

TECHNOLOGY, MEDIA AND TELECOMMUNICATIONS MATTERS

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The benefits of outsourcing in the current economic climate

In the current economic climate, it may seem inappropriate to consider outsourcing services when businesses are being forced to retrench staff and cut back on expenses. Outsourcing can, however, provide a number of benefits to customers by way of cost savings, reducing their asset exposure on their balance sheet and by obtaining access to new technologies. Properly exploited, the current economic climate could yield considerable benefit for a potential customer who has increased leverage to obtain broader business benefits at reduced costs.

It is imperative that the outsourcing contract is robust yet flexible enough to protect the customers' rights and to allow the customer to exit from the arrangement if required. The current trend in outsourcing arrangements demonstrates a shift away from long term contracts, with contracts rarely extending beyond a five year term. The inclusion of early termination rights for customers and the ability for the customer to adjust the service and pricing model during the course of the agreement to cater for changing business requirements and/or economic realities, allow for increased flexibility.

There are a number of different outsourcing structures that can be used, depending on specific business and technology requirements.

These structures include single supplier outsourcing, multi-sourcing (possibly with an integrator function) and the formation of a joint venture company to carry out the services. Another trend is that of so called "cloud computing" services whereby services are offered via the internet and the customer accesses software and server infrastructure shared across the providers' client base rather than having dedicated software and infrastructure in the providers' environment which is utilised only for the customer's services.

A successful outsourcing arrangement will generally result in reduced pricing. By outsourcing services, lower prices can be achieved as the provider is usually in the position to procure attractive prices due to economies of scale and in turn offer high quality services at an acceptable price. Outsourced services further assist in reducing internal costs such as training and personnel costs, which is particularly relevant when businesses are pressed to cut expenditure. Experienced professionals are expensive to retain and outsourcing the relevant services will transfer both the cost and risk of these resources to the service provider.

Although it is a generally accepted principle that outsourcing reduces costs, it is advisable to include mechanisms in the outsourcing contract, so that the customer can ensure that the outsource produces cost effective service delivery at the agreed

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service levels over the life of the agreement. Typical mechanisms include the imposition of service level penalties for failure to meet service levels, the conducting of benchmarking exercises to verify whether the fees are in line with the relevant industry average, the inclusion of extensive audit right provisions and ultimately the right to terminate.

Competition between service providers not only results in reduced prices, but is also an incentive to provide quality services and encourages service providers to remain at the top of their game regarding developments in their field of expertise. Service providers are expected to provide services at a "best practice" standard.

Provisions entitling the customer to conduct benchmarking exercises on a regular basis for the duration of the contract are essential. Where a benchmark reveals that the services are being performed at a level lower than the benchmarked standard and the price for the services is higher than the benchmarked standard, the contract should allow for the adjustment of the service levels and price in order to eliminate the variance. The contract should also provide for termination by the customer in the event that the provider is not willing to adjust the prices or service levels or in the event that successive benchmarking exercises reveal the continued failure of the provider to meet or exceed the benchmarked standard.

To ensure flexibility, the outsourcing contract must include detailed provisions with regard to a customer's termination rights and should include a right for the customer to terminate the agreement not only in cases of non-performance, but also for convenience. It is to be noted that a right to exit the agreement early would often attract a fee.

Popular of late are the so called "step in rights", whereby the customer has certain contractual mechanisms by which it can identify early indications that a breach is likely to occur. Such contractual mechanisms include the ability to investigate, audit, suspend the agreement and/or terminate the agreement in the case of *inter alia* fluctuating credit ratings of the provider, an indication of the provider not being able to meet its debts or the occurrence of a serious security or services breach by the provider. These rights would allow for expedited action on the part of the customer so as to minimise its risk with regard to service failure and resultant lack of business continuity in appropriate circumstances. Parent guarantees can also be requested as an added measure of protection.

The benefits of entering into outsourcing contracts remain relevant in the economic crisis and may even provide businesses with relief, provided the rights of the customer are adequately safeguarded.

Preeta Bhagattjee and Simone Gill

Affiliate Marketing Programs - reward and risk!

Affiliate marketing is an Internet-based marketing practice whereby a business rewards website publishers (affiliates) for each visitor or customer brought about by the affiliate's marketing efforts. As payment is only made to an affiliate on a per-click or per-sale basis, affiliate marketing programmes are a relatively cost effective way of advertising.

Businesses embarking on an affiliate marketing programme should consider the legal risks attached to such programmes, and manage these risks by ensuring that the affiliate adheres to stringent terms and conditions designed to protect the business and its website. These include data privacy and protection, virus protection,

spamming, intellectual property right infringement, false advertising, typosquatting and brand siphoning.

Businesses should ensure that all promotional material and means used by an affiliate (including websites) do not contain any objectionable content (such as racist, pornographic, defamatory, obscene, hate-oriented or illegal content) or content that would conflict with the brand and image of the business.

Affiliate agreements should also be commercially flexible to cater for changing market conditions or new marketing trends.

Ridwaan Boda

Additional requirements under interception laws

The Regulation of Interception of Communication and Provision of Communication-Related Information Act, No 70 of 2002 (RICA) was enacted to facilitate and regulate the interception of certain types of communications.

The RICA Amendment Act, No 48 of 2008 (the Act), amends RICA by introducing more detailed compliance obligations in respect of information to be recorded and stored by electronic communication service providers (ECSPs) providing mobile cellular communications services. An ECSP includes anyone who provides electronic communication services in accordance with the provisions of the Electronic Communications Act, No 36 of 2005, including internet service providers and any person who provides a local access communication service, public pay-telephone service, value-added network service and the like. In terms of the Act, ECSPs are obliged to record and store information (in or on a secure facility with controlled access) relating to (i) each SIM-card to be activated; and (ii) the details of the applicant (including the name, identity number and address and in the case of a juristic person, its name, address and registration number, including the details of its authorised representative). The ECSP is further obliged to verify the authenticity of the information obtained.

Where a customer (any person who receives or has received services or who has contracted with an ECSP to provide services) provides an activated SIM-card to anyone other than a family member, both the customer and the person who receives the SIM-card are obliged to provide the ECSP with all information which the ECSP is obliged to record, store and verify in terms of the Act.

The information recording and storage obligations imposed by the Act also apply to businesses that provide SIM-cards to their employees. In this case, the business is obliged to record the date on which, and the period for which, the SIM-card is provided and all information relating to the employee that the Act obliges an ECSP to record. It must also verify the recorded information, report any incidents of suspected use of false verification documents to the police and store all recorded information for a period of five years.

Non-compliance may in certain instances be an offence, for which a business could be liable for a fine of up to R2 000 000 or imprisonment for a period of up to 10 years.

Preeta Bhagattjee and Simone Gill

Managing the risks relating to termination of Outsourcing Agreements

At the commencement of an outsourcing relationship, the parties may often overlook issues that may occur, or become relevant, upon termination of the relationship. Including comprehensive provisions in an outsourcing agreement relating to the provision of termination and handover assistance by the service provider at the termination of an outsourcing relationship, is vital to a successful outsourcing arrangement. Such handover assistance would include the conversion and return of customer data and the return of assets, software, intellectual property and documentation. It typically also includes the provision of appropriate training and hand over advice and assistance.

Given the possibility of the relationship between the parties having soured at termination, placing positive contractual obligations on a service provider to carry out these handover activities serves as an effective tool to facilitate the smooth and orderly transition of the outsourced services from the incumbent service provider to

another provider or back to the customer itself. These contractual protections would also ensure that the service provider is obliged to co-operate with the customer and any replacement provider and assist with managing the risk relating to continuity of services.

In addition to agreeing the principles that will govern the handover process, the parties should agree a detailed disengagement plan at the commencement of the relationship that will establish the parties' respective obligations. It is advisable to provide for a minimum time period in which the service provider is obliged to perform these handover services.

To ensure continuity of the outsourced services, both during and after disengagement, the customer may require the use of assets, employees and third party services used by the service provider to provide the services.

Should the customer require the assignment of any third party licenses and/or contracts used by the service provider to provide the services, this should also be specifically catered for in the outsourcing agreement. The service provider should also agree to grant the customer and/or the replacement provider with the necessary licenses to use any relevant service provider intellectual property necessary to continue with the services.

The customer is often afforded the option to purchase any assets used by the service provider to provide the services to the customer and to offer employment to the service provider employees used to perform the services that it may wish to hire. Care should be taken in this respect to include provisions to prohibit the service provider from

charging placement fees and relying on any restraint of trade agreements in place between it and its employees. In addition, the impact of the provisions of section 197 of the Labour Relations Act, No 66 of 1995 should be considered and indemnities in this respect should be required.

The agreement should also specify how the fees in respect of these handover services will be calculated. The cost of disengagement will usually only be borne by the customer where an outsourcing agreement is terminated by the customer for convenience or as a result of a breach by the customer of any of its obligations pursuant to the agreement or where the agreement expires and is not renewed.

Preeta Bhagattjee and Simone Gill

Multi-sourcing - a new trend in outsourcing

In recent times, multi-sourcing has become popular in the sourcing market. As opposed to the traditional outsourcing model whereby all IT services are outsourced to a single service provider, with multi-sourcing, the services are allocated across a number of different service providers. This allows for specific services being provided by a service provider who has the best capabilities to provide such services, rather than one service provider who is, across all services, considered to have adequate all-round capabilities.

There are a number of commercial and technical benefits in certain businesses arising from embarking on a multi-sourcing approach, such as reducing the customer's dependency on a single service provider. At the same time, multi-sourcing does add more complexity.

For example, the customer would require more resources to manage multiple providers as opposed to just one provider in a single sourcing model. Often, one of the providers is appointed to undertake a service aggregator role to manage the services being provided by all the other service providers. This can add to a customer's cost base and would have to be appropriately managed in the contract to ensure that the customer is able to obtain the business benefits for it adopting a multi-sourcing model.

Multi-sourcing is not without legal risks. The contracting model is more complex, with a requirement to have separate contracts

in place with each of the service providers, that correlate with each other to ensure that the customer is appropriately protected. More care has to be taken to ensure that each service provider's scope of services is correctly defined to avoid any gaps in the services with certain service requirements "falling through the cracks" and consequently, none of the service providers claiming responsibility for performing these services. There are also issues of the sharing of intellectual property rights and confidential information between service providers, which would have to be appropriately catered for.

The service providers would be required to co-operate with each other to ensure that the customer obtains continuous, end to end services. It is advisable that appropriate contracting structures are put in place to safeguard the customer in this regard.

Multi-sourcing arrangements require more rigorous and comprehensive governance structures, with specific escalation and dispute resolution procedures that cater for inter-service provider related disputes or issues. Termination clauses also need to be carefully considered, with appropriate flexibility drafted into agreements to allow for one or more service provider's contracts to be terminated at a different time to the others, such as in the case of a termination as a result of the breach of the agreement by a service provider.

Preeta Bhagattjee

King III: IT Governance

The King III report on corporate governance was recently published by the Institute of Directors. The new report applies to all entities "regardless of the manner and form of incorporation or establishment". The preface of the report states that the principles have been drafted on the basis that, each entity is different in many ways and "[f]or that reason, we have not focused on or discussed the implementation of the code and each entity should consider the approach that best suits its size and complexity". The report does not prescribe specific mechanisms or approaches to corporate governance but sets out key principles that a business should adhere to.

Predecessor reports to King III did not specifically deal with IT governance as information systems were then only used as enablers to businesses, or at best, had a supporting function. Today IT forms part of the core of a business and is part of its strategy and thus "the risks involved in information technology (IT) governance have become significant".

Directors of companies owe a duty of care to shareholders of the company. King III states that a fundamental element of this duty of care is that of risk management. As indicated, IT is one of the key risk areas for companies and the onus of managing this risk lies not only with executives, but also directors. In order to manage the risks of a company and discharge their duty of care, directors need to implement good corporate governance including IT governance.

King III states that the "objective of IT governance is to understand the issues and the strategic importance of IT so that a company can sustain its operations and implement the strategies required [in] extending its activities into the future. IT governance aims at ensuring that expectations for IT are met and IT risks are mitigated". In order to mitigate this risk an entity must ensure that its IT governance structure is a "framework that supports the effective and efficient management of information resources (for example people, funding and information) to facilitate the achievement of corporate objectives. The focus is on the measurement and management of IT performance to ensure

that the risks and costs associated with IT are appropriately controlled".

King III provides four key areas of focus required to create an IT governance framework: (i) the strategic alignment of IT with the business' core strategy and function by creating collaborative solutions, including a focus on sustainability and the implementation of 'green IT' principles; (ii) value delivery: (concentrating on optimising expenditure and proving the value of IT); (iii) risk management: (addressing the safeguarding of IT assets, disaster recovery and continuity of operations); and (iv) resource management: (optimising knowledge and IT infrastructure).

Much emphasis is placed on the alignment of IT with business strategies. Such alignment "involves making certain that business and IT plans are linked together; defining, maintaining and validating the IT value proposition; and aligning IT operations with overall business operations".

Emphasis is also placed on IT security. With information being a key asset to businesses, the duty rests on the directors to ensure that this information is secure. The report states that "Information security deals with the protection of information, in its electronic and paper-based forms, as it progresses through the information lifecycle for capture, processing, use, storage, and destruction. For this reason, information security has to address people-, process- and technology-related dimensions in order to be truly effective."

In order to ensure compliance with the King III requirements, directors need to be fully apprised of the relevant laws relating to IT governance and the legal implications for their businesses.

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