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Weinstein Bankruptcy Decisions Find Talent Agreement Non-Executory, but Post-Closing Obligations Must be Honored

The Weinstein Company Holdings bankruptcy decisions clarify a buyer's ongoing obligations under contracts purchased in bankruptcy, subject to resolution of appeals.

Executive Summary

In the *In re The Weinstein Company Holdings LLC* (together with its affiliates, TWC) bankruptcy proceeding¹ and the *Lantern Entertainment LLC v. Bruce Cohen Productions* adversary proceeding², Judge Mary F. Walrath of the US Bankruptcy Court for the District of Delaware issued two related and important decisions. Ruling on a motion for summary judgment in a “test case” adversary proceeding initiated by Lantern Entertainment LLC (Lantern), the buyer of TWC’s assets, the court held that a work-for-hire agreement entered into by Bruce Cohen for production services related to the film *Silver Linings Playbook* was not executory for purposes of Bankruptcy Code § 365.³ Instead, the court found the agreement was transferred under Bankruptcy Code § 363. As a result, the court concluded that Lantern was not required to cure defaults (as required by Bankruptcy Code § 365) as a condition to acquiring the rights under the agreement.

At the same time, the court found that the cum onere principle — requiring the assignee of a contract to honor the agreement in total and accept both the obligations and benefits of the contract — applies to contracts sold under Bankruptcy Code § 363 (as well as those assumed and assigned under Bankruptcy Code § 365). As a result, the purchaser is responsible for the post-assignment obligations (e.g., participations) in exchange for enjoying its benefits.⁴ While specific to Mr. Cohen’s production agreement, this ruling has broader significance for talent who participate in the creation of films under work-for-hire agreements that are customary in the industry. The decision is also significant in closely analyzing the executoriness of an agreement, which itself is unusual, and strictly applying the “material breach excusing performance” standard, which applies a high bar for establishing a contract to be executory.

On the other hand, the case leaves certain issues unresolved, including whether Lantern could have acquired the rights to the films without purchasing the related talent agreements, allowing it to avoid both past and future participation obligations under such agreements.

Mr. Cohen and certain other interested parties have appealed the bankruptcy court’s decisions, leaving the ultimate outcome uncertain.⁵

Overview of Bankruptcy Proceedings

Following widespread allegations of sexual harassment and assault perpetrated by Harvey Weinstein, and unsuccessful attempts to structure an out-of-court transaction, TWC entered into an asset purchase agreement with Lantern to sell substantially all of TWC's assets and filed a chapter 11 petition in the US Bankruptcy Court for the District of Delaware on March 19, 2018.

On May 9, 2018, the court approved the sale to Lantern and authorized TWC to consummate the transactions contemplated under the Lantern asset purchase agreement. On July 13, 2018, the sale to Lantern closed. Prior to closing, Lantern's due diligence uncovered substantial unpaid participation liabilities under various talent agreements. While Lantern ultimately agreed to honor post-closing participation obligations,⁶ it denied responsibility for participations arising under such contracts prior to the closing.⁷

Given the similarities between the terms of the talent agreements, Lantern initiated an adversary proceeding against Bruce Cohen, producer of *Silver Linings Playbook*, to serve as a test case. In the adversary proceeding, Lantern sought an order of the court declaring that (i) Cohen's agreement was nonexecutory in nature, and (ii) as a result, Cohen's agreement was properly assigned to Lantern free and clear of any claims arising thereunder pursuant to § 363. The court decided the case pursuant to a summary judgment motion filed by Lantern.⁸

The Decisions

Executory Contract Under § 365

For purposes of Bankruptcy Code § 365, a contract is executory when the obligations of both parties to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing performance of the other.⁹ The determination of what constitutes a material breach is determined by applicable state law, and is a question of law to be determined by the judge.¹⁰ New York law governed the Cohen agreement.¹¹

Applying the US Court of Appeals for the Third Circuit's interpretation of New York law in *In re Exide Technologies*,¹² Lantern argued that a material breach under New York law is a breach that occurs prior to the rendering of substantial performance and is so substantial as to defeat the purpose of the entire transaction. The Third Circuit in *Exide* first determined whether the agreement contained at least one obligation for both parties that would constitute a material breach under New York law if not performed, then utilized a balancing test that takes into account "the ratio of the performance already rendered to that unperformed."¹³ The court agreed that this was the proper test to be applied to the Cohen agreement.¹⁴

Agreeing with Lantern's argument, the court found that the principal purpose of the agreement was the production of the film, which the court interpreted to mean that all material obligations of the parties began and ended with the production of the film.¹⁵ The court rejected Cohen's arguments that the agreement had the broader purpose of enabling the studio to market, distribute, and generally exploit the film after the film was made, and that the agreement was executory because it contained several ongoing obligations related to this purpose. Accordingly, the court found that the following ongoing obligations were insufficient to render the contract executory:

- An agreement to refrain from seeking to enjoin the distribution of the film
- A warranty that the work was original
- Mutual indemnification obligations

- Cohen's approval rights over the use of Cohen's name and likeness
- A right of first refusal and opportunity

This decision is significant, in part, because courts have looked to similar provisions in finding agreements to be executory in other contexts.¹⁶ Further, the court's reasoning suggests it would likely have reached the opposite conclusion in the context of a work-for-hire agreement related to an unreleased film. In fact, Lantern partially addressed this in its briefing, stating that "[t]he vast majority (if not all) of the use of Cohen's likeness and approval thereof in connection with promotional material has long passed. Even assuming the Agreement could have been deemed executory due to the inclusion of this provision in the days and weeks following the release of the Picture, the passage of time has virtually eliminated any potential obligation associated with this provision."¹⁷

§ 363 Sale

After finding that the Cohen agreement was not executory, the court determined that the Cohen production agreement was an asset of the bankruptcy estate that could be transferred to Lantern pursuant to Bankruptcy Code § 363.¹⁸

The court went on to elucidate the distinction between sales of non-executory contracts under Bankruptcy Code § 363, and assumption and assignment of executory contracts under Bankruptcy Code § 365. The court explained that assumption and assignment under Bankruptcy Code § 365 requires cure of pre-sale defaults whereas sale of such contracts under Bankruptcy Code § 363 does not. However, the buyer is responsible for post-closing obligations in *both* instances under the cum onere principle, which prevents an assignee from avoiding obligations that are an integral part of an assumed agreement.¹⁹ The court did not elaborate on the precise contractual burdens that would survive the transfer, but noted in its order that Lantern is required to "comply with all post-closing obligations arising thereunder, including, but not limited to its payment obligations."²⁰

Conclusion

The key takeaway from this decision is that remaining ongoing obligations in work-for-hire and potentially other agreements that are substantially performed (at least by one side) are unlikely to be considered executory. Nevertheless, industry talent whose agreements are acquired by the buyer will be entitled to have their post-sale participations and other rights honored by the buyer.

The decision is significant in providing clarity on a buyer's ongoing obligations under non-executory contracts purchased in Bankruptcy Code § 363 asset sales. Further, it marks a strict application of the legal standard for determining whether a contract is executory, rejecting certain ongoing obligations — such as covenants not to sue, indemnities, and the like — that courts have relied on in other contexts to find contracts to be executory.

However, the case leaves open a number of questions — principal among them, whether Lantern's intellectual property rights in the films it acquired derive from the talent agreements or whether the talent agreements are severable from Lantern's rights to own and exploit the underlying film.²¹ As part of the sale transaction, Lantern agreed to acquire the talent agreements, as well as the obligation to pay post-closing participations under such agreements. As such, the court did not need to decide this issue and, more broadly, clarified that its rulings did not operate to "quiet title," thereby leaving open one significant issue for future resolution.²²

As noted above, the decision has been appealed to the United States District Court for the District of Delaware, so the ultimate fate of the decision is yet to be determined. Stay tuned.

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Endnotes

- ¹ *In re The Weinstein Company Holdings LLC*, Case No 18-10601 (Bankr. D. Del. 2018).
- ² *Lantern Entertainment LLC v. Bruce Cohen Productions*, (*In re The Weinstein Company Holdings LLC*), Adv. Proc. No. 18-50924, (Bankr. D. Del. 2019).
- ³ References to the Bankruptcy Code are to 11 U.S.C. §101, *et seq.*
- ⁴ See *Order (I) Granting Lantern Entertainment LLC's Motion for Summary Judgment; (II) Denying Motion to Strike of Contract Counterparties; (III) Denying in Part, and Granting in Part, Joint Motion of SLP Contract Counterparties' to Clarify Sale Order; and (IV) Denying in Part, and Granting in Part, Contract Counterparties' Motion for Order Confirming that Counterparties' Agreements Have Been Designated by Lantern for Assumption and Assignment, Including Joinder of Committee, Lantern Entertainment LLC v. Bruce Cohen Productions*, Adv. Proc. No. 18-50924 (Bankr. D. Del. Jan. 23, 2019), ECF No. 50.
- ⁵ See *Notice of Appeal, Lantern Entertainment LLC v. Bruce Cohen Productions*, Adv. Proc. No. 18-50924 (Bankr. D. Del. Feb. 6, 2019), ECF No. 52; see also *Notice of Appeal, In re The Weinstein Company Holdings LLC*, Case No. 18-10601 (Bankr. D. Del. Feb. 5, 2019), ECF No. 2065.
- ⁶ See *Order Approving Amendments to Asset Purchase Agreement Entered Into By and Between the Debtors and Lantern Entertainment LLC.*, *In re The Weinstein Company Holdings LLC*, Case No. 18-10601 (Bankr. D. Del. July 11, 2018), ECF No. 1220.
- ⁷ *Id.* TWC also filed a statement giving notice that certain contracts, including the talent agreements, were not executory contracts and would be transferred to Lantern as part of the sale without payment of cure amounts, prompting objections from various talent agreement counterparties. See *Debtors' Statement Regarding Contracts to be Transferred Pursuant to the Asset Purchase Agreement with Lantern Entertainment LLC, In re The Weinstein Company Holdings LLC*, Case No 18-10601 (Bankr. D. Del. June 08, 2018), ECF No. 1003; the contracts listed on this statement were included on TWC's final list of contracts to be assumed. In a hearing immediately preceding the summary judgment ruling, Judge Walrath made clear that, if such contracts were determined to be executory, then Lantern would have no ability to later designate the contracts as excluded contracts and would be required to assume and assign the contracts (even though Lantern tried to reserve the right to exclude the contracts to the extent it disagreed with cure amounts later determined). See Transcript of Jan. 14, 2019 Hearing at 40:21-25, *Lantern Entertainment LLC v. Bruce Cohen Productions*, Adv. Proc. No. 18-50924 (Bankr. D. Del. Jan. 18, 2019), ECF No. 2005.
- ⁸ *Complaint for Declaratory Judgment Against Bruce Cohen Productions and Bruce Cohen, In re The Weinstein Company Holdings LLC*, Case No. 18-10601 (Bankr. D. Del. Oct. 17, 2018), ECF No. 1609.
- ⁹ *Enter. Energy Corp. v. United States ex. rel. I.R.S.*, (*In re Columbia Gas Sys. Inc.*), 50 F.3d 233, 239 (3d Cir. 1995); see also *In re Exide Techs.*, 607 F.3d 957, 962 (3d Cir. 2010).
- ¹⁰ *In re Exide Techs.*, 607 F.3d at 962.
- ¹¹ The Cohen agreement's choice-of-law provision stated that New York law applied.
- ¹² *In re Exide Techs.*, 607 F.3d at 962-963.
- ¹³ *Id.* at 962.
- ¹⁴ Transcript of Jan. 14, 2019 Hearing at 133:19-22, *Lantern Entertainment LLC v. Bruce Cohen Productions*, Adv. Proc. No. 18-50924 (Bankr. D. Del. Jan. 18, 2019), ECF No. 44.
- ¹⁵ *Id.* at 134:18-135:15, citing to *Otto Preminger Films, Ltd. v. Qintex Entm't, Inc.*, (*In re Qintex Entertainment, Inc.*), 950 F.2d 1492 (9th Cir. 1991) (holding that television movie contracts entered into with an actor and his agent were not executory because the parties had substantially completed their duties under the contracts at the time of the bankruptcy filing where the actor had finished acting for the television movie contracts prepetition, and concluding that the remaining obligations related to future royalty obligations, promises from both parties not to sell any production rights to third parties, mutual indemnification obligations, and a grant of exclusive rights to use and license the actor's name and likeness in connection with the films were insufficient to render the contract executory); *In re Stein and Day, Inc.*, 81 B.R. 263 (Bankr. S.D.N.Y. 1988) (holding that two book publication contracts were not executory where the books had already been published at the time of bankruptcy, even though the contracts had ongoing rights and obligations, including indemnification by the author for any breach of warranties as to ownership and non-infringement, and the publisher's option to publish the author's next book on terms to be arranged). In contrast, the *Qintex* court held that an unrelated agreement to colorize and subdistribute colorized versions of the movies was executory where the studio had only colorized half of the films because colorization of all of the films was an essential term of the contract.
- ¹⁶ For instance, courts have found intellectual property licenses to be executory based on similar provisions, although such ongoing obligations may be more fundamental to the agreement in that context. See, e.g., *In re Golden Books Family Entm't, Inc.*, 269 B.R. 311, 314 (Bankr. D. Del. 2001) (holding that a license was executory where each party had material duty of "refraining from suing the other for infringement of any of the [intellectual property] covered by the license.").

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- ¹⁷ Memorandum of Law in Support of Plaintiff's Motion for Summary Judgment to Determine the Nonexecutory Nature of a Contract at 17, *Lantern Entertainment LLC v. Bruce Cohen Productions*, Adv. Pro. No. 18-50924 (Bankr. D. Del. Oct. 18, 2018), ECF No. 7.
- ¹⁸ Whether or not the Cohen agreement was an asset of TWC's bankruptcy estate had to be addressed because the signatory to the agreement was SLP Films, Inc., a non-debtor. Cohen argued in his briefing that Lantern had not proved TWC's ownership of the agreement. See *Answering Brief of Defendants Bruce Cohen Production and Bruce Cohen in Support of Opposition to Plaintiff's Motion for Summary Judgment* at 11-14, *Lantern Entertainment LLC v. Bruce Cohen Productions*, Adv. Proc. No. 18-50924 (Bankr. D. Del. Nov. 11, 2018), ECF No. 10.
- ¹⁹ See Transcript of Jan. 14, 2019 Hearing at 121:5-18, *Lantern Entertainment LLC v. Bruce Cohen Productions*, Adv. Proc. No. 18-50924, (Bankr. D. Del. Jan. 18, 2019), ECF No. 44. The court reasoned that the *cum onere* principle applies to both sales under Bankruptcy Code § 363, as well as assumption and assignment under § 365, citing the Delaware bankruptcy court's opinion in *DB Structured Prods. v. Am. Home Mortg. Holdings, Inc.* (*In re American Home Mortgage Holdings, Inc.*), 402 B.R. 87, 98 (Bankr. D. Del. 2009) ("[T]he *cum onere* principle applies equally to the transfer of rights and obligations under a non-executory contract pursuant to §363 of the Bankruptcy Code as to the assumption and assignment of contracts and leases pursuant to § 365.") and the Third Circuit's opinions in *Folger Adam Sec., Inc. v. DeMatteis/MacGregor, JV*, 209 F.3d 252, 264 (3d Cir. 2000) and *University Medical Center v. Sullivan*, (*In re University Medical Center*), 973 F.2d 1065, 1081 (3d Cir. 1992).
- ²⁰ See *Order (I) Granting Lantern Entertainment LLC's Motion for Summary Judgment; (II) Denying Motion to Strike of Contract Counterparties; (III) Denying in Part, and Granting in Part, Joint Motion of SLP Contract Counterparties' to Clarify Sale Order; and (IV) Denying in Part, and Granting in Part, Contract Counterparties' Motion for Order Confirming that Counterparties' Agreements Have Been Designated by Lantern for Assumption and Assignment, Including Joinder of Committee, Lantern Entertainment LLC v. Bruce Cohen Productions*, Adv. Proc. No. 18-50924 (Bankr. D. Del. Jan. 23, 2019), ECF No. 50.
- ²¹ Lantern argued that individual performers do not retain copyright protection in their performance, even if a work-for-hire agreement is not executed. As such, Mr. Cohen would not have any rights in the underlying copyright or ability to disrupt exploitation of the film under applicable copyright law, irrespective of any work-for-hire agreement. See *Omnibus Objection of Lantern Entertainment LLC to (I) Supplemental Objection and Joint Motion of SLP Contract Counterparties to Clarify Sale Order; (II) Motion of Executory Contract Counterparties For Order Confirming That Counterparties' Agreements Have Been Designated by Lantern for Assumption and Assignment; and (III) The Official Committee of Unsecured Creditors' (A) Objection to Supplemental Notice of Filing of List of Assumed Contracts Pursuant to Sale Order and (B) Joinder to the Motion of Executory Contract Counterparties for Order Confirming That Counterparties' Agreements Have Been Designated by Lantern for Assumption and Assignment* at 12-18, *Lantern Entertainment LLC v. Bruce Cohen Productions*, Adv. Proc. No. 18-50924, (Bankr. D. Del. Jan. 07, 2019), ECF No. 25. In support, Lantern cited *Garcia v. Google, Inc.*, 786 F.3d 733 (9th Cir. 2015) (holding that an actress did not have a copyright interest in her five-second acting performance in a film trailer) and *16 Casa Duse, LLC v. Merkin*, 791 F.3d 247 (2d Cir. 2015) (holding that a film director did not have copyright interests in raw film footage or his directorial contributions to the finished film, notwithstanding the absence of a work-for-hire agreement).
- ²² Transcript of July 11, 2018 Hearing at 52:19-53:6, *In re The Weinstein Company Holdings LLC*, Case No. 18-10601 (Bankr. D. Del. July 12, 2018), ECF No. 1232 (noting that "if Lantern is taking the assets it's buying and assuming the risk associated with those assets. So, if there's a risk they buy something that . . . violates the contracts that they bought . . . without taking on other liabilities under some sort of other contract and there's a state law reason to proceed against Lantern they're not getting a release here.").