

## The Importance of Clear Drafting in Outsourcing Arrangements

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Outsourcing arrangements inevitably involve mutual interdependence between the customer and the supplier. The supplier is unable to perform some of the services in accordance with the service level requirements unless the customer performs some obligations, just as the customer may be unable to perform its normal business activities if the supplier fails to deliver the services it is contracted to provide under the outsourcing agreement. A recent decision in the UK courts in relation to an interim injunction offers a timely reminder of the importance of clear drafting in outsourcing agreements.

Disputes between customers and suppliers in outsourcing arrangements rarely reach the courts, at least in the UK, so this decision is interesting in the way in which it shines a light on a customer/supplier outsourcing dispute.

The dispute was between Powergen, a major electricity utility in the UK, and Vertex, a supplier of finance and administration services to Powergen.

The agreement between Vertex and Powergen related to nine different types of service for which there were separate transaction documents. These included services to India, which encompassed the provision of an Indian call centre for Powergen customers, and “stay warm services”, which related to end to end services to be supplied to a particular vulnerable class of Powergen customers. The agreement was originally entered into in 2002 for a ten-year term and at the time had an estimated contract value of £1.1 billion. It was a very large business process outsourcing transaction by UK standards.

It seems that the relationship was not a good one and that a series of renegotiations transpired, the most recent being in May 2005. Shortly after the May 2005 renegotiation disputes occurred over a range of issues. In relation to the “stay warm services,” a dispute surfaced as to whether or not Vertex should be managing the collection of ageing debt. Powergen said it should be doing this and Vertex argued, in effect, that this activity was outside the scope of the services. The way in which Vertex was handling the Powergen personal customer data and, in particular, whether it observed adequate security measures for the purposes of compliance with UK data protection legislation also caused a dispute between the parties.

In relation to the India services, the dispute, in the judge's mind, turned on the extent to which the customer had a contractual remedy in respect of the supplier's alleged failure to meet obligations to deliver the services in accordance with "good industry practice" where there were no specific service level criteria measuring the relevant shortcomings in performance.

Powergen eventually served notice to terminate the outsourcing agreement for material breach. Vertex responded by launching injunction proceedings arguing that Powergen should be enjoined from acting on its notice to terminate the outsourcing agreement and

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that it should be restrained from taking steps that prevented Vertex from fulfilling its obligation under the outsourcing agreement. Vertex argued, as it had to do to obtain an interim injunction, that it would suffer irretrievable and unquantifiable losses if Powergen were not enjoined.

### The Dependencies Argument

The outsourcing agreement contained a fairly standard carve out of liability for Vertex failing to perform its obligations under the agreement where the failure was due to Powergen not fulfilling its obligations. Powergen's obligations were described in quite general terms, including:

- to be responsible for the completeness, legal compliance and timely delivery to Vertex of all necessary pricing, regulatory and other information;
- to provide access to computer hardware and software owned by Powergen;
- to work with Vertex to identify new initiatives to reduce the cost to serve whilst maintaining compliance with any relevant SLA aspiring to perform the services in accordance with the agreed key performance indicators.

Vertex also argued that there was an implied term that Powergen would provide all such co-operation as Vertex required of it for the purposes of the outsourcing agreement.

The judge observed that in the complex relationship being documented in the outsourcing agreement

it is plain that the agreement requires extensive mutual co-operation if it is to work and there is scope for real and genuine disagreement as to what is the nature of the co-operation required by Powergen in order to enable Vertex to properly perform its obligations.

The judge did not think that it was appropriate to grant an injunction, which would have the effect of compelling the parties to work together. He also took the view that the particular

terms of the contract – the dependence on Powergen – were insufficiently defined to indicate to Powergen what exactly was required to not prevent or hinder Vertex from fulfilling its obligations under the outsourcing agreement. The court had to look at these types of obligations as if it would have to enforce them and provide that the party not complying with them would be in contempt of court. The judge was not prepared to impose what he regarded as an intolerable burden on Powergen employees to comply with particular obligations, pending a full trial of the issues that would not take place for months, with the potential sanction of contempt proceedings where it was not at all clear what the individual employees were required to do.

The judgment on this point is an important reminder for parties negotiating an outsourcing agreement to be absolutely clear as to the specific dependence the supplier has on the customer for the performance of the services. Although this was an interim hearing at which the issues between the parties were not argued fully, it is typical of the circumstances in

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which dependencies will be reviewed. By the time the matter gets to a full trial, the issues between the parties as to relative responsibilities are likely to have become completely unbridgeable. If anything, this judgment should be a warning to suppliers to be clear as to the dependencies both at the

overall and individual service level and not to rely on vague general language. The dependence should be aimed at “achieving a result” rather than more general language such as “run the business”. This judgement indicates that the courts, at least in England and Wales, are likely to interpret these dependency carve-outs in favor of the customer who has to perform the obligations and not generally as a shield for the non-performing supplier.

### Lessons for the Draftsman

Outsourcing agreements contain a mass of factual detail that is often technical in nature. At the time outsourcing agreements are being negotiated there is often considerable pressure to sign the deal and leave minutiae to be sorted out by the business people as they implement the agreement. The lessons from the Powergen case are helpful for lawyers seeking to ensure that their clients are properly protected by clear drafting.

While there were some issues around whether the supplier was in breach of its obligations and, specifically, whether it was meeting requirements – imposed on the customer – under the UK data protection legislation, a striking feature of the case is the uncertainty the parties had about central elements of the relationship. First, there was uncertainty about whether the collection of ageing debt was inside or outside the scope of the supplier’s obligations. It is hard to understand why an issue like this would not be a black and white matter.

Second, there was uncertainty about the level of the supplier's obligations. What, exactly, was meant by an obligation to deliver services in accordance with "good industry practice"? This is a commonly used standard in technology services agreements and lawyers should be alert to the possibility that their clients may not be able to measure it and that it therefore amounts to little practical definition of the required quality of service.

Third, there was uncertainty about the nature of the obligations on the customer. When faced with a request to enforce uncertain obligations, the court took the pragmatic decision that the obligations were, in fact, unenforceable.

Lawyers negotiating outsourcing agreements should remind their clients of the practical difficulties down the line if the agreement is weak on definitions of scope and obligations. ♦

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