

To Outsource or Not to Outsource

By Jen C. Salyers and Katheryn A. Andresen¹

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¹ Ms. Salyers and Ms. Andresen are Partners in Bonnabeau, Salyers, Stites and Doe, L.L.C., where they specialize in information technology law. Copyright © 2004 by Katheryn A. Andresen and Jen C. Salyers. All rights reserved.

I. Introduction

Although outsourcing, specifically off-shore outsourcing, is currently a political hot potato, businesses have used the outsourcing concept for centuries. In the 17th century, the East India Trading Company outsourced its buyers, translators and guides. In today's market, outsourcing allows businesses to contract for specific deliverables and services that are not a standard part of their business, but which are critical to expanding their growth.

In particular, it has become abundantly clear in the last few decades that companies in the 21st century require information technology ("IT") services and access to the Internet to succeed. For many companies, these IT services may include services like network management, customer service help centers, application development/implementation/management services, data center management and maintenance. Software service contracts in particular may encompass any aspect of business management: financial, human resources, distribution or time management. A company has several options for addressing these IT service needs including: hiring the staff needed to implement in-house; contracting with specific IT personnel for specific functions; or outsourcing the entire project and/or department for a specific deliverable or service.

Some companies have learned the hard way that deciding to keep everything in-house may be both costly and a deterrent to meeting growth goals as the company deals with IT issues that are not the primary service offered by the company. While internal staff means the company retains full control over the personnel and the security of company information, it is not necessarily the most efficient means of meeting the company's IT needs. The IT field changes daily and requires constant upgrades and modifications for advances made in both hardware and software.

Staff augmentation may meet the IT needs for smaller businesses. An example might be contracting with an independent contractor to manage the company's network. This type of contracting provides a company with more flexibility to increase or decrease the number of independent contractors as the business needs change without having the employment issues implicated when firing or terminating an employee. This type of contracting may be considered "simple outsourcing," but it is not without risks as Microsoft discovered in the late 1990's.²

Like Microsoft, larger companies are often able to negotiate better service contracts due to the amounts being spent on these software services. In the current market, it is common for large IT service contracts to cost millions and have initial terms anywhere from five to ten years. At this level of cost and commitment, all companies should be willing to take the time and legal precautions necessary to ensure they receive the expected deliverables and services. This is especially critical to ensure that a

² See *Vizcaino v. Microsoft Corp.*, 97 F.3d 1187 (9th Cir. 1996) ("*Microsoft I*") and page 2 *infra*.

company's intellectual property and company information is kept secure despite having IT contractors involved deeply in the operations of the company.

II. Staff Augmentation – “Simple Outsourcing”

Many companies have hired independent contractors for specific projects or functions. There are both business and legal issues to be considered before contracting with an independent contractor. An independent contractor provides the expertise the company requires without paying the premium for hiring an expert as a full-time employee. The company may, however, need additional investment in facilities or systems to provide the independent contractor with the tools he/she needs to deliver the services. Since the contract is on an individual basis, the company has more control over intellectual property protections as the independent contractor would be personally liable for violating the confidentiality clause or agreement.

Independent contractors should be hired using a written agreement. There are several questions that should be asked prior to signing a service agreement with an independent contractor: does the contractor operate as an individual or as a corporate entity; if the contractor operates as a corporate entity, what is the structure of this entity; does the contractor have employees; is the contractor currently licensed (if licensure is a requirement for the deliverable/service); does the contractor use personalized business cards, stationery and invoice forms; and is the contractor insured? These questions are designed in part to ensure that the independent contractor is not later deemed to be an employee for tax purposes which developed out of the *Microsoft I* case.

Heading into the start of the tech-boom in the 1990's, Microsoft found that it needed additional IT staff to meet its business needs. A decision was made to hire the additional personnel through staffing agencies on an independent contractor basis in order to avoid the added cost of providing the benefits to which a full-time employee would be entitled. Microsoft, however, was not willing to relinquish control over the contractors and used its size and power to negotiate contracts which were heavily weighted in Microsoft's favor for controlling the salary, location of the work, hours, equipment, and right to terminate. Microsoft was audited by the IRS for open tax years of 1989 and 1990 and the IRS determined there are twenty factors which may be considered to determine if a “contractor” is really an employee.³

Microsoft failed this twenty-factor test because the company treated the independent contractors like employees. These workers were ultimately deemed employees because they were: on the same teams as employees; supervised the same; performed the same functions; worked on site; had admittance keys; and received supplies and office equipment from Microsoft. After the IRS found these workers to be employees for tax purposes, several of the independent contractors sued Microsoft to be deemed employees in order to get 401(k) plan and stock purchase plan benefits. Although Microsoft won at the district court level in the Western District of Washington,

³ See 26 C.F.R. sss 31.3401(c)-1(b) and Rev. Rule 87-41, 1981 – 1 Cum Bull. 296, 2980299.

the Ninth Circuit reversed the district court and held that the independent contractors were employees.⁴

The primary test as to whether an independent contractor will be deemed an employee is whether the company has the right to control not just the end result to be accomplished but also “the manner and means” by which the result is accomplished. The twenty factors include: the ability to instruct the contractor; obligation to provide training; right to integrate the contractor into normal business operations; whether the services are rendered personally; the right to hire and/or supervise the contractor; whether there is an ongoing relationship; the ability to set the contractor’s work hours; if the work is full-time; if the contractor is required to work on site; whether the company may set the order of work; if there are reports required; whether the contractor is paid by time increments; whether the contractor may be reimbursed for travel and/or business expenses; who must furnish supplies for the contractor; whether the contractor assumes the investment or risk; whether the contractor realizes the profit or loss from the deliverable; whether the arrangement is exclusive or not; whether these services are available to the general public; whether the company has the right to discharge; and whether the company has the right to terminate the contract. The Supreme Court later reduced this twenty-factor test to the twelve most-significant considerations in *Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318, 112 S. Ct. 1344, 117 L.Ed. 2d 581 (1992). The *Darden* factors are: skill required; source of tools and instrumentalities; location of the work; duration of the relationship of the parties; hiring party’s right (or lack thereof) to assign additional projects; method of payment; hired party’s role in hiring and paying assistants; whether the work is part of the hiring party’s regular business; whether the hired party is in business; whether “employee benefits” are provided; and the tax treatment of the hired party.

III. Outsourcing Functions or Projects

Generally speaking, large outsourcing contracts are less likely to fall into the *Microsoft I - II* case issues because the contracts are generally with corporate entities who maintain control over the contracted workers. As in the case of the simple outsourcing, a company needs to do a cost-benefit analysis of outsourcing before entering into such a large, complex agreement. One of the first considerations is whether the function is one that requires an area of expertise not endemic to the company’s business. Outsourcing a process or service which is necessary, but not part of the core operations, can save a company both time and money in the long run. The return on investment (“ROI”) benefits include: a reduction of risk for employment issues while still receiving quality services by expert personnel; administrative convenience; single source control of company information security through a confidentiality provision or agreement; and flexibility to contract for these services in increments according to business needs.

Additional issues may arise with large-scale outsourcing. There may be a negative impact on internal employee morale if the outsourcing leads to a reduction in

⁴ *Vizcaino*, 97 F.3d 1187; confirmed by *Vizcaino v. Microsoft Corp.*, 120 F.3d 1006 (9th Cir. 1997) (“*Microsoft II*”).

workforce. In order to avoid the *Microsoft I and II* results, companies need to give up control over “the manner and means” in which the deliverables or services are provided. When entire functions are outsourced, a company must consider data security issues, as well as ensure that the outsourcing doesn’t take on a life of its own through cascading work orders or scope creep. Perhaps the biggest concern, however, is what happens when the outsourcing contract is either concluded or fails. In addition to regaining access and control over the company information at issue, a company will need to know in advance if there will be software, hardware or even formatting issues to be addressed to transfer that function either back in-house or to another vendor.

A Deloitte & Touche survey found that 53% of companies will ultimately attempt to renegotiate the original terms of a contract with their vendor partners and that one-fourth of these attempts will end in the termination of the relationship.⁵ Interestingly enough, longer-term contracts offer fewer cost savings to a company and may be more uncertain. These contracts do not always address changes in technology or unforeseen issues like the Y2K issue. In addition, these longer-term contracts bind both the company and the vendor financially and functionally in a relationship that means a loss of flexibility which is one of the key benefits to outsourcing.

IV. Specific Legal Protections to Consider

A company should address certain legal points in either a simple or complex outsourcing deal: description of the services; payment terms (addressing fees, timing of payments and expenses); materials/equipment; affirmative statement that relationship is as an independent contractor; warranty by the vendor that all necessary licenses and permits required are current and that liability insurance is carried; affirmation by the vendor that it is responsible for any taxes and that it is not entitled to employee benefits; definition of term and termination rights; confidentiality of company information; and dispute resolution terms. The legal structure of an outsourcing deal is often completed through a master service agreement (“MSA”) which has basic terms for all contractual work and individual work orders (or service level agreements) for the specific definition of the project/function, the timetable for the deliverables and the payment terms for that project.

Some of the common issues from outsourcing contracts include:

- who owns the deliverables (i.e. copyright);
- who is liable for confidentiality breaches;
- how is the intellectual property and company information protected;
- how does a company avoid having the contractor personnel deemed employees of the company;
- does the company have the right to hire any contractor personnel;
- what needs to be accomplished to ensure access to company information upon termination of the contract; and

⁵ Caldwell, B. “Outsourcing Backlash,” *InformationWeek*, (650 September 29, 1997, pp 14-16.)

- how much control can the company exert over the deliverables and services before running into the *Microsoft I* issues?

There are several provisions that are specific to an outsourcing MSA. These provisions specify the contractor's responsibilities and liabilities in providing contract personnel to meet the deliverables and services.⁶ A company may want the right to review resumes of the contractor's personnel and receive assurances from the contractor that these personnel are not employees of the company. In addition, the company may require a clause that these personnel are subject to a screening process for criminal backgrounds or even drug testing. This type of clause is especially critical for businesses dealing in the financial, health and insurance fields.

Another critical clause for IT outsourcing contracts is the "ownership" clause. When the deliverable for the contract is software or some other authored component, it is critical that the contract specify that the work will be completed on a "work for hire" basis. Under basic copyright law, the author (or programmer) of the deliverable is the copyright owner unless: (i) the author is an employee doing the work during the normal course of business for his/her employer; or (ii) the author signs a written agreement that specifies that the work will be on a "work for hire" basis. In order to avoid further complications if the copyright rights are not deemed to be appropriately classified as a "work for hire," most of these provisions continue with caveats that the contractor assigns all rights and will be contractually obligated to undertake any other action necessary to enforce the assignment of rights.

The copyright concerns in the "ownership" clause are part of the overall intellectual property and company information that should also be protected by terms in the agreement. Confidentiality clauses should be incorporated that require the contractor, as well as all of the contractor's personnel, to protect this information to maintain its confidentiality. The contractor will typically agree to return all confidential information upon the conclusion of the agreement. In addition, to fully protect the company's interests, the remedy for a breach of confidentiality needs to specifically include equitable relief (like acquiring a temporary restraining order). Confidentiality may also be addressed in a separate confidentiality or non-disclosure agreement ("NDA".) This type of drafting requires a clause in the master service agreement that specifically incorporates the NDA or Confidentiality Agreement into the main agreement. One benefit to a separate NDA is that a company may mandate that the contractor ensure all contractor personnel review and sign a copy of that agreement.

Another typical clause in an outsourcing contract is one that precludes solicitation of each other's employees. This bar on solicitation is typically limited to terms that are reasonable and likely to be upheld by a court (e.g. twelve months.) This provision, along with any non-compete provision may have different employment law implications that should be considered based on the jurisdiction to be applied to the contract. Some states will not enforce a non-compete provision, so some of the protections intended by this

⁶ See Section 2.3, 2.4 and 2.5 of the Draft Master Service Agreement attached which refers to "Consultant" rather than "contractor".

provision need to be addressed separately. For example, a software contractor may be asked not to re-use code that is developed specifically for the company. The limitations on this use may be limited to a functional version of the software, or allow re-use as long as it is less than a certain percentage of the final software product. In addition, the limit on use may be specifically geared only to a certain industry or competitive market.

A company should ensure that the protections included in the master service agreement are not removed or modified in the drafting of the specific work orders. To this extent, each work order should be reviewed for possible implications to the terms of the master agreement.

V. Conclusion

Companies should address this myriad list of issues in the outsourcing contract prior to any deliverables or services commencing. The reason for this review and inclusion of specific provisions is to avoid the *Microsoft I – II* outcomes where contractors were deemed employees and the company was out millions of dollars in additional benefits to be paid. A well-written contract is designed to avoid conflicts during the contract and through its termination. In particular, companies should ensure that the outsourcing contract will: provide the services or deliverables needed; allow for adequate remedies if the services or deliverables are not met; avoid uncapped liability should the contract fail; allow for modifications as needed; require assurances that the personnel used do not create further liabilities (i.e., by requiring criminal background checks); require assurances that the contractor will indemnify the company for any third party copyright or other violations; require assurances that the contractor and its personnel will protect the confidentiality of the company information; maintain contractual control over the quality of the deliverables or services without dictating the “manner and means” of that performance; and provide for the appropriate transfer of the deliverables or services back to in-house or to a third party should the contract fail or be terminated.

A. APPENDIX – Draft Master Services Agreement

[NOTE: This agreement is intended for educational purposes only and should not be used as an actual MSA agreement. Copyright @ 2004 by Katheryn A. Andresen and Jen C. Salyers. All rights reserved.]

THIS MASTER SERVICE AGREEMENT (the “*Agreement*”) is made as of this _____ day of _____, 2004 (the “Effective Date”) by and between _____, Inc. (“*Company*”), a _____ corporation with principal offices located at _____, and _____, Inc. (“*Consultant*”), a _____ corporation with principal offices located at _____. (Company and Consultant are each referred to herein as a “Party” and collectively as the “Parties.”)

1. DEFINITIONS

“**Addendum(a)**” means any document executed by both Parties which modifies this Agreement or any Work Order.

“**Agreed Specifications**” means

“**Agreement**” means this Master Service Agreement, and all current and future attached Addendum(a) and all mutually executed Work Orders.

“**Consultant Technology**” means all proprietary software created or otherwise provided by Consultant, and all text, multimedia, graphics, audio, video, data and other information utilized by Consultant in the Deliverables or Services.

“**Deliverables**” means any development materials, documentation, specifications, and any other deliverables delivered by Consultant to Company in accordance with one or more Work Orders.

“**Derivative**” means

“**Developed Work**” means

“**Intellectual Property Rights**” means, collectively, rights under patent, trademark, copyright and trade secret laws, and any other intellectual property or proprietary rights recognized in any country or jurisdiction worldwide, including moral rights and similar rights.

“**Services**” means the professional consulting or development services performed by Consultant renders to Company in accordance with one or more Work Orders.

“**Third Party**” means any entity other than Company and Consultant.

“**Work Order**” means a written order for any Service and/or Deliverable.

2. SERVICES

The Parties agree that Company is relying on Consultant’s skill and judgment to develop and deliver the Deliverables and/or provide technical personnel to perform the Services in a manner consistent with or exceeding generally accepted industry practices and procedures. Consultant will provide the Services defined in mutually executed Work Orders, which will be attached and incorporated into this Agreement as separate Exhibits. Unless specified in writing to the contrary, each Work Order shall be independent from, and have no impact upon other Work Orders.

2.1 Primary Contacts. Company and Consultant each appoint the individuals designated on the relevant Work Order to act as their respective primary contact (“Primary Contacts”). The Primary Contact will be responsible for his or her Party’s performance under a Work Order and will have approval authority for Change Authorization and certain other operational matters as set forth below or in the relevant Work Order. The Primary Contacts will act as the point of contact for all written notices, Work Order modifications, and review or sign off on the Work Order Deliverables and Services. Primary Contacts may not be changed without written notice to the other Party prior to the change.

2.2 Work Order. Each Work Order represents the Parties agreement as to the scope of work and time required to complete the Deliverables and/or Services.

2.3 Consultant’s Personnel. Company shall have the right to review any resume of any Consultant employee, agent, officer, director, or permitted subcontractor assigned to perform Services hereunder (“Consultant’s Agent”) prior to or during its engagement of Services. Consultant agrees that Consultant’s Agents are not employees of Company and are not entitled to any rights, benefits or privileges provided by Company to its employees. Consultant agrees to communicate this to Consultant’s Agents prior to their assignment to perform Services under this Agreement. Consultant acknowledges that it is solely responsible for the payment of compensation to its Consultant’s Agents, including taxes, contributions and benefits. Company will not have any obligation to pay any amount to Consultant’s Agents, including any “overtime” or premium payments. Consultant will allow Company to determine the selection of Consultant’s Agents for each Work Order. Consultant will monitor, supervise and direct Consultant’s Agents in the performance of the Services for Company. If Company determines that the Services of any of Consultant’s Agents are unacceptable for any reason, at Company’s request Consultant will assign a satisfactory replacement for such Consultant’s Agent within two weeks or Company may elect to terminate this Agreement or the relevant Work Order immediately for cause, in accordance with the provisions in Section __. In addition, Consultant shall bear the cost of any retraining due to Company’s exercise of its’ rights herein.

2.4 Consultant Responsibilities.

2.4.1 In conjunction with its usage of the Services:

2.4.1.1 Consultant shall furnish to Company in a prompt manner such data, documents, information, materials, decisions or approvals of Consultant as Company shall reasonably request or require.

2.4.1.2. Consultant shall ensure that all physical media that Consultant furnishes to Company for processing meet the specifications of the manufacturer of the equipment with which such media are to operate and any other specifications that Company may reasonably establish.

2.4.1.3 As part of Company's security measures, it will assign Consultant one or more user IDs and passwords which will enable Consultant to access the Hardware, Software and Internet (“Company Resources”) as necessary to perform the Deliverables and/or Services. Consultant shall maintain control of and accept responsibility for all use of

any IDs and passwords by Consultant and shall restrict the disclosure of such IDs and passwords to Consultant's personnel on need-to-know basis. Consultant shall take reasonable precautions to protect against the theft, loss or fraudulent use of such IDs and passwords. Consultant shall immediately notify Company of any suspected theft, loss or fraudulent use of such IDs and passwords.

2.4.1.4 Consultant shall be responsible for providing the resources and performing the obligations which it undertakes in the Work Orders.

2.4.1.5 Consultant will not use the Company Resources: (i) for unlawful purposes including, without limitation, infringement of patents, copyright, trademark, misappropriation of trade secrets, wire fraud, invasion of privacy, pornography, obscenity and libel, or (ii) to interfere with or disrupt other network users, network services or network equipment. If Company has reasonable grounds to believe that Consultant is utilizing its Company Resources for any such improper purpose, Company may suspend or terminate the Services immediately upon notice to Consultant.

2.4.1.6 Consultant and Consultant's Agents acknowledge that Company monitors the use of its Company Resources. Consultant consents and will cause Consultant's Agents to consent to such monitoring and to the use by Company of information obtained through such monitoring.

2.4.2 Reports. As more fully set out in a Work Order, Consultant shall confer with Company as often as may be reasonably necessary or requested by Company regarding the status of such Services and obligations due to be completed by Consultant under a Work Order and will provide written reports as set forth in any Work Order.

2.4.3 Screening Processes.

2.4.3.1 Company may require that Consultant submit any and all Consultant's Agents to be assigned in connection with the performance of Services under this Agreement and any Work Order to a screening process. This process may include, but not be limited to, employment eligibility verification, education verification, criminal background investigations, testing for substance abuse, and Department of Motor Vehicle inquiries. Consultant represents that all such investigations, inquiries, or tests required by Company will be conducted as a precondition of assignment to the performance of Services and provision of Deliverables under this Agreement and/or any Work Order, with the knowledge and consent of the Consultant's Agents involved, and in compliance with all applicable state and federal laws and regulations.

2.4.3.2 In addition to any criminal background checks that Company may require pursuant to Section 2.4.3.1 above, it is mandatory for Consultant to conduct, and document in Consultant's files, a criminal background check for Consultant's Agents performing Services for Company who has key or card key access to Company's offices. The background check must take place prior to such individual beginning to

perform Services on Company's premises, networks, and/or access to any Company Confidential Information or other Company data. The background check should include all states in which the individual resided or worked during the seven (7) years prior to the date such individual will commence performing Services for Company. In the event that an individual has had any felony or gross misdemeanor convictions during such seven (7) year period, Consultant shall inform Company of such information, and Company's Primary Contact shall have the sole discretion to make a final determination on the individual's eligibility to perform work for Company taking into account factors deemed relevant by Company. Consultant may select its verification sources, provided, however, that the source of the verification must meet Fair Credit Reporting Act (FCRA) standards and/or other relevant legal standards. Upon Company's request, Consultant will provide documentation to Company evidencing Consultant's compliance with the terms of this Section 2.4.3. A criminal background check completed prior to Consultant's Agent beginning Services on Company's premises will be valid for multiple Work Order's so long as the break in service from Company's projects does not exceed ninety (90) days.

2.4.4 Subcontractors. In performing its obligations under this Agreement, Consultant shall use only employees of Consultant and shall not subcontract any work to a subcontractor without the prior written approval of Company.

2.5 Ownership and Non- Compete. All Deliverables prepared by Consultant for Company under this Agreement shall belong exclusively to Company and shall be deemed to be "Works Made For Hire." To the extent such works are not deemed to be "Works Made For Hire," Consultant hereby assigns all proprietary rights, including copyright, in these works to Company without further compensation. All ideas, concepts, information, and written material disclosed to Consultant by Company, are and shall remain the sole and exclusive property and proprietary information of Company, and are disclosed in confidence by Company in reliance on Consultant's agreement to maintain them in confidence and not to use or disclose them to any other person except in furtherance of Company's business. In addition, all records, files, specifications, technical data and all related material that are used by, developed for, or paid for by Company in connection with the performance of any Services provided hereunder shall be and remain Company's sole property.

Consultant further agrees that all right, title and interest in and to all developments, creations, and copyrightable material which Consultant shall conceive or originate, whether individually or jointly with others, and which arise out of the performance of the Services, will be the property of Company and is by this Agreement assigned to Company along with ownership of any and all patent rights in the inventions and copyrights in such materials. Consultant agrees to execute and sign any and all applications, assignments, or other instruments which Company may deem necessary in order to enable Company, to apply for,

prosecute, and obtain copyrights, patents or other proprietary rights in the United States and foreign countries or in order to transfer to Company to acquire or exercise the rights set forth herein.

3. **TERM**

The term of each Work Order is set forth in, and renewable in accordance with, the Work Orders. A particular Work Order may be terminated without affecting the other Work Orders. This Agreement shall remain in effect for so long as there is outstanding any Work Order with a term then in effect, unless sooner terminated as provided herein.

4. **PAYMENTS**

4.1 Fees, Payment, and Taxes.

Consultant will pay the amount(s) specified in each Work Order. Fees remain in effect until the date specified in the Work Order. Payments are due within thirty (30) days of the date of Company's invoice. Late payments are subject to an interest charge, which is the lower of one and one-half percent (1.5%) per month or the maximum legal rate. Consultant is responsible for the payment of all taxes associated with this Agreement or Consultant's use of the Services.

4.2 Insurance.

Consultant shall maintain adequate liability insurance and insurance against loss or damage to Company's Hardware located on Consultant's premises (if provided). Upon request, Consultant shall furnish to Company evidence of insurance coverage.

5. **TERMINATION**

5.1 Consultant or Company may terminate this Agreement and all Work Orders, or any Work Orders, for convenience on or after the first anniversary of the Effective Date of the affected Schedule(s), upon a minimum of six (6) months' prior written notice to the other. If Consultant terminates any or all Work Orders pursuant to this paragraph on or before the end of the then-current term of the affected Work Order(s), Consultant agrees, as a condition to such termination becoming effective, to pay Company a termination charge in accordance with the affected Work Order(s) (the "**Termination Charge**"). The Parties acknowledge and agree that the Termination Charge represents a reasonable estimate of the loss of investment, lost profits and other economic loss and costs that would result to Company proximately from Consultant's early termination for convenience of this Agreement, that it is not a penalty, and that it will be in lieu of all other monetary remedies Company may have for such early termination. Any Termination Charge will be pro-rated for partial months.

5.2 If either Party believes that the other Party has failed in any material respect to perform its obligations under this Agreement, then that Party may provide written notice to the breaching Party describing the alleged failure in reasonable detail. If the breaching Party does not either: (i) cure the material failure within thirty (30) calendar days after receiving such written notice; or (ii) if the breach is not one that can reasonably be cured within thirty (30) calendar days after receiving such written notice, develop a plan to cure the failure and

diligently proceed according to the plan until the material failure has been cured, then the non-breaching Party may terminate this Agreement for cause by written notice to the non-breaching Party. Termination of this Agreement will be in addition to, and not in lieu of, other remedies available to the terminating Party under this Agreement.

5.3 Within thirty (30) days after the expiration or termination of this Agreement for any reason, the receiving Party must destroy the original and all copies (including partial copies) of all Confidential Information of the disclosing Party, including copied portions contained in derivative works. In addition, at such time, Consultant will return or destroy at Company's instruction the original and all copies (including partial copies) of all other materials provided by Company under this Agreement, including copied portions contained in derivative works. Within such time period, each Party will certify in writing to the other Party their respective compliance with this provision of the Agreement.

5.4 The following provisions shall survive termination of this Agreement for any reason: Sections __, __, __, and __.

6. CONFIDENTIALITY

Consultant acknowledges that by reason of its relationship to Company under this Agreement it may have access to Company's "Confidential Information," which includes, without limitation, certain information and materials concerning the other Company's business plans, pricing, customer information, technical information, marketing plans, research, designs, plans, methods, techniques, processes and know-how, whether tangible or intangible and whether or not stored, compiled or memorialized physically, electronically, graphically or in writing, which value would be impaired if such Confidential Information were disclosed to Third Parties. Consultant agrees to maintain all Confidential Information received from Company in confidence and agrees not to disclose or use such Confidential Information, other than in performance of this Agreement as permitted by Company, without the prior written consent of Company. Consultant hereto agrees not to disclose to any Third Party the terms of this Agreement without the prior written consent of Company, except to advisors, investors and others on a need-to-know basis under circumstances that reasonably ensure the confidentiality thereof, or to the extent required by law. Consultant's obligations of non-disclosure under this Agreement shall not apply to Confidential Information which: (i) is or becomes a matter of public knowledge though no fault of or action by Consultant; (ii) was rightfully in Consultant's possession prior to disclosure by Company; (iii) is independently developed by Consultant without resort to Confidential Information; or (iv) is required to be disclosed by law or judicial order, provided that prior written notice of such required disclosure is furnished to Company as soon as practicable in order to afford Company an opportunity to seek a protective order and that if such order cannot be obtained disclosure may be made without liability. Whenever requested by Company or upon the expiration or termination of this Agreement, Consultant shall immediately return to Company all manifestations of the Confidential Information or, shall return or destroy all such Confidential Information as Company may

designate. Consultant acknowledges that any breach of any of its obligations with respect to Company's Confidential Information under this Agreement may cause or threaten irreparable harm to Company and, accordingly, Consultant agrees that in such event Company shall be entitled to seek equitable relief to protect its interests.

7. **WARRANTY AND DISCLAIMER**

Consultant represents and warrants that: (i) it has the right, power and authority to provide the Services and Deliverables to Company for use or access pursuant to this Agreement and such will not violate or infringe upon the rights of third parties; and (ii) Consultant will perform the Services in a professional and workman like manner in accordance with industry standard practices. EXCEPT AS EXPRESSLY PROVIDED IN THIS AGREEMENT, COMPANY DISCLAIMS ALL OTHER WARRANTIES AND CONDITIONS, EXPRESSED, IMPLIED OR STATUTORY, INCLUDING WITHOUT LIMITATION, THE WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, TITLE AND NON-INFRINGEMENT.

8. **INDEMNITY**

8.1 Company Indemnity.

Subject to Sections 8.2 through 8.4, Company will: (i) defend Consultant against any claim that Company's contributions to the Service infringes any Intellectual Property Right of any Third Party, and (ii) pay reasonable costs, attorneys fees, damages and settlement fees finally awarded against Consultant resulting from such claims. In addition, if in Company's opinion, such a claim is likely to occur, Company may, at its sole option and expense, (subject to its agreements with its vendors) either: (a) procure for Consultant the right to continue using the materials in question; or (b) replace or modify the infringing materials so that they become non-infringing as long as functionality is not materially and adversely affected. If neither alternative (a) nor (b) is reasonably available, the Work Order affected by the infringing Services will be terminated with no further payment obligations by Consultant thereunder.

8.2 Exclusions.

Company shall not indemnify Consultant or be liable for claims based on: (i) the combination, operation or use of the Services (or any of Company's contributions of the Service) or other technology, content, data or materials provided by Company with technology, content, data or other materials not supplied by Company if the claim would have been avoided by use of other technology, content, data or other materials; or (ii) modifications to Service (or any of Company's contributions of the Service) or other technology, content, data or materials provided by Company if the modifications were not made by Company.

8.3 Consultant Indemnity.

Consultant will: (i) defend Company against any claim that: (a) the Consultant Content (or the combination, operation or use of the Services therewith), or any other materials or intellectual property supplied by or on behalf of Consultant hereunder infringes upon the Intellectual Property Rights of any Third Party, (b)

arises from or relates to a breach by Consultant of any of Consultant's warranties, the Company Policies, or of this Agreement, or (c) arises from or relates to the conduct of Consultant's business; and (ii) pay reasonable costs, attorneys fees, damages and settlement fees finally awarded against Consultant resulting from such claims. Without limiting Company's liability to Consultant for breach or non-performance of this Agreement, the Parties acknowledge and agree that by entering into and performing its obligations under this Agreement, Company does not assume and shall not be exposed to the business and operational risks associated with Consultant's business independent of this Agreement.

8.4 Conditions.

The indemnification obligations in Sections 8.1 and 8.3 are contingent on the Party seeking indemnification providing: (i) prompt written notice of receiving a claim; (ii) all necessary information within its control for the indemnifying party to conduct a defense; and (iii) the indemnifying party with sole control of defense and settlement negotiations. The non-indemnifying party may participate in the defense or settlement at its own expense. Company shall have no obligations to indemnify Consultant or to otherwise be liable to Consultant for claims based on or arising out of: (a) the unauthorized use of the Service or any abuse or misuse thereof, (b) the combination, operation or use of the Service in conjunction with Consultant Content not supplied by Company. This Section 8 states Company's entire liability and Consultant's sole and exclusive remedy for infringement of Intellectual Property Rights.

9. LIMITATIONS OF LIABILITY

EXCEPT FOR THE INDEMNIFICATION OBLIGATIONS HEREUNDER, AND EXCEPT IN THE CASE OF A PARTY'S BREACH OF THE OTHER PARTY'S INTELLECTUAL PROPERTY RIGHTS OR A BREACH OF EACH PARTY'S OBLIGATIONS WITH RESPECT TO CONFIDENTIALITY, AND CONSULTANT'S OBLIGATION TO PAY ALL REQUIRED FEES TO COMPANY, NEITHER PARTY SHALL BE LIABLE FOR ANY SPECIAL, INCIDENTAL, INDIRECT OR CONSEQUENTIAL DAMAGES OR FOR THE LOSS OF PROFIT, REVENUE, OR DATA, ARISING OUT OF OR RELATING TO THIS AGREEMENT EVEN IF THE OTHER PARTY HAS BEEN ADVISED OF THE POSSIBILITY OF SUCH POTENTIAL LOSS OR DAMAGES.

IN ANY EVENT, THE AGGREGATE LIABILITY OF COMPANY TO CONSULTANT FOR ANY REASON AND UPON ANY CAUSE OF ACTION (REGARDLESS OF THE FORM OF ACTION, WHETHER IN CONTRACT, TORT, WARRANTY OR OTHERWISE) SHALL BE LIMITED TO DIRECT DAMAGES NOT TO EXCEED THE AMOUNT OF FEES ACTUALLY PAID BY CONSULTANT TO COMPANY DURING THE SIX (6) MONTH PERIOD IMMEDIATELY PRECEDING THE MOST RECENT EVENT GIVING RISE TO THE LIABILITY (OR IF SUCH EVENT OCCURS IN THE FIRST SIX (6) MONTHS OF THIS AGREEMENT, THE AMOUNT ESTIMATED TO BE PAID IN THE FIRST SIX (6) MONTHS OF THIS AGREEMENT). THE FOREGOING LIMITATIONS APPLY TO ALL CAUSES OF ACTION IN THE

AGGREGATE, INCLUDING WITHOUT LIMITATION TO BREACH OF CONTRACT, BREACH OF WARRANTY, NEGLIGENCE, STRICT LIABILITY, MISREPRESENTATIONS, AND OTHER TORTS.

10. LAW AND DISPUTES

10.1 Governing Law. This Agreement will be governed by the laws of Minnesota, without regard to any principle of conflicts of law that would require or permit the application of the substantive law of any other jurisdiction. The Parties agree that the United Nations Convention on Contracts for the International Sale of goods shall not apply to this Agreement.

10.2 Export. Both Company and Consultant agree to comply fully with all relevant export laws and regulations of the United States to ensure that no information or technical data provided pursuant to this Agreement is exported or re-exported directly or indirectly in violation of law.

10.3 Dispute Resolution. Except for a Party's right to apply to a court of competent jurisdiction for a Temporary Restraining Order, Preliminary Injunction or other equitable relief to preserve the status quo or prevent irreparable harm and for the right to bring suit on an open account for simple monies due under this Agreement, and except with respect to proprietary rights and obligations with respect to confidentiality, for any problem, claim, or dispute arising from, out of, or based upon this Agreement, or the business relationship between the Parties:

1. Internal Escalation. The aggrieved Party shall promptly notify the other Party of the existence of the problem, claim, or dispute, and such other Party shall promptly undertake all reasonable efforts to resolve the matter, including but not limited to, submitting such problem, claim or dispute for resolution to a Manager of each Party. The Managers shall make a good faith effort to resolve the dispute as quickly as possible but within a period not to exceed twenty (20) business days unless otherwise mutually agreed.

2. Arbitration. Any question or dispute not settled under Section 10.3.1, above, will be resolved by arbitration administered by a panel of three neutral arbitrators in accordance with the then-current Commercial Rules of the American Arbitration Association, and judgment on the award may be entered in any court having jurisdiction thereof or over the applicable Party or its assets. In any such arbitration proceeding the arbitrators shall adopt and apply the provisions of the Federal Rules of Civil Procedure relating to discovery so that each Party shall allow and may obtain discovery of any matter not privileged which is relevant to the subject matter involved in the arbitration to the same extent as if such arbitration were a civil action pending in a United States District Court. The location of the arbitration will be Hennepin County, Minnesota. The arbitrators will have no authority to award any damages that are excluded by the terms and conditions of this Agreement. Either Party will have the right to apply at any time to a judicial authority for appropriate injunctive or other interim or provisional relief, and will not by doing so be deemed to have breached its agreement to arbitrate or to have affected the powers reserved to the arbitrators.

11. **GENERAL**

11.1 Notice. Any notice or other communication required or permitted to be made or given by either Party pursuant to this Agreement will be in writing, in English, and will be deemed to have been duly given: (i) five (5) business days after the date of mailing if sent by registered or certified U.S. mail, postage prepaid, with return receipt requested; (ii) when transmitted if sent by facsimile, provided a confirmation of transmission is produced by the sending machine and a copy of such facsimile is promptly sent by another means specified in this section; or (iii) when delivered if delivered personally or sent by express courier service. All notices will be sent to the other Party at its address as set forth below or at such other address as such Party will have specified in a notice given in accordance with this section.

11.2 Force Majeure. Neither Consultant nor Company shall be deemed to have breached or defaulted under this Agreement by reason of any failure to perform in accordance with its terms, if such failure arises out of causes beyond the control and without the fault or negligence of either Party, including acts of God or the public enemy, fire, floods, strikes, delinquencies by or the unavailability of products from vendors of equipment and services, failures of electrical power or communication service, or similar causes. Either Party shall promptly notify the other Party of the commencement and cessation of any such contingency, and during the continuance of such contingency performance of this Agreement shall be excused; provided, that upon cessation of any such contingencies the Parties shall perform in accordance with the terms of this Agreement.

11.3 Assignment. Consultant may not assign or otherwise transfer any right or obligation set forth in this Agreement without Company's prior written consent, which consent shall not be unreasonably withheld. Any purported assignment in violation of the preceding sentence will be void and of no effect. This Agreement will be binding upon the Parties' respective successors and permitted assigns.

11.4 Entire Agreement. This Agreement constitutes the entire agreement between the Parties, and supersedes all other prior or contemporaneous communications between the Parties (whether written or oral) relating to the subject matter of this Agreement. This Agreement may be modified or amended solely in writing signed by both Parties.

11.5 Severability. The provisions of this Agreement shall be deemed severable, and the unenforceability of any one or more provisions shall not affect the enforceability of any other provisions. In addition, if any provision of this Agreement, for any reason, is declared to be unenforceable, the Parties shall substitute an enforceable provision that, to the maximum extent possible in accordance with applicable law, preserves the original intentions and economic positions of the Parties.

11.6 Waiver of Rights. No failure or delay by either Party in exercising any right, power or remedy will operate as a waiver of such right, power or remedy, and no waiver will be effective unless it is in writing and signed by the waiving Party. If either Party waives any right, power or remedy, such waiver will not waive any successive or other right, power or remedy the Party may have under this Agreement.

11.7 Solicitation. During the term of this Agreement and for twelve months after its expiration or termination, neither Party will, either directly or indirectly, solicit for employment (other than through mass-market means such as internet or newspaper advertising), hire or retain for or on behalf of itself or its Affiliates any employee of the other Party (or any of its Affiliates) who was involved in the performance of the Party's obligations under this Agreement, unless the hiring Party first obtains the written consent of the other Party.

11.8 Incorporation of Work Orders. The Work Orders referred to in and attached to this Agreement are hereby made a part of it as if fully included in the text. Unless otherwise specifically so stated, a term contained in a Work Order shall apply only to the Services described in such Work Order. If there is a conflict between this Agreement and a Work Order, the Work Order will control (but only with respect to Services provided under such Work Order).

IN WITNESS WHEREOF, the parties have caused their duly authorized Representatives to enter into this Agreement, effective as of the Effective Date.

Company:
Name:
Address:

Consultant:
Name:
Address:

By: _____

By: _____

Name: _____

Name: _____

Title: _____

Title: _____

Effective Date: _____

Date: _____