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Glass Half Full for U.S. Creditors in Jaffe v. Samsung Electronics Co.: Fourth Circuit Rules In Favor of U.S. Creditors in Chapter 15 Jurisdictional Dispute

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March 5, 2014 - On December 3, 2013, the Court of Appeals for the Fourth Circuit upheld, in *Jaffe v. Samsung Electronics Co.*, the power, and the duty, of a United States Bankruptcy Court to condition the grant of Bankruptcy Code section 1521(a)(5) relief to a foreign insolvency administrator on conditions sufficient to protect the interests of all interested parties affected by the relief.

Jaffe v. Samsung concerned approximately 4,000 U.S. patents owned by Qimondo AG when it entered insolvency proceedings in 2009. These patents related to various kinds of semiconductor technology, and were subject to numerous cross-license agreements with other semiconductor manufacturers that allowed each cross-licensee to design freely without risk of running afoul of the dense “thicket” of overlapping intellectual property rights. The Fourth Circuit characterized these cross-licenses as, essentially, promises made by Qimondo not to sue the licensors. In exchange, Qimondo received a similar promise. The cross-licensees, who were the appellees (Samsung Electronics Company, Infineon Technologies, IBM, Hynix Semiconductor, Inc. Intel Corporation, Nanya Technology Corporation, and Micron Technology) are among the biggest semiconductor manufacturers in the world.

Michael Jaffe, the German insolvency administrator for Qimondo, successfully petitioned the Bankruptcy Court for the Eastern District of Virginia to recognize the German insolvency proceeding as a “foreign main proceeding” under Chapter 15 of the Bankruptcy Code. Specifically, Jaffe requested that the Bankruptcy Court entrust to him the administration of all of Qimondo’s U.S. assets, principally consisting of the 4,000 U.S. patents. The Bankruptcy Court granted Jaffe’s petition, but conditioned this discretionary relief on Jaffe affording the licensees the same treatment they would have received under Bankruptcy Code section 365(n). Section 365(n) allows the licensee of a

right to intellectual property under a rejected executory contract to elect to retain its rights under the license, just as they existed immediately before the bankruptcy case commenced.

Jaffe, however, sought to cancel unilaterally the cross-licenses, pursuant to section 105 of the German bankruptcy code, in order to relicense them for annual cash payments that would flow to and benefit Qimondo's creditors. The cross-licensees argued that the Bankruptcy Court correctly conditioned Jaffe's power to administer the U.S. assets of Qimondo on the protections in section 365(n), and that enforcing section 365(n) would not make the U.S. patents valueless, since they could still be sold to entities that had not yet licensed them.

The Fourth Circuit held that Chapter 15 requires courts to weigh the interests both of debtors and creditors, and particularly local creditors, when granting discretionary relief to foreign estate administrators under section 1521. This is required both by section 1506, which forbids the application of foreign bankruptcy law when granting comity would be manifestly contrary to the public policy of the United States, and by section 1522 which requires the Bankruptcy Court balance the interests of all interested parties before awarding any section 1521 relief.

In reaching this conclusion, the Fourth Circuit weighed the risk that allowing Jaffe to use German law to override section 365(n) and reject the cross-licenses could destabilize the semiconductor industry leading to decreased innovation, confidence, and competition against the benefits of an improved recovery for Qimondo's other creditors. The court also posited that other licensors might transfer their patents to German entities created only to allow them to reject the licenses in bankruptcy. Although these risks were difficult to quantify, the court determined that the Bankruptcy Court's decision granting the cross-licensees the protection of section 365(n) was a reasonable exercise of its discretion.

Chapter 15 of the Bankruptcy Code strikes an important balance between advancing international comity and providing fair and efficient insolvency proceedings for international businesses and protecting the national interests of the United States. The Fourth Circuit's decision in *Jaffe v. Samsung* shows the result of that balance: the German insolvency administrator was granted control over the U.S. assets of Qimondo, but subject to conditions that protected the public policy of the United States and the interests of Qimondo's American creditors.

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