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Outsourcing Game Development/What do Game Development Companies Need to Know About Offshore Outsourcing and Technology Transfers?

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Mark Phillips

What is Outsourcing? (and is it relevant for games?)

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- **Standard definition**
- **but is it a new departure for games?**
- **and how does it fit into current trends in the industry?**

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Why Outsource Development?

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- Flexibility to scale up/down resource
- Cost savings rather than use full time staff
- Internal team focuses on key work
- Shift risk to 3rd parties on non critical development
- Lack of available skill or resource in house/deadlines
- Increasingly specialist skill sets

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International Dimension

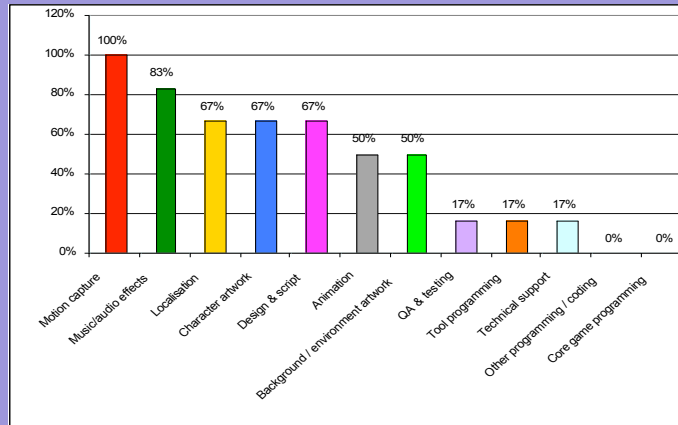
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- To go where the skill set is
- To minimise cost of labour/time differences
- Trends for Eastern Europe but long term India and Far East
- Conclusion:
 - (a) Too many teams + too few projects =
Dead Developer
 - (b) "Do what you do best and outsource the rest"

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What is outsourced?

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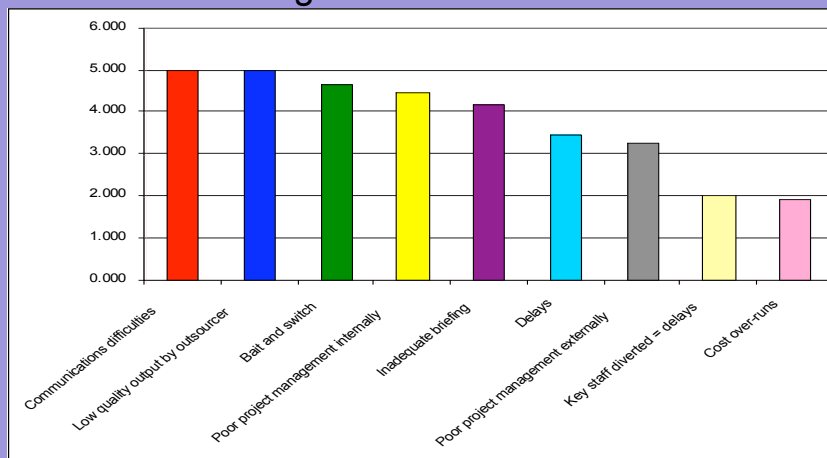


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Problems with Games outsourcing

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Pre-Contractual Issues

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- **Identity what you want and who will provide it,**
- **Due diligence -**
 - Financial stability/facilities/funding insurance
 - Depth of resources/key skills/biogs/freelancers?
 - Tools and technology, licences or proprietary?
 - Back up and security plans
 - Past portfolio/commitments
 - Production processes/scheduling and project management.
- **Scope deliverables, specification, benchmarks, access**
- **Fix price and timing and key staff**
- **Meet and greet**

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Contractual Issues

Aim for component based outsourcing – to ensure compatibility and synchronisation with other components and therefore:-

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- Specify services/product/technology
- Specification and change control procedure
- Schedule and who will deliver what assets, when and to whom and format and mode of delivery
- Price and payment/milestones/ delivery dates and deliverables
- Assets, 3rd party contracts (e.g. middleware licences), hardware, dev kits , original code
- Approval procedure (objective or subjective)
- Key staff and access to premises /staff
- Warranties/indemnities/service levels
- Limitation of Liability
- Intellectual Property – assignment/nature of licence/registration
- Source Code Escrow
- Exclusivity/Favoured Nations
- Carrot and stick for timely deliverables
- Termination for cause/insolvency/no cause
- Consequences of Termination
- Dispute resolution/jurisdiction/governing law
- Guarantee

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Offshoring- practical points

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Generally

- Choose a supplier with sufficient English speaking personnel
- But 2 nations divided by a common language
- Avoid bait and switch
- Back end payments
- Local inflation/forex/business risks
- Scope creep/project delays – over promising and under delivery

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Offshoring- practical points

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Structurally

- Structure – 3rd party supplier/captive entity/JV
- Tax – Structure/double taxation treaties /VAT treatment/transfer /withholding

Legally - Check local laws for:

- Data Protection/privacy (e.g. for MMOs)
- Employment issues including Transfer of Undertakings
- Regulatory Issues/Special Licences or approvals
- Formalities for execution (notary?) or assignment/registration with local ministries
- Exchange or export controls
- Local state grants or loans
- Intellectual property
- Competition/anti trust/Block Exemptions
- Impact of Insolvency
- Other public policy/implied contractual terms overruling contractual terms or governing law

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Certain Intellectual Property Issues

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- Overseas differences - Copyright/Moral rights/Patents/Design rights/Database rights
- The weakest link – in chain of ownership
- Need to carve out from assignment/exclusive licensing not just proprietary tools but licensed music/audio/generic graphics – the great “tree” debate.
- Check terms of tools/engine licences and even platform licence permit outsourcing.

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(In)soluble Insolvency Issues

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- Define termination trigger events to reflect local law procedures/restrictions
- Express post termination provisions
- BUT e.g. in UK – cannot automatically acquire title/property from insolvent UK company
- Alternative liquidator can disclaim onerous contracts
- Case study: impact of different treatments and culture in UK/US where US publisher, UK developer and UK financier:
 - Who owned the IP?
 - Did licence terminate?
 - Could management buy out UK studios and would US publisher have rights in studios?
 - Deal – quick and dirty or court approved?

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Data Protection

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- EU Data Protection Directive as implemented into member states
- Personal data to be processed in accordance with 8 data protection principles: Data controller is entity that determines purpose and manner in which data is processed
- Data controller responsible for compliance even if outsourced to data processor
- Data protection – principles include restriction on transfer of data outside EEA
- Exceptions

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Transfer of Undertaking (Protection of Employments Regulations) (“TUPE”)

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- What is transfer of undertaking and why relevant to outsourcing?
- Impact of TUPE – employment contracts automatically transfer
- Termination in connection with transfer can trigger compensation
- Need to consult
- Potential Restrictions on varying employment contracts
- Relevant in games outsourcing?

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Anti-Competitive Agreements

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- Article 81 & 82
 - Limited “Block exemptions” (i.e. safe harbours) apply
 - Most relevant to IP /Games transactions is the Technology Transfer Block Exemption
 - Applies to agreements between two undertakings which are mainly for transfer/licence of technology
 - Combined market shares
 - must be below 30% or (20% if parties are competitors)
- White list clauses:**
- No sublicensing
 - No use of protected technology after end of agreement
 - Minimum royalties
 - Minimum products
 - Non competes
- Hardcore clauses (for non competitors):**
- Setting prices
 - Restrictions of territory where or customers to whom licensee can make passive sales
 - Preventing licensee exploiting own IP
- NB Excluded/Grey Restrictions**
(e.g: obligation to licence back to assign improvements/No challenge clauses)

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Dispute Resolution Jurisdiction and enforcement

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- No single European jurisdiction, need to specify particular country in contracts
- Which law and courts to choose?
 - Consider enforcement – if going to enforce overseas
 - Risks of being “home-towned”
 - Increasing latitude in bringing cases in suitable EU territories thanks to Brussels Convention etc
 - Which courts are best?
- Who can sue?
 - National approaches govern this issue
 - Many rights now permit a licensee to sue

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Conclusion

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TIGA Survey

- 50% of publishers believe next gen development is impossible without outsourcing
- 33% essential and 17% important
- Publishers spend average of 16% of total development budgets on outsourcing, within 3 years set to rise to 27.5%
- UK Studios expenditure on outsourcing - £51m in 2005 and £135m in 2008

Where will power lie in shifting business models – Publisher/studio/outsourcer or the lawyer?

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