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Human Resource Managers Detect Management & Legal Disadvantages to Outsourcing

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Abstract: Outsourcing is "a practice used by different companies to reduce costs by transferring portions of work to outside suppliers rather than completing it internally." (Outsourcing, 2013) After the financial crisis of 2007-2008, many companies in the United States began to enhance their bottom-line profits by outsourcing and cutting costs instead of through the traditional route of top-line sales growth. In an attempt to effectively cut costs and generate profits for investors, more organizations engaged in outsourcing of jobs by means of offshoring. Offshoring is a form of outsourcing whereby jobs are relocated to a foreign country with a cheap labor force and low socioeconomic standards, and less regulations such as the EPA. From a Human Resources perspective, offshoring jobs is that there will be benefits to the organization such as cost and efficiency savings, focus on core activities, reduction of overheard costs, staffing flexibility, continuity, avoid organized labor, and risk management. In theory, the argument for offshoring is plausible and synergies can be created for companies; however, issues can result, creating huge disadvantages for organizations. Outsourcing can become detrimental to the financial health of an organization because of unforeseen costs. In addition, the organizational culture and employee morale begins to diminish when employees have no job security and they fear layoffs. Thus, there are pros and cons of offshoring jobs those Human Resources managers' must evaluate before choosing whether to offshore jobs or keep them domestically. Therefore, outsourcing jobs through offshoring can result in disadvantages to an organization because of hidden costs, bad publicity and low employee morale, quality problems, loss of managerial control, threat to confidentiality and security, and reliance on the financial health of the outsourced organization. This paper has been divided into two sections due to the comprehensive approach taken by the authors to provide a focused view on the legal aspects giving the reader an opportunity to use the information as a guide if needed, or for further research.

Keywords: Human Resource; Management; Outsourcing.

1. Hidden Costs

An organization's Human Resources manager must analyze the hidden costs before deciding whether to offshore jobs. "Decades ago, when many companies began outsourcing production overseas, they had several reasons for adopting that strategy. One of their most important objectives was to establish a presence in China, Brazil, India, and other high-growth countries with the potential to generate huge demand for goods and services. Another major driver of outsourcing was the availability of low-wage Chinese workers who could produce goods so cheaply that their output essentially flooded the global marketplace. Companies that outsourced production internationally were looking at incremental revenues, significant cost reductions, and huge profits. It seemed like a winning, can't-miss strategy." (Burton, 2013) However, in today's global marketplace, there are significant costs that sometimes trump the low cost labor and cheap manufacturing that is available in high-growth countries. For many companies, the offshored work is contracted with an outside vendor and anything that is not specifically covered in the contract will be an additional expense. These outside vendors usually have extensive experience in these types of contract negotiations and will ensure that they get the best deal when dealing with an organization's lawyers. As a result, a Human Resources manager will have to retain an outside law firm who specializes in these types of contracts so the company won't experience additional hidden costs. Thus, before jobs are even offshored, there requires planning and a huge cash flow investment.

Once jobs are offshored, management may believe that the cost-savings and synergies will begin to take effect immediately; however, there are many additional hidden costs that will be incurred by the organization. One of the biggest hidden expenses that an organization will face is the training of the offshored workers. The outside

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contracted vendor cannot just open the doors once the deal is in place with an organization and start production or provide service. There needs to be extensive training conducted by the internal employees of the organization to ensure that the manufacturing jobs and service jobs are transitioned correctly. Thus, an organization will essentially be paying two employees to do the same job until training is completed. Training must also take place face-to-face and the travel and hotel costs from the United States to overseas countries are not cheap. Once training is complete, there will be a transition phase or learning curve before the offshored employees can work at full capacity and produce a quality product or service, which can hamper production and profitability of an organization. After the training is complete, the domestic manufacturing/service operations must be shut down. This phase of offshoring jobs is also very costly because leases must be broken, property must be sold, and equipment must be transported to the overseas offices. The last phase of offshoring jobs is the mass layoff of the domestic employees. The Human Resources manager must provide these employees with a fair and sizable severance package or the severed employees might file a lawsuit. Even if the severance package is reasonable, some employees might still file a lawsuit and the United States courts tend to side with the employee rather than employer; as a result, the layoff of employees can become very costly. Some additional hidden costs that should be considered by an organization before offshoring jobs are listed below (Burton, 2013):

- Cost of an outdated outsourcing strategy
- Cost of management and coordination of contractors
- Cost of subpar inventory performance
- Costs of unplanned logistics activities and premium freight
- Cost of inappropriate sales and operations planning
- Cost of poor or substandard quality
- Cost of warranty, returns, and allowances
- Cost of supplier management
- Cost of cash flow
- Cost of unplanned and unforeseen risks

Therefore, there are many hidden costs that an organization will incur that will outweigh the potential cost-savings, which should cause an organization to think twice before offshoring jobs.

2. Bad Publicity & Low Employee Morale

If an HR manager has ever had to deal with a customer service representative in a foreign country who could hardly speak English? If the answer is "yes," the mere thought of dealing with this person can evoke some angry feelings and make your blood boil mainly because this person took an American job. Based on my own opinion, I despise companies who sellout and offshore jobs just to make a bottom-line profit for investors. From an ethical standpoint, when jobs are outsourced through offshoring, Americans lose jobs; as a result, families become destroyed by these types of events and a company suffers no repercussions. In fact, the executives of these companies are showered with huge bonuses and stock options just for cutting costs and making their projections for investors. In a perfect world, these executives would be incarcerated for the damage they have done to the American way of life. Legally, these companies who offshore jobs are not guilty of anything; however, morally and ethically they should be held accountable. In fact, some consumers who learn that an organization has offshored jobs will boycott that company's products or services and this could affect the financial well-being of the company. For example, a few years ago, Dell Inc. announced that they were shutting down operations in North Carolina and offshoring jobs to Mexico. (Smith, 2009) This caused many negative articles to be written about Dell Inc. and caused some consumers to boycott their products. Therefore, bad publicity from offshoring jobs can have a negative influence on an organization and cause a consumer to boycott these products and perceive the company as unethical.

From a Human Resources standpoint, the employees who remain part of a company after the offshoring process will have very low morale and the Human Resources manager must delicately manage these employees to ensure that productivity remains high and consistent. This can be a daunting task and ultimately productivity diminishes after jobs are offshored because the remaining employees feel like they have been betrayed by their employer. In an article from the American Journal of Business, the author developed a way to remedy the low morale of the remaining employees: "Effective communication among cross-functional areas reduces the negative effects of outsourcing projects on the morale and performance of the remaining employees. Management must step in and rebuild trust among the workers, and jobs may need to be reevaluated and expanded or changed to fit the new organization. This can be achieved through support and involvement of top management and by providing incentives to employees and vendors who meet and exceed the contracted performance expectations." (Elmuti, 2003) Therefore, offshore outsourcing is a great disadvantage for a company as bad publicity and low employee morale can cause the company to be perceived as unethical, consumers to boycott products, and the remaining employees to reduce their productivity, which, in-turn, will hurt the financial stability of the organization.

3. Quality Problems

Made in China…Made in Taiwan...Made in India...Made in Mexico…Made in Korea…Made in the Philippines…Why is a quality product rarely produced in a developing country? Most consumers associate American products with quality and they are willing to pay a premium for a domestically produced product. This

sounds like an oxymoron because you would expect to pay more for an imported product. However, when dealing with products from developing countries, there are many quality issues that result in a cost reduction for the American consumer. Furthermore, a consumer will also pay a premium for American services because it is synonymous with quality. Manufacturing and service jobs are offshored by companies with one goal in mind and that is cost-savings; even if the quality of the product or service is compromised. Offshoring of manufacturing operations saves millions of dollars in manufacturing expenses, which translates into higher gross margins and larger profits. This sounds like a great idea on the surface; however, if the quality of the product is compromised, there will ultimately be a decrease in consumer demand. Thus, if companies have historically produced a high-quality product and established their brand name, then consumers will not be willing to pay the same premium for a lower quality product that is produced by the same company after jobs are offshored and the product quality is compromised.

Recently, "Boeing's 787 Dreamliner has suffered numerous electrical system flaws beyond the battery problems that led to its current grounding, according to engineers with knowledge of the situation. Company engineers blame the 787's outsourced supply chain, saying that poor quality components are coming from subcontractors that have operated largely out of Boeing's view." (Gates, 2013) As a result, a company like Boeing, who produces airplanes that transport people through the air, cannot compromise the quality of their product or it can lead to a disaster such as a plane crash and loss of human life. Furthermore, Boeing's brand name and stock price have been pummeled recently by the news of these defective Dreamliner planes. Boeing's outsourcing of electrical components in their airplanes to foreign suppliers began as a way to save money for the company; however, it ended up costing the company more money in the long-run. Therefore, the Boeing example is a great lesson for any company as it shows that outsourcing or offshoring jobs to save money compromises the quality of the product and ultimately leads to additional expenses that can be detrimental to the financial stability of the organization.

4. Loss of Managerial Control

When a company outsources jobs through offshoring, they are essentially given up managerial control in one way or another. Management of the organization is given to another company who has a set of core values and beliefs that are different than their own. This outsourced company will not be driven by the same values and mission that your own company practices; as a result, the Human Resources function must manage them effectively to ensure that the two companies' goals are aligned and do not intersect. When work is offshored to foreign countries, there are different government regulations, politics, economics, and employee labor standards that are adhered to. Too often we here of sweatshops in countries like Thailand, the Philippines, and China who abuse their employees, make children work, have brutal working conditions, force employees to work around the clock, and pay their employees a poor wage. In these developing countries, this might be the acceptable and even legal practice; however, as Americans we are held to a higher standard and these practices should not be tolerated by any organization. Foxconn, a contract manufacturer, who operates in China and is best-known for making Apple products, has been the epicenter for poor working conditions. The working conditions at Foxconn are so bad that many employees have taken their own lives and it is not considered an anomaly. A pcmag.com article stated, "Suicide at Foxconn is not a new phenomenon. At least two dozen Foxconn workers in Shenzhen and Chengdu have taken their own lives since early 2010. Foxconn has forced employees to sign a pledge promising that they won't commit suicide and installed nets outside factory dormitories to deter potential jumpers." (Moscaritolo, 2013) When you look at what is going on at Foxconn and then take a look at your iPhone, iPad, or iPod, do you see a product that was made by slave labor? I don't think it is a stretch to say that Apple management indirectly killed these people to cut costs and make a larger profit for investors.

When an organization offshores jobs, the Human Resources function must be certain that the outsourced company practices similar policies because they are given up managerial control. If the outsourced company operates as a sweatshop, this can result in bad press for the organization and consumers will be more likely to boycott products and services. Furthermore, if the policies of the two organizations are extremely different, it is probably more efficient and cost effective for the organization to keep the jobs domestically with their own employees. Thus, giving up managerial control to an outside company for the purpose of offshoring jobs is a recipe for disaster because the organization really does not know what to expect from the contracted firm. The relationship could be a positive and be lucrative or it could turn into a disaster and be counterproductive; as a result, it is not in the best interest of an organization to give up any of their managerial control to outside companies for the purpose of offshoring jobs. Therefore, when an organization gives up control of anything including management, it should be considered a negative and a disadvantage because it just leads to more issues as functions within the company become disintegrated and, ultimately, more costly.

5. Threat to Confidentiality & Security

The livelihood of any good organization is the information that keeps it profitable, running, and growing. When a company has confidential information such as patents, drug formulas, R&D plans, payroll records, social security numbers, medical records, credit card accounts, bank accounts or computer software; is it a wise move to give an outside company access to this information? When you contract an outside organization and offshore jobs, a company is essentially giving them access to all their confidential information; as a result, there is a huge security risk that must be considered before jobs are offshored by a company's Human Resources department. Putting an

organization's information in the wrong hands can have disastrous consequences and could even bankrupt a company if the information is stolen or released to the public. Furthermore, trusting confidential information to outsourced workers in developing countries is like playing with fire, inevitably there will be security breaches and ensuing damage control. When offshoring jobs, an organization typically does "not price in the security risks when making outsourcing decisions. Organizations are too quick to fight up the cost savings of outsourcing, but don't really have an appreciation of what security risks that may introduce." (Ashford, 2013) Therefore, when an organization decides to offshore jobs and takes into account the combined expenses of the jobs and security, a persuasive argument can be made that there is actually little cost-savings or benefit for a company to outsource.

Basic logic should also play an important factor when an organization is thinking about offshoring jobs for cost-savings purposes. If a company has confidential information that could bankrupt or cause significant harm to them if it gets into the wrong hands, then it is not worth it to offshore jobs and gives contractors access to this information. If a company decides to keep jobs domestically, then the security risks will almost automatically be mitigated. There will also be some intrinsic value and goodwill built into this decision for the organization and its employees such as no loss of managerial control or jobs, feeling that the company values their employees, and consumers will perceive the company as ethical. Additionally, in a Wall Street Journal article, four of the most important information risks were identified when a company decided to outsource jobs (Deliotte, 2012):

- Operational and transaction risk
- Risks to the confidentiality of information
- Risks to business continuity
- Compliance risk

Therefore, an organization can be destroyed if there is a threat to the confidentially and security of their information; as a result, by offshoring jobs a company only enhances this risk just for cost-savings purposes that will ultimately be unrealized.

6. Reliance on the Financial Health of the Outsourced Organization

Large corporations like to be self-sufficient and they do not like to rely on anyone else to succeed, grow, and profit. However, when a Human Resources manager decides to offshore jobs, the organization begins to rely on the financial health of the outsourced organization for their sustained success. If the contracted organization goes bankrupt, it will have a huge impact on the company. If there is no business continuity plan in place, then the offshored manufacturing or service operations can cease without warning and severely damage a company financially. Furthermore, the company will have to increase spending and act quickly to restore production or service. This can include bringing the production or service jobs back domestically or hiring another contracted organization in a foreign country. If an organization is self-sufficient and has a positive cash flow, it makes little sense to offshore jobs as they would have to monitor the outsourced organization to ensure they remain financially stable. Also, the organization should develop a business continuity plan to ensure production and services are not interrupted if something goes wrong at the outsourced organization. If a business continuity plan ever had to be executed because the outsourced company went bankrupt, it would be very expensive. Thus, the rule of thumb for any organization would be to setup and conduct business so that there is no reliance on any outside organizations. Therefore, offshoring is a great disadvantage to a self-sufficient organization because they become reliant and are tied to the financial health of the outsourced organization.

7. The Legal Aspects an Introduction

The governing "law" of offshore outsourcing services is not contained in a definitive set of rules; rather, American companies that engage in any level of outsourcing have to be mindful of a web of piecemeal regulation from the state, federal and international levels. Whether the general trend of offshore outsourcing will continue to send these services to places with cheaper labor such as India and China is not only a question of free market economics but also one of regulatory feasibility. It is undeniable, however, that in the interest of maximizing profits, "moving jobs to a lower wage location is a common effect of globalization." (Emilcar, 2012).

This section will first address the various levels of regulation in context of outsourcing (*i.e.*, state, federal, and international). It will then analyze how contracts should be drafted in the interest of predictable expectation in outsourcing relationships. Finally, it will then turn to the nature of the realities of "law" of outsourcing including the means of dispute resolution and procedure governing resolution of such disputes.

8. State Regulation of Outsourcing

It is usually the state of a business's incorporation that governs how that business is able to expand, but businesses that have a presence in multiple states have to abide by the laws of each of those states. Congress' constitutional power to regulate both interstate and foreign commerce (in Article I, section 8, clause 3) significantly limits state laws' ability to regulate their own businesses. In the state-to-state arena of outsourcing, the federal government can supersede state law if the activity involves interstate commerce, but the state has occasion to legislate within the "pockets" of federal authority. When the state acts as a "market participant," for example, as

opposed to a regulator of others' private business relationships, state law often is not trumped by the federal government's power to regulate interstate commerce.

However, offshore outsourcing presents a more complicated scenario where the federal government's authority over foreign affairs (extrapolated from Congress' power in the enumerated powers of Article I, section 8 of the Constitution *as well as* the President's authority in a host of foreign affairs in Article II) hinders state law in a much more restrictive manner (than in interstate commerce situations). Courts have traditionally held that the central government has virtually plenary authority over foreign affairs. Some intermediate appellate courts have held, however, that the market participant exception should apply to foreign commerce. (Antilles Cement Corp. v. Fortuño, 2012). The United States Supreme Court has not had an occasion to rule on that issue, but even state "market participant" laws as they impact foreign commerce could be on shaky ground since "[s]tate laws affecting foreign commerce are subject to a higher level of scrutiny than those only affecting domestic commerce." (Gupta and Sao, 2009). If states are allowed to regulate offshore outsourcing (within the pockets of federal preemption), they should do so on a uniform basis. Gupta and Sao point out that states attempting to target one particular country or set of countries may lead a court to determine that such targeting likely interferes with the federal government's foreign affairs power and as such violates the Constitutional doctrine of federalism and the Supremacy Clause. The U.S. Supreme Court ruled as much when it held that the state of Massachusetts could not enact a state law that prevented Massachusetts companies from doing business with Burma. The Court ruled that the Massachusetts law was preempted by the federal foreign affairs power. (Crosby v. National Foreign Trade Council, 2000). Despite a presumption to not invalidate state laws, to the extent state laws on offshoring activity touches on the federal government's foreign relations power, the Court "has found preemption where it is impossible for a private party to comply with both state and federal law." (Gupta and Sao, 2009).

States, being mindful of these federalist inhibitions, have attempted to legislate incentive for state-side labor forces and product development by trying to pass laws that do not necessarily directly prevent offshoring but offer state tax incentives to have business remain in the United States. State politics, including in the realm of offshore outsourcing, exist in a hyper-politicized, media driven campaign cycle. Candidates for local political office often see a campaign opportunity in advocating for laws that protect the "American worker." "Political representatives at local, state, and federal levels have responded to and fomented these concerns by introducing bills and enacting legislation against offshoring as a means to garner the support of their constituencies." (Gupta and Sao, 2009). For the few state bills that have become law, lower courts have rendered conflicting decisions on whether these laws are preempted by federal law. The U.S. Third Circuit Court of Appeals held that federal law failed to preempt a Pennsylvania state law "requiring that goods purchased by state contractors be produced only with American steel." (Gupta and Sao (2009), citing Trojan Technologies Inc. v. Pennsylvania (1990)). However, in another case in California, a state court held that the mere existence of federal free trade agreements "is evidence of the federal government's exclusive power to set national policy in foreign trade" and invalidated California's "Buy American" statute. (Gupta and Sao (2009), citing (Bethlehem Steel Corp. v. Board of Commissioners of Dept. of Water & Power of City of Los Angeles, 1969)).

8.1. Survey of State Legislative Actions Directed at Outsourcing

The first decade of the twenty-first century revealed a heightened concern by state lawmakers in offshore outsourcing. Whether this business xenophobia was rooted in simple economic protectionism or something of a larger political concern (*e.g.*, the Massachusetts Burma case addressed above) is anyone's guess, but a critical mass of states attempted hundreds of pieces of legislation in the 2000s, with virtually none becoming state law or, as in the case of the Massachusetts law in *Crosby*, being struck down as conflicting with the federal government's authority over foreign affairs. According to the National Conference of State Legislatures, forty-four pieces of state legislation on outsourcing were introduced in 2010, and only five were enacted. Only one directly impeded offshore outsourcing – Tennessee House Bill 2822, which prohibits the state from entering into any contract for services performed by or at call centers, with a vendor who uses call center services in a foreign country. (National Conference of State Legislatures, 2010). A similar trend occurred (National Conference of State Legislatures, 2011) in 2011, with 30 bills introduced in 13 states two of which were enacted – one in Connecticut concerning banks (but only regulation of outsourcing of electronic data processing services) and one in Nevada which, like the 2010 act in Georgia, was simply a request for state agencies to conduct a review on the fiscal feasibility of outsourcing state-owned mobile equipment. Needless to say, states believe that the federal government's constitutional authority trumps their own in this area or there has simply not been enough political support for these measures. As such, states are not significant players in the regulatory framework for outsourcing. When businesses draft contracts relating to outsourcing, they often need only reference U.S. federal law and international agreements.

9. Federal Regulation of Outsourcing

The federal government's authority over foreign commerce specifically, and foreign affairs generally, while certainly authoritative over the states, needs to also comport with the U.S.'s treaty and other international obligations. The Constitution often defers to the federal government's single voice on foreign affairs. The U.S.'s World Trade Organization (WTO) 1994 Uruguay Round Agreements on Government Procurement (GPA) places restrictions on the location of public contract work and stresses "nondiscrimination by nations through their government procurement practices." (Gupta and Sao, 2009). However, U.S. domestic courts often approach

contentions concerning international law in this realm from a different perspective as they would federalism concerns in a domestic, constitutional sphere. The implementing legislation of the GPA in the United States Code prevents any WTO-based challenge to U.S. domestic law and states that only those provisions of the Uruguay Round Trade Agreements (of which the GPA was a part) that are consistent with U.S. law are valid. (Gupta and Sao, 2009). The United States Supreme Court has held that a later in time federal statute, when it conflicts with an earlier treaty provision (to which the U.S. is a party), controls. (Whitney v. Robertson, 1888). In that spirit, Congress has attempted, like the states, to regulate offshore outsourcing, and also like the states, most likely because of political pressure from constituents and political parties.

It is also a controversial issue as to the extraterritorial application of federal law. "U.S. federal (Employment Law: Outsourcing and Offshoring, 2011) employment laws will not apply outside of the United States, unless a statute provides for extraterritorial applicability." (CWS 3.0, 2011). Several federal civil rights statutes (Title VII of the Civil Rights Act, the Americans with Disabilities Act, the Age Discrimination in Employment Act) do provide for such application for American workers employed outside of the United States. The patchwork of applicability of American workers employed outside the United States is problematic, but the general respect for non-national discrimination (as evidenced in agreements such as the WTO's GPA) generally prevents extraterritorial application of U.S. law. Can contracts, however, governing outsourcing arrangements make foreigners abide by these U.S. laws even if their own laws conflict with these rules? While companies will want to ensure compliance with foreign laws, they have to also be mindful to what extent U.S. laws like the Fair Labor Standards Act (FLSA) can govern their conduct. In foreign lands as to non-American workers, it can't, but can its terms (most importantly, who can constitute a "co-employer" or "joint employer) be integrated into businesses' offshore outsourcing contractual agreements? Related, can American companies ignore more pro-labor local laws (such as in jurisdictions like India) to shirk shift lengths, minimum wage and the like? Again here, host countries to American offshore enterprises will protect their own and American firms must also respect these laws via the outsourcing contract establishing the relationship.

9.1. Survey of Federal Legislative Actions Directed at Outsourcing

In the context of federal government procurement, Congress has been successful really only in enacting legislation that requires businesses (both domestic and foreign) "seeking federal government contracts to use domestic workers in performing contract work." (Gupta and Sao, 2009). This law was passed as the Thomas-Voinovich Amendment (TVA) as part of the 2004 omnibus budget bill. Congress has attempted to focus subsequent concerns of offshore outsourcing on data protection, particularly with government sensitive information in certain employment sectors. Likewise, how Americans' personal data is transmitted overseas has been the subject of federal legislative proposals, most notably in 2005 by then Senator Hillary Clinton; she introduced "The Safeguarding Americans From Exporting Identification Data Act." (Gupta and Sao, 2009). Aside from the TVA, none of these legislative initiatives became law. Again, it is debated whether the reason for such stalemate is because of a political resistance within members of Congress' constituencies or the legal conflicts these federal laws may have with existing international agreements. One of the criticisms of the TVA is that it would have discriminated against foreign companies because it could have forced such companies to relocate (but not forcing domestic companies to do so); a bedrock principle of international agreements impacting trade and business is the principles of national treatment and non-discrimination as the U.S. seemingly endorsed when it adopted the GPA under the auspices of the WTO.

The recession of 2008 caused a heightened economic concern over offshore outsourcing. Americans were convinced that such practices, while advocated by businesses as expansive in market globalization and resulting in cheaper operating costs, were a direct result of high unemployment in the United States. Members of Congress were called on "to protect American workers from this perceived threat to their livelihood. In response, legislators have introduced many bills aimed at preventing offshoring. . .." (Emilcar, 2012). Congress attempted to use federal tax incentives to inhibit offshore outsourcing, arguing "that the U.S. Tax Code should not actively reward American corporations for creating jobs overseas." (Emilcar, 2012).

Here is a sampling of some of the more prominent pieces of federal legislation concerning offshore outsourcing from Congress in the last decade (from the 109th Congress of 2005-2006 to the 113th Congress of 2013-2014):

- House Bill 6279 – Understanding Offshoring and Outsourcing Act (2006) (Introduced 09/29/2006): This bill, at the outset of the peak of offshore outsourcing, merely sought to improve the collection of labor data by federal agencies to better measure and evaluate the impact of offshoring and outsourcing on public and private businesses.
- Senate Bill 3816 – Creating American Jobs and Ending Offshoring Act (2010) (Introduced 09/21/2010): This bill sought most overtly to end tax loopholes that encouraged American companies that offshored jobs overseas and sought to offer a payroll tax cut for companies that returned jobs to the U.S. from overseas. (Emilcar, 2012). *Status*: The Senate failed to muster the 60 votes required for cloture to end debate on the floor and the bill died as a result.
- Senate Bill 45 – (Offshoring Prevention Act, 2011a;2011b) Offshoring Prevention Act of 2011 (Introduced 01/25/2011): This bill sought to increase taxation on certain foreign corporations when those entities' profits were attributable to imported property into the United States. A

similar measure was introduced in the House of Representatives (House Resolution 2280) on 06/22/2011 but also stalled in the House Ways and Means Committee.

- Senate Bill 1247 – America Recruits Act (2011)America Recruits Act of 2011 (Introduced 06/22/2011): In response to, as the bill's findings section indicates, the 50% decline of American manufacturing output in the 2000s, this bill's stated goal was to "develop and recruit new, high-value jobs to the United States, to encourage the *repatriation* (emphasis added) of jobs that have been offshored to other countries." While this bill built on the objectives of S45 and HR2280, it was much more grandiose and comprehensive in scope, establishing a commission on findings for a long-term return of jobs to the U.S. from overseas.
- House Bill 790 – Outsourcing Accountability Act (2013) (Introduced 02/15/2013): This bill sought to change the duties of the Securities and Exchange Commission (SEC) by amending its enabling legislation (the Securities Exchange Act of 1934) to require disclosure of all foreign employees of all publicly traded companies filing SEC reports.
- House Bill 2740 – Stop Outsourcing and Create American Jobs Act (2013) (Introduced 07/18/2013): This bill directs the Secretary of the Treasury to develop and publish a list of countries that are offshore tax havens for businesses. It also amends the Tax Code to increase the penalties on those businesses that underpay taxes concerning an undisclosed foreign financial asset located in a tax haven country as well as increase penalties for fraud, tax evasion, and false statements involving transactions in these countries. It ends with granting preferences in awarding federal contracts to contractors who have not engaged in offshore outsourcing.
- Senate Bill 2569 – Bring Jobs Home Act (2014) (Introduced 07/08/2014): The bill seeks to provide an incentive for businesses to bring jobs back to America by a variety of amendments to the Tax Code, including tax credits for "insourcing" certain business functions that a company has traditionally placed in offshore outsourcing countries and to concomitantly deny deductions for certain specified outsourcing expenses. Like S3816 in 2010, a motion to invoke cloture to prevent debate on the bill did not get enough votes and further action on the bill did not come to fruition.

Only a few short months into the 114th Congress (2015-2016), Congress has already introduced four provisions similar in scope to some of the measures analyzed above. For example, S174 and HR297 are reiterations of 2013's HR2740 to reduce the tax benefit of certain country tax havens. Also, S162 and HR305 are similar to SB45. All four pieces of legislation thus far in 2015 have simply been introduced and referred to committee with no further action.

Politically, some analysts view these bills as "protectionist" in opposition to globalization, seeking to use domestic law (like the Tax Code) as a sword to dissuade the practice of offshoring. None of these bills have advanced out of committee save for the two that made it to the Senate floor (but those could not muster votes to end debate). The inability of these bills to become law begs the larger question of what forces are preventing federal offshoring legislation from becoming a reality. Of course, it may be a matter of economics to debate whether offshore outsourcing is really causally linked to domestic unemployment. A counter-argument to that could be that there are cheaper production and labor costs by using services in more inexpensive markets (like India and China), better for American firms' bottom lines. So, the economic wisdom, rather than the political consequences, of such legislation may have been the reason most of them did not make it to the President's desk for signature.

10. Contractual Relationships in Outsourcing

In the absence of any legislative regulation or in a conscious attempt to comply therewith, outsourcing companies have in their best interest to define terms and conditions of the outsourcing relationship. While these expectations cannot accommodate for all problems, legal departments of American companies engaging in outsourcing practices should seek to have contracts that are mindful of several things, including data privacy protection, business trade secret protection and end of term exit strategies. All the while, companies have to operate under these contracts within the legal and regulatory framework of laws affecting outsourcing and be mindful of the business costs of matters such as culture and customs of the outsourced service country. Cultural and societal mores of other countries are important here because countries to which outsourced services go "might have a different cultural attitude toward privacy and intellectual property than the personnel of" the firm's home country – the United States. (Weiss and Azaranm, 2007).

The business aspects of such a contractual relationship are not within the direct purview of this section. Common considerations of business risk, profit maximization, insurance of loss, etc. are all legitimate provisions of outsourcing contracts. The focus here, though, is how contracts legally bind parties to an outsourcing arrangement including how those contracts incorporate the relevant laws (explained above) on outsourcing. Such a contract should address, *inter alia*:

- the scope of the business engagement,
- the expectation of the parties,
- "well-designed and clearly articulated change-order governance" (Weiss and Azaranm, 2007),
- data and intellectual property protection including record retention policies,
- status of workers under the agreement (i.e., employees or independent contractors), payment to such parties, and cause for dismissal or removal,

- managerial authority,
- cause for termination of the agreement,
  and
- governing law of any disputes arising from the outsourcing arrangement including choice of law clauses as well as a choice of forum and dispute resolution mechanism.

The broad discretion inherent in contractual relationships can accomplish several goals. First, while American laws are presumed not to apply extraterritorially, outsourcing contracts can create obligations from these laws on foreign entities and individuals, effectively making American regulatory structures applicable to components of the outsourcing arrangement outside of the United States – transplanting American law outside of the U.S. by contract. Second, these contracts can "indemnify the customer in case of a violation of these laws by the vendor." (Weiss and Azaranm, 2007). Third, the agreements can adapt business expectations of foreign workers to those of the American model – in terms of business outputs, working conditions and labor conditions. While these contracts can liberally define the parameters of liability between parties, they cannot usurp legal liability in general. The United States' interest in export control because of national security is an example of this. Parties to an outsourcing contract can acknowledge the validity of the agreement subject to these conditions, but American companies cannot subrogate potential personal criminal liability as a result of the improper export of protected goods and services (*i.e.*, those in which the U.S. has a military or national security interest). Further, "export" is defined in the relevant U.S. trade laws very broadly to include, "[a]ny cross-border transfer, including the download of software from a website or the receipt of an email. . . ." (Weiss and Azaranm, 2007). Such activities done without the proper licensing rights can subject either the outsourcing American company to liability, the affected country or both under both U.S. federal law as well as international treaty obligations.

Contracts should also accommodate the cultural nuances of a host country including the business values and mores of such a country. These values and mores are most often incorporated into the host country's labor laws, but American companies, when drafting outsourcing contracts, would be best protected by not only acknowledging these important matters but actively incorporating these protections into outsourcing agreements. For example, India's labor laws tend to quite favorably protect the worker, and termination clauses in outsourcing contracts should incorporate the processes for employee termination accommodated by that foreign legal system's protections. Further, language and other cultural components such as length of work shifts and paid leave should be drafted into the agreement not only to further define expectation of the parties but also to ensure optimal business productivity of employees and resources of the host country. Nuances of the Indian legal and business framework are of particular importance because of the number of services being diverted there through American outsourcing as well as the willingness of a growing white-collar sector of Indian professionals ready to perform American work services for cheaper that were once the purview of American professionals. One observer has noted that in only a two-year span in the mid-2000s, "[b]usiness outsourcing had saturated the Indian economy . . . the signs of business outsourcing were everywhere." (Geis, 2007). As such, American companies have an interest in drafting outsourcing contracts in such a way that are amenable to Indian business practices and legal protections. Geis sees this as a trade-off in terms of the "agency costs of outsourcing." (Geis, 2007). While he analyzes the principle in an economic model sense, contractual concepts of agency principles are relevant as well. American ideals of what constitutes an employee or an independent contractor are often rooted in limiting legal liability. However, given India's strong individual employee protection in its domestic law, American agency notions of liability may not be effective. A compromise between these costs and how to shift liability dynamics needs to be reconciled with a pro-labor legal and regulatory framework in a carefully worded and detailed contractual arrangement. Geis admits that:

> [P]arties establishing an outsourcing relationship cannot write a perfect contract. Asymmetrical information will persist, and agents might take advantage of unexpected events to secure personal gains at the principal's expense. (2007).

But, a clever and comprehensive drafting and review process, being mindful of the terms addressed above as well as a knowledge of the existing legal framework (of both the U.S. and the host country) and a sympathy for business and ethical culture can put American companies on a good path to productive outsourcing.

11. International Treaty Obligations Governing Outsourcing

International treaty obligations affecting private businesses seek to foster the increase of productivity of businesses but also are drafted mindful of any cultural nuances of the countries that are parties to the agreement. The United States is a party to several international trade agreements which "have fostered a growing interconnectedness . . . creat[ing] a global perspective on the production of goods and services." (CWS 3.0, 2011). Notwithstanding the attempts to restrict offshore outsourcing based on political motives (as outlined above), the United States acknowledges its role in the North American Free Trade Agreement (NAFTA) as well as its overarching acceptance of the GPA from the Uruguay Round Agreements. While domestic law could possibly inhibit some objectives of these multilateral arrangements, as we've seen from the discussion above, the political will to pass such federal domestic legislation stopping offshore outsourcing's impacts has yet to be realized in U.S. law independent of the country's obligations under either NAFTA or the Uruguay Agreements. Even in the specific provisions of NAFTA, for example, the dispute resolution mechanisms seem to guide U.S. policy objectives in a pro-offshoring manner. Individuals who are aggrieved by offshoring practices under the countries governed by NAFTA do not have standing to bring claims for their grievances; only the United States can bring such claims for

individuals on their behalf if they choose to do so. In even deciding to bring a claim, the U.S. can guide offshore outsourcing policy at the behest of private companies. It is also the question of enforcement on the international stage that makes the U.S., as a sovereign actor, less amenable to the whim of the international community of non-discrimination under these international agreements. If a decision is rendered against the U.S. by the WTO, or an adverse decision by the NAFTA Secretariat, as examples, what legal mechanism monitors compliance? Political sanctions may result, but beyond the protections of sovereign authority and enforcement by legal means (to the extent the New York Convention addressed below enforces compliance), the U.S.'s economic power relative to other sovereign actors often determines how it will act on the international stage, including in the realm of offshore outsourcing.

12. Law Governing Outsourcing Disputes — Procedural Safeguards, Process and Dispute Resolution

What "law," then, governs individuals and businesses once a breach of contract is alleged as between an American company and a country where the outsourcing services are engaged? The first place to look, of course, is the language of the contract governing the relationship and a related attempt by the parties involved to resolve their differences in a non-adversarial forum. American companies are not served by the public relations conundrum that can result from media outlets in multiple countries covering a possible improper discharge of an Indian national or discrimination against a Chinese worker. That said, oftentimes the contract attempts to reflect the shared business values and legal norms of both countries while encompassing important matters like data privacy, intellectual property, etc. and also integrating the law of both the U.S. and the host country where feasible. One can easily see how lengthy these agreements can get, and lawyers involved in a dispute in this context, often need time to sort through the allegations and the facts underlying the dispute – this time costs money. Dispute resolution mechanisms (particularly of import when considering how to end the outsourcing relationship) are generally thoroughly covered in these contracts, but certain treaties govern the procedure and dispute resolution fora of all private international arrangements. In that vein, international *arbitration* and mediation can be incredibly valuable to an American company seeking to offshore part of its business.

Mindful of the "buck stopping" at national level sovereignty, even international trade agreements, such as NAFTA and those fostered by the WTO, "include dispute settlement procedures to resolve conflicts in lieu of judicial intervention." (Gupta and Sao, 2009). This is done, in part, because of the realization of the numerous "pitfalls that a U.S.-based party may encounter when trying to litigate a claim against a foreign party." (Weiss and Azaranm, 2007). United States firms that desire the courts' involvement can attempt to include a choice of forum clause in offshore outsourcing contracts, but like choice of law clauses in contracts, it is up to the state of the litigants to determine the enforceability of such provisions. Many states of the U.S. have strong policy considerations in choice of forum provisions in contracts, and these policy concerns make international contracts that much more difficult to enforce if litigation ensues. Further, it is tenuous, at best, to believe that a foreign country would accept a choice of forum in an American court for actions giving rise to the dispute occurring all in that foreign country. There is a strong possibility that these policy considerations could render a choice of forum clause unenforceable, further increasing legal expenses and compounding the concern of how to resolve a dispute. (Gupta and Sao, 2009). How can a judgment be enforced beyond any assets the foreign individual may have in the U.S.? What would be the legal fees involved in relitigating or attempting to enforce a U.S. judgment in a foreign court? A related concern is how pre-trial discovery of evidence will be handled in an international dispute. While the rules of discovery in the United States are very broad, they are much more closely observed by judicial authorities in other countries, with some countries viewing the American model of pre-trial discovery as time consuming, excessive and intrusive. If a clause on discovery is not clearly spelled out in an offshore outsourcing contract, the parties can resort to the Hague Evidence Convention which proves quite cumbersome for the American ideal of discovery. These would all be factors that have to be carefully considered in an offshore outsourcing contract, and because many of these events can result in cost prohibitive unknowns, "arbitration is a better means than litigation for resolving a dispute under an international outsourcing contract." (Gupta and Sao, 2009).

Because arbitration has become the preferred method to resolve international disputes, it has developed into a business in itself with some saying the legal expenses of it "comparable to those of litigation." (Weiss and Azaranm, 2007). Be that as it may, federal law in the United States preempts state laws on the subject so there is more clarity on dispute resolution in this context than the substantive laws governing offshore outsourcing addressed above. Further, virtually the entire civilized world has ratified the Convention on the Recognition and Enforcement of Foreign Arbitral Awards ("New York Convention") making any award decided in one signatory country enforceable in any other country. In this consideration, the jurisdictional and enforcement concerns of potential litigation are removed and enforcement of arbitral decisions are simply made executory by virtue of each country's recognition of the New York Convention. Any time spent by in-house counsel drafting arbitration clauses in offshore outsourcing agreements is well spent as many agree that "arbitration is clearly the better choice in an international dispute." (Weiss and Azaranm, 2007).

13. Discussion

On the surface, offshore outsourcing appears to be a plausible solution for cost-saving purposes. Offshore outsourcing has its pros and cons and a persuasive argument can be made in either direction for or against it.

However, when a Human Resources manager of an organization decides whether to offshore jobs, they need to analyze and delve into whether it would really be beneficial to an organization. Furthermore, just looking at the cost-savings aspect of offshoring jobs does not paint the full picture of the process. There are great disadvantages that are associated with offshore outsourcing and they include hidden costs, bad publicity and low employee morale, quality problems, loss of managerial control, threat to confidentiality and security, and reliance on the financial health of the outsourced organization. What must be taken into account are all these items, it does not make any sense for a Human Resources manager to outsource jobs. Ultimately, when an organization outsources jobs through offshoring, they end up incurring more expenses and getting a substandard product or service. Therefore, offshore outsourcing is a great disadvantage to any organization and the Human Resources manager must convey this message to management and stop this practice in the future.

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