



Third Party Troubles: Group Companies & Affiliates

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Introduction

It has, and continues to be, quite common to include third party rights for group companies into a technology contract. However, one needs to be alive to some of the associated considerations from both a customer and a supplier perspective, to ensure that obligations are only applicable to the extent intended by the respective parties.

Affiliates & Group Companies

From a customer's viewpoint, it is sometimes important to ensure consistency from a group procurement perspective, and to also minimise procurement costs, by including provisions which provide for benefits under the contract to the customer's group companies.

Therefore, concepts of 'affiliates' or 'group companies' are often included by a customer (and sometimes by the supplier, especially where it is looking for subcontracting or assignment rights). However, it is important for both the customer and the supplier, to be clear as to which entities will fall within the scope of these terms.

A 'Group' could be defined by reference to the Companies Act 2006 (the "Act"), by using the terms 'holding company' and 'subsidiary company' as defined in s1159 of the Act. However, as the *Enviroco Ltd-v-Farstad Supply A/S* [2011] decision showed (which resulted in a finding that an entity lost 'subsidiary' status when the shares of the respective company were transferred to a lender in connection with the taking of security), it is important to ensure that the definition is wide enough to cover the respective third parties.

Therefore, it is not just s1159 of the Act which needs to be necessarily used for such purposes. It is possible to use the wider scope provided by s1162 of the Act, which defines 'parent undertakings' and 'subsidiary undertakings' (with s1161 of the Act defining the meaning of an 'undertaking'), or it is possible to define the scope in other ways as is applicable in the specific circumstances (for example through brand or franchise names which entities trade under).

Legal and Business Considerations

Having identified the respective affiliates or group entities, there are consequences which will flow from the contract with regard to rights and obligations in respect of such third parties. Certain of these are considered below:

- **Licensing provisions:** where a supplier is procuring third party licences for a customer which are wide enough for the customer's group use as per the s1159 Companies Act 2006 meaning, then clearly the supplier can not accept licensing obligations which are wider than that. Both a supplier and a customer will therefore, need to be careful with regard to this, to avoid inadvertent intellectual property right infringement of a third party.

- **Liability:** a supplier may wish the contracting customer entity to accept responsibility and liability (and payment obligations) in respect of the customer's third party affiliates or group entities. Where such third party entities are group companies, then either an intra-group arrangement or more informal arrangement may mean that this does not cause an issue, in other circumstances, the customer will need to either: (1) put in place contracts with such third party entities, requiring indemnification with regard to liability arising from the third party entities' obligations; or (2) make a decision to exclude such third parties from the scope of the contract with the supplier.
- **Performance obligations:** From a supplier's perspective, it will be important to ensure that it is not accepting general obligations from a performance or assurance perspective, which it may not be able to perform, because of (by way of examples): practicalities associated with the location of the respective third parties (especially if they are overseas); the local jurisdiction that the respective third parties are subject to; or the different internal infrastructure that the respective third parties are using.
- **Assignment obligations:** Again it is common for a customer to request group or affiliate assignment rights, sometimes with such rights being capable of being exercised without the consent of the supplier. From a supplier's perspective, this could give rise to significant risks and liability, due to for example: some of the factors mentioned above with regard to performance obligations; or the fact that the contract has run smoothly because the supplier has a good working relationship with the customer's team (which may not necessarily be the case with regard to the assignee); or a broad definition for 'affiliates' or 'group companies' could give rise to supplier obligations being owed to new entities which did not fall within the scope of the original definition by virtue of share ownership or control, but which do now fall within the scope of the definition with regard to the assignee; or the contract could be assigned to a financially weak group entity or affiliate who can not perform the payment or liability obligations under the contract.
- **Legal boilerplate:** It is also important to ensure that the legal boilerplate is not overlooked, as it needs to be made clear, that the consent of the respective third parties is not required for contract variations, rescissions, terminations, settlements or waivers.

Final Thoughts

It is important therefore, that definitions of 'group companies' or 'affiliates' are only included in contracts after careful consideration by both the supplier and the customer. From the supplier's perspective in particular, it is vital that the wider performance, liability and assignment obligations owed to such third parties, do not make the original contract with the customer suddenly become more onerous, nor give rise to an adverse impact on the risk profile of the contract.