

Procurement

Anti-Avoidance and Contract Terms



Many Local Governments are seeking clarity around the anti-avoidance provisions of the *Local Government (Functions and General) Regulations 1996* and what is considered to be a reasonable length of time for the \$150,000 and above threshold.

This is a critical issue across all types of contracts. The Corruption and Crime Commission's (CCC) *Report on the Investigation of Alleged Public Sector Misconduct by a Local Government Employee in Relation to the Purchase of Management Systems Software (2013)* outlined that the legislative intent of Regulation 12 is:

"To prevent contract splitting, but a plain reading of this provision is that it requires tenders to be invited if a Local Government has already entered into two or more contracts."

It is notable too, that the CCC Report identified claims to 'uniqueness' were leveraged as a tender exemption opportunity under Regulation 11(2)(f) despite there being no evidence of market testing or any documented research supporting this claim. For example, finance systems may be proprietary to a particular vendor but finance systems in their own right are not 'unique' and at the end of a contract period, appropriate market testing should be undertaken in accordance with the Local Government Regulations.

Recommendations stemming from this report, led the Department of Local Government, Sport and Cultural Industries (DLGSCI) to amend the Regulations, with the aim of removing ambiguity with the purchasing and tendering practices of Local Government.

With particular reference to anti-avoidance provisions, a circular was issued in 2015 to highlight the amendments:

"Reports prepared by the CCC made recommendations that the anti-avoidance provisions be strengthened to ensure that contracts were not split for the purposes of avoiding the tender threshold.

Regulation 12 has been amended to clarify this. It is expected that if a Local Government reasonably believes that the purchase of a good or service from one supplier will exceed the tender threshold of \$150,000 they should publically (sic) invite tenders.

No timeframe for the tender threshold has been included in the regulations. However, Local Governments should consider the importance of testing the market through a public tender process for low value, repetitive contracts. **A best practice suggestion is that if the tender threshold is reached within three years, then a public tender is invited for that good or service."**

As indicated in the Department's circular, there is **no specific time limit** applied to the threshold as it is contract based; however, the Department has placed a three year period as the suggested reasonable time for consideration of a period contract.

For ICT and waste a three year time frame is not considered reasonable: as replacement of systems or a contract for waste is often a minimum of five years. Therefore, this becomes the reasonable length of time.

WALGA recognises that Local Governments could be at risk of being in breach of Regulation 12 for anti-avoidance provisions by the manner in which they procure ongoing licensing, support and maintenance for key software systems within their organisations.

The calculation of the total cost of ownership with IT software procurement is the issue, given that it is the *total* cost which determines the most appropriate method of procurement, for example, through written quotations or by a public tender. The *ongoing* component (licensing, maintenance and support) can easily be overlooked as

part of the total projected contract value, which may then lead to the selection of a non-compliant procurement method, such as simply seeking quotes or direct engagement with the vendor when the *real* value would indicate that a public tender should be undertaken (unless a tender exempt option exists).

The total contract value for an IT software procurement ought to include the entire cost of the purchase over the full contract period, including the software component, implementation, ongoing licensing fees, and maintenance and support. Regarding the procurement of software, WALGA recommends that consideration be given to:

- Licence Type;
 - Standalone
 - Network
 - Enterprise
 - Consumption-based (eg “cloud” services)
- Maintenance and Support costs for the life of the product; and
- Conditions of use, especially regarding additional users or modules that may increase the total value.

The ongoing components and predictable growth for IT purchasing are often overlooked when estimating the full contract value and in some cases, Local Governments are undertaking a series of annual contracts for the renewal of licenses, support and maintenance, which could be considered as contract splitting (anti-avoidance).

As an insight, the CCC has found Local Governments to be in breach of Regulation 12, anti-avoidance provisions due to the splitting of contracts particularly in relation to Management System Software, based on claims that the system was ‘unique’. Very few software systems are ‘unique’. Many products may be proprietary but rarely are they ‘unique’.

This is why WALGA believes it is reasonable to expect the installation of major business systems to have an even longer contract term.

Where licensing, maintenance and support is purchased annually, this is considered a *series* of one-year contracts. The total contract spend may exceed the regulatory tender thresholds, or Local Government purchasing policy.

To improve purchasing practices, when establishing a software licensing agreement consider:

- Total cost of ownership for IT software through consideration of whole of life costs and transactions costs related to acquiring, using, licensing, holding and maintaining the goods, and transitioning out to another product;
- Reasonable to anticipate a longer contract term for integral business systems;
- Build in extension options for licence renewals, maintenance and support;
- Consider Preferred Supplier Arrangements (PSAs); and
- If genuine sole source of supply, document appropriate justification.

Despite regular incidences of Local Government procurement activity being brought to the attention of CCC / (DLGSCI) inquiries, there remains serious risks due to a lack of compliance. To be compliant, Local Governments must purchase in accordance with their purchasing policy, as well as ensure that regulatory compliance is maintained. This may include public tender, seeking adequate written quotation, or use of tender exempt services such as the WALGA PSAs.

Misunderstanding or misuse of the ‘uniqueness’ provisions of Regulation 11(2)(f) and contract splitting under Regulation 12 have been highlighted in this fact sheet and Local Governments are strongly encouraged to develop risk management strategies to ensure any procurement activity that invokes either Regulation is tested against detailed research and an open and accountable statement of justification.

WALGA’s Procurement Services team can assist in selecting the right procurement option, and provide advice to ensure that your procurement processes are compliant with procurement policies and legislation.

**For further information please contact: Procurement Services on 92132514 or email
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