onerous property", eg, if the licensor in liquidation is obliged to pay renewal fees or, say, to sue infringers. Royalties do not stop the licence being "onerous property", but if there are minimum royalties, the liquidator may be more interested in selling off the licence along with the trade mark.

The Insolvency Act 1986 says that a disclaimer "operates so as to determine [ie, terminate]… the rights, interests and liabilities of the company [ie, the company in liquidation]… in respect of the property disclaimed" but it "does not, except so far as is necessary for the purpose of releasing the company from any liability, affect the rights or liabilities of any other person". The objective is to let the insolvent licensor off the hook, while, at the same time, trying to protect the rights of the licensee. The power to disclaim might, for instance, be used by a liquidator to get rid of the liabilities to pay rent on a property, but there is a lack of case authority to show how it might be used where an IP licensor goes under. Any person who sustains loss or damage as the result of a disclaimer (including potentially a licensee) becomes an unsecured creditor but might never recoup their loss.

Before and after

This uncertainty over the effect of a disclaimer in the case of licensor insolvency should be borne in mind when structuring a deal. Assignment is a possibility, but it may not be commercially feasible; and assignments in the two years before an insolvency may be struck down. Another option is for the trade marks to be held by an "insolvency remote" entity (essentially a non-trading company that will not run up debts). You can include in a licence an option to acquire ownership of the trade marks in the event of an insolvency only if the payment for that is full market value,

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otherwise creditors could be prejudiced. For important licences, consider:

> taking security (eg, a charge) over the licensed trade mark and then registering that security interest;

> phasing payments over the life of the licence, making it more attractive for an insolvency practitioner to keep the licence in existence; and

> imposing the obligation to pay renewal fees on the licensee (who could then perhaps deduct them from royalties), to make it less likely that a licence would be regarded as "onerous property".

If the insolvency has arisen and you have not already registered the licence, do so now. Watch out for notices from an insolvency practitioner and ensure they know about your licence. Consider making an offer to buy the IP rights, which should also help keep you informed.

Voluntary arrangements

A Company Voluntary Arrangement (CVA) is a compromise or other arrangement between a company and its creditors, the implementation of which is supervised by an insolvency practitioner. For instance, the directors might propose a CVA under which they pay only 70% of one type of debt (often rent due to a landlord – but it could also be licence fees due to a trade mark licensor), whereas other creditors get paid off in full. If the shareholders and creditors then vote in favour by more than 75%, the proposal is implemented, current management may remain in place and the proposal will be binding on all unsecured creditors, even if they did not attend the meeting (subject to the court's powers to overturn CVAs that are unfairly prejudicial or contain material irregularities). So a trade mark licensor could find itself out of pocket as a result of a proposal in which it played no part. This makes it important to look out for notice of a meeting and to attend.

Licensee insolvency

A licensor will usually have the right to terminate a licence on an insolvency event (which might be defined so as to occur soon after problems emerge, or only when some formal step is taken) – or at least to terminate for non-payment of royalties, but that may leave things too late. If there are minimum royalties, you might even consider leaving the licence in effect and then making a claim for the lost payments as a creditor, but the risk of reputational damage to the mark will usually militate against this. Where the insolvent licensee is obliged to pay renewal fees, it makes sense for the licensor to step in and pay, rather than running the risk of the trade marks lapsing. The good news is that the insolvency practitioner cannot assign the licence if the licence does not permit this. As explained above, a liquidator may be able to disclaim the licence, to get out of paying royalties, so the licensor is left having to find another licensee.

Insolvency and the US

If the insolvent company is based in the US, the first step is to review the licence to determine whether or not it is subject to the US Bankruptcy Code. If the licence is determined to be "executory", that is, where no essential or ownership rights have been transferred and where both parties still have important performance obligations remaining under the agreement, then the licence will be governed by the US Bankruptcy Code and subject to being assumed or rejected in bankruptcy.

Where the licensor has filed for bankruptcy protection, the bankruptcy trustee may either assume or reject the licence. If the licence is assumed by the trustee, the licensee can simply carry on operating under it. If, however, a trustee in bankruptcy rejects the licence, a licensee is left with two choices: treat the licence as terminated by virtue of the rejection and file a claim for monetary damages; or opt to retain its rights under the licence and continue to use the licensed IP. While this protection under the US Bankruptcy Code works for most IP rights, it does not work for trade marks. So trade mark licensees are at risk of losing their rights under the licence if their US-based licensor goes into bankruptcy.

Where the licensee files for bankruptcy, the licence may not be assigned by the licensee, unless the licensor consents or fails to object to this. A debtor-licensee may be able to assume a licence and continue to use the licensed IP while restructuring its business, despite the objection of the licensor, depending upon the type of IP licensed and the jurisdiction where the bankruptcy case is pending. ■