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Outsourcing: Prepare Now for Anti-Offshoring Legislation

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Whether any future U.S. jobs bills will contain anti-offshoring measures remains up in the air. But outsourcing customers don't have to wait to protect themselves from potential protectionist legislation.

President Barack Obama emphasized what some see as his anti-offshoring sentiment in his State of the Union address earlier this year, when he reasserted that the U.S. government should terminate tax breaks for American companies that ship jobs overseas and introduce tax advantages for those creating local jobs. (See also, "a

href="http://www.cio.com/article/492414/The_Truth_About_Obama_s_Tax_on_Outsourcing_">The Truth About Obama's Tax on Outsourcing.)

It's not just the federal government that has outsourcing customers concerned. Although states can't outright ban offshore outsourcing by a private company, several have enacted or are considering laws to slow the pace offshoring.

Such regulations may come in many forms—from restrictions on the export of personal data to changes in tax law, grants and incentive programs, to various reporting requirements about where work is being done and by whom. Thus far, the state laws that have been enacted have focused on government sourcing, not private transactions.

One way outsourcing customers can protect themselves from anti-offshoring legislation is to modify the "change in laws" provisions that are often included in contracts to address compliance issues. "No consensus has emerged," says George Kimball, an attorney in the San Diego office of Baker and McKenzie."But some contracts now provide for a process of consultation and adjustment that might lead to relocation of operations, equitable adjustment of charges, or in extreme situations, termination if future legislation prohibits, restricts or taxes offshore operations so severely that they cannot practically or economically continue."

Kimball offers this short sample clause:

> In the event of change in applicable laws, regulation or public policy that imposes a material, adverse impact on performance of Services outside of the United States or renders such performance unprofitable, then at either Party's request, the Parties shall meet and confer to discuss relocation of affected operations to the United States or such other location as may be mutually agreed by between the Parties. In such cases, the Parties will negotiate an equitable adjustment of change in the Charges sufficient to cover Supplier's reasonable, actual increased cost of providing such Services (including a reasonable margin) and reasonable, actual transition costs incurred by Supplier as a

> result of such change. Supplier will use reasonable efforts to minimize and mitigate any such transition costs and increased costs of providing the Services by, among other things, reasonably apportioning costs among other affected customers. If the Parties are unable to agree upon such a relocation and equitable adjustment in the Charges within sixty (60) days after the request to meet and confer, then (i) Customer may terminate the Agreement for its convenience in accordance with Section __, but without paying any Termination Charge; or (ii) Supplier may terminate the Agreement by giving one hundred eighty (180) days written notice to Customer and generally in the same manner as a convenience termination. In either case, Supplier shall be compensated for reasonable, actual shutdown costs (including, by way of illustration, severance, relocation and costs associated with premature disposition of assets or facilities, including unamortized investments in those assets and facilities).

Clearly, such a clause leaves much of the remedy open-ended, from what would constitute grounds for invoking this process to financial arrangements for any adjustments, relocation or termination. This approach lays out the questions that will arise while dealing with anti-offshoring laws, says Kimball, but not the answers.

It's also wise to include a right to benchmark clause if services need to be altered as a result of legislative changes, says Edward J. Hansen, a partner in Morgan Lewis and Brockius's business and finance practice.

Another alternative for offshore outsourcing clients is to opt to work with providers who have significant U.S. operations in the event that they're forced to move work onshore. Although India's IT service providers have been increasing their presence stateside, this would likely mean going with an American vendor with larger U.S. operations.

"It's important to remember that this will not be just about price, but also about migration risk," Hansen says. "It may be preferable to pay a little more for a domestic provider to re-solution than to have to migrate [to a new vendor]."

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