



# Toy and Game Licensing

Frederick Cohen and  
Oscar Alcantara

## Termination of Licenses: What Happens to License Rights if a Termination Was Wrongful

Disputes between licensors and licensees happen all the time. Although these disputes can usually be worked out, they are at times unresolvable and the licensor will typically end up seeking to terminate the license. In that case, the licensee loses its right to use and profit from the licensed property.

But what if the licensor was wrong? A licensor might take steps to terminate a license, for example, if it believes that the licensee has failed to make timely royalty payments; that the licensee is not complying with quality thresholds; or that the licensee has failed to meet minimum quantity requirements. If that belief is mistaken, however, and the license is wrongfully terminated, what right does the licensee have to continue enjoying the license? And if the licensee continues to use the license, can the licensor obtain an injunction preventing the post-termination use of the licensed property?

The courts have been inconsistent in the way they address these important issues. In some regions of the federal court system, unless a licensor can prove that its termination of the licensee was a proper termination, the licensor cannot obtain an injunction to stop the post termination use of the license. The Third Circuit, for example, considered the issue in a case involving Jiffy Lube service centers. [*S&R Corp. v. Jiffy Lube International, Inc.*, 968 F.2d 371 (3d Cir. 1992).] In *Jiffy Lube*, the franchisee

asserted that Jiffy Lube, the franchiser, had violated the parties' agreement. The franchisee withheld royalty payments and filed suit against Jiffy Lube for breach of contract. Although Jiffy Lube responded by terminating the franchise agreement for failure to pay, the franchisee continued to operate the service centers under the Jiffy Lube name. Jiffy Lube asked the court for an injunction to stop that use of the Jiffy Lube trademarks. Before deciding whether Jiffy Lube was entitled to an injunction, however, the court required Jiffy Lube to prove that the termination was proper and that the franchisee's use of the trademark was, therefore, unauthorized. If the termination had been wrongful, the franchisee would still have been entitled to use the licensed trademark.

The Eleventh Circuit took a similar view in a lawsuit involving termination of a McDonald's franchise. In that case, McDonald's claimed that the franchisee had failed to meet standards of quality, safety, and cleanliness. [*McDonald's Corp. v. Robertson*, 147 F.3d 1301 (11th Cir. 1998).] The Court held that, in order to obtain an injunction against the holdover franchisee, McDonald's must first prove that it properly terminated the contract, thus making the franchisee's use of the trademarks an unauthorized use. In the absence of a proper termination, McDonald's efforts to obtain an injunction would have failed.

That rule is not uniformly applied by the courts, however. In the Seventh Circuit, the courts have adopted a more licensor-friendly view. In a case involving a soda-bottling license, the owner of a secret formula for a green soft drink

sold the trade secret and the trademark GREEN RIVER in connection with the sale of its business. [*Green River Bottling Co. v. Green River Corp.*, 997 F.2d 359 (7th Cir. 1993).] During a transitionary period, the buyer was licensed to manufacture the soda with syrup supplied by the seller, but the secret formula of the syrup was to be held in escrow until the full purchase price was paid. The buyer allegedly fell behind in its payments, and the licensor terminated the relationship. The licensee then obtained green soda from another source and sold it under the trademark GREEN RIVER. The licensor was able to obtain an injunction against the licensee's continued use of the trademark, despite the licensee's argument that the agreement was wrongfully terminated. The Court held that, if the licensee believed its contract rights had been wrongfully terminated, its remedy was to sue for money damages—not to continue using the trademark.

In a similar case involving the Original Great American Chocolate Chip Cookie Company, the licensor terminated a shopping mall franchise for several alleged breaches, including health violations and failure to pay royalties. [*Original Great American Chocolate Chip Cookie Company, Inc. v. River Valley Cookies, Ltd.*, 970 F.2d 273 (7th Cir. 1992).] The franchisee acquired different batter from another source but continued to use the Cookie Company trademarks, prompting the franchiser to seek an injunction to prevent the franchisee's trademark infringement. The franchisee filed a suit of its own to have its franchise agreement reinstated because the termination was allegedly wrongful. The Court enjoined the franchisee from using the mark, holding that the franchisee's proper remedy for an allegedly wrongful termination would have been a suit for money damages—not a suit for reinstatement of the license, and certainly not the self-



help remedy of continuing to use the trademark to sell infringing product.

Neither of these views is entirely satisfying. If a licensing relationship has so deteriorated that the licensor wants to terminate the agreement, it seems impractical to require the licensor to continue to grant and support a license. At the same time, if the termination is wrongful, it may be unfair to the licensee to terminate the rights it had validly contracted for, depriving it of goodwill that it may have created in the brand.

One way to harmonize these cases is to recognize that the courts were weighing a variety of competing interests, many of which do not readily lend themselves to money damages. For example, in the *Jiffy Lube* and *McDonald's* cases, the franchisees had built goodwill in their businesses. An injunction could have destroyed that value in a way that money damages might never have

fully compensated. Similarly, the franchisers had well-established goodwill in their franchised brands. The court in each case refused to allow either party to obtain leverage over the other without firmly establishing which party was the wrongdoer.

In both the *Green River* and *Original Great American Chocolate Chip Cookie Company* cases, the same analysis was applicable, but with the added factor that the franchisee was no longer selling to the public the product that had come to be associated with the franchiser's trademark. Both of these franchisers attempted to sell a product that was different from what consumers expected. These cases, therefore, presented the court with an additional consideration, which is consumer confusion. In those cases, the court swung the balance in favor of the franchiser, the consumer, and the integrity of the trademark.

Because of these sometime competing interests, there can be great uncertainty in a licensee's continuing rights when a licensing dispute results in termination. A licensor may find that a terminated licensee, in fact, continues to exploit the license. A licensee, on the other hand, that believes it has been wronged by the licensor, may find its rights terminated despite that wrongful conduct. Such uncertainty may underscore the importance of attempting to resolve licensing disputes before they reach a point of no return, leaving the parties with nothing more than complicated termination issues.

---

*Frederick H. Cohen and Oscar L. Alcantara are partners in the Intellectual Property Group of Goldberg, Kohn, Bell, Black, Rosenbloom & Moritz, Ltd. in Chicago, IL. They focus their practice on intellectual property litigation and consulting.*