

in brief from
RAINEY COLLINS
LAWYERS
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WELCOME

to the spring edition of Rainey Collins In Brief Commercial Issues newsletter.

In this edition we focus on buying or selling a business, restraint of trade, intellectual property for business people, and getting tenants to pay rent promptly as well as useful and helpful articles and business seminars.

These articles and others are available on our "new look" website www.raineycollins.co.nz. You can download them or send them to others.

I trust you find the information of interest and use.

James Johnston
Chairman



JAMES JOHNSTON

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Buying Or Selling A Business? 6 Key Tips

Businesses ranging from corner dairies to big corporates change hands every day in New Zealand. Each transaction involves a number of contractual obligations between the parties. There are also third parties involved who are affected (including employees and landlords).

In a recent situation a Purchaser "inherited" two employees from the Vendor. The Vendor informed the Purchaser that they were "casuals". The contract did not deal with employee entitlements. Imagine the Purchaser's horror when after deciding to make the two 'casuals' redundant it transpired that they had worked in the business for many years and had to be paid significant redundancy and holiday pay.

Good contract drafting would have avoided this problem by properly dealing with the employees and their entitlements. Fintan Devine examines six key tips relating to the sale and purchase of businesses with a particular focus on the contractual obligations of the parties.

Tip #1 Consider How The Transaction Is To Be Structured

This is important because it has many implications in terms of obligations that the Purchaser takes over from the Vendor. Broadly speaking, in the ways business sales are conducted. The most common (especially for small to medium businesses) is the sale of assets from one party to another. In this type of transaction, the Purchaser starts more or less with a "clean sheet".

The alternative, where the business is operated by a company, is the sale and purchase of the shares in the company. In that type of transaction

the Purchaser may take over the debtors and creditors of the business. The Purchaser can also inherit other "baggage" including tax liabilities or benefits and employer obligations.

Tip #2 Get Advice On The Whole Contract

In our many years of experience we have found that going through the detail of the contract helps focus on the issues and ensures important details are not overlooked.

Tip #3 Due Diligence – The Importance Of Preparation

Most transactions will include due diligence by the Purchaser either before an agreement is reached or as a condition of the Purchaser being bound to complete an agreement. It is a good idea to compile a list of the documentation to be provided, before due diligence is undertaken.

At Rainey Collins we are able to provide Purchasers and Vendors with helpful checklists to assist with this. Vendors are often wary of due diligence conditions in agreements because they can provide the Purchaser with an "out" if the Purchaser has a change of heart.

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FINTAN DEVINE

Restraint Of Trade

You have just taken the exciting step of purchasing a well-established business – what is your worst nightmare? It could be the sign that has gone up, not too far away from your premises, advertising the new business that has just been opened up in competition with yours – by the person who sold it to you!!

How can you avoid this scenario?

Usually when you buy a business one of the things you will pay for is the goodwill of the business. For this reason, restraint of trade clauses are common in contracts for sale and purchase. Their purpose is to try to stop the vendor or seller setting up the same type of business to the detriment of the new purchaser. Often the vendor's personal involvement in the business will have created loyalty within its client base and the purchaser will need to establish him or herself in the area without competition from the vendor.

However, care must be taken in defining the terms of any restraint of trade. If they are too broad (e.g. cover too wide a geographical area, or extend for too long a duration) the Court will either decline to enforce them or will modify them to make them more "reasonable".

You should also think about who is bound by the restraint of trade. If you are contracting with a company, you should ensure that all directors and shareholders are bound by the restriction. That can require getting additional covenants from shareholders – separate from the contract to purchase the business.

There are no guarantees when it comes to restraint of trade clauses, but if you have a legitimate interest to protect and a carefully drafted restraint provision then you can rest easy that you have done all you can to protect your new business from unfair competition.



HOLLY DRUMMOND

Buying Or Selling A Business? 6 Key Tips continued

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Defining the extent of the due diligence to be undertaken can remove some of the uncertainty around these conditions.

Tip #4 What About Employees?

Both Vendor and Purchaser need to be especially careful in dealing with employees of the business. Vendors must be aware of their good faith obligations as employers and be able to demonstrate the efforts that have been made to protect the employment of their employees. It is compulsory to have employee protection provisions in all employment agreements and for these to be adhered to during the sale process.

Where a Purchaser takes employees with the business the Purchaser must be prepared in advance of the handover date. Preparation usually includes meeting with the employees and providing them with the proposed form of Employment Agreement and the opportunity to take advice about the Agreement.

Tip #5 What Is For Sale?

It is not unusual for there to be some uncertainty as to the subject matter of the sale. In today's environment, business sales often include intellectual property, licences, software and other assets that are not "bricks and mortar" assets.

Proof of ownership is something that should always be addressed and can sometimes cause headaches.

Tip #6 Leases / Licences

Where the business includes the transfer of a lease or a licence, both parties need to consider the requirement to obtain consents from third parties.

In most cases, the third parties will want to know that the Purchaser is suitable. The person willing to pay the most money may not always be the most suitable from the point of view of the third parties who will be obliged to have a continuing relationship with the Purchaser. Purchasers should also bear in mind that third parties will require information about their background, relevant experience and in some instances referees.

Summary

It is a cliché, but no two transactions are exactly alike. A methodical approach at all stages of the transaction will help ensure that the transition is as seamless and "hassle free" as both Vendor and Purchaser no doubt would like. Advice prior to "signing on the dotted line" is often vital to the success of the deal.



FINTAN DEVINE

Business Seminars

Business seminars on Buying and Selling a Business, Asset Protection, Business Succession, Contracting, and Intellectual Property for Business people are held regularly. See our website www.raineycollins.co.nz or call us on 0800 733 424 for details.

Other Helpful Articles

These articles and many more are available free to download from our website www.raineycollins.co.nz Just click onto the articles icon and choose the area of law you are interested in.



JENNY GRAHAM

Intellectual Property and Your Business ... More Valuable Than You May Think!

Recently, when acting for Robert, a client purchasing an existing business, we came across a business owner David who hadn't thought about intellectual property (IP). This left David trying to sell something that he couldn't prove he owned! Why? Because, as is the case with many businesses, a significant part of the value of David's business was intellectual property but he hadn't thought of it as such. As a result David hadn't taken any steps to protect it and make sure he owned it outright.

In our experience, it is a common mistake. There is a general misconception about IP and what it is. Okay... so what is it?

The element of creativity in IP seems to make many business owners think that they mustn't have any. This is a misconception because IP protects that which is "original" and "distinctive" rather than what is stereotypically "creative". In most cases IP is simply things that are not copies of other things. You may correctly be getting the feeling that the threshold is pretty low! So how is this relevant to your business?

Back to David...

David had built a well-known brand and had excellent Information Technology (IT) systems in place for service delivery. Those two things were integral to the success of the business. We therefore made enquiries for Robert as to the ownership of the branding and the systems. We had expected that the trading name and logo would be trademark protected, given the significant market recognition of the brand. They were not. Likewise we had expected the IT software facilitating the business service delivery to be protected and again it was not.

Trademark Protection

It is common for a company to trade under the mistaken belief that registering their company name and/or domain name prevents other traders from using a similar name. This is not the case. Only trade mark registration can grant exclusive rights

to use a trading name. Therefore, despite its value David could not put a premium price on strong branding (and resulting market position) because he could not "sell" exclusive rights to it.

Our client took those necessary steps immediately after taking over the business. Ironically perhaps, trade mark registration can cost as little as the \$112.50 registration fee. Compare that to the potential cost to your business if you don't protect your brand, both while you are trading and also at the point of sale. We recommend that all business owners at least consider whether or not trade mark protection is suitable for their business, particularly in the context of added value to that business in the event of a sale.

Copyright Protection

It is also common in business to produce things like promotional material, business systems and, of course, retail goods or services. All these things and more are potentially your IP, most likely copyright material, and of significant value to the success of your business. Often, however, you have arranged for others to produce the material for you. Unlike other areas of intellectual property, there is no formal registration process attaching to copyright material, so the best way to protect such material is to put in place contractual arrangements to put ownership beyond doubt. If you don't, you could be left with little say as to who owns what, because copyright law will determine those matters if a dispute arises.

Back to David...again

David, the business owner in our example, had software developed by an IT specialist to enable him to cost-effectively deliver the services his business offered. The computer software was crucial to the success of the business, but the lack of documentation around its creation meant that when David came to sell he couldn't be sure that he owned the software.

This was because the software was a "literary work" under the law and he had not paid for its creation. The IT specialist had been his nephew. Even though David's nephew was unlikely to dispute ownership while his Uncle owned the business (hence the lack of documentation), Robert didn't want to take on the business without documented evidence that the software was owned by the business.

David was fortunate that his nephew was happy to sign an agreement transferring ownership to the business to aid its sale. However, under any other circumstances, this could easily have significantly lowered the value of the business and/ or prevented the sale.

Lessons for you

Be aware that much of what is currently enabling you to be successful in business can include Intellectual Property worth protecting. Don't leave it until the last minute like David to protect it.



KIRSTEN FERGUSON

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It may be as simple as thinking about your business differently in light of what you've just read and taking steps yourself. You may however need to talk to your professional advisor.

Whichever course you take, taking action may well be one of the most beneficial things you do for your business this year!

A trade mark is a unique identifier, commonly referred to as a brand. They can include words, logo, colour, sound, and even smells – and any combination of those things. Broadly speaking, anything that can be graphically represented.

Intellectual Property concerns creations of the mind. In the context of your business it might be a clever

trading name, a smart business system or an ingenious retail product or service. Put simply it is a business asset.

Copyright applies to original works and attaches to the original expression of an idea. It protects the particular manner of expressing an idea or conveying information.

Landlords, Get Your Rent Paid Promptly!

A landlord client of ours recently came to us because tenants in his building were continually paying their rent late. Since the tenants had signed up he had had to follow them up with phone calls and letters each month until they finally got around to paying the rent. If this sounds familiar then read on ...

A new legal process is available to enforce payment of rent by tenants. Previously, when tenants had breached the lease by not paying rent, the landlord could take possession of the premises, sue the tenants, or enter the premises to uplift the tenant's chattels to pay for the rent. These options were not always practical and were difficult to follow through.

Now the landlord can give notice of the breach as soon as the rent is overdue, and ten days after that can cancel the lease. A notice under the new Property Law Act that the Landlord requires the rent to be paid is a quick and relatively easy way of getting tenants to pay outstanding rent. There are specific requirements under the Act as to what the notice must spell out including

exactly how much is owing and how long they have to pay the rent. The landlord must give the tenant not less than ten working days to pay it. Once the period specified in the notice has expired then the landlord is entitled to cancel the lease. A tenant who will happily ignore letters seeking payment may sit up and pay attention if a formal notice under the Act is received that stipulates cancellation if the outstanding rent is not paid.

The notice period (of at least ten days) can start running prior to the rent being in arrears for ten days, so you don't have to wait a whole month until you can do anything about non payment of rent.

Many landlords, like our client, will no doubt find that this new addition to the law surrounding leases will be a helpful tool in ensuring their tenants abide by their agreement under the lease to pay the rent on time. It is better for tenants too!

Now, instead of facing the inconvenience and cost of being locked

out without notice (as could happen before the new Act) they now receive notice of the risk of having their lease cancelled. However, if the tenant still does not pay and the landlord follows through and cancels the lease, the tenant will be liable to the landlord for damages (generally the total losses to the landlord arising from the cancellation of the lease).



CLAIRE COE

Did You Know ...?

On the subject of landlord remedies, the law has also abolished the right of "distrain". The right of distraint allowed the landlord to enter the premises and take the tenant's goods if rent had not been paid. There were strict rules regarding the process the landlord had to follow in using this self help remedy. Many landlords have been tripped up over the years for not carrying out the process correctly. Landlords need to be aware that they no longer have this right.

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