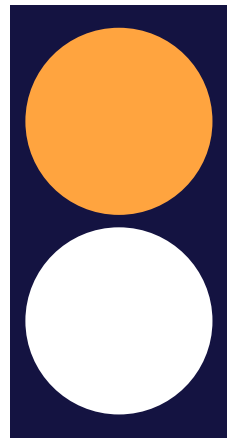


COMMERCIAL LAW

ARTICLE: THE IMPORTANCE OF INTANGIBLE ASSETS WHEN SELLING A BUSINESS

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Introduction

In most business sales, tangible assets such as stock, furniture and equipment are easy to identify, value and justify. It is usually the intangible assets such as tradeable intellectual property, goodwill and know-how that could make or break a business. Not only is it hard to accurately value, but it can also be significantly subjective. What a seller thinks has significant value can be of little value to a buyer and vice versa



Intangible Assets

1. Tradeable Intellectual Property

Tradeable intellectual property can be sold separately from the business and does not necessarily indicate that the business has ownership over them. Four types of tradeable intellectual property can be registered with IP Australia: trademarks, patents, design rights and plant breeder's rights. The Attorney-General's Department manages copyright in Australia, which is free and automatic.

<p>(a) Trademarks</p>	<p>Trademarks protect logos, phrases, words, shapes, letters, colours, sounds, smells, pictures, movements, aspects of packaging or any combination of these. They protect a business' brand and help customers identify the business' products and services in the market. Having a strong trademark can also add significant value to a good or service.</p> <p>Trademarks are exclusively owned. Separate from the business, they can be sold, transferred, commercialised through licensing agreements, or destroyed. It isn't necessary to sell the trademark together with the business, nor is it impossible for a trademark licence to be terminated upon the sale of a business. Potential buyers must identify the owner of the trademark and ensure that the trademark is purchased together with the business. The last thing a buyer wants is to buy a business without owning the core asset that represents that business.</p>
<p>(b) Patents</p>	<p>A patent protects any device, substance, method or process that is new, inventive and useful. The inventor "must use his knowledge and ingenuity to produce a new and useful thing or result, or a new method of producing an old thing or result."²</p> <p>Having a patent will grant the right to exclude others from using, making or selling that protected invention. It also becomes an asset for businesses to commercialise through patent licensing agreements. Like other intellectual property, the business does not have to be the patent owner because it uses, creates or sells that protected invention.</p> <p>It must be noted that a patent rarely protects a 'result'. A poorly written contract could allow the inventor to start another business with a better device, substance, method or process that yields similar results.</p> <p>Business buyers should assess whether the business owns the patent or has a patent licensing agreement. The latter requires an extensive review of the licensing agreement to capture any risks of the agreement being terminated by the patent holder upon the change of control of the business.</p>
<p>(c) Design Rights</p>	<p>A design right aims to protect the "overall appearance of the product resulting from one or more visual features of the product," such as its shape, configuration, pattern or a combination of visual elements. Now, design must have a physical and tangible form, be manufactured or handmade and be produced commercially to be protected. IP Australia is considering extending the design rights to protect virtual designs such as screen displays, screen icons and graphical user interfaces, as afforded by many other jurisdictions worldwide such as the United States, the European Union and its parties, Japan, Korea and China.</p>

	In Australia, design rights last up to 10 years maximum (five years plus five years renewal). Once the design rights expire, businesses can still use the design commercially, but it will no longer be exclusive, nor will there be an option to commercialise it. Buying a business solely for its design rights
(d) Plant Breeder's Rights	Plant breeder's rights give exclusive commercial rights over a new plant variety, including trees, flowers, shrubs, vines, algae and fungi. To be afforded protection, the plant must be a product of a selective breeding process, new or recently exploited, and distinct, uniform and stable. IP Australia grants protection for up to 20 years for most plant species and up to 25 years for trees and certain vines.

2. Goodwill

Goodwill lies at the heart of every business sale. It is sometimes considered as the premium price to pay on top of the other assets. It includes a range of intangible assets such as its growth potential, location, reputation, customer loyalty, branding, know-how, trade secrets and staff satisfaction.

According to the Australian Accounting Standard ASRB 1013:

"Goodwill which is purchased by the company shall be measured as the excess of the cost of acquisition incurred by the company over the fair value of the identifiable net assets acquired."

Unlike tradable intellectual properties, goodwill cannot be sold separately from the business, and poor business management can significantly decrease or destroy the value of the goodwill. Buyers should also consider their ability to manage the business and whether they can increase or keep the value of the goodwill.

Buyers should also conduct extensive due diligence on contracts such as supply, manufacturing, distribution, and employee agreements, as they often attach to a business's goodwill. For example, an exclusive supply agreement is valuable to any business and likely accounted for in the goodwill calculation. Buyers should review all agreements and consider the following:

1. Whether there is any change in control provisions that give the other party to the agreement the ability to terminate the agreement because the business's owners have changed;
2. The expiry of any key agreements; and
3. The terms and conditions of the agreements, including any restrictions or obligations.

The last thing a new business owner wants is to pay a premium for a business only to have their supply agreement terminated by the supplier.

Summary

Buying or selling a business without assessing important intangible assets can cost you dearly. Contact Ezra Legal to ensure that your business sale transaction includes the necessary assets you need to ensure the success of your business sale or acquisition.

Contact Information

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