

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF DELAWARE

In re)	
)	
DISCOVERY ZONE INC., et al.,)	
)	Civil Action No. 03-1034-KAJ
Debtors.)	
_____)	
MONTAGUE S. CLAYBROOK,)	
CHAPTER 7 TRUSTEE OF DISCOVERY)	
ZONE IN., DZ PARTY INC., DISCOVERY)	
ZONE (PUERTO RICO) INC., and)	
DISCOVERY ZONE LICENSING INC.,)	Bankruptcy Case No. 99-941 (PJW)
)	Adv. Proc. No. 01-1491 (PJW)
Appellant,)	
)	
v.)	
)	
PIZZA HUT INC.,)	
)	
Defendant.)	

MEMORANDUM ORDER

Presently before the Court is an appeal by Montague S. Claybrook, Chapter 7 Trustee of Discovery Zone, Inc. (the "Trustee"), from the October 3, 2003 Order of the Bankruptcy Court (the "Order") granting Summary Judgment in Adversary No. 01-1491 for Pizza Hut, Inc. ("PHI"). For the reasons that follow, the Order is affirmed.

I. Background

The issue before the Bankruptcy Court is whether payments made by Discovery Zone, Inc., et al. ("Debtor") to PHI during the Preference Period are protected under 11 U.S.C. § 547(c)(4).

On April 30, 1997 Debtor and PHI entered into a license agreement (the "Agreement"). (Docket Item ["D.I."] 2, Ex. A.) The Agreement authorized the Debtor to use PHI's trademarks in connection with food products prepared according to PHI's

propriety recipe and sold at Debtor's locations. (*Id.* at 4.) In return for the use of the PHI's trademarks, Debtor agreed to pay PHI a monthly license fee. (*Id.* at 10.)

On February 11 and February 26, 1999 Debtor payed to PHI license fees in the amounts of \$55,696.21 and \$109,139.91, respectively. (D.I. 2, Attachment 7 at 2-3.) These payments were made during the Preference Period. (*Id.* at 3.)

On April 20, 1999 the Debtor filed a voluntary petition for relief under Chapter 11 of Title 11 of the United States Code, 11 U.S.C. § § 101 *et. seq.*¹ (*Id.* at 3.) On May 23, 2000 the case was converted to a Chapter 7 and a Trustee was appointed. (*Id.* at 3.)

The parties entered a stipulation order on March 15, 2000, stipulating that for the months of March and the pre-petition part of April 1999, the Debtor owed PHI approximately \$164,800 for unpaid license fees. (D.I. 2, Att. 6 at 6.)

During the liquidation the Trustee attempted to avoid and recover the \$164,836.12 paid by Debtor to PHI during the Preference Period. (D.I. 2, Att. 7 at 4.) On October 3, 2003, the Bankruptcy Court granted PHI's motion for summary judgment, holding that the "continued use of its [PHI's] trademarks, products and proprietary recipes without paying the monthly license fees under the Agreement constitutes new value." (*Id.* at 9.)

II. Standard of Review

This court has jurisdiction over appeals from the Bankruptcy Court pursuant to 28 U.S.C. § 158 (a). On appeal, the court applies a clearly erroneous standard to the Bankruptcy Court's findings of fact and a plenary standard to its legal conclusions. See

¹Hereinafter, unless otherwise indicated, all references to "§ ____" are to a section of the Bankruptcy Code as codified at 11 U.S.C. § 101 *et. seq.*

Am. Flint Glass Workers Union v. Anchor Resolution Corp., 197 F.3d 76, 80 (3d Cir. 1999). When reviewing mixed questions of law and fact, the court will accept the Bankruptcy Court's finding of "historical or narrative facts unless clearly erroneous, but [will] exercise plenary review of the trial court's choice and interpretation of legal precepts and its application of those precepts to the historical facts." *Mellon Bank, N.A. v. Metro Communications, Inc.*, 945 F.2d 635, 642 (3d Cir. 1991) (internal quotes omitted).

III. Discussion

The facts of this case are not in dispute, there appears, however, to be one legal question in dispute and that is what constitutes "new value" under § 547(c)(4).

The Third Circuit has held that there are three requirements under § 547(c)(4) to find that a transfer is excepted from § 547(b):

[f]irst, the creditor must have received a transfer that is otherwise voidable as a preference under § 547(b). Second, after receiving the preferential transfer, the preferred creditor must advance 'new value' to the debtor on an unsecured basis. Third, the debtor must not have fully compensated the creditor for the 'new value' as of the date that it filed its bankruptcy petition.

In re New York City Shoes, 880 F.2d 679, 680 (3d Cir. 1989). Section 547 of Chapter

11 United States Code defines new value is defined as:

money or money's worth in goods, services, or new credit, or release by a transferee of property previously transferred to such transferee in a transaction that is neither void nor voidable by the debtor or the trustee under any applicable law, including proceeds of such property, but does not include an obligation substituted for an existing obligation.

11 U.S.C.A. § 547(a)(2) (West Supp. 1989). The United States Court of Appeal for the Third Circuit has held that “this definition of new value was intended, as construed from the House and Senate reports, to codify the usual rules of consideration.” *In re Spada*, 903 F.2d 971, 976 (3d Cir. 1990) (internal quotations omitted).

Other courts have found that the continued use of a creditor's property despite failing to make scheduled payments constitutes new value. *See, Southern Tech. College v. Hood*, 89 F.3d 1381 (8th Cir. 1996) (holding that continued use of rental property is new value) *Ross v. Philadelphia Hous. Auth. (In re Ross)*, 1997 Bankr. LEXIS 2352 (Bankr. D. Pa. 1997) (holding that when a creditor allows a debtor to remain in dwelling place after debtor failed to pay rent is a conveyance of new value). *Lease-A-Fleet, Inc. v. Morse Operations, Inc.*, 141 B.R. 853 (Bankr. D. Pa. 1992) (holding that continued use and supply of leased vehicles without payment constituted new value).

In the instant case, it is not contested that the transfer was otherwise voidable as a preference under § 547(b). It is also not contested that Debtor fully compensated the creditor for the alleged 'new value' as of the date that it filed its bankruptcy petition. The remaining question is whether the continued use of PHI's trademarks constituted a transfer of new value.

Under Third Circuit law, trademarks may be considered new value under § 547(b). *See, In re Spada*, 903 F.2d at 976. The remaining question, then, is whether Debtor received new value after PHI received the preferential transfer.

As Debtor was contractually bound to pay monthly royalty fees to PHI (D.I. 2, Ex. A at 10), the continued use of PHI's property, namely their trademarks, without

remuneration, constituted a transfer of new value. See, e.g., *In re Ross*, 1997 Bankr. LEXIS 2352. Additionally, as this use occurred after the preferential transfer (D.I. 2, Att. 6 at 2-5), all of the Third Circuit's requirements under *In re New York City Shoes* are met. 880 F.2d at 680. Consequently, the creditor is permitted to setoff the preferential transfer in an amount equal to the new value, which here is approximately one hundred percent of the transfer.

The Trustee offers one case for the proposition that intellectual property, and more specifically non-exclusive licenses, should be treated differently than tangible property. See, *Steege v. AT & T (In re Superior Toy & Mfg. Co.)*, 183 B.R. 826 (Bankr. D. Ill. 1995). This case, however, is easily distinguished from the present one. In *In re Superior Toy & Mfg. Co.*, the questioned new value was "packaging design, finished art, and catalog design." *Id.* at 830. Unlike the present case, the property at issue in that case was sold and not leased. *Id.* at 830. Further, the transfer of that property occurred before the preferential payment. *Id.* at 830. Therefore, *In re Superior Toy & Mfg. Co.* is distinguished from the present case and not applicable to this court's opinion. *Id.*

In sum, the court agrees with the conclusions reached by the Bankruptcy Court in its October 3, 2003 Opinion and Order, as well its rationale in support of those conclusions.

IV. Conclusion

Therefore, IT IS HEREBY ORDERED that the October 3, 2003 Order of the Bankruptcy Court in the captioned Adversary Proceeding is AFFIRMED.

Kent A. Jordan
UNITED STATES DISTRICT JUDGE

DATE: October 5, 2004
Wilmington, Delaware