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# The New Australian Government Standard Contract For ICT Procurement, SourceIT: The New Benchmark

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## Background

In May 2006 the Australian Government issued a consultation draft of a suite of model form ICT contracts to procure hardware, software, maintenance and support and consultancy services. These contracts are known as 'SourceIT'. These contracts are for use by Federal Government Agencies. The aim of these contracts was to increase consistency in contractual arrangements with the Australian Government, to reflect Australian Government policies, to reduce costs and to simplify the procurement process.

Following consultation with the ICT industry, including intense lobbying from the Australian Information Industry Association (AIIA), the Australian Government released version two of the contracts for immediate use in May 2007.

Given that in the 2004/2005 financial year the Australian Government entered into more than 24,000 ICT contracts, and spent more than \$3 billion on ICT procurement, these new contracts are the most important ICT contracts to be issued for many years. They will influence government, and probably non-government, ICT procurement for many years. The contracts include the Australian Government's new policies on limiting liability and ownership of intellectual property, both of which were warmly welcomed by the ICT industry. However, the contracts require ICT suppliers to meet much higher standards (when compared to the existing standard Australian Government ICT contract, GITC v4) when they supply ICT products and services.

Whilst the contracts are already available for use by Australian

Government (Federal) Agencies, the Australian Government Information Management Office (AGIMO) is seeking feedback on the contracts from Agencies and suppliers and will update the contracts over time.

## What this Article will Tell You

This article is the first of two articles which will provide an analysis of the SourceIT suite of contracts. This first article will provide an overview of the SourceIT contracts and a discussion of the legal terms and conditions that are common across the entire suite of contracts. The second article will be in the next issue of *Computers & Law* and will provide an analysis of the terms and conditions that are specific to the particular type of product or service that is the subject matter of each of the contracts. The second article will also provide guidance on how to complete the 'Contract Details' (which set out the specific variables for the product or service being bought) and the various schedules to the contract. This guidance will assist Agencies and suppliers to ensure that the final version of the contract documentation is complete and minimises risks for both parties.

## What are the SourceIT Contracts?

Four model form contracts have been developed:

- Hardware Acquisition and Maintenance;
- Licence and Support of Commercial off-the-shelf (COTS) Software;
- Licence of Commercial off-the-shelf (COTS) Software (without support); and
- IT Consultancy Services.

To support the use and implementation of SourceIT contracts,

a specific SourceIT website has been established by AGIMO which provides access to copies of the contracts as well as user notes. These user notes provide practical assistance to Agencies and suppliers alike on how and when to use the contracts. This website can be found at [www.sourceit.com.au](http://www.sourceit.com.au)

## Structure, Scope and Purpose of the Contracts

Each model contract (apart from the Software Licence) contains four sections. The format of the contracts is common, and the structure and sequencing of the clauses is similar across all the contracts, providing a common 'user interface'!

**The first section is the product or service specific terms and conditions** section which contains the clauses that relate to that particular product or service. For example, in the Hardware contract this section contains provisions dealing with installation and delivery; in the Licence Contract for COTS Software this section contains provisions relevant to the scope of the licence.

**The second section is the General Requirements** section which contains the 'legal boiler plate' clauses such as payment, indemnities, liability, confidentiality and termination.

**The third section is the Contract Details** which are contained within Schedule 1 and allow the parties to identify key pieces of information that are specific to that contract, including the parties' details, commencement date, initial contract period, option period, option notice period, the product or service being bought, the warranty period, any third party product warranties, relevant industry standards, approved subcontractors, the support period, intellectual property rights ownership and licences

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and limitation of liability to name a few. The Contract Details also allow the parties to alter the many default positions contained within the terms and conditions for issues such as ownership of intellectual property and escrow arrangements.

The Schedules contain other relevant documentation the parties may need to refer to during the term of the contract and information forming part of the contractual terms, such as the product specifications or the statement of work, fees and payment details, confidentiality schedule and undertakings.

The contracts are designed for use as one-off transactional contracts, and are not suitable for panel arrangements. They are also designed for use with simple procurement of ICT products and services. However given the amount of detail in some of the contracts it is possible for relatively complex arrangements to be based on these contracts. For example the License and Support Contract could be used for a fixed price implementation of a customised software application including the on-going support of that customised application.

Whilst the contracts are available for use by any Australian Government Agency, Agencies are not compelled to use them. It will be interesting to see how they are used in practice, whether they are used without amendment, or whether Agencies will amend them further for specific transactions. No matter how they are used, we believe that these contracts will be highly influential in the ICT procurement both from a government and an industry standpoint. It is likely that commercial organisations will adopt some of the clauses from SourceIT in their own ICT procurement contracts.

### Progress Made During Consultation

Whilst these contracts require the supplier to meet a much higher standard, the requirements (at least from an ICT industry point of view) and the business models that are reflected in the release version of SourceIT have improved significantly as a result of the consultation process. Some of the major improvements during that process include:

- improved business models (it is now possible to use a single contract (not two contracts) to buy hardware and its operating system);
- there is a standalone software 'Licence' only contract;

The following clauses have also been improved.

- the liability regime;
- indemnities (particularly the removal of a supplier's indemnity to the Customer for the losses arising from the supplier's breach of contract);
- IP ownership and licensing; and
- some new clauses provide the supplier with rights to audit the Customer's use of software products and a limited right for the supplier to terminate the contract if the Customer does not pay.

During the time that the model contracts were under development two major Australian Government policies were adopted dealing with:

- capping ICT supplier's liability ('A guide to limiting supplier liability in ICT Contracts with Australian Government agencies'<sup>1</sup>) and
- intellectual property (Statement of IP Principles for Australian Government Agencies<sup>2</sup>).

The release version of the SourceIT Contracts takes into account these policy initiatives.

### Key Obligations in the Boiler Plate Legal Terms and Conditions section of SourceIT

#### General Product and Service Warranties

The standard of the product warranty is very high. A supplier is required to supply the Products and/or Services with due skill and care and to the best of its knowledge and expertise, and in accordance with;

- the Service Levels;
- relevant Australian industry standards, best practice and guidelines, or where none apply,

relevant international industry standards, best practice and guidelines; and

- applicable laws and Commonwealth policies and specific requirements identified by the Customer.

These warranties are very broad. Further, industry standards, best practice, law and Commonwealth policies may change during the term of the Contract. The Contract Details allow the parties to identify 'relevant industry standards', however this does not limit the applicable industry standards to those identified.

In addition the Products and/or Services must comply with and be fit for purpose as set out in the relevant Specifications and Documentation. A Product (including documentation) must also be complete, accurate and free from material faults in design.

The supplier is required to warrant that:

- it will not, nor will it allow any third party under its direction or control to, negligently introduce Harmful Code (viruses, Trojan horses etc) into the Customer's system or the Product/Services;
- there is no Harmful Code in any Product/Service;
- it will meet any milestones or if there are no milestones, that it will supply the Product/Services promptly and without delay;
- that the Warranted Materials (essentially the products, services or deliverables provided under the contract) and that the Customer's use of those Warranted Materials does not infringe the intellectual property rights of any person; and
- it has the necessary rights to vest the intellectual property rights and grant the relevant licences to the Customer.

The level of warranties required becomes increasingly significant for a supplier as the Customer has the right to terminate the contract immediately without notice for breach of a warranty where that breach cannot be

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remedied. This will be discussed further below under 'Termination'.

The second article that will appear in the next issue of Computers & Law discusses the extent of the specific product and service warranties, and whether those warranties are time bound by a warranty period, the obligations to rectify defects, and the extent to which the industry standard exclusions apply (such as the warranty does not apply if the Customer does not use the product in accordance with the manufacturer's instructions).

### *Liability*

The contracts all provide for the parties to agree a **mutual** cap on liability in an amount identified in the Contract Details on a per occurrence basis (or series of related occurrences). The parties are able to agree that the cap applies on an aggregate basis. The cap does not apply to:

- personal injury;
- loss or damage to tangible property;
- infringement of intellectual property rights;
- breach of an obligation of confidence, security matter or privacy; or
- any breach of statute or any willfully wrong act or omission (including repudiation).

There is no exclusion of indirect or consequential loss, nor any exclusion of loss of profit, revenue, goodwill, reputation or loss of data.

The Australian Government policy relating to capping ICT suppliers' liability is based on the Agency having completed a mandatory risk assessment, following the Standards Australia -Australian and New Zealand Standards for Risk Management in AS/NZS 4360: 2004 Risk Management. The risk assessment process should enable the Agency to determine the level of the liability cap and appropriately allocate the risk between the parties. This policy takes the position that contracts imposing unlimited liability should only be agreed when there is a compelling reason to do so.

### *Indemnity*

The supplier is required to indemnify the Customer and its Personnel (which includes the Customer's subcontractors and professional advisers), against 'Losses' reasonably sustained or incurred by the Customer as a result of a claim made or threatened by a third party arising out of or in connection with:

- any negligent, unlawful or willfully wrong act or omission of the supplier or its Personnel (which includes the supplier's subcontractors and professional advisers);
- an allegation that any Services or "Warranted Materials" infringes intellectual property or moral rights.

It should be noted that 'Losses' include legal costs on a full indemnity basis whether incurred by or awarded against a party. However, the Customer is under an obligation to make reasonable efforts to mitigate its loss.

If the Customer wishes to enforce an indemnity it must permit the supplier to handle all negotiations for settlement and as permitted by law, to control and direct any settlement negotiation or litigation that may follow. However a supplier must adhere to a number of requirements including compliance with government policy and obligations as if it were the Customer. This obligation includes adherence to the Legal Services Directions and any direction issued by the Attorney General to the Commonwealth. This will limit the manner in which the supplier can conduct the settlement or litigation process.

### *Confidentiality*

Neither party is able to disclose the other's Confidential Information to a third party without the other party's prior written consent. Accordingly a supplier is not permitted to disclose Confidential Information to its Related Bodies Corporate or its subcontractors without the written consent of the Customer.

Either party can require the other to arrange for its Advisers or any other

third party (other than a Customer's employee) to enter into a personal written undertaking protecting the disclosure of confidential information directly with the discloser. The parties can agree the form of this undertaking and attach it to the relevant schedule to the contract.

The contracts set out a number of exceptions to the obligation not to disclose the other party's confidential information, for example, disclosure to Advisers and employees are allowed if the information is being disclosed solely in order to comply with obligations or to exercise rights under the contract. Confidential Information can be disclosed if it is authorised or required by law, including under the contract or under a licence. The Customer has additional rights to disclose the supplier's confidential information to the Minister, to Parliament or to other Agencies if it is in the Commonwealth's 'legitimate interest' to do so.

The other point to note is that the parties should agree what information is confidential at the time the contract is first signed (by completing the relevant schedule), and any changes or new confidential information that is introduced during the term of the contract should be agreed by way of amendment to the contract.

### *IP Rights and Grant of Licence*

Apart from the COTS Software Licence, the model contracts allow the parties to choose between two pre defined Intellectual Property (IP) models. The different IP Models apply to the rights of ownership and use of Contract Materials (essentially intellectual property created under the contract). There is express guidance printed in the SourceIT contracts which clearly states that the 'default' IP model that is drafted into each contract should not be seen as the Australian Government's preference. The default ownership position of Contract Materials is:

- that the Contractor owns the Intellectual Property Rights in the Software Licence and Support Contract, and provides a licence to the Customer to use the Contract Material;

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- that the Customer owns the Intellectual Property Rights in the Contract Materials in the IT Consultancy Contract.

The intellectual property arrangements differentiate between 'Contract Materials' and 'Auxiliary Materials'. Contract Materials are defined as *'any Material created by the Contractor on or following the Commencement Date, for the purpose of or as a result of performing its obligations under this Contract'*. Auxiliary Materials are defined as *any Material, other than Contract Material, which is made available by a party for the purpose of this Contract, on or following the Commencement Date, and includes:*

- (a) *Third Party Material;*
- (b) *any modifications that may be required [if a third party or the Customer claims that all or part of the Warranted Materials infringes their Intellectual Property rights] ;*
- (c) *error corrections or translations to that Material; or*
- (d) *derivatives of that Material where such derivative work cannot be used without infringing Intellectual Property Rights in the underlying Material.*

The definition of Third Party Material is very broad and includes: any Software, firmware, documented methodology or process, documentation, specifications, user and operations manuals and training materials).

The Auxiliary Materials are dealt with in a similar way across all the model contracts. The Contractor's license to the Customer for Auxiliary Material is a world-wide, royalty free, non-exclusive licence, (including the right to sublicense) to use, reproduce, adapt, modify and communicate that Material. This is a very broad licence, but does not include the right to exploit the Auxiliary Material for the Customer's commercial purposes.

Whilst most suppliers will feel comfortable granting this licence for any intellectual property (other than software or documentation 'products' which have their own commercial

price list, and perhaps training materials) that is owned by the supplier, where the supplier is sublicensing third party intellectual property, the supplier will need to obtain a sublicensing right from the third party which is at least equivalent to the licence that the supplier is required to grant to the Customer. In particular, where a supplier is sublicensing a third party software product which is a commercially available product (as opposed to a tool or methodology), the supplier is likely to need to amend this clause to reflect the licensing arrangements of the third party product.

Under the new Statement of IP Principles for Australian Government Agencies the use of intellectual property on a whole of government basis is encouraged. Suppliers should note that the licence granted under the SourceIT contracts is granted to the 'Commonwealth' and is not restricted to the Agency that signs the contract.

### Security, Audit and Access

The supplier, its subcontractors and Personnel (which include professional advisers) are required to comply with the security requirements set out in the contracts. These security requirements include obligations to comply with the requirements specified in the Commonwealth Protective Security Manual, any additional requirements set out in the Contract Details and any other security requirements notified, in writing, by the Customer to the supplier. Lawyers take note; if you represent a supplier, and the supplier signs SourceIT without amendment the supplier will require your firm to comply with some of the obligations in SourceIT!

There are particularly strict obligations on how a supplier is permitted to deal with 'Customer Data', including not being permitted to remove Customer Data from the Customer's premises or take it outside Australia without the Customer's prior written consent. Customer Data is very broadly defined and includes *'all data and information relating to the Customer'*. This will be particularly significant for the provision of support services which are regularly provided

from locations outside Australia and involve the transfer and use of 'Customer Data'.

\*The Customer has a very broad right of audit which includes audits of suppliers operational practices and procedures, the accuracy of invoices and reports, compliance with confidentiality, privacy and security obligations under the contract and any other *matters determined by the Customer to be relevant to the Services or Contract'*. The Customer also has the right to access the premises of the supplier at reasonable times on giving reasonable notice.

In addition to this the Customer is able to *'inspect and copy documentation, books and records, however stored, in the custody or under the control of the supplier, its employees, agents or subcontractors'*. This will include all records, documentation, books, information hardware and software. Further, the drafting of the relevant provisions does not limit inspection to documentation connected to the provision of the Product or Service.

These powers of audit and access are in addition to the statutory powers of the Privacy Commissioner and Auditor General. Suppliers should also note that these provisions are required to be included in their subcontracts with their subcontractors. These rights of access and audit are likely to be of great concern to many suppliers and their subcontractors and may breach a supplier's or subcontractor's internal confidentiality, security and privacy obligations, or similar obligations to third parties under pre-existing arrangements.

### Acceptance

As is appropriate in contracts that are designed for low risk procurements the default position in SourceIT is that Products are 'Accepted' upon the date the supplier delivers the Product in accordance with the Statement of Work and do not need to undergo Acceptance Tests.

However there are some issues with the Acceptance Test provisions in that:

- There are no default time frames for the Customer to complete any Acceptance Tests.

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- There are no specific obligations placed on the Customer (e.g. to provide the hardware environment when the Product being tested is a software Product).
- There is no express statement (though it might be implied) that the Product **has to be** 'Accepted' if it meets the requirements of the contract (i.e. there is an objective standard, and not a subjective standard for meeting the Acceptance Criteria.)
- There is no concept of materiality in considering whether the Product has met the Acceptance Criteria, i.e. any error/defect no matter how small enables the Customer to determine that the Product has not met the Acceptance Criteria.

The supplier does have the opportunity to rectify the defects if a Product/Service fails the Acceptance Test. However, the supplier only has 5 days from the date the Customer notifies of a failure to rectify the defects. The Customer has the right to terminate the contract if any part of the Product or Service fails (for any defect no matter how small or inconsequential) the Acceptance Test on two or more occasions. The concept of repeat acceptance testing is a very practical solution, even if the timeframes for rectification are extremely tight.

### Personnel

A key issue here is that the definition of 'Personnel'. Personnel is defined as *'in relation to a party, any natural person who is an employee, officer, agent or professional adviser of that party or, in the case of a supplier, of a subcontractor'*. The inclusion of 'professional adviser' is unusual and results in the Customer having significant control over a supplier's professional advisers.

Specified Personnel include the supplier's subcontractors and Personnel specified in the Contract Details.

The supplier must provide the Services to which their particular expertise relates, with the active involvement of, and using the

expertise of the Specified Personnel. If one or more of the Specified Personnel becomes unable or unwilling to be involved in providing the Services then the supplier must notify the Customer immediately and if requested by the Customer, the supplier must provide a replacement person of suitable ability and qualifications at no additional charge at the earliest opportunity. The Customer must approve the replacement person prior to their appointment.

The Customer may at any time request the supplier to remove Specified Personnel, the supplier's subcontractors or Personnel from work in respect of the contract. The Customer must also approve replacement Personnel prior to their appointment. Accordingly the Customer can not only remove an individual from a project, the Customer can effectively remove a subcontractor from the project simply by giving notice. The drafting suggests that the Customer could remove a supplier's professional advisers from the project too! The relevant contract provisions do not allow any exceptions (such as maternity leave or an employee resigning) to the supplier's obligation to provide the Specified Personnel to provide the services personally.

There is no contractual obligation on the Customer to act in good faith, reasonably or to provide reasons when requiring Personnel or Specified Personnel to be removed. The contracts do not provide any relief to the supplier if Specified Personnel are unable or unwilling to provide Services or if the Customer requires removal of Specified Personnel or Personnel; the supplier is still obliged to meet its obligations under the contract.

It should be noted that any breach of the obligations relating to Specified Personnel constitutes a breach of a material provision and may give rise to the Customer terminating the contract for cause.

### Termination

*Termination by Customer for Convenience*

The Customer has the right to terminate for convenience at any time, by notice or reduce the scope of the services. If this occurs the Customer is only liable for:

- payment for 'Services rendered' before the effective date of termination; and
- reasonable costs incurred by the supplier and directly attributable to termination.

The Customer also has the right to reduce the scope of the Services, including for a machinery of government change. If this occurs the Customer's liability to pay the Service charges or to provide Customer Material abates in accordance with the reduction in the Deliverables or Services. Accordingly suppliers need to recognise and manage this risk particularly if there are high fixed costs or long term costs associated with a contract.

There is no provision in any contract for a minimum service period or any 'pre-agreed' break costs.

### *Termination by Customer for Cause*

The Customer has the right to terminate for cause effective immediately by giving notice to the supplier, if the supplier:

- breaches a material provision where the breach is not capable of remedy; and
- breaches any provision of the contract and fails to remedy a breach within 14 days after receiving notice requiring it to do so.

The contracts identify breaches of particular contract clauses that would constitute a breach of a material provision, including:

- a breach of Product warranties, for example, *'the Software and Documentation will be complete, accurate and free from material faults'*;
- and a failure to comply with the clauses dealing with:
  - Personnel
  - Intellectual Property Rights;
  - Insurance;

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- Confidentiality and privacy;
- Protection of personal information; and
- Conflict of interest.

### *Termination by Contactor*

As a result of the consultation process the supplier now has a very limited contractual right to terminate a contract. This contractual right is limited to the right to terminate if the Customer has not paid a correctly rendered invoice despite two written notices from the supplier. There is no contractual right for a supplier to terminate if the Customer breaches its obligations to keep the supplier's confidential information confidential or if the Customer uses the supplier's software in breach of the license terms for example.

### **Summary**

It is clear that the Australian Government has raised the bar for ICT suppliers that want to provide their products and services to Federal Government Agencies. Whilst the consultation process significantly

improved the usability of the suite of contracts and reduced some of the extreme contractual risks, there remains a significant number of clauses that many suppliers will find hard to accept without amendment.

Where there is any negotiation on a contract, it will inevitably cost both the Agency and the supplier money and time. Lengthy negotiations are not really appropriate or necessary when simple products and services are being bought and sold; these contracts should require a minimum number of items that require negotiation or careful consideration when choosing which of the various default positions apply. As the Australian Government is intending to review the contracts based on feedback and experience of their use in the field it is important that suppliers and Agencies alike provide their comments back to AGIMO. In this way it is more likely that the next version of the contracts will see improved workability and a more cost effective simple procurement process for both government and industry.

*This article is based on a presentation by Mike Pym at AIIA's seminars on the SourceIT Model Contracts in Sydney and Canberra 19/20 June 2007. Mike Pym provided substantial advice to the AIIA on the AIIA's submission to AGIMO during the consultation process, and has been heavily involved in assisting the AIIA in the consultations and negotiations with various State and Federal Governments on ICT procurement over the past decade or more, especially GITC v4, GITC v 5 (Qld), ProcureIT (NSW) and SourceIT. Mike Pym is the director at Pym's Technology Lawyers.*  
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<sup>1</sup> Australian Government, Department of Communications, Information Technology and the Arts, August 2006, "A guide to limiting supplier liability in ICT contracts with Australian Government agencies".

<sup>2</sup> More information about the Statement of IP Principles is located on the Attorney General Department's website at [www.ag.gov.au/cca](http://www.ag.gov.au/cca).