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Outsourcing Agreements and exit provisions

AstraZeneca UK Ltd ("AstraZeneca") v International Business Machines Corporation ("IBM") [2011] EWHC 306 (TCC)

By Barry Fishley and James Ralph

A recent (and rare) UK High Court judgment has provided very useful guidance on the operation of termination and exit provisions in the context of outsourced IT services. The decision should guide (and act as a warning) to those wishing to outsource its IT facilities, and indeed any collaborative, complex long-term partnership. Prior to contract signature, the parties must ensure that they identify (or agree a method for determining) which services are to be provided by the outgoing service provider beyond termination of the agreement, the duration and the fees to be charged (or mechanism for determining them).

Facts

AstraZeneca and IBM entered into a master services agreement ("**MSA**") in 2007 whereby IBM agreed to provide IT infrastructure services to AstraZenca, including desktop management, network maintenance and server storage hosting. In April 2010, AstraZeneca gave notice of termination.

Termination of the MSA did not lead to immediate termination of the applicable services under the contract (the "**Services**") – IBM was required to continue to deliver the Services up to and including the date determined to be the end of the "Exit Period", including "**Termination Assistance**" in accordance with Schedule 22 of the MSA. Termination Assistance included preparation of an exit plan and an IT transfer plan. As is often seen in outsourcing agreements, this mechanism of providing Services beyond termination and Termination Assistance during the Exit Period was intended to facilitate the return of the Services back to AstraZeneca or alternatively to a successor supplier.

The primary disputes related to (a) the nature of IBM's obligations during the Exit Period; and (b) payment to IBM for discharging those obligations.

The nature and scope of IBM's obligations during the Exit Period

Schedule 22 gave AstraZeneca the ability to request IBM to provide "**Shared Services**" using "shared infrastructure" for up to 12 months following the date of termination.

IBM attempted to minimise its obligations to provide Shared Services during the Exit Period by asserting that "shared infrastructure", which was not defined in the MSA, should only include hardware and software (e.g. servers, storage devices and application software used to provide the Services) and that as a result of this interpretation there were no material Shared Services. AstraZeneca argued for a much wider "shared infrastructure" definition that would encompass the physical environment and their underlying services such as power supply, heating, ventilating, access control/security and specialist staff.

Mr Justice Ramsey took heed of the principles in *Investors' Compensation Scheme v West Bromwich Building Society* [1998] 1 All ER 98, namely that the court must ascertain the meaning which the MSA would convey to a reasonable person, possessing all the background knowledge which would reasonably have been available to the parties in the situation which they

were at the time of the contract but excluding their previous negotiations and declarations of subjective intent.

Mr Justice Ramsey's decision turned on the "strong indication" that elements of staff, infrastructure and physical and logical security could all be matters of "shared infrastructure", noted in Schedule 22A as being any area of the Services "not dedicated solely for the purposes of AstraZeneca". Hence, he determined that the wider interpretation must be applied, meaning IBM was obliged to provide a wider variety of Services for the Exit Period than they had envisaged, including shared equipment, systems and facilities.

As a further blow to IBM, Mr Justice Ramsey determined that AstraZeneca was able to select exactly which Shared Services it required to be provided by IBM during the Exit Period, rather than merely an "all-or-nothing" approach.

Payment to IBM for discharging its obligations

An appendix to Schedule 22 provided that AstraZeneca would pay a fixed fee for IBM's Termination Assistance as set out in the attached exit plan (which had to be detailed and costed). However, the fixed fee was merely left blank with no amount mentioned. IBM argued that no fee could be determined and thus no Termination Assistance provided by IBM without AstraZeneca providing an IT transfer plan (being one or more plans prepared by AstraZeneca's for transferring some or all of the Services in the event of termination) and knowing the precise duration of the Exit Period. This argument failed even though the judge held that AstraZeneca was under obligation to provide an IT transfer plan. The judge stated that the fixed fee was neither conditional upon AstraZeneca producing an IT transfer plan nor upon the parties agreeing the duration of the Exit Period. Rather, it was held that the parties' intention was that IBM would provide a figure for the fixed fee, but that the fee may change depending on the content of the IT transfer plan and the actual length of the Exit Period. Indeed, Mr Justice Ramsey noted that if the exit plan had to be amended to take account of the IT transfer plan and that if such amendments changed either party's obligations under the exit plan, the amendments would only be binding if agreed by the parties pursuant to the MSA's change control procedure (presumably therefore protecting IBM from being out of pocket).

Conclusion – lessons learned from this case

- The task of determining and enshrining the nature of exit provisions in the contract will be much easier at the start of a collaboration, when the parties are on good terms and eager to establish strong working relationships. To this extent, the parties should look to agree an exit plan prior to the services commencing or, in the absence of such agreement, as a bare minimum, the contract should set out principles which will apply, for example:
  - the scope and duration of assistance the service provider will provide following termination;
  - identifying any assets and third party contracts that may transfer from the service provider;
  - the level of costs (and responsibility) or a fee determination mechanism, for example, day rates. In addition, also consider whether the responsibility and/or level of fees should be dependent on the reasons for termination (for example, where termination is due to the service provider's material breach); and
- identifying any services/ obligations which will be excluded from termination assistance.
- An obvious point, - but the parties should ensure that all critical elements of the contract are completely agreed by signature. For example, the fact that there was no figure for the fixed fee in the MSA should not have happened.
- We would expect to see provisions requiring the parties to review and update the exit plan periodically (say, annually) throughout the term of the agreement.
- Any confidentiality and/or licence terms which the service provider will seek to impose on a successor service provider before it is obliged to cooperate with it to ensure a seamless transfer of the services should be pre-agreed.

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Michael A. Epstein	(michael.epstein@weil.com)	+1 212 310 8432
Barry Fishley	(barry.fishley@weil.com)	+44 20 7903 1410

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