

## Change of Control?

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### What is change of control?

There is no standard definition for “change of control;” however, there are some common transactions in which a change of control may be triggered, including these:

- a sale of all or substantially all of a target company’s assets
- any “merger” of the target company with another company
- the transfer of a certain percentage of the target company’s issued and outstanding shares **from the target company to the acquirer**

Other events may be included in change-of-control definitions such as reorganizations, consolidations or other transactions in which one of the following occurs:

- more than 50% of the board members change
- change in shareholders who have the right to elect more than 50% of the board

A transaction where the acquirer of the stock, assets or rights is an “affiliate” of the target company may be an exclusion from the change-of-control definition.

### Change of control 2.0

The transactions mentioned above are usually covered in change-of-control provisions in agreements between companies. However, there are other events that may trigger a change of control that you as a party to an agreement might want to guard against.

For instance, a company may change suppliers or subcontract with new parties, which may result in a change in the detail, quality or timing of obligations under the agreement, or a competitor may acquire one of your suppliers and you may no longer wish to do business with that supplier.

If the agreement includes a minimum product purchase requirement for a significant period of time, a change-of-control provision may ensure that a party would not have to meet this commitment. Change of control can also be used to deter a competitor from merging with, or another company wanting to acquire your supplier if the purchase volumes represent a significant portion of their business and your termination would significantly affect the worth of the company.

### Change in management = change of control?

For some companies, a change in ownership may not be a concern, but if the agreement is very specific or relates to a novel product or service, it may be difficult to replace/duplicate

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with another company. A company may decide it doesn't want to spend the time or have the inconvenience of having to get to know new management if the other party is acquired or take the risk that the new management will not be a good fit with them or their project team. The new managers may not prioritize the project in the same way once they have assessed the company's assets.

If a company is venture capital funded, it can be important to include a change-of-control provision such that if the funder isn't seeing the desired growth, it has the option of disposal via merger or sale.

## **Know what you need when drafting the change of control provision ...**

A lot of agreements do not allow an assignment; however, this does not cover a change of control. At the end of the day, a company must determine the circumstances under which it would not want to continue the agreement as originally negotiated and drafted. A party may try to ensure that the other party seeks consent to make the change and maintain the agreement, or provide some form of payment as compensation for the change, while retaining the right to terminate the agreement. In addition to termination, a party may seek reimbursement of some investments made pursuant to the agreement due to the fact that the change of control creates a significant threat to its business.

## **... make sure you have enough time to adapt ...**

In a change-of-control provision the period a party has in order to decide what action it wants to take in response to the change of control needs to be long enough for it to plan and implement an alternative strategy if required. Without that time limit, change-of-control clauses are inherently uncertain. If a party wishes to terminate an agreement, it is important for it to avoid taking steps whose effect is to affirm the continuance of the agreement after that party becomes aware of the change of control and within the time limit (if applicable) as it may be held to have waived its rights. If a time limit is included, it is important that the expiration of the time to terminate is recorded in a way that the time limit is not missed.

## **... and cover your back with an adequate termination clause**

Any termination should be without liability, as the party who agrees to a merger is doing that voluntarily and it is under that party's control. If there is an acquisition, from due diligence the acquiring company should know that there is a risk of termination and that the other party could walk away without liability.

It may be, however, that a company is happy with the acquisition or merger (change of control) as it means the other party becomes more skilled in the applicable field, stronger financially or bigger geographically.



A licensee should consider the impact of agreeing to a change-of-control provision or it may reduce the value of the company in the eyes of any potential acquirer. This is especially important for small and medium-size enterprises.