Business rescue and liquidation have consequences for IP

By Bernadette Versfeld

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Intellectual property is often overlooked when a business is compelled to seek business rescue or liquidation, but it may form a valuable asset, requiring decisions to be made on whether to sell it or maintain it.

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In the current economic climate, many businesses will unfortunately find themselves in the unenviable position of having to decide between business rescue and liquidation.

Whatever the decision, it is important for any business rescue practitioner or liquidator to carefully assess the company's intellectual property (IP) assets, which are often overlooked in these proceedings.

First the basics. No business operates without IP. IP describes an umbrella of rights which fall into two categories: registered and unregistered.

The registered IP of a business may include patents for chemical compounds in medicines, trade mark registrations for valuable brands such as Apple, registered designs such as the Coca-Cola bottle or Plant Breeders' Rights which allows agricultural companies to protect plant varieties, e.g. those that grow at a faster rate.

Unregistered IP may include copyright, trade secrets and know-how. It is often more difficult to establish what unregistered IP a business owns, but this exercise must be undertaken as a business may own some very valuable unregistered IP which can be monetised. For example, a business like Coca-Cola owns copyright in the artistic and musical works in its advertising, its recipe is probably one of the most famous and valuable trade secrets in the world, and it owns a tremendous amount of know-how in the operation of its business around the world.

Whether IP is registered or unregistered, businesses have a monopoly over those rights and own a valuable asset which can be commercialised in a number of different ways.

Business rescue

A business rescue practitioner should carefully consider the business's IP and whether it can be restructured to increase revenue or decrease liabilities.

If any IP is not being used by the business and there is no intention of using it in future, the business rescue practitioner can either license it to a third party to generate revenue or have it valued in order to sell it. If the IP is already licensed, there may be restrictions on its further exploitation. If the business is paying license fees for IP which it no longer uses, then the termination of the license should be considered.

An IP portfolio can be extremely large, with many registered rights, resulting in ongoing maintenance costs for the business. Generally, trade marks are renewed every 10 years and patents and designs are renewed annually. If IP is not being utilised, these registrations should possibly be abandoned to reduce the business's liabilities.

Another possibility is collaborating with third parties to resuscitate the IP of a business for purposes of providing the confidence lenders require in order to raise capital for the business.

Liquidation

It is a misconception that IP loses value upon liquidation. IP is critical to the operation of any business, especially if it is technology-based, for example one that relies heavily on software.

Upon liquidation, all property including IP is sold and distributed among creditors with secured, preferred, and concurrent claims, so it is vital for a liquidator to identify and value that IP before it is sold.

IP is often overlooked in a liquidation, which is unfortunate since it can considerably increase creditor returns. We frequently find valuable registered IP remaining in the name of a liquidated business at the Companies and Intellectual Property Office. It is critical to appreciate that after liquidation, it is no longer possible to secure ownership of this IP, so whatever IP the business owns must be investigated and appropriately dealt with, before the liquidation process is finalised. As already observed, if it is still possible to commercialise this IP, the liquidator can have it valued and sold.

We are often asked what happens to an IP license upon liquidation. The rights and obligations of the licensee and the licensor in relation to IP assets are governed by a contractual agreement, whether oral or in writing. Licensor obligations could include the obligation to maintain or develop an IP asset or continue to pay registration expenses to preserve its value. In general, contracts not completed by the insolvent licensor are not terminated or suspended, and the liquidator can choose whether to abide by them or repudiate them. This election must be exercised on the instruction of the creditors of the insolvent estate since the liquidator’s actions must be in the interests of the joint creditors.

The consequence of a liquidator's repudiation is that a licensee cannot claim specific performance, but all other breach remedies remain available. If the licensee refuses to accept the liquidator's repudiation of the agreement, he/she will perform in terms of the agreement and become a concurrent creditor in the insolvent licensor's estate with a claim for damages. If the licensee accepts the liquidator's repudiation of the agreement, all performances rendered by the licensee and the licensor up to that point must be returned to the other (*provided no forfeiture clause exists in the agreement*), and the licensee will have a concurrent claim for any additional damages suffered.

The consequence of a liquidator's election to abide by the contract is that the liquidator steps into the shoes of the insolvent licensor. The licensee will be entitled to receive full performance in terms of the agreement and will be obliged to render full performance in return. The liquidator will be obliged to take over the whole agreement and may not amend any of its terms. The costs of performing under the contract come out of the insolvent licensor's estate. If the insolvent estate has insufficient funds to facilitate performance, creditors with proven claims will need to contribute any shortfall.

IP is a valuable asset for a business. Since no business is immune to the ravages of an economic slowdown, it is very important to understand, long before business rescue or liquidation, how the business's IP assets and licences may be impacted by the event.

ABOUT THE AUTHOR

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