ACTUAL TEST V. HYPOTHETICAL TEST

Below, where it says IP license, read "executory contract" in the context of *ipso facto*.

If a Debtor cannot assign an IP license without consent of the licensor, can it at least assume the license? That question has led courts to exam
closely the first seven words of Section 365(c): "The trustee may not assume or assign …"

> When the statute says that the trustee may not assume or assign an IP license, does the word "or" really mean "and" too?
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> What happens when a Debtor is only trying to assume an IP license and is not actually trying to assign it? Does the Bankruptcy Co
> language mean that it can neither assume nor assign the license or does it only mean that the Debtor cannot assign the license?
>
> The ***hypothetical test*** reads Section 365(c)(1)'s language as asking whether the Debtor *hypothetically* could assign the license eve
> if the Debtor is only proposing to assume the license.
>
> The ***actual test*** interprets the statute's language as asking only what the Debtor is actually proposing to do

The US Court of Appeals for at least 3 circuits have adopted the hypothetical test: they have all held that Section 365(c)(1) gives most IP licensors (the non-debtor counterparty) a veto right over proposals by a Chapter 11 debtor to assign - and even to assume - IP licenses

> The Ninth Circuit: CA, NV< AZ and a number of other Western states
> The Third Circuit: including DE
> The Fourth Circuit: (VA, WV, MD, NC and SC)

According to Justice Kennedy, one "arguable criticism of the hypothetical approach is that it purchases fidelity to the Bankruptcy Code's text by sacrificing sound bankruptcy policy" in that it may prevent debtors-in-possession from continuing to exercise their rights under non-assignable contracts, such as patent and copyright licenses."

Kennedy further remarked on what he called a "windfall" to non-debtor parties to valuable executory contracts. While outside bankruptcy the non-debtor cannot renege on its agreement, if the debtor files bankruptcy "then the non-debtor obtains the power to reclaim - and resell at the prevailing, potentially higher market rate - the rights it sold to the debtor."

Where the hypothetical test applies as it does in the Ninth Circuit, a non-exclusive trademark license cannot be assumed by a debtor-in-posses
See *In re N.C.P. Marketing Group*, 337 B.R. 230 (D. Nev. 2005).

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