What To Do If A Real Party In Interest Goes Bankrupt[1]

By

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Introduction

One of the sad facts of a litigator's life is that occasionally real parties in interest go bankrupt--right in the middle of interesting, remunerative litigations. These unfortunate occurrences pose many questions for the counsel for both (or all) parties. However, this article focuses on what the BPAI can be induced to do.

The relevant statute is 11 USC 362(a), which reads as follows (with emphasis supplied):

> (a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970, operates as a stay, applicable to all entities, of--
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> > (1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;
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> > (2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title;
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> > (3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;
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> > (4) any act to create, perfect, or enforce any lien

> against property of the estate;
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> (5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;
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> (6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title;
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> (7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and
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> (8) the commencement or continuation of a proceeding before the United States Tax Court concerning a corporate debtor's tax liability for a taxable period the bankruptcy court may determine or concerning the tax liability of a debtor who is an individual for a taxable period ending before the date of the order for relief under this title.

What the Court Said in Checkers v. Commissioner

Checkers Drive-In Restaurants, Inc. v. Commissioner of Patents and Trademarks, 51 F.3d 1078, 34 USPQ2d 1574 (D.C. Cir. 1995), is a trademark case, and "the Court" is the Court of Appeals for the District of Columbia Circuit. Nevertheless, I believe that what it said is relevant to our practice.

In Checkers, Checkers and a competitor named CRG had reciprocal petitions to cancel each other's registrations pending before the TTAB when CRG went into bankruptcy. CRG thereupon petitioned the TTAB for a stay pursuant to 11 USC 362(a), and the TTAB purported to granted the stay. Actually, however, the petition and the granting of the petition were superfluous. An 11 USC 362(a) stay is triggered upon the filing of the bankruptcy petition without the necessity of a court order.[4] Thus, what the TTAB really did was to recognize the existence of the statutory stay, which was no doubt

important for its internal administrative purpose.

During the pendency of the stay, Checkers (not CRG) failed to file its section 8 affidavit evidencing its continued use of its mark. When the Post-Registration Section cancelled Checkers' registration, Checkers appealed to the Commissioner (now Director),[5] seeking to justify its failure to file its Section 8 affidavit on the ground that the stay had prevented it from doing so. The Commissioner affirmed the action of the Post-Registration Section, and, when Checkers sought court review of the Commissioner's decision, so did the District Court for the District of Columbia and the Court of Appeals for the District of Columbia Circuit.

The Court of Appeals for the District of Columbia Circuit noted that it had previously held that, "although the automatic stay blocks many legal actions against the debtor, it does not similarly bar claims brought by the debtor against other parties."[6] It continued in summary form that:

> The policies underlying the automatic stay--those of sheltering the debtor from the demands of creditors and preserving the bankrupt's estate pending orderly distribution by a trustee--are not implicated by an act, such as Checkers's filing of a section 8 affidavit, that has no effect upon a claim against the debtor or the property of the estate, but rather maintains the status quo with respect to the property of an entity engaged in litigation with the debtor.[7]

Its subsequent, detailed analysis returned repeatedly to the theme of "maintain[ing] the status quo."

Checkers first argued that, since its petition to cancel CRG's registration was premised in part on the existence of its (i.e., Checkers's) registration, "any act to maintain its federal registration--such as the filing of a section 8 affidavit--constituted the 'continuation' of its claim against the debtor within the meaning of subsection

362(a)(1)."[8] However, the Circuit Court didn't just disagree with this argument, it characterized it as "specious"[9]--reasoning as follows:

> We recognize that Checkers's filing of a section 8 affidavit could, in some attenuated sense, be deemed necessary to the maintenance of part of Checkers's cancellation petition against CRG. Without a valid federal registration, Checkers might not have had standing to pursue that portion of its cancellation petition claiming injury from CRG's alleged interference with rights guaranteed to Checkers by federal law. However, to acknowledge that the section 8 filing was tangentially related to Checkers's ability to litigate a portion of its claim against CRG is not to bring that filing within the scope of section 362(a). Any construction of section 362(a) that would reach the filing at issue here would extend the power of the bankruptcy courts into a whole host of activities far removed from the concerns addressed by the Bankruptcy Code.[10]

Next, Checkers:

> [sought] to invoke subsection 362(a)(1)…by arguing that its filing of a section 8 affidavit continued a claim against the debtor because it prevented CRG from prevailing in its own cancellation claim against Checkers. Checkers points out that the Commissioner's Rules of Practice in Trademark Cases provide for entry of judgment against a respondent in a cancellation proceeding where the respondent allows his or her registration to be canceled pursuant to section 8 while the proceeding is pending."[11]

However, the Circuit Court found that:

> This contention also lacks merit. Checkers's position amounts to an argument that section 362(a) disabled it from taking any action to fend off CRG's attempts to cancel Checkers's service mark registration. However, it is well settled in this circuit and others that the section 362(a) automatic stay does not require persons involved in litigation with a debtor to capitulate to the debtor's every demand. *See Inslaw*, 932 F.2d at 1473 ("Fulfillment of the purpose [of the automatic stay] cannot require that every party who acts in resistance to the debtor's view of its rights violates § 362(a) if found in error by the bankruptcy court."); see also *In re Merrick*, 175 Bankr. 333, 338

> (Bankr. 9th Cir. 1994) ("The automatic stay should not tie the hands of a defendant while the plaintiff debtor is given free rein to litigate."); *Martin-Trigona*, 892 F.2d at 577 ("There is ... no policy of preventing persons whom the bankrupt has sued from protecting their legal rights."). Thus, the fact that Checkers's filing of a section 8 affidavit might have prevented CRG from winning total victory presents no basis for the application of subsection 362(a)(1).[12]

Finally, Checkers:

> argue[d] that its filing of a section 8 affidavit was stayed by subsection 362(a)(3), which bars acts to exercise control over property of the bankrupt's estate. As Checkers sees it, by filing an affidavit necessary to maintain its own service mark registration, Checkers would have taken an act to exercise control over the right to use the "Checkers" service mark, in derogation of CRG's own claim to that right. Central to Checkers's theory is the notion that, by virtue of their cross-cancellation claims, Checkers and CRG each were vying for the single and exclusive federal right to use a service mark employing the word "Checkers" in interstate commerce. Thus, in Checkers's view, any act that served to maintain its own claim to that right was an act to "exercise control over" property of the bankrupt's estate within the meaning of subsection 362(a)(3).[13]

However, that argument faired no better:

> Checkers misunderstands the nature of the right created by federal registration under the Lanham Act. We recognize that federal registration constitutes prima facie evidence of the registrant's "*exclusive* right to use the registered mark in commerce." 15 U.S.C. §§ 1057(b), 1115(a) (emphasis added). However, we also note that *each* federal registration constitutes such evidence. In this case, therefore, the federal registrations of *both* Checkers and CRG constituted prima facie evidence that each enjoyed the exclusive right to utilize its respective service mark in commerce. While the cross-cancellation proceeding[s] might ultimately have established that protection of the rights of one registrant required cancellation of the service mark of the other, each held an independent property right in its own service mark until that decision was made, if ever. Thus, contrary to Checkers's theory, its filing of a section 8 affidavit would

> have affected only its own property, not the property of CRG. Accordingly, the required filing was not stayed by subsection 362(a)(3).[14]

The opinion in Checkers contains one more passage that is potentially relevant to our practice:

> while the application of the section 8 filing requirement may appear harsh in this case, Checkers failed to avail itself of a simple means of avoiding this result. Checkers neglected to take the prudential step of seeking clarification from the bankruptcy court, or even from the Commissioner [of Patents and Trademarks], as to whether its section 8 filing obligation was stayed.[15]

How Checkers Might Apply to Interferences

The opinion in Checkers answers some questions for the interference bar -- and raises some questions.

Answers

First, because 11 USC 362(a) applies to the TTAB, it applies to the BPAI. Thus, in at least some cases an interference is automatically stayed pursuant to 11 USC 362(a).[16] The question of which cases are automatically stayed is discussed hereinafter.

Second, since 11 USC 362(a) is a statute, it trumps 37 CFR 1.103(a), which says that "The Office will not suspend action if a reply by applicant to an Office Action is outstanding." That is, in those cases to which 11 USC 362(a) applies, the stay is automatic even if an applicant-interferent is under an order to do something.[17]

Third, the fact that an 11 USC 362(a) stay is in place does not relieve the opponent of the bankrupt of its obligation to pay maintenance fees.

Questions

The questions that Checkers raises mostly revolve around the meaning of the

phrase “maintaining the status quo.”

Suppose that you represent a patentee-interferent. At one level, your participation in the interference represents an effort to “maintain” one or more claims in the patent. Since those claims were in the patent at the time that the interference was declared, that is arguably an attempt to “maintain” the status quo ante the declaration of the interference. However, in many such cases it will actually be more important to your client to prevent yours opponent’s client from obtaining a patent -- or, at least, to delay its doing so.[18] Of course, by definition, prior to the declaration of the interference, an applicant-interferent has an application, rather than a patent. However, if its patentee-interferent opponent’s principal purpose in litigating the interference is to prevent or delay issuance of a patent to the applicant-interferent, can that really be said to be an effort to “maintain the status quo ante”? Put otherwise, is the real distinction between using the interference offensively and using it defensively?

Now, suppose that you represent an applicant-interferent that provoked the interference with a patentee-interferent by filing a suggestion of interference and that, during the pendency of the interference, your client goes bankrupt. Is the proceeding automatically stayed pursuant to 11 USC 362(a) or isn’t it because the whole proceeding is an effort to change the status quo ante -- that is, to obtain a patent for your client and to take down your opponent’s patent?

Next, suppose that you represent the non-bankrupt (such as Checkers in the Checkers case), that it is to your client’s advantage (for whatever reason) to obtain a stay, and that your opponent (for whatever reason) has not notified the APJ of the existence of the stay. In that case, since the stay is automatic, presumably you could notify the APJ of

the existence of the stay.

Next, suppose that you represent the non-bankrupt, that it is to your client's advantage to obtain a stay, and that the interference does not qualify for an automatic stay pursuant to 11 USC 362(a). In that case, you could ask the bankruptcy court to issue an order to the BPAI staying the interference under its (the bankruptcy court's) broad equitable powers under 11 USC 105.[19] The "stay" in that case would be an injunction issued by the bankruptcy court.[20] Your argument would be that the interference was "threatening" the bankruptcy petitioner's assets,[21] which of course would normally be the case.

Finally, a very practical question. What if you or your opponent asks the APJ to recognize the existence of an 11 USC 362(a) stay, the APJ either recognizes the existence of the stay or refuses to do so, and you don't like whatever it is that he or she did? Checkers advises us that we can seek clarification of questions concerning 11 USC 362(a) from the PTO,[22] but what if you don't like the APJ's ruling?

Of course, you can seek reconsideration of the individual APJ's decision by a panel of APJs pursuant to 37 CFR 41.125(c), but what if the panel's decision also goes against you?[23] Can either or both parties seek immediate review of the decision? Does that depend on whether the APJ or the panel recognized or refused to recognize the stay?

We believe that you could obtain immediate review of either a decision to recognize the stay or a decision to refuse to recognize the stay by way of petition for a writ of mandamus to the Federal Circuit.[24] Moreover, we believe that at least the bankrupt could seek relief from the panel's ruling from the bankruptcy court "for cause"[25] under 11 USC 362(d).[26] We say "at least the bankrupt" because requesting

relief from a stay by this technique is only clearly available to bankrupts--i.e., to the "real party in interest." If you represent the bankrupt's opponent and you want the stay lifted, you would have to somehow demonstrate that your client's interest is so intertwined with the bankrupt's interest that you would be considered to be a "real party in interest." [27]

Conclusion

Bankruptcy will add an additional, disruptive element to an interference not only for the bankrupt but also for the non-bankrupt. Bankruptcies happen rarely, and what should be done when the bankruptcy occurs during the pendency of an interference is unclear. Guidance from the BPAI should be sought - keeping in mind the Bankruptcy Code's goal is fair and orderly resolution of claims against the bankrupt estate. The BPAI may have to bend to the will of the bankruptcy court.

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[4] In re Meis-Nachtrab, 190 B.R. 302 (N.D. Ohio 1995). See also Boynton v. Ball, 121 U.S. 457, 466-67 (1887) ("where the bankruptcy proceedings are brought to the attention of the court in which a suit is being prosecuted against a bankrupt, that court shall not proceed to final judgment until the question of his discharge shall have been determined").

[5] This would now be a petition under 37 CFR 2.146(a).

[6] 51 F.3d at 1082, 34 USPQ2d at 1578.

[7] Id.

[8] 51 F.3d at 1083, 34 USPQ2d at 1579.

[9] Id.

[10] 51 F.3d at 1084, 34 USPQ2d at 1579, footnote omitted.

[11] 51 F.3d at 1084, 34 USPQ2d at 1580.

[12] 51 F.3d at 1084-85, 34 USPQ2d at 1580.

[13] 51 F.3d at 1085, 34 USPQ2d at 1580.

[14] 51 F.3d at 1085, 34 USPQ2d at 1581.

[15] 51 F.3d at 1085-86, 34 USPQ2d at 1581.

[16] In re Thomassen, 15 Bankr. 907, 909 (9th Cir. Bankr. App. Panel 1981) ("All proceedings are stayed, including arbitration, license revocation, administrative, and judicial proceedings. Proceeding in this sense encompasses civil actions as well, and all proceedings even if they are not before governmental tribunals." (quoting H.R. Rep. No. 595, 95th Cong., 1st Sess. 340 (1977), 1978 U.S.C.C.A.N. 6297.)). Actual notice of the bankruptcy proceeding is not required. In re Carter, 16 B.R. 481, 483 (W.D. Mo. 1981). The bankruptcy petition is notice to the world. Mueller v. Nugent, 184 U.S. 1, 14 (1902). However, you must inform the APJ of the existence of the stay so that he or she can "do the necessary" with respect to the BPAI's internal procedures.

[17] Note that, because ex parte prosecution is not designed to maintain the status quo, the same would not be true of ex parte prosecution--including pre-interference and post-interference ex parte prosecution.

[18] The PTO normally does not issue a patent to a prevailing applicant until after the interference (including court review of the BPAI's decision) is concluded. See Dunner et al., Court of Appeals for the Federal Circuit: Practice & Procedures § 7.06, "Withholding of Issuance of Patent or Certificate of Registration Pending Federal Circuit Decision."

[19] "The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of [the Bankruptcy Code]." 11 USC 105(a). See, e.g., In re Baldwin-United Corp. Litig., 765 F.2d 343, 348 (2d Cir. 1985) ("The Bankruptcy Court has authority under § 105 broader than the automatic stay provisions of § 362 and may use its equitable powers to assure the orderly conduct of the reorganization proceedings."); and SMF Realty Co. v. Consolini, 903 F. Supp. 656, 662 (S.D.N.Y. 1995) ("When courts act to extend the automatic stay to a non-debtor, they do so by means of their authority under Section 105(a) of the Bankruptcy Code …. Thus, in order to achieve the Bankruptcy Code's goals of fair and orderly resolution of claims against the bankrupt estate, courts may enjoin a suit against a non-debtor defendant if it would offer a plaintiff the means to make an "end run" around the protection provided by the Code to the debtor.")

[20] Id.

[21] In re Penn Terra Ltd., 24 BR 427, 433 (W.D. Pa. 1982) ("where government regulatory proceedings threaten assets of the debtor's estate, the Court can, in its discretion, impose a stay.").

[22] Or, at least, concerning how the PTO applies 11 USC 362(a) -- since we suspect that the PTO has no special expertise in bankruptcy law.

[23] A petition to the CAPJ under 37 CFR 41.3 would not be appropriate since 37 CFR

41.3(b)(2) indicates that the CAPJ has no jurisdiction to decide petitions concerning "procedural issues" in "pending contested cases."

[24] See Morris v. Diamond, 208 USPQ 202, 204-205 (CCPA 1980) (Rich, J.) (holding writs of mandamus to review decisions by APJs (then Examiners-in-Chief) are appropriate in extraordinary circumstances when no meaningful alternatives are available) . The petitioner must prove a clear abuse of discretion when relief is sought from a discretionary action. Either recognizing or failing to recognize a 11 USC 362(a) stay or a 11 USC 105(a) injunction could qualify as a clear abuse of discretion. See generally Gholz, "Extraordinary Writ Jurisdiction of the CCPA in Patent and Trademark Cases," 58 JPTOS 356 (1976).

[25] Whether or not to lift the stay to allow a proceeding to continue is left to the discretion of the bankruptcy court. A variety of factors the bankruptcy court may take into account include: (1) whether relief would result in a partial or complete resolution of the issues; (2) lack of any connection with or interference with the bankruptcy case; (3) whether the other proceeding involves the debtor as a fiduciary; (4) whether a specialized tribunal with the necessary expertise has been established to hear the cause of action; (5) whether the debtor's insurer has assumed full responsibility for defending it; (6) whether the action primarily involves third parties; (7) whether litigation in another forum would prejudice the interests of other creditors; (8) whether the judgment claim arising from the other action is subject to equitable subordination; (9) whether movant's success in the other proceeding would result in a judicial lien avoidable by the debtor; (10) the interests of judicial economy and the expeditious and economical resolution of litigation; (11) whether the parties are ready for trial in the other proceeding; and (12) impact of the stay

on the parties and the balance of harms. In re Sonnax Industries, 907 F.2d 1280, 1286 (2d Cir. 1990).

[26] "On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay … such as by terminating, annulling, modifying, or conditioning such stay … for cause." 11 USC 362(d)(1).

[27] Carway v. Progressive County Mut. Ins., 183 B.R. 769, 775 (S.D. Tex. 1995) (citing A.H. Robins Co. v. Piccinin, 788 F.2d 994, 1001 (4th Cir. 1986)).