

The Parliament of the Commonwealth of Australia

Senate Legal and Constitutional References Committee

**Inquiry into the Outsourcing of the Australian
Customs Service's Information Technology**

May 2002

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TABLE OF CONTENTS

REFERENCES COMMITTEE MEMBERSHIP	iii
GLOSSARY OF ACRONYMS	vii
CHAPTER ONE	1
BACKGROUND TO THE INQUIRY	1
Reference to the Committee and Terms of Reference	1
Background to the Inquiry.....	2
Previous related inquiries	4
CHAPTER TWO	7
OUTSOURCING AND THE USE OF OUTSOURCING BY CUSTOMS.....	7
The Outsourcing of Public Sector Services.....	7
The Outsourcing of IT Services	8
IT Outsourcing in the Australian Customs Service.....	9
CHAPTER THREE	13
THE CUSTOMS CONNECT FACILITY	13
Introduction	13
The Need for a New Connection Facility.....	13
The CCF Implementation Process.....	17
Financial Costs and Benefits of the CCF	20
CHAPTER FOUR.....	23
THE CCF CONSULTATION PROCESS.....	23
Introduction	23
Outline of consultations undertaken.....	23
Proper Consultation.....	24
Consultation with Tradegate and Connect	25
CHAPTER FIVE.....	29
TRANSITION TO THE CCF	29
Procedures if the CCF is not in place.....	30

APPENDIX 1	23
INDIVIDUALS AND ORGANISATIONS THAT PROVIDED THE COMMITTEE WITH SUBMISSIONS	23
APPENDIX 2	25
WITNESSES WHO APPEARED BEFORE THE COMMITTEE	25

GLOSSARY OF ACRONYMS

ACS	Australian Customs Service
AFIF	Australian Federation of International Forwarders
AGAL	Australian Government Analytical Laboratories
AEC	Australian Electoral Commission
AUSLIG	Australian Surveying and Land Information Group
CEO	Chief Executive Officer
CCF	Customs Connect Facility
CMR	Cargo Management Re-engineering
COMPILE	Customs On-Line Method of Preparing from Invoices Lodgeable Entries
CSP	Communication Service Provider
DIMA	Department of Immigration and Multicultural Affairs
EDI	Electronic Data Interchange
EDS	Electronic Data Systems Australia
ICS	Integrated Communication System
IT	Information Technology
NCA	National Crime Authority
OASITO	Office of Asset Sales and Information Technology Outsourcing
RFI	Request for Information
RFT	Request for Tender
SME	Small and Medium Enterprises
VAN	Value Added Network

CHAPTER ONE

BACKGROUND TO THE INQUIRY

Reference to the Committee and Terms of Reference

1.1 On 26 June 2001, on the motion of Senator O'Brien (at the request of Senator Bolkus), the Senate referred to the Legal and Constitutional References Committee the following matters, for inquiry and report by the last sitting day in December 2001:

- (a) the processes involved in, and the consequences of, the outsourcing of the ACS's information technology;
- (b) the benefits and problems associated with the current and proposed ACS communications systems;
- (c) the needs and capabilities of importers, exporters and service providers in respect of ACS information technology and communications systems;
- (d) the way in which the ACS has conducted consultations with importers, exporters, and service providers in relation to information technology and communications systems; and
- (e) issues associated with the involvement of the ACS in e-commerce.

1.2 A federal election was held on 10 November 2001. Following the election, Parliament recommenced on 12 February 2002. The Committee met on 14 February 2002 to consider references not disposed of at the end of the 39th Parliament, and resolved to recommend to the Senate that the Inquiry into the Outsourcing of the Australian Customs Service's Information Technology should be re-adopted with a reporting date of 14 May 2002. Senator McKiernan tabled a report to that effect in the Senate on 11 March 2002, and the recommendations contained in the report were agreed to by the Senate.

1.3 The Committee advertised the inquiry on 7 July 2001 in the Weekend Australian newspaper, and received 8 submissions (including 1 supplementary submission), which have been made public and listed at Appendix A.

1.4 A public hearing was held in Canberra on 15 March 2002. Witnesses are listed at Appendix B.

Background to the Inquiry

1.5 Certain aspects of the Australian Customs Service's (Customs) IT outsourcing contractual arrangements were raised during the Senate Legal and Constitutional Legislation Committee's consideration of Estimates in late 2000¹ and early 2001.² In particular, Senator Lundy asked a number of questions concerning the Tradegate company, which had been established around 1990 and which facilitated electronic access to Customs services by customs brokers, importers and freight forwarders.³ Tradegate, or its CEO, had advised that business would be affected by the development of an alternative access service by Customs. The development of such a system was required by the *Customs Legislation Amendment and Repeal (International Trade Modernisation) Act 2001*, which was the subject of a report by the Senate Legal and Constitutional Legislation Committee in May 2001. Tradegate believed that this service, developed for Customs by the company EDS, could have detrimental effects on Tradegate, and on some of its users.

1.6 Senator Lundy's questions related primarily to:

- The status of Tradegate as previously the only supplier of an access service;
- The transparency and equity of the tender and contract process relating to the new Customs Connect Facility (CCF);
- The extent to which the contract between Customs and EDS made provision for the development of new services or systems, such as the Customs Connect Facility (CCF); and, if so, whether such information should have been provided to Tradegate;
- The value of consultation between Customs and the user community in the effective management of business and development of new systems and the decrease in such consultation; and
- The extent to which informal connections and discussions between Tradegate and Customs, which ceased on EDS taking over IT, were an integral part of the arrangement between Customs and Tradegate; and the effect of this in customer relations and Tradegate's position;

1.7 Senator Lundy indicated concern about the answers provided, and subsequently requested that the issue be referred for further investigation.

1.8 The essence of Tradegate's and Senator Lundy's concern, was not the outsourcing of IT services *per se*.⁴ All of Customs' IT had been outsourced to the EDS company, and other contractors,⁵ from early 1998, prior to the government's IT Outsourcing Initiative.⁶ Tradegate

1 Senate Estimates *Hansard*, Legal and Constitutional, 22 November 2000, pp. 66-72

2 Senate Estimates *Hansard*, Legal and Constitutional, 19 February 2001, pp. 64-82

3 The date of Tradegate's commencement is unclear. In *Submission 1*, p.3 Tradegate stated that it was awarded the Customs contract in 1991, while in *Submission 7*, p.4 Customs stated that Tradegate was formed and awarded the Customs contract in 1989.

4 The issue of the cost effectiveness and usefulness of IT outsourcing was considered by the Senate Finance and Public Administration References Committee in 2000-2001

5 *Submission 7*, Australian Customs Service, p.5

6 Senate Estimates *Hansard*, Legal and Constitutional, 19 February 2001, p. 74

itself was also an outsourced service provider,⁷ although its original links with Customs were obscured by time and by the involvement of a range of groups in its administration.⁸

1.9 Nonetheless, outsourcing is an important issue in that a number of concerns raised by Tradegate arise from the fact that a new relationship developed with an outsourcer (EDS) was seen to have had a series of specific and broader effects on Customs IT, and on Customs' relationship with Tradegate. While there is general agreement that certain events (in relation to the development of new communication access arrangements for Customs) occurred, there is a difference of opinion as to whether such effects were necessary, beneficial, cost-effective, and implemented in accordance with appropriate standards and policies.

1.10 These concerns, and the questions raised by Senator Lundy, are reflected in the five terms of reference, which are listed above in paragraph 1.1. Those terms of reference cover:

- a) The processes which Customs has undertaken in developing and managing the outsourcing of its information technology; and the consequences of it doing so;
- b) The effectiveness, for Customs and for the users of its systems, of both the current access system (via Tradegate, but not exclusively so) and the proposed system (allowing users to connect directly to customs via a number of means, including a new access system run by EDS on Customs' behalf);
- c) Whether the current and proposed systems are effective in terms of the operational and technical needs and capabilities of users of the systems;
- d) Whether the Customs' consultation processes, with respect to their IT systems generally (and with respect to the Tradegate hub/Customs Connect Facility in particular, as these are the point at which users interact with Customs systems) have been appropriate; and
- e) Broader issues of practice and principle concerning public sector outsourcing; the mix of public and private service providers; contract development and management; and the principles that should apply to public resources.

1.11 The Committee has divided the chapters of this report into issues rather than terms of reference. The chapters deal with:

- Outsourcing, and the extent of Customs information technology outsourcing (chapter 2, covering terms of reference (a), (c), (d), and (e));
- The Customs Connect Facility (CCF), including the need for (and circumstances surrounding) new means of access to Customs systems, the financial costs/benefits for users of the CCF, and the implications for Tradegate (chapter 3, covering terms of reference (b), (c), and (d));
- The effectiveness and fairness of the consultation processes undertaken by the Customs in relation to the CCF (chapter 4, covering terms of reference (a), (d), and (e)); and
- The process of transition which must now be undertaken in order to implement the CCF (chapter 5, covering terms of reference (b),(c), and (e)).

7 See *Submission 1*, Tradegate, p. 2

8 See *Submission 1*, Tradegate, p. 2

Previous related inquiries

1.12 A number of inquiries relevant to this report have been conducted by the Commonwealth, especially since the commencement of the government's IT outsourcing initiative. A number of these, and their relationship to the current report, are outlined below.

Review of the Whole of Government Information Technology Outsourcing Initiative (the Humphry Report) – December 2000

1.13 The report was conducted by Mr Richard Humphry AO, reporting to the Minister for Finance and Administration (then the Hon John Fahey MP). As implied by the review's title, the Humphry review focussed on the agencies involved in the whole of government IT outsourcing process. As noted above, Customs had commenced its IT outsourcing process prior to the commencement of the whole-of-government process ("the Initiative"). It was not, therefore, directly subject to review in the Humphry report. Despite this, the Humphry report outlines a number of challenges encountered by Commonwealth agencies in undertaking IT outsourcing, particularly as regards transition to an outsourced environment. These conclusions provide useful background to the current report.

1.14 One of the Humphry Report's most important conclusions did not relate to IT itself, but rather to the management of relationships during the transition to an outsourced environment. Humphry wrote that:

It is clear to me that the implementation of the Government's IT Outsourcing Initiative is primarily an organisational and people management exercise that revolves around IT. It is not simply a matter of signing a workable contract for IT services. Fundamental to an understanding of transition is that it is not merely a technology issue. The implementation project at its heart is about the management of human resources and cultural change, of which technology is an important but not dominant element.⁹

1.15 It follows that in meeting its terms of reference, and particularly terms of reference (a), (c), (d) and (e), the Committee should consider how Customs managed stakeholder relationships during its IT outsourcing process, and not just how Customs managed the contractual and technological aspects of the process.

1.16 Humphry also noted that:

Sufficient attention has not always been given to the necessary process of understanding an agency's business. As a consequence, post contract uncertainties and associated risks have not always been anticipated. This approach has resulted in a large number of issues still needing resolution well after contract signing, which has added considerably to the risks of implementation.¹⁰

9 *Review of the Whole of Government Information Technology Outsourcing Initiative* ("the Humphry Report"), p.39

10 *Review of the Whole of Government Information Technology Outsourcing Initiative* ("the Humphry Report"), p.32

1.17 This caution articulates directly with term of reference (c) for this inquiry. Customs' business is reliant upon its Electronic Data Interchange (EDI) systems, and upon the capacity of importers, exporters and service providers to interact with these systems.¹¹ As a result, the requirements and wishes of users are a critically important parameter for any developments in Customs' systems.

Rebooting the IT agenda in the Australian Public Service – August 2001

1.18 This report was the final report of the Senate Finance and Public Administration References Committee Inquiry into the government's IT outsourcing initiative. The recommendations of the Finance and Public Administration Committee focus on procurement skills, contract design, probity issues and intellectual property issues, but the discussion in the report is much more wide-ranging. A number of the issues to be dealt with in the current report were raised in submissions and evidence to the Finance and Public Administration References Committee.¹²

1.19 As with the Humphry Report, "Rebooting the IT Agenda" did not assess the Customs' outsourcing arrangements directly, as the Customs/EDS contract was not developed as part of the whole of government outsourcing initiative. However Customs made a submission to the inquiry¹³, and on several occasions the report drew on Customs' experiences, as expressed in the "Lessons Learned" section of the submission. In particular, the report drew on Customs statement that:

There needs to be a mechanism whereby service providers gain a quick but comprehensive understanding of the business of agencies, Government processes and requirements and of the Auditor-General. They also need to understand that these can change quickly in response to evolving business needs, legislative changes or variations in Government requirements.¹⁴

Senate Legal and Constitutional Legislation Committee Report, May 2001

1.20 In May 2001 the Legal and Constitutional Legislation Committee reported on an inquiry into three Bills, among them the *Customs Legislation Amendment and Repeal (International Trade Modernisation) Bill 2000*. In the course of this inquiry, the Legislation Committee examined the Cargo Management Re-engineering (CMR) process undertaken by Customs, and within the CMR process, the new communications arrangements under

11 See *Submission 7*, Australian Customs Service, p.3: "Current [EDI] systems now provide for almost 100% of the processing and clearance of imports, exports and cargo"

12 For instance, Connect's submission to this inquiry included as an appendix its submission to the Finance and Public Administration Committee's inquiry. In it, Connect raised a number of issues related to arrangements between Customs and Tradegate.

13 This submission forms Appendix A of *Submission 7*.

14 *Submission 7*, Australian Customs Service, p.29, as quoted in *Rebooting the IT Agenda in the Australian Public Service*, Final Report on the Government's Information Technology outsourcing initiative, August 2001, p.130

development. Whilst the Committee considered evidence from Tradegate and Connect¹⁵ on this issue, it considered that the question of the implementation of new communications technology was beyond its brief, and concluded as follows:

The Committee notes that Tradegate (and [Connect]) believe they have not been properly consulted about the transition between the two systems. The Committee is of the view that as the contract between Tradegate and Customs is to be extended to July 2002, there is an opportunity to remedy some of those concerns about consultation. The Committee recommends that Customs be required to undertake further consultation to ensure that industry is given sufficient notice of the kinds of information standards they will be required to have to operate competently within the new system. [The Committee] again notes the difficulties for business in an environment that is being fundamentally reformed and urges Customs to release the implementation plan in relation to the commencement of the CMR system as soon as possible.¹⁶

15 In this report, “Connect” refers to the company known at different times as Paxus, AT&T Easylink, connect.com.au, and Connect Internet Solutions.

16 Senate Legal and Constitutional References Committee, *Consideration of legislation referred to the Committee: Inquiry into the Provisions of the Customs Legislation Amendment and Repeal (International Trade Modernisation) Bill 2000, the Import Processing Charges Bill 2000, and the Customs Depot Licensing Charges Amendment Bill 2000*, p.46

CHAPTER TWO

OUTSOURCING AND THE USE OF OUTSOURCING BY CUSTOMS

The Outsourcing of Public Sector Services

2.1 The outsourcing or contracting of public sector services in Australia goes back as far as European settlement, as the First Fleet itself was an outsourced service provided to the UK government by private contractors.¹ Contracting of mail delivery and postal services in Australia goes back over 150 years, and the outsourcing of construction and works activities has often been undertaken by all three levels of government in Australia.²

2.2 Since the mid-1990s outsourcing of government activities in Australia has received increased attention consistent with policies to advance microeconomic reform. The Productivity Commission outlined the rationale for outsourcing some government activity as follows:

Increasingly, governments are recognising that while they might have a responsibility to *fund* services, they are not always best placed to *provide* the service. By funding others to provide the service (through a competitive process) delivery to clients can be improved and savings can be made to the benefit of taxpayers and/or other programs. [...] If properly applied, [outsourcing] can lead to significant improvements in accountability, quality and cost effectiveness, while providing benefits to clients, taxpayers and the broader community.³

2.3 It follows that successful outsourcing has two strategic goals:

- More efficient and effective delivery of outcomes; and
- Streamlining of departments and agencies in order to allow them to focus on their core responsibilities.

2.4 These goals, and the means of meeting them, have been codified in the *Commonwealth Procurement Guidelines and Best Practice Guidance* issued by the Department of Finance. The most recent edition states:

Value for money is the core principle governing Commonwealth procurement. This core principle is underpinned by four supporting principles:

1 Noted in Industry Commission Report No. 48 of 1996, *Competitive Tendering and Contracting by Public Sector Agencies*, p.74

2 Industry Commission Report No. 48 of 1996, *Competitive Tendering and Contracting by Public Sector Agencies*, chapter A2

3 Productivity Commission, *Stocktake of Progress in Microeconomic Reform*, June 1996, p.167

- Efficiency and Effectiveness;
- Accountability and Transparency;
- Ethics: and
- Industry Development.⁴

The Outsourcing of IT Services

2.5 The provision of information technology services was one area of government activity where outsourcing was seen to offer savings and efficiencies. The Senate Finance and Public Administration References Committee⁵ has provided a useful account of the development of the IT outsourcing process. It notes that market testing with a view to outsourcing IT services was first directed in 1991, and given impetus in the Labor government's Industry Statement in March 1991. Development of the IT outsourcing policy was undertaken by the Department of Finance in accordance with the Industry Statement. A review was conducted by the Department of Finance in 1994⁶, and then in 1996/1997 the Auditor General conducted a performance audit of the IT outsourcing process undertaken by the Department of Veterans Affairs⁷. Though this review focussed on one agency, its key recommendations were relevant across government.

2.6 In April 1997 the Minister for Finance, the Hon John Fahey MP, announced "in-principle approval to outsource ... Information Technology (IT) infrastructure, subject to the successful completion of competitive tendering processes."⁸ In the press release, the Minister made it clear that the process was intended to meet both of the strategic goals outlined in paragraph 2.3 above, in that it was to:

"[achieve] the best value for its information technology dollar, to support the delivery of services at the lowest cost to the taxpayer. [...] The Government will become a purchaser and not a provider of IT infrastructure, with services supplied by providers whose business – and core competency – is IT."⁹

2.7 Two important characteristics of this initiative were the centralised control of the process, and the "clustering" of agencies. In November 1997, control of the overall progress of the initiative was vested in the Office of Asset Sales and Information Technology Outsourcing (OASITO). This centralised control was seen as necessary in order to overcome

4 Department of Finance, *Commonwealth Procurement Guidelines and Best Practice Guidance*, 12 February 2002, p.5

5 Senate Finance and Public Administration References Committee, *Re-booting the IT agenda in the Australian Public Service*, pp.7-12

6 Minister for Finance's Information Technology Review Group, *Clients First: The Challenge for Government Information Technology*

7 Australian National Audit Office, *Management of IT Outsourcing – Department of Veterans Affairs*, Audit Report no. 21

8 The Hon John Fahey MP, Minister for Finance, *Outsourcing of Information Technology Initiative*. press release 16/97, 25 April 1997

9 The Hon John Fahey MP, Minister for Finance, *Outsourcing of Information Technology Initiative*. press release 16/97, 25 April 1997

the “agencies’ inertia and resistance to change” which had been responsible for previous delays in IT outsourcing.¹⁰ The Humphry Review and the Senate Finance and Public Administration References Committee identified this central control as a weakness of the initiative, which inhibited support from agencies:

While agencies generally supported the principles of outsourcing, serious concerns were expressed about managing the process through the imposition of a “top heavy central agency focussed on administrative structure”. A number of agencies were concerned with the apparent requirement that they rely solely on such a body for the development of outsourcing tenders and negotiating contractual arrangements.¹¹

2.8 Under the initiative, agencies were “clustered” into groups based on perceived IT and business synergies. These clusters were intended to increase the size of the outsourced contracts, in order to attract lower per-unit service costs. However, clustering arrangements also presented some difficulties:

Cluster 3 includes large, geographically-dispersed, Budget-funded agencies (such as DIMA and AEC); small, commercially-focussed agencies (such as AGAL, AUSLIG and IP Australia); and, for the first 18 months, the NCA, which had more stringent security requirements than the rest of the Cluster. These differences have contributed to a range of operational difficulties for both Cluster agencies and the External Service Provider. [...] An issue for smaller agencies within a group can be the potential for the External Service Provider to concentrate its service delivery efforts on the larger agencies. [...] The commercially-focussed agencies ... have also expressed concern at various times about the implications for their commercial arrangements and relationships arising from service delivery failures by the External Service Provider.¹²

2.9 By initiating its IT outsourcing arrangements prior to the commencement of the whole-of-government initiative, Customs was largely able to avoid both central control by OASITO and inclusion in a “cluster” with other agencies.

IT Outsourcing in the Australian Customs Service

Outsourcing to Tradegate

2.10 Customs has used information technology to streamline its procedures since the early 1970s.¹³ In the late 1980s, Customs implemented an “Electronic Initiative Program” under which more complex computer systems were introduced in order to automate Customs processes.¹⁴ In 1988, the National Communications Working Party on Cargo Movements recommended that Customs work towards a national Electronic Data Interchange (EDI) network. As a result, Customs joined with various other industry players (including road and

10 *Review of the Whole of Government Information Technology Outsourcing Initiative* (“the Humphry Report”), p.4

11 Senate Finance and Public Administration References Committee, *Re-booting the IT agenda in the Australian Public Service*, p.17

12 Australian National Audit Office, *Implementation of Whole-of-Government Information Technology Infrastructure Consolidation and Outsourcing Initiative* pp. 62-63

13 *Submission 7*, Australian Customs Service, p.3

14 *Submission 7*, Australian Customs Service, p.3

rail carriers, shipping lines, freight forwarders, customs brokers and importers, port authorities, AusTrade and Qantas¹⁵) to form Tradegate, a not-for-profit organisation which was then “awarded an exclusive contract by Customs to supply electronic network services to Customs’ users.”¹⁶

2.11 While this contract may be regarded as “outsourcing”, it does not appear to have been a competitive tendering process. Instead, that competitive process was undertaken by Tradegate itself, which called for tenders for the national EDI communications network¹⁷. This contract was won by Paxus¹⁸, which later became AT&T Easylink Services Australia, then connect.com.au¹⁹, and finally Connect Internet Solutions²⁰. Customs had therefore undertaken its first IT outsourcing well before the widespread push for IT outsourcing in the early to mid 1990s. The contract between Customs and Tradegate was renewed in 1996 and 1999,²¹ and has recently been extended to mid-2003, with a 12 month option to mid-2004.²²

Outsourcing of IT Infrastructure

2.12 In 1996, within months of the current Government coming to office, Customs took the decision to market test its IT functions with a view to outsourcing them if the testing process indicated this would be worthwhile. This decision was partially a response to the growing impetus for outsourcing described in paragraph 2.5 above, and partially a response to more immediate factors. These factors related to:

- The Government’s references to IT contestability in its 1996 post-Election document “Meeting our Commitments” ; and
- Formal and informal discussions between agencies soon after the election in 1996 that outsourcing of IT was inevitable and there were early indications that some form of grouping of departments and agencies might be envisaged.²³

2.13 At the same time, Customs “separately concluded that there were significant changes needed in the way in which IT supported an array of changes which Customs was determined to pursue.”²⁴ These changes amounted to a re-engineering of Customs’ IT systems, and evolved into the Cargo Management Re-engineering (CMR) process.

2.14 Deloitte Touche Tohmatsu was appointed to test whether outsourcing was appropriate for the Customs’ IT, and a Request for Information (RFI) was issued to provide the industry with an opportunity to inform this process. After the Deloitte Touche Tomatsu

15 *Submission 7*, Australian Customs Service, pp. 3-4

16 *Submission 7*, Australian Customs Service, p. 4

17 *Submission 1*, Tradegate Australia, p.13

18 *Submission 1*, Tradegate Australia, p.13

19 *Submission 4*, Connect, Appendix A, p.III

20 *Transcript of Evidence*, Connect Internet Solutions, p.2

21 *Submission 1*, Tradegate Australia, p.13

22 *Transcript of Evidence*, Tradegate Australia, p.15

23 *Submission 7*, Australian Customs Service, p.21

24 *Submission 7*, Australian Customs Service, p.21

report had been received, Customs took the decision to outsource. This decision was made by the end of 1996. The reasons Customs cites for this decision are as follows:

- The need to modernise Customs applications and to ensure that its systems would enable the delivery of improved performance.
- The probability that Customs would achieve longer term economies from moving to an open platform architecture.
- The probability that access to a highly skilled IT workforce would be more easily obtained through a major outsourcer than by continued Customs efforts to tap into a difficult labour market.²⁵

2.15 It is clear from the second of these reasons that, even at this early stage, Customs saw the outsourcing of its IT systems and the move to a more open platform environment as linked objectives. The new operating environment was regarded as an outcome of the outsourcing process, and therefore an exercise to be undertaken by the contractor.

2.16 From responses to the RFI, Customs identified 9 contractors as “having the potential to provide Customs with effective applications management and IT infrastructure services presently provided internally, at a cost that was at least competitive”²⁶.

2.17 In July 1997 Customs issued to those nine contractors a Request for Tender (RFT) for the provision of information technology services. Three tenders were received, from Andersen Consulting, EDS Australia, and IBM GSA. EDS was the preferred tenderer.²⁷ A contract was signed on 23 December 1997 and the handover date, upon which EDS began providing all services, was 28 March 1998. The initial contract was for five years, with two extensions, each of two years. EDS has bid for these extensions to be adopted, and Customs is currently considering whether to extend the contract.²⁸

Outsourcing of the Cargo Management Re-engineering Process

2.18 As noted above, the Cargo Management Re-engineering (CMR) process emerged after Customs identified the need to upgrade and modernise its Electronic Data Interchange (EDI) systems. The Cargo Management Strategy, as it was then known, commenced a series of consultations in March 1996. In November 1997, following the decision to outsource, Customs made a final decision to pursue the re-engineering of its cargo systems. It is apparent from these dates that consideration of cargo management re-engineering occurred concurrently with consideration of outsourcing, which also commenced just after the election in March 1996.

2.19 According to Customs, the negotiation of the outsourcing arrangements emphasised the need for system re-engineering to take place. In its submission, Customs stated that “The tender process itself reinforced Customs view that there was a need to modernise its cargo

25 *Submission 7*, Australian Customs Service, p.22

26 Australian Customs Service *Request for Tender No. A22, Provision of Information Technology Services*, par. 1.1.1

27 Australian Customs Service *RFT No. A22, Provision of Information Technology Services, Evaluation Report*, p.17

28 *Transcript of Evidence*, EDS Australia, p.50

systems. [...] All three tenderers identified the need to modernise cargo systems and Customs sought elaboration from all bidders on this aspect.”²⁹ Further, the outsourcing tender evaluation report stated:

An ACS review separate to the consideration of outsourcing has confirmed the business need to re-engineer in the commercial area. ACS also has underway a separate re-engineering project dealing with passenger processing. Re-engineering is expected to result in business improvements, including operational efficiency in other parts of the ACS.³⁰

2.20 Following the commencement of the contract between Customs and EDS, development of the CMR systems were delayed as the issue of year 2000 (Y2K) readiness arose. Once Customs’ systems were ready for the year 2000 date change, consideration of the CMR recommenced.³¹ One important element of the CMR process was the Customs Connect Facility, or CCF. The CCF, once implemented, will allow Customs users to connect directly to Customs, without requiring them to go through the Tradegate hub.

2.21 According to Customs, it was initially expected that the design and building of the CCF would be put out to tender, but then it was discovered that the work could be completed by EDS under the outsourcing contract:

Regarding the Customs Connect Facility that we are talking about: at one stage we were intending to put the connection facility out to contract – in other words, invite tenders to provide that connection into the new Customs system. Since that time our contractor – EDS – has gone down a different path which, instead of using a number of Unix boxes, involves an IBM Mainframe. We have negotiated with EDS for it to provide in addition to the large mainframe an AIX front-end capability, which means we do not have to go out to contract, that all that we will need to enable people to connect with our mainframe will actually come through in essence a box tied in with the IBM system.³²

2.22 In accordance with the contract, EDS engaged IBM, Baltimore and SecureNet as subcontractors to develop the CCF applications (i.e. the software). In early 2002, however, “Customs and EDS ... agreed that ... Customs should effectively take over the contract arrangements with those three organisations.”³³ Consequently Computer Associates has been contracted to lead a consortium including IBM to develop the CCF applications. The CMR, including the CCF, is due to be in place by July 2003.

29 *Submission 7*, Australian Customs Service, p.6

30 Australian Customs Service *RFT No. A22, Provision of Information Technology Services, Evaluation Report*, p.17

31 *Transcript of Evidence*, EDS Australia, p.48

32 Mr Lionel Woodward, Legal and Constitutional Legislation Committee, *Supplementary Estimates Hansard*, 22 November 2000, p.67

33 *Transcript of Evidence*, Australian Customs Service, p.56

CHAPTER THREE

THE CUSTOMS CONNECT FACILITY

Introduction

3.1 The Customs Connect Facility was by far the most contentious issue canvassed during this inquiry. It was central to Senator Lundy's original concerns during the Estimates hearings of 2000 and 2001. The issue revolves around four main concerns, which will be dealt with in this chapter. They are:

- the need for a new connection facility;
- the CCF implementation process;
- the financial costs and benefits of the new connection facility; and
- the implications the new connection facility has for Tradegate

The Need for a New Connection Facility

3.2 The Committee found widespread agreement among all stakeholders that Tradegate has provided an effective service during the past decade. Customs, for instance, "acknowledges that Tradegate has performed a valuable service in encouraging the adoption of electronic commerce and that it has provided a reliable, quality service."¹ The Australian Federation of International Forwarders cited this reliability as a reason why the Tradegate hub should be left to operate as it does currently:

Industry is very concerned that the ACS is withdrawing from the existing, very complex, cross Industry IT arrangement that is in place and is working well, for no apparent good reason. If the ACS, or the Government policy favours expansion of competitive access that is fine, but it does not justify removal of the existing highly successful service. This, in reality, would amount to a reduction in competition. Industry, generally, does not wish to be compelled to move off its tried and proven technology for what is an unknown and unproven IT experience. We believe this would be bordering on folly at additional unnecessary cost to all concerned.²

3.3 Notwithstanding this satisfaction with Tradegate's service, Customs made the decision to implement the CCF in the wider context of Cargo Management Re-engineering. "Customs does not believe ... that providing a good service and having support should be the reason to maintain an exclusive access arrangement, whether that arrangement is with Tradegate or an IT outsourcing provider."³ Customs has provided the Committee with a number of reasons for the introduction of the CCF, namely:

- was the Tradegate arrangement becoming deficient?;

1 *Submission 7*, Australian Customs Service, p.7

2 *Submission 3*, Australian Federation of International Forwarders, p.5

3 *Submission 7B*, Australian Customs Service, p. 4

- Tradegate as a “monopoly”;
- Users’ desire for alternative forms of access to Customs; and
- connection options for small and medium users.

3.4 Each of these will be discussed below.

Was the Tradegate arrangement deficient?

3.5 The Committee is satisfied that the technology utilised by Tradegate and by Connect was up to date and effective in maintaining widespread satisfaction with Tradegate’s services. For instance, Connect stated that prior to responding to the RFI in relation to the CMR project, “[Connect] had invested in upgrading the networks involved in servicing the Tradegate contract.”⁴

3.6 The use of the term “legacy system” by Customs, however, appears to have caused some concern to Tradegate and Connect, because it may be read to imply deficiency. Statements from Customs such as “It is those legacy systems which we are seeking to re-engineer”⁵ may have contributed to this perception. Certainly Mr George Brownbill, Government Relations Consultant, ACIL Consulting, who appeared before the Committee for Connect, felt that the “legacy systems” - and therefore Tradegate itself – had been regarded as inadequate. He stated:

...there was a fairly clearly expressed view that Tradegate, Connect and the whole apparatus was some kind of “legacy system”. There was a very clear set of indicators ... that it was out with the old and in with the new.⁶

3.7 Notwithstanding the Committee’s view that Tradegate’s technology was up to date, it is apparent that the upgrading of Customs’ systems opened new connection opportunities which had not previously been available. In particular, the decision to install an IBM Mainframe system with an AIX front end (and associated software) allowed EDS to develop, within the bounds of the original contract, a new connection facility. While this is the result of developments on the part of Customs, it is not the result of any deficiency on the part of Tradegate.

Tradegate as a “Monopoly”

3.8 Government policy is that, where possible, public monopolies should be exposed to market competition. The 1993 Report by the Independent Committee of Inquiry into National Competition Policy (“the Hilmer report”) took as one of its six basic elements of competition policy “reforming the structure of public monopolies to facilitate competition.”⁷

4 *Submission 4*, Connect, Appendix A, p.XI

5 Mr Lionel Woodward, Legal and Constitutional Legislation Committee, Supplementary Estimates *Hansard*, 19 February 2001, p.75

6 *Transcript of Evidence*, Connect Internet Solutions, p.4

7 *National Competition Policy*, Report by the Independent Committee of Inquiry, August 1993, p.xvii

3.9 Tradegate had an exclusive contract to provide access to Customs systems, and as a result, what amounted to a “public monopoly”. This aspect of Tradegate’s operations, and the potential for the CCF to remove the “monopoly”, was commented upon by the Australian Exporters and Importers Association as follows:

We support the end of the effective monopoly of data transmission to the ACS through Tradegate/connect.com. [...] We believe that if there is an open communication gateway into the ACS’s computer systems, normal commercial competition amongst telecommunications and software providers will drive costs down for all importers and exporters including SMEs, where a monopoly has failed to do so.⁸

3.10 There are, however, circumstances which justify monopolies. For instance, a “natural monopoly” exists when the output or service of a market “can be supplied by a single firm at a lower cost than by any combination of two or more firms.”⁹

3.11 In the late 1980s, when the creation of Tradegate was contemplated, the state of technology was such that an exclusive gateway, supported by a single hub, was the most efficient arrangement, resulting in what amounted to a “natural monopoly”. Customs then chose to outsource this “monopoly” rather than exercising it itself. Technology has, however, advanced, and the original circumstances which justified the “monopoly” arrangement no longer exist. This tends to support Customs’ view that new means of connection should be facilitated. Customs noted:

Customs believe that, while it was appropriate to have an exclusive access arrangement to foster electronic commerce in the cargo area in the late 1980s and early 1990s, it is no longer appropriate given currently extensive electronic commerce and the ISP market place.¹⁰

3.12 Consideration of Tradegate as a “monopoly” is further complicated because, while Tradegate has exclusive access to Customs’ systems and many users connect directly to the Tradegate hub, some users engage other companies or “bureaus” such as Telstra and IBM to provide them with EDI services. Where this occurs, Tradegate provides the bureau or company with free use of the Tradegate hub in order to enable them to engage Customs systems. Mr Neil Perry, General Manager E-Commerce, from Connect, stated:

If you are an exporter and you want your export clearance number and you sign up with Telstra, what you pay is purely what you decide to pay Telstra, between you and Telstra. We do not charge anything, and we do not charge Telstra anything either, for that service in and out of Customs. So it is a level playing field.¹¹

3.13 The Committee agrees that Tradegate has made substantial efforts to provide its services in a manner consistent with competition and a “level playing field”. This diminishes the strength of the argument that the CCF was necessary in order to overcome a “monopoly”. Further, the Committee considers that continued references to Tradegate as “a monopoly” are unhelpful and potentially misleading.

8 *Submission 5*, Australian Exporters and Importers Association, pp 1-2.

9 *National Competition Policy*, Report by the Independent Committee of Inquiry, August 1993, p.269

10 Australian Customs Service, Answer to question on notice no. 8, 28 March 2002

11 *Transcript of Evidence*, Connect Internet Solutions, p.6

Users' Desire for Alternative Means of Access

3.14 According to Customs, an important driver for the development of the CCF was the business needs and wishes of the Customs' clients and user groups. In its submission, Customs outlines the results of a consultation process undertaken on their behalf by PriceWaterhouse Coopers, which concluded that "industry clients want flexibility in the way they exchange electronic documentation with ACS."¹² The submission expanded on this in a table from the PriceWaterhouse Coopers report which indicated that express carriers, service providers, freight forwarders, stevedores and shipping companies all sought direct access to customs.

3.15 Several of these groups, plus the importers surveyed, sought the capacity to interact with Customs over the Internet. Exporters sought a flexible series of options including arrangements analogous to Tradegate's service (via Communication Service Providers (CSPs)). The only group to emphasise the importance of connection via CSPs was the Communication Service Providers themselves. Based on this information it appears that Customs, in implementing the CCF, was clearly responding to the requests of its client community.

3.16 The Australian Exporters and Importers Association supported implementation of the CCF,¹³ while the Australian Federation of Importers and Exporters opposed it, supporting instead the continuation of the Tradegate model.¹⁴ The Customs Brokers and Forwarders Council of Australia expressed its dissatisfaction with the CCF for failing to meet the levels of service provided by Tradegate.¹⁵ By commissioning the PriceWaterhouseCoopers report, Customs did undertake a process to establish the wishes of its client groups and developed the CCF in response. In evidence, the Committee received views from both sides of this debate.

Connection Options for Small and Medium Users

3.17 In its submission, Customs put the view that one worthwhile outcome from implementing the CCF was the provision of more appropriate connection options for small and medium enterprises, and particularly those who seldom deal with Customs. The Customs submission stated:

Small importers with low volume Customs transactions may wish to connect directly to Customs using their Internet browser to lodge import declarations. By doing this they will be able to take advantage of Customs interactive screens that will assist them in completing declarations.¹⁶

3.18 Although this issue attracted little comment in relation to connection options (as opposed to costs, discussed below), it does seem to be one issue where there was a certain amount of agreement. In evidence, Mr Neil Perry of Connect stated that:

12 *Submission 7*, Australian Customs Service, p.11

13 *Submission 5*, Australian Exporters and Importers Association, p. 1

14 *Submission 3*, Australian Federation of International Forwarders, pp. 4-5

15 *Submission 2*, Customs Brokers and Forwarders Council of Australia, p.4

16 *Submission 7*, Australian Customs Service, p.8

We have no objection to Customs developing other access methods through the Web and through various encryption methodologies. We feel that they could be attractive to small and occasional users but we strongly believe that many large industrial strength users do not want to use Internet mail as their way of communicating to Customs.¹⁷

It follows, then, that Customs' effort to provide a suite of connection options suitable for different sized businesses with different Customs use patterns, was reasonable.

Conclusion

3.19 The Committee is of the view that the development of the CCF arose as a result of three primary drivers: the implementation of technology which allowed the CCF to become a viable proposition; feedback from some surveyed users to Customs, indicating that they wished to access Customs services directly; and a concern for SMEs, for whom a connection facility which allowed them to deal directly with Customs systems, using the internet, may be the most appropriate means of interacting with Customs systems.

3.20 While the implementation of the CCF will remove a "monopoly" and increase competition, this outcome is somewhat peripheral. As Tradegate's performance in providing its services was responsible, the existence of a "monopoly" did not, of itself, require a response. Finally, while the development of technology facilitated the implementation of the CCF, the Committee does not consider that Tradegate's system was deficient. Tradegate provided an efficient, and widely praised service.¹⁸

3.21 On balance, given the feedback from client groups and the existence of new technological options, and in the wider context of the ongoing CMR process, it was reasonable for Customs to decide to implement a new connection facility.

The CCF Implementation Process

3.22 Several witnesses before the Committee were critical of the process used by Customs to implement the CCF. Two main concerns emerged:

- The "on again, off again" nature of the contract for the CCF; and
- The status of the Request For Information (RFI) issued in March 1999, and the allegation that Customs misused information supplied in response to that RFI.

The On-Again, Off-Again Nature of the CCF Contract

3.23 In March 1997, Customs released the *Cargo Management Strategy*, following a process of consultation which had begun the previous year. Taking a long term strategic view, Customs stated:

17 *Transcript of Evidence*, Connect Internet Solutions, p.9

18 See, *Submission 4*, Connect, p.3; *Submission 3*, Australian Federation of International Forwarders, p.4-5; and *Submission 7A*, Australian Customs Service, p.7

Elsewhere in this report there is mention of the immediate implications of the Internet upon our role, but there are some very broad statements which could be added:

- The Internet will continue its exponential growth;
- It will become the so-called information super highway;
- Proprietary networks will not survive as discrete entities. Rather they will merge with and augment the Internet;
- All commercial data will come into Customs via the Internet; and
- Today's concern about security and reliability will be overwhelmed by technological advances and commercial pressures.¹⁹

3.24 Even at this early stage Customs was aware of the need for a facility to enable "all commercial data [to] come into Customs via the internet" and that it saw the provision of such a facility as a component of the Cargo Management Strategy. As noted in the previous chapter, development of the CMR project began once the outsourcing contract with EDS was in place and the issue of transition to Year 2000 had been dealt with. At this stage, the intention was "that EDS would issue an RFT [Request for Tender] to select a subcontractor for the CCF."

3.25 In March 1999, Customs released a Request for Information (RFI) regarding the proposed CCF. At this time the target environment for Customs had not been finally resolved, so it was not known that Customs would move to an IBM Mainframe with an AIX front end. The proposed means of implementing the CCF was still expected to be via a subcontractor to EDS. The purpose of the RFI was to obtain information from supplier and user groups about the functionality required from the CCF.²⁰

3.26 Following the RFI, EDS and Customs agreed on the target environment for Customs. This had consequences for the development of the CCF, as "it was considered the CCF should use [the software product set associated with the new mainframe and front end] as its base and it was not necessary for EDS to seek tenders for a subcontractor."²¹ As a result, the expected RFT did not eventuate.

3.27 EDS subsequently engaged subcontractors (IBM, Baltimore and SecureNet) to develop the CCF. This situation remained in force until late 2001, when Customs and EDS agreed that Customs should take over the contracts.²² A tender to that effect was issued in November 2001, and closed in December 2001²³. Computer Associates was the successful tenderer, and currently leads a consortium to complete the "design and build"²⁴ of the CCF.

19 Australian Customs Service, *The Cargo Management Strategy*, March 1997, p.17

20 Australian Customs Service, *Request for Information on "Communications Service Provider" Concept By 18 May 1999*, s.2

21 *Submission 7B*, Australian Customs Service, p.8

22 See Chapter 2, footnote 33.

23 *Submission 7A*, Australian Customs Service, p.2

24 *Transcript of Evidence*, EDS Australia, p.46

IBM will have the lead role for the CCF with Computer Associates being responsible for the overall co-ordination of the CCF with the ICS.

3.28 As a result, in the period between early 1999 and early 2002, the CCF was initially subject to an RFI with the expectation that an RFT would be issued by EDS. Then, because EDS was to complete the project within their existing contracts, the CCF was no longer subject to an RFT. In order for EDS to carry out the work, it engaged subcontractors. Finally, Customs took up direct control of the contract by conducting a tender process, resulting in a contract with Computer Associates.

Status of the 1999 Request for Information

3.29 As noted above, Customs released a Request For Information (RFI) in March 1999 to seek industry requirements for the CCF. At the time of the RFI's release, Customs expected that the RFI would be followed by a Request For Tender (RFT), probably to be issued by EDS. This expectation may have been shared by other parties. However the RFI itself did not commit Customs to issuing an RFT. The only statement in the RFI which may have suggested that future contracts would be let, was as follows:

Information received will be taken into consideration in designing the proposed gateway functionality. It may lead to further processes involving the selection and possible certification of a range of service providers associated with the re-engineered cargo management system.²⁵

3.30 Connect responded to the RFI on 11 May 1999.²⁶ Connect describes the content of its response as follows:

The response by [Connect] to the RFI included extensive detailed information about [Connect's] solution architecture to help the ACS understand the complexity of the tasks involved.²⁷

3.31 The information provided by Connect, along with that provided by other respondents to the RFI, was provided to EDS as part of the process of developing the CCF. The view of Customs was that "there is nothing wrong with that."²⁸ Indeed, the RFI specifically allowed Customs to do so:

Customs will have the rights to use, reproduce, modify and adapt any information, concepts, ideas or methods indicated in any response to the RFI for any purpose (including for any future procurement process or disclosure to any third party), without any liability to account to any respondent²⁹

25 Australian Customs Service, *Request for Information on "Communications Service Provider" Concept By 18 May 1999*, para 2.2

26 *Submission 4*, Connect, Attachment A, p.VI

27 *Submission 4*, Connect, Attachment A, p.X

28 Mr Lionel Woodward, Legal and Constitutional Legislation Committee, Supplementary Estimates *Hansard*, 22 November 2000, p.69

29 Australian Customs Service, *Request for Information on "Communications Service Provider" Concept By 18 May 1999*, Attachment 4, para A.2.5.1(b)

3.32 Connect, however, have the view that by disclosing this information to EDS, Customs acted outside the bounds of probity:

... questions arise as to probity of the ACS using its in-house capacity to develop an alternative model to Tradegate – based on information provided by [Connect]. This information was supplied as part of [Connect's] (then trading as AT&T Easylink Services Australia Limited) submission to the ACS responding to the RFI on the Communication Services Provider Concept. The revelation of sensitive information to a competitor was certainly not expected by [Connect] and raises the issue of the distinction between the ACS and EDS being blurred significantly. [Connect] provided information to the ACS in good faith and believes EDS, in receiving the information, was essentially treated as an extension of the ACS.³⁰

3.33 The basis for Connect's belief that the information should be held in confidence was the "Master Services Contract" between Connect and Tradegate, which was "back-to-back" with the contract between Customs and Tradegate. That contract states that each party (Tradegate and Connect) would maintain confidence with respect to the other's confidential information.³¹

Conclusion

3.34 The Committee is of the view that the contracts between Customs, Tradegate and Connect are not relevant to the information supplied in response to the RFI, as the contracts cover information passed as a result of the contractual relationship. The RFI process took place outside this relationship. The RFI documentation makes it clear that information provided in response to the RFI can be used by Customs. The information was sought and used by Customs in order to design the CCF.

3.35 The Committee considers that since EDS were responsible for developing the CCF, it was proper for Customs to pass on the information it received in response to the RFI. The Committee is satisfied that the probity of Customs is not in question. The Committee notes that this issue was characteristic of the disconnected consultation and communication process which had developed between Customs, Tradegate and Connect. This is discussed at some length in Chapter 4.

Financial Costs and Benefits of the CCF

3.36 Submissions and evidence before the Committee questioned whether the implementation of the CCF would provide a financial cost or benefit to users of Customs systems. In particular, the issue of cost changes for small and medium enterprises (SME's) was raised.

3.37 Tradegate operates with a flat rate cost structure. In its submission, Connect explained that "costs are averaged over all entries so that they are independent of the size or geographical location of the business concerned."³² These costs are set on an annual basis by a Committee consisting of users, Tradegate, Customs, and Connect.³³ The effect of this is

30 *Submission 4*, Connect, Attachment A, p.XI

31 Connect provided the text of the relevant clauses in *Submission 4*, Attachment A, p.X

32 *Submission 4*, Connect, p.3

33 *Transcript of Evidence*, Tradegate Australia, p.20

that larger customs users, who might under other circumstances expect discounted rates, effectively subsidise smaller users.

3.38 Tradegate also imposes two small levies on users, to replenish the Tradegate Development Fund and the Cargo Automation Development Fund, two funds created to improve the development of e-commerce. These funds began as a way of utilising an overpayment of fees to Customs³⁴ and have continued as a result of the levies. At least some of Tradegate's customers question the need for the levy:

Both of these funds provide grants, in effect re-directing money from importers to other entities, including the ACS itself. This is not a normal compliance function and an end to these abnormal charges could reduce data transmission costs by 5% overnight for all importers, including SMEs.³⁵

3.39 The intention of the CCF is, by opening the connection mechanism to competition, to decrease the costs for both large and small users. Large users would benefit by receiving the full benefit of their economies-of-scale, and small users would benefit from direct access to Customs using a web browser and normal internet service provider. Such service would be slower, but according to Customs, much less expensive:

We do know that communications options using the Internet are varied and at different cost structures depending on the relationship that individual companies might have with their providers or with their bureaus or value added networks. We do know, though, that communication over the Internet and using Internet protocols is certainly more cost effective than what we have with the dedicated lines now.³⁶

3.40 While this may be the case, Customs did not maximise the support of industry by releasing a cost-benefit analysis or the outcomes of economic modelling to demonstrate that costs will decrease. During Senate Estimates hearings in early 2001, Customs provided the following advice:

EDI over the Web – which is what we are talking about – costs about one tenth as much as it does over a VAN [Value Added Network]. [...] A practical example is New Zealand Customs, which moved network providers to the electronic commerce network and from the X400 to the Internet. Overall, the industry EDI charges were reduced from NZ\$2 Million to about NZ\$200,000 annually – that is the cost to importers.³⁷

3.41 The lack of clear guidance by Customs as to the likely outcome in terms of costs appears to have been felt by its user community. In evidence, Mr Brian Lovell and Mr Peter Brown, of the Australian Federation of International Forwarders, were asked whether their members were concerned that costs would increase as a result of the proposed changes. Their answer was as follows:

Mr Lovell – They have no idea. What we are saying is nobody has any idea because we have not received the detail to understand what the costs might be.

34 *Transcript of Evidence*, Tradegate Australia, p.23

35 *Submission 5*, Australian Importers and Exporters Association, p.2

36 *Transcript of Evidence*, Australian Customs Service, p.70

37 Mr Lionel Woodward, Legal and Constitutional Legislation Committee, Additional Estimates *Hansard*, 19 February 2001, p.64

Mr Brown – But we know there will be a cost. We have not been able to quantify it.

Mr Lovell – Nothing ever goes down.³⁸

3.42 Customs has advised the Committee of the basis for its belief that costs will decrease. This advice is as follows:

In the case of direct connections the cost will depend on the bandwidth and arrangements with carriers, eg some organisations may obtain discounts because of other business activity with the carrier.

In the case of clients coming via an ISP or a VAN their costs should be no higher and probably lower than under current EDI arrangements where they already pay the charges set by their VAN including carrier costs, and the costs of EDI over the internet are expected to be considerably lower than the current COMPILE costs.³⁹

Conclusion

3.43 The Committee notes the Australian Federation of International Forwarders' concern about the lack of information provided to Customs users. Customs has stated its view that services will be delivered more cheaply. Other than the evidence presented in paragraph 3.40 of this report, the Committee has received no further evidence on this point.

38 *Transcript of Evidence*, Australian Federation of International Forwarders. p.41

39 *Submission 7C*, Australian Customs Service, p.2

CHAPTER FOUR

THE CCF CONSULTATION PROCESS

Introduction

4.1 Several organisations, in submissions and evidence before the Committee, were critical of the consultation process undertaken by Customs during the development of Cargo Management Re-engineering (CMR) generally, and the Customs Connect Facility (CCF) in particular. A number of witnesses maintained that the consultation process:

- was not a proper consultation process, but rather an exercise in information dissemination; and
- did not recognise the special relationship between Tradegate/Connect and Customs.¹

Outline of consultations undertaken

4.2 Customs advise that the CMR consultation process began in 1996. At that time, Customs foreshadowed a need for a change to connection arrangements. The CMR process was then delayed as the extent of the potential “Y2K” computer problems became apparent.²

4.3 In March 1999 the CMR Industry Reference Group (IRG) was formed and the matter of the CCF was immediately on the IRG’s agenda. Customs released the Request for Information relating to the CCF on 26 March 1999. As part of the consultation process on the CCF, Customs held a series of workshops in May 1999.

4.4 Following these consultations Customs released an exposure draft of the General Specifications for the CCF at the end of 1999. CCF Business Requirements were released shortly afterwards, in March 2000. These were revised in August 2000.

4.5 In early 2001 further consultations were undertaken to assist the development of the Integrated Cargo System, which allows users to conduct Customs transactions once they connect to Customs through the CCF. A series of consultations, especially with software developers, continued until late 2001.

4.6 Customs organised a series of consultations leading to an industry roundtable meeting held in October 2001, and attended by a wide range of industry stakeholders including Tradegate, Connect, freight forwarders, software developers, exporter and importer bodies, and major export and transport companies including Hewlett Packard, Coles Myer, Qantas, Telstra and TNT. This led to additional consultations, particularly on internet security

1 See *Submission 1*, Tradegate, p/4.10; *Submission 2*, Customs Brokers and Forwarders Council of Australia, pp. 4-5; *Transcript of Evidence*, Australian Federation of International Forwarders, p.36.

2 See *Transcript of Evidence*, EDS Australia, p.48

issues. The Committee understands that the consultation process has continued, with an Industry Consultation Group on connection methods meeting as recently as 29 April 2002.

4.7 In addition, Customs informed the Committee that “the cargo community provides comments as issues arise”.³ However, the view of the AFIF⁴ and the Customs Brokers and Forwarders Council of Australia⁵ was that there were not adequate opportunities for consultation.

Proper Consultation

4.8 As noted above, Customs were criticised in evidence and submissions for inadequate consultations. The Australian Federation of International Forwarders (AFIF) told the Committee that “...industry, with very few exceptions, does not regard the [Cargo Management Re-engineering] approach to consultation to be much more than a one-way passing of information from time to time about the latest ACS position [...] The so-called CMR process has been a solo act rather than a duet, in our opinion.”⁶

4.9 Tradegate noted that “... e-commerce cannot be performed alone, it requires extensive and community-wide consultation to be successful.”⁷ Tradegate recognised the similarity between the CCF and other e-commerce projects, and concluded:

This concept was first raised by Customs in January/February 1999 ... [Customs] indicated that [they] would shortly be issuing an RFI on the subject.

There had been **no prior consultation** [sic] with either Tradegate or its technology supplier on the subject. Before the EDS outsourcing position, such a concept would have been extensively canvassed by Customs with Tradegate and our technology suppliers **before** [sic] agreeing upon any major changes to the technology supply position, particularly where the changes could impact the end user community.⁸

4.10 As the Committee has noted above, Customs had been conducting consultations with industry into the CMR process since 1996. At the time the RFI was released, March 1999, Customs indicated that it was prepared to consider different connection options:

It is not envisaged that any CSP [Communication Service Provider] arrangement would be exclusive. It is also important to note that connection to any CSP facility would be very much a matter of commercial choice. It is proposed that users who wish to connect with Customs individually via the Internet or existing VANs would be able to do so. Indeed it may be that existing VANs may wish to act as CSPs. Large volume users may also wish to propose direct connection to the Customs gateway.

3 *Submission 7*, Australian Customs Service, 13

4 *Transcript of Evidence*, Australian Federation of International Forwarders, p.36

5 *Submission 2*, Customs Brokers and Forwarders Council of Australia, pp. 3-4

6 *Transcript of Evidence*, Australian Federation of International Forwarders, p.36

7 *Submission 1*, Tradegate, p.11

8 *Submission 1*, Tradegate, p.4. Emphasis in the original.

Within this context, Customs will consider all options. CSPs could take a variety of forms and could be established by individual entities or by new or existing associations of current Customs clients.⁹

Conclusion

4.11 On balance, the Committee does not support the view that Customs undertook an improper consultation process. The Committee considers that Customs provided adequate opportunities for its stakeholders to have input into the requirements for the CCF at appropriate points in the process.

Consultation with Tradegate and Connect

4.12 When the Customs Connect Facility (CCF) consultation process commenced in 1999, both Tradegate and Customs agree they had a mutually successful e-commerce relationship spanning ten years. Based on this successful relationship, Tradegate advised that it had an expectation that it would remain a key stakeholder during the development and implementation of the CCF.

4.13 Tradegate and its technology supplier, Connect, expressed particular dissatisfaction with the roles given to them during the consultation process. Tradegate advised the Committee accordingly:

We are an outsourcer to Customs now. We outsource all of the communications, EDI and value-added services technology today. I would have thought that it was almost incumbent upon Customs to consult extensively with us, as a supplier, on that issue. Prior to outsourcing, I might add—when we enjoyed what I would say was an extremely good relationship with all levels of Customs, particularly on the technical computer side—that consultation would have been going on continuously from the moment the idea came into either our minds or Customs' to look at something differently. Post outsourcing, when all of the people left, it stopped.¹⁰

4.14 While the relationship between Customs and Tradegate was direct, there was no direct contractual relationship between Customs and Connect. Connect's contractual arrangements with Tradegate mirrored Tradegate's contract with Customs, but while Tradegate was a not-for-profit industry based organisation, Connect provided its services to Tradegate on a for-profit commercial basis.

4.15 The Committee notes, on the basis of evidence received during the inquiry, that the implementation of the CCF may result in a loss of market share for Tradegate, and may result in the need for Tradegate to reassess its services and prices.

4.16 Tradegate believes that a number of aspects of its relationship with Customs, taken together, justify a stronger consultation process than was undertaken. These include that Tradegate have a ten-year relationship with Customs IT systems; that they have skills and experience in e-commerce and EDI applications; that they have knowledge of the user community, and the capacity to communicate with them authoritatively; that they are a not-

9 Australian Customs Service, *Request for Information on "Communications Service Provider" Concept* By 18 May 1999, para 4.2-4.3

10 *Transcript of Evidence*, Tradegate, p.15

for-profit industry based organisation; and that the CCF was likely to have a significant impact for their business operations.

4.17 Tradegate and Connect both advised that they have had no consultations with EDS regarding the development of the CMR. In evidence, Tradegate were asked to describe the extent of their consultation with EDS with regard to the CMR and CCF projects. Mr Andrew Robertson of Tradegate stated:

Essentially none. I can recall one meeting maybe four years ago where I was introduced to a gentleman from EDS by the then project manager of CMR. That is the only one where CMR was discussed in the context of EDS/Tradegate. In terms of the current legacy systems, we meet every quarter to monitor service levels.¹¹

4.18 EDS confirmed this, explaining:

[Direct consultations with Tradegate or Connect] would not be appropriate. We are a service provider to Customs. Customs would need to feel that it was the time and the place to have those discussions. [...] The time has not been right yet.”¹²

4.19 A further issue was the composition of the board of Tradegate. Mr John Drury, a Deputy Chief Executive Officer of Customs, who appeared before the Committee as Acting Chief Executive Officer, also held a position on the Tradegate board. The Committee notes an apparent diversion between Tradegate’s understanding of Mr Drury’s role, and Mr Drury’s understanding.

4.20 Article 4.2 of Tradegate’s Articles of Association lists the various voting categories for representatives on the Board of Directors. The fifth of those is “Federal, State and Local Governments”¹³ and Mr Drury was the Board Member elected from this voting category.¹⁴ As a result, he was “there as a government representative, not as a Customs official.”¹⁵ At Tradegate’s 2002 Annual General Meeting he did not stand for re-election to this position.

4.21 Mr Drury told the Committee that he went to some effort during Tradegate Board proceedings to emphasise his role as a representative of government generally rather than Customs in particular. He advised the Committee, for example, that he did not speak or vote on issues related to the CMR, and “made it clear to the Chairman, the CEO of Tradegate and to other board members that [he was] not there as a funnel for matters dealing with Customs.”¹⁶

4.22 Tradegate indicated that it did consider Mr Drury, at least informally, acted as a representative of Customs on the Tradegate Board. In response to questions on this issue

11 Legal and Constitutional References Committee *Hansard* , 15 March 2002, p.25

12 *Transcript of Evidence*, EDS Australia, p..54

13 Tradegate, *Articles of Association* (1998) p.5

14 *Transcript of Evidence*, Australian Customs Service, p.60

15 *Transcript of Evidence*, Australian Customs Service, p.60

16 *Transcript of Evidence*, Australian Customs Service, p.60

Tradegate confirmed that it considered Customs to be represented on the Board. Mr Robertson of Tradegate advised “Yes. Currently they are; that is correct.”¹⁷

4.23 The Committee considers that Tradegate was mistaken in its understanding of Mr Drury’s role, and that Mr Drury acted properly in his endeavours to fulfill with probity his roles as a Customs officer and a Tradegate Director.

Conclusion

4.24 In response to the criticisms made by Tradegate and Connect, Customs expressed the view that it would be inappropriate for the consultation process to favour, or appear to favour, Tradegate ahead of other potential service providers:

It was Customs’ view that, given the policy direction taken to replace internal Customs gateways with a single flexible Internet gateway, consultation should be with the Customs community as a whole rather than with any one service provider or company. Tradegate and connect.com were included in such consultative arrangements.¹⁸

4.25 In the Committee’s view, it would have been beneficial for Customs to have had better communications with Tradegate, and therefore to have utilised this relationship to assist the successful implementation of the CCF. While Customs did conduct proper and appropriate consultations with the relevant stakeholder community, additional consultation should have been held on a continuous basis with Tradegate and Connect. These consultations should have included technical discussions between EDS and Tradegate/Connect (facilitated as necessary by Customs), which should have begun immediately once EDS took over the operation of Customs’ information technology.

17 *Transcript of Evidence*, Tradegate Australia, p.20

18 *Submission 7B*, Australian Customs Service, p.6

CHAPTER FIVE

TRANSITION TO THE CCF

5.1 This report has considered two major IT-related projects undertaken by Customs: outsourcing to EDS, and the development of Cargo Management Re-engineering, and as part of that, the development of the Customs Connect Facility. Each of these projects was complex, both from a technical IT perspective and in terms of the procurement process required to complete them.

5.2 The Committee considers that Customs has performed in a satisfactory manner from a technical perspective. The upgrading of its IT systems, which resulted in the CMR process, was necessary in order to replace internal Customs' systems, which were once-state-of-the-art but were now deficient. The Committee considers that once the decision to use an IBM Mainframe was made, it was also appropriate that Customs explore the option of utilising the new equipment's capacity to the fullest, by establishing the means for direct connection by users.

5.3 The Committee is satisfied with the procurement performance of Customs, but recognises that the fluctuating state of the contracts for the design and build of the CMR – from the initial contemplation of an RFT, to consideration of the project under EDS' contract, to the final contracting of Computer Associates – has drawn criticism from stakeholders, particularly Connect. While each of these changes were made for appropriate reasons, they amounted to a complex sequence for interested stakeholders to follow.

5.4 The Committee, however, is concerned about Customs' stakeholder relations. At the outset of the CMR development process, Customs and Tradegate enjoyed positive and productive relations. Further Tradegate, as a collective with a board structured to represent different portions of the industry, gave Customs immediate access to feedback from users of its online systems.

5.5 The Committee notes the Humphry Report's conclusion that IT outsourcing "is primarily an organisational and people management exercise that revolves around IT."¹ Following from this, the Committee is of the view that the implementation of CMR and the CCF is primarily about developing e-commerce systems, but would have benefited from improved communications between Customs and Tradegate/Connect.

5.6 The CCF is not yet in place, but CMR (and therefore, by extension, the CCF) has an implementation deadline of 20 July 2003. This date represents the commencement of Schedule 3 of the *Customs Legislation Amendment and Repeal (International Trade Modernisation) Act 2001*, which contains the following provision, to be inserted into the

Customs Act 1901:

1 *Review of the Whole of Government Information Technology Outsourcing Initiative* ("the Humphry Report"), p.39. See also paragraph 1.14 of this report.

126D CEO to maintain information systems

The CEO must establish and maintain such information systems as are necessary to enable persons to communicate electronically with Customs.

5.7 This leaves Customs and its team of outsourced providers (principally EDS and Computer Associates) less than 18 months to design, build and implement the CCF. It also implies that, should Customs fail to meet the deadline, the CEO of Customs may be in breach of Section 126D of the *Customs Act 1901*. Some client stakeholders have expressed concern that Customs may not be able to meet this timetable. The AFIF, for example, stated that “if they ... successfully achieve it by July 2003, they will be doing very well.”²

5.8 A key element of the implementation of the CCF will be the transition from the old system to the new. Tradegate’s concerns regarding consultation have a particular focus on the transition from current systems to the CMR and CCF:

We do not know the timetable for introduction. We know that we have this July 2003 deadline, but a lot of things have to happen prior to that in a planned time scale way, and we do not know what that is. We do not know the impact of that change because we do not know what is going to happen when. I do not know when to wind down existing networks. We do not know whether the transition is going to be a big bang approach or a gradual approach over time. We do not know which systems are going to be phased in first. It is not clear and it needs to be clarified very quickly.³

5.9 The Committee is hopeful that the outcomes of this inquiry will inform and improve the transition process. The Committee notes that it is important that this complex technical and stakeholder management task can be undertaken successfully, and within the required time frame. The Committee considers that this will be facilitated by a positive and productive relationship with Tradegate and Connect.

Procedures if the CCF is not in place

5.10 Schedule 3 of the *Customs Legislation Amendment and Repeal (International Trade Modernisation) Act 2001* contains a number of offences which apply if a person fails to electronically communicate information required by Customs. Many of these offences attract penalties of 60 penalty units (\$660), and many of them attract strict liability. An example is s.117A, which reads in part:

117A Submanifests to be communicated to Customs

(1) The person in charge of the place at which the consolidation of goods for exportation by a ship or aircraft is to be carried out must, so as to enable the exportation, prepare and communicate electronically to Customs a submanifest in respect of the goods.

Penalty: 60 penalty units.

(1A) An offence against subsection (1) is an offence of strict liability.

2 *Transcript of Proceedings*, Australian Federation of International Forwarders p.43

3 *Transcript of Proceedings*, Tradegate Australia p.26

(2) A submanifest must communicate such information as is set out in an approved statement.

5.11 Some importers and exporters have raised concerns that if Customs fails to meet the deadline for implementing the CCF, the importer or exporter may be in breach of the legislation, and that given the imposition of strict liability, the failure of Customs to implement the CCF may not provide the importer or exporter with a defence.

5.12 In response, Customs stated that “it is still clearly the ambition of Customs to meet its obligations in that respect [the deadline].”⁴

5.13 The Committee considers that, while it is highly unlikely that the Commonwealth would ever bring proceedings against an importer or exporter under these circumstances, the industry concerns are reasonable. It is reasonable for industry to expect a level of certainty regarding the procedures which will be followed should the CCF (and ICS) fail to be implemented by the deadline. It would clearly be unacceptable for industry to be exposed to potential penalties if Customs does not provide a means for them to comply with the law.

5.14 The Committee notes Section 126E, contained within Schedule 3 of the *Customs Legislation Amendment and Repeal (International Trade Modernisation) Act 2001*. This section, entitled “Communication to Customs when information system is temporarily inoperative,” provides that if Customs systems become inoperative, people can meet their communication obligations in the following ways:

(a) if another information system by means of which the person can communicate information to Customs is operative — electronically by means of that other system;

(b) by document given or sent to an officer doing duty in relation to the matter to which the information relates.

5.15 Although Section 126E appears to be designed for operation once the ICS has commenced, the Committee suggests that these provisions may also be suitable for use in the event that the ICS and CCF are not implemented on time. Subsection (a) above appears to provide a means whereby Customs could continue to allow users to communicate via current arrangements until the CCF and ICS are online and stable.

5.16 The Committee notes that if current processes were to continue, this would require the current arrangements between Tradegate and Customs to continue. This potential for continued reliance on Tradegate’s services highlights the critical importance of Customs re-establishing close co-operation, at technical and managerial levels, with Tradegate.

5.17 While this section appears to provide a satisfactory contingency plan, an announcement, by the CEO of Customs, or by the Customs Minister, that this plan is to be adopted, may provide the level of certainty sought by the industry.

Conclusion

5.18 The Committee is of the view that Customs should take immediate steps to reassess its consultation processes in the light of the concerns which have been expressed to the

Committee, principally by Tradegate and Connect, but also by other organisations such as the AFIF. An improved consultation process should be undertaken in order to ensure that the implementation of the ICS and CCF is undertaken successfully, and on time.

Recommendation 1

The Committee recommends that Customs undertake a review of its consultative processes with a view to developing a strategy for consultation processes for the rest of the ICS implementation process.

Recommendation 2

In order to provide certainty for industry, the Committee recommends that, in the event that the Customs Connect Facility and the Integrated Cargo System are not in place on the date required by the *Customs Legislation Amendment and Repeal (International Trade Modernisation) Act 2001*, Customs invoke the procedures described in Section 126E of that Act.

**Senator Joseph Ludwig
Acting Chair**

APPENDIX 1

INDIVIDUALS AND ORGANISATIONS THAT PROVIDED THE COMMITTEE WITH SUBMISSIONS

1. Tradegate Australia Ltd
2. Customs Brokers and Forwarders Council of Australia Inc
3. Australian Federation of International Forwarders Ltd
4. connect.com.au
5. Australian Exporters and Importers Association
6. Community and Public Sector Union
7. Australian Customs Service

APPENDIX 2

WITNESSES WHO APPEARED BEFORE THE COMMITTEE

Public Hearing held in Canberra on Friday, 15 March 2002

Ms Gail Batman, National Director, Passengers and Information Technology, Australian Customs Service

Mr John Begley, Chairman, Tradegate Australia Ltd

Mr Peter Brown, Former Deputy Chairman (CMR), Australian Federation of International Forwarders

Mr George Brownbill, Government Relations Consultant, ACIL Consulting (representing Connect Internet Solutions).

Mr John Drury, Acting Chief Executive Officer, Australian Customs Service

Mr Brian Lovell, Chief Executive Officer, Australian Federation of International Forwarders

Mrs Jennifer Peachey, National Director, Office of Business Systems, Australian Customs Service

Mr Neil Perry, General Manager, E-Commerce, Connect Internet Solutions

Mr Matthew Reynolds, National President, Community and Public Sector Union

Mr Andrew Robertson, Chief Executive Officer, Tradegate Australia Ltd

Ms Sheelagh Whittaker, Executive Vice President, EDS Australia

