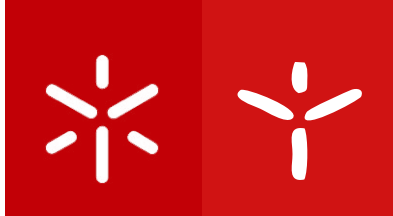




**Universidade do Minho**  
Escola de Direito

Isabel Fidalgo Vieira Mateus da Silva

**Outsourcing contract: a legal perspective**



**Universidade do Minho**  
Escola de Direito

Isabel Fidalgo Vieira Mateus da Silva

**Outsourcing contract: a legal perspective**

Dissertação de Mestrado  
Mestrado em Direito dos Negócios, Europeu e Transnacional

Trabalho realizado sob orientação da  
**Professora Doutora Catarina Santos Serra**

## DECLARAÇÃO

Nome: Isabel Fidalgo Vieira Mateus da Silva

Endereço eletrónico: isabelfidalgomateus.silva@gmail.com

Bilhete de Identidade/Cartão do Cidadão: 13846157

Título da dissertação: Outsourcing contract: a legal perspective

Orientador: Catarina Santos Serra

Ano de conclusão: 2016

Designação do Mestrado: LL.M. in European and Transglobal Business Law

É AUTORIZADA A REPRODUÇÃO INTEGRAL DESTA DISSERTAÇÃO APENAS PARA EFEITOS DE INVESTIGAÇÃO, MEDIANTE DECLARAÇÃO ESCRITA DO INTERESSADO, QUE A TAL SE COMPROMETE.

DE ACORDO COM A LEGISLAÇÃO EM VIGOR, NÃO É PERMITIDA A REPRODUÇÃO DE QUALQUER PARTE DESTA TESE/TRABALHO.

Universidade do Minho, \_\_\_\_/\_\_\_\_/\_\_\_\_\_

Assinatura:

## **Acknowledgments**

It was a privilege to have been part of this very rewarding LL.M. programme. The last two years provided me with knowledge regarding the interpretation of legal information in several areas of law.

First of all, I would like to thank Professor Catarina Santos Serra, my thesis supervisor. She demonstrated me the importance of efficiency, responsibility and matureness, as well as her guidance and availability were indispensable.

In addition, I would like to show my gratitude to my family and closest friends, whose support was particularly important in this work.

I would like to thank my companions Ana Novais, Ana Oliveira, Agbessi Neto, João Lages, José Fernandes and George Rosa.

I would also like to thank the recommendations and opinions of Dr. Fernando Resina da Silva and Dr. Nuno Cerejeira Namora. Finally, I leave a word of appreciation to CIP (Confederação Empresarial de Portugal) and Provedor da Ética Empresarial e do Trabalhador Temporário (Portugal).

## **Abstract**

The aim of this research is to analyse the risks and complexities associated with the outsourcing contract as it is currently developed by the parties. This transfer of activities or services to an external party follows no standard form. In practice, many of the particularities of the transferences are not agreed in advance, nor let alone scrupulously detailed in the contract. In addition to the need of ensuring precise terms, this relationship also requires a certain contractual flexibility, which enables to minimize the risks, and the impact of changes in the service level. The doubt remains as to whether it is necessary deeper negotiation, carried out by business national organizations, in order to provide a more harmonized standard form, a specific legal framework or (just) better contractual governance.

This contract is a mixed type of contract, meaning that it has resemblances with other legal figures, such as the subcontract. However, it may have distinct characteristics. In this work we examine these differences and how it may lead to the proliferation of the option of establishing “*ad hoc*” long term contracts and inherent service-level agreement, which entails several complexities that might lead to contractual failure. We will also examine the special contours that these contracts, acquire when several jurisdictions are contemporaneously involved, which substantially impact the contract, the stages of the process, and common issues arising in a contractual relationship.

**Keywords:** outsourcing contract and BPO, outsourcing legal risks, offshoring, contractual governance, relational reliability.

## Resumo

O meu objectivo com esta pesquisa é analisar o impacto dos riscos e complexidades associadas ao contrato de outsourcing, tal como ele é utilizado actualmente pelas empresas. A transferência de actividades ou serviços para um terceiro, não tem uma forma padrão de tratamento. Aliás, poderá dizer-se que ele assume especificidades consoante o serviço ou a actividade em causa. Na prática, muitas das especificidades da transferência não são previamente acordadas e nem muito menos escrupulosamente detalhadas no contrato. Contudo, esta relação contratual por si só requer uma certa flexibilidade visando minimizar os riscos e o impacto de alterações no nível do serviço. A dúvida permanece sobre se é necessária mais negociação, por parte das entidades públicas com natureza empresarial, que visam o desenvolvimento de um ambiente comercial competitivo com as entidades privadas com o objectivo de tentar harmonizar e difundir certos padrões, um específico enquadramento legal ou (só) uma melhor *contractual governance*.

Este contrato corresponde a um tipo misto de contrato, que significa que ele tem semelhanças com outras figuras legais, como o subcontrato. No entanto, pode ter características distintas. E, este trabalho examina essas diferenças e como isso leva à proliferação da opção de estabelecer contratos “*ad hoc*” de longo prazo e acordo de nível de serviço inerente, o que implica várias complexidades que poderão levar ao incumprimento contratual. Também serão examinados os contornos especiais que estes contratos adquirem quando estão simultaneamente envolvidas várias ordens jurídicas, o que pode implicar a aplicabilidade de leis nacionais ou menor nível de protecção e implementação legal, as etapas do processo, e os problemas que usualmente surgem nesta relação contratual.

**Palavras-chave:** contracto de outsourcing, riscos legais do processo de outsourcing, offshoring, contractual governance, confiabilidade relacional.



## Table of Contents

|  |     |
|--|-----|
| Acknowledgments .....  | iii |
| Abstract.....  | iv  |
| Resumo .....   | v   |
| Abbreviations.....   | IX  |
| Introduction.....  | 1   |
| Part I. General Considerations about the Topic .....   | 3   |
| 1. Origin and Evolution .....  | 5   |
| 2. The Concept of Outsourcing.....   | 9   |
| 3. Corporate Governance and Innovation.....  | 10  |
| 4. Types of Outsourcing .....  | 17  |
| 5. Outsourcing as an Ancillary Option to the Business Process of Reengineering<br>.....  | 20  |
| 6. Outsourcing as an Ancillary Option to Downsizing.....   | 21  |
| 7. Advantages and Disadvantages of Outsourcing .....   | 22  |
| 8. Outsourcing and Other Strategic Approaches .....  | 25  |
| Part II. The Legal Process of Outsourcing .....  | 29  |
| 1. Comparison Between the Concepts of Subcontract and Outsourcing .....  | 31  |
| 1.1. Analysis of Subcontracting Concept in Light of Portuguese Law and that of<br>Other Jurisdictions Within Existing Frameworks of Contract Types ..... | 34  |
| 2. Stages of the Outsourcing Process.....  | 38  |
| 3. Legal Issues .....  | 39  |
| 4. The Contract of Outsourcing .....   | 48  |
| 4.1. Due Diligence .....   | 48  |
| 4.2. Balanced Relations.....   | 49  |
| 4.3. Scope of the Agreement.....   | 49  |
| 4.4. Precise Terms.....  | 50  |
| 4.5. Ownership, Confidentiality of Data and Non-disclosure Agreements .....  | 51  |
| 4.6. IP Rights, Ownership and Third-Party Rights .....   | 54  |
| 4.7. Price .....   | 58  |
| 4.8. Liability.....  | 60  |



|  |     |
|--|-----|
| 4.9. Exclusivity and Non-Compete Clauses .....   | 63  |
| 4.10. Communication .....  | 64  |
| 4.11. Termination and Exit.....  | 65  |
| 4.12. The Choice of Law and Jurisdiction .....   | 67  |
| 5. Legal Perspective of the Outsourcing Contract Under the Portuguese Civil Code .....                 | 68  |
| 6. The Service Level Agreement .....   | 71  |
| 7. Common Issues Arising in an Outsourcing Contractual Relationship (or Possible Failure Reasons)..... | 75  |
| Part III. Considerations and Recommendations .....   | 79  |
| 1. The Need to Avoid Legal Pitfalls .....  | 81  |
| 2. Should a New Legal Framework Be the Solution? .....   | 84  |
| 3. Should Better Contractual Governance Be the Answer?.....  | 88  |
| 4. Conclusion .....  | 91  |
| Part IV. Bibliography .....  | 93  |
| References.....  | 95  |
| Books/Reviews .....  | 95  |
| International Conventions .....  | 101 |
| Online Resources .....   | 101 |
| Legislation.....   | 102 |

## **Abbreviations**

BPO - Business Process of Outsourcing

CC - Portuguese Civil Code

EEA - European Economic Area

EU - European Union

GATT - General Agreement on Trade and Tariffs

IPR - Intellectual Property Rights

IT - Information Technology

KPO - Knowledge Process of Outsourcing

OECD - Organisation for Economic Cooperation and Development

R&D - Research and Development

SLA - Service-Level Agreement

UK - United Kingdom

USA – United States of America

WTO - World Trade Organisation



## Introduction

At the present moment, companies' traditional strategies are suffering changes, mostly due to market competition. Firms are rethinking their strategic and operational organization.<sup>1</sup>

Due to this competitiveness, companies transfer processes or activities to external third parties, outsourcing companies, on a daily basis in order to minimize costs, but primordially, also achieve the added value of being able to focus on their core activities. This thesis shows the myriad of legal risks that are associated with the business process of outsourcing, especially when it involves different jurisdictions, at the same time. The concept of outsourcing is not a novelty, due to the fact that its origin lies in the subcontract concept. Nevertheless, the former is characterised by a more evolving contractual long-term relationship. This research will focus on the structure, which it is currently developed by the parties, regarding its content and relationship. This transfer of activities or services for an external party has no standard form to be handled, and the doubt remains between the necessity of negotiation or eventual framework or a better contractual governance.

Despite the fact that there are risks associated, it is usual for parties to enter into an outsourcing contract and inherent service-level agreement. However, not all the complexities are not taken into account. These might translate into attrition, opportunistic behaviour, or even termination of the relationship. The reasons for relationship failure are numerous, however, these obstacles have been overcome by the establishment of contracts between the parties, although some national laws regarding certain matters that substantially impact the contract and the agreement will also be applicable.

The outsourcing contract is considered a mixed type of contract with specific contours. Though these business transactions are constantly negotiated, no standard form exists, and international efforts to harmonise guidelines have been few. The most complex or sensitive transactions often involve IT, intellectual property rights, data transfer and financial services. Although the European Union has already enacted Directives concerning these matters, there are additional issues that need to be strengthened and discussed. This has already been subject to discussion in the literature on occasion, yet the positions may not be the same. This work provides an insight into the outsourcing contract, which entails a certain complexity and requires wise handling. Therefore, it becomes relevant also to understand the concept of

---

<sup>1</sup> Leitão Marques, M. M. (1987), *"A Empresa, o Espaço e o Direito"*, Revista Crítica de Ciências Sociais, 22, p.70.

outsourcing, the stages of the process and associated legal risks, common issues that arise during the contractual relation, the exposure to the national laws of the contracted party, as well as the question of how this relation is sustained by a maturity process carried out by the parties, although eventual legal pitfalls may exist.

Moreover, a substantial part of the academic literature mainly approaches outsourcing on an economic and managerial perspective, yet, a legal perspective has also developed in a less substantial amount. Subsequently, under the purpose of this work an analysis was made under the scope of law. In some parts of the second and third chapters, a discussion under the Portuguese Civil Law was also carried out, regarding the comparison of the concept of outsourcing with other established legal figures. Thereby, this approach may be seen as important to further understand the distinctive characteristics of the outsourcing contract, under an international perspective.

**Part I. General Considerations about the Topic**



## 1. Origin and Evolution

The outsourcing has its roots in the eighteenth century, with Adam Smith's known treatise on the division of labour. Evidently, the concept of outsourcing did not exist at that time, but it existed in one way or another as mercantilism, markets and transactions developed and became more sophisticated.

Smith build up a basic theory of international trade that “if a foreign country can supply us with a commodity cheaper than we ourselves can make it, better buy it of them with some part of the produce of our own industry employed in a way in which we have some advantage”.<sup>2</sup> If we here replace “foreign country” with “company”, we see a clear contemporary application of Smith’s classic principle.

Outsourcing is a management approach which has developed into an economic and political context. After the Second World War, the business model of that time encouraged the establishment of large companies, endowed with many human and material resources, which concentrated itself all production phases. Without major technological changes and fluctuations, companies developed their activities in stable markets. In the early 1970’s, this scenario began to reverse. The oil crises that led to the instability of markets coupled with technological innovations, dictated a radical change in the business model. In the late 1980’s, companies started to follow a new path, in other words, downsizing their internal structures, reducing its resources, engaging in contracts with third parties of non-essential functions, thus developing outsourcing.<sup>3</sup>

From an early stage, outsourcing has taken three different characteristics: production, which has to do with the manufacture of products and components (manufacturing outsourcing), information technology (IT) related to, among other things, the network management and development. The third characteristic is related to the business process, business process of outsourcing (BPO), in which a service provider takes responsibility for a particular area of business such as finance or human resources.

The outsourcing has emerged in the early 1960’s, when some companies in the area of information technology, began to hire third parties to process their data. However, the similarities with the features of today, only began to develop from the 1980s on as a response

---

<sup>2</sup> Smith, A. (1776), “*An Inquiry into the Nature and Causes of the Wealth of Nations*”.

<sup>3</sup> Contractor, F. J., Kumar, V., Kundu, S. K., & Pedersen, T. (2010), “*Reconceptualizing the firm in a world of outsourcing and offshoring: The organizational and geographical relocation of high-value company functions*”, *Journal of Management Studies*, pp.1428-1431.



of companies to the economic recession and high inflation rates. The Eastman Kodak known decision-making shift, in 1989, was revolutionary and definitely boosted the outsourcing strategy.<sup>4</sup>The firm hired an IBM subsidiary information technology systems company, ISSC.<sup>5</sup> This managerial strategic option was very wise, due to the fact the business in which Kodak<sup>6</sup> is competitive is photography and not information technology.<sup>7</sup> Companies have become aware of the benefits to be gained from outsourcing, such as a greater willingness from management to invest in strategic objectives, the optimization of business processes, cost reduction and risk-sharing. Consequently, certain services or internal functions began to be developed by external suppliers.<sup>8</sup> The continuous need of companies to develop competitive strategies, in order to maximize their market positions, came to dictate the strengthening of cooperation between organizations and the consolidation of partnerships.

Thus, the link between the company and the service provider has been transformed, from a simple business relationship to a partnership<sup>9</sup>, where transparency, communication, trust and reciprocity are essential values.<sup>10</sup> They become interdependent because they have common objectives: the satisfaction of customer expectations and the sharing of benefits. Currently, strategic partnerships correspond to the last stage of outsourcing.

We note that unlike the first years, outsourcing has been extended to the core competence of enterprises.<sup>11</sup> Each company, naturally, has its specific objective, but ceased to be essential to the company itself to pursue it. The bet in less possession, and more appropriate development of partnerships, allows an increment in the results, indispensable for the maintenance on the market. Some authors may argue that organizations became almost irrelevant whether the subject of outsourcing is the core or any other function. The important thing is to choose a third party which can produce the best results, in any of the functions. Nonetheless, other authors argue that there are business activities that can never be subject of

---

<sup>4</sup> American incorporated company.

<sup>5</sup> *Id.*

<sup>6</sup> Since 1994, this management tool became even more present in the USA market, with the signing of the NAFTA agreement, which potentiated and leveraged trade relations between American companies and their Northern and Southern neighbours.

<sup>7</sup> Lee, J.-N. L. J.-N., Huynh, M. Q. et al. (2000), "*The evolution of outsourcing research: what is the next issue?*", Proceedings of the 33rd Annual Hawaii International Conference on System Sciences.

<sup>8</sup> Facility management encompasses logistics services essential to the functioning of the organization, also called soft services such as cleaning, reception, secretarial work, maintenance, as well as fleet management and purchasing management.

<sup>9</sup> Kav, K., & Koper, M. (n.d.), "*What outsourcing can bring in the long run?*", Faculty of Management Koper.

<sup>10</sup> In the context at stake, this will also involve the longevity of the relationship. The change of partners implies an increase in costs resulting from the adaptation of the new partner, to the business and its specific procedures.

<sup>11</sup> Gary Hamel, & C. K. Prahalad (1994), "*Competing for the future*", Harvard Business Press, July-August issue.

outsourcing, as, for example, the company's strategic planning, and financial department, the supervision of the customer satisfaction and the control of suppliers. Along with the evolution of outsourcing, there have been a few related concepts that have emerged. These concepts derive from the various typologies of outsourcing that exist and will later be approached in this research. We will explore three: the right-sourcing, the in-house, off-site, the co-sourcing and out-tasking.

The right-sourcing may mean the right balance between the services or activities that the company decides to keep under its implementation and those that decide to permit third parties to do so. Secondly, the term in-house applies when the contractor in outsourcing performs its activity, at the premises of the contracting company. Thirdly, off-site is the opposite concept of in-house, in this situation the contracted company exercises its activity on their own premises. In fourth place, the co-sourcing modality is characterized by the sharing of the risk of the operation between the contractor and the contracted company. Lastly, the out-tasking, is considered a modified form of the traditional outsourcing. In this situation, it has hired an outsourcing company for performing a task, a function or a specific service.

In recent years, the challenges posed by globalization have led to the transfer of operational areas of companies to other countries. The permanent search for competitiveness, along with the implementation of policies for reducing costs and the strategic need to enter into new markets, has persuaded companies to divert part of its economy, to other countries that offer considerable economic advantages. A recent study published by the consultant Deloitte (2014) concluded that developing sourcing locations like India, the U.S.A., China and Poland can be expected to see growth of 15%-27%. Besides, other developing sourcing countries like Philippines, Romania, Mexico, Brazil and Malaysia can be expected to achieve higher rates of growth, leading to a potential doubling of the outsourcing market in these countries.<sup>12</sup> The target countries for this transfer were the developing countries.

However, there are detractors of this new business strategy. Thus, there are issues associated with this development in the business world that translate into matters of internal security, as well as, the fear of the lack of quality of services provided in countries with patterns below average. The relocation involves the elimination of jobs in developed countries, and the corresponding exploitation of the labor force in developing countries has generated

---

<sup>12</sup> Deloitte (2014), "*Deloitte's 2014 and Beyond Global Outsourcing and Insourcing, Survey 2014*", December.

controversy, in several developed countries.<sup>13</sup> In addition, cultural and linguistic differences are regarded by many as obstacles associated with the difficulty in controlling remote operations. These are some arguments against this commercial trend, which it is seen by many as a further economic and social threat to countries, such as the USA where this, despite everything, gained strength.<sup>14</sup>

The General Electric Co. was one of the precursors of relocation, having approximately 12,000 people working in India, China and Mexico. Many other companies have done the same, taking advantage of the fact of labour in these countries, motivated by the presence and level of requirement of foreign companies, be ever more qualified.<sup>15</sup> This relocation is also known as offshore outsourcing or offshoring, understood as outsourcing of functions and services to companies located in other distant countries. This model was developed over recent years, as a result of technological progress at the level of the internet, telecommunications and satellite transmissions.

To provide for the increasing needs of developed countries, ideal destinations for the hiring of offshoring outsourcing have arisen. Currently, India is considered as the most appropriate nation to this modality of outsourcing, due to the low cost of labour and high educational level, particularly in the areas of information technology, the relative political stability and fluency in English. Despite its undeniable success, the offshoring constitutes an important challenge for the business organizations. Although it is true that dissatisfaction has been growing, generating many situations of back-sourcing, in other words, the company may opt for a process reversion and produce internal functions previously outsourced. In addition to the already mentioned linguistic and cultural differences, other factors contributed to the failure of many attempts of offshoring process. This may be related to the increasing risks of the operation, resulting from the ever greater number of service providers in offshoring, and the observation costs surpassing estimations or contractual specifications, as a result of global economic and financial instability.<sup>16</sup> However, this dissatisfaction has not curbed the development of offshoring. Many companies, contractors and suppliers have reached a certain degree of maturity in their relationships, continuing to invest in this important business strategy.

---

<sup>13</sup> Holcombe, J. K. (2005), "Solutions for regulating offshore outsourcing in the service sector: using the law, market, international mechanisms and collective organization as building blocks", 7 J. Bus. L..

<sup>14</sup> *Id.*

<sup>15</sup> In 2005, Jack Welch was elected the most admired CEO, in the past 20 years, by the readers of the magazine Chief Executive, and by Fast Company Magazine. See, A. Krames, Jeffrey (2001), "The Welch Way: 24 lessons from the World's Greatest CEO", McGraw-Hill, 1st Edition.

<sup>16</sup> Lacity, M.C. and Hirscheim, R. (1993), "The information systems outsourcing bandwagon", Sloan Management Review, Fall, pp.73-86.

## 2. The Concept of Outsourcing

The term outsourcing has an Anglo-Saxon origin and widespread use in the business world, although in certain European countries other terms are used with the same meaning. The increase in productivity, performance and quality of service are vital factors that determine the success of organizations. As Sanders *et al.* state, “Outsourcing today means many different things to many executives. It may mean a single system contract for the relatively small percentage of the budget, or it may span multiple-systems and represents a significant transfer of assets, leases and staff of a vendor who operates, manages and controls the company’s information systems functions”.<sup>17</sup>

The definition of outsourcing is not uncontested. We can understand this term in a broader or narrower sense. Outsourcing consists of hiring services and activities of a business, from an external entity that specializes in this service. The execution of all the activities and processes related to an area or function, including even its management on a daily basis, is therefore transferred to this third party. The difference between outsourcing and subcontracting, which will be addressed later in this research, may seem to be non-existent: the literature commonly refers to these terms as being synonymous. Normally, firms resort to subcontracting to satisfy peak demand or the needs of a particular activity or season. As some authors write, there is not a transfer of daily management, but “(...) outsourcing comprises the delegation of the day to day management of the outsourced activity to third parties. It is the element of delegation of management, which differentiates outsourcing from subcontracting. Once the price and service levels have been established, in-house responsibility is to manage the contract rather the activity.”<sup>18</sup> As we will see in the next chapter, we face two realities with different characteristics.

The relationship of outsourcing is characterized as being long-term. Hiring a company of couriers to deliver an order is not outsourcing, hiring it to deliver all the company's orders for a period of five years is outsourcing. In a BPO a company transfers a business function for the outsourcer and not just a simple activity. There are different definitions proposed in literature, but it is often described as being a strategic decision, that encompasses the contracting of external entities to provide certain non-strategic activities or business processes.

---

<sup>17</sup> Saunders, C., M. Gebelte e Q. Hu, (1997), “*Achieving Success in Information systems outsourcing*”, California Management Review, Vol.39, Nº2, pp.63-79.

<sup>18</sup> Wood, D., Barrar, P., O’Sullivan, K. (1996) “*Outsourcing Finance Activities: a Practical Approach for Small and Medium Enterprises*”, Institute of Chartered Accountants in England & Wales.

That is accomplished by means of agreements or contracts with companies, with the ambition of bettering the competitive advantage.<sup>19</sup> This leads to a discontinuation of in-house processes.<sup>20</sup> Others define outsourcing as “the transfer of the production of goods and services that had been performed internally to an external party”.<sup>21</sup>

Although the differences are subtle, there are many variations in outsourcing definitions. In addition, it is important to stress that several types of outsourcing exist, but their general form remains the same. Within all the proposed definitions, it is commonly argued that outsourcing means a discontinuity of the internal processes or activities, which is also known as the make-or-buy decision.<sup>22</sup> This management strategy is thus of great relevance in the organization's response to the constraints of a competitive market and competition.

### **3. Corporate Governance and Innovation**

The business organization has a key impact on the development of its economic activity and development. In today's competitive business landscape, companies are constantly adapting to the markets. The long-term survival of a company in the market depends essentially on its continued ability to adapt in time. The sustainability of the company depends on this issue and also on the ability to innovate, in other words, trying to always be *avant-garde*. Besides, technological innovation can be studied in different areas. Economics appear unable to properly demonstrate why companies with identical external conditions present different results with respect to performance in innovation. On the other hand, the literature about corporate governance provides some useful insights, in order to understand the entrepreneurial innovation activity, considering the economic effects of different modes of coordination between company shareholders and management. In order to understand firms' innovation performance, economists found it useful to look further, inside the firms, at their structure.

The corporate governance system is extremely important in the performance of corporations, which balances the interests of investors and managers. The efficiency of the

---

<sup>19</sup> Espino-Rodríguez, T. F., & Padrón-Robaina, V. (2006), “*A review of outsourcing from the resource-based view of the firm*”, International Journal of Management Reviews.

<sup>20</sup> Kern, T. & Willcocks, L. (2000), “*Exploring information technology outsourcing relationships: theory and practice*”, Journal of Strategic information systems, Vol.9, pp.321-350.

<sup>21</sup> Ellram, L. & Billington, C. (2001), “*Purchasing leverage considerations in the outsourcing decision*”, European Journal of purchasing and supply management, Vol.17, pp.15-27.

<sup>22</sup> Edvardsson, I.R., Oskarsson, G.K. and Vesteinsdottir, S. (2011) “*Enhancing customer services and core competencies: outsourcing in Icelandic service SMEs*”, International Journal of Entrepreneurship and Small Business, Vol.14 No.3, pp.313-333.

corporate governance determines if the value of firms can be enhanced.<sup>23</sup> In line with the aforementioned idea, every country is finding a suitable model which can improve the performance of corporations efficiently.<sup>24</sup> Presently, a large proportion of worldwide companies are composed of investors and managers. In broad terms, this involves the issue of how to align the interests of both parties and ensure that the companies are managed in accordance with the interests of investors. In this way the distribution of rights and responsibilities in the company is specified.<sup>25</sup> A more restricted definition would entail “corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investments”<sup>26</sup>.

The term “innovation” can refer to technological or organizational innovations. Technological innovation is related to an attempt to create a new product or process, new types of commodities or machinery used in production, which may be a novelty in the market. The latter regards new ways of organizing work and is not limited to the organization of the production process within a given firm, but may also include arrangements across firms.<sup>27</sup>

A system of corporate governance shapes a company’s innovation activity through three main ways: corporate ownership, corporate finance and labour. The first aspect involves the distribution of control rights and residual income rights within the corporation, fundamentally within the company's ownership structure. Secondly, it is important to mention through how businesses finance innovative production. The third dimension is related to labour. This has been neglected by the traditional corporate governance research. However, it is considered a central concern for corporate governance and performance.

It is widely recognised among legal and economic policymakers that the institutions of corporate governance have a direct correlation with technological development.<sup>28</sup> Technological innovation is vital in order to keep the business growing profits in the long

---

<sup>23</sup> ‘During this process, two models formed: the “outsider” system and the “insider” system. It is commonly believed that a country has different backgrounds of historical, economic, political, cultural, legal system, subsequently, the structures of corporations based on which corresponding corporate governance systems are shaped’, Wei, Yuwa (2003), “*Comparative Corporate Governance- A Chinese Perspective*”, Kluwer Law International, p. 206.

<sup>24</sup> Zheng, Xia (2009), “*Could the Different Countries’ Corporate Governance Regimes be Harmonized?*”, Management Science and Engineering, Volume 3, No.2.

<sup>25</sup> Hansmann, Henry & Kraakman, Reinier (2011), “*Reflections on the end of history of Corporate Law*”, Yale Law & Economics Research Paper N° 449.

<sup>26</sup> Shleifer, A. And Vishny, R.W. (1997), “*A survey of corporate governance*”, Journal of Finance.

<sup>27</sup> Edquist, C., Hommen, L. and McKelvey, M. (2001), “*Innovation and employment: process versus product innovation*”, Cheltenham: Elgar.

<sup>28</sup> Lazosnick, W. (2005), “*Corporate Governance, innovative enterprise, and economic development*”, paper prepared for the UNU-WIDER project on Institutions and Economic Development.

term.<sup>29</sup> However, innovation has specific characteristics that stand out within the usual indicators of economic performance.<sup>30</sup> These particularities are related with the specificity of the investments that require the combination of knowledge and experiences by those who are involved in innovation or R&D teams. The unpredictability about both the results and future profits may be risky, and this creates a margin for opportunistic behaviour from one of the parties.

Due to the stated characteristics it becomes difficult to specify each party's obligations in a contract. Thus, there arises the issue of incomplete contracting and distortion of the initial investment decision. The corporation itself, as a legal entity under the separate law of shareholders, acts as a reservoir of all property rights over the assets used in production. Directors and managers thus acquire a mediator position and are less prone to engage in opportunistic behaviours than are shareholders, who have an interest in gaining returns from their investments.<sup>31</sup> The company's production, however, is a collective work where the financial investors inject money and employees' human capital.

The process of innovation involves the management of human and other resources. This task of management and decision-making is designed to accommodate innovation in three levels of corporate decision-making, strategic, operational and transaction level. In addition, the capacity to innovate depends also on how the company organizes internally its resources, and their interaction with the market and other companies.

The resources can be obtained and organised internally, or externally, from the market.<sup>32</sup> This issue is generally referred to in the literature as a make-or-buy decision. If the company decides to resort to the existing options on the market, it may choose to purchase resources over business acquisitions or employment contracts. Over the past few years, outsourcing (BPO) has become the norm rather than the exception.<sup>33</sup> A firm might choose to hire resources through contracts of outsourcing or consulting work, depending on the type of activity that is at stake. There is an ongoing debate about the relationship between outsourcing and innovation. This

---

<sup>29</sup> Bassett-Jones, N. (2005), "The Paradox of Diversity Management, Creativity and Innovation", *Diversity, Management, Creativity and Innovation*, 14 (2), pp.169-175.

<sup>30</sup> *Id.*

<sup>31</sup> Lazonick, W., P. A. (2005), "Dynamic capabilities and sustained innovation: strategic control and financial commitment at Rolls-Royce plc.", *Industrial and Corporate Change*, 14 (3), pp. 501-542.

<sup>32</sup> Mäntysaari, P., (2012), "Organising the Firm. Theories of Commercial Law, Corporate Governance and Corporate Law", Springer-Verlag Berlin Heidelberg.

<sup>33</sup> Mahnke, Volker (2002), "The process of vertical dis-integration: an evolutionary perspective on outsourcing", *Journal of Management and Governance*.

chapter's section 6 will address the advantages and disadvantages of outsourcing, which depends on which activity or process is at stake. Firms can make the decision to share resources with other companies through cooperation or joint ventures.

As we have seen, the system of corporate governance shapes a company's innovation activity in three main areas, namely corporate ownership, corporate finance and labour. The structure of ownership of enterprises is the manner through which property rights are distributed within the company. Usually, the degree of concentration of capital ownership is considered to be a crucial factor in determining the structure of a corporation's property. As a consequence, a company which has a dispersed share ownership structure is less likely to develop an innovation culture. Ownership concentration, large shareholders or a controlling shareholder are important factors which are likely to encourage a culture of innovation and resource allocation for that purpose.

Thus, there are two different approaches to dealing with the relationship between the ownership structure and the innovation. One approach is concentrating ownership. This implies a more efficient control of management strategies and, in turn, reduces the high costs associated with the agency for innovation. The logic of this agency cost approach holds that diffuse ownership adversely affects corporate innovation activity because it allows the managers to pursue their own ambitions, such as increasing their riches and personal reputation, to the detriment of projects that increase revenues." A disperse ownership entails high monitoring costs, as a consequence, small shareholders may not sense any stimulus to monitor management behaviour".<sup>34</sup> As has already been mentioned above, the contractual costs associated with projects involving innovation are especially high due to the long-term and high-risk nature of innovation. Some authors have observed that the contractual solutions are not likely to solve problems of agency between dispersed shareholders and managers. The firm is less likely to have a robust innovation culture when it is diffusely held. The concentration of ownership structure is one of the factors that can bring benefits. If the company has a majority shareholder committed to the development of the business, this can be a source of various types of ancillary services. Nevertheless, a non-controlling shareholder may also be a source of capital or auxiliary services. Thus, firms can use his *de jure* and *de facto* powers of control in innovation-friendly ways. Moreover, the shareholder may also provide know-how and other information,

---

<sup>34</sup> However there is another device that increases control over the managers. Management stockholding consists on the leverage of equity value in manager's revenues and voting power. This percentage aims to reduce managers' risk aversion. Belloc, F. (2009), "Corporate Governance and Innovation: A Survey", Journal of Economic Surveys.



as well as help in relations with third parties, resource management and other services. The shareholder can even be a source of capital or a signalling mechanism that makes it easier for the firm to raise funding from other investors.

Another of the approaches stresses that various ownership structures relate to different, methods of application, in contractual incomplete relations concerning specific investments by company-internal and external investors. As the literature shows us, the ownership concentration tendentially fosters confidence and commitments.<sup>35</sup> Thus, in situations of diffuse ownership, the individual shareholders may use their "exit" option anonymously. On the other hand, a concentrated shareholder cannot do so because of reputational consequences, thereby, large shareholding, encourages long-term relations between shareholders and other stakeholders (like employees, suppliers and external financiers), as well as supporting specific investments of a company.

In the past a few researchers concluded that institutional ownership has a negative effect on R&D intensity. However, subsequent studies have shown exactly the opposite.<sup>36</sup> Several authors have demonstrated a positive correlation, alleging that institutional owners have better incentives and the ability to monitor than other possible owners.<sup>37</sup> Being that these investors are driving forces in the process of innovation, and this has been explained by a better control and protection of reputation of managers in case the R&D "(...) project fails. Besides, there is also a more positive relationship between innovation and institutional ownership when competition in the market of the products is more intense or when there is protection against hostile takeover bids".<sup>38</sup>

Another relevant aspect of corporate governance is related to the availability of financing. Corporate finance involves the issue of ensuring the allocation of financial resources

---

<sup>35</sup> Mayer, C. (1997), "Corporate Governance, competition and performance", *Journal of Law and Society*.

<sup>36</sup> See, supra note 34.

<sup>37</sup> Shleifer, A., & Summers, L. H. (1988), "*Breach of Trust in Hostile Takeovers. Corporate Takeovers: Causes and Consequences*", (Vol. I), University of Chicago Press.

<sup>38</sup> The automobile industry has been the target of pressure of capital markets. has been pointed out the great value destroyer in terms of shareholder value. The low market capitalization of some of the companies is that in fact the places under the threat of a hostile takeover. In addition, institutional investors expressed their dissatisfaction regarding corporate governance structures in the car industry. "Rather than as means for financing the more importante role the stock market played for Volkswagen was in its function as a market for corporate control. The low market valuation of the company made it an easy pray for attempts of a hostile takeover. In view of the critique of the Volkswagen-law by the EU and rumoured interests of car companies to buy VW this was regarded as a real threat by the actors at VW. The fear of a hostile takeover has been the main driver for a number of measures to enhance investor relations and improve the profitability of the company.", Jürgens, Ulrich, (2002) "*Corporate Governance, innovation, and economic performance: A case study on Volkswagen*", WZB Discussion Paper, WZB Berlin Social Science Center, No. FS II 02-205, p.35.

to irreversible investments with uncertain returns, one of the essential conditions for innovation. In other words, it requires patient capital.<sup>39</sup> The large and liquid stock markets promptly provide companies with equity finance, thus acquiring an important status in supporting the aggregate corporate innovation activity.<sup>40</sup> Some authors argue that the relationship between the stock market and innovation can be as beneficial as it can be harmful. For example, shareholders of successful companies may be unable to wait until the innovation generates commercial revenue and might “go public” to take advantage of the stock market evaluation of innovation. In such a case, the allocation of resources may be left under the control of the company, given to the separation of ownership of assets, and managerial control made possible by stock markets.<sup>41</sup> In the presence of the stock markets, the acquisitions of assets exercise a great influence over the investment strategies of companies. In a typical case of an acquisition, a competitor makes an offer to the dispersed shareholders of the target company, and if they accept the offer, he acquires the control of the company and may replace the management. Therefore, takeover threats can negatively affect the long term strategies based on specific investments, such as the innovation processes.

Lastly, it is necessary to make a reference to the labour issue. Nowadays, firm-specific skills are acknowledged as an essential input to innovation production. Theories of both corporate governance and corporate innovation have done little until recently to address the problems raised by investments, in firm-specific human capital. This dimension also entails the analysis of labour unions, worker participation and employee resistance to innovation.<sup>42</sup> However, the three dimensions we have seen must not be considered in isolation, if one’s aim is to explore the effect on companies’ innovation business adequately. The literature has demonstrated a tendency to focus on individual dimensions, which leads to contradictory outcomes. In spite of the plurality of purposes, in different research fields, there only a few studies that mention the effect of governance structures on the firm’s ability to innovate. In

---

<sup>39</sup>Lazonick W., (2010), “*The Chandlerian corporation and the theory of innovative enterprise*”, *Industrial and Corporate Change*, 19, pp. 317-349.

<sup>40</sup> Gugler, K., (2001), “*Corporate governance and economic performance*”, Oxford: Oxford University Press.

<sup>41</sup> See, supranote 34.

<sup>42</sup> For detailed discussion on this dimension see, among others, see, Ibsen, C. L., & Mailand, M. (2011), “*Striking a balance? Flexibility and security in collective bargaining*.” *Economic and Industrial Democracy*, 32 (2), p. 161 – 180; Ibsen, C. L., & Mailand, M., (2009), “*Flexicurity and Collective Bargaining: Balancing Acts Across Sectors and Countries*”, FAOS Forskningsnotat; Nickell, S. and Nicolitsas, D. (1997) “*Human capital, investment and innovation: what are the connection?*”, CEP Discussion Paper No.20, Oxford: Oxford University; Machin, S. and Wadhvani, S. (1991), J. and Sheehan, M., (2003), “*Labour market deregulation, “flexibility” and innovation*”, *Cambridge Journal of Economics* 27 (1): 123-143; McCain, R.A. (1980); Zwick, T. (2002) “*Employee resistance against innovations*”, *International Journal of Manpower* 23 (6): 542-552.

addition, analysis at the level of business and organizational strategies should be better integrated with an analysis of what corporate law and labour law establish at a national level. In the corporate context, innovation is the result of the fact that companies apply their ideas with the aim to continue to meet the needs and expectations of customers. In addition, organisational capabilities and skills can enable the company to “set the agenda” before its competitors do, in order to always be a step forward. The strategic organisation structure must be defined regarding the type of business environment. It also requires the appropriate combination of strategy, organisation and finance. From the commercial law perspective, it entails the use of legal tools and practices at all three levels of corporate decision-making (strategic, operational and transaction level). This reasoning must always be kept. Otherwise, it will not lead to the intended ambitions.

As we have seen, company resources can be obtained and organised internally, or externally and acquired from the market. The literature generally refers to this process as the option of a firm to choose to hire resources through contracts of outsourcing as a make-or-buy decision. As we have seen, a company’s innovation process may be costly and time-consuming. Customers expect service suppliers to suggest innovation and not wait for customer's ideas for innovation. In sum, outsourcing customers are eager to reap the benefits of an innovation in technology and mature process to be able to help achieve success in their own business. However, this need for innovation conflicts with the main weapon of providers of this service: the price. Innovation is a very expensive process.<sup>43</sup>

Companies organize themselves in different ways, by evaluating which activities should be available in-house and which may be outsourced. This last option may entail the mitigation of agency problems. The question is, what types of outsourcing actually exist?

---

<sup>43</sup> Lacity M.C., Solomon S., Yan A., Willcocks, L.P. (2011), “*Business process outsourcing studies: a critical review and research directions*”, *Journal of Information Technology*, 26, pp.221-258.

#### 4. Types of Outsourcing

The various types of outsourcing are defined in function of several classification criteria. If the criterion used is the scope of outsourcing, we will find two possibilities: total outsourcing and selective outsourcing or partial. A total external hiring involves at least 80% of the functions of the organization; partial outsourcing involves an assignment of less than 80% of functions.

Another criterion is the one that “(...) measures the level of decision or the level of the intensity of the relationship, between the contracting company and the contracted party. This criterion refers to operational, tactical and strategic outsourcing”<sup>44</sup>. Through this classification, it is possible to observe that the intensity of the relationship between the organization and the supplier of services increases.

In operational outsourcing, the decision of hiring a third party outside the organization takes into account the total need of performing simple or partially certain functions or sub-functions. Decisions are planned in the short term. The relations between the company and the outsourcer are simple and almost limited to the mere monitoring of services provided, not leading to changes in the quality and level of service. Differently, tactical outsourcing presupposes a deeper relationship between company and supplier. The decision to execute tactical outsourcing involves the provision of human and material resources that enable the achievement of the benefits to the organization. This is a decision focuses on decreasing costs.

In strategic outsourcing, we have achieved the highest level of intensity in relations, between the organization and the supplier. This decision, with long-term planning, presupposes a strong cooperation between the two companies. Despite focusing on reduction of costs, the strategic outsourcing decision meets other important realities in the pursuit of the objectives of the company. It implies improvement of the quality of the operations, access to specialized resources and specific know-how and the competitive advantages. Within the company, this corresponds to management decisions which imply a comparison between the advantages of keeping the activity in-house and turning to the market. Other decisions may involve integrating transferences into the production process. This decision implies a relevant investment, whose return is essential to the organization.

---

<sup>44</sup> Franceschini, F., Galetto, M., et al. (2003), “*Outsourcing: guidelines for a structured approach*”, *Benchmarking: An International Journal*, 10 (3), pp.246-260.

If we consider a classification based on the objective of outsourcing, we find that according to some authors, core outsourcing, which covers strategic activities (core functions) of the organization and the peripheral outsourcing in which the activities covered are peripheral to the core of the company (non-core functions).<sup>45</sup> The level of service and involvement between the outsourcer and organization lead to two types of outsourcing: BPO (Business Process of Outsourcing) and the KPO (knowledge process of outsourcing).<sup>46</sup> Some authors consider that the KPO is only a sort of business process of outsourcing. There are differences that stand out and justify this differentiation. The BPO handles with the implementation by the outsourcer, standard processes of organization, having as support a long-term contract. In the knowledge process, the outsourcer provides knowledge, which requires high technical analytical skills, relying on human resources with qualifications and experience, in the field in question.

Within the business process of outsourcing, the literature commonly refers to three different types that reflect the geographic location of the contracting parties, namely offshore,

---

<sup>45</sup> Another classification distinguishes outsourcing in public and private sphere. In the latter, both parties (organization and supplier) are private entities. In counterpoint, we can also have the situation of a public entity entering in a contractual relation with a private entity. Outsourcing is an activity that is manifested predominantly in the private sector. Yet, the need to cut the growing deficits in public accounts has led the governments to search for forms less expensive to provide public services. The privatisation of public enterprises partially solved this problem, but in sectors where was not feasible, outsourcing has emerged as a credible alternative. As it was mentioned, the use of outsourcing emerged as a manifestation of the reforms of the public administration. An OECD report from 2005, which handles with the theme “*The use of mechanisms- type of the market for the supply of services to governments*” pointed three categories of mechanisms that support the modernisation of the public sector: outsourcing, the public-private partnerships and vouchers.

In sum, within this context outsourcing is defined as the ‘government procurement of private entities for the provision of services’. The public-private partnerships refers to ‘agreements by which the private sector financing, projects, builds, maintains and operates the infrastructural (...) assets provided by the public sector’. Lastly, vouchers entail ‘(...) separating the provision of public services of its financing. The financing remains with the government in the form of a voucher that is issued in favour of individual entities which may exchange by services of a scale of suppliers.’

The driving factors that lead to the growth trend of outsourcing in public sector are related with “(...) the reduction of costs and the improvement in services, brought by the involvement of the know-how of the private sector in public sector activities. Although there are similarities between the private and the public sector, there is also noticeable differences. The private sector organizations should obtain a profit for their shareholders, but are not so limited about how to achieve this. The public sector organizations have to demonstrate that they are adding value to taxpayers' money, but are restricted by a set of legal and political requirements. In fact, the missions of public entities were redefining itself, redirecting to certain peripheral functions for private outside suppliers. In the perspective of the State, these are peripheral functions which are essential and have to do with the welfare. Thus, the governments have been taking of decisions such as the current form of outsourcing or the creation of public-private partnerships. However, these figures are sometimes confused. The outsourcing contract involves a partnership between customer and supplier. Despite the similarities, the concept of public-private partnerships may be closer to concept of joint venture. Therefore, if an outsourcing company engages in contracts with a government it might be said that there is a likelihood of resemble with a joint venture, thereby differentiating it from outsourcing, essentially, by the level of integration between the parties and by the contractual duration, more extended than in outsourcing contract.” This distinction is far from being consensual, in view of recent trends in outsourcing relationships. Blöndal, J., (2005),” *Market-type Mechanisms and the Provision of Public Services.*” OECD Journal on Budgeting, 5 (1), pp.79-106.

<sup>46</sup> An analysis of core and non core functions will be provided later, on section five of this chapter.

onshore and nearshore. The offshore outsourcing means the relocation of a business function from one country to another. This may involve the manufacture of products, service centres or other operations to a different country. The offshoring is often used to reduce the cost of doing business, looking for the company to move part of their operations to countries with more favourable economic situations.<sup>47</sup>

In outsourcing onshore, the service provider exercises its activity in the same country of the customer, while in nearshore outsourcing the provider's country is near the customer's country. Other authors understand that four categories of outsourcing exist, divided in function of two assumptions. These translate into the prior existence of the activity or process in-house, and the proximity of the contracted function to core competence of the organization. Thus, depending on whether or not there is proximity to the core and whether we are dealing with a function or service previously exercised in-house, we find, respectively, strategic outsourcing with transfer of activity or the traditional outsourcing with transfer of activity. On the other hand, whether or not there is no proximity to core competence, but never having been exerted before the function in the organization, we are faced with the direct strategic outsourcing and the traditional direct outsourcing.

Another important distinction is stated and based on the characteristics of the existing relationship between the organization and the supplier, distinguishing four types of outsourcing.<sup>48</sup> Thus, we might have a total outsourcing, multiple supplier outsourcing, strategic alliance outsourcing (joint venture) and insourcing. Thereby, in total outsourcing, we find a partnership with a single supplier, established with the main purpose of the reduction of costs. On the other hand, in a multiple supplier scenario, the primary objective is to stimulate competition between the various suppliers in order to obtain, in addition to lower costs, more capacity for innovation. Nevertheless, in this type of relationship we often find alliances between suppliers, which concert values and balance their proposals for the services or functions that frustrates the desired aims. In the third place, the outsourcing of strategic alliance implies a relationship, where the organization shares with the outsourcer risks and profits, but retains the strategic control of the operation. Finally, insourcing translates into the in-house maintenance of functions or services, which are transferred to the contracted party. Sometimes,

---

<sup>47</sup> Blended-shore is a combination of onshore with offshore outsourcing. This option requires selecting a partner that can leverage their multiple locations to provide a coverage of scale, services, and savings. The outsourcing company, makes the investment, for instance the construction of contact centres, in several countries, staff, its management and its maintenance.

<sup>48</sup> Currie, W. L., Willcocks, L. P. (1998), "Analysing four types of IT sourcing decisions in the context of scale, client/supplier interdependency and risk mitigation", *Information Systems Journal*, 8, pp.119-143.

the distrust in outsourcers may deter companies from relying on them. There are situations where services or processes that once were outsourced and now are internalized again due to contractual termination or breach of contract. This is also known as back-sourcing or retro-sourcing.<sup>49</sup>

If we take into account the typologies that emerge from different authors in the literature review, it is possible to gather among the various typologies proposed, foundations for constructed reasoning. Through the first classification, we observe that there are different degrees of intensity in the contractual relationship (operational, tactical and strategic outsourcing). Four other characteristics that could be added are based on the existing relationship between the organization and the supplier (total outsourcing, multiple supplier outsourcing, strategic alliance outsourcing and insourcing). As we have seen, this relationship is also characterized in accordance with the geographical location of the contractual parties (offshore, nearshore and onshore).

Nevertheless, alongside the outsourcing it is possible to observe other management tools.

## **5. Outsourcing as an Ancillary Option to the Business Process of Reengineering**

There are other decisions that may be taken by a company, with the aim of reducing costs, improve quality and competitiveness. However, none of them should be confused with the concept of outsourcing.

The reengineering is a decision of extreme relevance for a company, due to the impact that it has on the business processes and production, entailing a radical change.<sup>50</sup> As it is argued on the literature, reengineering translates into the radical rethink and redesign of the business processes of a company, having as an objective obtaining drastic improvements in areas such as, costs, quality of services and time. This consists “(...) in the renunciation of all former business processes, which involves so many difficulties and there is the risk of not being implemented enough changes or be made in exaggeration.”<sup>51</sup> Of course, there are other associated risks, for instance, the adaptability of the human resources of the company to the new procedures introduced. Thus, it is possible to find here a connection between two business

---

<sup>49</sup> Walters B., Tang Z., (2006), “*IT-enable strategic management*”, Idea Group Inc.

<sup>50</sup> Hammer M., Campy J., (1993) “*Reengineering the corporation: a manifesto for business revolution*”, Harper Business.

<sup>51</sup> Sako, M. (2010), “*Outsourcing versus shared services*”, Communications of the ACM, July 2010, Volume 53, No.7.

decisions, being that one is a consequence of another. After the implementation of a process of reengineering, a company is sometimes faced with the need to proceed to the total or partial substitution of its employees. These processes are characterised by being time-consuming and costly. Therefore, the weighing of costs is essential, as well as the need to achieve, as soon as possible, those desired quality patterns. Therefore, it is very common for a company to choose to contract with one or more outsourcers as a way of ensuring the achievement of its objectives. The relationship between reengineering and outsourcing has divided some authors. In the literature, it is argued that outsourcing is one form of reengineering, and there are those who consider that it is one of its instruments. Among the various managerial tools available to a company's organization, reengineering and outsourcing are independent, and can be used together or separately, concluding that "(...) outsourcing must not be synonymous with reengineering".<sup>52</sup>

## **6. Outsourcing as an Ancillary Option to Downsizing**

In the late 1980s, companies started to realize that their internal bureaucracy represented an excessive deadweight, due to the numerous hierarchical levels that were hindering the decision-making process.<sup>53</sup> The need to achieve high levels of efficiency owing to competition, and constant changes in the market, has led to a rethinking of the organizational structure of enterprises. Downsizing has arisen as a tool that enables the "slimming" down of organizations, reducing their resources and improving communication between the various hierarchical levels. This reduction of resources and the need to focus on core businesses, has led to many companies choosing outsourcing, through the recruitment of third parties to carry out non-core functions and procedures. Both in reengineering and downsizing, there are many situations in which such decisions are accompanied by outsourcing without, however, the terms being deemed as distinct either in motivation or in the objectives. In addition to internal organizational aspects, there are various reasons that conduct a company to decide the implementation of downsizing. Among them it is possible to identify the necessity to be prepared for future changes in the market, an aim that is reached by avoiding dispersions and betting on a greater concentration on their core activities. The reduction of costs and reduction of resources entails a considerable decrease of

---

<sup>52</sup> Greaver, M.F., (1999), "*Strategic outsourcing: a structured approach to outsourcing decisions and initiatives*", New York: AMACOM: American Management Association.

<sup>53</sup> Allen, J. (1988), "*Surviving Corporate Downsizing*", Wiley & Sons.



labour and social costs.<sup>54</sup> The use of new technologies, more efficient than the available resources also leads to the implementation of downsizing.<sup>55</sup> This managerial solution has thus become, over the years, essential to the survival of many businesses, since its use permits encourage competitiveness and the maintenance of financial balance.

## **7. Advantages and Disadvantages of Outsourcing**

The most obvious advantage of outsourcing is the reduction of costs. This managerial option decision enables the reduction of fixed operational costs (human resources and equipment), transforming them into variable costs. The company will use the surplus of financial resources in activities related to its objectives, reinvestments and modernising the organization.

This leads to several implications in labour relations. As regards human resources, outsourcing welcomes a legion of detractors, who highlight the unemployment and lack of labour stability as its natural consequences.<sup>56</sup> The business specialization, resulting from the strategic decision of outsourcing, derives from the internal reduction of resources which before were geared to the performance of functions or services. On the other hand, it is also true that the recourse to outsourcing implies the creation of new firms, outsourcers, which generate employment, covering all levels of qualification.

Thus, to the employee, the most visible repercussion has to do with some of its precarious employment situation, which essentially replaced by amendment of their remuneration conditions, from fixed to variable. If there is a perception of future uncertainty about the human resources allocated to the areas to be transferred outside it is very demoralising and might temporarily affect the productivity of the company. This position, particularly in relation to firing as a consequence of outsourcing, presupposes full respect for human rights and labour guarantees.

---

<sup>54</sup> The determination to achieve the objectives of the downsizing, came to determine some excesses generating the high unjustified dismissals of many workers, a practice that has been condemned by the majority of authors. Many organizations have been far more, seriously jeopardizing their own growth.

Hamel G., Prahalad C.K., (1994) “*Competing for the future*”, Harvard Business Press, July – August issue.

<sup>55</sup> The mergers between companies also entail the decision of downsizing. Generally, organizations in the phase of prior negotiations to a merger, agree on the remission of middle and senior management, avoiding duplication of functions and costs in a future single organizational structure.

<sup>56</sup> For a detailed analysis on fragmented employment relationship, see, Rendingha, Maria Regina (1995) “*A relação laboral fragmentada. Estudos sobre trabalho temporário*”, Coimbra Editora.

If we look at the issue of offshoring outsourcing, the consequences for the working world can be completely diversified.<sup>57</sup> As we have seen, in this case the outsourcing decisions imply the transfer contract of areas of activity of the organization, to distant countries in general in developing, with production costs guaranteed lower.<sup>58</sup>

In this context, outsourcing can increase unemployment. Companies reduce their resources, leaving to create jobs in a new country. The creation of employment actually may increase in the contracted company's country.<sup>59</sup> This reality has been assuming important political contours in Europe, by the agreement attempts triggering corrective political attitudes and sanctions.<sup>60</sup> Other factors are also relevant, as labour, social changes and awareness of new needs, and have a large direct correlation in the costs borne by companies of outsourcing.<sup>61</sup> The maintenance of the functions or services in-house has a higher cost than that provided by the outsourcer, which according to the needs of a company, temporarily provide the execution of these functions or services. Resorting to outsourcing also allows greater control over the costs. The fact that the implementation of functions or services have been specified in the contract, allows a greater predictability of operating costs.

Yet the progressive specialization of resources of outsourcers, as the only way to afford the requirements of the market, has begun to change the costs of these companies. Naturally, the maintenance of high standards of quality is not compatible with cheap resources. Increasingly, the outsourcers begin to use more expensive and qualified resources, which results from the increase in costs of provision.<sup>62</sup> Business expansion, the opening of new markets and the increasing specialization are obvious advantages for companies of outsourcing. Accordingly, where the firm requires specialized resources not available internally, the outsourced company can carry out its supply of immediate and temporary manner, according to the necessities. Undoubtedly, it would be more time consuming and expensive to carry out directly the hiring of these resources on the market, still running the risk of their possible

---

<sup>57</sup> For more related aspects to outsourcing offshoring, see, Chapter I, section 1 and 4.

<sup>58</sup> Contractor, F. J., Kumar, V., Kundu, S. K., & Pedersen, T. (2010), "Reconceptualizing the firm in a world of outsourcing and offshoring: The organizational and geographical relocation of high-value company functions", *Journal of Management Studies*, pp.1428-1431.

<sup>59</sup> Amiti, M., & Wei, S.-J., (2005), "Service offshoring, Productivity, and Employment: Evidence From the United States", *IMF Working Papers*, 05 (238).

<sup>60</sup> This issue has already been the subject of a public hearing in the European Parliament, Roethig, O. (2004), European Parliament, The Committee on Employment and Social Affairs. in: "Offshoring and outsourcing: impact on employment in Europe".

<sup>61</sup> Gareis, Robert, (2004), "Business Process Outsourcing under Sarbanes Oxley: Challenges and Complexities", Baker& McKenzie.

<sup>62</sup> See Chapter 1, section 3.

inadequacy to the desired function. In BPO the risk is on the supply side and this responsibility is expressly provided for in the contract.

With the transfer to third parties of non-core operational functions, the company may allocate resources to the development of their objective and focus on its core business. In the literature, it has been sustained that “(...) core activities are those that the firm performs better than any other company, needed to sustain the profitable operations and non-core activities, those that can easily be outsourced”.<sup>63</sup> Perhaps, there may be functions that today are considered strategic and as such, not subject to a decision to outsource.<sup>64</sup> However, in the near future they may become essential functions, very close to the core of the organization. The ability to make predictions about the future of the company and of the market is, of course, limited, which is why the decision to outsource risks ought to be considered. Moreover, the increase of productivity is highlighted as one of the advantages of outsourcing and in particular, the offshoring.<sup>65</sup> In fact, a company with outsourcers in various countries with different time zones provides functions and non-stop services.<sup>66</sup>

As was already discussed, outsourcing might be a downsizing ally. The disproportionate reduction of the organization, becoming almost empty, is one of the disadvantages. The company may reduce its permanent employees, becoming in extreme cases almost virtual, comprising only a small group of internal staff that manages a vast network of outsourcing contracts. This situation, by virtue of the loss of technological and human resources, might lead to the total loss of competitiveness of the organization. Nevertheless, there are cases of great success in almost “virtual” companies such as, Amazon or Benetton. The loss of control over functions and knowledge is also indicated as another disadvantage of decision of outsourcing.<sup>67</sup> On a regular basis, companies share information and expertise with the outsourcers and this may represent a risk. The outsourcers, increasingly robust, can become competitors of the organization. This situation “(...) worsens increasingly, with ongoing technological progress, which is reflected in the need to ensure the secrecy of the organization's procedures”.<sup>68</sup> Thus, it becomes mandatory to tacitly introduce an obligation of confidentiality for the outsourcer in contracts.

---

<sup>63</sup> Quinn, J. B., Hilmer, F. G. (1994), “*Strategic outsourcing*”, Sloan Management Review, 35, pp.43-55.

<sup>64</sup> *Id.*

<sup>65</sup> Kim, S. (2006), “*Legal Issues in Outsourcing: What Businesses Should Know*”, Rider University.

<sup>66</sup> This practice is known as blended outsourcing. See, Chapter1, section 4.

<sup>67</sup> Raassens, N. (2011), “*The Performance Implications of Outsourcing*”, Tilburg University.

<sup>68</sup> Vining, A. R., & Globerman, S. (1999), “*A conceptual framework for understanding the outsourcing decision*”.

Loss of control of functions or services, and the consequent increase in the importance of the supplier, are thus difficulties foreseeable in the renewal or contract renegotiations. Lastly, there is the tendency, on the part of outsourcers of subcontract services that were entrusted to him, by the client company. These cases usually stem from the need to divert resources for more important clients, the simple lack of responsiveness or sufficient knowledge to a good contractual implementation. Consequently, outsourcing companies subcontract other companies, often smaller in size and with higher quality standards. This subcontracting, often carried out without consulting the client company, leads to a drop in the level of quality and productivity loss by the outsourcer. This can lead to a complaint for contractual failure on the initiative of the client company, with the losses that arise. In order to preclude this situation, it must be previously specified in the contract between the parties, thus avoiding the possibility of subcontracting.

## **8. Outsourcing and Other Strategic Approaches**

Accounting for the distinction between outsourcing and joint venture is not an easy task. Several authors consider outsourcing to be a form of joint venture and others argue that the concepts are distinct. The concept of outsourcing entails a commercial agreement, between two or more persons, to pursue a single and defined project. The necessary elements are expressly set forth or implied in the agreement: the pursuit of the group for a common purpose, and the sharing of profits and losses and equal powers of each member in the direction of the project. Therefore, it is characterized as an association between two or more companies with the aim of development of an activity or business, which in isolation would not be possible. This association can take many forms, but all share the risks and profits between the various entities that integrate it. In the joint ventures, the profit is not necessarily the immediate objective. The objectives to be achieved within the joint venture may be the entry in a particular market, access to new technologies and so forth.

Among the possible issues related to joint venture, we will only address the one that relates to its legal form.

Thus we may find two possibilities: a) there are present only operational interactions, within a given period, based on the commitments involved in the agreement, without the creation of a specific legal entity (a corporate joint venture), and b) the organization may not have a legal entity, in other words, the need for equity interest does not arise (a non-corporate joint venture). In an outsourcing relationship companies always keep their own identity as well

as a legal and commercial independence leading to the thought that it is not possible to find a corporate outsourcing.

Despite the apparent proximity between the concepts of outsourcing and the non-corporate joint venture, the issue of independence justifies the differences between the two terms. The matter of the independence of the parties is manifested through the contract, and in respect of profits. Indeed, the profits of the outsourcer are the result of the supply activity. On the other hand, the profits of the contracting company are derived from its core business.<sup>69</sup> The outsourcing contract must “(...) declare unequivocally that the parties are independent of one another.”<sup>70</sup> Indeed, in the joint venture, the profits derive from the business unit created by the various integrated entities. However, another closer concept of a joint venture is the strategic alliance.<sup>71</sup> The distinction between the two is also the subject of controversy. Some authors sustain the strategic alliance is a form of joint venture, while others consider it to be an independent notion: “(...) I use the strategic alliance to encompass all forms of agreement between partners, and joint venture for those agreements that involve either the establishment of a new and independent company, joint ownership of the partners, or the minority ownership of one of the parties by one or more partners.”<sup>72</sup> The distinction is also relevant to the strategic alliance term, as well as for outsourcing, because this figure, as was already mentioned, does not admit the assumption of ownership by any of the companies on the other. At this point, it could be said that there is similarity between the figures that we analysed, even as differences prevail. There is a tendency to confuse the concept of outsourcing with apparent similar concepts. The origin of modern-day outsourcing lies in subcontract, joint ventures and strategic partnership. While much has been written about business management issues and outsourcing, very little has been written about legal and tax considerations in outsourcing. The development of subcontracting and the outsourcing is inserted in a broader movement, that is the development of contractual relations between the companies and their organizational structures. Therefore, understanding the characteristics that distinguish the concept of outsourcing of legal figure of the subcontract becomes relevant.

---

<sup>69</sup> Burnett, R. (2012), “Outsourcing IT - The Legal Aspects: Planning, Contracting, Managing and the Law”, (2nd ed.), Gower Publishing.

<sup>70</sup> *Id.*

<sup>71</sup> As association between companies, the strategic alliance seeks to agglomerate the synergies of the group that creates, which may include companies with differentiated activities or even companies that compete in the same market. Therefore, given the need for the enlargement of the market and growth of the organization, the decision to strategic alliance can enable the achievement of these objectives without the need for recourse to other decisions. Nevertheless, there are another possible paths that allow the pursuit of the same objectives, but are much more difficult and costly, as the merger or acquisition of companies

<sup>72</sup> Thompson, Jonh L., (1993), “*Strategic management*”, (5<sup>o</sup> ed), Cengage Learning Center.





## **Part II. The Legal Process of Outsourcing**





## 1. Comparison Between the Concepts of Subcontract and Outsourcing

There are similarities between these two concepts and in the fact some authors consider them to be as synonyms.<sup>73</sup> As we will explain later, we may face two scenarios with different characteristics. In the First Chapter, part 2, we saw a definition for the concept of outsourcing. In addition, here it is worth analysing the subcontract concept.

The European Union defines subcontracting as the situation that results from a contract concluded between a company called the “main contractor” and a company called the “subcontractor”.<sup>74</sup> Thus, it is agreed that in the implementation of another contract concluded between the “subcontractor” and a third party called “subcontracted”, which must deliver goods or provide services that the “subcontractor” must incorporate or use in or in overall deliveries that have been ordered by the main contractor. At the legal level, the “subcontracted party” is not a signatory of the contract concluded between the principal contractor and his “subcontractor”. Therefore, it is possible to observe a derivation and dependence on another previous consent of the same nature, which constitutes the basis or main agreement, and the results strictly have a correlation with the birth and contents of the second. In other words, it can be said that subcontracting occurs when the subcontractor concludes a contract with a third, without unlinking the corresponding usefulness to its contractual position. Such a legal relationship presupposes the existence of two contracts: the basic and the derivative.<sup>75</sup>

Departing from a broader definition of industrial subcontracting, it is designated as the operation whereby a company (contractor) entrusts to another (subcontractor) a certain task.<sup>76</sup> This is executed in accordance with a set of specifications or pre-established requirements, a part or the whole of acts of production of goods or certain specific operations.<sup>77</sup>

The OECD considers that two main forms of subcontracting exist: subcontracting of structural and cyclical or occasional. The structural subcontracting is reflected in the strategic

---

<sup>73</sup> Pizarro Nóbrega, S. (2010), “*O contrato de Outsourcing*” (1o ed.), Wolters Kluwer Portugal and Coimbra Editora, p.55 et sq.

<sup>74</sup> Community, E., (1983), 82/854/EEC: Council Decision of 10 December 1982 “*on the rules applicable, in the fields of export guarantees and finance for export, to certain subcontracts with parties in other Member States of the European Communities or in non-member countries*”, (L), p.2.

<sup>75</sup> Gomes, O., (2009), “*Contratos*” (26o ed.), Rio de Janeiro: Editora Forense, p.168.

<sup>76</sup> Marques Leitão Manuel, M., (1990), “*A subcontratação na comunidade económica europeia*”, Oficina do CES, Coimbra, p.2.

<sup>77</sup> However, there are several modalities of subcontracting according to various criteria, such as, among others, the distinction between subcontracting cyclical or structural, of capacity or skill, labor or production, domestic or international, with recipient determined or undetermined, among others. See: Europeias, C. das C. (1992), “*Guia Prático sobre os Aspectos Jurídicos da Subcontratação Industrial na Comunidade Europeia, Parte I*”, (Vol. I), Serviço das Publicações Oficiais das Comunidades Europeias, p.15.

decision by the company to call upon the expertise of other companies outside the group, in order to establish a permanent and regular relationship.<sup>78</sup>

While the cyclical or occasional subcontracting is the temporary employment of another company as a way to get goods and services that the first firm normally produces, but has momentarily stopped producing. Thus, it is done within certain conditions of the product and time limits previously agreed by the parties. It can be argued that this cyclical nature of subcontracting may correspond to what we define as outsourcing, which is the supply of goods and services produced before internally in the contracting company, differing only due to the occasional character mentioned above.

Outsourcing presupposes a lasting relationship, unlike subcontracting, where we observe contracts for the short and medium term. Through the simple comparative analysis of these definitions in relation to outsourcing, we can derive obvious differences.

First and foremost, it is possible to note that in the subcontract, unlike in outsourcing, we find two contractual relations. In fact, the subcontract assumes a contractual sequence, the main contract concluded between the “main contractor” and “subcontract” company, and the second contract concluded between the latter and “subcontracted” party, which is in charge of the implementation of the whole or part of the subject of the first contract.

Moreover, it can be inferred that this contract is an ancillary contract to the extent that it depends on a main contract, which in principle features the same content. In relation to the subject of the contract, there is an identity of the subject between the derived and main contracts, being that the scope of the subcontract cannot be wider than that of the base contract and is in fact usually more reduced.<sup>79</sup>

On the one hand, in outsourcing it is possible to verify the existence of a contract. On the other hand, the outsourcing company does not perform all or part of the subject of the contract, but usually certain functions or services before conducted internally at the firm.

Therefore, is possible to conclude that instead of two parties involved, as happens in the outsourcing contract, in subcontracting, we always find three intervening parties: the “main contractor”, the “subcontractor”, and the “subcontracted”.<sup>80</sup>

Regarding the characteristics and size of the companies involved, the subcontractors are often similar to those companies that outsource. Usually, these companies that subcontract are

---

<sup>78</sup> OECD, (2010), “*Measuring globalisation: OECD Handbook on Economic Globalisation Indicators*”, (2° ed.), pp.201-202.

<sup>79</sup> Martínez Romano, P., (1989), “*O Subcontrato*” (2o, 2006th ed.), Almedina, pp.95-101.

<sup>80</sup>*Id.*, pp.121-122.

smaller and less well equipped than the contracted companies have a large part of the time, more resources and technological means than the contracting firms.

The type of relation between the companies also differs. Outsourcing is described as being an immersive, deeply engaging relationship of partnership, between the contracting and the outsourcing company. In addition to providing human and technological resources, outsourcing also seeks to increase productivity as well as quality standards of the contracting company. Outsourcing firms also share the risks and benefits of the activity or process at stake. Therefore, the specialization of these companies enables efficiency in boosting the production of the contracting company.

In subcontracting, however, the subcontractor limits itself to making available its resources for the good contractual execution. In this case, the relationship is purely commercial, not involving any partnership. Thus, we see that the “main contractor” has no relationship with the “subcontracted” party, due to the intermediate contractual figure between them, the “subcontractor”.<sup>81</sup>

Some authors sustain that the difference between outsourcing and subcontracting relies on the transfer of control.<sup>82</sup> In subcontracts there is no transfer of control of the activity or process. The ownership of the business process remains with the “subcontract” company, which indicates and sorts the form as the service is to be provided. On the other hand, in outsourcing contracts, there is a transfer of control, whereby the contracted company exercises its activity with complete autonomy. The way the objectives are achieved is laid down in the contract, and the outsourcing company acquires full responsibility.

After this analysis, it is possible to identify differences that might be autonomous enough to consider two figures that have in common the fact that they are not normatively typified.<sup>83</sup>

---

<sup>81</sup> See, supra note 79.

<sup>82</sup> Tum, J., Norton, P., & Wright, J. N., (2006), “*Management of Event Operations*”, Event Management Series, Elsevier, p.120.

<sup>83</sup> In the current Portuguese Civil Code, the subcontract not merited typification as contractual form. The legislator has defined only two subcontracts, subleasing (Art.1060º) and subcontracting (Art.1213º, para. 1), not meaning that, by virtue of the application of the principle of contractual freedom, that there can be no other subcontracts.

## **1.1. Analysis of Subcontracting Concept in Light of Portuguese Law and that of Other Jurisdictions Within Existing Frameworks of Contract Types**

The objective of this research is not to develop specific issues of from one jurisdiction in particular. In order to provide some comparisons with other legal figures with which the outsourcing may have resemblances, it is relevant to make an analysis of the law. For that reason, we will undertake a comparison, taking as its point of departure the Portuguese legal framework, namely, the Portuguese Civil Code from Chapter IV to Chapter XIII.<sup>84</sup>

The Portuguese Civil Code does not treat the subcontract as an autonomous figure.<sup>85</sup> Therefore, it would be advantageous for the case law, and especially the doctrine, to concentrate on this figure in order to find the common elements needed to outline a structure, and perhaps drawn up a general theory of the subcontract.<sup>86</sup> With only a few exceptions, neither Portuguese nor foreign legal doctrine have shown themselves prone to admit the need to formulate a general theory of the subcontract. It has even been stated that despite many subcontracts presenting peculiar characteristics, the construction of a general category would be artificial and could not explain the true nature of the subcontract. Following this reasoning, we subsequently consider that each of the contractual figures should be studied separately, but that a total unitary study of the subcontract is not feasible. In recent years foreign researchers have written monographs on the subcontract, which exposes the need for the creation of an autonomous discipline.<sup>87</sup>

Actually, the fact that the outsourcing contract entails, in many cases, a provision of services, it does not, however, fall within the concept of contract for the provision of services, as established in article 1154<sup>o</sup> of the Civil Code. The contract for the provision of services is one in which a party undertakes to provide to the other certain result of her intellectual work or manual, with or without remuneration. The essential difference between the two figures lies in the compensation aspect. While in the contract for services there may or may not be retribution,

---

<sup>84</sup> See, pp.69-71.

<sup>85</sup> The same occurs in other diplomas of civil law, such as the Brazilian, Spanish, French, Italian, German and Swiss. See, supra note 80.

<sup>86</sup> In addition, there are certain specific aspects and effects which would involve themselves in itself an autonomous treatment with respect to the general theory of the subcontract. Moreover, also the possibility of relationship between subjects who are parties in different legal relations comes to demand the creation of a unitary discipline of the subcontract. Only this unitary discipline can explain the role of the intermediary in two relationships in which is part and, especially, the possibility of third parties, in particular some legal business, be sued by one of the parties in the contract on the basis of liability obligational relationship. Thus, it becomes necessary to seek the common denominators of subcontractual phenomenon. Both national and foreign doctrine does not have shown propensity to admit the need to formulate a general theory of the subcontract. See, supra note 80, p.18.

<sup>87</sup> See, supra note 79, p. 19.

in an outsourcing contract, there always exists a payment, due to the fact that it is an onerous contract.

The representation mandate and working contract or contracting agreement are, in accordance with article 1155° CC, two of the modalities of contract for the provision of services. The article 1157° CC tells us that the mandate is a contract by which a party undertakes to practice one or more legal acts for the account of another. The essential characteristics of this contract rely on the fact that the mandate has always as its object the practice of one or more legal acts, being that the legal act should be practiced, on account of the principal.<sup>88</sup> By taking into account the aforementioned, it is possible to find a fundamental difference, in other words, in the outsourcing contract the provider acts on his own account, and not on account of the contracting company.<sup>89</sup> As mentioned, the outsourcing contract is onerous and mandate representation presumed to be free of cost, implying costs only when practiced by a lawyer or solicitor.

The notion of contract is amended by article 1207° of CC and describes it as being a contract whereby one party agrees with the other to carry out certain work through a price. Moreover, it follows that in a works contract we are faced with the completion of a construction in a specific, previously determined space of time. The concept of completion of a work should be understood not only the construction or the creation, but also as the repair, modification or demolition of a thing.<sup>90</sup> In the outsourcing contract, the outsourcing company provides a specialized service that is not confused with this concept of work.

Another relevant aspect, it is related to the issue of autonomy. In a subcontract agreement, the “subcontracted” party has a certain degree of autonomy from the owner of the works that has hired him. On the other hand, the “subcontracted” party is also subject to respect for the rules of the art or profession, such as for architectural or engineering requirements, within the framework of the implementation of this work.<sup>i</sup> In an outsourcing relationship, this subjection is not found. Furthermore, another difference that can be observed is related to the price. As it is possible to observe in paragraph 2 of article 1211° CC, concerning the payment

---

<sup>88</sup> See, supra note 80, pp.33-36.

<sup>89</sup> Article 1178° of the Portuguese Civil Code entails this representation mandate aspect.

<sup>90</sup> In relation to the characterization of the works contract, see Menezes Leitão, L., (2008), “*Direito das Obrigações*”, Vol.3, (6a ed.), Almedina, pp.511 et seq.

<sup>90</sup> See, supra note 79, pp. 103-108.

of the price, or in paragraph 1 of article 1216° CC, concerning changes to the work, these consubstantiate considerable differences compared to the contract of outsourcing.<sup>91</sup>

In the current Civil Code, the subcontract has not merited a classification as contractual form. The legislation only defines two subcontracts, these being the sublease and subcontracting, in articles 1060° and 1213° CC, respectively. The subcontract may be qualified under Portuguese law as sale, performance of services, works or even as atypical contract or "mixed" that combines elements of other contracts. However, this does not mean that by virtue of the application of the principle of contractual freedom, that there can be no other subcontracts (article 405° CC paragraphs 1 and 2).

If we take into account the observed countries it is possible to see that the subcontract is not as such subject to a typical contract and named, lacking for this reason, a specific normative discipline.<sup>92</sup> In large percentage of European jurisdictions, subcontracting is regulated by the general rules of the respective Civil Code and the general laws of the contractual 'type' in that best fits, depending on the case in question.<sup>93</sup> After an analysis of some of the legal aspects of subcontract, present in some European jurisdictions, the situation described above is common to several jurisdictions.<sup>94</sup> Thus, the subcontract is governed by the general rules of the Civil Code and by the contractual 'type' that best fits depending on the cases, in particular, the provisions on the contract of sale, works, provision of services or even as atypical contract or "mixed" that combines elements of other contracts.

Nowadays, there are standard contracts on subcontract drawn up by business organizations or large companies, such as *Verband der Deutschen Automobilindustrie* (Union of German Companies in the automotive sector), but do not have great diffusion outside the sector to which they are related. Nevertheless, they tend to impose such contractual clauses to their subcontractors. Both parties may have interest in trying to conclude a written appropriate contract that governs the specific form and consensual fundamental aspects of their relationship. In the absence of a solution of this nature, the contract shall be governed in many cases, by general contractual clauses imposed by the other party. However, in its absence or in respect of

---

<sup>91</sup> This issue will be developed in the next topic.

<sup>92</sup> See, Europeias, C. das C., (1992), " *Guia Prático dos Aspectos Jurídicos da Subcontratação Industrial na Comunidade Europeia, Parte II*", (Vol. 292), Serviço das Publicações Oficiais das Comunidades Europeias.

<sup>93</sup> In line with the provisions of the relevant conventions, that the jurisdiction in question has ratified. See, supra note 94, p. 64.

<sup>94</sup> The jurisdictions covered in this practical guide are Germany, Belgium, Denmark, Spain, France, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal and United Kingdom, see, supra note 92.

aspects not covered by these general clauses, the legal standards of Civil Code of the jurisdiction at stake may be applied, but a relative uncertainty that can subsist in this respect.

Not only is the foreign subcontractor often forced to accept the general clauses, most of the time, established previously and in a manipulative way by the other party. This constitutes a further reason for which the foreign subcontractor may try always to safeguard, in any form, the possibility of negotiating a specific contract *ad hoc* to regulate the subcontracting relationship.<sup>95</sup>

All things considered, subcontracting is usually temporary and may involve, for instance, subcontracting with a third party to execute a relatively small project. On the other hand, outsourcing is usually permanent. It takes the form of the decision that a certain function is alien to the company's core activities, and the subsequent engagement in a contract with an outsourcing company to manage this function for them. Subcontracting is an older term, which traditionally refers to the practice of hiring an outside company or provider to perform specific parts of a business contract or project. Therefore, a company subcontracts another company to perform an activity which cannot be executed in-house. The "main contractor and the contracting" party throughout the project have a reasonable amount of control over the process. Outsourcing, however, involves contracting operations of specific business processes, with the aim of boosting production. Thus, there is a host of services or processes usually associated with marketing, legal services, bookkeeping, financial services, business consulting, logistics, innovation (R&D), human resources, payroll, data entry or call centres. Subcontracting and outsourcing are two operations management strategies that are intended to reinforce the operation of a company or business. However, they may have slight differences between them. Due to the demands of economic life, and the relations of force which determine the contractors and subcontractors, we are witnessing a trend toward the subcontracts being concluded without sometimes a real negotiation between the parties. However, these contracts acquire a pivotal position in relations between companies, because increasingly each clause must be analysed with accuracy. Before addressing the contract of outsourcing it is important to understand the legal issues in the outsourcing process, which may arise at each step of the process.

---

<sup>95</sup> See, supra note 92, p.30.



## 2. Stages of the Outsourcing Process

During the business process of outsourcing, several legal issues may arise at each phase of the outsourcing process. If they are not properly addressed, it can translate into a costly financial burden. It is frequently suggested in the literature that the accurate and timely analysis of the legal aspects of outsourcing, as well as a right contractual supplier selection avoids potential blockages and is half way to confidence in the success of the relationship.<sup>96</sup> In order to accomplish such, it is relevant to understand in which stage of the outsourcing process, which are the concerning legal aspects to take into account. Before drafting the contract, which is leading legal problem, it is necessary to evaluate all legal main matters involved.<sup>97</sup> However, there is a lack of literature regarding a description of the stages of the outsourcing process and the attached relevant legal aspects.<sup>98</sup>

The legal aspects of BPO could be approached in general, all over the world. In addition, these general considerations are not deemed to belong to a specific type of outsourcing or industry. In other words, they are suitable for any kind of BPO.

According to Perunovic et al., there are five stages in the outsourcing process: the preparation phase, vendor selection, transition, management relationship and reconsideration.<sup>99</sup>

Busser in his survey, that took into account a wide range of different outsourcing models from the current literature and commercial organizations, claims that every stage entails a division into key-activities.<sup>100</sup> Thus, in the preparation stage the activities that are implied might be the definition of the outsourcing strategy, definition of the supplier selection criteria and the screening of potential suppliers. The vendor selection stage involves the execution of a shortlist of potential suppliers, request for a proposal, choose the vendor, negotiation of the SLA and finalization of the contract. Subsequently, the transition stage requires the definition of the communication system between the parties, exchange of knowledge and information, transfer of assets, people, information, hardware and software, as well as, a description of the performance indicators and checklist. The fourth stage is connected with the management and maintenance of the relationship, performance monitoring and evaluation by use of benchmark

---

<sup>96</sup> Godfrey-Faussett, M., (1997), "Telecommunications *outsourcing - a legal perspective*", Computer Law and Security Review: The International Journal of Technology and Practice, 13 (3), p.176.

<sup>97</sup> It has been argued that the legal risks attached to the offshore outsourcing process are a legion. See, Duening T., Click R. (2005), "Essentials of business process outsourcing, *Essentials Series*", Volume 34, John Wiley & Sons, p.212.

<sup>98</sup> Busser, N. J. M. (2009), "Legal issues in the outsourcing process: *An overall perspective*", Universiteit van Tilburg, p.9.

<sup>99</sup> Perunovic Z., L. P. J. (2007), "Outsourcing Process and Theories", In POMS 18th Annual Conference, p.3.

<sup>100</sup> See, supra note 99, p.11.

data, relationship analysis, handling with meetings and communication. Lastly, in the reconsideration stage, the contract will be terminated or renegotiated.

Of course, each outsourcing model has slight differences, but there are commonalities among the several possible outsourcing processes.<sup>101</sup> Therefore, the legal aspects of outsourcing may also be approached in common.

### 3. Legal Issues

Godfrey argues that there exist four core categories of legal issues by outsourcing a process or activity: the physical assets, property, contracts and employees.<sup>102</sup>

Within the first category, physical assets, we can find the issue of due diligence. Due diligence entails a certain degree of caution and care.<sup>103</sup> Thus, due diligence translates into a procedure by which the eventual supplier examines all kinds of documentation related to the business which has to be outsourced, a research duty done by both parties. This careful procedure is carried out, in order to analyse all risks and threats connected with the business operation, as well as, quickly assess them and find a solution.<sup>104</sup> Thereby, it encompasses information regarding third party contracts, financial specificities, insurances, contractor issues, licenses and support agreements, leases, terms of employment and property rights.<sup>105</sup>

Godfrey sustains that the due diligence procedure varies in complexity and formality from business to business. Ideally, the process ought to be formally concluded, and subsequently gather all the information which the outsourcing company needs placed in a data room, even as only limited access to the senior management of the contractor.<sup>106</sup> On the other hand, this method is time consuming and may lead to an unintended certain precocious hostile environment between the parties. In order to circumvent this inconvenience, some formalities should be implemented, within the available time and resources, with the aim of enabling the supplier a sensible degree of access to the business and management of the department at stake.

---

<sup>101</sup> See, supra note 99.

<sup>102</sup> The importance given to each of the described categories might differ regarding the business at stake. See, supra note 98, p.8.

<sup>103</sup> See, supra note 97, pp.176-181.

<sup>104</sup> Burnett, R. (2012), "Outsourcing IT - The Legal Aspects: Planning, Contracting, Managing and the Law", (2nd ed.), Gower Publishing, p.19.

<sup>105</sup> In the cases, where assets were transferred becomes wise to perform a due diligence and contractually negotiate a warranties clause. See, supra note 97, p.177.

<sup>106</sup> Cf., *Id.*

Secondly, the property category is related to intellectual property aspects. Namely, the transfer, use, disclosure, protection and development of intellectual property are some of the major legal issues in BPO. It is known that there is an agreement on Trade Related Intellectual Property issues (TRIPs), under the auspices of GATT/WTO.<sup>107</sup> Therefore, the signatory members agreed to harmonize their intellectual property laws in a given agreed period frame. This convergence entailed a race to the bottom, due to the fact, that it is possible to observe several asymmetries regarding the level of intellectual property protection between countries.<sup>108</sup> The author or creator of an original work is the first owner of the work. The intellectual property in the work belongs to the employee while the company has the exclusive rights of using the work within two years of the creation of the work.<sup>109</sup>

In the event that a particular employee is being hired with the aim of creating technology, assistance and resources provided by the company, in such cases, it belongs to the contractor.<sup>110</sup> Due to certain requirements in the field of intellectual property law, an enterprise should clearly state in the outsourcing contract that it has the exclusive right to original work created by one of the employees. In the situation that a company possesses intellectual property, there are probably no obstacles to adopt these properties on the outsourcing contractual stipulations.

In contrast, if the company only holds an intellectual property due to a license, the scenario may be inverse, because a license agreement might not enable this. These incidents may be precluded if the due diligence is properly carried out. Accordingly, it is pertinent to mention also in this category the rights of third parties. There are circumstances in which the department in question has to be outsourced and is a subsidiary of a group or mother company.<sup>111</sup> Usually subsidiaries are supported by its group or mother company. Since the coming into force of the contracts (rights of third parties), which abolished the doctrine of privity of contract and allowed certain third parties to enforce a term of the contract, it may be advisable to note the interest of a certain third parties in particular clauses of the agreement.

---

<sup>107</sup> The TRIPS Agreement is Annex 1C of the Marrakesh Agreement, 1994.

<sup>108</sup> Siebeck, W. E., Evenson, R. E., Lesser, W., Braga, C. A. P., Lacey, R. M., & Heaver, R. (1990), "*Strengthening the Protection of Intellectual Property in Developing Countries, A Survey of the Literature*", No. 12, World Bank Discussion Papers, pp.69-87.

<sup>109</sup> Kennedy, G., & Clark, D. (2006), "Outsourcing to China – Risks and benefits", The Computer Law and Security Report, 22, p.253.

<sup>110</sup> A self-employed contractor or a consultant from an external agency or a freelancer engineer, in providing services to an organization, is not an employee of that organization. See supranote 108, p.105.

<sup>111</sup> See, supra note 98, p.19.

Thirdly, we have the category of contracts and an associated important annex document, the service level agreement.<sup>112</sup> The BPO long term relationship is governed by the contract and by the SLA. The SLA acquires two main objectives, namely to provide a clear definition of each party's obligations since day one, as well as, to enable the development of the relationship in time.<sup>113</sup> A service level agreement is intrinsic to the contract.<sup>114</sup> This agreement has a binding effect on both of the parties. Functionally speaking, it foresees and focuses on those issues which are more prone to rise and furnishes mechanisms for ensuring that the specifications at stake are actually accomplished. Moreover, there are two kinds of service-level agreements.<sup>115</sup> Thereby, the most common and core type is the guaranteed service agreement. Whenever a company is considering outsourcing a service or activity, the advisable service level translates into the guaranteed service agreement. Additionally, there is the guaranteed capacity agreement which may be applied when a certain proportion of assets will be used for the contractor, being the guaranteed capacity agreement.

In this document, the outsourcing company agrees to attain specific levels of execution. If these obligations are not accomplished, the SLA furnishes us with the several rights and remedies.<sup>116</sup> In practice, the service level agreement is one of the most negotiated outsourcing contract provisions. There are relevant aspects of the SLA that ought to be addressed in the first place. The first aspect is deemed with the establishment of what to measure, in other words, the definition of the service levels and key performance indicators to measure, like quality, capacity, and so forth. Once the SLA is agreed it is fundamental to state clearly the precise terms, variables and responsibility, in other words, it is relevant the planning for changes within the SLA, due to the fact that the buyer and the vendor need to anticipate that service levels may vary over time.<sup>117</sup> This acquires a major relevance and should be discussed and agreed due to changes that may occur regarding technology, regulation or economy.

---

<sup>112</sup> The SLA and the outsourcing contract will be addressed further on this research.

<sup>113</sup> Godfrey-Faussett, M., (1997), "Telecommunications *outsourcing - a legal perspective*", Computer Law and Security Review: The International Journal of Technology and Practice, 13 (3), p.178.

<sup>114</sup> Barrar P., G. R. (2006), "Global Outsourcing Strategies: An International Reference on Effective Outsourcing Relationships", Gower Publishing, p.235.

<sup>115</sup> Burnett, R. (2012), "Outsourcing IT - The Legal Aspects: Planning, Contracting, Managing and the Law", (2nd ed.), Gower Publishing, p.19, pp.231-232.

<sup>116</sup> Duening T., Click R. (2005), "*Essentials of business process outsourcing, Essentials Series*" Volume 34, John Wiley & Sons, pp. 135-171.

<sup>117</sup> Godfrey-Faussett distinguishes ten provisions that should be inscribed in the SLA. The remarks regard the description of the services which will dictate exactly what the user gets for its money; control of change that is guaranteed by an incorporated mechanism. In addition, with a pragmatic point of view, a dispute management clause that foresees to save time and reduce expenditure if a dispute arises; a liability provision that describes clearly the types of compensation and the ones whose the outsourcing company will not be liable in the case of a serious

An additional pertinent subject has to do with the liability of the parties within the contract. Within an outsourcing relationship the contractor is relying on an external party to perform a part of his business function entailing a risk acceptance. The SLA deals with predetermined or day-to-day failures of the supplier.<sup>118</sup> The parties could use service credits as a guarantee, but, in the case of more serious failures on the side of the supplier, the contractor may invoke some greater remedy against the outsource supplier than the payment of a service credit. Thus, the limitations of liability provisions acquire importance. The supplier will try to limit the scope of his liability.<sup>119</sup> However, if it happens that a supplier breaches in meeting its obligations by failing to perform, it enables the contractor to sue for damage up to the extent of his loss, even in the cases where the limitation of liability was not previously stipulated on the contract. It is important to specify in the contract the specific eventual types of loss during the relationship, and consequently, the ones that might be recoverable or non-recoverable.<sup>120</sup>

Another relevant issue, within contract category is the termination and exit provisions. Naturally, the outsourcing agreement ought to enable termination due to a breach of contract, or at the end of an agreed term. *A priori*, the termination may come from both parties.<sup>121</sup> On the one hand, the outsourcing company is entitled to end the outsourcing agreement whenever the user breaches its material obligations or in the case of insolvency. On the other hand, the contracting company is entitled to end the relationship when the outsourcing company breaches one of its material obligations, runs into specific financial difficulties, after a certain period of time or at a specific milestone on the payment of a fee. In addition, it is also entitled when there is a change in control or ownership of the supplier or in the event that there is a change in the nature of the supplier.<sup>122</sup>

---

failure on the commitment with the service provision. Thereby, it is fundamental a complete set of service level statements in order to ensure adequate methods of performance measurement acquire effect. Furthermore, it is advantageous to preview a rebate scheme in order to demonstrate the role of individual services in relation to each other and the relative severity of different pattern levels, as well as, the creation of a liquid damage regime, which can prove to be less expensive and time consuming. Lastly, it is wise to re-rendering termination and transfer of supplier, by describing both parties rights of termination regarding all legal matters. *See*, Godfrey-Faussett, M., (1997), "Telecommunications outsourcing - a legal perspective", *Computer Law and Security Review: The International Journal of Technology and Practice*, 13 (3), pp.177-181.

<sup>118</sup> *See*, supra note 116, p.238.

<sup>119</sup> *Id.*

<sup>120</sup> The first law enacted regarding control limitations of liability in the context of outsourcing agreements was the Unfair Contract Terms Act of the United Kingdom, in 1977 and may be characterized as being complex. *See*, supra note 116, pp.239-241.

<sup>121</sup> *See*, supra note 120, p.180.

<sup>122</sup> *Id.*

Usually, suppliers cannot end the contract because of the extreme cost, risk and disruption resulting to the buyer. Essentially, the outsourcing company may have the right to terminate the contract only due to the failure of the contracting party to pay the amounts owed to the supplier. When the parties have come to terms about the termination of the agreement, the contracting company might want to take services or activities back-sourced, as well as, can enter into a contract with another outsourcing company.<sup>123</sup>

If there is a termination of the contractual relationship due to one of the motives mentioned above, there are rights that should be taken into account, such as, the contracting party's need of information regarding the method of how the current services that are being supplied. As well as it is advisable to have a provision entailing the outsourcing company to assign important third party contracts either to the contracting company or to a new eventual supplier which is put in place, along with the option of acquisition of indispensable equipment being used by the outsourcing company. Along with what is mentioned above, the eventual acquisition of equipment, the contracting party might likewise request to solicit key employees. These exit specificities are agreed between the contractual parties, as also will be in line with the circumstances of termination.<sup>124</sup>

These commercial relations also involve legal issues which have to do with confidentiality. The outsourcing company will handle very sensitive information of its client, which might not deem to be automatically covered by law. In order to avoid the disclosure of confidential information, it is important to contractually stipulate this matter or by non-disclosure agreement.<sup>125</sup>

In addition, provisions regarding disaster recovery are commonly ignored<sup>126</sup>. However, it is fundamental to preview disaster recovery and business continuity strategies in the outsourcing contract.<sup>127</sup>

---

<sup>123</sup> Burnett, R. (2012), "Outsourcing IT - The Legal Aspects: Planning, Contracting, Managing and the Law", (2nd ed.), Gower Publishing, pp.171-187.

<sup>124</sup> See, supra note 120, pp.180-181.

<sup>125</sup> Whenever, the contracting party sends the potential outsourcing supplier a request for proposal, the suppliers are not obliged to regard the information as being confidential. It is strongly recommended to send the request of proposal in addition with a "non-disclosure Agreement", that previously has to be signed and then they can receive the request for proposal. See, supra note 123, pp.35-36.

<sup>126</sup> See, supra note 120, pp.168-169. Cf. also, Busser, N. J. M. (2009), "Legal issues in the outsourcing process: An overall perspective", Universiteit van Tilburg, p.25.

<sup>127</sup> The contracting company should consider these provisions with the company responsible for securing outsourcing, governing like this the terms and risks. Duening T., Click R. (2005), "Essentials of business process outsourcing, Essentials Series", Volume 34, John Wiley & Sons, p.220.

Last, but not least, there is an important behaviour that may help to overcome some of the outsourcing failures. In order to have an evolving and long term business relationship, there should be good and effective communication abilities, precluding simple problems from becoming complex ones.<sup>128</sup> Effective communication may be done through formal and informal mechanism.<sup>129</sup> Thus, it is important to stipulate in the agreement a project manager, in order to handle and, maintain, a continued relationship with all the involved parties, on a daily basis management of the BPO.

The fourth main category of legal aspects in BPO handles the transfer of employees. These contracts may involve the transfer of employees.<sup>130</sup> Usually, companies transfer a substantial amount of their employees in the affected area, to the outsourcing supplier, retaining only a small number of employees to communicate with the contractor. Thus, there is a reduction of employment in the contracting company, which is considered one of the biggest cost variables in service and manufacturing companies.<sup>131</sup>

However, this employment, reduction in the contracting company may entail risks for the outsourcing supplier, due to the fact that these employees have specific legal rights in several outsourcing situations.<sup>132</sup> Following this reasoning, it is significant for both contractual parties to obtain updated specialized employment law advice in order to ensure that the proper rules and assistance are provided. Within the EU, the Transfer of Undertakings Directive<sup>133</sup> automatically reinforces the rights of the employees, and entitles them to work under the same previous conditions, in the cases where a process or activity is outsourced or transferred.<sup>134</sup> Therefore, it is understood that the employee has the right of his or her employment to carry on the current terms and conditions, not being dismissed as a result of this process, as well as the right to know this change in the company will affect him or her. In the cases where this Directive does not apply, it is relevant to stipulate this protection in the contract.<sup>135</sup>

---

<sup>128</sup> See, supra note 123, pp. 126-157, 171.

<sup>129</sup> Barrar P., G. R. (2006), "*Global Outsourcing Strategies: An International Reference on Effective Outsourcing Relationships*", Gower Publishing, p.244.

<sup>130</sup> Sharpe, M. (1997), "*Outsourcing, Organizational Competitiveness, and Work*", Journal of Labor Research, XVIII (4), Springer-Verlag.

<sup>131</sup> See, supra note 129, pp.183-202.

<sup>132</sup> See, supra note 127, pp.83-100.

<sup>133</sup> The Directive 2001/23/EC on the Transfer of Undertakings protects the contracts of employment of people working in businesses that are transferred between owners. Moreover, it substituted the previous one known as the Acquired Rights Directive 77/187/EC.

<sup>134</sup> Burnett, R. (2012), "*Outsourcing IT - The Legal Aspects: Planning, Contracting, Managing and the Law*", (2nd ed.), Gower Publishing, p.87.

<sup>135</sup> The Directive 2001/23/EC is implemented in the United Kingdom by the "*Transfer of Undertakings and Protection of Employment Regulations*" (TUPE) regards offshore outsourcing transferences, outside EU are also caught by the TUPE, according to English courts. See,

As a consequence of all EU Directives, member states enact the requirements by implementing into the national legislation. Therefore, it is implemented into national laws in a variety of ways.<sup>136</sup> The Transfer of Undertakings Directive provides an EU legal framework designed to protect the employment rights of individuals impacted by a transfer of services, between companies.

This directive was designed with the purpose to protect the employment rights of workers impacted by a transfer of services.<sup>137</sup> This includes most European sourcing contracts, such as first generation outsourcing (client to service provider), second generation outsourcing (old service provider to a new service provider) and shared services (employee moves between subsidiaries). In circumstances where there is no identifiable group of employees servicing a client, as well as those in which there is an organised group of employees, but which does not run the services predominantly to one specific client, this Directive may not be applied. Nor does it apply to the contracts which entail a particular event or task of short-term duration, or to contracts which are exclusively or mostly concerned with the supply of goods to the client. The scope of application covers both public and private spheres whether or not engaged in economic activities, and to the employees' transferred due to a relevant business.

In accordance with article 3<sup>o</sup>, para. 1 of the Directive, “the rights and obligations of the transferor arising from a contract of employment or from an employment relationship previously established at the time of a transfer shall, due to that transfer, be transferred to the new transferee”.<sup>138</sup> Thus, “(...) the transferee shall continue to observe the terms and conditions agreed in any collective agreement on the same terms applicable to the transferor under that agreement, until the date of termination or expiry of the collective agreement or the entry into force or application of another collective agreement.”, in accordance with article 3<sup>o</sup>, para.3.<sup>139</sup>

---

Goodman, M., Robertson, N., Lambert, L. D., Goodman, M., Robertson, N., & Lambert, L. D. (2011), “*A Practical Guide for Global Employers: The European Rules on Dealing with Employees When Business Changes – Anticipating the Pitfalls, Mayer Brown Speakers*”, Mayer Brown.

<sup>136</sup> There are certain aspects which are determined under the aegis of the national employment framework, such as, employment rights.

<sup>137</sup> In line with the above mentioned directive, it is also important to take into account other European legislation. Thus, is relevant to consider the Directive 95/46/EC, regarding the protection of individuals with regard to the processing of personal data and on the free movement of such data. In addition, there is another Directive which assures that the employee is informed of how this change in the company will affect him, entitled as Directive 2002/14/EC “on establishing a general framework for informing and consulting employees in the European Community”, Official Journal of the European Communities, (L 80/29).

<sup>138</sup> Council Directive. (2001), Directive 2001/23/CE “on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses.” Official Journal of the European Communities, (L 82/16)..

<sup>139</sup> *Id.*



Nevertheless, there is some margin for member-states, regarding aspects of liability for the obligations applying before and after the transfer, and on some procedures adopted to ensure that the transferee is properly notified of all rights and obligations.

Regardless of that, these issues do not affect the rights or obligations themselves as it is possible to observe in article 3°, para.2.<sup>140</sup> In addition,“(...) old age, invalidity and survivor benefits beyond statutory social security schemes can be carved out of the above obligations, unless they apply to present or former employees immediately or prospectively entitled to such benefits” , thus excluding invalidity, following article 3°, para.4.<sup>141</sup> Regarding dismissals, the transfer itself cannot constitute grounds dismissing staff, dismissal by transferor or transferee. However,“(...) economic dismissals due to economic, technical or organizational causes requiring changes in the workforce may establish valid grounds for dismissal”, as per article 4°, para.1.<sup>142</sup> The Member-states may fix out specified groups of employees not protected from dismissal in national legislation. If the company is going through serious economic problems, special provisions might apply in relation to insolvency, such as, modified terms and conditions in order to safeguard the transferring entity’s subsistence. According to article 5°, para.3 “(...)”, provided that the situation is declared by a competent public authority, and open to judicial supervision (...)”, in accordance with the national legislation on the case.<sup>143</sup>

Another one of the obligations of the transferor, and the transferee is that they ought to inform the affected employees, regardless of whether they are represented by employee representatives, as well, information regarding the proposed date, reasons for the transfer and its implications for the affected employees. These are enshrined in Directive 2001/23/CE “*on the approximation of the laws of the Member States relating to the safeguarding of employees*” rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses<sup>144</sup>, as well as, in Directive 2002/14/EC establishing a general framework for informing and consulting employees in the European Community.<sup>145</sup> Moreover, in the circumstances that “(...) measures in relation to his employees, he shall consult the representatives of these employees in good time on such measures with a view to reaching an

---

<sup>140</sup> *Ibid.*

<sup>141</sup> *Ibid.*

<sup>142</sup> *Ibid.*

<sup>143</sup> *Ibid.*

<sup>144</sup> *Ibid.*

<sup>145</sup> European Parliament and of the Council. (2002). Directive 2002/14/EC “*Establishing a general framework for informing and consulting employees in the European Community*”, Official Journal of the European Communities, (L 80/29).

agreement.” following article 7°, para. 2<sup>146</sup>. Thus, these obligations apply whether or not it is a company controlling the employer, rather the employer itself, which is taking the decisions. According to article 7°, para.4 “(...) is it irrelevant whether some of these obligations are breached due to a lack of information provided by the controlling company”.<sup>147</sup>

On the one hand, if the employee transfer is managed poorly, other issues may arise. For example, the service might decline below the required service levels, thus triggering early service credits, additional exit and recruitment cost incurred. The existing staff may be disrupted, as well as, potential unfair dismissal proceedings. On the other hand, if the employee transfer is managed well, the employees are more prone to respond to well-managed and positive consultation, feedback and retention of employees’ knowledge that may improve the transition and service, lower attrition rates, and improved assimilation into the new service provider culture. Due to the reasons above mentioned, in order to manage the transfer properly, it is important to build the costs into the business case, especially be careful with liability issues and subsequently disputes that may arise. Subsequently, it is advisable to appoint resources to manage the employee transfer process, ensure that the key tasks and action dates are identified in a timely manner and added to the plans.<sup>148</sup>

Having said this, it becomes important to understand more deeply the contract of outsourcing and, as we have seen, the service level agreement (SLA).

---

<sup>146</sup> See, supra note 138.

<sup>147</sup> *Id.*

<sup>148</sup> See, supranote 145.

## 4. The Contract of Outsourcing

As we have seen in the first chapter of this research, due to the nowadays growing fierce competition in the markets, companies may feel the necessity of contracting external third-party suppliers. In order to focus on their core competencies they may enter into outsourcing contracts of certain activities or processes. Subsequently, they engage into long-term contracts. However, the contracts can involve several jurisdictions at the same time and be subject to those national laws. Therefore, these relationships became much more complex and more scattered in relation to its geographical location. As it will be developed here further, the parties may avoid certain legal constraints by negotiating and coming to terms about the governing clauses of the contract as well as, the provisions of the service-level agreement. In a relationship of outsourcing, the respective contract is the most relevant document. The clauses which will regulate the relation between the companies involved becomes thus, the cornerstone for the success of both.

### 4.1. Due Diligence

In a contractual efficiency perspective, we will depart from the principle that certain essential issues were hitherto established. In other words, not only the strategic decision of outsourcing is undoubtedly taken by management, as well as, the concrete needs of the company are determined with accuracy. Lastly, the outsourcing company is already chosen, after a careful selection.<sup>149</sup> Accordingly, prior to the choice of outsourcer company it is strongly recommended to perform a due diligence procedure.<sup>150</sup> In fact, we are handling the choice of a future partner in a relationship that involves the sharing of profits and risks.<sup>151</sup> Consequently, it is natural that the contracting company proceeds to a full audit to the outsourcing company, so as to know their financial capacity, their current and future commitments, guarantees provided, and other elements which could affect the business to celebrate. Otherwise, a failure or mistake in any one of these steps brings serious consequences to the expected result of a contract and the relations between the parties.

---

<sup>149</sup> Rippert, S., Weimer, K., Heeder, O., Lochmann, R., Weiss, S., & Llp, R. S. (2006), *“Outsourcing Handbook”* (1st ed.), Cross-border Handbooks, p.56.

<sup>150</sup> See, p.57, para.3.

<sup>151</sup> The partner term here should not be misunderstood with an eventual partnership relation or joint-venture that this outsourcing relationship may futurely evolve. This aspect will be further mentioned. Sparrow, E. (2003), *“Successful IT Outsourcing: from choosing a provider to managing the project”* (1st ed.), Springer-Verlag London, pp.105-106.

In a relationship of outsourcing a myriad of problems may arise, therefore, becomes extremely useful and beneficial to the negotiation of all clauses. This prior stipulation of several key provisions avoids eventual attrition between the parties, but of course it is utopian to predict all future situations.

#### **4.2. Balanced Relations**

As a result, it is important to avoid entering in a cycle of dependency, by considering the recruitment of more than one supplier, in order to increase the competitiveness, and quality of service provision. The option of a single outsourcing supplier often leads to the degradation of service provisions, the creation of routines and demotivation. Regarding the extension of contracts, the option for very long periods may create some problems. These obstacles to the eventual change of an outsourcing provider and might jeopardize the autonomy of the contracting company. Thus, the contracting company may feel reluctant to replace the provider, due to the fact of having to pay a contractual compensation.

In fact, the conclusion of contracts with minor duration terms, and the possibility of being automatically renewable, ensures greater freedom of the parties. Nevertheless, early termination clauses, and the measure of corresponding compensation are always indispensable. The communal problem in outsourcing contracts is related with an exaggerated dependence on the supplier, in particular in contracts concerning high technology products and technical expertise. Thus, acquires a major importance to contractually predict ways of reducing this dependence, as well as engaging into contracts with more than one outsourcing partner.

#### **4.3. Scope of the Agreement**

The scope of the contract acquires a major leading role in this relationship, containing several eventual services that are part of the contract. Due to the wide range of possibilities, these boundaries should be clearly and accurately set forth. Specially, in the circumstances where assets or employees are transferred, even more precision has to be put in place. Yet, there might be other services which were not clearly stated in the contract and might raise doubts regarding its coverage within the scope. The BPO raises a panoply of services complexities that can raise issues.

These complementary services cannot be implicitly assumed by the contracting company as part of the contract. Assuming that the clauses must be clearly established in precise

terms, as well as all related functions, it may not be reasonable to accept additional costs for the contracted company, which might lead to contract unprofitability.<sup>152</sup> The scope clauses should not be so broad as to preclude similar situations, which is why it is important to acknowledge that the scope immediately appears on an early stage, as part of the request for a proposal, in order to guarantee clear intentions. At a later stage, assets or other resources may also be disclosed in the contract in order to assess the entailed risks, although they are frequently omitted or disregarded by the parties. As a possible path to circumvent this scenario, the parties may resort to the stipulation of a clause making refers to these unidentified resources, in order to cover the issues that should have already been revealed, although having to bear additional costs.

It becomes vital to delimit the scope, in order to come to terms regarding the price of the contract.<sup>153</sup> Once the contract is signed, it probably will be difficult to change the scope without being subject to additional payments. By clearly expressing this aspect, naturally parties will try to narrow problems during the contractual term. In accordance with what is stated, the parties can also agree ramp-up clauses, regarding specific hours of the day with higher volume of service.<sup>154</sup> This again leads us to the thought that reliance on just one supplier should be avoided.

#### **4.4. Precise Terms**

In line with the delimitation of the scope of the contract, terms should be accurate, effective and the language should be intelligible to those who will be dealing with the outsourcing relation. The contract, as a regulatory element of relations between the companies, should not enable vague and imprecise interpretations of its clauses. All services or functions and how they should be performed, must be thoroughly detailed, always corresponding to the needs of the company and concrete capacities of outsourcer. As to the level of services, the contract should specify the parameters and procedures of measurement and tolerance levels. In the next topic will be addressed this relational flexibility. The desirable contractual balance implies a set of important procedures. Although often ignored, the pre-contractual phase is essential for the two companies, constituting a decisive step in order to reduce possible risks.

---

<sup>152</sup> Vagadia, B. (2007), "*Outsourcing to India- A Legal Handbook*", Springer-Verlag Berlin Heidelberg, p.81.

<sup>153</sup> Kim, S. (2006), "*Legal Issues in Outsourcing: What Businesses Should Know*", Rider University, p.2.

<sup>154</sup> Heinzl, A., Dibbern, J., & Hirschheim, R. (2006), "*Information Systems Outsourcing*", (2<sup>o</sup> ed.), Springer-Verlag berlin Heidelberg, p.143.

The drafting of service level agreement defines exactly the needs of the client company, and delimits the responsibility of the supplier. Moreover, it is fundamental to keep a close and transparent relationship between the two companies, aligning the objectives of both. Thus, the contract shall contain the clauses that regulate this joint management.<sup>155</sup> Therefore, interfaces that enable for reciprocal adaptation are required, and should be constituted by internal organs intended for their management, supervision and strategic decision-making.

#### **4.5. Ownership, Confidentiality of Data and Non-disclosure Agreements**

Often, and especially when engaging outsourcing contracts, companies need to make sure that they are effectively protected regarding the aspects of the business in question, namely substantial amounts of personal information of their customers and employees.<sup>156</sup> In order to protect this information it is important to acknowledge, if the eventual contracted party is compliant with relevant data protection laws. This information normally may comprise sensitive issues, as per purchasing records, social security numbers, financial data, payroll and benefits information, medical data and so forth. The outsourcing company has access to the customer's operations, to its core business, lists of clients, production processes, intellectual property, technologies, policies of quality, obtaining information on which should be hanging the secrecy and confidentiality. The supplier has access to the customer's operations, lists of clients, production processes, technologies, policies of quality, obtaining information, which should be under the tutelage of secrecy and confidentiality provisions

This provision entails certain specificities on the supplier side in order to attain the desired safeguarding of the information, being these restrict, monitor and record access to this information and enable such access only to key employees that have confidentiality provisions enforceable in the outsourcing company jurisdiction. Besides, a residual information clause may be considered due to the experience gained in the outsourced project by the outsourcing employee as well as the safeguarding of the contracting party IP rights.<sup>157</sup> However, the contracted company will try to limit this obligation period. In order to prevent these situations

---

<sup>155</sup> At this point it is important here to note that for the contracting company is required to define an internal communication plan. The outsourcing decision is not always to the liking of the company's employees. In the near future, it may cause the extinction of some jobs. Thus, the maintenance of an internal environment that does not harm the development of the outsourcing process is critical, which is why a clear and efficient internal communication policy will only bring benefits.

<sup>156</sup> See, pp.62-66.

<sup>157</sup> Vagadia, B. (2007), "Outsourcing to India- A Legal Handbook", (1st ed.), Springer-Verlag Berlin Heidelberg, p.129.

from emerging it is advisable to ensure separate agreements, regarding the jurisdiction in question.<sup>158</sup> Nevertheless, it is advisable to come to terms regarding confidentiality of information of third parties, such as the subcontractor, and as well previous written approval of the contracting company.

Currently, data protection demands a complete protection and it has been considered an important field of law due to the fact that comprises a person's right to control the circulation of his or her personal data.<sup>159</sup> In Europe, the EC Data Protection Directive sustains this position, by acknowledging the primordial importance of privacy, as a fundamental right and establishing a complete and reasonable legal framework.<sup>160</sup> Privacy rights in Asia, by contrast, have historically been more relaxed than those in Europe.<sup>161</sup> This framework enacts onerous burdensome agreed requirements on any person that gathers or processes information related to individuals, regarding information of a personal or professional nature. These requirements translate into several principles that embrace data subject right of access, proportionality and transparency principles. The directive also contains the legitimate basis, purpose limitation, data quality, data security and confidentiality, rectification, deletion and objection, restrictions on onwards transfers. Furthermore, we can observe an added protection where special categories of data and direct marketing are involved, and a prohibition on automated individual decisions.

As we have seen, not every jurisdiction provides the same level of protection. The Directive specifies that personal data may not be transferred to jurisdictions outside Europe that do not enable a reasonable level of protection for these information.<sup>162</sup> On the one hand, the European Union has enacted long standing stringent provisions that reduce the scope of the processing and transfer of personal information<sup>163</sup>, on the other hand, the United States has taken into consideration a more concentrated methodology, on that information that merely encompasses the processing that generates real harm to individuals.<sup>164</sup> Due to the variety of

---

<sup>158</sup> Rubin, H. (2007), "Supply-Side / Manufacturing Outsourcing — Strategies and Negotiations", *GeorgeTown Journal of International Law*, 38 (1948), p.727.

<sup>159</sup> See, supra note 157, p.146.

<sup>160</sup> European Parliament and of the Council. (1995), Directive 95/46/EC "on the protection of individuals with regard to the processing of personal data and on the free movement of such data", *Official Journal of the European Communities* (No L 281/31).

<sup>161</sup> See, supra note 157, p.122.

<sup>162</sup> *Id.*, p.147.

<sup>163</sup> Holcombe, J. K. (2005), "Outsourcing in the Service Sector: Using Mechanisms, and collective Organization as Building Blocks", *U. PA. Journal of Labor and Employment Law*, (December 2003), p.552.

<sup>164</sup> Kim, S. (2006), "Legal Issues in Outsourcing: What Businesses Should Know", *Rider University*, p.2., p.4.

levels of protection, among different countries, it is important to take into consideration where these information were collected which will entail the applicable laws to those. The concept of transfer comprises distinct circumstances, these being the physical movement of data to an eventual processor placed in different countries, remote access by the foreign processor placed in a different country, and thirdly remote access by the offshore processor to the data available in the jurisdiction where they were collected. Regardless of the place where the information is transferred, in an offshore relationship, the contracting company ought to evaluate the laws or the lack of these, in the contracted party jurisdiction. This might affect the information, as well as, can entail additional risks or benefits for the contracting company.

According to Rubin, there has been a remarkable movement by market known outsourcing companies which envisage a global harmonization in the processing of confidential information, due to the substantial differences of levels of protection provided by national laws.<sup>165</sup> The contracting company must consider the EU Data protection Directive enacts obligations on the data controller instead of the data processor.

In accordance with the Directive, personal data entails “(...) any information relating to an identified or identifiable natural person (‘data subject’), an identifiable person is one who can be identified, directly or indirectly, in particular by reference to an identification number or to one or more factors specific to his physical, physiological, mental, economic, cultural or social identity(...)”.<sup>166</sup> The large scope of this Directive is acknowledged for being very detailed and embraces the processing of personal information, which comprises the processes of obtaining, recording, storing, amending, retrieving, disclosing, and destroying the data. The applicability of this framework covers the processing of personal data stored in electronic files and the non-automatic files. Regarding the subset of sensitive personal data, this may entail additional measures.

As we have seen, there are two distinct figures that may hold the data nevertheless, being subject to different obligations. The data controllers (contracting company) can be individuals or entities that decide the reason underlying the processing and the way the data will be processed. The company which operates this treatment of the data is the data processor. This process must be fairly conducted, as a requirement of the framework. Moreover, in order to be cautious, the data might not be transferred outside the European Union, if that country

---

<sup>165</sup> See, supra note 158, p.726.

<sup>166</sup> Article 2<sup>o</sup>, a), European Parliament and of the Council. (1995), Directive 95/46/EC” *on the protection of individuals with regard to the processing of personal data and on the free movement of such data*”, Official Journal of the European Communities, (No L 281/31).



does not guarantee a reasonable degree of protection for the rights and freedoms to the related data subjects.

Although, in the circumstances that a company is considering outsourcing processing of data, firstly it becomes relevant to assess the legal criteria and inherent risk of the jurisdiction from or for which the company intends to transfer or provide access to data.<sup>167</sup> This evaluation consists of verifying if the country embraced OECD guidelines on the Protection of privacy and transborder flows of personal data<sup>168</sup> as well as their implementation, recognition of the general rule of law, more specifically the capacity of engaging and binding themselves under contracts, and lastly general or sector specific laws which tackle the processing of personal data.<sup>169</sup> By considering the aforementioned criteria, under the aegis of the European Directive there are lesser obligations on the data processor sphere. Following this reasoning, the advisability of contractually predicting the data processor obligations becomes clear, as does compliance with local laws of that jurisdiction, in accordance with the European Directive, when the latter is applicable.<sup>170</sup>

#### **4.6. IP Rights, Ownership and Third-Party Rights**

In the outsourcing agreement, intellectual property rights and inherent ownership constitute crucial concerns.<sup>171</sup> Naturally, the contract ought to state which party will retain the ownership of any IPR that might be used or developed by the outsourcing company during the relationship, as well as, who will own the outcomes or improvements. Therefore, the contracted party most of the time necessarily uses existing third party intellectual property rights, which might be licensed or provided under contract to the contracting company. Thus, it becomes indispensable to obtain authorisation from the third party owner before enabling access to the outsourcing company. Regarding the circumstances at stake, the contracting company may prefer the intellectual property rights to be assigned or novated to the contracted party, in order to give the control which is necessary to handle the service.

---

<sup>167</sup> Vagadia, B. (2007), "*Outsourcing to India- A Legal Handbook*", (1st ed.), Springer-Verlag Berlin Heidelberg, p.126.

<sup>168</sup> OECD (2013), "*The OECD Privacy Framework* ", (2nd ed.), OECD Publisher.

<sup>169</sup> See, supranote 163.

<sup>170</sup> The European Commission has approved three sets of standard contractual clauses as providing adequate protection to transfer individual's personal information. Thus, two types of model clauses relate to transferring personal information from one company to another company who will use it for its own purposes. Thirdly, there is another contractual model for transferring personal information to a processor acting under your instructions.

<sup>171</sup> See, pp.58-59.

Nevertheless, additional rights are stipulated during the outsourcing contract effectiveness, entailing that these return to the contracting company sphere or be transferred to the incoming third party outsourcer when the contract is terminated or expires. However, this ought to be specifically contractually agreed between the parties due to the fact that the contracting company may object to providing the solution to competitors. Thus, it becomes wise to carefully analyse all the patent rights repercussions, which cover entire processes, inventions and methods, in order to avoid certain circumstances. If a service provider secures a patent in inventions that it discovered, in the course of the contract, it could block the customer from using or improving inventions crucial to its business.<sup>172</sup> Due to these complexities regarding patents, several legal issues emerge as time elapses and the involvement in the business of the contracting party becomes greater, which may give rise to opportunistic behaviour as far as updates, termination and renewal pricing.

Intellectual property has the coverage of the law in a certain jurisdiction since it is registered properly there and contractually specified. Otherwise, litigation may arise. In relation to copyright ownership, the holder of it cannot transmit authorship to another party, although it may transfer some of the rights. As we have seen, these transfers need to be very precise and accurate to be monitored, as well as, record all changes that have occurred by way of only who acquires the ownership is entitled before the authorities and courts.<sup>173</sup> These should be laid down in contractual provisions, and the contracting party may assure that it has the right to make this transfer of the outsourcing company, as we have seen.

Generally, all EU countries ratified fundamental treaties, such as the Berne Convention or the WTO, in order to harmonize and raise the bar to ensure intellectual property protection.<sup>174</sup> As we have seen, patents need to be registered in the jurisdiction in question, in order to be covered by that law. In Europe it is possible to have full EU jurisdictions coverage, by proceeding to the register in the European Patent Office. But, any dispute that may arise should be launched in each of the countries. However, outside the European Union, for instance, in Asian countries, the enforcement of these laws is still developing, and therefore may not grant the same level of protection. Several IP matters may arise, and as we have seen in this research these compliance requirements must before be analysed carefully in the due diligence stage, in

---

<sup>172</sup>See, supranote 167, pp.138-139.

<sup>173</sup> Rippert, S., Weimer, K., Heeder, O., Lochmann, R., Weiss, S., & Llp, R. S. (2006), "*Outsourcing Handbook*" (1st ed.), Cross-border Handbooks, p.57.

<sup>174</sup> *Id.*

order to avoid enforcement of these rights which are characterized as being bureaucratic and time consuming.<sup>175</sup>

It is common to observe in the agreements, the obligation on the supplier side of making the necessary efforts to preserve the license's validity. In those circumstances, it is stated in the agreement that the contracted party might also possess IP rights in order to handle the services, has the duty to retain it till the end of the relationship.

But, if the contracted party is not entitled to a legal license, previously that should be licensed by the client, it may extend the liability, having thus the right to pursue an indemnification against the contracting company. Otherwise, the service provided is likely to suffer interferences due to attrition among the parties. If the outsourcing company does not come to terms with the contracting party, the license might be terminated.

In regards to trademarks, it ought to be established in the agreement how and to what end they may be used for, as a way to dodge the eventual loss of good will on the contracted party's behalf. Due to the myriad of risks that ascend when the contracted party becomes deeply involved in the business of the contracting company, such as access to patented innovations, sensitive information, trade secrets, it acquires a major role to be sure that the IP level of protection has the same strength, as in the contracting company sphere.<sup>176</sup> Accordingly, as we have seen becomes fundamental to settle down a provision that does not able the possibility of misuse, and the restriction to provide it to other competitors or a sub-license to a third party without previous consent.

The origin of modern day outsourcing lies in subcontracting, joint ventures and strategic partnership. As we have already mentioned in this research, the deep knowledge that the contracting party has about the client business, this relationship may evolve, and acquire another contours.<sup>177</sup> Here, the true meaning of the concept of partnership acquires substance, while the meaning that has been given along this research is the connection among the business parties, also known as being a kind of partnership. This joint development of intellectual property with the outsourcing company permits at the same time, the provision of the requested service. Within this possibility, the agreement needs to clearly recognize who will retain the ownership of the intellectual property rights, the allocation of rights. In addition, a narrow

---

<sup>175</sup> Kim, S. (2006), "Legal Issues in Outsourcing: What Businesses Should Know", Rider University, pp.3-4.

<sup>176</sup> Heinzl, A., Dibbern, J., & Hirschheim, R. (2006), "Information Systems Outsourcing", (2<sup>o</sup> ed.), Springer-Verlag berlin Heidelberg, pp.145-146.

<sup>177</sup> See, pp.42-44.

definition of this joint foreground technology as well as, the allocation of costs in the agreement needs to be agreed due to the hypothetical need to join in a lawsuit.

Regularly, the contracting company retains ownership, by imposing to the service provider to assign such IP to the former, which can be subject to pay supplementary payments for the stated assignment of the intellectual property rights. The methods and provisions regarding the payment should be accurately established in the agreement.

On the other hand, each of them could be co-owner of the IP and split the eventual income, earned through the licensing the IP to a third party.<sup>178</sup> These possibilities emerge, sounding as a fair and reasonable solution, to the issue that IP leads almost necessarily to a deep relation between the parties. This joint development may be fruitful for both, due to the fact that there was a common contribution in this relationship.

Despite the widely held presumption that both co-owners might together use trade secrets in their business and make an effort to protect from an eventual leak, a joint IP ownership in an offshoring transaction is a pledge of unforeseen outcomes and conflicting rules that can arise in each type of IP. However, according to Rubin the experience proves that these relations result, by taking into account that wide license rights are secured to both.<sup>179</sup>

From the contracting company's perspective, there might be the wrong perception that will have a better control. This is gained in the management of the joint venture relation and how it is conceived. While joint ventures, in an outsourcing context, strengthen the principle of partnership, they aim to entail a strategic alliance relation. Nevertheless, some complexities may appear on exit due to the joint venture structure.<sup>180</sup> By evolving the outsourcing relation to a joint venture, exists a stronger tendency to sensitive IP services being safeguarded exists, for the reason that the share of risks it may be sustained that the costs of commercialization with outsourcing partners can help to maximize the return on IT investments and at the same time allows to focus on its core business (contracting company).

This may constitute an advantage for one of the parties, but for the other, it may not be and may be faced in a situation that needs almost to accept so, in order to keep that business.<sup>181</sup> The advantages translate into obtaining equity investment for the venture, an access to the other

---

<sup>178</sup> Kobayashi-Hillary, M. (2004), "*Outsourcing to India: The offshore advantage*" (1st ed.), Springer-Verlag berlin Heidelberg, New York, pp.97-104.

<sup>179</sup> Rubin, H. (2007), "*Supply-Side / Manufacturing Outsourcing — Strategies and Negotiations*", *GeorgeTown Journal of International Law*, 38 (1948), pp.723-726.

<sup>180</sup> Kluwer, W. (2008), "*Outsourcing Contract Structures*", *International Outsourcing Law and Practice*, (May 2008), pp.8-13.

<sup>181</sup> *Id.*

party technology and a business opportunity may be here found, as the basis is to provide services to other customers.<sup>182</sup> However, not only will it require more management time due to the complexities, but also appeal to senior management attention as these investments frequently require a different decision making process and joint ventures can be seen as being more strategic than operational.<sup>183</sup> Hence, within joint venture contract relation, there is more likelihood to enhance relational effect, by reducing the risk of opportunism between the parties. As we have seen, by putting them on a parity position regarding the risks incurred it will incentive a common effort that outputs gains.<sup>184</sup>

Naturally, there are other possible contract types<sup>185</sup>, but in accordance with the survey of Oshri et al. survey, when used as a stand-alone contract, a joint venture contract enlarges the positive effect of the quality of the client-supplier relationships on the ability to achieve strategic innovation by being positive and significant.<sup>186</sup>

#### **4.7. Price**

Normally there are issues associated with the fixed price service levels, also known as “lump sum amount”. The price mechanism can be calculated in numerous possibilities, and the ability to adapt to the new rules of the market and technological innovations are just some of them.

The contracting company is interested in obtaining maximum success in their business, through the use of a company of outsourcing. This objective should be achieved with maximum quality of service and lowest price. However, the contracted party may have a different perspective.<sup>187</sup> Their concern has to do with the maintenance of the customer and with the need to guarantee the return of the investment made. As we have seen the supplier might attempt to avoid the financial penalties which may arise from failure of the SLA, either of their failure to meet contractual objectives. As mentioned, the price acquires a great importance in the

---

<sup>182</sup> Ibid.

<sup>183</sup> Oshri, I., Kotlarsky, J., & Gerbasi, A. (2015), “*Strategic innovation through outsourcing: The role of relational and contractual governance*”, *Journal of Strategic Information Systems*, 24 (3), p.212.

<sup>184</sup> Sparrow, E. (2003), “*Successful IT Outsourcing: from choosing a provider to managing the project*”, (1st ed.), Springer-Verlag London, p.212.

<sup>185</sup> See, supra note 180, p.205.

<sup>186</sup> See, supra note 183, pp.204-215.

<sup>187</sup> Sparrow, E. (2003), “*Successful IT Outsourcing: from choosing a provider to managing the project*”, (1st ed.), Springer-Verlag London., pp.39-60.

outsourcing contract, constituting a concern for the parties. Obtaining a fair price implies the observation of some procedures. According to Vagadia, it becomes essential to understand and forecast of reasonable manner the internal costs of the business process, its current status and as probably will be at the end of the contract.<sup>188</sup> Nevertheless, relevant data on costs may be received, from independent sources, as other organizations, business data for benchmarking and comparable proposals of more than one supplier, and may thus contribute to the establishment of a fair market price. On the one hand, a price which is better than the current operations and reasonable from the market point of view, is certainly a good price. On the other hand, these outsourcing contracts may seem costly, but if the idea is to negotiate in order to obtain the lowest price, it may harm the interests of the contracting company.<sup>189</sup>

The outsourcing contracts are essentially based on the models of fixed price and cost plus.<sup>190</sup> In this latter model, the supplier indicates a price for the volumes or services agreed, charging additional values where production increases compared to the objective laid down in the contract. There are other models of pricing used in this type of contract.<sup>191</sup> Thus, it is possible to establish a price per unit, where the price corresponds to a unit of service, which increases depending on the services requested and provided. The underlying reasoning has to do with the fact that the supplier is limited to specific, and punctual needs of the client company, being seen as a reduced investment. Furthermore, if we observe the model price on the basis of incentive, also known as cost plus incentive fee, the contracting company seeks to encourage the supplier to maintain high levels of production.<sup>192</sup> Similarly, in the results participation method, or gainsharing, the contracted party receives part of profits that helped to generate.<sup>193</sup> In addition, other models can be considered, such as, the price indexed to the real costs, in which the supplier is reimbursed for the actual costs, be they direct or indirect.<sup>194</sup> As a last price method approach, the parties may opt for the use of a price evolution mechanism, as a function

---

<sup>188</sup> Vagadia, B. (2007), *"Outsourcing to India- A Legal Handbook"*, (1st ed.), Springer-Verlag Berlin Heidelberg, p.81.

<sup>189</sup> Regarding exchange rate fluctuations and their financial burden, see, Weiss, R. M., & Azaran, A. (2007), *"Outward Bound: Considering the Business and Legal Implications of International Outsourcing"*, Georgetown Journal of International Law, 38 (3), 735, p.745.

<sup>190</sup> See, Heinzl, A., Dibbern, J., & Hirschheim, R. (2006), *"Information Systems Outsourcing"*, (2<sup>o</sup> ed.). Springer-Verlag Berlin Heidelberg, p.144.

<sup>191</sup> Rubin, H. (2007), *"Supply-Side / Manufacturing Outsourcing — Strategies and Negotiations"*, Georgetown Journal of International Law, 38 (1948), p.722.

<sup>192</sup> See, supra note 180, p.82.

<sup>193</sup> Id.

<sup>194</sup> Kobayashi-Hillary, M. (2004), *"Outsourcing to India: The offshore advantage"* (1st ed.), Springer-Verlag Berlin Heidelberg, New York, pp.182-183.

of the increase in production costs and their own evolution of contract, which can comprise, for example the provision of new services.

Despite these pricing options, the contract may also provide for the development of the price through its indexing, for instance, the rate of inflation. Some contracts may include a benchmarking clause or competitive comparison, ensuring the periodic amendment of the price, by allowing a comparison with the average value practiced by similar companies, in the market.<sup>195</sup> Broadly speaking, if the results of benchmarking revealed that the prices, in similar contracts exceed a margin previously defined in the contract (3% or 5%), the price laid down in the contract is automatically adjusted, regarding the same values. Through the introduction of this clause, there is the guarantee of attaining competitive prices, especially in situations of increased competition between several outsourcers. The clause also provides a more effective protection in times of crisis in the markets.<sup>196</sup> Therefore, the assessments and revaluations that are carried out during the contract's term of validity constitute the only way that the contracting company has to ascertain the competitiveness of established price, and the agreed service levels. In the event of certain changes in the market, that may translate into the business and its objectives may become obsolete as well as, some of the initial contractual provisions.

#### **4.8. Liability**

The already mentioned precise terms, and scope of the services need to be established, in order to allocate the obligations and inherent risks, between the parties, in the outsourcing agreement. This matter is subject to intense negotiations due to the fact often property rights are also involved and there is a wide range of risks associated with the business. The rights related to property are asserted between the parties. Some of the risks that the outsourcing relationship entails are related to project overruns, consumption of certain resources, operational risk, low service performances or incomplete services. Subsequently, this gives rise to unforeseen indirect and direct costs. In addition, it also bears the risks associated with confidentiality before competitors, due to the transfers of employees, eventual breaches of

---

<sup>195</sup> This could be defined by the International Benchmarking Clearinghouse (IBC), a member-based nonprofit organization, based in Texas, U.S.A. Besides, has been characterized by having a systematic and continuous process of measurement and comparison of practices of an organization with those who are world leaders, to obtain information that may help to improve its level of performance. Thus, this is a technique of observation and adaptation of the best practices of the best companies in the marketplace.

<sup>196</sup> Sparrow, E. (2003), "*Successful IT Outsourcing: from choosing a provider to managing the project*" (1st ed.), Springer-Verlag London, pp.87-89.

security, compliance with legal and regulatory risks, and circumstances considered force majeure.

Nonetheless, it is advisable to consider provisions regarding situations such as mergers and acquisitions, changes in control, and so forth. In order to ensure that the outsourcing company can afford eventual damages arising from the contractual relation, it becomes advisable to analyse certain protections. Therefore, it may be requested to the contracted party to be entitled to an insurance, to also warrant a continuation of the services.<sup>197</sup>

The parties may consider including in the contract limited liability through the establishment of ceilings regarding direct damages. In order to liquidate damages it is very common to find provisions of service credits.<sup>198</sup> However, these normally do not cover all the costs, because they aim to be focusing and enforceable, but there are exceptions. The parties will try to exclude consequential damages. But, subsequently, there are indemnification provisions, on which each party can rely.

In accordance with the above, there are disclaimers and other warranties, but there are also circumstances for which a party will not want to handle the responsibilities. Disclaimers are necessarily embraced in the contract, however, it is relevant to take into account the warranty and indemnity clauses.<sup>199</sup> In practice, the contracted party proposes and advises the contracting company, after having access to the documentation or files. The contracting party will require precision on the reports, data of any performance indicators, and results of action. Nevertheless, there is the likelihood of trying to assure that the operations or system are completely shielded or error-free. This is a difficult provision to establish in contracts involving technology, due to the fact that the parties need to be acquainted with a margin of error, and this ought to be clearly included in the SLA.

Normally, the main indemnities are mutual and it is wise to have some flexibility. However, as stated above<sup>200</sup>, the establishment of maximum ceilings or the possibility to preclude indirect, punitive or consequential damages tendentially narrows the scope of infringement or wrongdoing clauses, but there are serious risks that should be considered.<sup>201</sup> If a negligence provision is excluded or restricted, it will only be reliable if it has been integrated

---

<sup>197</sup> See, supra note 188, pp.87-89.

<sup>198</sup> See, p.60, para.2.

<sup>199</sup> Kim, S. (2006), "Legal Issues in Outsourcing: What Businesses Should Know", Rider University, p.3.

<sup>200</sup> Vagadia, B. (2007), "Outsourcing to India- A Legal Handbook" (1st ed.), Springer-Verlag Berlin Heidelberg, p.77.

<sup>201</sup> Rubin, H. (2007), "Supply-Side / Manufacturing Outsourcing — Strategies And Negotiations", *GeorgeTown Journal of International Law*, 38 (1948), p.720.



in the contract.<sup>202</sup> When there is a certain imbalance, it has to be considered if it is in accordance with the national laws, in question, in the case of submitting to court appreciation. This is controversial, in situations where the only certainty is that consequences exist, and damages stays in a nebulous area.<sup>203</sup> There are also other aspects that influence the allocation and limitation of liability<sup>204</sup>, such as the parties' bargaining power, eventual competition, variety of exceptions and so forth.<sup>205</sup>

Generally, mutual indemnities embrace complaints by transferred employees regarding labour issues, whose responsibility lies with the contracting party if these arise before to an eventual transfer. As we have seen before, the outsourcing company has the responsibility for the complaints, of their selection of transferred employees, concerning acts or omissions in their selection of transferred employees. Moreover, it is advisable to assure liability allocation of equipment leases, software licenses and other contracts that are transferred to the contracted party. In line with the aforementioned, the contracted party is liable in relation to breaches of patents, non-disclosure of sensitive information, copyrights or other IP rights and laws.<sup>206</sup> Nevertheless, other indemnities may be considered or required by the parties,<sup>207</sup> and the penalties incorporated in the contract.<sup>208</sup> Thus, this enables the contracting party to claim compensation without the burden of proving the occurrence. Regardless of these damages surpass the ceiling of the contractual corresponding penalty, usually is handled in accordance with the penalty provision.<sup>209</sup>

Within this context, it is also worth emphasizing the subcontracting provisions.<sup>210</sup> The contracting party needs to be diligent, by establishing it in the agreement. Conversely, in these circumstances, the contracted party is likely to be liable for eventual acts and omissions of all these subcontractors. In addition, the contracting party may have the possibility of being considered a recipient third party, in order to be safeguarded from collateral contracts.

---

<sup>202</sup> Rippert, S., Weimer, K., Heeder, O., Lochmann, R., Weiss, S., & Llp, R. S. (2006), "*Outsourcing Handbook*" (1st ed.), Cross-border Handbooks, p.64.

<sup>203</sup> See, supra note 201, p.729.

<sup>204</sup> Heinzl, A., Dibbern, J., & Hirschheim, R. (2006), "*Information Systems Outsourcing*" (2o ed.), Springer-Verlag Berlin Heidelberg, p.149.

<sup>205</sup> See, supra note 201, p.728.

<sup>206</sup> Id.

<sup>207</sup> See, supra note 200, p.77.

<sup>208</sup> See, supra note 202, p.62.

<sup>209</sup> See, supra note 200, pp.104-109.

<sup>210</sup> See, pp.48-55.

Within the liability sphere, it becomes also relevant to address precise *force majeure* clauses. The scope of this clause might comprise the exclusion of liability, acts or omissions related to improbable scenarios outside the control of the parties, but their risk needs to be recognized and managed.<sup>211</sup> Companies by engaging in these costly relationships, usually try to avoid the burden of potential costs related to losing the service.<sup>212</sup> As we saw in the first chapter of this research, frequently most contracted outsourcing companies are located in less developed countries. It becomes fundamental to settle down certain events that may occur, such as governmental acts, foreseeable accidents, acts of nature, unusual situations outside the control of both parties.<sup>213</sup>

Within this range of possibilities, some are more probable than others. It is advisable to separate them into sections, regarding its degree of predictability as well as, their respective management enforcement procedure, in order to continue to provide the stipulated services.<sup>214</sup> An outsourcing contract can be terminated due to breach, frustration, and failure of performance.<sup>215</sup> As we have already above referred, despite these clauses be precisely defined, some opportunist behaviour may arise in relation to trying to exclude or restrict liability.

#### **4.9. Exclusivity and Non-Compete Clauses**

Certain values, such as confidentiality and exclusivity should constitute contractual commitments. Certain values such as exclusivity, may be questionable. The ideal would be to prevent the contracted part, from performing the same task for a competitor of the contracting company. Nowadays, the outsourcing companies may become eventual competitors, and the contracting party will attempt to circumvent, by trying to enforce non-compete clauses<sup>216</sup>, in relation to his current, as well as, probable clients during and after the termination of this outsourcing relationship.<sup>217</sup>

However, these provisions may not be enforceable under several national laws, by the fact of being considered a barrier to trade. Thus, it becomes relevant to comply with the national laws,

---

<sup>211</sup> See, pp.59-60.

<sup>212</sup> Hanson, A. (2016), "*Legal Process Outsourcing To India: So Hot Right Now!*", SMU Law Review, 62, pp.1907-1912.

<sup>213</sup> Kim, S. (2006), "*Legal Issues in Outsourcing: What Businesses Should Know*", Rider University, p.3.

<sup>214</sup> See, pp.66-67.

<sup>215</sup> Vagadia, B. (2007), "*Outsourcing to India- A Legal Handbook*" (1st ed.), Springer-Verlag Berlin Heidelberg, pp.73-74.

<sup>216</sup> *Id.*, pp.119.

<sup>217</sup> Heinzl, A., Dibbern, J., & Hirschheim, R. (2006), "*Information Systems Outsourcing*" (2o ed.), Springer-Verlag berlin Heidelberg, p.148.

regarding non-disclosure of information on IP, and protection of ownership. Furthermore, this acquires relevance by enabling post contractual protection, assuring at least some rights.<sup>218</sup>

#### **4.10. Communication**

The resorting to comparative studies with other companies, or benchmarking, becomes essential to update the contract concluded. These evaluations and the possibility of recruitment, by the client organization of a specialized company for this purpose, must be included in the contract of outsourcing. Thus, the conduct of audits, the promotion of meetings and the sending of periodic reports, also contributes either to the strengthen of relations, as well as, for the resolution of minor conflicts that may arise.<sup>219</sup>

In accordance with Sparrow, it is important that frequent communication should be maintained, even when things are going well.<sup>220</sup> The degree maturity of the relationship is not only achieved through problem solving, but also by planning eventual opportunities, and good performances need to be recognized. All relationships have their apogee, which emerged from effective communication.

The clauses relating to the obligation to provide information and advice, on the suppliers' behalf are equally important. The contracted party, as a specialized company, must permanently advise the client to choose the most rational and efficient procedure. On the other hand, the supplier may not fulfil these duties and obligations without the support of the customer, the latter will assume contractually have the duty to collaborate with the supplier. The communication between the two companies contributes significantly to the success of the relationship. The means of communication used, regardless of the type, as well as the forms of transmission of data should be specifically contained in the contract, thus ensuring their compatibility and a good contractual execution. In accordance with the aforementioned, it is important to invest in effective outsourcing governance, accurately organize the procedures, in the relationship between the parties, decision-making processes and the means of communication. Otherwise, it will not be easy to ensure the success of a contract for outsourcing.

---

<sup>218</sup> Rubin, H. (2007), "*Supply-Side / Manufacturing Outsourcing — Strategies and Negotiations*", *GeorgeTown Journal of International Law*, 38 (1948), pp.727-728.

<sup>219</sup> *See*, p.59.

<sup>220</sup> Sparrow, E. (2003), "*Successful IT Outsourcing: from choosing a provider to managing the project*" (1st ed.), Springer-Verlag London, p.106.

The use of a skilled outsourcing management team makes the business more prone to have an effective and profitable relationship, to evaluate and advise on the opportunities, risks and service level performance. Therefore, three phases can be distinguished, namely transaction management, governance, performance and quality management. The transition management is lengthy and needs to be smooth, as it may contribute to the success of the contract. Besides, this involves detailed, desk-level know-how, documents and files, for instance regarding technology, employees, functions and so forth.<sup>221</sup> Secondly, governance stage is characterized by a communication, continuous process that contributes to the development of the services. In addition, there is an evaluation of the risks, issuing of timely reports, which assess the enforcement resorting to indicators and collaboration. Thus, through the monitoring of the outsourcing company, it is possible reviewing service levels and relationship management.<sup>222</sup> As we have seen, this contributes to the boost of a partnership-style relationships with high levels of trust and commitment. Nevertheless, sometimes there is a lack of contractual and relational flexibility, fundamental for the maintenance and progress of the business.<sup>223</sup>

#### **4.11. Termination and Exit**

The possibility of the production return to the internal scope of the company or be transferred to another supplier, in the event of contractual failure or the term of the contract, shall appear in the clauses of the contract, thus making it technically feasible. In addition, to the possible termination reasons alluded above, it becomes relevant to recall other common causes. This may comprise provisions such as, change in control, insolvency, financial problems, either party going out of business, merger and acquisitions, material breach of one of the parties, and expiration of the contractual term or disputes.

This clause of reversibility, in contracts involving IT services acquires even more emphasis. This safeguard aims to ensure the contracting company, the possibility of transfer back in-house or for other outsourcing company solutions developed, otherwise, the production of the company may cease. The contract shall contain all the procedures considered essential to the transfer, such as, the conditions and the technical means, the human resources involved and

---

<sup>221</sup> See, supra note 220, pp.107-108.

<sup>222</sup> Kobayashi-Hillary, M. (2004), *“Outsourcing to India: The offshore advantage”* (1st ed.), Springer-Verlag berlin Heidelberg, New York, pp.160-161.

<sup>223</sup> Kern, T., & Willcocks, L. (2000), *“Exploring information technology outsourcing relationships: theory and practice”*, The Journal of Strategic Information Systems, 9 (4), pp.10-11.

the deadlines for the implementation of the transfer.<sup>224</sup> The form of avoiding unforeseen situations is also fundamental, entailing the cause of existence of these clauses of hardship, allowing any of the parties to require the opening of new negotiations, whenever an event of economic or technological nature, seriously affects the balance of benefits.<sup>225</sup> As we have seen, it is advisable to address this in contract provisions. Due to the reason that these contracts are costly and lengthy, the contracting party will probably try to narrow the termination options of the outsourcing company.<sup>226</sup>

Generally, outsourcing agreements are characterized by certain unpredictability.<sup>227</sup> As we have seen in this research<sup>228</sup>, the outsourcing agreement needs to establish specific procedures that will be orderly put in place, after the respective termination cause. These may entail the return of materials, assets to the contrary party or purchasing right, license duties and other obligations, non-compete issues, and might even contain an automatic renewal provision.<sup>229</sup> If the contractual relationship is not renewed, the services will be transferred back in-house or to another outsourcing company.<sup>230</sup> Thus, it becomes advisable to clearly establish the supplementary transition services, in order to attain this assistance, in each respective termination cause. Along with the aforementioned, the definition of the duration and amount of services<sup>231</sup>, aspects of confidentiality, assets, third party contracts, licenses, employees and costs should also be foreseen.<sup>232</sup>

---

<sup>224</sup> Weiss, R. M., & Azaran, A. (2007), "*Outward Bound: Considering the Business and Legal Implications of International Outsourcing*", Georgetown Journal of International Law, 38 (3), 735, p.746.

<sup>225</sup> Heinzl, A., Dibbern, J., & Hirschheim, R. (2006), "*Information Systems Outsourcing*" (2o ed.), Springer-Verlag Berlin Heidelberg, p.151.

<sup>226</sup> Kim, S. (2006), "*Legal Issues in Outsourcing: What Businesses Should Know*", Rider University, p.4.

<sup>227</sup> Geis, G. S. (2006), "*Business outsourcing and the agency cost problem*", Notre Dame Law Review, 82 (3), 955, pp.994-1002.

<sup>228</sup> See, p. 59.

<sup>229</sup> See, supra note 225, p.151.

<sup>230</sup> Rubin, H. (2007), "*Supply-Side / Manufacturing Outsourcing — Strategies And Negotiations*", Georgetown Journal of International Law, 38 (1948), pp.732-734.

<sup>231</sup> See, supranote 225, p.150.

<sup>232</sup> See, supra note 230, p.733.

#### 4.12. The Choice of Law and Jurisdiction

In order to easily overcome some problems that may arise during the relationship, the parties should establish an escalating method of solving disputes. This method avoids litigation and almost certain disruptions in the transactions. Only after the application of this resolution process should the parties think about other options available. This procedure is agreed to by the parties, such as time periods of the comprised steps when service level performances are not reached, reports, problem solving within a certain period and the intervention of the parties. Before resorting to arbitration, it is wise to resort to this procedure.

The contracts of outsourcing most of the time involve eventual conflicts of laws. Therefore, if we are handling multijurisdictional contracts, it will increase company liability issues.<sup>233</sup> On the other hand, International Treaties can acquire a relevant role, regarding the protection of rights eventual, due to the fact that the judicial systems may be completely different, lengthy and expensive. The contractual aspects that can be caught under the national laws of the contracted company may be related labour laws, liability laws, and competition and IP rights.<sup>234</sup>

As the literature mentions, arbitration may entail costs and time similar to that provoked by litigation in courts.<sup>235</sup> In accordance with the Rome Convention, European companies can choose their contracts applicable law.<sup>236</sup> There are a few alternative dispute resolution mechanisms, being arbitration, the most resorted practice, however, it is recommended to stipulate into a contract provision.<sup>237</sup> As we have already seen, there are contractual aspects that will fall under national laws of the contracted party jurisdiction. Thus, arbitration is a private procedure, which entails a binding decision given by an impartial third party, after hearing both contractual parties.<sup>238</sup> Therefore, if this procedure is launched, the parties cannot demand the

---

<sup>233</sup> See, supra note 225, p.155.

<sup>234</sup> See, supra note 230, p.730.

<sup>235</sup> Weiss, R. M., & Azaran, A. (2007), "Outward Bound: Considering the Business and Legal Implications of International Outsourcing", *Georgetown Journal of International Law*, 38 (3), 735, p.751.

<sup>236</sup> in: <http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=URISERV:l33109&from=PT>. (last time consulted: 13/04/2016).

<sup>237</sup> Heinzl, A., Dibbern, J., & Hirschheim, R. (2006), "Information Systems Outsourcing" (2o ed.), Springer-Verlag berlin Heidelberg, p.153.

<sup>238</sup> Rubin, H. (2007), "Supply-Side / Manufacturing Outsourcing — Strategies And Negotiations", *GeorgeTown Journal of International Law*, 38 (1948), p.731.

agreement in court<sup>239</sup>, except in the circumstances provided by law.<sup>240</sup> Furthermore, the arbitration awards are difficult to appeal successfully, so it may be cautious to establish additional clauses, thus limiting the arbitrary eventual decision and define that arbitration should follow the contractual terms.<sup>241</sup> Currently, several countries have ratified the New York Convention and the Geneva Convention, arbitral awards became final and binding on the parties and persons claiming under them.<sup>242</sup> <sup>243</sup> In addition, has the advantage of enabling to enforce the award in a third jurisdiction.<sup>244</sup> The party jeopardized party may enforce this award in any jurisdiction, where the assets or properties are placed, provided that these awards are enforceable against that party, in any country that has ratified the Convention.<sup>245</sup> Through this procedure is easier to avoid litigation in a domestic dispute as well as, mitigate some risks associated. In practice, more outsourcing relationships reach the termination phase for non-fault reasons, than for contract breach-based termination.<sup>246</sup> Although, it may be difficult to contractually predict every single situation, it is important to take all these above considerations into account, in order ensure more legal certainty and try to avoid eventual budget overruns, which can involve expensive amounts.

## **5. Legal Perspective of the Outsourcing Contract Under the Portuguese Civil Code**

As we have already stated, the objective of this research is not bonded with the deepening of the specific issues of the legal body, from one jurisdiction in particular.<sup>247</sup> However, due to the resemblances of the outsourcing concept with other legal figures, again, these references are thus carried out. Therefore, it is established this comparison taking as point

---

<sup>239</sup> This is only permissible for the competent state court, if the parties have expressly provided for such a possibility in the arbitration agreement. The state court may have to intervene in arbitration, however, it should be regarded as exceptional. In these cases, it refers to matters that the parties may not submit to the arbitrators of knowledge or only by state intervention can be resolved.

<sup>240</sup> Sparrow, E. (2003), "*Successful IT Outsourcing: from choosing a provider to managing the project*", (1st ed.), Springer-Verlag London, pp.219-225.

<sup>241</sup> See, supra note 235.

<sup>242</sup> This is important to take into account at the due diligence stage.

<sup>243</sup> *Id.*

<sup>244</sup> See, supra note 235, p.752.

<sup>245</sup> Outsourcing Law Group (2014), "Practice Guide on Exit Services in Outsourcing", p.3.

<sup>246</sup> *Id.*

<sup>247</sup> See, pp.49-53.

of departure the Portuguese legal framework, namely, since Chapter IV until the provisions of Chapter XIII of the Portuguese Civil Code.<sup>248</sup>

From a legal standpoint, first of all we can say that we are facing an atypical contract, due to the fact that it may not be typified in the law, as a discipline itself. This scenario might be observed in several jurisdictions. The outsourcing contract is also a mixed type of contract, as it is a combination of elements of other contracts. Para.2 of the article 405°CC refers to this type of contracts implicitly, because the parties can gather in the same contract provisions of two or more contracts, total or partially regulated by law. Thus, in the contract of outsourcing, we find characteristic elements of other contractually identified figures in law, as the leasing (art. 1022°), the works contracts (Art.1207°) and the provision of services (art. 1154°). As mixed contract it combines to two or more obligations, corresponding to the other party, a singular obligation, due to the fact that the contracting company is responsible for the payment of the price, while the outsourcing company necessarily has to accomplish several duties.

In relation to the structure of the business, the contract of outsourcing is bilateral or synallagmatic, insofar as emerging obligations for both parties. The cause or existing synallagma is functional, the reciprocity is manifested and reveals during the life of the contract. Moreover, given that, from the outsourcing contract emerge several obligations for both parties, it is considered an onerous contract. It might not be observed a perfect objective balance or absolute economic consideration of the benefits. As a general rule, here the importance is given to the subjective equivalence, meaning that matches the assessment or the desire of the contracting parties. As an onerous contract it is also commutative, for the reason that at the moment of its celebration the parties have the certainty of their duties and advantages of both. Regarding its formation, it is characterized for being not a formal contract, not solemn or consensual, since it is not subject to any form prescribed by law. In this type of contracts, the contracting party can express according to their will, counting to do that with a minimum of clarity. In accordance with Art.219° of CC, the validity of the declaration does not depend on the observance of special negotiation form, except when it is stated in the law. It follows that the perfection of the contract is reached only by simple agreement of wills, in line with the principle of consensus. This is further characterized by being the main contract, because it is not dependent on any other contract, thus having an autonomous existence. In relation to the execution of the contract over time, the contract of outsourcing is a contract of continuous

---

<sup>248</sup> See, pp.31-37.



implementation, in virtue of the parties being attached to the compliance with continuing obligations, during a certain period of time or contractual duration. The contract which we analyse is recognized as being *intuit personae*, due to the fact that the outsourcing company specific characteristics are a decisive element, in order to engage in a contractual relationship. For this reason, the contracted party becomes the causal element of the contract.

The para.1 of article 227° states that both during the negotiation of the contract as well as, the preliminary stage, the process ought to be carried out according to the rules of good faith, under penalty of responding to damage that culpably caused to the other party. The outsourcing contract is still subject to the binding force principle. In paragraph 1 of art. 406° of CC it is stated that the contract should be punctually accomplished, and can only be modified or be extinguished by mutual consent of the contracting parties, and in the cases established by law. Following this reasoning, the post-contractual responsibility also acquires special significance. In an outsourcing contract certain obligations or duties remain after the contractual relationship extinction. The Civil Code does not specifically address the post contractual liability. Nevertheless, but does make the connection with the good faith principle. In addition to Art.227° above mentioned, we can still relate it to Article 239° concerning the integration of the declaration of negotiating, which provides that in the absence of a special provision, the negotiating declaration must be integrated in harmony with the desire that the parties would have had if they had provided for the point missing, in accordance with the good faith. The paragraph 2 of Art. 762° also states that in the compliance with the obligation, as well as, in the exercise of the corresponding duty, should the parties to proceed in good faith. Thus good faith, refers to primary obligations or typical specificities of the obligation, accessory duties of conduct either by the side of the debtor, either by the side of the creditor. We can therefore conclude, that the post-contractual liability is a consequence of the omission of the respect of the principle of good faith. The violation of this principle, stems for its author the duty of compensation derived from the conduct of one of the parties, after the termination of the contract.

Frequently, the outsourcing contracts involving multinational companies are drafted in accordance with the parties will, being commonly introduced an arbitration clause, in order to circumvent some obstacles probably inherent, when different jurisdictions are in question. However, as we have already seen there are certain legal issues which are normally under the tutelage of the outsourcing company jurisdiction, in the event of the parties do not come to terms regarding a certain provision, this contract can be subject to court interpretation and

appreciation.<sup>249</sup> Therefore, the spirit of the law and underlying principles could be a good cornerstone and articulated for drafting the outsourcing contract.

## 6. The Service Level Agreement

Throughout this work, we have repeatedly discussed the service level agreement, acknowledging its high importance in the context of contract of outsourcing, as an indispensable annex document.<sup>250</sup> It is recognized by being formal and containing all the parameters and responsibilities which relate to the supplier, whatever the subject of the contract in question. In order to contribute to a good implementation or contractual success, the requirements formulated by the parties are contained in the agreement. Alongside with SLA, there is the possibility of drafting a SWO, also known as operational level agreement, which details the obligations of the contracting party before the contracted party. In the perspective of an outsourcing company, it is a document of great usefulness due to the already mentioned fact, which the excellence in the fulfilment of the contract of outsourcing depends not only of one of the parties involved, but both parties as partners in this business.<sup>251</sup> An SLA is not a document that contains all aspects, nor is it a contract of outsourcing. The service-level translates into a detailed memorandum that specifies the expected results of many elements of the function in outsourcing.<sup>252</sup>

This document contains the definition of minimum requirements, the performance and quality of the provision of the service or supply of the product, and here lies the essentiality of this agreement. Without it the provision of services or activities would fluctuate between the mere execution, and partial or definitive failure. This latter scenario would place us closer to other types of contracts, where the partnership, essential to outsourcing, is not so obvious. The SLA reflects the expectations of each of the parties, the contractual object and also contains the commitments agreed upon between customer and supplier. Thus, the above mentioned had its origins in the concrete needs of the contracting company, the capabilities of the contracted party, as well as the aggregate costs. Therefore, this agreement provides a very explicit description of goods or services to be executed, as well as, certain indexes which should be

---

<sup>249</sup> See, p.88, para.1.

<sup>250</sup> See, pp.59-60.

<sup>251</sup> Kavaleff, A. (2005), “*Successful Outsourcing through Proactive Contracting – Strategy, Risk Assessment and Implementation*”, in *Managing Contracts and Risks*, Stockholm Institute for Scandinavian Law, p.12.

<sup>252</sup> Pizarro Nóbrega, S. (2010), “*O contrato de Outsourcing*”, (1o ed.), Wolters Kluwer Portugal e Coimbra Editora, p.67.

attained so that the commitments are effectively met. At least, the SLA should include, in addition to, the exact description of the services of the supplier the already referred periods of time, in which the service will be delivered, the expected quality of service, and the ways to measure of performance.<sup>253</sup>

We are therefore faced, with a management tool of contracting party expectations, as well as, an instrument to measure the implementation capacity of the outsourcing company. Through it is possible to manage the quality and quantity of the services rendered, which measures by themselves the service level, being that the quality is of even greater importance. In addition to these aspects, this agreement embodies an important means of communication between the parties, as an instrument of prevention of future conflicts, by having clearly describing the rights and obligations of the parties. Due to an intrinsic connection to the business, to its opportunity and its adequacy in the market, the SLA can never be a set of rules with fixed procedures. It is a document subject to changes and revisions, adjusting the levels of performance to the current reality of the business. If this relational and contractual flexibility is not considered, the needs of the contracting company and the efforts of the contracted party easily will no longer match.<sup>254</sup>

Following this reasoning, we conclude that the SLA transforms the outsourcing contract into a contract by objectives, with direct influence on the remuneration of the supplier. The contracting company determines the limits of its claim, which must be fixed with adequate reasonableness, being that the achievement of a value below the objective fixed may imply a smaller payment. Conversely, obtaining a value above that objective can reflect a payment plus. For this reason, the contracted company will tend to fully comply with the objectives settled down in the SLA, or even, to overcome them.<sup>255</sup>

In accordance with the above mentioned, these objectives are integrated by concepts such as the quantity and quality of the service provided. These are constantly measured by the contracting company. For this purpose measuring instruments are used, by graduating the supplier performance. Nevertheless, these parameters for service level measurements depend on the type of the services in question.<sup>256</sup> Therefore, there are various possibilities of key

---

<sup>253</sup> Sparrow, E. (2003), *“Successful IT Outsourcing: from choosing a provider to managing the project”*, (1st ed.), Springer-Verlag London, pp.146-159.

<sup>254</sup> Robertson, C. B. (2011), *“A Collaborative Model of Offshore Legal Outsourcing”*, Arizona State Law Journal, 617, pp.42-46.

<sup>255</sup> See, supra note 258.

<sup>256</sup> Heinzl, A., Dibbern, J., & Hirschheim, R. (2006), *“Information Systems Outsourcing”* (2o ed.), Springer-Verlag berlin Heidelberg, p.143.

performance indicators (KPI) and key quality indicators (KQI).<sup>257</sup> The former has to do with the actual performance of the service, in other words, quantifiable measurements used to determine the efficiency and effectiveness of the service. The latter is related to the overall quality of service rendered felt by the contracting company, having regard to the vital elements conditioners of success for a negotiation strategy. These indicators of measurement acquire an essential role in the development of the outsourcing contract. Nevertheless, they are also essential all the procedures for monitoring the performance of the supplier. The implementation of mechanisms that provide for the issuance of service level reporting is important, both as a means of communication between the parties, either as a means of checking the desired effectiveness.

Besides, this document ought to mention all the penalties in the event of failure of the foreseen objectives, or the incentives, in cases in which the established targets as objective are overcome. In the event of repeated failure to meet the objectives, it may involve the contract renegotiation, or even the possibility of the contracting company claiming the payment of compensatory allowances. In this last case, we are faced with a penalty clause inserted in the SLA, which once established with reasonableness, safeguards the contracting company of losses arising from contractual failure. As we have already seen the service level agreement has a relevant role along the relationship of outsourcing, as a parallel contract document. In accordance with Goo J., Kishore R. et al., the specific features of the SLAs impact relational governance in information technology outsourcing relations.<sup>258</sup> Naturally, this also applies to other types of services.

According to Mayer et al., incomplete contracting encourages the literature to view formal and relational contracts as complement for one another, particularly when we are dealing with IT outsourcing contracts, which are necessarily incomplete.<sup>259</sup>

Thereby, it could be said that relational governance brings up the relevance of the implementation of commitments, possibilities, and prospects that arise through trust and social empathy. A substantial part of empirical work has verified that relational governance upgrades

---

<sup>257</sup> Kobayashi-Hillary, M. (2004), "Outsourcing to India: *The offshore advantage*" (1st ed.), Springer-Verlag berlin Heidelberg, New York, pp.193-196.

<sup>258</sup> Goo, J., Kishore, R., Rao, H. R., & Kichan, N. (2009), "*The Role of Service Level Agreements in Relational Management of Information Technology*", Management Information Systems Research Center, 33 (1), p.119.

<sup>259</sup> Mayer, K. J., and Argyres, N. S. (2004), "*Learning to Contract: Evidence from the Personal Computer Industry*", Organization Science (15:4), pp.394-410.

the performance of interorganisational exchanges in broad-spectrum.<sup>260</sup> In particular, in contracts involving IT outsourcing, as well as, the inherent function that commitment, mutual dependence, trust, and relational norms have in the sustenance of exchange relationships. A social business environment of trust, and collaboration will reduce the risk of contractual opportunist behaviour scenarios and other eventual exposure situations that may arise. Besides, the parties are probably more safeguarded in relation to situations that might not have been contractually foreseen.

Practitioners commonly refer that the answer to successful management in IT outsourcing relations is achieved by the use of formal and comprehensive SLAs that define specifically the levels to meet business objectives.<sup>261</sup> According to Poppo and Zenger, the relationship entails a dynamic complementary relationship regarding a formal contract and relational governance.<sup>262</sup> They argue that a clear, and precise drafted outsourcing contract as well as, the respective SLA may lead to longer, collaborative and trust and commitment exchange interactions. Besides, Goo J., Kishore R. et al. widen the vision promulgated by Poppo and Zenger that formal contracts and relational governance function as complements, instead than substitutes. Therefore, a lack of well-developed contracts leads to erroneous conclusions pertaining to the value of SLAs in promoting relational governance, and in managing successful outsourcing relationships.<sup>263</sup>

Due to the rarely mentioned myriad of legal issues on this study, it is possible to observe that even if the parties are accurate regarding settling down all the relevant provisions in the contract, and subsequently the service performance aspects in the SLA, many times the aimed objectives and relationship fails.

---

<sup>260</sup> See, supra note 258, p.121.

<sup>261</sup> Id.

<sup>262</sup> Poppo, L. and Zenger, T. (2002), “*Do Formal Contracts and Relational Governance Function as Substitutes or Complements?*”, *Strategic Management Journal* (23:8), pp. 707-725.

<sup>263</sup> See, supra note 256, p.140.

## 7. Common Issues Arising in an Outsourcing Contractual Relationship (or Possible Failure Reasons)

Presently, the recourse to the business process of outsourcing, by the transfer of processes or activities to an external party, especially those related to technology, IP, high-end functions, innovation, logistic operations and so forth, have a beneficial impact on companies, which translates into more efficiency. International companies are resorting more and more to this management tool. However, this is a process which is very complex and has a long-term duration, requiring some hard and soft skills in the relationship. The costs of this operation may be seen as high, but the key value associated relies also on the ability of the contracting companies to concentrate on their core competences. Sometimes, companies try to achieve lowest costs and that might not constitute an advantage. Regardless of the parties trying to achieve complete contracts and SLAs, and might appear that there is no margin to failure, yet outsourcing efforts continue to fail.<sup>264</sup> Perhaps, the objectives<sup>265</sup> of contract may not have been set down clearly.<sup>266</sup> As we have seen, due to the multijurisdictional relationships, the parties may include an arbitration clause in the contract.<sup>267</sup> Therefore, this is proven by the reason that disputes between contracting companies and suppliers in outsourcing arrangements, barely reach the court rooms.<sup>268</sup>

As we saw in the beginning of this chapter, outsourcing is distinct from subcontracting, due to usually embrace transferred activities or processes, that were previously done in-house, but it may not be the case.<sup>269</sup> This may raise the likelihood dismissals of employees. However, it might not be the wisest solution, since the company is engaging into a contract, in order to take some burden outside his scope by transferring to a third party, and this will make it less prone to reap the benefits of the added value of being able to concentrate on their primordial target. Another outcome of the above seen, is a certain stress and inefficiencies between the company employees', in the event of ambiguity in their internal communications, that needs to be avoided by assuring awareness in the workplace.

---

<sup>264</sup> Sparrow, E. (2003), *Successful IT Outsourcing: from choosing a provider to managing the project*, (1st ed.), Springer-Verlag London, p.195.

<sup>265</sup> Barthélemy, J. (2003), *The seven deadly sins of outsourcing*, Academy of Management Executive, 17 (2), p.90.

<sup>266</sup> Prinsley, M. (2007), *The Importance of Clear Drafting in Outsourcing Arrangements*, Mayer Brown Publications, pp.1-2.

<sup>267</sup> See, pp.87-88.

<sup>268</sup> *Id.*

<sup>269</sup> See, pp.23-25 and 48-55.

In what regards communication, there are circumstances in which the parties' expectations are not very well defined and aligned, which may give rise to additional costs, and deficiencies in the service provided.<sup>270</sup> Here, the SLA has a major role entailing the service level performance benchmarks and all the specificities that impact the relationship, on pace with the outsourcing contract. If the aim is to have a successful business, it is also important to concisely explain and make sure that the contracted party understands business's needs.<sup>271</sup> Thus, the foundations for the relation may be seeded.<sup>272</sup> Within this context, it is also incumbent to refer that multijurisdictional relations involve differences, regarding to transition of processes, language, technical terms or limitations, and additional costs can emerge. As we have seen above, it is recommended that businesses agree upon the use of an outsourcing management team in order to handle with this relation.<sup>273</sup> This team is responsible for planning accurately all aspects and eventual asset transference. Even more, has an important role in assuring regular, formal and informal communication, reports and meetings to discuss how the relation evolves or upgrades. Regardless of the mere reception of the monthly reports providing that the service levels are met, does not mean that frequent communication shall not be observed.<sup>274</sup>

Furthermore, one of the least mentioned aspects of the outsourcing relationship, of this research has to do with the vendor selection. However, this is one of considerations taken into account at the due diligence, pre-contractual primordial stage of the relationship, which enables the contracting company to make a risk analysis.<sup>275</sup> Once this assessment is done, it is possible to conceive certain harbour safe contractual terms as well as, respective force majeure clauses, damages, warranties and indemnities, liability and so forth. In association with the above mentioned, this risk analysis allows to have a clear notion of how these outsourcing arrangements costs vary depending on the location.<sup>276</sup> However, costs may rise depending on the location of the outsourcing company, regarding the associated costs with the communication, inflation, relationship these should be foreseen not after the contract is

---

<sup>270</sup> See, supra note 264, pp.201-200.

<sup>271</sup> See, supra note 265, p.89.

<sup>272</sup> Heinzl, A., Dibbern, J., & Hirschheim, R. (2006), "*Information Systems Outsourcing*" (2o ed.), Springer-Verlag Berlin Heidelberg, pp.283-298.

<sup>273</sup> See, p.62, para.2, and p.85, para.2.

<sup>274</sup> See, supra note 264, pp.197 and 206.

<sup>275</sup> See, supra note 272, pp.161-185.

<sup>276</sup> See, supra note 264, pp.202-203.

concluded.<sup>277</sup> Often it occurs that multinational companies, try to avoid eventual changes in local cost related for instance, with inflation, by engaging into outsourcing contracts with more than one supplier, and balancing the volume of the services, as well as, avoiding dependence<sup>278</sup> and exposure.<sup>279</sup>

Nevertheless, each outsourcing agreement should also entail some contractual flexibility. Due to eventual changes that may not be contractually established, and this aspect is advisable to be taken this into account at the risk analysis.<sup>280</sup> Thereby, it is relevant to mature the relationship with a partner-style relationship by having a prone adaptive contracted party, in order to attain a share of interests and changes. Sometimes, the contracting company does not handle with the outsourcing company in a structured way, due to the fact that not regard them as a long term business partner.<sup>281</sup> From a practical standpoint, usually companies are unwilling to disclose the reasons of relationship failure, in order to avoid exposing themselves.<sup>282</sup>

---

<sup>277</sup> Lacity, C. M., Willcocks, L. P. (2009), *“Information Systems and Outsourcing, Studies in Theory and Practice”* (1st ed.), Palgrave Macmillan, pp.173-174.

<sup>278</sup> See, pp.67-68.

<sup>279</sup> Kvedaraviciene, G., & Boguslauskas, V. (2010), *“Underestimated importance of cultural differences in outsourcing arrangements”*, Engineering Economics, 21 (2), p.187.

<sup>280</sup> Sparrow, E. (2003), *“Successful IT Outsourcing: from choosing a provider to managing the project”*, (1st ed.), Springer-Verlag London, p.202.

<sup>281</sup> Lacity, M. C., & Hirschheim, R. (1993), *“The Information Systems Outsourcing Bandwagon”*, Sloan Management Review, 35, pp.80-85.

<sup>282</sup> Barthélemy, J. (2003), *“The seven deadly sins of outsourcing”*, Academy of Management Executive, 17 (2), p.87.





### **Part III. Considerations and Recommendations**



## 1. The Need to Avoid Legal Pitfalls

When a company is considered to engage in an outsourcing agreement, it needs to be diligent and evaluate all the risks involved in order to minimize impacts on business.<sup>283</sup> Despite that fact, outsourcing may entail some concerns and inherent responsibility. The contracting company has to focus in overcoming these obstacles and defying them, as well as accurately drafting the contract and SLA. Subsequently, a company should embody all relevant provisions regarding rights, penalties, transfers, communication, reporting, damages, duties, termination and exit, pricing, and all the considerations described along this research, in this way forming solid foundations for a long-term relationship.<sup>284</sup>

The negotiation procedure may be a lengthy process, but it is the best option, in order to avoid unforeseen costs. Even if the parties take into consideration all fundamental provisions that must be tackled and try to attain a complete contract, as we have seen in this research, other unpredictable situations may emerge. We have also seen, in chapter 1 and 2, how it is fundamental to retain or recruit key staff in order to develop the relation with the outsourcing company. This outsourcing management team, previously agreed to by the parties, has the role of ensuring a liaison between the contractual parties, handling communication and all related matters, monitoring the services provided, or implementing contractual disciplinary procedures.<sup>285</sup> The agreement ought to be flexible, in order to enable eventual changes within the relation. Both parties may win from this scenario, and the contracted party might acquire a proactive role, by constantly advising the contracting party regarding new services and technologies that may arise, and the possibility of incentives and gainsharing.<sup>286</sup> However, a proactive contract, in the sense of also establishing a range of provisions in order to safeguard themselves, especially the contracting party. Inherent to the risks of this agreement, there are also legal risks associated that can impact the contractual performance. These associated legal risks stem from the specificities that outsourcing relationships acquire when several jurisdictions are contemporaneously involved. Therefore, it becomes crucial to pay attention to national applicable laws at an early stage. Nowadays, companies are resorting to outsourcing

---

<sup>283</sup> Bean, L. (2003), "*The profits and perils of international outsourcing*", Journal of Corporate Accounting & Finance, 14 (6), September/October, p.9.

<sup>284</sup> Vagadia, B. (2007), "*Outsourcing to India- A Legal Handbook*" (1st ed.), Springer-Verlag Berlin Heidelberg, p.163.

<sup>285</sup> Honess, S. (1997), "*Outsourcing - A legal perspective on contract critical success factors*", Information Security Technical Report, 1 (3), pp.57-58.

<sup>286</sup> *Id.*

as a tool to enable themselves to attain cost reductions, quality or technological enhances, and concentrate on their businesses.<sup>287</sup> This encompasses not only services or processes associated with IT and communications, but has a broader scope, embracing areas as manufacturing, audit and finance, procurement and real estate. On the one hand, outsourcing agreements may create substantial value if drafted, balanced, maintained and managed effectively, on the other hand, it can entail emerging risks, which has a direct correlation with the contracting company's overall business.

Companies ought to stress the clear drafting of agreement terms throughout their negotiation period. The failure of an outsourcing agreement, acquires even more complexity in multijurisdictional outsourcing contracts, where the recognition of significant national laws and regulations is important and provides certainty. If the above referred is not taken into account, the agreement is of limited value. The outsourcing complex agreement entails a myriad of legal issues that directly impacts the business, thus envisaging accurate organization of legal, commercial and operational factors which need to be coordinated. Despite that fact, that there is not a standard procedure that addresses all matters involved.<sup>288</sup> As we have seen, there are fundamental provisions that should be laid down, in order to achieve the aimed value and objectives.<sup>289</sup>

In the last section of Chapter 2, we saw that the most common issues are especially related to the scope of the agreement, ownership and third party rights, liability, intellectual property, non-compete clauses, communication and confidentiality, and so forth.<sup>290</sup> Despite other legal issues that deserved reference long this research, these above mentioned reasons are those which can entail more numerous pitfalls. Thereby, it is worth analysing what has not worked until now.

Through experience assisting clients, consulting firms can provide some reliability in identifying that there are major flaws, in the way outsourcing has been applied and managed. According to Kirkegaard, numerous pitfalls lie in the way of trying to validly quantify a phenomenon which has no commonly agreed-upon definition, also arguing that firms have clear incentives to remain unnoticed, arguing that companies are laying off workers because of offshoring and offshoring outsourcing. Kirkegaard argues that there is the lack of official

---

<sup>287</sup> Wright, C. (2004), "*Avoiding the Pitfalls in Outsourcing*", International Business Lawyer, 32, April, pp.19-33.

<sup>288</sup> *Id.*

<sup>289</sup> Jackson, T., Iloranta, K., & Mckenzie, S. (2001), "*Profits or Perils? The Bottom Line on Outsourcing*", Booz, Allen, Hamilton Strategy Business Quarterly Journal, p.3.

<sup>290</sup> *See*, pp.96-98.

statistical data of services sectors, and multinational companies, as well as research due to this subject's embryonic state in the literature. However, the above question has appeared on the media and politicians' agendas. This contrasts with the reports of industry experts and consultants, which rely mostly on unpublished interviews with corporate executives, by implementing their own evaluation methods.<sup>291</sup>

---

<sup>291</sup> Kirkegaard, J. F. (2005), "*Outsourcing and Offshoring: Pushing the European Model Over the Hill, Rather Than Off the Cliff!*" (Vol. 3), Working Paper Series, Institute for International Economics, p.5.

## 2. Should a New Legal Framework Be the Solution?

In general terms, it is possible to say that at the beginning, under the law, the company was only seen as the addition of a form of property, with a set of contracts, and to the economy, as an independent organization with inherent operating means which are used to pursue an economic activity. However, today, the law and economics intersect their reading codes, in other words, economic sense of the company is analysed by the law, trying to controvert the economic reality into laws, and the economy uses the established laws to clarify its concepts. The autonomy of a company shall have as an essential reference, the legal autonomy. The truth is that, the company is the first and the main institutional reference of industrial production, from which the rest of the eventual framework derives, whether public or private. Of course, the company can acquire various contours, and these concepts are a reference to the form of property and consequently the surplus distribution mode, but do not affect what often is termed as corporate substrate.

According to Marques,” (...) the tendency to build a concept of the purely abstract company has taken root, either from a legal point of view or from an economic point of view. It has also appeared from a technical perspective, relating to the production in large series, and in psychological terms, on the behalf of those who direct and who perform it, in a way to make or intend to make, a neutral representation itself immutable, in space and time”.<sup>292</sup> The contractual freedom of expression may entail several meanings. It has to do with the freedom to contract, to choose the other party and with the establishment of the contract's content. This latter means, the content of the contract cannot be unilaterally imposed by one of the parties. Conversely, a contract must be the result of a free debate, in this subsidiary legislation, and lastly appears related to the possibility of a party set freely a discipline-type for their contracts, and the other party is limited to adhere. In summary, the limitations of the principle of contractual freedom, in the specific field of contracts between companies, can be analysed mainly from two perspectives, which somehow oppose the limitations resulting from the will of the parties, and regulatory limitations.

Outsourcing is a relationship that can be established between both companies in the same country as well as in different countries. By taking into account the economic reasons already presented, and in particular the fact that the wage differentials are one of the reasons that lead companies to outsource, it is not surprising that the problem of international

---

<sup>292</sup> Marques Leitão Manuel, M. (1989), “*Subcontratação e Autonomia Empresarial- O caso Português*”, Universidade de Coimbra, pp.27-28.

outsourcing is one of the topics required under the subcontracting study. However, Draetta <sup>293</sup> points out that, “(...) from a legal point of view, the subcontract is among the various types of international agreements, and has been the less subject of studied by doctrine (...)”, a situation which, according to the author, leads this relationship “(...) to be less apparent as cooperation between companies, for example, in the joint venture”.<sup>294</sup> The international outsourcing can function as a complement or alternative to the advantageous role of subsidiaries of multinational companies.

Thus, taking into account all the problems that may arise regarding the qualification of the subcontract, as being a purchase and sale contract, services contract or as an employment relationship, the best solution in the case of subcontracts it seems sensible to frame it to an atypical or innominate contract. In fact, the economic and social role of industrial subcontracting combines the provision of work or transfer of property by one of the contracting parties, with the subordination concerning some issues of the production process and in many cases, the economic dependence that may emerge. Therefore, this seems generally not to conform to the typical negotiation scheme, the essential core of any of the three contracts before analysed. These outcomes result from the fact that none of them can provide an appropriate legal framework to all peculiar, complex and multifaceted reality of industrial subcontracting. Regarding outsourcing agreements, the same circumstances lead to the same conclusion of both parties’ option for the elaboration of a contract, in order to at least circumvent the application of some national rules in question, such as arbitration.

Varela argues that in mixed contracts, in some cases the combination of rules is required, in other cases the absorption of secondary types by observing the predominant type of negotiation, and finally, the fixing of a regime in each case, through the discipline of similar contracts. Therefore, to find out which situations occur, depends mainly on the analysis of the cause of mixed contract, that is, the economic function, it aims to fill, and its confrontation with the cause of the typical and nominated contracts.<sup>295</sup> Marques argues that industrial subcontract, and its relation to the contract in action, provides a solution and justification, for subcontract juridical qualification.<sup>296</sup>

---

<sup>293</sup> Draetta, Ugo (1985), “*Il Diritto dei Contratti Internazionali. La Cooperazione tra Imprese*”, Padova, Studi e Pubblicazioni della Rivista di diritto internazionale privato e processuale, Cedam, 25, p.13.

<sup>294</sup> See, p.76.

<sup>295</sup> Varela, J.A. (1968), “*Contratos mistos*”, Boletim da Faculdade de Direito, Universidade de Coimbra, Vol.44.

<sup>296</sup> Marques Leitão Manuel, M. (1989), “*Subcontratação e Autonomia Empresarial - O caso Português*”, Universidade de Coimbra, p.228.



The intervention of states and international organizations, such as the OECD, in subcontracting relationships has not featured so far for mandatory measures, rarely having assumed the legislative form. First, at the European level, it has been an encouraged practice, and there is even financial support to do so. Second, it has aimed indirectly blurring the relationship of inequality between the parties, in industrial subcontracting.<sup>297</sup> However, it confines itself to regulation produced by companies using such standard-setting instruments, guiding documents, industry associations and so forth. The negative judgment, in the field of comparative law, which has been made on state intervention attempts by mandatory rules that protect the position of subcontractors, and the notion of the peculiar nature and versatility of this form of contractual relationships between companies, which actually might contribute to relativize the effectiveness of this form of action.<sup>298</sup> Thus, the dominant regulation of subcontracting should be sought in their own relationships between companies, dissecting the private power mechanism of the contracting company, which allows it to determine the behavior of legally independent companies, in the rationale of cost minimization. The same is also applicable, in relation to outsourcing companies. The subsidiary intervention or state of corrective works as a kind of counterweight, to exorbitant cases with external effects, or as a player's agent's own relationship, in the context of an industrial restructuring policy, acting in a logical way in agreement with the companies, now autonomous in relation to them and eventually be the contractor company who might take advantage. It is shown so that the regulation of subcontracting reveals a considerable shrinkage of public intervention, with respect to emerging forms of private self-regulation of both agreements between undertakings, as the dominant positions stemming from the unequal power between them, in the current organization of the market economy. The existence of this self-regulation, both at the national and international level, is itself a deterrent to public intervention, as well as limit their effectiveness.

According to Marques, a substantial analysis shows the relative autonomy and specific characteristics of this contractual practice, which will lead to the need to rethink the whole state intervention in the public and private economy, not purely in an abstentionist sense, but in the sense of to adapt, to recent technological and organizational changes, in production systems.<sup>299</sup>

---

<sup>297</sup> This is done through the access to European subsidies to small and medium enterprises. In the Portuguese case, IAPMEI is the public institute that is encumbered of the management of the attribution of these funds, as well as give provide some support regarding the concerning business.

<sup>298</sup> See, supra note 296.

<sup>299</sup> See, supra note 296, p.453.

Moreover, it is assumed that a new model should not be characterized only by a relative shrinkage in the intervention imperative means, and greater consultation as well as, negotiation, together with the recognition of the capacity for self-regulation of private entities. According to Kirkegaard, there is a necessity of European policy response, in order to benefit from offshoring and offshore outsourcing, as well as, Europe therefore first needs to increase the flexibility of its labor markets.<sup>300</sup>

Nevertheless, most of the time the parties opt for the establishment of mixed contracts referred to above, in order to achieve reconciliations with a more rapid resolution of conflicts between parties, through the introduction of arbitration clauses, and other prior mechanisms, in the outsourcing agreement. Thus, this translates into a way of reducing some uncertainty of the legal classification of this relationship, trying to reduce their contractual exposure to national laws. However, some of them that should be taken into account, at the stage of drafting the agreement, which will be necessarily applicable in the jurisdiction of the contracted company.<sup>301</sup>

Some authors argue for a degree of legislative immunity for multinational contracts, with a basis in the fact that these contracts often refer back to clauses regarding general principles and customs of the economic sectors under consideration and so forth. This is a mean of avoiding the application of a state law, both in material and formal aspect.<sup>302</sup> In addition, this situation has been exacerbated by the growing importance of private codes of conduct, the so-called "soft law". These private codes of conduct emerged due to the establishment of parties' own contractual clauses. This contributes to the indifference of certain relationships, between companies' rights in force in national or regional areas where they operate. Internationally speaking, outsourcing may appear associated with a transfer of activity or technology transfer, making it relevant to emphasize the European Directive Data Protection as well as national laws and international treaties, ratified by the jurisdiction of the contracted company, in order to try to ensure the maximum data level of protection and other legal issues, due to the abyssal discrepancies in protection strength levels between the countries.<sup>303</sup>

---

<sup>300</sup> Kirkegaard, J. F. (2005), "*Outsourcing and Offshoring: Pushing the European Model Over the Hill, Rather Than Off the Cliff!*", Working Paper Series, WP 05-1, p.20.

<sup>301</sup> See, pp.87-89.

<sup>302</sup> Leitão Marques, M. M. (1987), "*A Empresa, o Espaço e o Direito*", Revista Crítica de Ciências Sociais, Nº 22, p.79.

<sup>303</sup> See, pp.70-78.

### 3. Should Better Contractual Governance Be the Answer?

In accordance with what has been suggested along this research, the parties need to be accurate and lay down all the provisions in the contract and SLA. This also brings immediately the inherent need of contractual governance maintenance, which contributes to the success of the relationship that ought to be sustained by effective communication forms and contractual flexibility, regarding aspects that can vary during this long-term relation. Geis' analysis suggests that outsourcing transactions can acquire several contours related with numerous strategies to divide financial gains, allocate control, determine monitoring rights, set exit terms, and parse operational risk. Yet taken together, these varied terms probably enable the parties, to structure ordinal relationships.<sup>304</sup> As we have seen, in accordance with Goo J., Kishore R. et al., the specific features of the SLAs impact relational governance in information technology outsourcing relations.<sup>305</sup> Naturally, this also applies to other types of services. Thus, a contract needs to wisely balance the flexibility needed to remain technologically competitive, yet be detailed enough to include specific performance criteria and to allow for managing the costs specified in the contract.<sup>306</sup> Therefore, contract flexibility is a very desirable objective, which must be constructed into outsourcing agreements. The underlying reasoning is to acknowledge that certain external elements, not under the control of the contracting party might entail variations. As we have seen, it is possible to observe in literature, and on this research being said that an incomplete contract is synonymous with a flexible contract, nevertheless, might not be the only path to be followed.

On the one hand, a completely contingent contract confers flexibility to an agreement, and on the other hand, there is a high cost in drafting contracts with ample flexibility, due to the fact that a substantial part of the risk may be shifted to the contracted party, or split between the parties. Incomplete contracting constitutes a less lengthy way, although at the end, might not worth it.<sup>307</sup> Therefore, contracts may or may not be wholly complete. If the contract is complete, in accordance with the classical view of contracts, it specifies the obligations of the parties eventually, in different jurisdictions. However, as exchange hazards increase,

---

<sup>304</sup> Geis, G. S. (2010), "An Empirical Examination of Business Outsourcing Transactions", *Virginia Law Review*, 96 (2), p.292.

<sup>305</sup> See, pp.94-95.

<sup>306</sup> Goo, J., Kishore, R., Rao, H. R., & Kichan, N. (2009), "The Role of Service Level Agreements in Relational Management of Information Technology", *Management Information Systems Research Center*, 33 (1), pp.119-145.

<sup>307</sup> Harris, A., Giunipero, L. C., & Hult, G. T. M. (1998), "Impact of Organizational and Contract Flexibility on Outsourcing Contracts", *Industrial Marketing Management*, (27), p.376.

contracts may become less complete, because it is impossible to predict a certain stability in some countries.<sup>308</sup> This should propagate the explicit and clear drafting of the agreement, however parties further specify contracts only when the risk is significant.<sup>309</sup>

In line with the above said, the communication, business relationship, trust and commitment, constitute the foundations for relational reliability, thus, this acquires additional relevance in incomplete contracts. Subsequently, this contributes to attaining the primary objectives, avoiding counterpart eventual opportunistic behaviour, and observing an expectable behaviour in the future. Especially, in circumstances where legal institutions are perceived as weak, there is a tendency to rely on relational reliability, in order to protect their transactions from economic risks, however, it is inherently, a less reliable enforcement method than contracts.<sup>310</sup> Zheng-Zhou and Poppo sustain that due to the fast progress of emerging economies, and subsequently, a service provider today can tomorrow be a competitor, making formal contracts more reliable than personal relationships with partners, to safeguard risky market transactions.<sup>311</sup> According to these authors, legal enforceability moderates that relationship between contracts and relational reliability, in particular, the effect of contracts on relational reliability declines as legal enforceability increases. Their results also provide important managerial insights, regarding the role of trust development in outsourcing relationships, by arguing that influences the maturity of process integration, contractual flexibility, cultural comprehension, increasing the likelihood of reciprocity on the relation.<sup>312</sup> Frequently, authors argue that from a relational governance perspective, both relationship and contract are indispensable governance mechanisms in directing IT outsourcing engagement.<sup>313</sup> Qi, C., & Chau, P. Y. K, also extend the view propagated by Poppo and Zenger<sup>314</sup> that formal contracts and relational governance function as complements rather than substitutes.<sup>315</sup> Following this reasoning, legally astute management teams enables the contracting companies

---

<sup>308</sup> Poppo, L., & Zenger, T. (2002), “Do formal contracts and relational governance function as substitutes or complements?”, *Strategic Management Journal*, 23 (8), pp.707-725.

<sup>309</sup> See, supra note 313.

<sup>310</sup> Zheng Zhou, Kevin, Poppo, L. (2010), “Exchange hazards, relational reliability, and contracts in China: The contingent role of legal enforceability”, *Journal of International Business Studies*, 41 (5), p.866.

<sup>311</sup> See, pp.83-84.

<sup>312</sup> Schoenherr, T., Narayanan, S., & Narasimhan, R. (2015), “Trust formation in outsourcing relationships: A social exchange theoretic perspective”, *International Journal of Production Economics*, 169, pp.401-412.

<sup>313</sup> Qi, C., & Chau, P. Y. K. (2012), “Relationship, contract and IT outsourcing success: Evidence from two descriptive case studies”, *Journal of Decision Support Systems*, 53 (4), pp.859 – 869.

<sup>314</sup> See, supra note 308.

<sup>315</sup> *Id.*

to evaluate and build dynamics, to use and comply with the legal system of the outsourcing company jurisdiction. The outcomes might be the use of formal contracts as complements, and not substitutes to relational governance, which advocates adds substantially to the relation, and reduces costs. In order to overcome the numerous legal multijurisdictional pitfalls, the use of contracts and inherent agreement as well as, other legal tools to provide options and circumvent limitations, by looking at them as opportunities.<sup>316</sup> As we have already seen in this research, contract law a sine qua non among multinational companies, which enables the contractual parties to set their own contractual provisions, and bargaining typically takes place in the shadow of the law.<sup>317</sup> Yet, Courts can enforce this also known, manager-made law, since it does not collide with national rules.

In line with the opinion sustained by Poppo & Zenger<sup>318</sup>, Bagdley and all mention that contract customization and relational governance, both directly and indirectly increased service-level performance, as measured by satisfaction with the cost, quality and promptness of the outsourced service or process.<sup>319</sup> Thus, it is possible to conclude that legally astute management teams realize more value in their contractual relationships than teams lacking that standpoint.

Pollack also problematizes the hypothesis of adequately regulate international legal outsourcing, whereas theoretically conceivable, in practice it would translate into a utopia. Moreover, it would envisage a viable prevailing, comprehensive, substantial agreement, a range of rules and mechanisms that entails the collaboration of a wide variety of stakeholders, and government bodies, which seems improbable to happen. It would likely take years to progress from talks to completion<sup>320</sup>

---

<sup>316</sup> See, also, Hanson, A. (2006), “*Legal Process Outsourcing to India: So Hot Right Now!*”, SMU Law Review, 62.

<sup>317</sup> Bagdley E., C. (2008), “*The Value of Legal Astuteness*”, The Academy of Management Review, 33 (2), pp.384-387.

<sup>318</sup> See, supra note 310, pp.861-878.

<sup>319</sup> Harris, A., Giunipero, L. C., & Hult, G. T. M. (1998), “*Impact of Organizational and Contract Flexibility on Outsourcing Contracts*”, Industrial Marketing Management, (27), pp.374-384.

<sup>320</sup> Pollack V., D. (2006), “*I’m Calling My Lawyer... in India!*”, Ethical Issues in International Legal Outsourcing, UCLA Journal of International Law & Foreign Affairs, (99), p.158.

#### **4. Conclusions**

Nowadays, outsourcing has become a common management practice among companies. Throughout this analysis, we observed that through outsourcing, companies can minimize their costs, by the transfer of an activity or process to an external third party, which will be an extended arm of the contracting organization, being thus a partner.

However, although the outsourcing agreement contains the provisions freely settled by both parties, there are certain national laws of the contracted company's jurisdiction that will be deemed applicable. Therefore, these ought to be taken into account, at the time of drafting the contract and inherent service-level agreement (SLA). These issues have to be evaluated by a structured stages approach, in order to be wise and cautious. Due to the fact that the outsourcing contract acquires specific complexities, that distinguish it from the subcontract, there may be obstacles to the creation of a unitary figure. The main conclusions of this essay translate into the following:

**1-** The multijurisdictional outsourcing relationship acquires peculiar contours and entails a myriad of legal risks associated. Thus, there are circumstances in which the legal enforcement may be weaker, due to the fact that some of the applicable laws do not provide the same level of protection. In addition, it is interesting to observe that one of the most outsourced activities or processes are related to IT and intellectual property rights, and beforehand parties know that several complexities will emerge, in addition to unpredictable ones.

**2-** Throughout this research, we developed a comparison between the concept of outsourcing and other legal concepts, with which the former has resemblances. Nevertheless, it is possible to conclude, the outsourcing concept acquires contours that enable us to distinguish it from the subcontract. The subcontract does not deserve to be classified as a contractual form. If we take into account some mentioned European jurisdictions, in section 1.1 from chapter 2, it is possible to see that the subcontract is not usually subject to a typical and regulated contract, lacking for this reason, a specific normative discipline. In a large part of European jurisdictions, subcontracting is regulated by the general rules of the respective Civil Code and the general laws of the contractual 'type' that it best fits, depending on the circumstances. Considering this it is possible to observe some legal uncertainty associated with subcontract qualification. Therefore, in subcontract parties often opt for the establishment of their own contractual terms.

In the outsourcing multijurisdictional relationships due to its inherent complexities, the parties may also opt for defining their own contractual terms.

**3-** In the literature we find authors who argue that a substantial analysis shows the relative autonomy and specific characteristics of this contractual practice. This leads to the need to rethink the nature of State intervention in the public and private economy. Companies should not achieve this change through pure abstention, but rather through adapting to recent technological and organizational changes, in production systems. Moreover, it is stressed that a new model should not only be characterized by a relative shrinkage of intervention of imperative means, but also by greater consultation as well as negotiation, together with the recognition of the capacity for self-regulation of private entities. In order to benefit from offshoring and offshore outsourcing Europe should also increase the flexibility of its labour markets.

**4-** In short, there is no standard form to handle outsourcing agreements. However, it would be plausible to observe the implementation of guidelines, on the European Union's behalf, as a complement to a few indirect outsourcing related directives. . Thus, the reaching of a consensus and an agreement concerning directly these matters ought to be a priority for national bodies, in order to harmonize, and contribute to the development and safeguard ownership rights.

**5-** Therefore, it should be envisaged the creation of standard guidelines regarding each activity or process of outsourcing, in order to contribute to the development and safeguard of ownership rights of foreign or national companies. Through the intervention of these public entities, business or companies organizations may have a more sustained knowledge of these commercial relations, in each jurisdiction. Harmonization of the practices that ought to be observed should occur on the legal levels of protection and enforcement, in several jurisdictions. This may constitute an attempt to constitute specific standards, which would be sustained by a good contractual governance, as well as sense of trust and commitment, contractual flexibility and effective communication. Otherwise, opportunistic behaviour may result, along with eventual failure and termination of the contractual relationship. This would be more plausible, rather than an eventual juridification of the concept of outsourcing, as in the case of subcontract.

## **Part IV. Bibliography**





## References

### Books/Reviews

Amiti, M., & Wei, S.-J. (2005), "*Service offshoring, Productivity, and Employment: Evidence From the United States*", IMF Working Papers, 05 (238).

Bagdley E., C. (2008), "*The Value of Legal Astuteness*", The Academy of Management Review, 33 (2).

Barrar P., G. R. (2006), "*Global Outsourcing Strategies: An International Reference on Effective Outsourcing Relationships*", Gower Publishing, Ltd.

Barthélemy, J. (2003), "*The seven deadly sins of outsourcing*", Academy of Management Executive, 17 (2).

Bassett-Jones, N. (2005), "*The Paradox of Diversity Management, Creativity and Innovation*", Journal of Diversity, Management, Creativity and Innovation, 14 (2).

Bean, L. (2003), "*The profits and perils of international outsourcing*", Journal of Corporate Accounting & Finance, 14 (6).

Belloc, F. (n.d.), "*Corporate Governance and Innovation: A Survey Corporate Governance and Innovation*", Journal of Economic Surveys, Forthcoming, (June 2009).

Blöndal, J. (2005), "*Market-type Mechanisms and the Provision of Public Services*", OECD Journal on Budgeting, 5 (1).

Burnett, R. (2012), "*Outsourcing IT - The Legal Aspects: Planning, Contracting, Managing and the Law*", (2nd ed.), Gower Publishing, Ltd.

Busser, N. J. M. (2009), "*Legal issues in the outsourcing process: An overall perspective*". Universiteit van Tilburg.

Contractor, F. J., Kumar, V., Kundu, S. K., & Pedersen, T. (2010), "*Reconceptualizing the firm in a world of outsourcing and offshoring: The organizational and geographical relocation of high-value company functions*", Journal of Management Studies, 47 (8).

Draetta, U. (1985), "*Il Diritto dei Contratti Internazionali. La Cooperazione tra Imprese*", Padova, Studi E Pubblicazioni Della Rivista Di Diritto Internazionale Privato E Processuale, Cedam, (25).

Duening T., C. R. (2005), "*Essentials of business process outsourcing*", Volume 34 de Essentials Series. John Wiley & Sons.

Edquist, C., Hommen, L. and McKelvey, M. (2001),” *Innovation and employment: process versus product innovation*”. Edward Elgar Publishing.

Edvardsson, I.R., Oskarsson, G.K. and Vesteinsdottir, S. (2011), “*Enhancing customer services and core competencies: outsourcing in Icelandic service SMEs*”, *International Journal of Entrepreneurship and Small Business*, 14 (3).

Ellram, L., & Billington, C. (2001), “*Purchasing leverage considerations in the outsourcing decision*”, *European Journal of Purchasing and Supply Management*, 7 (1).

Espino-Rodriguez, T. F., & Padrón-Robaina, V. (2006), “*A review of outsourcing from the resource-based view of the firm*”, *International Journal of Management Reviews*, 8(1).

Europeias, C. das C. (1992), “*Guia Prático dos Aspectos Jurídicos da Subcontratação Industrial na Comunidade Europeia*”, Parte II (Vol. 292), Serviço das Publicações Oficiais das Comunidades Europeias.

Europeias, C. das C. (1992), “*Guia Prático sobre os Aspectos Jurídicos da Subcontratação Industrial na Comunidade Europeia*”, Parte I (Vol. I). Serviço das Publicações Oficiais das Comunidades Europeias.

Franceschini, F., Galetto, M., Pignatelli, a., & Varetto, M. (2003), “*Outsourcing: guidelines for a structured approach*”, *Benchmarking: An International Journal*, 10 (3).

Geis, G. S. (2006), “*Business outsourcing and the agency cost problem*”, *Notre Dame Law Review*, 82 (3).

Godfrey-faussett, M. (1997), “*Telecommunications Outsourcing. A Legal Perspective*”, *Computer Law and Security Review: The International Journal of Technology and Practice*, 13 (3).

Gomes, O. (2009), “*Contratos*”, (26o ed.), Rio de Janeiro: Editora Forense.

Goo, J., Kishore, R., Rao, H. R., & Kichan, N. (2009), “*The Role of Service Level Agreements in Relational Management of Information Technology*”, *Management Information Systems Research Center*, 33 (1).

Greaver, M. F. (1999), “*Strategic Outsourcing: A Structured Approach to Outsourcing. Decisions and Initiatives, General business*” / AMACOM, AMACOM Div American Mgmt Assn.

Hammer Michael, Champy, J. (2009),” *Reengineering the Corporation: A Manifesto for Business Revolution. Collins Business Essentials*”, Zondervan.

Hansmann, Henry & Kraakman, R. (2011), “*Reflections on the end of history of Corporate Law*”, *Yale Law & Economics Research Paper*.

Hanson, A. (2016), *“Legal Process Outsourcing to India: So Hot Right Now!”*, SMU Law Review, 62.

Harris, A., Giunipero, L. C., & Hult, G. T. M. (1998), *“Impact of Organizational and Contract Flexibility on Outsourcing Contracts”*, Industrial Marketing Management, (27).

Heinzl, A., Dibbern, J., & Hirschheim, R. (2006), *“Information Systems Outsourcing”* (2o ed.). Springer-Verlag Berlin Heidelberg.

Holcombe, J. K. (2005), *“Outsourcing in the Service Sector: Using Mechanisms, and collective Organization as Building Blocks”*, U. PA. Journal of Labor and Employment Law.

Honess, S. (1997), *“Outsourcing - A legal perspective on contract critical success factors”*, Information Security Technical Report, 1 (3).

K., H. G. & P. C. (1994), *“Competing for the future”*, Harvard Business Press, (July - August).

Kav, K., & Koper, M. (n.d.), *“What outsourcing can bring in the long run?”*, Faculty of Management Koper.

Kavaleff, A. (2005), *“Successful Outsourcing through Proactive Contracting – Strategy, Risk Assessment and Implementation. In Managing Contracts and Risks*, Stockholm Institute for Scandinavian Law.

Kennedy, G., & Clark, D. (2006), *“Outsourcing to China – Risks and benefits”*, The Computer Law and Security Report, 22.

Kern, T., & Willcocks, L. (2000), *“Exploring information technology outsourcing relationships: theory and practice”*, The Journal of Strategic Information Systems, 9 (4).

Kim, S. (2006), *“Legal Issues in Outsourcing: What Businesses Should Know”*, Rider University.

Kirkegaard, J. F. (2005), *“Outsourcing and Offshoring: Pushing the European Model Over the Hill, Rather Than Off the Cliff!”*, Vol. 3., Institute for International Economics.

Klaus, G. (2001), *“Corporate Governance and Economic Performance”*, Oxford University Press.

Kluwer, W. (2008), *“Outsourcing Contract Structures”*, International Outsourcing Law and Practice, (May 2008).

Kobayashi-Hillary, M. (2004), *“Outsourcing to India: The offshore advantage”*, (1st ed.), Springer-Verlag berlin Heidelberg, New York.

Krames A., J. (2011), *“The Welch Way: 24 lessons from the World’s Greatest CEO”*, (1st ed.), McGraw-Hill.

Kvedaraviciene, G., & Boguslauskas, V. (2010), “*Underestimated importance of cultural differences in outsourcing arrangements*”, *Engineering Economics*, 21 (2).

Lacity M.C., Solomon S., Y. A. (2011), “*Business process outsourcing studies: a critical review and research directions*”, *Journal of Information Technology*, (26).

Lacity, C. M., Willcocks, L. P. (2009), “*Information Systems and Outsourcing, Studies in Theory and Practice*”, (1st ed.), Palgrave Macmillan.

Lacity, M. C., & Hirschheim, R. (1993), “*The Information Systems Outsourcing Bandwagon.*”, *Sloan Management Review*, 35.

Lazonick, W. (2006), “*Corporate Governance, Innovative Enterprise, and Economic Development*”, (No. 71), UNU - Wider.

Lazonick, W., P. A. (2005), “*Dynamic capabilities and sustained innovation: strategic control and financial commitment at Rolls-Royce plc*”, *Industrial and Corporate Change*, 14 (3).

Lee, J.-N. L. J.-N., Huynh, M. et al. (2000), “*The evolution of outsourcing research: what is the next issue?*”, *Proceedings of the 33rd Annual Hawaii International Conference on System Sciences*.

Marques Leitão, M. M. (1987), “*A Empresa, o Espaço e o Direito*”, *Revista Crítica de Ciências Sociais*, 22.

Mahnke, V. (2000), “*The process of vertical dis-integration: an evolutionary perspective on outsourcing*”, *Journal of Management and Governance*.

Mäntysaari, P. (2012), “*Organising the Firm. Theories of Commercial Law, Corporate Governance and Corporate Law*”, Springer-Verlag, Berlin Heidelberg.

Marques Leitão, M. M. (1989), “*Subcontratação e Autonomia Empresarial- O caso Português*”, Universidade de Coimbra.

Marques Leitão, M. M. (1990), “*A subcontratação na comunidade económica europeia*”, Oficina do CES, Coimbra.

Martinez Romano, P. (1989), “*O Subcontrato*”, (2o, 2006th ed.), Almedina.

Mayer, C. (1997), “*Corporate Governance, competition and performance*”, *Journal of Law and Society*.

Mayer, K. J., & Argyres, N. S. (2004), “*Learning to contract: Evidence from the personal computer industry*”, *Organization Science*, 15 (4).

Menezes Leitão, L. (2008), “*Direito das Obrigações, Vol. III*” (6a ed.), Almedina.

OECD. (2013), “*The OECD Privacy Framework*”, (2nd ed.), OECD Publisher.

Oshri, I., Kotlarsky, J., & Gerbasi, A. (2015), "*Strategic innovation through outsourcing: The role of relational and contractual governance*", *Journal of Strategic Information Systems*, 24 (3).

Perunovic Z., L. P. J. (2007), "*Outsourcing Process and Theories*", in: POMS 18th Annual Conference.

Pizarro Nóbrega, S. (2010), "*O contrato de Outsourcing*", (1o ed.), Wolters Kluwer Portugal and Coimbra Editora.

Pollack V., D. (2006), "*I'm Calling My Lawyer... in India!*".*Ethical Issues in International Legal Outsourcing.*", *UCLA Journal of International Law & Foreign Affairs*, (99).

Poppo, L., & Zenger, T. (2002), "*Do formal contracts and relational governance function as substitutes or complements?*", *Strategic Management Journal*, 23 (8).

Qi, C., & Chau, P. Y. K. (2012), "*Relationship, contract and IT outsourcing success: Evidence from two descriptive case studies*", *Decision Support Systems*, 53 (4).

Quinn, J. B., Hilmer, F. G. (1994), "*Strategic outsourcing*", *Sloan Management Review*, (35).

Raassens, N. (2011), "*The Performance Implications of Outsourcing*", Tilburg University.

Redinha Gomes, M. R. (1995), "*A Relação Laboral Fragmentada. Estudos sobre o trabalho temporário*" (2, Stvdia), Coimbra Editora.

Rippert, S., Weimer, K., Heeder, O., Lochmann, R., Weiss, S., & Llp, R. S. (2006), "*Outsourcing Handbook*", (1st ed.), Cross-border Handbooks.

Robertson, C. B. (2011), "*Collaborative Model of Offshore Legal Outsourcing*", *Arizona State Law Journal*.

Rubin, H. (2007), "*Supply-Side / Manufacturing Outsourcing — Strategies And Negotiations*", *GeorgeTown Journal of International Law*, 38 (1948).

Sako, M. (2010), "*Outsourcing versus shared services*", *Communications of the ACM*, 53 (7).

Saunders, C., Gebelte M., H. Q. (1997), "*Acchieving Sucess in Information systems outsourcing*", *California Management Review*, 39 (2).

Schoenherr, T., Narayanan, S., & Narasimhan, R. (2015), "*Trust formation in outsourcing relationships: A social exchange theoretic perspective*", *International Journal of Production Economics*, 169.

Sharpe, M. (1997), “*Outsourcing, Organizational Competitiveness, and Work*”, Journal of Labor Research, XVIII (4).

Shelfier, Andrei and Vishny W., R. (n.d.), “*A Survey of Corporate Governance*”, The Journal of Finance, LII (2).

Shleifer, A., & Summers, L. H. (1988), “*Breach of Trust in Hostile Takeovers*”, Corporate Takeovers: Causes and Consequences (Vol. I)”.

Smith, A. (1776), “*An Inquiry into the Nature and Causes of the Wealth of Nations*”.

Sparrow, E. (2003), “*Successful IT Outsourcing: from choosing a provider to managing the project*”, (1st ed.). Springer-Verlag London.

The Chartered Institute of Management Accountants. (2001), “*Contracting Out the Finance Function.*”, London.

Thompson, J. L., M Scott, J., & Martin Frank. (2014), “*Strategic management*”, (7th ed.), Hampshire: Cengage Learning.

Tum, J., Norton, P., & Wright, J. N. (2006), “*Management of Event Operations. Management*”, Elsevier.

Vagadia, B. (2007), “*Outsourcing to India- A Legal Handbook*”, (1st ed.), Springer-Verlag Berlin Heidelberg.

Varela, J. (1968), “*Contratos mistos*”, Boletim Da Faculdade de Direito Da Universidade de Coimbra, 44.

Vining, A. R., & Globerman, S. (1999), “*A conceptual framework for understanding the outsourcing decision*”.

Walters Bruce, T. Z. (2006), “*IT Enabled Strategic Management: Increasing Returns for Organizations*”. Idea Group Publishing.

Wei, Y. (2003), “*Comparative Corporate Governance: A Chinese Perspective*”, Volume 3 of Global trade and finance series, Kluwer Law International.

Weiss, R. M., & Azaran, A. (2007), “*Outward Bound: Considering the Business and Legal Implications of International Outsourcing*”. Georgetown Journal of International Law, 38 (3).

Wright, C. (2004), “*Avoiding the Pitfalls in Outsourcing*”, International Business Lawyer, 32 (April), 2010.

Zheng Zhou, Kevin, Poppo, L. (2010), “*Exchange hazards, relational reliability, and contracts in China: The contingent role of legal enforceability*”, Journal of International Business Studies, 41 (5).

Zheng, X. (2009), “*Could the Different Countries’ Corporate Governance Regimes be Harmonized?*”, *Management Science and Engineering*, 3 (2).

### **International Conventions**

The Geneva Arbitration Convention 1927.in:  
[http://www.uncitral.org/pdf/english/texts/arbitration/NY-conv/XXII\\_1\\_e.pdf](http://www.uncitral.org/pdf/english/texts/arbitration/NY-conv/XXII_1_e.pdf) (last time consulted: 27/04/2016)

The New York Arbitration Convention (1958). Retrieved from:  
<http://www.newyorkconvention.org/english> (last time consulted: 27/04/2016)

The World Trade Organization. TRIPS Agreement is Annex 1C (1994). Retrieved from:  
[https://www.wto.org/english/tratop\\_e/trips\\_e/t\\_agm0\\_e.htm](https://www.wto.org/english/tratop_e/trips_e/t_agm0_e.htm) (last time consulted: 27/04/2016)

### **Online Resources**

“*Deloitte’s 2014 and Beyond Global*”, Outsourcing and Insourcing, Survey 2014, in:  
<http://www2.deloitte.com/us/en/pages/strategy/articles/2014-global-outsourcing-and-insourcing-survey.html> (last time consulted: 27/04/2016)

Gareis, R. (2004), “*Business Process Outsourcing under Sarbanes Oxley: Challenges and Complexities*”. Retrieved from: <http://www.outsourcing-center.com/2004-04-business-process-outsourcing-under-sarbanes-oxley-challenges-and-complexities-article-37782.html> (last time consulted: 27/04/2016)

Jackson, T., Iloranta, K., & McKenzie, S. (2001), “*Profits or Perils? The Bottom Line on Outsourcing*”, Booz, Allen Hamilton, Available on:  
[http://www.boozallen.com/content/dam/boozallen/media/file/FINAL\\_Outourcing\\_Broch.pdf](http://www.boozallen.com/content/dam/boozallen/media/file/FINAL_Outourcing_Broch.pdf)

Prinsley, M. (2007). *The Importance of Clear Drafting in Outsourcing Arrangements*. Mayer Brown Publications. Retrieved from  
[https://www.lexisnexis.com/documents/pdf/20080125111014\\_large.pdf](https://www.lexisnexis.com/documents/pdf/20080125111014_large.pdf) (last time consulted: 27/04/2016)

Outsourcing Law Group. (2014),” *Practice Guide On Exit Services In Outsourcing*”, Retrieved from:  
[http://www.mofo.com/~/\\_media/Files/ClientAlert/140604ABetterWayOut\\_Attachment.pdf](http://www.mofo.com/~/_media/Files/ClientAlert/140604ABetterWayOut_Attachment.pdf) (last time consulted: 27/04/2016)



## Legislation

Código Civil (1966). Português. *in*  
[http://www.pgdlisboa.pt/leis/lei\\_mostra\\_articulado.php?nid=775&tabela=leis&so\\_miolo=](http://www.pgdlisboa.pt/leis/lei_mostra_articulado.php?nid=775&tabela=leis&so_miolo=)  
(last time consulted: 27/04/2016)

Council Directive. (2001), Directive 2001/23/CE on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses. Official Journal of the European Communities, (L 82/16). Retrieved from: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32001L0023&from=PT> (last time consulted: 27/04/2016)

European Parliament and of the Council. (1995), Directive 95/46/EC on the protection of individuals with regard to the processing of personal data and on the free movement of such data. Official Journal of the European Communities, (No L 281/31). Retrieved from: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:31995L0046&from=en> (last time consulted: 27/04/2016)

European Parliament and of the Council. (2002), Directive 2002/14/EC establishing a general framework for informing and consulting employees in the European Community. Official Journal of the European Communities, (L 80/29). Retrieved from: [http://eur-lex.europa.eu/resource.html?uri=cellar:f2bc5eea-9cc4-4f56-889d-3cc4c5ee5927.0004.02/DOC\\_1&format=PDF](http://eur-lex.europa.eu/resource.html?uri=cellar:f2bc5eea-9cc4-4f56-889d-3cc4c5ee5927.0004.02/DOC_1&format=PDF) (last time consulted: 27/04/2016)

Community, E. (1983). 82/854/EEC: Council Decision of 10 December 1982 on the rules applicable, in the fields of export guarantees and finance for export, to certain subcontracts with parties in other Member States of the European Communities or in non-member countries, (L), 20–22. Retrieved from: <http://data.europa.eu/eli/dec/1982/854/oj> (last time consulted: 27/04/2016)

---