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IT Contracts: Telecommunication and Internet Issues

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> **This paper, delivered to the LexisNexis IT Contracts Forum in April 2008, focuses on identifying telco and internet issues arising in IT contracts, and assessing and managing the risk associated with these.**

INTRODUCTION

1 It is rare for IT services not to involve telecommunication and/or internet services. In a contract context, Telco/Internet services will be part of the IT contract or integrally tied up with the IT contract (or both). Additionally:

1.1 Internet Protocol (IP) underlies many ICT services: there is a common thread;

1.2 Convergence of IT, Telco, Internet and content is an increasingly significant factor, and voice traffic is rapidly moving to an IP platform.

2 This paper focuses more on identifying issues rather than providing detailed drafting solutions, as assessing and managing the risk (including as to drafting contracts) sometimes does not get the attention it deserves. Additionally other papers at this seminar go into detail on important areas such as service levels.

3 We deal with this by using examples.

RISK ASSESSMENT: XERO and MYOB AS EXAMPLES

4 In deciding how to handle on-line aspects of IT, including the approach to contracts, a risk assessment is needed. It is important to go through this process before deciding on what terms in the contract are appropriate. Maybe this is something that lawyers don't always involve themselves in enough? This may often be more important than traditional areas of focus such as boilerplate terms? It is typically something the business unit does, so the lawyer's work should tack on easily to an existing work stream. It may mean getting into the contract terms beyond the boilerplate.

5 An evolving example of the approach, where there is an IT, Telco and Internet overlap, is Software as a Service (SaaS)[1].

6 A typical SaaS product is the Xero accounting package which is being developed in Wellington. Legacy accounting packages, such as MYOB and Quicken, work from the customer's servers (ie: typically there is no IT and Telco component unless, say, the customer uses a wide area network (WAN) to communicate between its offices).

7 Xero must have Internet connectivity at its end, to enable the customer to access the service. That is part of Xero's service to the customer, which it subcontracts to an ISP. If that Internet connectivity falls over, so does the Xero service overall. Xero is likely to have a high reliability, high capacity link to the Internet. Local access links described in this way are often made up of a single physical path to a point where the ISP makes available diverse physical paths. From the point where there is physical diversity (redundancy), the risk of outages or service degradations is reduced but never 100% eliminated.

8 In relation to that single physical path local access, a Xero may decide the risk is so

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[1] SaaS is a software application delivery model by which a software vendor develops a web-based software application, and hosts and operates (either by itself or a third party) the application for use by its customers over the Internet. Customers do not pay for licensing the software: they pay for using it.

high (eg; of a digger cutting the fibre: "spade fade"), that it will buy physically diverse local access. For example, it may buy a fibre connection from the back of its site, with the existing fibre arriving in the front of the site. Or it may take a wireless connection to support the fibre connection.

9   For its part, the customer buys Internet connectivity (typically via an ISP) to be able to communicate with the Xero service over end-to-end Internet circuits. If that connectivity fails, the overall Xero service in effect fails, but for reasons outside Xero's control.

10 Either party may choose to buy dedicated telecommunication circuits instead of relying on the Internet. The line between the two increasingly becomes unclear, particularly as all services become IP based. The same or overlapping networks and infrastructure are used, and IP increasingly is the ubiquitous transport mechanism.

11 Ironically, sometimes the Internet services might be more reliable than dedicated circuits, given the multiple paths over which Internet traffic can travel (ie; there is diversity, to get around failed circuits). ISPs can provide services – with the look and feel of Internet services - that have improved Quality of Service (QoS). Fibre local access instead of DSL could be used; higher QoS DSL can be purchased, etc.

12 There really is no clear delineation between "the Internet" and other circuits and services. The more so with convergence.

13 Coming back to the example, Xero's customers send data by the Internet to Xero's servers. This is processed by Xero's software. Reports (such as financial accounts) are sent back to the Customer.

14 Xero's customer accesses the Xero servers by way of the Internet. The customer's own ISP provides that service.

15 So the customer, to use the Xero service, is reliant on its own ISP's service (which often has components outsourced by the ISP), and on Xero's Internet access, which is made available under contract to the customer (and that access is outsourced to Xero's ISP).

16 This is a fairly simple example: often these situations can be more complicated.

17 Increasing the reliability of these Internet links can markedly increase cost. This can be caused by using additional circuits; services with higher QoS; 24x7 help desk rather than business hours only; more rapid times within which the supplier must remedy an outage, etc.

18 No Telco provider (or provider such as Xero) can promise 100% reliability. It can only reduce the likely outage periods. Subject to the provider actually implementing steps such as more rapid correction of outages, etc, having SLA with rebates don't really change this underlying reality. What they mainly do is to encourage the provider to perform services optimally (and to meet higher standards of service, as contracted. Almost invariably the rebates are much smaller than the true loss caused to the customer by an outage. In this way, SLAs can be seen sometimes to favour vendors rather than customers) although there are reputational and PR issues when SLAs are not met. This reality is a factor in assessing how contracts are drafted. SLAs are nonetheless important.

19 In the near term, SaaS products are typically used by SMEs, often in situations where some outages are acceptable (and the cost of belt and bracing the service is uneconomic). It is appropriate in those circumstances for the customer to wear most of the risk. A Xero outage, in relation to its accounting services, would generally be acceptable as getting the accounts done is not mission critical. Even a delay of a day or two could be acceptable.

20 Over time, SaaS products may move to more mission-critical situations and toward large organisations such as government departments and listed companies.[2] Then SaaS vendors and their customers will be much more concerned about connectivity (for example, in the same way that banks would be now in relation to EFT-POS systems, which in fact have similarities with SaaS services, given the outsourced way in which the Banks operate EFT-POS).

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[2] There is some debate about whether SaaS will move away from the SME space even over time

21 While the technical people will look closely at these risks and take steps that are appropriate, we as lawyers do have a role to check and reflect risk and its minimisation (as appropriate in the circumstances) in the contracts. Working with the business and technical units can be important. There will be times when this really matters and others where it doesn't.

WEBSITES

22 These provide another example. Many organisations are keen to have their websites relatively reliable but it's not the end of the world if they are down for short periods, particularly if the sites are informational in nature. They won't pay what can be considerable additional cost for more robust service. Note that, in practice, some quite large organisations have been caught by buying low quality website services without checking out their reliability, only to have them fail. This type of problem is surprisingly common.

23 Some websites are clearly mission-critical. An example is MED's Personal Property Security Register (PPSR). The PPSR, under statute, allows securities to be registered only on-line. This should be close to 100% reliability although there have been material outages.

OUTSOURCING AND MULTI-SOURCING

24 Outsourcing is an example of what are often large scale combined ICT contracts. Many IT and Telco services can be supplied by one vendor (and in turn the IT services may be supplied to the customer by the vendor from a remote location, over Telco/Internet links). This more traditional form- where one vendor primes the supply of services and subcontracts to others - might be used by a large organisation. It is a "One throat to choke" model.

25 That outsourcing model is increasingly being replaced by the customer contracting directly with various providers. That is a situation, particularly for large projects, which is sometimes called multi-sourcing. Even in those situations, a purchaser of services will typically end up by contracting with other parties as well including for

telecommunication, internet and IT services.

26 Multi-sourcing is an example of where there may be issues about where a supplier's responsibilities and services start and stop, and also where the performance of a service by one provider relies on performance by another. These demarcation and dependency issues are a key focus in drafting contracts, to reduce the rise of problems "falling between the cracks". This is an important issue for Telco and Internet components.

DATA WAREHOUSING

27 Given the scale and risk, customers will often opt for higher reliability connectivity with the Data Warehouse provider. The ISP or telecommunications provider may have an initial draft contract which does not provide sufficiently strong service levels around issues such as availability of the service; response and problem resolution time; Help Desk availability; proactive and reactive monitoring, and so on. Hard negotiating may be needed, focussing on what's important (a risk assessment approach enables this).

28 For larger contracts, it may be viable, and preferable, to seek to agree the customer's own contract terms rather than using the vendor's terms (the vendor will, understandably, resist that approach on smaller deals). The choice of which way to go here could be important, and the challenge in drafting the customer's own terms not underestimated.

REMOTE ACCESSING THE WAN/LAN

29 This raises the sort of issues noted above. It is an example of privacy and security issues around Telco and Internet-related services. Generally privacy and security will be a key consideration for all Telco and Internet services and an acute example is remote access, where PDAs and laptops can erode privacy and security protections.

30 Organisations have quite heavy responsibilities, including where their information and information held on behalf of third parties, goes to the customer's providers. We have covered these issues extensively in several articles on www, wigleylaw.com including:

CONCLUSION

31 Rare is the IT contract that does not involve a Telco and Internet element. This brings with it additional risks to be minimised. A legal assessment of the approach is important so that appropriate contracts can be agreed, focussing on the important issues.

We welcome your feedback on this article and any enquiries in relation to its contents. This article is intended to provide a summary of the material covered and does not constitute legal advice. We can provide specialist legal advice on the full range of matters contained in this article.

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