



## Outsourcing Transactions – Strategies, Tactics and Gotchas – Part 3

Take particular care in defining the scope of the services and the parties' respective rights to terminate

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In part three of this continuing series on outsourcing transactions, we will address two elements that require a unique approach in outsourcing negotiations: services definition and termination rights.

### Scope of Services Issues

Unresolved scope disconnects are, in my view, one of the most common sources of failure and/or significant customer dissatisfaction in outsourcing relationships. It is unfortunately normal to have significant disconnects between the vendor and the customer regarding the scope of the services to be provided. And, in a purely tactical sense, a scope disconnect that does not get resolved prior to execution of the agreement will hurt the customer more than the vendor, because the likely result will be change orders and additional charges that the customer was not expecting.

The standard approach for outsourcing customers to mitigate the risk of insufficient service descriptions is to include what is known as a "sweep clause" in the outsourcing contract. These clauses will (i) include within the contract scope additional

services that are incidental to the specifically enumerated services in the Statement of Work, and (ii) in certain cases, use additional means to define the contract scope such as by including within scope all work being done by the people or department being transitioned.

While a sweep clause can be helpful to the customer in certain circumstances, there really is no substitute for being rigorous in articulating the expected services both pre-award (during the RFP or other solicitation process) and in the contract itself. To facilitate this rigor, the best approach is to involve counsel in the drafting of the RFP, as well in the drafting of the contractual Statements of Work, Service Levels and other substantive schedules to the outsourcing agreement. Experienced counsel can work with your internal subject matter experts and stakeholders to create contract-worthy descriptions of the services, rather than relying on the often vague and merely aspirational language sometimes prepared by the vendor's engineers—e.g. you want "Vendor will do A and B in accordance with X and Y" rather than "A and B will be done (somehow, by somebody)".

Counsel will also be able to identify (as is often the case) when additional internal experts or stakeholders need to be included in the service description/definition process.

### Termination for Cause/Suspension of Services

Newcomers to outsourcing transactions are often surprised to learn that the respective rights of the parties to terminate the agreement for cause are commonly (and, from the customer's perspective, should be) asymmetrical. The difference in rights flows from the asymmetrical positions of the parties—the services are frequently mission-critical and difficult to replace for the customer, and any termination or suspension of service would have significant negative consequences on its business.

In a typical agreement, therefore, the vendor's right to terminate for cause is limited to circumstances where the customer has failed to pay undisputed amounts owed for a significant period of time and after written notice. (The vendor would, however, still have the right to contract damages for any customer breach of the agreement.) When representing the customer,

I prefer to also include a provision explicitly stating that the vendor shall not under any circumstances suspend or withhold the provision of the services unless pursuant to a termination in accordance with the agreement. The end result under this approach is that for as long as the customer is paying for the services, the vendor must continue to provide them.

### **Customer's Right to Terminate for Convenience**

Finally, if you get nothing else from this series, get this: From the customer's perspective, you should

always have the right to terminate an outsourcing agreement for convenience. These are long-term relationships, and for any number of reasons, the parties may turn out not to be a good fit. The "problems" in the relationship may not even be the fault of the vendor (and therefore not a breach of the agreement).

In many outsourcing arrangements, however, the vendor will have upfront costs and/or deferred margin that it expected to recover over the multiyear term of the agreement. It is therefore often appropriate to negotiate specified exit fees upon customer's termination for convenience.

The bottom line is that many a customer has been happy to pay the exit fee just to end a dysfunctional relationship, and without the sometimes difficult and costly task of proving cause.

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