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## **Legal Voice: Contracting for International Outsourcing**

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International outsourcing occurs where a customer turns over responsibility for a function performed in more than one country. For example, a customer might turn over work being done in the U.S., the U.K. and France to a service provider who would then perform the work in the U.S., the U.K. and France using its related companies in those countries. International outsourcing creates unique legal issues because it generally involves multiple contracting parties (on both sides), legal systems, and specific local legal issues such as labor laws, intellectual property, and data privacy. This article raises some of the issues and questions that are unique to international outsourcing.

### **“International” Not “Offshore”**

It's easy to confuse international outsourcing with offshore outsourcing. Offshore outsourcing occurs when a customer turns over responsibility for a function being performed in one country to a service provider who will perform it in a different country. For example, a customer in the U.S. might turn over application maintenance to a service provider who will perform the work in India. That work would most likely be performed under a contract between the customer's U.S. company and the service provider's U.S. company. In offshore outsourcing, the key issue is moving the work to another country; in international outsourcing, the key issue is coordinating outsourcing efforts where the work is performed in the original country.

### **Coordinating the Parties**

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To execute an international outsourcing successfully, the first step is to decide how the contracting will be done. Contracting can be done in a “core” country under that country’s laws, but with global application. However, that requires a high degree of global coordination. Contracting can also be done simultaneously in various countries, which requires little coordination but loses many of the advantages of a global outsourcing. A third alternative, combining benefits of both the centralized and decentralized approach, is to develop a core contract in a core country, then replicate that agreement, with appropriate localizations, in the other countries.

A key factor in deciding on the contracting approach is the motivation for an international outsourcing transaction. If the motivation is merely to create a larger customer relationship, justifying larger discounts and simplifying relationship management, the decentralized approach works. The extra coordination required for the centralized approach is worth the effort if the motivation is to achieve economies of scale by, for example, replacing help desks in many different countries with a single multi-lingual desk in one jurisdiction or replacing data centers in individual countries with a single integrated data center.

With the contracting approach settled, the parties must develop contracting teams. Obviously, the contracting approach determines how the teams will be organized. In particular, the “one contract” approach requires a great deal of local involvement to make sure that all local issues are considered in the core contract. Each country team should include people with expertise in the outsourced function, finance, operations, law, tax, labor/employment and, of course, outsourcing contracting.

## **Legal Systems**

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Each country has its own legal system. The legal system involves both the set of laws and the way that disputes are resolved. Dispute resolution tends to involve either courts or arbitration.

Arbitration is particularly advantageous in large cross-border transactions. This is because international arbitration provides a reliable way for contracting parties to avoid litigation in the potentially hostile and almost certainly unfamiliar courts in another party's country. Also, a single arbitral award can be enforced in multiple countries. Furthermore, the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, ratified by the majority of the world's governments, makes properly rendered arbitration awards far easier to enforce abroad than comparable court judgments.

Therefore, a prevailing party in an international arbitration can seek out the jurisdiction where a losing party's assets are located, confirm the arbitral award there, and attach those assets as if the award were a local court judgment.

## **Data Protection and Privacy Regulation**

Part of the efficiency in an international outsourcing transaction arises from processing data from one country in another country. In the EU, the Data Privacy Directive restricts transfers of personal data from a country within the EU to a non-EU country. The burden of compliance with the EU Directive remains with the "data controller" - generally the customer and not the outsource provider.

However, in order to comply, the customer usually will need to impose specific obligations on the provider dealing with issues such as security of the personal data. The parties will also have to satisfy themselves that they can find an acceptable route through applicable restrictions on the transfer of personal data to a non-EU country that is necessary for the purpose of the outsource solutions.

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More generally, the customer will be bound by the privacy laws of each of the jurisdictions where it gathers data. As a result, the customer must bind the service provider to adequately protect all data from a country under that country's laws, even if the data is being maintained in another country. This makes it imperative to understand all of the relevant data protection and privacy laws.

## **Labor and Employment Law**

Every country has its own labor and employment laws to protect the rights of employees. For example, U.S. lawyers familiar only with the WARN Act might be surprised by the provisions of the EU Acquired Rights Directive. That directive gives employees in a business protection in the event of a transfer of that business – essentially they transfer with the business on terms and conditions, which are in most respects the same. Transfers of services to an outsource provider at the beginning of an outsource arrangement and back to the customer or to a new service provider on termination of the arrangements will often be business transfers in which employees in the EU will transfer as a matter of law. Great care needs to be taken to assess all labor-related issues in outsourcing arrangements in the EU.

## **Real Estate**

Often the outsource provider will need to be given access to the customer's premises. Sometimes the outsource provider needs to have a permanent base within the customer's premises and care must be taken to comply with local legislation and local lease arrangements to ensure that the service provider can be given appropriate access and does not, inadvertently, acquire security of

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tenure through the operation of local law or somehow prejudice the customer's rights to occupy the space.

## **Intellectual Property**

Most intellectual property rights are national. For example, rules dealing with ownership of intellectual property can be subtly different from country to country. Great care needs to be taken with ownership of intellectual property in materials generated during an outsourcing engagement. For example, a typical U.S. outsourcing contract might create some of the following unexpected results when used in the U.K.:

- In the U.S., a customer might rely on a “work made for hire” clause to assure itself of rights in developed technology. There is no "work made for hire" concept in the U.K.
- In the U.S., joint ownership (with a waiver of the right to an accounting) is an effective way to resolve disputes on joint technology because it allows both owners full rights to use and license the technology. In the U.K., joint ownership has the opposite effect: absent express agreement, neither party can license the technology without the consent of the other party.
- In the U.S., parties fight hard for software patent rights because software patents are potentially a very valuable outgrowth of an outsourcing transaction. In the EU, patents are harder to obtain for software related inventions, and thus the entitlement to any patent rights that may be generated in Europe will be of less value.

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- In the U.S., under the *Feist* case, pure fact databases created under the outsourcing agreement are rarely protected by intellectual property laws. The EU, on the other hand, has a specific intellectual property right – the database right – which protects pure fact databases.

## **Taxes**

Structuring an international outsourcing transaction in a tax-efficient manner requires careful tax planning by international tax lawyers. Taxes may vary, for example, based on where services are performed, the entities performing and receiving services, the entity that acquires title to intellectual property created during the engagement, whether intellectual property is assigned or licensed, where invoices are rendered and paid, and how invoiced amounts are characterized on the invoices.

## **Termination**

If the customer's reasons for an international outsourcing are simply to achieve the convenience of having a single service provider and the economic benefits of being a larger customer, the customer will want the right to terminate on a country-by-country basis as the economics change and alternative solutions present themselves to the customer. On the other hand, if the customer is outsourcing to implement "integrated global solutions," this sort of a provision would have a significant adverse effect on the economics of the proposed solution.

## ***Lessons from the Outsourcing Journal:***

- International (that is, multi-country) outsourcing transactions raise unique issues.

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- A fundamental question is whether the outsourcing is intended to provide a global integrated solution or whether it is merely an aggregation of country-specific transactions.
- In an international outsourcing transaction, the parties will each need country-specific legal support in labor/employment, tax, privacy, and general contracting issues.

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